Consultation Response

New Connections Charging – Consultation

Introduction

The Home Builders Federation (HBF) welcomes the opportunity to respond to this Ofwat consultation. Importantly, our response incorporates comments received from HBF members - some of whom may also decide to respond separately. As the national trade association representing major UK House Builders and SMEs, who in turn are responsible for providing around 80% of all new housing in England and Wales, we trust that both quantitative and qualitative weight will be afforded to our response.

With HBF having been involved in this matter for over two years, we are more than willing to meet with Ofwat and/or Defra in response to any subsequent queries, questions or requests for further evidence and/or information. That said, we cannot avoid registering our considerable disappointment (and concern) that our customer-focused comments, inclusive of well-considered recommendations and presented in our response to Ofwat's March 2016 related 'Discussion paper', appear to have been almost totally ignored. Indeed, many of our concerns were repeated in our response to the Defra Charging Rules Guidance consultation which closed on 22nd July 2016. Looking at the timing of Ofwat's consultation, there is compelling evidence to suggest that our latest round of comments may have also suffered a similar fate by being excluded from consideration by Ofwat in the development of its current proposals.

Given the impact this seismic change in 'charging' will have, in particular when it comes to new housing provision, we firmly believe that a structured, quantitative and qualitative response is called for rather merely responding to a limited number of questions. More importantly, the failure to address a number of developer registered concerns as an integral part of this consultation is quite worrying. Our response is therefore structured as follows:

1. *Section 1 – A series of opening 'general' comments*
2. *Section 2 – provides a short response to each of the 8 questions posed*
3. *Section 3 – provides a more detailed critique of the consultation. This part of our response identifies a number of supporting evidence and information papers previously disclosed by the HBF. These papers were provided to aid the various Defra Task & Finish Group discussions and thus we consider them to be of fundamental importance.*
4. *Short Concluding Summary*

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SECTION 1: GENERAL COMMENTS

a) We view this consultation as a missed opportunity to introduce more rigorous control over a monopoly Water and Sewerage Sector where developer customers will continue to have limited competitive alternatives. Moreover, in terms of satisfying the principal objectives of fairness, proportionality and above all, transparency, no other Utility Regulator adopts the kind of 'light touch' approach now proposed by Ofwat.

b) It is concerning to note that despite positive and contrary statements from Defra in 2012 and the EFRA Select Committee in 2013, the impact assessment supporting this consultation does not include any of the required cost data and evidence. Instead, Ofwat make somewhat heroic and aspirational assertions that:

"*Costs will not be greater than at present …"*

This is accompanied by a quite concerning statement on page 3 of the impact assessment that:

"Benefits have not been monetised due to a lack of data …."

In the absence of robust cost data/evidence, which WaSCs, WoCs and Ofwat have had four years to collate, it is difficult for HBF and its members to share Ofwat's confidence that the current proposals will be beneficial for anyone other than the Water and Sewerage Sector. More importantly, based on the reported experience of HBF members, together with the evidence HBF has already provided in its series of evidence-based information papers, we fully expect developer costs to increase. Indeed, the diversity in attitude and approach to infrastructure delivery amongst WaSCs and WoCs, who remain a series of privatised monopoly businesses, free to interpret the legislation as they see fit and in a climate of weak regulatory control, only supports what we say. For more detailed information and comment see paragraphs 3.2.1 to 3.2.3 of section 3 of our response, together with HBF Paper 9 cited in the references.

c) This consultation fails to clearly define and/or re-affirm the statutory obligations placed upon all WaSCs and WoCs pursuant to S37 *et al* and S94 of the Water Industry Act 1991, together with the requirements that underpin Licence Condition 'C'. It is a crucial omission and one of fundamental importance when it comes to off-site foul sewerage infrastructure provision. If the Charging Rules and subsequent Charging Arrangements are to meet the required test of fairness, proportionality and transparency then Ofwat must clearly define the duties and obligations placed on all WaSCs and WoCs and ensure that these are properly and appropriately discharged.

The subjective interpretation of their S94 obligation(s) by at least 4 southern-based WaSCs is a regular source of conflict between developers and those WaSCs. This is particularly so when these same WaSCs seek to secure developer funding for off-site public foul sewer network reinforcement that is not in consequence of a new development. More often than not demand for developer funding is pursued through an inappropriate use of the planning system. The Charging Rules will not stop this from happening - left unresolved, it represents one of the greatest risks to project viability and therefore future housing delivery, in particular in the South of England. Indeed, during the consultation period four WaSCs have already conceded that the new Charging Rules will not stop them using the planning system to secure developer funding for off-site foul sewer network improvements, despite their statutory S94 obligations.

