

Ofwat
Centre City Tower
7 Hill Street
Birmingham
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4th June 2021

By E-mail: charging@ofwat.gov.uk

Dear Sirs,

RE: **CONSULTATION ON THE SCOPE & BALANCE OF DEVELOPER CHARGES & INCENTIVES**

W A Consultancy provides advice and guidance to a number of Developer Clients (and established Engineering Consultants) on all aspects of Water and Sewerage infrastructure provision. In addition, it continues to be retained as an expert witness on sewerage/drainage and land acquisition due diligence matters. With over 50 years' experience in a crucial part of the Utility Sector, augmented with sector specific research, supplemented with access to client disclosed evidence, W A Consultancy is well placed to provide a balanced and unbiased perspective of the efficacy and equitable fairness of the charging regime confronting the Developer Community. We therefore trust our response makes an effective contribution to the consultation process and that it will be afforded full weight and respect, as declared by Ofwat in its' declared Strategy for engagement⁽¹⁾.

1. GENERAL COMMENTS

1.1 In the preamble to the consultation, Ofwat state the charging regime:

- ***"... should be doing more to tackle long-term challenges for the water sector"***,
- ***"... water companies should provide incentives for developers to build water efficient new homes and sites with sustainable drainage"***.

There is wide consensus on both counts with developer attitudes and approaches to environmental sustainability, inclusive of improved utility asset/resource resilience, continuing to make a significant and positive difference. That said, the consultation presents a series of proposals that seek to place a substantial part of an obligation to 'do more' on developers rather than be a shared, collaborative responsibility involving the water and sewerage sector. In many respects, the consultation is presented as a proxy for developers to offset the infrastructures investment pressures confronting water and sewerage companies as it tries to respond to population growth and the consequences of climate change.

1.2 A major concern voiced by our clients', in addition to the Development Community in general, is that whilst reforms are continuing, they are leaving in their wake a litany of costs and charges that are so staggeringly variable they defy logic. Furthermore, the absence of evidential justification, especially when one considers the various cost items that make up water company individual costs and charges is not helping. In the three years that charging rules and charging arrangements have been in place, annual inter-company comparisons, undertaken on a strict like for like basis, have repeatedly identified significant variation(s) and a lack of clarity in company costs and charges.

• ⁽¹⁾ "Time to Act Together" - Ofwat's Strategy (October 2019)

To their credit, Ofwat appear to have acknowledged this problem, having had several attempts to gain a more detailed understanding of the issue(s), but regrettably, the situation today is somewhat worse when compared to the charging environment that existed pre-April 2018. It is unfortunate, given the effort that has been expended, but the collective view of Developer Customers is that we have a charging regime that cannot be considered to be cost reflective - this primary issue must be effectively dealt with before further reform(s) are considered, especially against a background of excessively escalating developer costs.

1.3 Continued High Levels of Potable Water Leakage – A Major Disincentive

Whilst excessive levels of leakage from water company mains and assets is allowed to continue, it creates an unhelpful mindset, i.e., by working against the much-needed attitudinal change to water use that is crucially important to improved resilience. Moreover, relying on the Developer Community to provide offset mitigation is anathema to the statutory obligations placed on all water companies – a principle not considered in the Frontier Economics Report. Ofwat is strategically positioned as the statutory regulator to ensure more effective and responsive incentives (both positive and negative) are in place for water companies to better deal with leakage. In its annual Report to Defra⁽²⁾ (June 2020), Ofwat conceded that in the five years up to and including 2019, cumulative levels of leakage had effectively remained static. Furthermore, recent data confirms the underlying level of leakage is the equivalent of one person's daily water use (metered) for each and every day, namely, c 130 litres/p/day. If water is to be labelled the valuable and finite resource it is, then water companies, facilitated by Ofwat, must be seen to be doing much more to tackle leakage. This is crucial, in addition to being part of a shared commitment to improved resilience – a commitment that needs to be better/proportionately defined through collaborative working rather than subjective ideology.

