

9 October 2017

Trust in water

Proposal to grant a variation of appointment to Icosa Water Services Limited to enable it to provide sewerage services to a site called Union Corner

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1. About this document

We propose granting a variation of appointment to Icosa Water Services Limited (“**IWS**”) as a sewerage company and varying the appointment of South West Water (“**SWB**”) as a sewerage company. This notice is a consultation on this proposal under section 8(3) of the Water Industry Act 1991.

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 the variations of appointment set out above.

2. The Site

IWS has applied for a variation of its appointment to be able to provide sewerage services to a site called Union Corner (**“the Site”**), which is in SWB’s sewerage services area.

When fully built the Site will consist of 104 household dwellings; this is made up of 68 open market homes and 36 affordable housing units. The scheme received full planning approval in November 2016.

The site is expected to be fully built in September 2019.

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 sewerage company; and
- vary the appointment of SWB as a sewerage company by excluding the Site from its sewerage services area.

By means of the above, IWS will become the 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/or 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 customers more generally across England and Wales, who in our view benefit from the effective operation of the new appointment and variation mechanism.

¹ The legal framework for new appointments is set out in the Water Industry Act 1991 (WIA). Section 7 of the WIA 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.

6. The application

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

6.1 Unserved/consented/large user 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 provided us with a letter from SWB confirming they agreed that the Site was unserved. The Site predominantly comprises green-field land used for agricultural and recreational purposes. Having reviewed the facts, we are satisfied that the Site is unserved.

We received confirmation that SWB is satisfied that the Site is unserved on 14 March 2017.

6.2 Protecting customers

Ofwat acts to protect customers, 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 certain 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.

² The majority of business, charity and public sector customers (“Business Customers”) where the area of the relevant appointed company is wholly or mainly in England were able, from 1 April 2017, to switch their retail suppliers. Where the appointed company operates wholly or mainly in Wales, Business Customers whose premises are, or are likely to be, supplied with at least 50 MI per year are able to switch retail water suppliers (but not retail sewerage services).

6.3 Price

IWS proposes to match SWB's charges for its customers on the Site. It does not propose to offer customers a discount beyond those charges.

6.4 Levels of service

Every appointee is required by its conditions of Appointment to publish a Code of Practice on debt and a Customer Code for its household customers. We have assessed IWS's proposed Code 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 Code of Practice and the Customer Code than they would have been if SWB were to be the customers' sewerage services provider.

6.5 Site owner choice

IWS has the consent of the developer (Barratt Homes) to become the sewerage services provider.

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 or variation. Both the EA and DWI informed us that they are content for us to consult on this application³.

6.8 Incumbent'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 SWB'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

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 WIA.

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.

In assessing the impact that granting the Site may have on the incumbent’s customers, we compare the revenue the incumbent might have been expected to receive and the maintenance costs it would expect to incur if it were to serve the Site directly, as opposed to the revenues it would receive and costs it would incur from the proposed variation arrangement.

We recently updated the approach we take to this calculation to reflect the current price setting regime and the latest financial data. Our previous approach relied on asset data that had previously been provided by the water and wastewater companies, but which we no longer collect. As a result, our old approach to assessing the bill impacts relied on increasingly outdated information, making it less reliable. Additionally, we now have access to information that was not available when our initial methodology for assessing bill impacts was designed. This includes information such as the accounting separation information data that the companies provide to us on an annual basis. We will continue to refine our approach further to take into account data that we will receive each year in July. For the purposes of this assessment, we have used our updated approach.

Using our updated approach, we estimate a potential £0.006 increase to the sewerage bills of existing SWB customers if we grant this variation to IWS.

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.

Therefore we consider that granting this variation to IWS would have a very small financial impact on SWB’s customers’ bills and could have potential benefits for customers.

6.9 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/or sewerage company.

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

IWS has provided bank statements, showing a balance that indicates it has sufficient security in place for this application in line with our minimum requirements.

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 IWS would be able to finance its functions if the variation is granted.

7. Conclusion and next steps

In assessing IWS's 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 would be able to finance, and carry out, its functions. We have also considered the effects of granting this variation on the existing customers of SWB.

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

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 the Case Management Office at Centre City Tower, 7 Hill Street, Birmingham, B5 4UA or by email at andrew.cheema@ofwat.gsi.gov.uk.

Representations must be received by Ofwat no later than 17.00 hours on 6 November 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](#).

8. Site maps

Inset plan - sewerage