A second but equally important consideration is the considerable time that is taken by Local Authority Planners, WaSCs and Developers to interrogate and resolve a significant number of spurious claims made by certain WaSCs that foul sewer capacity issues can only be addressed through the planning system. It is evidently clear within the framework of this consultation that Ofwat have no appetite to either intervene or engage in order to address this matter. We would venture to suggest that this is an abdication of Ofwat's responsibility, compounded by both Planners and Ofwat conceding that what is being allowed to happen is affecting housing delivery in key parts of the UK.

d) Given the intrinsic importance of the reform proposals that are under consideration we are alarmed at a consultation period that is a mere 22 working days, whilst also being undertaken during the peak holiday period. Of even greater concern is the fact that the Ofwat consultation was released just two working days after the close of the Defra consultation that is to set out guidance in support of the Charging Rules. There is a clear implication that the Defra consultation was a somewhat meaningless exercise given there was little, if any opportunity for the Defra consultation responses to be distilled, duly considered and factored into the Ofwat consultation. See also paragraph 3.2 of Section 3 of this response.

e) A secondary heading to the Ofwat consultation is "Trust in Water". Corporate trust is an ethos we fully support but before we can place greater reliance on this concept, the Water and Sewerage Sector needs to become more consistent and better managed if not regulated by Ofwat. However, Ofwat's current proposals advocate an even 'lighter' almost entirely non-interventionist approach. This will leave WaSCs and WoCs free to effectively set their own, un-audited Charging Arrangements. Moreover, in the absence of appropriate, 'checks and balances' there is nothing to prevent these Charging Arrangements being based on the most extreme of potential cost scenarios.

   In our opinion and based on the evidence HBF has already presented, this a sector of the Utility Industry that is in urgent need of more effective control and management by the Regulator. At present there is a great deal of mistrust in every aspect of water and sewerage infrastructure delivery. Ofwat's proposals are unlikely to deliver a greater level trust and by Ofwat's own admission, will lead to an increase in disputes to be resolved by the formal determination process, or more worryingly, through the Courts – see page 47 of the consultation.

f) The consultation should have clearly defined what infrastructure charges are to be used for – this remains a critical omission. Moreover, it is concerning to note that despite the developer community having paid over to WaSCs around £2.60 billion in infrastructure charges since sector privatisation in 1989, there is no audit trail as to where, when and how this significant contribution has been invested. The current proposals do not effectively address this issue.

g) The proposals do not adequately address the considerable diversity in customer attitude, and approach that exists within the Water and Sewerage Sector. HBF has presented evidence to this effect and whilst some variation is a reasonable expectation, the degree of diversity remains of concern. The approach to foul sewer modelling being a particular case in point, with Ofwat reluctant to resolve such a vexed issue and/or take up the HBF suggestion that a jointly agreed protocol should be put in place as an integral part of the future Charging Rules. We firmly believe that the latter should be the case, or alternatively for the industry to seek redress through a referral to the Competitions and Markets Authority.

h) The lack of any breakdown of non-contestable costs has been a constant source of concern for most house builders for many years. The need for WaSCs to provide cost transparency, as

proposed in this consultation, is welcome but it would be useful if Ofwat were to define how this is to be undertaken and what items of cost are to be disclosed. We say this as several HBF members are reporting a significant escalation in indirect costs, for example, overheads. This issue was also covered in HBF Paper 12.

i) The underlying principles for reform are reasonable but with a bit more rigour, time and consultation, this could be a productive change that helps promote other government priorities like brownfield regeneration and SuDS. Rather than rushed, ill-considered proposals that levy open-ended costs onto house builders, this could be an opportunity to make a real and positive difference.

SECTION 2: RESPONSES TO QUESTIONS

Our response to each question has deliberately been kept short – section 3 of our submission provides more detailed commentary, where appropriate and is to be read alongside each of the questions.

Question 1: In light of our updates and clarifications do you agree that we still retain the key features and approach of our March proposals?

In essence – no. There are many aspects of the March 'Discussion Paper' that we could not agree with and it is disappointing to note that many of the issues raised in our earlier consultation responses have still to be addressed. At present, we have no confidence that proposals that are effectively built on 'aspiration', coupled with a 'light touch' Regulator approach rather than effective management and control of the Water and Sewerage Sector, will deliver. With an accompanying sectoral lack of understanding of the land allocation and development process *per se* it leaves us with further concerns – see section 3 of this response for further details.

Question 2: Do you agree with updates and clarifications to our proposed rules?

No – there is a compelling need for additional and far more precise definitions. Similarly, more detailed explanation of what can and cannot be included as part of the Charging Arrangements. In our opinion, the following matters must be addressed and in unequivocal terms, as an intrinsic part of the Charging Rules:

- What is the extent of the obligation(s) placed upon all WaSCs and WoCs pursuant to S37 et al of the Water Industry Act 1991?

- What is the extent of the obligation(s) placed upon all WaSCs pursuant to S94 of the Water Industry Act 1991? In the context of existing public foul sewer networks what does effectually provide and maintain mean? Legislation requiring WaSCs to effectually drain their area and to provide and maintain their assets, at their cost, has effectively remained unchanged since the Public Health Act 1936.

