

11 November 2019

Trust in water

Variation of Independent Water Network Limited's appointment to include North Whiteley, Southampton

1. About this document

Variation of Independent Water Network Limited's appointment to include North Whiteley, Southampton

On 7 October 2019, Ofwat began a [consultation on a proposal](#) to vary Independent Water Networks Limited's ("**IWN**") appointment to become the water provider for a development in Southern Water Services Limited's ("**Southern Water**") water supply area called North Whiteley in Southampton ("**the Site**").

The consultation ended on 4 November 2019. During the consultation period, we received representations from two organisations, which we considered in making our decision. On 7 November 2019, we granted IWN a variation to its existing appointment to enable it to supply water to the Site.

This notice gives our reasons for making this variation.

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2. Introduction

The new appointment and variation 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, IWN applied to replace Southern Water to become the appointed water 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

IWN applied to be the water appointee for the Site under the unserved criterion set out in section 7(4)(b) of the Water Industry Act 1991 (“**WIA91**”). IWN will serve the Site by way of a bulk supply agreement with Southern Water.

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.

IWN has provided us with a letter from Southern Water dated 23 July 2019, which confirms the Site is unserved.

Based on the information contained in the letter, we are content that the Site is unserved.

3.2 Financial viability of the proposal

We will only make an appointment if we are satisfied that the proposal poses a low risk of being financially non-viable. We assess the risk of financial viability on a site-by-site basis and also consider the financial position of the company as a whole.

Based on the information available to us, we concluded the Site demonstrates sufficient financial viability, and IWN has satisfied us that it can finance its functions and that it is able to properly carry them out.

3.3 Assessment of ‘no worse off’

IWN proposes to match the charges to customers on the Site, that is, it will not offer a discount.

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

3.4 Effect of appointment on Southern Water's customers

In considering whether customers will be no worse off, we also looked at the potential effects of this variation on the price that Southern Water'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 on customers of Southern Water. 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 Southern Water 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 IWN.

In this case, we have calculated that if we grant the Site to IWN, there may be a potential impact on the bills of Southern Water's existing customers of £0.021. 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.

3.5 Developer choice

Where relevant, we take into consideration the choices of the site developer. In this case, Bovis Homes Limited said that it wanted IWN to be the water 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 IWN's appointment. The points raised in the response are set out below.

4.1 CCWater

CCWater stated that it expects new appointees to provide customers with prices, levels of service and service guarantees that match, or ideally, better those of the existing service provider. It stated that it is disappointed that there is no direct financial benefit to customers from having IWN as their water provider, rather than Southern Water.

CCWater also stated that the principle which Ofwat applies when considering applications for NAVs is that customers, including existing customers of incumbent water and sewerage companies, should be no worse off as a result of the appointment – and it adds that, ideally, the incumbent's existing customers should receive some benefit from the new arrangements.

Further, CCWater stated it appreciates the cost to existing customers is likely to be around £0.021 per annual bill for Southern Water customers once the Site is fully built, and that this is a negligible effect, but that it is unclear whether there will be any significant benefits arising from this arrangement for the incumbents' customers.

We note CCWater's concerns regarding the impact on existing 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.. We do not require applicants to better the service and price of previous incumbents.

4.2 EA

The EA stated IWN had not responded to its pre consultation concerns. These included IWN having proposed per capita consumption (“PCC”) of 132 litres per

head per day (l/h/d) but without having given any detail as to how this will reduce over time. This is given that the development is in Southern Water's area where, comparatively, PCC will have reduced to 120 l/h/d by 2024-25.

We asked IWN to respond to this concern. IWN stated that it was mirroring the PCC with the incumbent region to ensure it can satisfy the no worse off principle; it was unsure why it had stated a PCC of 132, instead of 125. IWN clarified that it should have included the PCC to be aligned with IWN's 2019 Water Resource Management Plan ("WRMP") which is set at 125 by 2030. This is also based on all properties in the Site being built to modern plumbing standards, with every property being metered. IWN stated for the WRMP it has not predicted a lower PCC than 125 because this is lower than the required industry target for PCC of 130 by 2030.