1.4 Whilst new homes must and will continue to be designed/constructed to be both environmentally sustainable and energy efficient, bailing out water companies from their statutory responsibility by requiring all new homes go beyond present Building Regulation requirements for water use, to secure what in effect would be a nominal 'environmental offset', is mere semantics. Moreover, Ofwat and water companies in general appear to have little to no appreciation of a house building industry already working with Government on the Future Homes Standards, inclusive of reductions in potable water use and how this will be achieved against other competing environmental requirements - see later comments. From a water company perspective, in the absence of clear rules, together with effective direction relating to an agreed and consistently applied water use specification, (and therefore cost) water company subjective discretion will continue - evidenced by the considerable variation in how reductions/offsets (when given) are being applied.

1.5 In terms of the contribution to water use reduction achievable via new housing, whilst still a matter of considerable importance, what this will likely yield needs to be put into context. Likewise, those areas where only water companies and Ofwat can make a positive difference.

- New housing represents no more than 10% of all annual housing transactions
- The existing housing/building stock is the area that needs far greater incentive to reduce water use though a combination of mandatory metering and a requirement for water fittings that use less water to be an integral part of the refurbishment/DIY market. Compulsory metering for new homes has been in place since 1999 but Ofwat appear reluctant to progress to compulsory metering for all building typologies – what are the reasons for this if water is considered such a finite and precious resource?

• Water Services Regulation Authority (Ofwat) Annual Report and Accounts 2019 -20 (June 2020)

- Current water company attitudes to incentives relating to new homes are such that few, if indeed any water companies know what is required to achieve a daily use of 100 litres/p/day, whilst at the same time taking note of the compliance requirements of the Government's Future Homes Standard. For example, the role that wastewater heat recovery systems are expected to play and the minimum delivery requirements for baths and showers for this concept to make a meaningful contribution.
- For new homes, reducing per capita water use to say 100 litres/p/d in non-water stressed areas, before applying any incentive through reduced infrastructure charges, and taking current average household occupation of 2.15 persons/dwelling, (MHCLG data) yields a comparatively low reduction in water use. Moreover, the level(s) of incentive being offered by water companies hardly covers the additional cost of the fittings required to meet a lower water use requirement. In many instances the reduction is set at a level of incentive that is a dis-incentive resulting in a default to current Building Regulation requirements.
- By comparison, if water companies were to achieve a 1% reduction in current cumulative levels of leakage, they could provide the annual water needs for c. 90,000+ new homes. Therefore, is this not a defining moment for Ofwat to redefine what constitutes an "economic level of leakage"?
- The concept of reduction in personal water use matched to a reduced infrastructure charge will have a short shelf-life as water companies will rebalance this discount to zero as Part G of the Building Regulations mandates reduced per capita water use – this is already taking place, see United Utilities, who have set the 2021/22 discount benchmark at zero for a certified water use of 100 l/p/d.

1.6 In the introduction and throughout the consultation, Ofwat repeatedly refer to "the balance of charges". However, in their report of August 2020, disclosed on 27th April 2021, Frontier Economics state in unequivocal terms:

"We understand that there is currently no agreed common definition of the balance of charges. Therefore, the concept of keeping the balance of charges broadly maintained is ambiguous, because it is not clear precisely what should be broadly maintained".

The foundation of Ofwat's Charging Rules was predicated on two fundamental principles. Water & Sewerage Companies were required to adhere to these principles when producing their Charging Arrangements for new connections – namely:

- 1. The Balance of Charges to be maintained**
- 2. Charges should be Cost Reflective.**

In the absence of 'a balance' ever having been defined, in principle but more importantly from a fiscal perspective, raises serious questions about the cost reflectivity of company charging arrangements. If Ofwat's Charging Rules and Company Charging Arrangements are to have credibility this is a matter requiring urgent resolution given the wider ramifications for every aspect of water and sewerage company costs and charges. Moreover, this lack of evidence-based clarity/definition has worked against one of the underlying principles the reforms were meant to address, namely trust and confidence in monopoly water and sewerage businesses. As the evidence supporting our submission portrays, there is complete disarray in company charges accompanied by a persistent and significant divergence in cost that makes it difficult to determine anything other than speculative costs for any new build project, especially if the construction programme crosses financial year boundaries. It is regrettable to say, but the outcome is one of a series of reforms that have introduced unnecessary complexity, in addition to having failed to provide cost neutrality for developers, (as a worse case outcome). They have instead enhanced the commercial interests of water and sewerage companies.