- What can or cannot be included as part of a S185 public sewer diversion? How asset betterment is defined and how are developer contributions assessed on a fair, equitable, proportionate and transparent basis?

- Similar principles apply to the diversion of existing water mains.

- What is acceptable in terms of off-site modelling criteria and how are the results of such to be used to determine developer contributions that are fair, equitable, proportionate and transparent? This is a major issue that Ofwat has failed to address.

- What is meant by pre-existing shortfalls in capacity and capability? This should be clearly defined. For example, it is accepted by the Water and Sewerage Sector that excessive surface water/groundwater infiltration into existing foul sewer networks is a pre-existing problem. Moreover, that it falls to the WaSC to deal with and at its cost.
  We agree that existing sewer networks should be modelled in their present condition but the developer should not be expected to fund mitigating infrastructure improvements that are ostensibly not in consequence of new development. However, at least five WaSCs are using pre-existing infiltration to justify extensive and expensive network improvements that they insist are paid for by the developer. Moreover, it has been confirmed by both DCLG and respected Planning Consultants that reliance on planning to resolve such pre-existing problems is *ultra vires* (In a planning law context). This should be made abundantly clear in the Charging Rules. We do not accept that Ofwat can continue to dodge such an important issue.

- What can/cannot be included in off-site requisitions, in particular those specific to off-site sewers? In addition, Ofwat need to be mindful of the fact that recourse to S98 off-site sewer requisition does not happen very often. A combined infrastructure and network improvement charge (as proposed) has the propensity to introduce a charging regime that is neither representative, nor in consequence of new development. It also runs the risk of being disproportionate and therefore, (in our opinion) open to challenge.

- What can/cannot infrastructure charges be used for? For example, they should not be used for maintenance of existing networks – this should be clearly stated. (See later comments).

- How are sites that have had a previous use to be dealt with? This is particularly important given the Government's commitment to increasing development on brownfield land.

Question 3: Do you agree that offsetting the infrastructure charge, rather than requisition charge, has merit? If so, when and how should this change be brought about?

At this stage we do not necessarily agree with this proposal. That said, we are not averse to exploring the concept a little further but would first ask the simple question; what is this part of Ofwat's proposal trying to achieve? We would be interested to see how this would work in practice as the examples used as part of the Task and Finish Group discussions were far from being representative. Moreover, we have previously called for typical examples to be provided to aid both evaluation and discussion but despite assurances that this would be the case, none have been forthcoming.

Question 4: Do you have comments on our approach to implementing the rules?

We have concerns over the rush to introduce a new charging regime that in our opinion, is still not fit for purpose and biased towards the commercial interests of the Water and Sewerage Sector. Moreover, to have new Charging Arrangements in place by the 1st April 2017 without those arrangements, in particular costs having been subjected to any form of scrutiny is a major concern.

Furthermore, based on Ofwat's current proposals the transitional arrangements contain no provision to restrain WaSCs/WoCs from imposing Charging Arrangements that are more expensive for the developer and better suited to the commercial interests of WaSCs and WoCs. Ofwat has made it quite clear that agreement is necessary on any charging structure – this is not helpful when having to deal with monopoly privileged businesses. In our opinion the following implementation process stands the best chance of filtering out as many unintended consequences as possible, whilst making the most productive use of limited resources. More importantly, it is a process that meets the key objectives of fairness, proportionality and transparency:

Each WaSC/WoC sets out their Charging Arrangements by 1st February 2017 – this is still a very tight deadline.

- All Charging Arrangements (costs) are to be accompanied by full disclosure as to how they have been determined.
- Each WaSC/WoC is to issue its draft 'Charging Arrangements'. Thereafter they are to be subjected to local/stakeholder consultation under the auspices of Ofwat – suggested consultation period, two months.
- Amendments to be introduced where appropriate.
- Charging Arrangements to be crystallised and introduced by a defined cut-off date set by Ofwat. Relying on the concept of working 'smarter', we would suggest an implementation date of April 2018 as this will have synergy with the introduction of the intended Market Reforms.

This process may delay the intended introduction on 1st April 2017 but it would represent a fair, equitable, proportionate and transparent introduction of a charging regime that has a better chance of success. It should also minimise the number of determinations. By contrast, the current proposals will see un-audited Charging Arrangements introduced with Ofwat taking corrective post-introduction action, if indeed they and only they, believe it to be appropriate. This type of approach does not build trust and leaves the Developer Community exposed to additional, unbudgeted cost. By following Ofwat's current timescale, the potential (adverse) impact on housing delivery should not be under-estimated and Ofwat have already conceded that they expect their proposed Charging Rules to increase the number of formal determinations. Disputes equate to delays in housing provision.

Question 5: Do you agree with the approach we have taken in our draft impact assessment? Can you provide quantitative figures in terms of the potential benefits or costs? Is there anything we have missed?

