



Ofwat
Centre City Tower
7 Hill Street
Birmingham
B5 4UA



Nicola Cocks



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16th September 2020

Consultation on Charging arrangements for new connection services

Dear Sir/Madam

Thank you for the opportunity to respond to the consultation on charging arrangements for new connection services which was published in May.

A detailed response to each of the questions asked is included in the attached document.

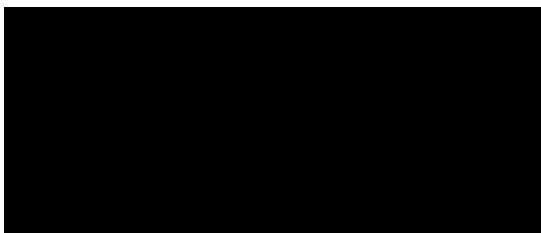
We are supportive of the proposed standardisation of terminology and having common clear worked examples across all companies charging arrangements. We believe improvements in these areas will help to close the perceived gap in pricing as you will see in our responses to questions 4 and 5.

These improvements could alleviate the requirement for a common methodology, which could require significant changes to companies' systems or commercial arrangements. We believe the timescale for implementation of any significant changes to methodology should be no earlier than 2023-24 and any mandatory changes to the rules on cost reflectivity should also align to this timescale.

Companies are concerned about the competition law risk around establishing a group to look at creating a common methodology for charging. We propose a small working group including Ofwat, Water UK and water company representatives to create the terms of reference in order to gain a consensus across the industry that any competition law issues have been addressed before the larger group commences its work.

We look forward to working with you to implement improvements to the charging arrangements.

Yours faithfully



Nicola Cocks
Regulation Director



Charging arrangements for
new connection services for
English companies:
comparative analysis and
consultation

16th September 2020



Q1: Do you agree with our proposal on common terminology and the way we propose to implement it? What do you think would be the impact of harmonising terminology for charges for new connection services?

1.1 Thames Water agree that using common terminology will be beneficial for customers and make it easier for them to understand services across the water companies charging arrangements. There would be some systems changes required to embed these into all our documentation, however, we believe it is reasonable to make these changes in line with the proposed timescales from April 2022.

Q2: Do you agree with the definitions in the glossary (Appendix 1)? Please tell us what definitions you would amend, remove or add.

1.2 Thames Water have reviewed the glossary and propose the following amendments:

1.3 We suggest that the definitions for footpath and carriageway align to the National Joint Utilities Group definitions as set out below, and we would like to point out that footpath and footway are not the same thing as your glossary currently suggests:

Table 1 NJUG definitions¹

Carriageway	A way constituting or comprised in a highway, being a way (other than a cycle track) over which the public have a right of way for the passage of vehicles. It might be useful to add that reinstatement is required to comply with the New Roads and Streetworks Act (NRSWA)
Footpath	A highway over which the public have a right of way on foot only.
Footway	A way comprised in a highway which also comprises a carriageway, being a way over which the public have a right of way on foot only.

Source: NJUG Publication Volume 1, Issue 5, 2018, Glossary, page 15

1.4 We notice that in Appendix 2 you use the term “Made Ground” in the proposed examples which is not in the glossary. We suggest that “Made Ground” is replaced in your examples with Footpath.

1.5 “Unmade Ground” is referred to as having no surface, we suggest amending this to having “no laid surfacing”.

1.6 The use of “Charging Rules” and “Charging Scheme Rules” are very similar and could easily be mixed up by customers. We would propose changing the titles to help differentiate them as “New Connections Charging Rules” and “End User Charging Scheme Rules” respectively.

