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Dear Richard

**Response to Ofwat Consultation: "New appointments and variations – a consultation on Ofwat's policy relating to highway drainage"**

This response is provided for and on behalf of Independent Water Networks Ltd a subsidiary of Brookfield Utilities UK (BUUK). We welcome the opportunity to comment on Ofwat's proposals and offer the following comments.

We think there are a number of ongoing issues with the way prices to new appointees are calculated, however these are out of scope of this consultations. We note Ofwat's comment in respect of current practices:

- Highway authorities are allowed to use the public sewer system for drainage of roads
- Sewerage companies are prohibited from charging highway authorities for that service.
- Sewerage companies recover the costs of highway drainage from all customers through the sewerage charges.

**Policy Proposal 1**

Point 1 of your proposed policy: *"... it is reasonable for the bulk discharge price to include a contribution to the existing appointee's highway drainage costs"*.

We support the principle of cost reflective charges but unfortunately there is, at this stage, no transparency or cost breakdown over what is included in the incumbent's current domestic and non domestic charges. This issue is further compounded by the lack of a common industry charging methodology.

We believe that some incumbents already include these costs in their large user tariffs. Planning conditions (particularly on greenfield sites) generally require new sites to make their own drainage arrangements and to utilise sustainable drainage options as alternatives to traditional drainage solutions. Where, under these circumstances, highway drainage costs are already included in bulk discharge prices, the effect is that new entrants may be paying for a drainage services that is not being provided.

Our primary concern is that increasing the boundary 'large user' charges will either seriously harm or destroy what little fragile competition currently exists in the water sector. The net income of new appointees ('all the way' charges less the bulk boundary charge) is already wafer thin on smaller sub 500 plot sites so this proposal is likely to foreclose even more of the market to completion. Note that c80% of new developments have less than 500 plots meaning that only c20% of the market have margins that are large enough to support competition.

## **Policy Proposal 2**

*Point 2: "If a new appointee's site contains public roads that do not drain to the public sewers of the existing appointee, or there are no public roads on the site, we are likely to consider that it is reasonable for the new appointee not to contribute to the highway drainage costs of the existing appointee".*

We agree with this point. As stated above this is more likely to be the case on greenfield developments (this being the majority of sites in respect of which new appointees apply for inset appointments). The use of combined sewers (and instances where new developments are more likely to use an incumbent's sewer system to discharge highway drainage) tends to be seen only on dense urban developments where all of the watercourses have been built over, e.g. central London.

Either way, and as indicated in response to Policy Proposal 1 above, we believe that such charges should be identified separately. New appointees will therefore have full transparency as to what charges are being levied for highway drainage.

## **Policy Proposal 3**

*Point 3. "The amount of highway drainage charges payable should be a matter for commercial negotiation between new appointees and existing appointees, on a case-by-case basis."*

Whilst we acknowledge there is a significant element that is a matter for commercial negotiation, such negotiations are not undertaken on an equal footing for the following reasons:

- Incumbents' strong monopoly positions and ability to behave in a dilatory manner can leave new appointees accepting unfavourable terms in order to meet a client's development timeframes.
- New appointees will not necessarily be able to judge whether such charges are fair and reasonable.

- Setting charges on a case by case basis suggests that highway drainage costs are recovered differently from new appointees than they are by the incumbent when it owns and operates the the relevant network itself. Our understanding is that incumbents recover such charges on an average cost basis from their end customers. Such different treatment would appear unduly discriminatory.

#### **Policy Proposal 4**

Point 4: *"A bulk discharge price should as far as possible be cost reflective, which should include taking into account the existence of efficient and sustainable drainage solutions which may result in less highway drainage entering the public sewers of the existing appointee."*

Subject to the points above we agree with this as a general principle. However such principles should apply equally to new appointees and to the end customers of the water undertaker.

We believe that the current bulk tariffs have been developed for large commercial customers and have not been refined for new entrants. There is no transparency on how the bulk tariffs have been made up and therefore no evidence that they are currently cost reflective.

As a licenced undertaker we believe that the available margins on small sites are not sufficient to operate a reasonably efficient business. We would therefore be supportive of any initiative that leads to the introduction of new cost reflective charges for new entrants.

As indicated, whilst in principle we recognize the need to levy charges that reflect the costs associated with providing a service pertaining to highway drainage, it is equally (if not more) important the the bulk prices as a whole be unbundled through an industry-wide common charging methodology which gives greater transparency on the inputs and cost drivers used to develop these prices.

We would be happy to discuss any of the points raised in this consultation if this would be of help.

Yours sincerely

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