Given the complete lack of data and evidence in respect of costs/quantum within the impact assessment we found this question quite surprising. In many respects the complete absence of any cost comparison data has denied all consultees the opportunity to give the proposals the scrutiny they deserve. In many respects, this single question alone reinforces why the HBF and its members still have serious concerns, in particular when it comes to future project viability, especially at the crucial land acquisition stage. Similarly, the potential impact on new home

provision in general. No business would make key investment decisions without having access to quantitative and qualitative evidence/data – we consider the impact assessment both poor and disingenuous – it is a critical flaw in this consultation. Furthermore, the evidence sought in the second question has to some degree already been provided by the HBF by way of the Information Papers previously disclosed. Again, the house building industry's comments and concerns do not seem to have been considered.

Question 6: Do you have any comments on the drafting of our new connections rules?

See section 3 of our response.

Question 7: Do you have any comments on the draft changes to the charges scheme rules?

We are somewhat confused by this question as it appears to cover the same ground as questions 1 and 2. That said, see our earlier responses and those contained in section 3.

Question 8: Do you have any comments on the drafting of our proposed licence modification, including the wording of the illustrative example?

In our opinion, more salient information is required. For example, it does not explain how WaSCs/WoCs can undertake off-sets for infrastructure charges, i.e. credits for sites that have had a former use. It also fails to address the 5-year time period where off-sets/credits are applicable, similarly, matters specific to eligibility. Licence Condition C should also contain an explicit definition as to what infrastructure charges can be used for, i.e. they should not be used for asset maintenance – an approach that has already been conceded by at least one WaSC.

SECTION 3: OFWAT CHARGING RULES CONSULTATION – GENERAL REVIEW/CRITIQUE

3.0 This section of our response constitutes a more in-depth critique of the Ofwat consultation. It considers a number of key issues beyond those limited to the eight questions posed. In many respects it distils the major issues and concerns that HBF has raised during the last two years or so. Moreover, we view this part of our response as being of equal if not greater relevance and/or importance to the limited number of questions that have been posed.

3.1 Impact Assessment & Related Matters

In 2012 Defra issued their first in-depth consultation on new Charging Rules for the Water & Sewerage Sector, namely:

"Charging for Water & Sewerage Infrastructure within New Development (IA No. Defra 1383)"

Of particular note, the accompanying Regulatory Impact Assessment (Full Economic Assessment) included the following directive statement:

"Description and scale of key monetised costs by main affected groups: At this stage costs have not been monetised – we would expect Ofwat to consider these in the development of new guidance". **(Our underlining for emphasis).**

The Ofwat consultation of July 2016 makes no attempt to fulfil this obligation but instead cites and depends upon a lack of available evidence from WaSCs and WoCs to defend its position. Moreover, two statements in the accompanying Ofwat Impact Assessment (Appendix 4 to the consultation) contain two statements that in our opinion are wholly unacceptable:

(i) "Costs have not been monetised because it is inherently difficult to say what the costs will be. Costs will not be any greater than at present, or if so, only minimally greater".

(ii) "Benefits have not been monetised due to a lack of data".

How a fundamental change in Water and Sewerage Sector charging can even be considered let alone introduced in the absence of crucial financial evidence, is quite concerning.

3.0.1 With no effective Regulatory Impact Assessment in place how can we possibly move forward on an informed basis? Furthermore, this consultation effectively places responsibility for each 'impact assessment' in the hands of individual WaSCs and WoCs as they formulate their respective 'Charging Arrangements'. In our opinion and for the reasons articulated earlier, this consultation could be considered to be fatally flawed. Moreover, its proposals are predicated on a new Charging Regime that is heroically aspirational whilst being remarkably thin on factual evidence, in particular when it comes to costs/quantum.

3.0.2 Following the Defra consultation of 2012 Ofwat have had a full four years to gather the necessary evidence in terms of current charges and costs. The conspicuous absence of such vital information in this, the latest of Ofwat's consultations, does not allow for informed consideration of the proposed Charging Rules. In many respects, we have no idea what future costs will be. For the Developer Community, what is being presented is effectively a venture into the unknown, underscored by aspirational reassurances that 'it will be alright on the night'. Not an appropriate way forward for such a major change in the delivery of water and sewerage infrastructure.

3.0.3 A well-researched and considered Impact Assessment is a fundamental pre-requisite for any policy change of magnitude and in this instance, for an Industry Economic Regulator not to produce a substantive Impact Assessment is an abdication of its responsibilities. Moreover, in June 2013 the EFRA Select Committee commented as follows, in the context of reviewing the then Draft Water Bill:

"The Government believes that the mechanisms in the Bill that allow Ofwat to set out enforceable charging rules and require them to take account of ministerial guidance will enable it to set fair and appropriate charges in consultation with stakeholders". **(Our underlining for emphasis).**

This obligation was crystallised in the eventual Water Act 2014 but it would appear that the requirement to first heed Charging Rule guidance, as issued by Defra on behalf of the Minister, has effectively been ignored in the apparent rush to introduce the current consultation. Our view is that this represents a further flaw in the consultation process.

