

August 2018

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 Barty Farm, Bearstead, Kent**

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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 Southern Water Services Limited (“**SRN**”) as a sewerage company. This notice is a consultation on this proposal under section 8(3) of the Water Industry Act 1991 (“**WIA91**”).

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 this consultation notice, Ofwat will decide whether or not to grant the variation of appointment set out above.

## 2. The Site

IWS has applied for a variation to its appointment to be able to provide sewerage services to a site called Barty Farm (“**the Site**”). The Site boundary map can be viewed in section 8 of this document.

The Site is within the sewerage services area of SRN. If granted, IWS will provide sewerage services to 100 household customers, there are no business customers on the Site. IWS proposes to provide sewerage services to the Site by way of bulk discharge agreement with SRN.

Planning permission has been sought for the Site and is expected to be granted in 2018. The Site is expected to be fully built out by 2021.

### **3. The applicant**

On 20 October 2016, Icosa Water Limited was appointed as a water and sewerage undertaker for a site called West Raynham in Norfolk. On 20 December 2016, IWS (the applicant), who is a subsidiary of Icosa Water Limited, applied to take over the appointment for the West Raynham site under the consent criterion. Since then Ofwat has agreed to vary IWS' areas of appointment so that it serves a further seven sites for water and/or sewerage services. The register of new appointments and variations can be viewed [here](#).

## **4. The proposal**

Ofwat proposes to:

- grant a variation of appointment to IWS as a sewerage company; and
- vary the appointment of SRN 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 legislation<sup>1</sup>, 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 – ie customers of the existing provider and customers more generally across England and Wales, who in our view benefit from the effective operation of the new appointment and variation mechanism.

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<sup>1</sup> The legal framework for new appointments is set out in the WIA91. Section 7 of the WIA91 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 WIA91.

### **6.1 Unserved status of the Site**

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 has provided an independent report which confirms the Site is unserved. The Site is greenfield and has no assets or properties within its boundary. On 11 July 2018 SRN confirmed to us that it agrees with the findings of the independent report. Having reviewed the facts of this Site, and taking into account the independent report we consider the Site to be unserved.

### **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 (“Business Customers”) in England and Wales are able to choose their supplier<sup>2</sup>.

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.

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<sup>2</sup> The majority of Business Customers where the area of the relevant appointed company is not wholly or mainly in Wales (and whose premises are, or are likely to be, supplied with at least 50 MI where the relevant area is wholly or mainly in Wales) can effectively switch suppliers of water and/or sewerage from 1 April 2017.



### **6.3 Price**

IWS proposes to charge customers on the Site charges equivalent to those of SRN, it does not propose to offer a discount.

### **6.4 Levels of service**

Every appointee is required under its conditions of appointment to publish a Code of Practice on debt 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 SRN were to be the customers' water and sewerage services supplier.

### **6.5 Developer choice**

IWS has the consent of the developer (Dandara Limited) to be the sewerage services 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. The DWI informed us that it is content for us to consult on this application. The EA advised it is content for us to consult, noting that it has requested assurances prior to it providing approval for this Site. It has sought assurances that SRN is happy to receive sewerage from the Site and that it has capacity in its sewerage network and at the subsequent sewerage treatment works. IWS has advised that it will communicate the requested information when this becomes available. This application will not be granted until the EA has received the requested information and has confirmed that it is satisfied.

## 6.7 Incumbent's existing customers

In considering whether customers will be no worse off, we also considered the potential effects of this or variation on the prices that 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 to quantify the possible effect in an easily understandable way.

We have assessed the potential magnitude of this impact by comparing how much SRN might have expected to receive in revenue from serving the Site directly, were they to serve the Site, with the revenues they might expect from the proposed arrangement with IWS.

We estimate that there will be a £0.001 increase in the annual sewerage bills of existing SRN customers if we grant this variation to IWS. This is once the Site is fully built out.

This estimate does 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 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 or sewerage company.

IWS is currently applying to be appointed to serve a number of sites. This application is being considered as a package with four other sites: Common Road, Benhall Mill Road, Rochester Riverside and West End Lane (together referred to as "**the Five Sites**"). Four of the five Sites are small, smaller sites generally generate much lower profit margins than larger sites so demonstrating financial viability of an individual site can be more difficult. We have therefore approached the financial viability assessment on a portfolio basis. This allows some higher risk sites to be balanced

by some lower risk sites. This allows the applicant the opportunity to demonstrate the financial viability of the Five Sites as a package.

In this case, we considered the estimated revenues and costs of the entire Site relating to sewerage services should the relevant variation be granted and we assessed the financial viability of the applications in respect of the Five Sites on a portfolio basis. We think the likelihood of this Site not being financially viable is small if it is being considered as a package.

