

Ofwat's New connections charges consultation responses

Consistent Terminology

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?

Response:

We support the move to consistent terminology in most cases. It will be easier for those who need to work in different water areas to navigate charging arrangements and find specific information quicker if some terminology is harmonised and consistent. However, we have some specific concerns that we outline in response to question 2, where the definitions put forward do not work. We would expect these to be either amended or removed and we explain our proposal in each case.

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

Response:

We have 2 key issues with these definitions:

- They should be self-contained. When looking at any definition you can understand what it refers to, instead of then having to go read a number of further definitions. For example, "alternative point of connection" could be redefined as "Any point on our network other than the nearest practical point where the main or sewer is the same size or larger than the new connecting main or sewer".
- They should be consistent. For example, "long length" (which we recommend removing) refers to 'roads' when there is a definition for carriageway.

We think that it would be useful to produce diagrams to aid understanding. For example, a diagram could easily clarify the constituent parts of your service connection definition.

Further, we have specific issues regarding some definitions outlined below:

- Alternative point of connection
This definition is not self-contained and should be redefined as "Any point on our network other than the nearest practical point where the main or sewer is the same size or larger than the new connecting main or sewer".
- Carriageway & Footpath
The proposed definitions here are misleading. Some footpaths are tarmac or concrete covered ground and, equally, some roads are not tarmac covered. These definitions should be based on the use of the path and defined in a way that is not dependant on the construction material. For example:
Footpath (unmade ground)
Pavement (made ground)
Road (made ground that is used as a vehicle access way)
- Communication Pipe
We believe that the amended definition for 'Communication Pipe' is potentially problematic, as the meter housing and stop valve is not always found on the length of pipe that runs between the property boundary and the new or existing water main.

For example, the suggested definition does not account for wall mounted meters or other alternative locations. We would suggest that either this portion of the definition is removed or clarified to state that it does not always include these (the latter is a less preferable option as it will not allow for consistent or comparable charging).

- Diversions Charges

This definition is not self-contained and should be expanded to include that they are “charges to recover costs reasonably incurred in diverting mains or public sewers”.

- Domestic Premises & House

We are unclear if, as presented here, both “house” and “domestic premise” are required as there appears to be no distinction between them. We think there is value in having a different definition for properties that are a single dwelling (house) and properties that comprise of multiple dwellings (block of flats). This aids in talking about connections vs connected properties.

- Existing main

This definition should be expanded to clarify that it could include off-site and on-site pipework.

- Infrastructure charges

We feel it would be beneficial to include some clarity around re-developments, as this is an area that can cause some confusion amongst customers. Our suggested definition would be: *“Infrastructure Charge” means the charges described in section 146(2) of the Water Industry Act 1991. That is, a charge paid by the developer to the water company when a property is connected to the company’s water supply or sewer for the first time or following re-development, which contributes to wider network reinforcement to meet the increased demand arising from the new connections.*

- Long length & Short length

We think this definition should be removed. It does not align with the way all companies set their charges and so could create confusion in trying to implement it industry-wide. For example, rather than talking in terms of long and short sides we include a 2m length within the connection charge and then work on a per metre basis thereafter.

- Self-lay

This definition is not self-contained and should be redefined as “Where developers, or their contractors, install new water mains and service pipes instead of asking us to do the work”.

- Service Connection, Supply Pipe

Not only are these definitions not self-contained, we found them confusing. We suggest diagrammatic aids when defining these items (alongside communication pipes and service pipes).

Presentation of Charges

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 to be required?

Response:

It is unclear if this proposal is some additional presentational guidance on the same scenarios as last year, or incorporating the additional guidance section A2 of the consultation document, or maybe even both.

We agree with the principle of creating a common way to present worked examples. This will enable developers who operate nationally to easily pick up any companies charging schemes and understand what is changing year on year.

When picking the correct level of detail care needs to be given to ensure that the purpose of the analysis - that developers can easily see how their charges may be changing year on year - remains the most important factor rather than also using this analysis for industry-wide unit rate comparisons.

Due to this, we do not support disaggregating the costs too far or providing too specific guidance on individual items – if the purpose were to create industry-wide comparisons these reservations would be even greater.