3.0.4 On page 7 of the Ofwat Regulatory Impact Assessment, we also found the following statement of some concern:

"A rule-based framework will allow us to assess compliance with our rules rather than determining whether charges comply with primary legislation".

This reads as though the 'rules' will subjugate legislation – in our view, this is unacceptable. It would be far more appropriate for Ofwat to re-affirm precisely what the statutory obligation(s) of all WaSCs and WoCs are before crystallising any intended Charging Rules, in particular the statutory obligations placed upon all WaSCs and WoCs, by virtue of S37 *et al* and S94 of the Water Industry Act 1991, as well as Licence Condition C.

3.2 Consultation Period & Proposed Transitional Arrangements

3.0.5 Issued a mere 2 working days after the close of the Defra Charging Rule Guidance consultation, (22nd July 2016) the latter having set out proposals for the quasi-statutory 'guidance' that is to inform the new Charging Rules, one can reasonably surmise that that the Defra consultation was a somewhat meaningless exercise.
In a procedural context, it is quite clear that the Ofwat consultation was finalised well in advance of 22nd July. Moreover, Ofwat's now declared timetable and objectives lend credible support to this comment.

3.0.6 The only consistency that can be attributed to the Ofwat consultation of August 2016 is that it continues with the theme of presenting ill-considered, *fait accompli'* rules to the exclusion of resolving many of the critical issues raised by the HBF in a series of evidence-based papers. These 'papers' have been disclosed to partner and stakeholder interests over the last year or so with the aim of providing a snapshot of reality through the eyes of a developer customer, in addition to informing Defra Task and Finish Group discussions specific to the Charging Rules - see 'reference' section cited at the close of our response.

3.0.7 To suggest that further modifications to the 'Charging Rules' are likely take place after Defra has published the response to its recent and related consultation, (Defra response expected in autumn 2016) raises a number of concerns. With the Ofwat timetable for the introduction of the new Charging Rules effectively crystallised, the apparent lack of synergy with the Defra consultation will mean that any corrective change(s) that may need to be considered could well be discounted by Ofwat. Similarly, as WaSCs and WoCs will be well advanced in setting their respective charging arrangements, any sensible changes arising from the Defra consultation may also run the risk of being discarded. There is a serious and worrying disconnect here.

3.3 Other Relevant Comments

3.3.1 The Ofwat consultation contains a number of sweeping statements about 'saving cost for developers' and 'helping housing delivery' but in the absence of supporting evidence, these must remain as unsubstantiated and somewhat hollow assertions. Furthermore, what is stated/suggested by Ofwat remains highly speculative – based on HBF evidence and the experience of our members, there is every prospect that developer costs will increase. The subjective variability in approach by all WaSCs and WoCs when it comes to specific sections of extant legislation, especially where charging is already taking place, remains a key concern. There is nothing to stop the Water and Sewerage Sector introducing Charging Arrangements that reflect a 'worst case' cost scenario and/or Charging Arrangements lacking

robust supporting evidence. A 'light touch' Regulator approach by Ofwat has the propensity for a significant increase in Developer costs. There is past evidence to this effect.

3.3.2 The concept of introducing 'rules' implies a degree of rigour or control – the Ofwat proposals fall a long way short of this simple requirement. In many respects the current proposals are nothing more than a weak, directional protocol that will leave WaSCs and WoCs free to carry on as before. To be effective, rules need to have enforceable quantitative and qualitative objectives – the consultation contains neither and it is difficult to understand how the Regulator will be able to exercise effective management and control over 20+ divergent approaches to defining developer costs at a time when consistency, fairness and proportionality are key objectives.

3.3.3 The Ofwat proposals fail to deal with two of the most vexed issue(s) raised by the HBF and many of its members, namely, how several WaSCs interpret and thereafter, approach their obligations under S37 *et al* and S94 of the Water Industry Act 1991, in addition to their obligations/limitations under Licence Condition C. Similarly, the right for a developer to connect to the public sewerage system under S106 of the same 'Act'. In many respects, one can reasonably conclude that the Ofwat proposals better serve the commercial interests of the Water & Sewerage Sector, rather than the needs of a major customer contributing in excess of 3% to the UK's GDP through the provision of much needed new housing.

