Dispute referred under section 51C of the Water Industry Act 1991

Extent to which costs associated with the adoption of the Water Main at the former Greenfield site at Alyn Meadows, Tudor Court, Hope can be included in the developer payment

Energetics Design & Build Ltd vs. Dee Valley Water plc

Final Determination
Issued to parties on 20 June 2013

Please see our more recent final determination on similar matters, issued in December 2015

Contents

1. Introduction and Background

This determination concerns a dispute referred to the Water Services Regulation Authority (“Ofwat”) by Energetics Design & Build Ltd (“Energetics”) under section 51C(11) and section 30A of the Water Industry Act 1991 (“WIA91”) on 28 June 2012.

The dispute is between Energetics and Dee Valley Water plc ("DVW") and, as set out in section 51C(11) of the WIA91, concerns the payments and security required to be provided under section 51C of the WIA91.

More specifically, Energetics disputes the payments which DVW require Energetics to pay to DVW as a condition of Energetics' compliance with an adoption agreement ("Adoption Agreement"). The payments under dispute relate to the adoption by DVW of a water main and service pipes built by Energetics on behalf of Taylor Wimpey Homes North West Ltd in respect of properties at Alyn Meadows, Tudor Court, Hope ("the Site").

This determination follows a draft determination that was sent to Energetics and DVW on 11 March 2013 for Energetics' and DVW's comments ("Draft Determination").

Except where the context requires otherwise, terms we have used in this determination which are not defined within this determination have the meaning given to them in the WIA91.

1.1 The parties

Energetics is a multi-utility infrastructure provider (electricity, gas, telecoms and water) and asset owner. It provides design and build services through to final connection and on-going operation of regulated energy networks. Energetics has informed us that it is expanding into the self-lay water market in England and Wales. It has a strong presence in the North West and is looking to expand into the Midlands and Wales.

DVW is a statutory undertaker that provides water services in North East Wales and the North West of England.

1.2 The site

The Site is a development comprising of 53 new build properties at Alyn

Meadows, Tudor Court, Hope. The water supply to the properties will purely be for domestic purposes. The Site is within DVW's area of appointment.

Energetics has been appointed to install the mains at the Site on behalf of the developer Taylor Wimpey North West Ltd ("Taylor Wimpey"). Energetics is therefore the self-lay operator ("SLO") on the Site.

1.3 The dispute

The developer, Taylor Wimpey, appointed Energetics on 11 May 2012 as its SLO in respect of the Site to act on the developer's behalf with DVW. The SLO negotiated with DVW regarding the terms of the Adoption Agreement to be entered into in respect of the Site, on behalf of Taylor Wimpey. In particular, these negotiations related to the relevant design and construction charges payable by Energetics to DVW, and the payment associated with the asset values payable to Energetics by DVW in respect of the water main laid by Energetics.

On 3 May 2012, Energetics met with DVW. At this meeting DVW confirmed that there was no requirement for other water mains, tanks, service reservoirs, pumping stations, or additional capacity within an existing main to enable the adopted main to be incorporated into its supply system.

On 16 May 2012, Energetics made a formal application to DVW for technical approval of its design, approval to self-lay the mains and services and the provision of DVW's terms of agreement.

On 18 June 2012, DVW responded, setting out the following requests for payment (incl. VAT) in relation to the adoption of the water main. Payment of these was a requirement in the Adoption Agreement in respect of the Site.

a) Processing agreement: £445.42 * ("Cost Item (a)")
b) Design site mains for costs: £2,079.05 * ("Cost Item (b))")
c) Design non contestable work: £1,072.33 * ("Cost Item (c)")
d) Design – check SLO designs: £1,724.15 * ("Cost Item (d)")
e) DVW non contestable connection: £3,594.75[1] * ("Cost Item (e)")
f) Inspection fee (supervision): £4,441.61 ** ("Cost Item (f)"
g) Service pipe security/retention: £4,209.79 ** ("Cost Item (g)")

* payment by SLO at time of signing agreement

** payment taken from Asset Payment at time of vesting

[1] DVW has refunded Energetics the VAT payment on this item, as it is not applicable.

