

31 May 2017

Trust in water

Proposal to grant a variation of appointment to Icosa Water Services Limited as a water and sewerage company for Barnhorn Green, Bexhill-on-Sea

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Contents

1. About this document	3
2. The Site	4
3. The applicant	5
4. The proposal	6
5. Our approach to the assessment of this application	7
6. The application	9
7. Conclusion and next steps	13
8. Site maps	14

1. About this document

This notice is a consultation under section 8(3) of the Water Industry Act 1991 on our proposal to grant a variation of appointment to Icosa Water Services Limited as a water and sewerage company and make consequential variations to the appointments of South East Water Limited as a water company and Southern Water Limited as a sewerage company.

The consultation period will last for 28 days from the date of publication of this notice. Having considered any representations submitted during the consultation period in response to the consultation, Ofwat will decide whether or not to grant a variation of appointment to Icosa Water Services Limited as a water and sewerage company.

2. The Site

Icosa Water Services Limited (“**IWS**”) has applied to be the water and sewerage company for Barnhorn Green in Bexhill-on-Sea “**the Site**”.

When fully built, the Site will consist of 341 domestic dwellings, and a number of non-household properties such as office spaces, a nursing home, a doctor's surgery and a primary school. The scheme received outline planning approval for 275 units in November 2014.

The Site is within the water and sewerage services areas of South East Water Limited (“**SEW**”) and Southern Water Limited (“**SRN**”) respectively. IWS is in the process of negotiating bulk agreements with both SEW and SRN.

3. The applicant

IWS was granted appointments as a water and sewerage undertaker on 31 May 2017. It took over a site called West Raynham in Norfolk, from Icosa Water Limited. Icosa Water Limited is the parent company of IWS and it was appointed as a water and sewerage undertaker on 20 October 2016. By consent, it asked that we terminate its appointments and appoint IWS as its replacement for the West Raynham site.

4. The proposal

Ofwat proposes to:

- grant a variation of appointment to IWS as a water and sewerage company; and
- vary the appointment of SEW as a water company and SRN as a sewerage company by excluding the Site from their water supply area and sewerage services area, respectively.

By means of the above, IWS will become the water and sewerage services supplier for the Site.

5. Our approach to the assessment of this application

The new appointment and variation mechanism, set out in primary legislation¹, 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. In particular, in relation to unserved sites, we consider that we must ensure that the future 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:

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

We clarified these two policy principles in February 2011 when we published our New appointments and variations – [policy](#) and [process](#) documents. In November 2012, we published our '[Statement on our approach for assessing financial viability of applications for new appointments and variations](#)'. This states that we will adopt a company-based assessment of financial viability, rather than a detailed site-based assessment, where it is appropriate to do so.

When we assess whether customers will be no worse off as a result of the appointment, we not only consider the customers on the site but also the generality of customers. These include not only the customers of the existing provider but also

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

customers more generally across England and Wales, who, in our view, benefit from the effective operation of the new appointment and variation mechanism.

6. The application

IWS has applied to be the water and sewerage company for the Site under the unserved criterion, set out in section 7(4)(b) Water Industry Act 1991 (“**the Act**”).

6.1 Unserved status of the Site

Unserved: 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 served by the existing appointee.

IWS submitted an independent reporter’s site status report to show that the Site is currently unserved. The reporter’s report set out that there is one property (“**the Property**”) within the variation boundary which is connected to both the water and sewerage networks of the incumbents. The Property is adjacent to land which will form the main access road to the Site but does not form part of the development, although it is owned by the developer. The reporter’s report recommended that if the Site is to be considered un-served, that the proposed development boundary be modified to exclude the land and buildings associated with the Property.

The report concluded that (with the exception of the Property) the plan reviewed did not indicate the presence of any public water supply assets. The report also concluded that there is a sewer rising main running south west across the eastern side of the Site. There is also an existing sewage pumping station outside the development boundary that is connected to this rising main – SRN confirmed that it owns both of these assets.

The report noted there are no connections to the rising main within the site boundary (with the exception of the Property). It also stated that (with the exception of the Property) the Site is unserved for surface water drainage.

Accordingly, in response to the reporter’s report, IWS resubmitted the Site map to Ofwat, with the boundary now excluding the Property.

We shared the reporter’s report with both SEW and SRN on 23 March 2017. Both SEW and SRN have stated that they agree that the Site is unserved. Given the reporter’s report and the confirmation of both companies, we are satisfied that the Site is unserved for water and sewerage services.

6.2 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 both existing customers as well as potential new 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 and variations – only business, charity and public sector customers in England and Wales are able to choose their supplier².

