



Water Services Regulation Authority Section 8(3) of the Water Industry Act 1991

Proposal by the Water Services Regulation Authority (Ofwat) to vary the appointments of Anglian Water and Cambridge Water as water companies

This notice is a consultation on this proposal. The consultation period will last for 28 days. Having considered any representations submitted in response to the consultation, Ofwat will decide whether or not to grant the variations to these companies' appointments.

The Site

Anglian Water has applied to be the water company to 1,500 new household properties at a site called Northstowe Phase One, in Cambridge (the Site).

The Site is in the water supply area of Cambridge Water, and is in the sewerage services area of Anglian Water itself.

The proposal

Ofwat proposes to:

- i. vary the appointment of Anglian Water as a water company by adding the Site to its water supply area; and
- ii. vary the appointment of Cambridge Water as a water company by excluding the Site from its water supply area.

By means of these variations, Anglian Water will become the water supplier for the Site.

Policy for new appointments and variations

The new appointment and variation mechanism, set out in primary law¹, provides an opportunity for entry and expansion into the water and sewerage sectors by allowing one company to replace the existing appointee as the provider of water and/or sewerage services for a specific area. This mechanism can be used by new companies to enter the market and by existing appointees to expand their businesses.

When considering applications for new appointments and variations, Ofwat operates within the statutory framework set out by Parliament, including our statutory duty to protect consumers, wherever appropriate by promoting effective competition. We consider that we must ensure that customers on a site – who do not have a choice of supplier – are adequately protected. When assessing applications for new appointments and variations, the two key policy principles we apply are that:

1. customers, or future customers, should be no worse off than if the site had been supplied by the existing appointee; and
2. Ofwat must be satisfied that an applicant will be able to finance the proper carrying out of its functions as a water and/or sewerage company.

We clarified these two policy principles in February 2011 when we published our 'New appointments and variations – a statement on our [policy](#) and [process](#) for new appointments and variations'.

The application

Anglian Water has applied to be the water company for the Site under the unserved criterion, set out in section 7(4)(b) Water Industry Act 1991.

Unserved status of the Site

To qualify under the unserved criterion, an applicant must show that at the time the appointment is made, none of the premises in the proposed area of appointment is

¹ The legal framework for new appointments is set out in the Water Industry Act 1991 (WIA91). Section 7 of the WIA91 sets out the criteria by which an appointment or variation may be made. Section 8 of WIA91 sets out the procedure for making an appointment or variation.

served by the existing appointee. In general we require an independent report that verifies the site as being unserved. But in this case Cambridge Water has confirmed that it considers that the site is unserved and, having considered the facts of the site², we are satisfied that an independent report is not required. This is consistent with our policy and process statements on new appointments and variations, published in February 2011.

Protecting customers

Ofwat acts to protect consumers, especially those who are unable to choose their supplier. In assessing applications to supply new development sites, Ofwat acts on behalf of end customers who are not yet on site to protect their interests. The fact that future customers on a site have not directly chosen their supplier is not a position unique to new appointments – very few customers in England and Wales are able to choose their supplier³.

Recognising this, our assessment of an applicant's proposals includes analysis of its plans to ensure customers will be at least no worse off in terms of their annual bills and levels of service than if they had been supplied by the existing appointee. We will continue to protect customers on the Site by regulating the new appointee's prices and service levels.

² Anglian Water told us there used to be one connected customer for water on the site, (a golf clubhouse) but those premises are no longer in use. Anglian Water has reviewed Cambridge Water's existing asset plan for the site, which confirms none of Cambridge Water's assets are within the site boundary.

³ The only customers that can choose their supplier are non-household customers that consume at least 5 MI per year and are supplied by a company that is wholly or mainly in England (and at least 50 MI for companies wholly or mainly in Wales) and satisfy the water supply licensing (WSL) eligibility criteria. Those non-household customers that consume at least 50 MI in England (and at least 250 MI in Wales) can switch under either the water supply licensing (WSL) or the new appointments and variations (NAV) framework.

Price

Anglian Water proposes to match the fixed and volumetric water charges of Cambridge Water. The WaterSure tariff will be available to those customers that apply and qualify for it⁴.

Having considered Anglian Water's pricing proposals, we are satisfied that customers will be no worse off in terms of their annual bills than if they had been served by Cambridge Water.

Levels of service

Every appointee is required under conditions G, H and I of its conditions of appointment to publish codes of practice on debt, leakage and a customer code for its household customers.

Anglian Water currently has a set of codes for its current appointment, which satisfy the relevant licence conditions. Anglian Water's customer code of practice sets out the standards of service its customers can expect to receive in a range of areas, and sets out the payments the company will make to customers if it fails to meet these standards. These satisfactorily cover the minimum requirements of the GSS Regulations⁵.