Energetics complained to us on 28 June 2012 about the charges listed above. It disputes items a) to g) above on the grounds that section 51C of the WIA91 does not entitle DVW to charge Energetics for any of these costs where there are no “offsite works”[2]. DVW has confirmed in its representations to us in respect of this determination that there are no offsite works, i.e. it has not and does not need to provide additional capacity, other water mains, tanks, pumping stations or service reservoirs to enable the adopted main to be incorporated into its supply system.

[2] The term "offsite works" was used by Energetics in its complaint, and it is being used in this determination to refer in this case to other water mains, tanks, service reservoirs, pumping stations or additional capacity within an existing main to enable the adopted main to be incorporated into DVW’s supply system.

2. Our analysis

There are two questions that we must consider in order to determine this case. The first of these is whether we have jurisdiction to make a determination. To do this we need to consider whether there is in fact a dispute between the parties.

Should we find that there is a dispute, we then need to consider whether section 51C of the WIA91 permits DVW to require from Energetics the costs that it required as part of the Adoption Agreement.

2.1 Jurisdiction

Section 51C(1) WIA91 states that the section applies "*where an agreement is, or is to be, entered into under section 51A*". And section 51C(11) WIA91 states that *"(a)ny dispute between the water undertaker and the other person as to the payments to be made or the security to be provided […] may be referred to the Authority for determination […]*"

This dispute has been referred to us by Energetics in respect of the costs to be paid and the security to be provided pursuant to the Adoption Agreement.

Although Energetics has signed the Adoption Agreement, the wording above shows our ability to determine disputes under section 51C WIA91 applies irrespective of whether an agreement has been entered into.

We are therefore satisfied that there is a dispute in this matter which it has the powers to determine.

We encourage the parties first to exhaust negotiations before requesting a determination from us. Where negotiations have proved unsuccessful, parties should approach us at the earliest possible opportunity. We would usually expect this to be before any Adoption Agreement is signed.

2.2 Was DVW entitled to recover the costs it did from Energetics?

The next question for us to consider is, does section 51C WIA91 permit DVW to require the amounts requested from Energetics pursuant to the Adoption Agreement?

The provisions relevant to the self-lay of water mains are sections 51A to 51E of the WIA91. Section 51A provides that a water undertaker may agree with any person constructing, or proposing to construct, a water main to be used for domestic purposes that if the water main is constructed in accordance with the terms of the adoption agreement, the undertaker will, at an agreed date, adopt the water main. The ownership of the water main therefore transfers, on the agreed date, from the person who constructed the water main to the water undertaker.

Section 51C of the WIA91 then sets out the financial conditions of compliance with an Adoption Agreement. In particular subsections (1) to (4) provide:

> *(1) This section applies where an agreement is, or is to be, entered into under section 51A above in relation to a water main ("the adopted main") by, or on behalf of, a water undertaker and a person constructing or proposing to construct that water main.*
>
> *(2) Where this section applies, the water undertaker may, as a condition of the undertaker's compliance with the agreement, require that person to pay to it the costs mentioned in subsection (3) below.*
>
> *(3) The costs are those reasonably incurred by the undertaker in connection with the adopted main equivalent to the costs referred to in section 43(4)(a) and (b) above, as if references there (and in section 43(5)) to the provision of the new main were references to the incorporation of the adopted main into the undertaker's supply system.*
>
> *(4) For the purposes of any payment required to be made by virtue of subsection (2) above, the water undertaker may require the person to provide such security as it may reasonably request, and the provisions of subsections (4) and (5) of section 42 above shall apply to any security so required as they apply to security required under that section.*

This means that, in accordance with sections 43(4)(a) and (b) referred to above, the costs are *"the costs reasonably incurred in providing such other water mains and such tanks, service reservoirs and pumping stations as it is necessary to provide in consequence of the [incorporation of the adopted main into the undertaker's supply system]; and such proportion (if any) as is reasonable of the costs reasonably incurred in providing or procuring the provision of any such additional capacity in an earlier main as falls to be used in consequence of the [incorporation of the adopted main into the undertaker's supply system]."*

DVW has confirmed in its letter to us (dated 13 July 2012) that it will not be providing any other water mains, tanks, service reservoirs, pumping stations, or any additional capacity within an existing main to enable the adopted main to be incorporated into DVW's supply system.