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 in whose geographical area the relevant site sits. We will continue to protect customers on a site by regulating the new appointee's prices and service levels.

6.3 Price

IWS proposes to match its customer charges with the charges of customers of SEW and SRN – i.e. – it will not offer a discount.

6.4 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 and leakage and a Customer Code for its household customers. We have assessed IWS' proposed Codes of Practice and Customer Code, and our view is that these are of an appropriate standard. Our view is that customers on the Site would be no worse off in relation to the points covered by the above Codes of Practice and the Customer Code than they would be if SEW and SRN were to be the customers' water and sewerage suppliers, respectively.

² The majority of business, charity and public sector customers ("Business Customers") who are in the area of an appointed company that operates wholly or mainly in England have been able, since 1 April 2017, to switch suppliers of water and sewerage. For companies operating wholly or mainly in Wales, only those Business Customers supplied with at least 50 MI per year, can switch suppliers but only in respect of water, not sewerage services.

6.5 Site owner choice

IWS has the consent of the developer, Barrett David Wilson Homes, to become the water and sewerage provider for the Site.

6.6 Environment Agency (EA) and Drinking Water Inspectorate (DWI)

We take the views of these organisations into account before progressing to formal consultation on an application for a new appointment. Both the EA and DWI informed us that they are content for us to consult on this application³.

6.7 SEW's and SRN's existing customers

In considering whether customers will be no worse off, we also considered the potential effects of this variation on the prices that SEW's and SRN'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. 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.

We have assessed the potential magnitude of this impact by comparing how much SEW and SRN might have expected to receive in revenue if they were to serve the Site directly, as opposed to the revenues they are likely to receive from the proposed arrangement with IWS.

We recently updated the approach we take to estimating the impact granting a new appointment may have on the annual bills of the incumbent's customers. We updated the approach to reflect the current price setting regime and the latest financial data in our possession. We will refine our approach further to take into

³ The Environment Agency and the Drinking Water Inspectorate will also be formally consulted on the proposals, as they are on the list of organisations which must be formally consulted as set out in section 8(4)(b) of the Act.

account data that we will receive in July 2017. For the purposes of this assessment, we estimated the impact using our previous approach and our revised approach.

Using our latest approach, we estimate a potential £0.06 increase of the water bills of existing SEW customers, and a potential £0.02 increase of the sewerage bills of existing SRN customers if we grant this variation to IWS.

Using our previous approach we estimate a potential £0.01 increase on the water bills of existing SEW customers, and a potential £0.00 increase on the sewerage bills of existing SRN customers if we grant this variation to IWS. The difference between these two methods is therefore small.

Our estimates do not take into account the potential spill-over benefits to customers arising from dynamic efficiencies achieved as a result of the competitive process to win sites.

We consider that granting this variation to IWS would have a very small financial impact on customers' bills and could have potential benefits for customers.

6.8 Ability to finance and properly carry out its 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 and sewerage company.

We have considered the estimated revenues and costs of the entire Site relating to water and sewerage services should the relevant variation be granted. We are satisfied that the Site demonstrates financial viability.

We are satisfied that the financial security provided by the applicant's parent company complies with our policy requirement, in that it covers one year's annual operating costs required to supply the number of connections the business is projected to have in two years' time.

On this basis, our current view is that the risk of this Site not being financially viable is small and as a result we are currently satisfied that Icosa Water would be able to finance its functions if the new appointment is granted.

7. Conclusion and next steps

In assessing IWS' application, we have considered the general benefits of new appointments. Our view is that our two key policy principles would be met in this case, as customers would be no worse off, and IWS is likely to be able to finance, and carry out, its functions. We have also considered the effects of granting this variation on the existing customers of SEW and SRN.

We are currently minded to grant the variation under the unserved criterion and we are consulting on our proposal to do so.

7.1 Where to send submissions

Any person who wishes to make representations or objections with respect to the application should do so in writing (which includes by email) to Brigitte Gaylor at Centre City Tower, 7 Hill Street, Birmingham, B5 4UA or by email at brigitte.gaylor@ofwat.gsi.gov.uk

Representations must be received by Ofwat no later than 17:00 hours on 28 June 2017. Further information about how to make representations or objections, including information on the treatment of confidential information, can be obtained from Ofwat at the above address or at <http://www.ofwat.gov.uk/foi/>

Ofwat will only use the information you have provided for the purpose of this consultation. We will retain your information in accordance with Ofwat's retention schedule and will not share with third parties unless we have a legal obligation to do so. For further information please see Ofwat's Privacy Policy in our [Publication Scheme](#).

Sewerage Map