- 1.7 In our view and that of our clients before reforms can be considered there has to be an evidenced-based understanding of precisely how costs and charges are actually made up. Without this, cost reflectivity and confidence in costs and charges will remain unfulfilled ambitions. Evidential transparency is the key, but it remains in short supply. For example, water and sewerage companies have asset managers in place but this role is limited in the context of new residential development. Developers do not know what justified proportion of this overhead cost is allocated to Developer charges. Furthermore, there are other aspects relating to costs and charges that fall into the latter category. In many respects, a 'time out' enabling wholesome re-consideration of the charging reforms, i.e., what they should and should not embrace and what they were meant to achieve, would not go amiss. Is this possible before irreparable damage is done?
- 1.8 The collective view is that the proposals outlined in the consultation should have been accompanied by a Regulatory Impact Assessment, (as Defra would normally expect to see) thereby providing greater cost and charging granularity. This is especially important given the significant increase in Developer Community costs. In addition, an RIA would enable the true contribution from NAVs and Self-lay Providers to be better evaluated and compared against original expectations. That said, CEPA's report of May 2021 provides an indication of the market penetration from both SLPs and NAVs, but it is disappointing to note this still falls a long way short of providing effective competition. (There are c 5000 active housing sites, therefore with NAVs reported by CEPA serving c.169 sites, the percentage NAV penetration is a little over 3% - see NHBC website for the number of NHBC sites registered – NHBC registrations constitute 80% of all active housing sites).

2. RESPONSES TO SPECIFIC QUESTIONS

Q1 – Do you have any comments on key conclusions from the Frontier Economics Report?

Whilst Ofwat has asked for comments solely on the Report's conclusions there are several aspects of the Report that raise questions about the accuracy/veracity of its content and therefore, the recommendations and conclusions that have been advanced. Moreover, Frontier Economics do not appear to have taken cognisance of earlier, crucial Government guidance. Likewise, the purpose and intent behind previous legislation. Whilst earlier and related quasi-statutory guidance merited a review by Frontier Economics, e.g., RD 2/95, and para 3.12 of Ofwat's May 2004 "Handling Requisitions and Disputes", the RIA accompanying the Draft Water Act 2014 has always been of particular relevance in establishing the rationale and justification for asset payments/income off-sets:

REGULATORY IMPACT ASSESSMENT (IA No: Defra 1383) – 18th June 2012 **Charging for water & sewerage infrastructure within new development**

"The rationale for asset payments is that because WaSCs obtain a long-term benefit from the additional charges from the new consumers in new development, they should help meet the costs of extending their supply network within developments. Where WaSCs adopt self-laid water supply assets the payment to the developer reimburses the cost developer incurs in self-laying the assets". (Our underlining for emphasis).

Whilst pertinent to matters of cost, charges, and requisitioning, page 11 of the RIA also stated, *inter alia*:

"Fifteen WaSCs responded to a request to provide the requisition and asset payment for a hypothetical development of 150 properties where the mains layout had been specified. The exercise demonstrated that there was considerable variation in the range of requisition charges (£0 - £6700) and asset payments (£21,646 - £96.800) which clearly indicate that there are considerable differences between the water and sewerage companies' approach in calculating these sums".

When comparing the narrative from the 2012 RIA with the *raison d'être* for the current consultation not only does little progress appear to have been made in terms of effectively resolving significant cost and charges diversity, but clearly, there has been a quantum shift towards the Developer Community paying far more for water and sewerage infrastructure – see our supporting evidence.