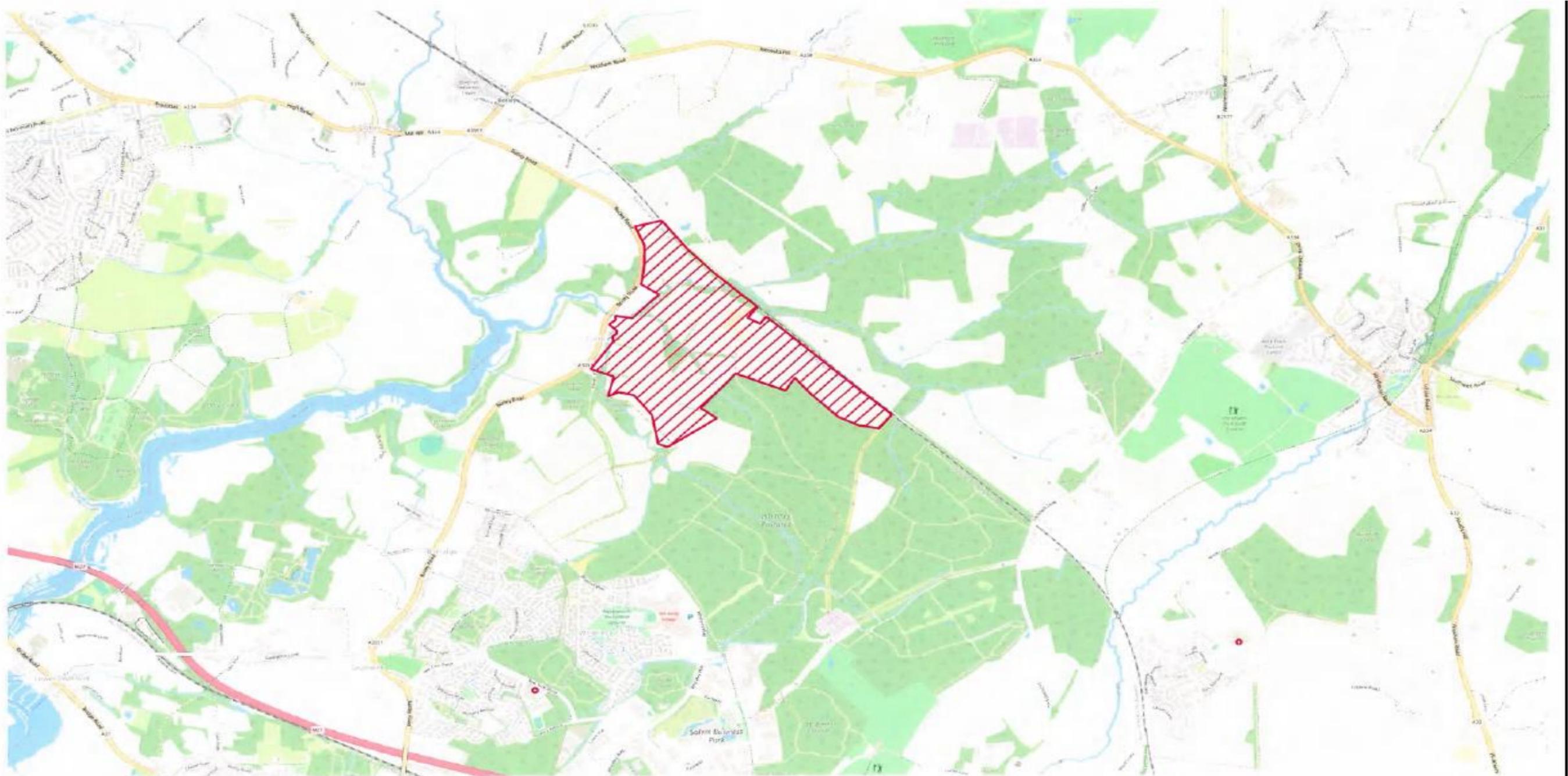
Further, IWN stated it expects to see some areas with a lower PCC than 120 in the future but are currently planning on a PCC of 125, as per the WRMP. It states that it will constantly review this as part of its annual reviews which will affect its future WRMPs. It noted that this Site was not included in the WRMP but will be included in the annual reviews once it is built out.

On 6 November 2019, the EA confirmed that they are comfortable with IWN's response.

5. Conclusion

Having assessed IWN's application, and having taken into account the responses we received to our consultation, we decided to grant a variation to IWN's area of appointment to allow it to serve the Site for water. This appointment became effective on 08 November 2019.

Appendix 1: Site Map



PLAN REFERRED TO IN THE VARIATIONS
OF THE APPOINTMENTS OF INDEPENDENT
WATER NETWORKS LIMITED AND
SOUTHERN WATER SERVICES LTD, AS
WATER UNDERTAKERS, MADE BY THE
WATER SERVICES REGULATION
AUTHORITY ON.....

CS
Jally

ADDRESS: NORTH WHITELEY, SOUTHAMPTON,
SO30 2HB
OS GRID REFERENCE: 453187, 111196

SCALE: 1:30000
DRAWN BY: CS
DATE: 29/08/2019

0 750 1500 m



NORTH WHITELEY INSET WATER SUPPLY MAP 2

PROJECT: N0020175 (73318)



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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