## 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 would be able to finance, and carry out, its functions. We have also considered the effects of granting the proposed variation on the existing customers of SRN.

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

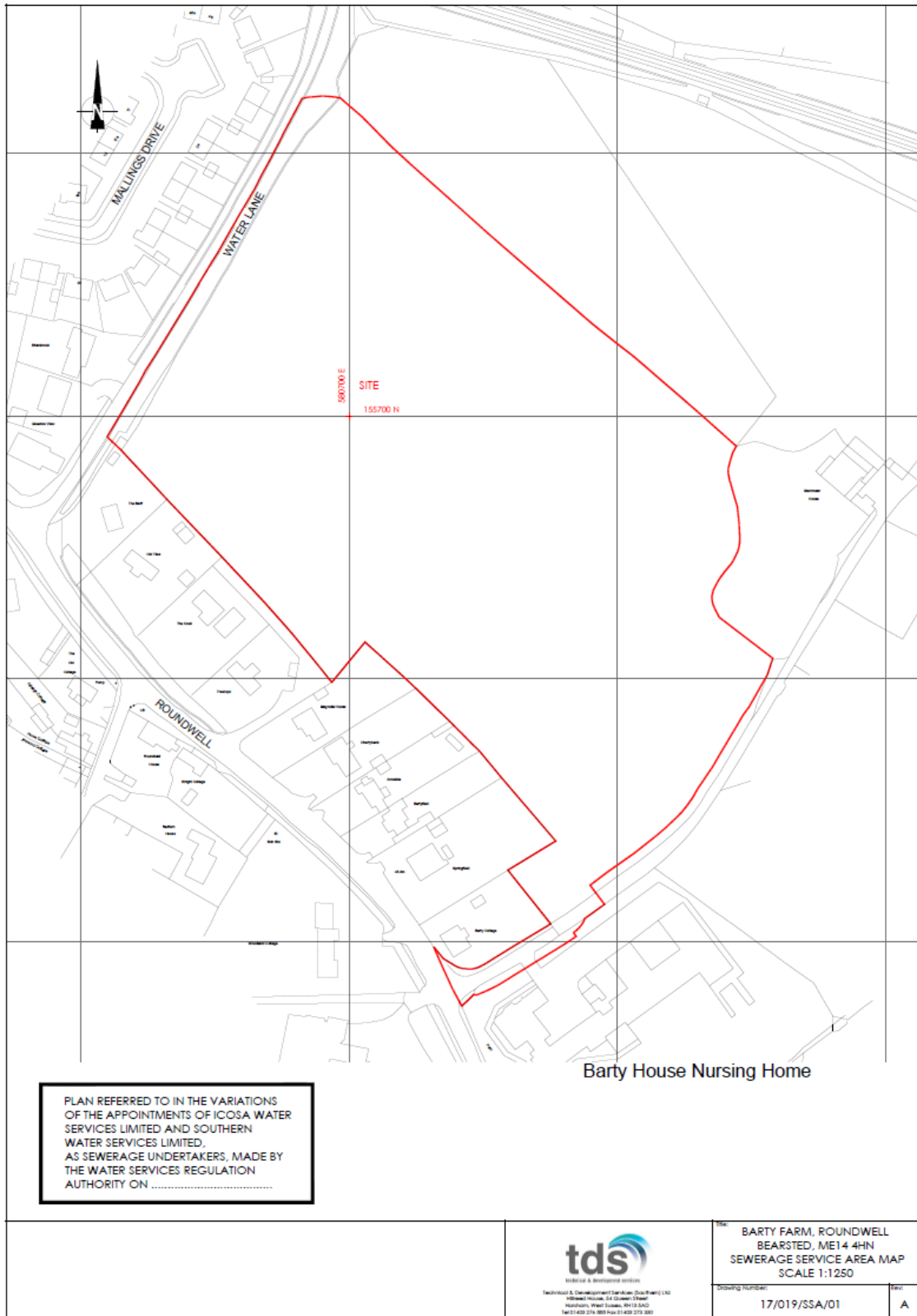
### Where to send submissions

Any person who wishes to make representations or objections with respect to the application should do so in writing to Hayley Robinson at Centre City Tower, 7 Hill Street, Birmingham, B5 4UA or by completing the web form.

Representations must be received by Ofwat no later than 17.00 hours on 5 September 2018. 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 map



Ofwat (The Water Services Regulation Authority) is a non-ministerial government department. We regulate the water sector in England and Wales. Our vision is to be a trusted and respected regulator, working at the leading edge, challenging ourselves and others to build trust and confidence in water.

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