3.3.4 Allowing WaSCs and WoCs to tailor charges to their local circumstances, without a clear demonstration of what 'local circumstances' look like, raises further concerns. Similarly, the fact that the initial and founding rationale of each respective charge appears to undergo no Regulatory assessment prior to it being crystallised. This is not consistent with established Regulatory Impact procedures and represents an approach that is not conducive to serving the interests of customers from a fair, equitable, proportionate and transparent perspective. Moreover, if/when respective Charging Arrangements are eventually disclosed by WaSCs and/or WoCs how can inequitable costs be challenged by developers? Is the house building industry to accept what is presented without the ability to challenge in a fair and timely manner? Furthermore, if we are to build trust then the Water & Sewerage Sector requires more prescriptive management and control, not an increasingly light touch approach. Handing over to WaSCs and WoCs a significant amount of discretion in setting infrastructure and other charges creates the wrong impression in that it sends a clear and unequivocal signal that the commercial strength that comes with the exercise of monopoly privileges is acceptable – this is not conducive to a productive working relationship. Neither does it foster fair, equitable and proportionate business conduct. It is also contrary to establishing a business relationship based on trust. Moreover, such an approach is not adopted by any other Utility Regulator. Indeed, it is noteworthy that so called 'voluntary arrangement' were introduced as part of the reforms in the Energy Sector but a complete failure of such forced their early withdrawal in favour of a more effective interventionist approach by the Regulator. In many respects and for consistency, this is the 'management' model that should be replicated in the Water and Sewerage Sector.

3.3.5 Ofwat's proposals will not stop WaSCs and WoCs using commercial arrangements to circumvent the legislation – these arrangements will fall outside of Ofwat's remit and it remains a concern that Ofwat are advocating the flexibility within WaSCs and WoCs that will allow this to take place – see also, our earlier comments relating to four WaSCs who have already confirmed that intend to continue to use the planning process to secure developer funding for off-site foul sewer network improvements, even if it is not in consequence of new development.

3.3.6 As proposed, the new Charging Rules will effectively take us back to the infrastructure charge 'free for all' that came to pass following 'Sector' privatisation in 1989. With Ofwat now proposing that all WaSCs and WoCs will be able to set a single, untested (in the short term) infrastructure charge that is to reflect off-site network reinforcement, plus infrastructure charges, can only have one outcome, namely, additional costs will more than likely be imposed upon developers. For example, based on evidence previously provided by the HBF, the diversity/variability in charging across all WaSCs and WoCs has been shown to be wholly inconsistent and by several orders of magnitude. Moreover, the 'combined' approach, now advocated by Ofwat, could see a single sewerage infrastructure charge ranging from the current £367/dwelling to figures conceivably in excess £10,000/dwelling. A recent Southern Water demand for developer funded off-site foul sewer network reinforcement equated to £13,350/dwelling for work that is not considered to be in consequence of new development. More importantly, if costs of this magnitude are allowed to become common-place it would require a compensating reduction in land value of around £0.55 million/hectare, or in the case in question, compromised project viability with development now unlikely to proceed. We therefore have many concerns about the approach now advocated by Ofwat.

3.3.7 The new Charging Rules will allow WaSCs and WoCs to have self-audit arrangements by way of an annual assurance report. We seriously question the wisdom of such a principle in a part of the Utility Sector made up of a series of monopoly privileged businesses. Just how robust will the Regulator audit of these reports really be?

3.3.8 Ofwat appear to have turned aside the evidence provided by the HBF in its response to proposals for variable infrastructure charges (potential reductions), i.e. in those instances when developers incorporate water saving devices that contribute to lower water use criteria than the current Building Regulations require. Importantly, the case study cited in the Ofwat consultation is out of context as the intended pilot(s) are taking place in a local authority/WaSC district that is already defined as a 'water stress' area. Moreover, in response to this issue local plan policies already require the provision of lower water usage fittings. More importantly, the need for compliance with the Code for Sustainable Homes has been cited as the underlying basis for this concept but the 'Code' was actually withdrawn by Government over a year ago with the Building Regulations amended accordingly. We would also refer Ofwat to our separate e-mail correspondence concerning this matter given that the proposals under this section of the consultation come many unintended and expensive consequences for house builders.

3.3.9 The Ofwat proposals will not deal with the frequently articulated complaint from WaSCs that the local plan process does not provide sufficient certainty when considering water and sewerage infrastructure investment decisions. We disagree and on several counts – see the content of earlier evidenced-based papers produced by HBF. More importantly, for some WaSCs, in particular those in the south of England, the consultation provides reassuring comfort that they will be able to continue as before by undertaking little if indeed any local plan related investment in fulfilment of their S37 and S94 obligations - that is, until approached by a developer considering the development of an allocated/consented site. Based on the experience of HBF members, the approach now advocated is unlikely to facilitate the provision of new homes. Rather, it has the propensity to introduce barriers to housing delivery through compromised project viability, in addition to delaying new site starts.

3.3.10 In the context of housing delivery, the consultation lays bare how little the Water and Sewerage Sector, including Ofwat, understand about housing market dynamics, land acquisition, the planning process and the delivery of new homes. Moreover, the following statement cited in the Ofwat consultation raises a number of concerns:

> ***"…. should allow companies more freedom to incentivise development to take place in areas with existing capacity in infrastructure or where the cost of providing additional infrastructure is less …."***

To suggest that the proposals will facilitate local plan decisions (in the short term) shows a complete lack of understanding of both the local plan land allocation process and the development process *per se*. It does not work in the manner perceived by Ofwat. Furthermore, in the context of existing local plan land use allocations, if the Ofwat approach was to become anywhere close to reality, the unintended consequence would be a significant number of local plans being found 'unsound'.

