

**Northumbrian Water Response to New Connections Charging  
Emerging Thinking for Discussion - April 2016**

**Overview**

We strongly support the proposal to move to a rule based framework rather than one based on interpretation of primary legislation. We agree that the move to a rules based approach allows both the regulator and the industry to be more flexible and innovative in delivering a transparent and fair service to developers and is consistent with the regulatory approach to other forms of charge.

Section 3.5.3 recognises that dealing with disputes is time consuming for all parties. It results in a series of determinations, which is an inefficient and complex way of setting out regulatory guidance. A more open dialogue, similar to the existing approach to setting customer tariffs, will be more suited to the needs of all parties.

**Q1 Have we missed any key issues with the current framework?**

Whilst issues such as the use of the statutory planning framework have been raised, we agree that the consultation is best to focus on the areas within Ofwat's remit – the development of a charging framework. Whilst there are many new development areas that could be discussed, an intense focus on charging is the most productive way to make significant progress in delivering better service to developers.

**Q2 Do you agree with our emerging thinking to require work that is remote from the site to be recovered through infrastructure charges only, to increase transparency?**

We do agree with the proposal that network reinforcement should be paid for through a single charging mechanism. We do not believe this necessarily has to be through infrastructure charges – it could be through requisition charges instead, or by using the higher of the two charges, thus ensuring no perception of double charging.

**Q3 Do you agree with our emerging thinking to allow companies to develop new approaches to charging?**

We do support this as a principle, but we have some concerns over the way this might be managed. If individual companies come up with different approaches, there will, by definition, be a multiplicity of charging mechanisms across the country.

Many national developers deal with water companies across the country. In the discussions we have been involved in, we believe their preference is likely to be for a single approach across the industry.

It is not easy to deliver both innovation and standardisation, but this tension should at least be recognised in the same way that the trade off between predictability and cost reflectivity has been considered. We generally favour standardisation of the rules for charging, but with cost reflective variations in the actual levels of charges.

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**Q4 Do you agree with our emerging thinking to promote a level playing field through increased transparency?**

The key area where a 'level playing field' is required is in the calculation of the asset value for the self lay option. We agree that removal of the requirement for the 12 year income deficit approach would aid transparency through reduced complexity.

To ensure a level playing field for sewerage, we believe clause 32 in the draft charging rules should be removed at this stage. Allowing companies to make a choice about whether to make asset payments for sewer assets would mean there was not a level playing field across the country for a sewer self lay market.

**Q5 What would be the impact of requiring wastewater asset payments?**

We agree with Ofwat's proposal not to set this as a requirement for April 2017. Introducing asset payments would significantly change the current balance between contributions to costs by developers and bill payers, contrary to Government guidance.

Our estimate for the average value of sewers adopted by NWL each year is £20m pa. Our sewerage wholesale income for 2014/15 was £307m, so household sewerage bills would increase by up to 7% (£13) per year. Note: it is not possible to defer these costs 'over the life of the assets', as the expenditure applies each and every year, so deferral would merely accumulate much higher costs for future years.

Whilst the legislation for water and sewerage is the same, there are very practical reasons why developers will typically requisition water mains yet lay the sewers themselves for later adoption. It is these practical differences (size and position of sewers versus mains) that drive the different financial decisions of developers. It is not necessary to have a 'level playing field' between water and sewerage – they are separate discrete services often delivered by different water / sewerage companies.

For this reason, we feel that clause 32 in the draft charging rules should be removed at this stage. Allowing companies to make a choice about whether to make asset payments would mean there was not a level playing field across the country for a sewer self lay market.

**Q6 Do you agree with our emerging thinking regarding information provision from companies to improve transparency?**

We support the proposal for a single document for new connections charging, we already have a separate New Development Charges Scheme available on our website.

A set of principles for what each charge is expected to recover would also be very helpful – it would aid consistency across the industry and give confidence to developers.

**Q7 What further information should Ofwat seek to collect from companies to aid transparency of charging in relation to new connections, as well as enabling ongoing monitoring and enforcement?**

High level data such as the total annual expenditure on new development could be included in the Regulatory Accounts or Annual Performance Report. The numbers of new properties connected each year would also be useful for all stakeholders. The existing publication of receipts from developers in the regulatory accounts should continue.

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This data, along with the published explanation of the basis of developer charges by each company should significantly increase transparency and allow for monitoring by Ofwat.

**Q8 Do you have any specific suggestions on the draft rules set out in appendix A1?**

Ofwat must take care to ensure that these rules are compatible with the relevant legislation. Indeed, a second Appendix showing how Sections 51CD, 105ZF and 144ZA of the WIA91 apply would help all parties in reviewing the potential charging rules.

In the past, Ofwat has issued regulatory guidance in this area which has subsequently had to be withdrawn as it was not compatible with existing legislation. All stakeholders need to be assured by Ofwat that their guidance is compatible with legislation and can thus be relied upon.

To ensure a level playing field for sewerage, we believe **clause 32** in the draft charging rules should be removed at this stage. Allowing companies to make a choice about whether to make asset payments for sewer assets would mean there was not a level playing field across the country for a sewer self lay market. Our response to Q5 explains why we believe payments for sewer assets are not in the interests of developers or customers in general.

**Q9 Do you consider it to be appropriate for Ofwat to set requirements for companies to engage with their stakeholders as part of the charging rules?**

Customer engagement is a key part of the trust and confidence agenda, particularly in setting out charging rules. It is appropriate to require companies carry out focused and proportionate customer engagement on charging rules, where appropriate. Ofwat should not prescribe the approach or scale of such activity however, leaving that to companies to decide.

**Q10 Do you consider that any additional actions will be required to ensure an effective transition?**

Ofwat should recognise that charging changes are often best made over a period of time. This allows for the gathering of customer views, evidence of earlier changes and for changes to be made with the confidence of all parties.

With the single till revenue control, companies also have a responsibility to ensure that incidence effects of changes are managed, as changes to the level of revenue recovered for new connections have direct impact on the levels of charge for all other customers. Any changes to new connection charges therefore also need to be considered alongside the wholesale charging rules (currently under consultation) and the existing charging rules.

For this reason, we believe that April 2017 should be seen as the start of a process of reform. Companies should be able to set out longer term plans for future charging changes, alongside any changes for 2017-18. This opportunity for dialogue will ensure a 'no shocks' approach to charging reform, ensuring trust and confidence in the sector for all stakeholders.

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