1.7 “Communications Pipe”. The additional wording (in red in your glossary) ignores some of the nuances around the statutory position as to which part of the service pipe vests in the

¹ NJUG Publication Volume 1 Issue 5 2018

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undertaker. For example, where the meter/OSV is laid inside the boundary of the premises and as near as practicable to the street, the communication pipe will extend beyond the boundary of the property and up to the point of the meter/OSV. Another example is that where the main connecting the property to be connected is not laid in a street that abuts onto that property, the communication pipe will only extend to the boundary of the street in which the main is laid. If the additional definition is to be accurate it needs to reflect all of this or will be misleading in some cases. The additional wording could be removed, or alternatively add a caveat that stipulates the additional words apply to most but not all cases, as there are exceptions.

- 1.8 The use of “we” should be removed from the definition of “No Excavation” and replaced with “the water company”.
- 1.9 We would like to suggest that the word “Practical” is replaced with “Practicable” (the meaning of which is “capable of being put into practice”) when describing “Point of connection”.
- 1.10 The “Requisition Charge” definition could be simplified as “charges set for the provision of a New Water Main S41 (1) and New Public Sewer S98 (1)”.
- 1.11 Under “-Self-Lay Provider” the term “operative” is generally used to describe an individual carrying out a piece of work and could be confusing if used here. We suggest replacing the word operative with “company”.

Network Reinforcement

- 1.12 Lastly, we request that Ofwat amends its definition of “Network Reinforcement”. We wrote to you in December 2018 highlighting that NAV customers are required to pay an Infrastructure Charge equivalent, however NAV bulk supplies are not included in the list of allowed application types included in the Network Reinforcement definition, this is therefore creating a cross subsidy between customer groups. A response was received in January 2019, advising that you would reflect on this further. We note that in January 2020 you issued a NAV Policy FAQ² which included the following question, “How do companies recover charges for new infrastructure?” The answer advises that the infrastructure charges collected by NAVs are for enhancements for upstream services required by the incumbent company, hence we believe you have linked payment of these infrastructure charges directly to Network Reinforcement spend required by the incumbent water company.
- 1.13 This is further supported in the recent RAG consultation 4.09 appendix 1 (June 2020 Consultation version) where the footnote confirms that contributions collected by NAVs and passed onto the incumbent water company are inside the price controls.
- 1.14 This should be reflected in the Network Reinforcement definition to ensure that work on our network subsequent to appointment under section 7(4) of the Water Act should be considered Network Reinforcement. This would ensure that all water companies apply this consistently, and that the costs are included in the calculation of infrastructure charge prices.
- 1.15 Thames Water intends to include NAV related reinforcement to the matching of infrastructure charges for the current 5 year rolling period and going forward.
- 1.16 The wording in the Network Reinforcement definition, “It also includes the additional capacity in any earlier Water Main or Sewer that falls to be used in consequence of the provision or

² Ofwat NAV Policy – Frequently Asked Questions, Jan 2020



connection of a new Water Main or Sewer” is ambiguous and should be made more explicit. We have not been able to find any evidence that Water Companies are applying this to their calculations, and we are unsure how this could be applied in practice.

- 1.17 We would like clarification on whether the intention is to reclassify earlier investment for growth ahead of need, for example to enable efficient planning and delivery of capacity, as Network Reinforcement when developer applications which will utilise this capacity are received. Thames Water currently use a planning horizon of up to 25 years when planning our infrastructure upgrades and this could mean reclassifications will eventually spread over multiple AMPs. We note that this would need to be explained in Annual Performance Report (APR) tables. We are happy to work with Ofwat to explore how this could be incorporated into the APR in a transparent and clear way.

Q3: Do you agree with the proposal to set out explicit expectations on the presentation of worked examples? What do you think would be the right level of detail required?