3.3.11 The rationale for requisitioning, in particular S98 sewer requisitions, needs to be better explained. The origin of 'requisitioning' dates back to the Water Act of 1973, having been introduced in response to a growing number of instances when third party land owners were imposing inequitable payment demands for the construction of off-site sewers across third party land. At the time, if there was no agreement with land owners to construct such sewers to an agreed point of outfall, it was a valid reason for planning refusal. Requisitioning was never seen as a mechanism to facilitate off-site sewer network improvement and/or reinforcement.

3.3.12 The consultation confirms that developers should not be required to bear the costs of reinforcing, upgrading or otherwise changing existing network infrastructure to address pre-existing shortfalls in capacity or capability. This is most welcome but the 'rules' need to state in unequivocal terms what is defined as a pre-existing deficit, shortfall or problem, for example, high volumes of surface water/groundwater ingress into existing foul sewers. Far greater definition of what this actually means is essential to enable fair, equitable and representative Charging Arrangements to be produced by WaSCs.

3.3.13 The rules should state quite clearly what is acceptable in terms of foul sewer capacity modelling and how the results of such are used to determine equitable and proportionate developer contributions. What is being allowed to take place at present is accompanied by unprecedented variability but Ofwat have effectively refused to intervene and work with WaSCs and the Developer Community to agree an appropriate and representative protocol. There are a raft of issues surrounding existing foul sewer modelling and these remain a serious concern for the HBF and its members given the adverse implications that arise in terms of delay, (up to 6 to 9 months in some instances) cost(s) (excessive) and the interpretation of modelling results. Moreover, we have gone in excess of a year with requests to WaSCs for the disclosure of modelling criteria – these requests have effectively been ignored even when modelling work (Up to £50k in some instances) has been paid for by HBF members.

3.3.14 Within the consultation, Ofwat accept that the imposition of the new Charging Rules may well result in an increase in the number of determinations, in particular in the short term – we agree. Of more concern is that on page 47 of the consultation, Ofwat also confirm that larger complaints over infrastructure charges will be decided through the courts rather than through

the Water Redress Scheme, (WATRS). This is unacceptable, similarly, the fact that anything other than minor economic disputes will also fall outside of Ofwat's remit and left to be dealt with through the Courts, including possible Judicial Reviews. (Minor economic disputes have not been defined by Ofwat). In short, there is no expedited dispute resolution process. Moreover, the approach advocated implies an abdication of Regulator responsibility – this continues to be consistent with an earlier observation/comment from the Government Select Committee, who at the time were critical of Ofwat's lack of intervention.

3.3.15 What do Ofwat envisage in terms of charges to promote environmental protection? What environmental protection measures and legitimate costs will this capture? The Charging Rules need to be far more explicit on all counts. This has the propensity to be an open cheque book.

3.3.16 The new Charging Rules will not stop WaSCs relying on an inappropriate use of the planning system to resolve pre-existing network problems at the developer's expense. In many respects there will be little change to what currently takes place within five established WaSC operating areas, for example Southern Water, who routinely state that there is no capacity in their foul sewer network(s) whenever a house builder submits a planning application. As previously advised, reliance on the planning system to resolve pre-existing problems that are the statutory obligation of other bodies is effectively, *ultra vires* and open to challenge up to and including the Secretary of State.

3.3.17 There are far too many loose ends associated with this consultation. Whilst the need for change has been recognised by Ofwat, house builders now face the prospect of WaSC/WoC Charging Arrangements that have not been properly scrutinised and/or subjected to rigorous evaluation through a formal review/consultation process before they are introduced. This is a further extension of the *fait accompli* approach that has been very evident as the Charging Rules have evolved. Moreover, the various evidence based papers produced by the HBF appear to have been ignored, despite containing many sensible recommendations.

3.3.18 Ofwat admit that in the past there has never been any accounting of costs against recovery but that they now want WaSCs and WoCs to undertake this task from April 2017, i.e. once the new Charging Rules are implemented. This is a sad indictment of Ofwat not regulating a critically important area – see pages 33 and 34 of the consultation.

3.3.19 It is becoming increasingly apparent (through our separate discussions with WaSCs) that many WaSCs and WoCs are failing to understand the direction Ofwat wanted them to take when it comes to any form of off-site network reinforcement.
Clearly, there is a serious disconnect here when considered alongside the intent that underpinned Ofwat's earlier Emerging Thinking consultation. Moreover, it is far from clear in this latest consultation what Ofwat expects. Furthermore, the whole area of Licence Condition C in respect of infrastructure charges is far from satisfactory from the HBF perspective.

3.3.20 The transitional arrangements are unlikely to work and have the propensity to introduce confusion and delay. In our opinion, there will be no smooth transition.