Further comments on the Frontier Economics Report follow:

- It is noteworthy that Frontier Economics could find no definition of the 'balance of charges' and how this has been determined in actual monetary terms. It remains a crucial omission in arriving at charging reforms that are supposedly fair, affordable, transparent, evidenced based and cost reflective. Somewhat surprisingly, the CEPA Report dated 24th May 2021 (*Approach to Regulation of Developer Services at PR24*), and also prepared for Ofwat, continues the theme of a balance of charges whilst appearing to attach little importance to key statements in this regard, as articulated by Frontier Economics. Is there a reason for this?
- The Frontier Economics Report makes no reference to the statutory duties and obligations placed on all water and sewerage companies pursuant to sections 37 *et al* and section 94 of the Water Industry Act 1991. On both counts water and sewerage company duties to provide, maintain and fund adequate infrastructure to meet future needs remains paramount. Moreover, Section 2 of the WIA 1991 effectively confirms:
 - a. *"Ofwat must carry out its function that will seek to secure water companies carry out their statutory duties and finance their statutory obligations, and ..."*
 - b. *"Secure the long-term resilience of water companies' water supply and wastewater systems"*
- Frontier Economics do not appear to have attempted to define in monetary terms what these obligations actually represent when it comes to cost, inclusive of a detailed and apportioned breakdown identifying actual Developer contributions in preceding years. Surely, this is crucial, unless Water and Sewerage Companies do not have adequate income/expenditure reconciliation data from 1989 onwards? If fairness, transparency and cost reflective charging is to be the basis for any charging reform, then evidence to this effect must surely be allowed to inform any recommendations/conclusions, whilst being the bedrock for any justified fiscal reform.
- As confirmed by Frontier Economics the scope and structure of the Report is, based on, **".... our analysis on economic principles"**. We don't believe this is sufficient for the reasons cited in our response, especially when considering the statutory duties and obligations placed on all water and sewerage companies. Relying solely on an economic perspective to the exclusion of key sectoral statutory obligations can only result in biased conclusions – the very outcome the report exhibits.
- Whilst Ofwat has confirmed it will not implement a requirement for the Developer Community to fund improvements in strategic infrastructure there is concern that this may change after 2025. The unanimous view of our clients is that Ofwat should confirm that this issue will remain off the agenda, even after 2025. Moreover, we would question how water and sewerage companies could effectively and fairly apportion developer contributions in the absence of full evidential disclosure. For example, using the most common size of site, i.e., between 50 and 100 dwellings, how would the demand profile (and therefore contribution to cost) from relatively small sites be accurately determined? In many instances these sites would represent a nominal addition to an existing and significantly larger network. Furthermore, the concept of aggregated sites is unlikely to make a significant difference. In addition, it is reasonable to presume that the contribution from those sites that may have had a previous use, and connected to existing networks, would be factored into any network capacity assessment.

Also, when considered alongside a policy of reduced water consumption, the impact on existing networks/assets has the propensity to yield capacity betterment. Why have these factors not been considered by Frontier Economics?