- 1.18 Thames Water agrees that the use of worked examples is beneficial for customers and for Ofwat to set out explicit expectations to ensure all Water Companies publish them in a way that means they are consistent and comparable as far as practicably possible. In our 2020-21 charging arrangements we have published the examples as required in the Information Notice 1905 2020-21.
- 1.19 Rather than change the examples from last year we propose you provide greater clarity over what is required in the examples from last year’s Information Notice. Continuing with these examples would be more consistent for customers rather than changing the examples again.
- 1.20 Our responses to Q4 and Q5 should be taken into account when determining the level of detail required and how explicit the expectations are around what is included in each example. The examples published should include all charges for activities and materials expected in an average job in the surface type being used, to ensure they are transparent for customers. For example, is a service connection charge a “tapping only connection” or should it also include service pipe and boundary box fitting excavation and reinstatement? You could also consider requesting the average number of trial holes, traffic lights, and other fittings that might be charged for separately by some companies.
- 1.21 In your Appendix A2 you require service connections to include average traffic management, but this is not a requirement listed for mains examples. The average traffic management costs should be included in all types of worked examples where it is applicable. We would expect that, as a minimum, there would be traffic management required for connections in the road to an existing main.

Q4: Please highlight any substantive areas of our analysis you think are missing or could be improved

- 1.22 There are significant differences in the way each water company has presented its charges. Some companies charging arrangements exclude or separate out many activities Thames Water consider a fundamental part in the delivery of the whole job. We believe this makes the analysis and comparisons between each company inconsistent as we do not believe all activities or materials have been included in the examples.



- 1.23 In our response to Q5 we have investigated the different charging levels between Thames Water and Bristol Water as compared in the consultation. We believe most of the difference has been identified and the charges are not directly comparable – see Q5 response for full details. Considering this, the conclusion Ofwat has drawn that there is no link to higher charges where there is greater SLP penetration levels, may not be correct. We therefore believe the analysis could be improved by ensuring the charges included in the analysis (and published examples) are, like-for-like, and include all charges for an average job.
- 1.24 We believe that there is a direct correlation between the proportion of SLP penetration and the overall cost of providing mains. Figure 3.1 in the consultation uses the proportion of connections made by SLPs to benchmark market share. In our response to the Effective markets RFI (October 2019) we present an alternative view of market penetration for SLPs at paragraph 2.187 and the accompanying table 12. This showed that SLP market share on this alternative measure was 59% rather than 30% represented in Figure 3.1 We believe that this is a much more appropriate measure of SLP activity in our region as outlined in paragraphs 2.185 and 2.186 of our effective markets response due to the disproportionately large number of properties connected each year which are internal flats within larger apartment buildings. If this measure was used in Figure 3.1 then Thames Water’s position on the table would shift to the left in your analysis and the overall correlation would be much more apparent.

Q5: What do you think are the reasons for the differences in charging levels? Do you think these differences are a problem? Please provide evidence to support your views where possible.

- 1.25 Thames Water publishes charges which are “all inclusive” to comply with Ofwat’s requirements to make the charging easy for a customer to understand and we have received positive feedback from customers that our arrangements are among those that are easier to use.
- 1.26 The table below shows the breakdown of the example used in the consultation to compare prices between Thames Water and Bristol Water. We have looked at Bristol Water’s charging arrangements to explore what might be driving the difference.

Table 2 Total requisition and connection charges - Scenario 2 (50 houses)

	BRL	TMS	
Requisition	Connection 180mm (PE) - 1 connection	2,195	7,110
	Pipe laying: 180mm PE, road surface - 10m	2,896	7,400
	Pipe laying: 180mm PE, unmade surface - 90m	7,158	29,700
	Pipe laying: 125mm PE, unmade surface - 100m	5,331	22,000
	Pipe laying: 90mm PE, unmade surface - 100m	4,565	21,000
	Standard traffic management (where not included already in the fixed charges)	-	-
	Sub-total	22,144	87,210
	Total admin fees (application, administration, design, inspection, etc)	1,794	-
Sub-total	23,938	87,210	
Service connection	Total New connection charge 3m - no excavation - 50 connections	14,975	16,500
Total charge	38,912	103,710	