As an appointed undertaker, Anglian Water is required to publish a set of key performance indicators (KPIs). Anglian Water's 2013-14 KPIs raised no concerns, with the company meeting leakage and security of supply targets and delivering a low level of supply interruptions. Additionally, Anglian Water's overall service incentive mechanism (SIM) score of 87 was the second highest in England and Wales, reflecting a high level of customer service.

Having considered Anglian Water's overall service levels, and compared them with those of Cambridge Water, we are satisfied that customers on the Site will receive a

⁴ Through the WaterSure scheme, households on meters who receive certain means tested benefits or tax credits, and are either responsible for three or more children under the age of 19, or have a medical condition which requires significant additional use of water, can apply to pay no more than the average household bill for their region.

⁵ The Water Supply and Sewerage Services (Customer Service Standards) Regulations 2008

level of service that is comparable with the level of service they would have received had they been served by Cambridge Water.

Developer choice

Ofwat takes into consideration the choice of the site developer. In this case, the Site developer has said that it wants Anglian Water to be the water company for the Site.

Environment Agency and Drinking Water Inspectorate (DWI)

We take the views of these organisations into account before progressing to consultation on an application for a new appointment. Both the Environment Agency and DWI informed us that they are content for us to consult on this application.

Cambridge Water's existing customers

In considering whether customers will be no worse off, we also looked at the potential effects of this variation on the prices that Cambridge Water's existing customer base may face.

The calculation necessarily depends on a range of assumptions, and there are clearly difficulties involved in quantifying the effect on Cambridge Water. So it is necessary to use a simplified set of figures. We have expressed the effect in 'per bill' terms to try to quantify the possible effect in an easily understandable way.

Broadly, we have assessed the potential magnitude of this impact by comparing how much Cambridge Water might have expected to receive in revenue from serving the Site directly, with the revenues they might expect from serving the Site indirectly via a bulk supply agreement with Anglian Water. The lower bound of the range takes into account the benefit to Cambridge Water as a result of Anglian Water serving the site, by estimating the costs that Cambridge Water is likely to avoid, such as retail costs and capital and operating costs associated with the local network used to serve the site. The upper bound of the range does not take these avoided costs into account. We look at these differences in revenue and costs over a hundred year timeframe to reflect the long-lived assets that will be used to supply customers at the Site.

In this case, we have calculated that if we grant the Site to Anglian Water, there may be a potential impact on the bills of Cambridge Water's existing customers of between -£0.13 and -£0.55. The negative impact means that the costs avoided by Cambridge Water outweigh the revenue forgone as a result of Anglian Water serving the site, resulting in a benefit for existing customers of Cambridge Water.

We are comfortable that this range accounts for the uncertainty in the costs that may be avoided by Cambridge Water. It is important to note that we do not have information on the level of developer contribution that Cambridge Water would have received had it served the Site. So we have used data on the level of developer contribution that Anglian Water will receive as a proxy. Generally, this will understate the level of developer contributions, as we might expect a new appointee to offer more attractive terms to a developer than an incumbent in order to win the new development.

Further, this impact does not take into account the potential spillover benefits to customers arising from dynamic efficiencies achieved as a result of the competitive process to win new sites. We set out the wider benefits we consider stem from the new appointments and variations framework below.

Wider benefits

The new appointment and variation mechanism provides a means for companies from outside the water and sewerage sectors to enter the market and for existing water and sewerage appointees to expand their businesses.

Entry and expansion (and even the threat of such by potential competitors) can lead to benefits for different customers in different ways (such as developers of new housing sites and household and non-household customers). Examples of benefits delivered through the new appointment and variation mechanism include price discounts, better services, environmental improvements and innovation in the way services are delivered. Benefits can also accrue to the existing appointee's customers, because when that appointee faces a challenge to its business that challenge can act as a spur for it to raise its game.

These wider benefits that we consider stem from the new appointments and variations framework are set out more fully in our [policy statement](#).

Overall assessment of effect on customers

Overall, we consider that customers on the Site will be no worse off being served by Anglian Water than they would have been had they been served by Cambridge Water.

Ability to finance the proper carrying out of functions

We have a statutory duty to ensure that efficient appointees can finance the proper carrying out of their functions. When a company applies for a new appointment or variation, it must satisfy us that it is able to carry out all of the duties and obligations associated with being an appointed water or sewerage company.

In this case, Anglian Water has satisfied us that it can finance its functions.

Conclusion and next steps

In assessing Anglian Water's application for this variation, we have considered the general benefits of new appointments. We are satisfied that our two key policy principles have been met in this case, as customers will be no worse off, and Anglian Water will be able to finance its functions.

So we are minded to grant the appointment under the unserved criterion. We are consulting on our proposal to do so.

Where to send submissions

Any representations about, or objections to, this proposal should be sent in writing to Richard Field, Senior Associate, Casework, Ofwat, Centre City Tower, 7 Hill Street, Birmingham, B5 4UA so as to be received no later than 12 December 2014. Submissions can also be emailed to: Richard.Field@ofwat.gsi.gov.uk.