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Trust in water

# Modification to Instruments of Appointment for new connections charging

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## About this document

This document provides notice of a modification that we have recently made to the licences of the water companies that are wholly or mainly in England. The Welsh Government is separately considering how the provision of new connection by water companies should be charged for in Wales.

This modification relates to licence condition C and was made so that the water companies could implement our new charging rules on 1 April 2018.

### Implications for water companies

The licence condition C modification removes the current cap on the maximum infrastructure charge that a water company could charge when connecting new properties to the public water and sewerage system. We needed to remove this because after 1 April 2018, infrastructure charges will no longer be a fixed charge that water companies can levy whenever a new property is connected to their network. Instead, this will be a charge that reflects general network reinforcement costs that will be incurred by a water company.

### Implications for customers

We consider developers will benefit from the new connection charging rules that will come into place on 1 April 2018 as charges will better reflect the cost of the services. We have also included transitional provisions in the licence modifications so that, for example, developers will not pay twice for network reinforcement costs. Developers can choose to pay for works under the current charging arrangements rather than the new charging rules, if they agree this with their water company before 1 April 2018.

For new appointees, we have simply removed licence condition C as part of our licence simplification process. We do not consider this to have any impact on the quality and price of developers' services. Developers (and end-customers) are already protected by condition B of the the licence of new appointees (NAVs) which prevents them from from charging their customers more than the equivalent charges of the regional incumbent water company (i.e. the so-called "no-worse-off" principle). This will also mean that the transitional arrangements in licence condition C of the regional incumbent water companies will effectively apply to the NAVs through this no-worse-off principle.

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## 1. Licence modification

Water companies (also referred to as appointed companies or appointees) hold appointments as water and/or sewerage undertakers under the Water Industry Act 1991. Their Instruments of Appointment (IoAs) contain a number of conditions relating to their activities.

Under section 55 of the Water Act 2014 (WA14), the Water Services Regulation Authority (Ofwat) may modify the conditions of an appointment under Chapter 1 of Part 2 of the Water Industry Act of 1991 (WIA91) where we consider it necessary or expedient to do so in consequence of provision made by or under Part 1 of the WA14.

On 19 October 2017 we modified the conditions of appointment of the IoAs for the appointed companies whose areas are wholly or mainly in England. These were made under section 55 of the Water Act 2014 (WA14) and can be viewed individually.

In accordance with section 55, we [consulted](#) the holders of the IoAs that we proposed to modify, together with the Secretary of State, Welsh Ministers and wider stakeholders. Having fully considered the 26 responses we received to that consultation, in addition to responses to our earlier consultations on the proposed modifications, we modified the IoAs on 19 October 2017 for the reasons set out in this Notice. Details of the modifications are set out in section 3 below, and the company specific modifications are available individually:

- [Affinity Water Limited](#)
  - [Anglian Water Services Limited](#)
  - [Bristol Water Plc](#)
  - [Cholderton and District Water Company Limited](#)
  - [Northumbrian Water Limited](#)
  - [Portsmouth Water Limited](#)
  - [Severn Trent Water Limited](#)
  - [South East Water Limited](#)
  - [South Staffordshire Water Plc](#)
  - [South West Water Limited](#)
  - [Southern Water Services Limited](#)
  - [Sutton and East Surrey Water Plc](#)
  - [Thames Water Utilities Limited](#)
  - [United Utilities Water Limited](#)
  - [Wessex Water Services Limited](#)
  - [Yorkshire Water Services Limited](#)
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- [Albion Water Limited](#)
  - [Icosa Water Services Limited](#)

- Independent Water Networks Limited
- Leep Water Networks Limited
- Severn Trent Services (Water and Sewerage) Limited
- SSE Water Limited
- Veolia Water Projects Limited

## 2. Background

Water companies have a duty to allow new connections to be made to their existing networks, including for new housing development. We have powers, introduced by the WA14, allowing us to move from the current legislative charging framework for these new connections to a principle-based, more transparent and cost reflective charging framework.