Source: Thames Water Analysis, data from Bristol Water and Thames Water



- 1.27 We believe that the service connections charge for Bristol Water is their Tapping only fee which excludes laying of the service pipe and any reinstatement, the cost of the boundary box and its installation. These activities and materials are included in the Thames Water charge. If the equivalent activity was included then this would add c£46k to Bristol Water's charge, explaining most of the overall difference.³
- 1.28 The remainder of the difference could be largely explained by the other costs that Bristol Water charge for separately⁴:
- Trial holes, excavation rock/concrete, granular fill, topsoil strip-store-reseed, fencing, crossing point, certain types of concrete, coloured tarmac, anti-skid surfacing, road marking lines-letters and shapes, relaying kerbs-edging and road studs, 2-4 way traffic lights, 2 man stop go, road and lane closures, reinstatement of land drains, other fitting and thrust blocks.
- 1.29 We do not believe there has been any allowance for these costs in the example for Bristol Water, but all the above are included in the Thames Water charges in the surface types as applicable and averaged out. Hence the charges are not directly comparable between the two companies and may not accurately reflect the total charge a Bristol Water customer might expect to pay on average.
- 1.30 We have noticed similar differences in other water companies' charging arrangements too, so this is not just a difference between Thames Water charges and Bristol Water charges. For example, Anglian separately price or charge actual cost for traffic management, street closure and permits, third party costs, crown and protected undertaker fees, trial holes, water fittings (air valves, washout, fire hydrant and other), line stop, private land compensation to third party owner.⁵
- 1.31 We do not believe the differences in charges are an issue providing companies can demonstrate they are cost reflective, but the apparent scale of the differences could be closed by ensuring the charges are directly comparable on a like-for-like basis. The proposal by Ofwat to be more explicit on ensuring the worked examples include all costs for an average job would assist in this.

Q6: Do you agree with our proposal to modify the Charging Rules for New Connection Services to explicitly include cost-reflectivity in the general principles? What other measures, if any, could be put in place to provide greater assurance that water companies' charges are cost reflective?

- 1.32 Thames Water agrees with the general principles of cost reflectivity and we are confident that our overall charges for New Connections meet this requirement.
- 1.33 We would like to understand further at what level of granularity you are proposing changing the rules on cost reflectivity. Thames Water has a schedule of rates for water connections activities, which we have been able to ensure is cost reflective overall but does not ensure each individual activity within the schedule is cost reflective. The commercial arrangements

³ <https://www.bristolwater.co.uk/wp-content/uploads/2019/01/New-Connections-Charges-Schedule-19-20.pdf> Examples 3 and 4 on page 20 and charges in section 5.

⁴ <https://www.bristolwater.co.uk/wp-content/uploads/2019/01/New-Connections-Charges-Schedule-19-20.pdf> Section 4.

⁵ <https://www.anglianwater.co.uk/siteassets/developers/development-services/developer-charging-arrangements-2019-2020.pdf> section D6-8 and E9-11



we have in place with our suppliers cover the whole suite of Developer Services activities and do not tender the activities separately.

- 1.34 We agree that it is important to ensure that companies are monitoring their supply chain to ensure the arrangements are fair to customers and excess profits are not being made. However, as the nature of these commercial arrangements will differ between companies it may prove difficult to enforce an obligation across the sector for more granular cost reflectivity without involving some significant commercial renegotiations.
- 1.35 There may also be systems constraints or resource increases for our suppliers to take into consideration depending on the granularity required. Any changes to systems or resourcing levels could result in additional cost to our suppliers which are likely to be passed on in the rates and end up increasing customers' charges.
- 1.36 As a result of this consultation, we have commissioned an external consultant to review the schedule of rates at an activity level and to carry out some benchmarking to highlight any areas for improvement. We will consider the outcomes of this review when setting our tariffs for 2022-23 and make any amendments we feel are required.
- 1.37 We recommend that you issue further clarity on what additional requirements you are looking for regarding cost reflectivity and that implementation into the rules is aligned with the timelines of the outputs of the proposed working group to which we have responded in more detail in Q8.

Q7: What do you think are the benefits and disbenefits of having common charging methodologies. Do you think companies should adopt common methodologies?