3. Representations on the Draft Determinations

In the Draft Determination, we set out our view that:

1. We do have jurisdiction to determine this dispute;
2. Section 51C of the WIA91 means DVW was not entitled to require the following payments from Energetics under the Adoption Agreement:
   - Processing arrangement
   - Design site mains for costs
   - Design non contestable work
   - Design – check SLO designs
   - DVW non contestable connection
   - Inspection fee (supervision);
3. Section 51C of the WIA91 does not prevent DVW from requiring a service pipe retention under the Adoption Agreement.

Both Energetics and DVW responded to the Draft Determination. The issues raised in the responses are summarised below.

3.1 Energetics

Energetics agreed with the content and conclusions of our Draft Determination, and did not make representations which challenge our approach in this matter.

3.2 DVW

3.2.1 Connection to existing mains

In relation to connection to existing mains, DVW disagreed with our conclusion that DVW is not entitled to recover the "DVW non contestable connection" cost from Energetics under the Adoption Agreement. Specifically, DVW stated that:

"DVW does not require the provision of additional capacity, tanks, pumping stations or service reservoirs in connection with this scheme. At no point has DVW *specified that "other mains" would not be a requirement for the provision of the 'new main'. The spur main to the existing infrastructure is required and referred to as the non-contestable connection, charges should apply under Section 51C(3), (Section 43(4)(a) and (b)). The connection unquestionably qualifies as "…such other water mains…as it is necessary to provide…".*

We give our view in section 4.1.

3.2.2 Other charges

In relation to the other charges that we propose to disallow, DVW disagreed with our conclusion that DVW is not entitled to recover these costs from Energetics under the Adoption Agreement. DVW's view is that Sections 51A to E do not specify that other charges cannot be made for these provisions, and that Section 142(1)(a) enables undertakers *"to fix charges for any services provided in the course of its functions"*.

We give our view in section 4.2.

4. Our response to the representations

Having reviewed the comments provided by Energetics and DVW, we are satisfied that the content of the Draft Determination is factually correct and accurately reflects the detail and scope of the complaint, set out in section 1.3 above.

We did not receive any representations about our jurisdiction to determine this dispute. We set out our jurisdiction to determine this dispute in section 2.1 above.

We have carefully considered the representations that we received on the Draft Determination. In this chapter we respond to the representations that we received.

The provisions relevant to the self-lay of water mains are sections 51A to 51E of the WIA91. Our approach to determining this dispute has been to consider whether or not DVW was entitled to recover the costs it considers it incurred in adopting the main at the Site pursuant to the Adoption Agreement under section 51C of the WIA91. Since our draft determination of 11 March 2013 and the response from DVW, we have considered this point further. We set out our views below.

4.1 Connection to existing mains

Section 51A of the WIA91 sets out provisions with respect to agreements for the adoption of water mains or service pipes. Section 51A(7)(a) states that an Adoption Agreement may, in particular, include terms:

"for the provision (at the expense of the person constructing or proposing to construct the water main) by— .

i) that person; or

ii) the water undertaker,

of such associated infrastructure at or downstream of the point of connection with the undertaker's supply system as it is necessary to provide in consequence of incorporating the new water main into that system".

Section 51C of the WIA91 explicitly deals with the financial conditions relating to adoption of a water main. As noted at 2.2 of this document, section 51C(3) WIA91 expressly refers to *"the costs referred to in section 43(4)(a) and (b)"*. There are only two subsections ((a) and (b)) under section 43 WIA91. As such, section 51C(3) could have simply referred to section 43(4) should there have been the intention for the wording at the start of that subsection (*"For the purposes of this section the costs reasonably incurred in providing a water main ("the new main") shall include—"*) to be included in respect of the costs referred to in section 51C(3).

As this wording has been excluded from the reference in section 51C(3) we consider that the list of costs that can be charged by the undertaker under section 51C(3) is limited to those set out in section 43(4)(a) and (b) WIA91.

In our draft determination we concluded that DVW was not entitled to charge for the spur feed connecting the new water main to the existing water main ("Spur Feed"), on the basis that Sections 43(4)(a) and (b) WIA91 do not explicitly reference spur feeds.

However, DVW considers that the DVW Spur Feed to the existing infrastructure is required and qualifies as *"…such other water mains… as it is necessary to provide in consequence of the provision of the new main"* as referenced in section 43(4)(a) of the WIA91.

Energetics was given the opportunity to comment on DVW's representations which were provided to Energetics on 10 April 2013. Energetics did not provide representations with respect to this point.