Water companies whose areas are wholly or mainly in England (“English water companies”) must implement our charging rules in relation to charges for new connection services that have effect from 1 April 2018. We published our [proposed set of charging rules](#) in August 2017 (“the Rules”). For companies whose areas are wholly or mainly in Wales, we will consult and publish our rules, following the publication by the Welsh Government of final supplementary charging guidance to Ofwat on developer charges and other matters.

The Rules change the definition of infrastructure charges from a maximum value set out in Condition C (Infrastructure Charges) of the IoAs, to a charge based on the costs incurred by the appointee in providing offsite reinforcement works. This rule change deletes Condition C from the IoAs.

### 2.1 Consultation to date

We formally consulted on proposals to amend the IoAs in July 2016, alongside our [consultation on our proposed rules on new connections charging](#) under s55 of the Water Act 2014 (WA14). In this consultation, we proposed that licence condition C would cease to have effect from 1 April 2017. This date would coincide with the date from which our proposed new connections charging rules would have effect. 17 responses were received by the deadline of 26 August 2016 that had specific comments about the proposed changes to the licence condition.

As part of their responses to the consultation on the Rules, a wide range of stakeholders, including both appointees and major trade bodies representing developers raised concerns that it would not be practicable to implement the Rules on 1 April 2017.

As a result of comments received in response to the July consultation, we reviewed and updated our proposals and published a [further consultation](#) on 6 October 2016. The updated proposal delayed the implementation of the Rules until 1 April 2018. We therefore consulted on a modification of licence condition C which would change the date on which licence condition C ceased to have effect from 1 April 2017 to 1

April 2018. We received two responses to the October consultation, both of which were supportive of this proposed change.

We consulted on a revised wording of the proposed licence modification in June 2017 to align with the transitional arrangements in the commencement order published earlier in 2017 that implemented the sections of the Water Act 2014 necessary to implement the Rules. In this consultation, we also proposed to remove Condition C from NAVs rather than modifying them in the same way as other appointees. This is because licence condition B for the NAVs already prevents NAVs from setting charges that would be higher than those of the regional incumbent water company (known as the “no-worse-off” principle), making the transitional arrangements in licence condition C unnecessary. As a result we are able to simplify the licence of the NAVs without reducing customers protection.

Finally, on 18 August 2017 we wrote to three appointees that had not previously responded to the previous consultations to ensure that they were fully aware of the proposed licence changes.

### 3. The modifications

For most appointees, we have amended licence condition C to add the following condition:

“16 Cessation of this Condition

16.1 Subject to sub-paragraph 16.2, this Condition (including the Appendix) shall cease to have effect on 1 April 2018 and shall not limit the amount of any Infrastructure Charge in respect of each Charging Year starting on or after that date.

16.2 This Condition (including the Appendix) shall continue to have effect in relation to a connection made on or after 1 April 2018 in the following circumstances:

(a) in relation to a Water Infrastructure Charge, if the premises are connected to a water main that:

(i) was provided by a water undertaker under section 41 of the Water Industry Act 1991 and the charges for that water main were calculated on the basis of the provisions of the Water Industry Act 1991 before they were amended by the Water Act 2014; or

(ii) was, or will be, adopted by a water undertaker in accordance with an agreement to which new charging rules do not apply; and

(b) in relation to a Sewerage Infrastructure Charge, if the premises are being connected to a public sewer that:

(i) was provided by a sewerage undertaker under section 98 of the Water Industry Act 1991 and the charges for that public sewer were calculated on the basis of the provisions of the Water Industry Act 1991 before they were amended by the Water Act 2014; or

(ii) was, or will be, adopted by a sewerage undertaker in accordance with an agreement to which new charging rules do not apply.

16.3 In this paragraph “new charging rules” means rules about charges issued by the Water Services Regulation Authority under section 51CD or 105ZF of the Water Industry Act 1991.”

For NAVs, we removed Condition C from their licences entirely.

