

February 2021

Variation of Icosa Water Services Limited's appointment to include Twigworth in Gloucester

About this document

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On 19 November 2020, Ofwat began a [consultation on a proposal](#) to vary Icosa Water Services Limited's ("**Icosa Water**") appointment in order for it to become the water and sewerage services provider for a development in Severn Trent Water Limited's ("**Severn Trent Water**") water and sewerage services area called Twigworth, Gloucester ("**the Site**").

The consultation ended on 17 December 2020. During the consultation period, we received representations from three organisations, which we considered in making our decision. On 26 January 2021, we granted Icosa Water a variation to its existing appointments to enable it to supply water and sewerage services to the Site.

This document gives our reasons for making this variation.

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1. 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 Severn Trent 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.

2. 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 a bulk supply and bulk discharge agreement with Severn Trent.

3.1 Unserved status of the Site

To qualify under the unserved criterion, an applicant must show that at the time the appointment or variation is made, none of the premises in the proposed area of appointment or variation are served by the existing appointee.

Icosa Water has provided a letter from Severn Trent, dated 28 May 2020 confirming that, in Severn Trent’s view, the Site is unserved for water and sewerage services. We therefore consider that the Site is unserved.

3.2 Financial viability of the proposal

We will only make an appointment or variation 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 will match Severn Trent’s charges for the Site. 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 Severn Trent. 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 Severn Trent.

3.4 Effect of variation on Severn Trent'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 Severn Trent'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 Severn Trent. 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 Severn Trent 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, we estimate that there would be no impact on the water bills of Severn Trent's customers and a small increase (£0.006) impact on the sewerage bills of Severn Trent's 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.

3.5 Developer choice

Where relevant, we take into consideration the choices of the site's developer. In this case, the Site's developers– Bovis Homes Limited – said that they wanted Icosa Water to provide water and sewerage services for the Site.

3. Responses received to the consultation

We received three responses to our consultation: from the Consumer Council for Water (“**CCW**”), the Drinking Water Inspectorate (“**DWI**”) and the Environment Agency. We considered these responses before making the decision to vary Icosa Water's appointment. The Environment Agency and the DWI confirmed that they had no comments to make on the consultation. The points raised in CCW's responses are set out below.

3.1 CCW

CCW's response stated that in general it expects new appointees to provide consumers with prices, levels of services and service guarantees that match or ideally better those of the incumbent company. CCW supported Ofwat's proposal to make this variation, but conveyed its disappointment that there would be no direct financial benefit to customers from having Icosa Water as their provider of water and sewerage services rather than Severn Trent as Icosa Water proposes to charge customers for water and sewerage services on the same basis as Severn Trent.

CCW agreed with our overall assessment that customers on the Site will be no worse off in terms of the levels of service if served by Icosa Water rather than Severn Trent. It said that Icosa Water's levels of service generally match or exceed those offered by Severn Trent. For example, Icosa will contact customers within two hours to arrange for a test if they make a water quality complaint that may be causing an illness; Severn Trent does not commit to such a response.

CCW noted that Icosa Water will not be able to offer a social tariff to its financially vulnerable customers in the way Severn Trent can, although it will offer the standard WaterSure tariff. CCW stated that it may be appropriate for Icosa Water to tailor some of its services and that it expects it to offer appropriate support to individuals in financial difficulty, especially if they would otherwise have benefited from a social tariff. It states this should not be at the expense of its other customers.

CCW further commented on our estimate that the variation would result in a £0.006 per year increase in the sewerage bills of Severn Trent Water's existing customers once the Site is fully built out. It appreciates that this will have a negligible effect on bills, but states that it is unclear whether there will be any significant benefits arising from this arrangement for the incumbent's

customers. It questions the value of the NAV regime if it cannot deliver benefits to customers.

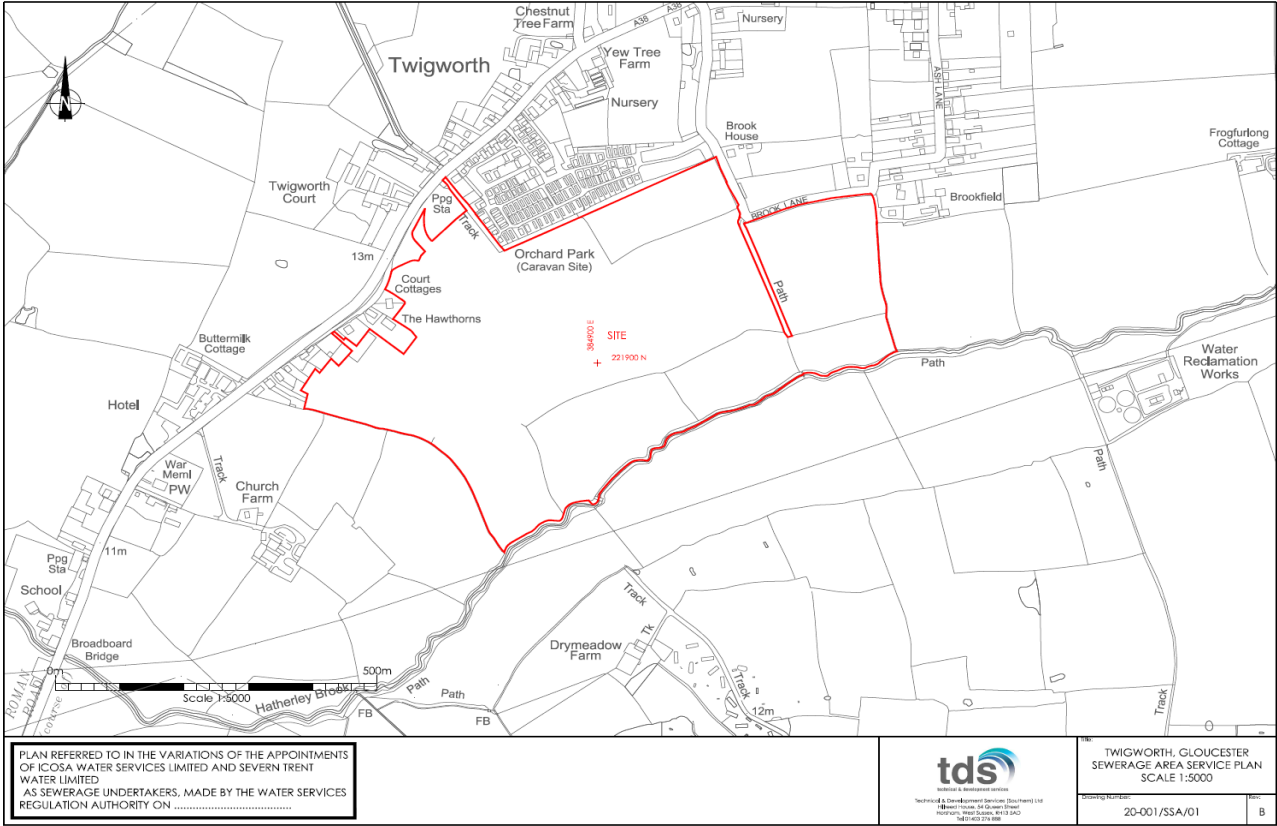
Our response

One of our key policies is that customers should be no worse off if a NAV application is granted. An applicant must therefore ensure that overall its new customers will be 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. We do not require applicants to offer a better service and price than the incumbent.

4. 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 variation became effective on 27 January 2021.

Sewerage



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