- 1.38 We think it would be possible to make changes to the charging arrangements which make the presentation of charges more consistent across the water companies, thus providing customers with a similar benefit without having a full common methodology. For example, the rules could be more explicit in what should be included in the fixed charges and what should be published as separate add-on charges.
- 1.39 Thames Water agree that having common charging methodologies, which remove areas of ambiguity for customers, would benefit them in making charging arrangements easier to understand. This would remove some of the issues that we have highlighted in our responses to Q4 and Q5.
- 1.40 There is a disbenefit around the perception of collusion and anticompetitive practises. We have elaborated further and made proposals on how to resolve this in our response to Q8.
- 1.41 A further disbenefit could be to restrict innovation within companies charging arrangements by creating too rigid a framework for tariffs.

Q8: Do you agree with the high-level scope of the proposed New Connection Charges working group? Please tell us your views on the proposed working group, including whether Ofwat should make the work mandatory, for example through a change to our new connection rules.

- 1.42 We agree that improving consistency in terminology and the presentation of charging arrangements would be beneficial to customers. However, we think that there are many complexities to consider when looking to develop common charging methodologies.
- 1.43 Water companies have different contractual arrangements already in place with their suppliers, and information may not be available in a common format. There may be

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contractual restrictions impacting water companies' ability to change what is required from their suppliers within the proposed timescales.

- 1.44 There may be systems changes required for Water Companies and their suppliers in order to comply with any changes that are necessary. These could take time to implement and be tested and there would be a cost associated in doing this, which is likely to be passed onto customers as suppliers will need this to be funded through their prices.
- 1.45 Companies are concerned about the competition law risk around establishing a group to look at creating a common methodology for charging. Some companies perceive this risk to be higher than others. We see that there are two options to alleviate this. Either participation in a group is made a regulatory requirement as it is in the electricity sector or there needs to be very clear terms of reference agreed for this group including review and approval by relevant legal colleagues.
- 1.46 To eliminate the need for making the working group a regulatory requirement, we propose a small working group including Ofwat, Water UK and Water Companies is established to create the terms of reference in order to gain a consensus across the industry that any competition law issues have been addressed before the Working Group commences.
- 1.47 If there are significant changes required to our existing tariff models as an outcome of the review, then we believe best practise would require external assurance that our models are compliant with the rules, as we did when the Charging Rules were first implemented. This would need to be built into the timeline.
- 1.48 There could be an impact on the calculation of the NAV discount for capital maintenance and replacement costs for Bulk Supplies, which should be considered alongside the responses and outcomes of the NAV consultation currently taking place.
- 1.49 There would need to be a balancing of the need to standardise and the need to allow for innovation and maintain the spirit of competition that D-MeX is driving Water Companies towards.
- 1.50 Any impact on customer groups as a result of price changes resulting from a change in methodology would also require consideration and potentially the need for a period of consultation with customers.
- 1.51 Ofwat is proposing to standardise terminology through a change in the rules from April 2022, which we believe is a reasonable timeframe.
- 1.52 We are concerned about the timeline for implementing more extensive change. Dependant on the scale of changes proposed by the working group, we do not consider that there would be enough time for water companies to compile recommendations by mid-2021, Ofwat to approve and companies to robustly make changes to their methodologies in just a couple of months following the issuing of the approval. Best practise would imply that these changes are likely to require external assurance and consultation with customers before obtaining Board Approval in January 2022. We consider this to be an extremely challenging timeline.
- 1.53 We think the earliest that these changes could be mandated through a change in the rules would be April 2023 for Water Companies to have in place robust models, systems and assurance to ensure they can comply. This would also allow for customer consultation if required. However, should there be a requirement for some water companies to change their



commercial arrangements with suppliers this could take longer. Ofwat could publish the changes as aspirational best practise guidance from April 2022, but delay mandating the changes to the rules depending on the scale of changes and the recommendation from the working group.

