

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

## South East Water response

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# 1. Introduction

Thank you for consulting on the proposed changes to the charging rules for new connection services (English undertakers) and the charges scheme rules.

We support the proposal to apply the income offset to the infrastructure charges to ensure that offsetting is available irrespective of whether undertakers, self-lay providers or new appointees are asked to provide the infrastructure by developers. We also welcome the clarifications to the requirement to maintain the balance of charges between developers and customers.

However, it is essential that the proposal on offsetting also receives the broad support of both SLPs and NAVs.

## Observation on the context of the proposed changes

We recognise the merit of the proposed changes but we are conscious that new connection charging should be considered in the context of the wider issues created by changes to the legislative and regulatory framework for market opening.

There is a discrepancy between the role undertakers are expected to play by market participants and the legislative and regulatory framework resulting from the changes to their duties to provide connections in exit areas. There is continuing uncertainty about the structure of the new connection market for non-household premises, the relevant provisions of the wholesale retail code and the respective roles of water supply licensees and undertakers in relation to the provision of new connection services. In certain cases the powers of undertakers to carry out works to provide new connections may be affected due to these legislative changes.

Considering that the scope of the new connection charging rules is defined by reference to the duties of undertakers, on the interpretation of the current legislative framework which we believe to be the most likely to be correct as it is consistent with the approach adopted in the wholesale retail code, a large proportion of the new connection services provided directly by undertakers to developers are no longer covered by the duties referred to in the new connection charging rules. The related connection and requisition charges are therefore out of the scope of the new connection charging rules. This is especially problematic regarding the requirement to maintain the balance of charges between developers and customers.

We believe that work to resolve these issues should be a priority with the aim of resolving them by April 2020 as the current situation is unsatisfactory. It creates regulatory uncertainty which hinders the efforts made by Ofwat and companies to achieve the best compliance outcomes.

There is also a risk that delays in resolving these issues will lead to the dissatisfaction of market participants that will have a negative impact on their perception of the services provided by

undertakers, even where the root causes of the issues are beyond the control of undertakers. This is particularly important as Ofwat is introducing the new D-MeX measure.

## 2. Responses to the consultation questions

### QUESTION 1:

**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.**

We do not have comments on the proposed wording of the revised new connection rules and charges scheme rules.

However, these changes will only achieve their goal with the required certainty if the issues mentioned in our introduction are resolved.

We refer to our response to the consultation on changes to the charges scheme rules, wholesale charging rules and the charging rules for new connection services in November 2018. Our main comment was that the new definition of network reinforcement includes a criterion that the reinforcement works must relate to infrastructure provided pursuant to a duty or an agreement with “a person other than a relevant undertaker”. This excludes reinforcement relating to NAV sites.

We believe that this defect in the definition of network reinforcement should be remedied as part in the proposed revision of the new connection rules. Please refer to our consultation response dated 20 November 2018 for further details.

**QUESTION 2:**

**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 agree with the proposal to have similar information requirements across all charging rules.

Typical developments considering all new connection charges seems to be the appropriate approach. Categorising sites by reference to size (e.g. length of main and number of service connections) between individual household connections and small, medium and larger developments would seem to be a suitable approach.

In respect of packages of services, to the extent that certain types of services may be associated with certain categories or sizes of sites, there may be potential to refine the analysis. For example developers may predominantly carry out excavations whilst individual customers would not. However, this should be assessed based on the mix of services for certain types of sites in each company's area and on whether differences in the mix of services lead to measurable differences of impact.

It may be beneficial to share feedback from companies on the criteria for typical sites and on possible handling strategies to help define a consistent approach and identify best practice. This could be done as a workshop or other approach that Ofwat may choose.

A higher threshold than 5 % is required, and 10% may be more suitable. It would be useful however to keep this under review as companies are developing their assessments and models and more data becomes available.

**QUESTION 3:**

**As part of this consultation, we are asking for comments on implementation issues that we may not have identified.**

The consultation document has identified the main implementation issues including transitional provisions to avoid double discounting.

We refer to our comment in the introduction of this response on the need for a coherent and consistent regulatory framework especially in relation to non-household premises in an exit area.

For the implementation of the changes, NAVs will need to update the definition of their infrastructure charges in their own charges schemes to ensure that they reflect the new structure and amount of the infrastructure charges of the incumbent providing a bulk supply.

We expect that the balance of charges between developers and customers will be affected to some extent by the proposal to apply the income offset to infrastructure charges but the consultation document does not address these types of practical considerations.

There may be cases where the total amount of the income offset would be greater than the total amount of the infrastructure charges due in respect of a site. This would bring the amount of infrastructure charge to zero. The benefit of some of the offset would be lost and the proportion of costs paid by developers would increase. The balance of charges between developers and customers would therefore be affected.

The balance of charges between developers and customers before 1 April 2018 is in part the result of how the income offset was calculated before that date. The revenue assumption was based on the average end-user metered bills. Where a bulk supply is provided to a NAV the bulk supply charges are based on the wholesale charges (adjusted in accordance with Ofwat May 2018 guidance), not end-user charges. When the income offset is applied to the infrastructure charges collected by NAVs, companies that apply an income offset may no longer be able to use revenue assumptions based on end-user average metered bills in order to maintain the equivalence across requisition, self-lay and NAVs. This will have an impact on the balance of charges between developers and customers before and after 1 April 2018. We recognise that companies are free to determine how they calculate their income offset, but considering that the proposed changes can be expected to have a mechanical impact on the balance of charges and the comparability of the different procurement channels for new connections, it would be useful to understand how Ofwat has considered these issues. It would be useful for this to be addressed in the relevant decision document and if necessary recognised in the charging rules.

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