For example:

- if costs are disaggregated too far, they may go beyond the level of detail in some charging schemes and present a lot of potentially variable percentage changes that could confuse users. i.e. if manhole rates are required separately to sewer lengths. This will cause confusion for developers as in their day to day dealings with the charges they would not see this level of detail.
- if overly specific guidance is given, then the company may be devising charges purely for this exercise. i.e. if it is required to assume MDPE pipes, and company policy is to use barrier pipe (as is the case for Wessex Water) then an MDPE rate will be required and never seen by developers outside of these examples.

To this end we suggest that when presenting these scenarios, only the headline new connection and requisition costs, by what is contestable and un-contestable are quoted. This will allow a clear focus on the headline costs that they will have to and could incur and the changes to them, while avoiding the potential pitfalls outlined above, and while still being able to see a like for like comparison across the country.

When presenting these, we do think that added workings or commentary on how the example is created from the company's specific charges would be of great use to developers and ensure greater transparency and trust in the exercise. However, this will be dependent on the specific charging arrangements and so will differ between companies.

Additionally, we do not think that adding multiple similar scenarios, such as the 12 connection scenarios in A2, is proportionate. It is not possible to create a set of examples that is all encompassing. Having lots of examples will be hard to digest and could confuse readers. We favour keeping the 2020-21 structure of only 2 lengths.

Infrastructure charges present an issue here too. Including them removes the ability to compare across the country. Additionally, with the pressure to move to regional charges, this

will add to the confusion in presenting these here. Therefore, we think they should be excluded. As we have the requirement to ensure they are cost reflective, monitored through table 2K of the APR, there is protection for customers to ensure they are set at the correct levels.

Analysis of charges

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

Response:

The levels of detail in the worked examples do not easily support cross company comparison. For this purpose, a greater degree of specificity is required. For example, is the meter a dumb meter or a smart meter; is it just the cost of the install or is it the fully allocated cost?

To improve a cross-company comparison, exact scopes and materials should be specified.

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.

Response:

There will be a large degree of differences between companies, depending on their regional circumstances, procurement and delivery strategies, and approach to risk. These will drive legitimate differences in costs and are controlled for through an appropriate cost assessment methodology as part of the price control process – these should not be of concern.

However, until there is confidence that like for like jobs are being compared there could still be issues.

A potential issue is how companies use the “exceptional circumstances” clause. Differing definitions here could lead to differing levels of complexity being included in “average” prices and so lead to a distortion when comparing across the industry.

Cost reflectivity principle

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?

Response:

We agree with this proposal in principle, and we have adopted this as a principle in the round when setting our charges to ensure that they are fair and enable competition in this market. However, we have concerns over the time period in which it would be adopted and how we would demonstrate compliance with it.

Setting up front fixed charges creates a natural opposition to fully cost reflective charges. We disaggregate our charges to a level agreed with stakeholders through extensive engagement and charge the average price for each item. These are calculated based on historical, actual costs. This ensures that we are cost reflective in the round when considering what we have previously delivered. This does not and cannot give us a cost reflective quote for each job.

This averaging process will then result in the cheaper jobs being more attractive to competitors in this market. Thus, over time we would expect to see more of the simple, cheaper jobs go to alternative providers, whereas we continue to deliver the more expensive jobs.

Finally, with large capital jobs we will not see income and expenditure necessarily line up in a given reporting period. Some large requisitions can take more than three years to complete, whereas we would expect to receive the income up front.

Therefore, we think that although we would agree with this as an overriding principle, we would be very wary of including it as rule that compliance with is measured annually through the APR.

Industry collaboration

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

Response:

Although we can see some benefits, such as comparability between companies, in having common methodologies we believe that companies charging structures should be owned by the company's board and defined through engagement with the company's stakeholders.

We engage with our stakeholders annually to ensure that we are setting our charges in a way that works for them and for us.

If engagement is done correctly, with the correct stakeholders and across the country then naturally charging methodologies should converge to deliver these benefits while retaining the flexibility to deal with specific local issues.

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.

Response:

We have serious concerns about the potential competition law implications of the proposed industry discussions around charges and in particular note the General Court's findings in the EU Dole Food competition case:

Therefore, unless there was a regulatory requirement to participate in such a group we would not look to enter into discussions along these terms.