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## Ofwat grants new appointment to Icosa Water Limited

On 17 August 2016, Ofwat began a consultation on a proposal to grant a new appointment to Icosa Water Limited (**ICO**) to become the water and sewerage services provider for a site in Anglian Water's water supply area and sewerage services area called West Raynham in Norfolk (**the Site**). The Site will consist of 172 household properties and 7 non-household premises. The consultation ended on 16 September 2016. During the consultation period, we received representations from two organisations, which we considered in making our decision. On 20 October 2016, we granted a new appointment to ICO to enable it to supply water and sewerage services to the Site.

This notice gives our reasons for granting this appointment.

### Introduction

The new appointment and variation mechanism, specified by Parliament and set out in primary legislation, allows one company to replace the current company 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 companies to expand into areas where they are not the appointed company. In this case, ICO applied for a new appointment as the appointed water and sewerage company for the Site. Previously, the water and sewerage services to the Site were provided by a private supply.

A company may apply for a new appointment (or a variation of its existing appointment to serve an additional site) if any of the following three criteria are met:

- None of the premises in the proposed area of appointment is served by the existing appointed company at the time the appointment is made (**the unserved criterion**);
- Each premises is likely to be supplied with at least 50 mega litres per year (in England) or at least 250 mega litres per year (in Wales) and the customer in relation to each premises consents (**the large user criterion**);
- The existing water and sewerage supplier in the area consents to the appointment (**the consent criterion**).

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When considering applications for new appointments and variations, Ofwat operates within the statutory framework set out by Parliament, including our duty to protect consumers wherever appropriate, by promoting effective competition. In particular, in relation to unserved sites, we seek to ensure that the future customers on the 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:

1. Customers, or future customers, should be no worse off than if they had been supplied by the existing appointee; and
2. We 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.

Entry and expansion (and even the threat of such by potential competitors) can lead to benefits for different customers (such as household and non-household customers and developers of new housing sites). Benefits can include price discounts, better services, environmental improvements and innovation in the way services are delivered.

Benefits can also accrue to customers who remain with the existing appointee, because when the existing appointee faces a challenge to its business, that challenge can act as a spur for it to improve its services. We believe the wider benefits of competition through the new appointments and variations mechanism can offset any potential disbenefits for existing customers that might arise. We consider these potential disbenefits in more detail below.

## **The application**

ICO applied to be the water and sewerage services appointee for the Site under the unserved criterion set out in section 7(4)(b) of the Water Industry Act 1991 (**WIA91**). ICO proposes to serve the Site by entering into a bulk supply agreement with Anglian Water to provide water services and to provide sewerage services itself. The Site is currently served by a private supply from a borehole and sewerage treatment is provided by an on-site treatment works.

## **Financial viability of the proposal**

We will only make an appointment if we are satisfied that the proposal poses a low risk of being financially non-viable. We assess the risk of financial viability on a site-by-site basis and also consider the financial position of the company as a whole.

Based on the information available to us, we concluded that the proposal was at low risk of being financially non-viable.

## **Assessment of ‘no worse off’**

ICO will charge customers based on Anglian Water’s existing metered water and sewerage tariffs with an initial £5 per year discount when compared to Anglian Water’s sewerage tariff. ICO has Codes of Practice and a Charges Scheme in place, and we are

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satisfied that customers will be offered an appropriate level of service. As such, we consider that customers will be 'no worse off' being served by ICO instead of by Anglian Water.

## **Effect of appointment on Anglian Water's customers**

In considering whether customers will be no worse off, we also looked at the potential effect of this variation on the price that Anglian 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 customers of Anglian Water. It is therefore necessary to use a simplified set of figures. We have expressed the effect in 'per bill' terms to try and quantify the possible effect in an easily understandable way. Broadly, we have assessed the potential magnitude of this impact by comparing how much Anglian 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 ICO. The lower bound of the range takes into account the benefit to Anglian Water as a result of ICO serving the Site, by estimating the costs that Anglian Water would be likely to avoid if they served the Site, 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 ICO, there may be a potential impact on the bills of Anglian Water's existing customers of between -£0.01 and £0.01 per year. We are comfortable that these ranges account for the uncertainty in the costs that may be avoided by Anglian Water.

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.

## **Developer and customer choice**

Where relevant, we take into consideration the choices of the Site's customers or developers. In this case, the Site owner said that it wanted ICO to be the water and sewerage company for the Site.

## **Responses received to the consultation**

We received two responses to our consultation, from the Consumer Council for Water and the Environment Agency. We considered these responses before making the decision to vary ICO's appointment. The main points raised in the responses are set out below.

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## **Consumer Council for Water**

The Consumer Council for Water (**CCWater**) is happy that ICO is offering guaranteed standards and voluntary service standards which match the standards offered by Anglian Water.

CCWater also raised concerns that, while in this case, the impact on the bills of the incumbent's existing customers would be negligible, there were no clear benefits for existing customers.

## **Environment Agency**

The Environment Agency was supportive of the application in general, but wanted assurance that ICO has appropriate plans for communicating with its customers during a period of drought. The Environment Agency also highlighted the fact that ICO will be required to decommission the existing unlicensed borehole used to supply the Site once the supply from ANH has been established. It also reiterated that ICO's new sewerage treatment works will need to meet the conditions of the recently issued Environmental Permit for the Site. Finally, the Environment Agency confirmed that ICO is aware of these requirements and has plans in place to meet them.

## **Conclusion**

Having assessed ICO's application, and having taken account of the responses we received to our consultation, we decided to grant a new appointment to Icosa Water to allow it to serve the Site for water and sewerage services. This appointment became effective on 21 October 2016.