

13 February 2020

# **Variation of Icosa Water Services Limited's appointment to include Chapel Gate, Launceston**

## 1. About this document

### Variation of Icosa Water Services Limited's appointment to include Chapel Gate, Launceston

On 30 October 2019, Ofwat began a [consultation on a proposal](#) to vary Icosa Water Services Limited ("**Icosa Water**")'s appointment to become the sewerage services provider for a development in South West Water ("**South West**")'s sewerage services area called Chapel Gate in Launceston ("**the Site**").

The consultation ended on 27 November 2019. During the consultation period, we received representations from three organisations, which we considered in making our decision. On 13 February 2020, we granted Icosa Water a variation to its existing appointment to enable it to supply 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 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 South West to become the appointed 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 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 a bulk discharge agreement with South West.

#### **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 applied for a variation based on the unserved criterion, and the Site is greenfield. Icosa Water provided a letter from South West, dated 1 August 2019, confirming that, in South West's view, the Site is unserved for wastewater. Icosa Water confirmed that there are no existing customers on the Site, and all of the 140 households will be new build properties. Icosa Water also clarified that the property visible within the boundary map for the Site is unserved. On 6 November 2019 Icosa Water provided us with additional confirmation from South West that it considers the Site to be unserved for sewerage services.

Given the information provided by the applicant and South West, we consider 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 Icosa Water 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’**

Icosa Water proposes to match the charges of customers on the Site of South West, 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 South West. 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 South West.

### **3.4 Effect of appointment on South West 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 South West'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 South West. 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 South West might have expected to receive in revenue from serving the Site directly, were it to serve the Site, with the revenues it 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 increase in the bills of South West's existing customers of £0.008.

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, the developer, Barratt David Wilson Homes, said that it wanted Icosa Water to be the sewerage company for the Site.

## 4. Responses received to the consultation

We received three responses to our consultation, from the Consumer Council for Water (“**CCWater**”), South West and the Environment Agency (“**EA**”). We considered these responses before making the decision to vary Icosa Water's appointment. The points raised in the response are set out below.

### 4.1 CCWater

Overall, CCWater agrees with our assessment that customers will be no worse off if served by Icosa Water rather than South West.

CCWater recognised that Icosa Water was proposing to exceed most of the service standards offered by South West but expressed disappointment that, by setting charges at the same level as South West, Icosa Water was not offering any direct financial benefit to customers.

CCWater accepted that, given its relative size, it may be appropriate for Icosa Water to tailor some of the services that it provides. CCWater set out its expectation that Icosa Water would offer appropriate, flexible support to any customer in financial difficulty who would otherwise have benefitted from a social tariff. CCWater noted that this should not be at the expense of its other customers and expects Icosa Water to research the views of its customers on cross-subsidy before introducing any social tariffs.

CCWater noted that our calculations suggested that granting the variation would lead to a £0.008 increase in the annual sewerage bills for South West's customers and noted that it had not identified any significant benefits to South West's existing customers from the proposals.

One of our key policies is that customers should be no worse off if an application is granted. An applicant must therefore ensure that its new customers are made no worse off in terms of price and service quality than if they had been served by the incumbent. We consider that this requirement has been met by Icosa Water through its proposal to exceed many of the levels of service and match the pricing set by South West. We do not require applicants to offer a better service and price than the incumbent.



## **4.2 South West Water**

South West noted that it supports the development of markets where customers could benefit, or in the least suffer no detriment, and agreed that Ofwat's estimate of a potential increase of £0.008 on the sewerage bills of existing South West customers is negligible. It also noted that Icosa Water had liaised with South West regarding the query raised in section 6.1 of the consultation, in relation to the unserved status of the Site, and South West has provided further information confirming its view that the site is unserved.

South West confirmed that it agrees to the proposal to grant this variation.

## **4.3 EA**

The EA confirmed that it has no objection to Ofwat granting this variation.

## **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 sewerage services. This appointment became effective on 14 February 2020.



Ofwat (The Water Services Regulation Authority)  
is a non-ministerial government department.  
We regulate the water sector in England and Wales.

Ofwat  
Centre City Tower  
7 Hill Street  
Birmingham B5 4UA

Phone: 0121 644 7500  
Fax: 0121 644 7533  
Website: [www.ofwat.gov.uk](http://www.ofwat.gov.uk)  
Email: [mailbox@ofwat.gov.uk](mailto:mailbox@ofwat.gov.uk)

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