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Dear Ofwat,

**Consultation on charging rules for new connections and new developments for English companies from April 2020**

Thank you for the opportunity to respond to this consultation, please see our response to your questions below. The consultation overall did not provide us with sufficient clarity on what the proposed charging rules mean in practice, which left us uncertain as to whether the approach we have taken after careful consultation with developers, NAVs, SLPs and wider customer representatives such as CCWater is in line, or not, with this guidance. We wanted to include worked examples to illustrate the point, but unfortunately we unable to do so within the timescale for the consultation. If it is helpful, we would be willing to explore this further. We note the timing of this consultation and agreement of the rules is important, so that these can be applied to the developer services income forecasts at PR19.

Please let us know if we can be of further assistance.

Yours faithfully,

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**Q1. Do you have any comments on the proposed wording for the New Connection Rules and Charges Scheme Rules (see Appendix 1 tables, and the rules for consultation), which will come into effect from April 2020.**

Our view is that there is some ambiguity in the guidance, as it appears to require that the balance between contributions to costs and other customers is retained, but also that infrastructure charges reflect the costs of off-site network reinforcement over a five year period. In our view it is not possible for both of those principles to always be simulatenously applied, as this could stifle changes in costs and markets.

Specifically in rule 19, this assumes appears to assume that the costs remain the same. However, the costs, in particular what is included in infrastructure charges (prior to considering income offset) related to network reinforcement vary, and this is a principle within the guidance. We think the correct interpretation is that the balance of charges remains the same, and other customers do not gain or disbenefit from changes in the developer services market. The balance between current and future customers, should include that income offset (alongside other charges) should remain broadly the same, the principle that developers should benefit from the contribution through income received from the new mains specifically needed for a new development (“on-site” as a customer / developer typically used term, broadly equivalent to “contestable” activities). This is important, particularly the benefits for NAVs and SLPs in terms of lowering the total cost of supply through their activity. Costs can vary (including through volume and through competitive activity). Income will also therefore vary (income offset with volumes, broadly), and also with a timing difference between cost and income (implied by the basis of infrastructure charges).

From our perspective, the description on page 12 of the consultation “that the income offset has to check the balance across all costs associated with developments” is slightly different to what the “balance of costs” is, because the contribution to costs will vary where network reinforcement costs change.

The proposed wording in the New Connection Rules could be interpreted as requiring the level of income offset to be included at a way that maintains its level, or as requiring developer services income as a whole to remain the same. The focus in the consultation on contestable work may not consider that income offset and infrastructure charges relate to off-site network reinforcement and the requisitioning of mains to connect to this. The overall principle should be that if the costs of new development as a whole are lower, developer contributions are also lower. We consider that the principle should be that that gross infrastructure charges should relate to network reinforcement costs and this variation is part of maintaining the principle that the balance of charges between different customer groups reflects costs (which is why the change was introduced). We think that a worked example, based on where costs and volumes vary are required, to illustrate that it is not the absolute level of developer services income that stays the same, but the relative balance of developer costs between current and future customers that is being maintained, which we think is the principle that was the intention behind Defra’s charging guidance. The reference to “costs” is the balance of costs associated with new development and other network enhancements. This would imply that developers should continue to benefit broadly from the same principle that income offset reflected the on-going contribution of customers to the offsite network capacity which would also benefit future developments, which would be within the general bill contributions those customers would pay.

There are clearly two possible interpretations, and we were not clear from the consultation which was correct, or if it is that developer charges as a whole should stay the same (ie the

basis of income offset changes even where off-site network reinforcement falls and infrastructure charges fall in the short or medium term, but with income offset falling to offset this). Even if the latter interpretation was the intention in the consultation, we were not sure this was correct in terms of the guidance.

**Q2 Do you have any comments on our proposal to introduce an information requirement on bill stability? More specifically:**

- **Do you find the proposed requirement helpful in supporting the charging principle of bill stability?**
- **Is the suggested 10% threshold for significant bill increases appropriate for striking the right balance between more scrutiny on bill increases and flexibility for companies to make changes as necessary?**

**In order to assist companies in implementing this requirement effectively, we welcome views on:**

- **what criteria would be most appropriate to define typical new developments; and**
- **what services should be included in a typical package**

We have no objection to the introduction of the rule to require companies to provide a statement on the impact of significant bill increases of greater than 10%, and agree that this provides consistency with the Charges Scheme Rules and Wholesale Charges Rules whilst also recognising the need for flexibility in allowing the higher threshold.

However, this very much will depend on Q1 – we cannot conclude whether 10% will be sufficient, or what happens if interpretation 2 (developer services income irrespective of reinforcement or volume cost changes should stay the same) means there are more dramatic changes.

We agree that the impact assessment is best made against illustrative types of new connection and developer packages of services.

In practice, we have used a wide range of examples of charge changes in order to demonstrate that the overall cost of a development is not being affected by the move to the charging arrangements consultation. This excludes infrastructure charges (but includes income offset), as the infrastructure charge may move differently to this. We think companies will need some flexibility in how they are consulting on and defining the charges for this 10% test, and this may depend on the conclusion as to what is intended from Q1.

We think that gross infrastructure charges should be considered separately from the on site development worked examples. This is important for transparency, where the income offset value relates to assumptions on cost recovery for on-site mains, which will need to be monitored for the overall balance of charges. However this would not apply for interpretation 2, where effectively developer service charges should not be changing by more than 10% in any case, except perhaps for gross infrastructure charges (hence the lack of clarity we identify in Q1).