

15 August 2019

Trust in water

## **Variation of Icosa Water Services Limited's appointment to include Forstal Lane, Coxheath**

## 1. About this document

### Variation of Icosa Water Services Limited's appointment to include Forstal Lane, Coxheath

On 24 June 2019, Ofwat began a [consultation](#) on a proposal to vary Icosa Water Services Limited's ("**Icosa Water**") appointment to become the water and sewerage services provider for a development in South East Water's ("**SEW**") water supply area and Southern Water's ("**SRN**") sewerage services area called Ulcombe Road in Headcorn ("**the Site**").

The consultation ended on 23 July 2019. During the consultation period, we received representations from two organisations, which we considered in making our decision. On 14 August 2019, we granted Icosa Water a variation to its existing appointment to enable it to supply water and sewerage services to the Site.

This notice gives our reasons for making this variation.

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## 2. Introduction

The new appointment and variation (“**NAV**”) mechanism, specified by Parliament and set out in primary legislation, allows one company to replace the current company 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 companies to expand into areas where they are not the appointed company. In this case, Icosa Water applied to replace SEW and SRN to become the appointed water and sewerage company for the Site.

A company may apply for a new appointment (or a variation of its existing appointment to serve an additional site) if any of the following three criteria are met:

- None of the premises in the proposed area of appointment is served by the existing appointed company at the time the appointment is made (the “**unserved criterion**”);
- Each premises is likely to be supplied with at least 50 mega litres per year (in England) or at least 250 mega litres per year (in Wales) and the customer in relation to each premises consents (“**the large user criterion**”);
- The existing water and sewerage supplier in the area consents to the appointment (“**the consent criterion**”).

When considering applications for new appointments and variations, Ofwat operates within the statutory framework set out by Parliament, including our duty to protect consumers, wherever appropriate by promoting effective competition. In particular, in relation to unserved sites, we seek to ensure that the future customers on the 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:

1. Customers, or future customers, should be no worse off than if they had been supplied by the existing appointee; and
2. We 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.

Entry and expansion (and even the threat of such by potential competitors) can lead to benefits for different customers (such as household and business customers and developers of new housing sites). Benefits can include price discounts, better

services, environmental improvements and innovation in the way services are delivered.

Benefits can also accrue to customers who remain with the existing appointee, because when the existing appointee faces a challenge to its business, that challenge can act as a spur for it to improve its services. We believe the wider benefits of competition through the new appointments and variations mechanism can offset any potential disbenefits for existing customers that might arise. We consider these potential disbenefits in more detail below.

### **3. The application**

Icosa Water applied to be the water and sewerage services appointee for the Site under the unserved criterion set out in section 7(4)(b) of the Water Industry Act 1991 (“**WIA91**”). Icosa Water will serve the Site by way of bulk supply and bulk discharge agreements.

#### **3.1 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.

Icosa Water has provided an independent report which confirms the Site is unserved.

Given the information provided to us by Icosa Water, SRN and SEW, we consider the Site to be unserved.

#### **3.2 Financial viability of the proposal**

We have a statutory duty to ensure that 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 revenues and costs of the Site relating to the provision of water and sewerage services should this variation application be granted. Icosa Water has submitted the Site as a package alongside another application, namely Ulcombe Road.

We are satisfied that as part of a package the combined, cumulative financial position of the Site demonstrates sufficient financial viability under our standard assessment. The Ulcombe Road site considered alongside this application was granted on 6 August 2019.

#### **3.3 Assessment of ‘no worse off’**

Icosa Water proposes to match the charges to customers on the Site of SEW and SRN, that is, it will not offer a discount.

With regard to service levels, we have reviewed Icosa Water's Codes of Practice and its proposed service levels and compared these to the Codes of Practice and the performance commitments of SEW and SRN. Based on this review, we are satisfied that customers will be offered an appropriate level of service by Icosa Water and that overall customers will be 'no worse off' being served by Icosa Water instead of by SEW and SRN.

### **3.4 Effect of appointment on SEW and SRN's customers**

In considering whether customers will be no worse off, we also looked at the potential effects of this variation on the charges that SEW's and SRN's existing customer bases may face.

The calculation necessarily depends on a range of assumptions, and there are clearly difficulties involved in quantifying the effect on customers of SEW and SRN. It is therefore necessary to use a 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. Broadly, we have assessed the potential magnitude of this impact by comparing how much SEW and 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 Icosa Water.

In this case, we have calculated that if we grant the Site to Icosa Water, there may be a potential impact on the bills of SEW's existing customers of £0.004, and £0.001 for SRN's existing customers.

This impact does not take into account the potential spillover benefits to customers arising from dynamic efficiencies achieved as a result of the competitive process to win new sites.

We therefore consider that granting this new variation to Icosa Water would have a negligible impact (if any) on customers' bills and could have potential benefits for customers.

### **3.5 Developer choice**

Where relevant, we take into consideration the choices of the site developer. In this case, the developer (Chartway Group Limited) said that it wanted Icosa Water to be the water and sewerage company for the Site.

## 4. Responses received to the consultation

We received two responses to our consultation, from Consumer Council for Water (“**CCWater**”) and the Environment Agency (“**EA**”). We considered these responses before making the decision to vary Icosa Water's appointment. The responses to the consultation did not raise any issues that have made us reconsider our recommendation that this variation be granted. The points raised in the responses are set out below.

### 4.1 CCWater

In its response, CCWater stated it was disappointed that there are no direct financial benefits to customers from being served by Icosa Water rather than SEW for water services or SRN for sewerage services, as Icosa Water proposes to match the charges of SEW and SRN. It noted that Icosa Water, unlike SEW and SRN, does not offer a social tariff. Until it can provide a social tariff, CCWater stated that it would expect Icosa Water to offer appropriate, flexible support to any individual customers in financial difficulty that would otherwise benefit from a social tariff. However, it noted that Icosa Water proposes to match or exceed many of the service standards currently provided by SEW and SRN, notably more generous compensation in the event of service failures or following sewer flooding. For this reason, CCWater supports our proposal and agrees with our assessment that customers will be no worse off.

We have noted CCWater's concern that there is no direct financial benefit to customers. One of our key policies is that customers should be 'no worse off' if a NAV is granted. That is, an applicant must ensure its new customers are made no worse off in terms of price and service than if they had been supplied by the previous incumbent. This requirement has been met by Icosa Water in its proposal to improve the levels of service and match the charges of SEW and SRN. We do not require applicants to better the service and price of the previous incumbent(s).

### 4.2 Environment Agency

The EA raised no objections to the application. It noted that development on the Site should not commence until connection to both SRN's sewerage and SEW's water supply networks is agreed. It also stipulated that properties should not be occupied until both SRN's sewerage and SEW's water supply networks are operational, and until any necessary SRN downstream improvements implemented. Finally, the EA noted that additional flows from the Site must not lead to deterioration in the performance of SRN's downstream sewerage assets.



## **5. Conclusion**

Having assessed Icosa Water's application, and having taken account of the responses we received to our consultation, we decided to grant a variation to Icosa Water's area of appointment to allow it to serve the Site for water and sewerage services. This appointment became effective on 15 August 2019.





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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