## 4. Why were the modifications made?

The changes were required in order to implement the new charging rules which will come into force on 1 April 2018 for English water companies. As part of these rules, the infrastructure charges will change from being a fixed sum for each new connection based on a maximum value set by Ofwat, to a charge based on the costs incurred by the appointee in providing offsite reinforcement works. The infrastructure charge will also cover some of the the offsite costs incurred as a consequence of a water main or sewer requisition, which were previously part of the requisition charges. Water companies will be required to determine infrastructure charges in accordance with the principle that such charges will, over a rolling five year period, cover their expenditure on network reinforcement driven by new development and growth (with any other amounts that the relevant undertaker receives for network reinforcement to be deducted accordingly). This will ensure that the infrastructure charges will be cost-reflective and increase the clarity and transparency of charges. This, together with the requirements that the current balance of charges between customers and developers is broadly maintained will ensure that developers will be protected. In order to make this change, the previous limit on the maximum size of infrastructure charges, as set out in Condition C of the IoAs had to be removed.

Licence condition C also contained a requirement for a water undertaker to inform the relevant sewerage undertaker of any new premises that are connected to the water supply network. As a consequence of this licence change, this provision would be revoked from 1 April 2018. We do not think this change is desirable and as highlighted as part of our consultations on the new connections rules, we propose to retain this requirement. We have received no comments that disagree with this approach. As a result, we will be consulting in late October or early November 2017, as part of wider licence simplification work, on a proposal to place this requirement somewhere else in the companies' licences.

## 5. Responses to the consultations

This section includes a summary of the consultation responses to all of the consultations we have undertaken on this proposed changes to licence condition C.

### 4.1 Larger Appointees

During the consultations about this proposal, the larger appointees (except Sutton and East Surrey) have responded at least once to agree, or at least confirm that they do not object, to the proposed modification. Some minor comments have been received, however we have not proposed any alterations to the proposed change based on these comments. Northumbrian Water and South Staffordshire Water asked for clarifications on the meaning of parts of the proposed licence condition change.

Affinity Water questioned whether we could use section 55 of the WA14 to make these licence condition changes. It believed that our ability to use these powers expired on 31 December 2016.

Section 55(1) of the WA14 gives Ofwat a power to modify the conditions of appointment of appointees where it considers it necessary or expedient to do so “in consequence of provision made by or under [Part 1 of the WA14]”. Section 55(5) says that the power “may not be exercised after the end of the period of two years beginning with the day on which the provision in question comes into force”. The “provision in question” is the provision in consequence of which a modification is necessary or expedient (which in this case includes sections 16(2) and 17 of the WA14) and not section 55 itself. Section 16(2) of the WA14, for example, which gave Ofwat the power to make rules about appointees’ statutory charges schemes (which include infrastructure charges), came fully into force on 1 November 2015 and consequential changes can therefore be made by Ofwat until 31 October 2017.

### 4.2 Welsh Appointees

The proposed changes do not directly affect companies that operate wholly or mainly in Wales. As a result, Dee Valley did not comment on the consultation and Welsh Water only commented on the July 2016 consultation to say that they were awaiting the process for developing new connections rules that will apply to the companies wholly or mainly in Wales.

### **4.3 Small and/or new appointees**

We received response to the July 2016 consultation from 5 NAVs (Icosa Water, Scottish and Southern Energy, Albion Water, Veolia Water Projects and IWN). Only Veolia Water Projects provided specific comments on the proposed licence change to raise concerns that it could result in the company incurring additional costs to model their rolling 5-year investments in infrastructure reinforcement and may receive a lower income when it is required to set infrastructure charges that do not exceed those set by Wessex Water.

### **4.4 Other responses**

CCWater has not commented on the proposed licence condition change other than to confirm that it did not have concerns over our decision to delay the implementation until 1 April 2018.

Under s55 of the WA14, we are required among other things to consult the Welsh Ministers and the Secretary of State. However, as the licence condition changes only affects companies that are wholly or mainly England, only the Secretary of State may direct us either not to make the proposed modifications or to amend them as directed. As part of the July consultation, we wrote to Welsh Ministers and the Secretary of State. Defra does not have any objections to the proposed change to licence condition C.

We did not receive a formal response from the Welsh Government to any of these consultations.