- Page 14 of the Report suggests that leakage and sewer infiltration reduction yielding network improvement/betterment should be funded by the Developer Community. This is manifestly unfair and inequitable given the statutory obligations placed on all water and sewerage companies – see earlier parts of our response.
- Section 185 Diversions - Frontier Economics have not considered two important aspects, namely:
 - I. When diverting existing water or sewerage infrastructure no account has been taken of replacing aged infrastructure with new by applying the Bacon Woodrow formula to determine a fair and equitable contribution from the water or sewerage company – this formula should be applied in all such instances. Moreover, several water companies have embarked on a programme of replacing asbestos cement pipelines given their deteriorating condition/vulnerability and the negative perceptions associated with asbestos fibre release. As many water mains are constructed in this material the contribution to asset betterment made by the Developer Community should be specifically recognised in these instances.
 - II. There are a number of occasions when formal easements are in place, and which include 'lift and shift' clauses requiring water and sewerage companies to divert at their entire cost – this too should have been recognised in the Report.
- The Report makes the false assumption that Developers decide where new development takes place. Land-use allocations in Local Plans are a function of the local democratic process. Developers merely respond to these decisions and turn local plan decisions into construction reality, whilst providing water and sewerage companies with the means to improve their respective balance sheets by their acquiring additional income generating assets at nil cost.
- Frontier Economics appear to have missed the fact that Water Companies are statutory consultees at the Local/Strategic Plan stage and therefore are able to have sufficient forward visibility on future infrastructure investment needs. They are also well positioned to advise planning authorities of network capacity limitations and how and when these are to be overcome as part of the sector's statutory obligations.
- The Report considers what happens in the Energy and Communication Sector(s) respectively. However, the Report is not entirely correct when it comes to who provides the infrastructure. More importantly, it ignores the fact that asset payments are an integral part of the construction/provision contract.
- The position in the water and sewerage sector whereby Developers pay for the provision of water and sewerage infrastructure and then 'gift' income generating assets to water and sewerage companies is unprecedented. Over a five-year period, the value of this revenue stream is c. £0.50 billion. Moreover, the position advanced by Frontier Economics that most new connections are related to existing customers is not tenable when the number of first-time buyers is taken into consideration, i.e., an average of 335,800/year over the last 5 years. (See Yorkshire Building Society Report). It is an important aspect not accounted for in the Report, likewise, the fact that water and sewerage companies are required to meet the infrastructure needs of a growing population and therefore new household formations.
- In tandem with the last bullet-point the Report does not account for those sites that have had a former use, other than housing, and which were connected to existing company water and sewerage infrastructure. Latest Government data shows land that has had a

previous use represented 53% of all new residential development sites. A crucial aspect missed by the Report and one that has a significant bearing on water and sewerage company infrastructure provision, network capacity considerations, costs, and charges, especially infrastructure charges.

- The Report implies that newly constructed infrastructure may be susceptible to snagging at a level that exceeds the performance of existing assets, thereby increasing water and sewerage company costs. There is unanimous developer (and consultant) disagreement on this front supported by an extensive body of evidence. Typically, the Developer Community pays for compliance inspections; secondly, evidence gathered over 40 years shows post-adoption intervention is almost non-existent; thirdly, the automatic transfer of private sewers in October 2011 resulted in sewerage company financial provisions for maintenance/corrective intervention hardly being spent in the subsequent 10 years. Finally, Frontier Economics did not disclose any evidence in support of their related and somewhat subjective comments.
- The Report makes no attempt to define the value of the income offset based on actual company charging arrangements. The income offset identified in the Report is around £140/dwelling more than the current average – see schedule accompanying this submission. Comparison of the two figures also shows the progressive erosion of the income offset that has taken place since 2018. Irrespective of the value used, the immediate increase in cost for Developers would be considerable. We have provided a more accurate analysis based on current company charging arrangements for 2021/22 – it forms an integral part of this response. From this schedule, it can be seen that the average value of the income offset, based on current company charging arrangements, is c. £462/dwelling. Depending upon who's forecast of new connections over the next 5 years you use, i.e., Ofwat's or Water and Sewerage Companies, the latter being better aligned to Government net new home completions, the cumulative additional costs for Developers over 5 years could be up to £0.76 billion. The schedule is also worthy of further scrutiny as it identifies how water company mains costs have increased over the last two years, i.e., in a range from 29% to an unprecedented high of 355%. How can increases of this magnitude be justified?

With Ofwat having set the required criteria for disclosure of typical company costs using a series of housing scenarios – cost comparison accuracy and consistency being the *raison d'être* - how costs far exceeding the underlying level of inflation can be justified needs to be explained if not fully investigated by Ofwat. At present, these costs and charges are far from credible.