Section 219(1) of the WIA91 defines a water main as *"any pipe […] which is used or to be used by a water undertaker […] for the purpose of making a general supply of water available to customers or potential customers of the undertaker […], as distinct from for the purpose of providing a supply to particular customers"*.

In this case, we consider that the Spur Feed is a pipe used by DVW for the purpose of making a general supply of water available to the customers on the Site. We have therefore concluded that Spur Feed does fall within the above reference at section 43(4)(a) of the WIA91 as it does represent a "water main" as defined under section 219 of the WIA91. Therefore, we have determined that DVW is entitled to recover the costs reasonably incurred in providing the Spur Feed from Energetics as a condition of DVW's compliance with Adoption Agreement in respect of the Site (i.e. cost item (e)).

4.2 Other charges

Turning to the other cost items, set out below, DVW consider that these costs can be recovered under Section 142 (*"Powers of undertakers to charge"*).

The other charges consist of:

1. Processing agreement: £445.42
2. Design site mains for costs: £2,079.05
3. Design non contestable work: £1,072.33
4. Design – check SLO designs: £1,724.15
5. Inspection fee (supervision): £4,441.61

Section 142 is a general provision which sets out the powers of undertakers to charge. It gives undertakers the power *"to fix charges for any services provided in the course of carrying out its functions".*

In our Draft Determination, we set out that Section 51C of the WIA91 is a specific provision regarding the financial provisions to apply in respect of what costs an undertaker may require a person to pay as a condition of the relevant undertaker complying with an Adoption Agreement[3]. Given that there is a specific provision that applies here, we do not consider that Section 142 of the WIA91 (which is a general provision) would override this specific provision. We therefore consider that it is reasonable that the specific provision under Section 51C of the WIA91 should form the basis of any appropriate cost recovery under the Adoption Agreement in respect of the Site in this case.

However, when considering DVW's recovery of its costs in respect of these other cost items, we would note that when we sets price limits it makes an allowance for the operating expenditure (opex) needed for a company's day to day spending to run its services. This opex includes providing services to developers such as those listed above, and includes opex items that may be related to specific capital expenditure items. At the last price review in 2009, DVW were allowed an annual average of £11 million for opex which is paid for through the bills its customers pay. Therefore, while we consider that the legislation does not allow DVW to recover these costs directly from Energetics, DVW is funded for these activities through its opex allowance when we sets price limits. We are therefore satisfied that its approach and interpretation of the Act is reasonable.

[3] As set out in section 51C(2) of the WIA91.

5. Determination

We have carefully considered the responses to the Draft Determination and has had regard to all the circumstances of this case.

For the reasons set out earlier in this determination, we consider that in this case section 51C WIA91 does limit the costs that DVW can recover. Specifically, we have determined that DVW was not entitled to require the following payments under the Adoption Agreement in respect of the Site:

a) Processing agreement: £445.42
b) Design site mains for costs: £2,079.05
c) Design non contestable work: £1,072.33
d) Design – check SLO designs: £1,724.15
e) Inspection fee (supervision): £4,441.61

We determine that DVW is, however, able to charge Energetics £3,594.75[4] for the Spur Feed (Cost Item (f)), on the basis that the Spur Feed to the existing infrastructure qualifies as *"…such other water mains… as it is necessary to provide in consequence of the provision of the new main"* and that the cost is *"reasonably incurred"* in respect of the Spur Feed[5] .

We have determined that Section 51C of the WIA91 does not prevent DVW from requiring Cost Item (g) from Energetics (the "service pipes retention" under the Adoption Agreement in respect of the Site (£4,209.79)). This is because this security payment relates to the adoption of service pipes. While section 51A of the WIA91 sets out the position in respect of service pipes, section 51C of the WIA91 explicitly only relates to the costs of the adoption of water mains (and not service pipes). This dispute has been referred to us under section 51C(11) of the WIA91, and therefore by definition relates to payments required to be made or security required to be provided by virtue of section 51C of the WIA91. We therefore determine that section 51C of the WIA91 does not prohibit such a security payment under the Adoption Agreement in respect of the Site.

[4] We note that DVW has refunded Energetics the VAT payment on this item, as it is not applicable.
[5] See section 43(3) of the WIA91.

Interest is payable to Energetics on the amounts held by DVW. The interest rate should be calculated in accordance with our Information Notice on interest rates.