3.3.21 Page 9 of the consultation contains a statement of grave concern, namely, companies will be allowed to introduce innovative charges. In a Utility Sector that lacks meaningful and

responsive competition this is a worrying change of direction, made all the more concerning by a lack of definition and quantum. What is intended?

3.3.22 The unilateral withdrawal of the 12-year income deficit approach is a concern given that no definitive cost comparisons support this part of the consultation.

3.3.23 Informal discussions with two WaSCs over the last few days has revealed that even parts of the Water & Sewerage Sector are struggling to understand what they in turn are required to do. In both instances, each WaSC has commented that the Ofwat consultation and its proposals lack clear direction – this is entirely consistent with the HBF view.

3.3.24 Looking at the role of SLOs HBF has always viewed these organisations as being integral to introducing greater competition into the Water & Sewerage Sector. However, the Ofwat proposals in this regard are structured in such that they will be counter-intuitive, having the propensity to reduce competition. In this context, we are in total agreement with the comments made by Fair Water Connections in their response to this consultation.

SECTION 4: CONCLUDING COMMENTS

As proposed, we cannot see the Charging Rules and the subsequent Charging Arrangements being the success that Ofwat perceive. In many respects, this is a poor consultation made all the more so by a lack of evidence in respect of quantum/future cost.

There is a reliance on heroic aspiration on the part of Ofwat but in reality, the lack of direction and effective Regulatory control over many aspects of water and sewerage procurement/delivery is of noteworthy concern. Moreover, for two WaSCs to admit that they also considered the consultation proposals lacked meaningful direction, were somewhat nebulous and left them wondering what was expected of them, only serves to reinforce the HBF comments and our underlying concerns.

Importantly, the imposition of Charging Arrangements that have not undergone robust scrutiny before being introduced represents a significant risk to end customers, in particular the house building industry.

The prospect of unacceptable increases in cost, accompanied by many potential unintended consequences, leading to possible delays in housing delivery, are very real, especially if WaSCs continue to use the planning system as they are at present.

It also seems somewhat futile and a waste of limited resources that Ofwat accept, by their own admission that there will likely be a significant increase in the number of disputes- especially in the short term. Disputes have wider cost and delay implications. Furthermore, by placing a greater reliance on dispute resolution through the Courts rather than through effective Regulatory control will result in further expense and delay.

Whilst disputes are being resolved we are not building houses. As we have advocated in our response, it is far better to resolve the issues before they impact on housing delivery.

The HBF remains committed to seeing effective reform within the Water & Sewerage Sector, indeed it is long overdue. However, the current proposals from Ofwat do not, in our opinion, meet the required objective(s). We naturally have what we believe to be sensible and workable

alternatives that meet the objectives of fairness, appropriate commercial balance, proportionate charging and transparency and will be more than happy to discuss these in greater detail. In many respects we have already disclosed this information in HBF Paper 12 but it appears to have been ignored.

References: HBF Evidence-based Papers Previously Disclosed

1. **General Paper – Sewerage Infrastructure Availability -v- New Housing Delivery (A fundamentally Important Question) – 4th Oct 2015**
2. **Paper 1 – Off-site Network Reinforcement & the Architecture of the Charging Rules (February 2016)**
3. **Paper 2 – The Architecture of the Charging Rules in Relation to S45 (WIA 1991) – Charges for the Making of a Connection (Feb 2016)**
4. **Paper 3 - The Architecture of the Charging Rules in Relation to S185 (WIA 1991) – Charges for Moving Infrastructure & Apparatus (Feb 2016)**
5. **Paper 4 – Section 46 WIA 1991 – Charges for Ancillary Works Relating to the Making of a Connection with a Water Main (Feb 2016)**
6. **Paper 5 – Section 104 WIA 1991 – Charges Contained in Agreements Relating to the Adoption of Sewers Etc. [Self-Lay] (Feb 2016)**
7. **Paper 6 – Water UK Market Reform/Charging Rules Workshop – HBF Comments/Response – 8th February 2016**
8. **Paper 7 – Legal Aspects of the Supreme Court Decision of 9th Sept 2009 [Barratt -v- Welsh Water (October 2015)**
9. **Paper 8 – Abstracts from Past Ofwat Price Determinations (Future Water & Sewerage Charges 2005-10 & 2010-15 Final Determinations) (February 2016)**
10. **Paper 9 – Planning Conditions/Section 106 & Foul Sewerage Infrastructure (20th March 2016)**
11. **Paper 10 – Market Reform & Charging Rules: Defra Planning T & F Group – Evidence as at 14th April 2016**
12. **Paper 11 – WaSC Use of Planning to Secure Developer Contributions – (4th June 2016)**
13. **Paper 12 – The Charging Rules: What Would Be Good from the HBF Members Perspective (June 2016)**
14. **Presentation to Defra and Shared with Ofwat (Foul Sewer Modelling – A Health Warning for Housing Delivery) 6th July 2016**