- The Report does not consider how network capacity is determined, especially for existing foul sewers and how this in turn influences the cost components of the infrastructure charge, in particular when determining the level/cost of network reinforcement. Serious questions continue to be raised about how network capacity is determined, evidenced by a recent determination against Southern Water that has resulted in a refund to a major developer of c. £0.55 million. This followed exposure of an unjustified/ flawed S98 requisition. Several housing projects fall into this category and as such, further determinations can be expected.
- We have enclosed as part of the submission an independent paper that goes into detail about the way foul sewer network capacity assessments are undertaken and how they are unrepresentatively skewed to favour the commercial interests of water and sewerage companies. We see no reason why this evidence should not be placed in the public domain and would ask that this be the case. Further discussion/engagement with Ofwat concerning this important matter would be welcome. The Paper also responds to some of the questionable assumptions that Frontier Economics have relied upon.

- The Frontier Economics Report refers to water and sewerage company retained contractor costs and whether these are representative and reasonable. Company Board Assurance Statements do not provide the necessary reassurance in this regard, and we would advocate that time is spent evaluating term contractor rates/provisions to ensure they are fair and representative, in addition to providing customer value for money. Are contractor margins in the water and sewerage sector fair and representative of national civil engineering contractor rates? No one actually knows for sure.
- For the reasons articulated in our response we believe Section 5.5 of the Report is largely superfluous, especially in the absence of factual evidence relating to actual income and expenditure on housing related infrastructure since sector privatisation in 1989, i.e., where, when, and how infrastructure charges have been ringed fenced, invested, and appropriately audited. Ofwat are asked to provide evidence in this regard if it exists.

Q2 – We seek views on our reasoning and proposals with respect to charges for strategic assets, income offsets and the balance of charges rule.

Taking each aspect in reverse order we would respond as follows:

Balance of Charges – as stated previously and confirmed by Frontier Economics, 'balance of charges' has not been defined and remains both ambiguous and subjective. Evidence, especially monetary, would help explain and define what the 'balance' is, if indeed it exists at all after one acknowledges and takes into consideration the statutory obligations placed on all water and sewerage companies.

On page 13 of the consultation, Ofwat make the following statement:

“Companies are now required to publish annually the revenues and associated costs for network reinforcements/infrastructure charges and set charges on the basis of average five-year cost”.

Despite looking for this information it has not been found. Moreover, each company's charging arrangements for 2021/22 made no mention of such and how it has informed their revised infrastructure charges. Frontier Economics also made no reference to this requirement in their Report thereby raising further questions regarding just how thorough their investigations may have been.

Income Offsets – Ofwat concede in the consultation that removal of the income offset will result in increased costs for Developers. How does this reconcile with the statutory guidance issued to Ofwat by Defra, i.e., that cost neutrality for Developers is the expected worst-case outcome of the reforms? Ofwat extoll the virtue of improved competition and the prospect of competition being able to provide an element of compensating provision. However, with only two NAVs prominent in the marketplace and with little prospect of additional players with sufficient critical mass, this remains nothing more than an aspirational comment, unless Ofwat can disclose evidence to the contrary. (See earlier comments regarding NAV market penetration). The time taken to secure a NAV licence from Ofwat (c. 4 months) is also working against the principle of effective competition. Similarly, barriers to increased competition from Self-lay Providers are also undermining any effective increase in competition matched to a growing volume in housing output.

Before arriving at their respective recommendation and proposal, neither Frontier Economics nor Ofwat appear to have looked into the history of income offsets, especially the long-established precedent created in earlier legislation. Section 37 of the Water Act 1945 introduced the principle for income offset with subsequent legislation upholding the requirement until the Water Act of 2014 handed to Ofwat unprecedented power to re-configure water and sewerage company charging arrangements. The *raison d'être* for income offsets is both simple and fully justified, having been

enshrined in earlier and subsequent iterations of established legislation - consider the construct of Section 37 of the Water Act 1945:

"It shall be the duty of every water undertaker to develop and maintain an efficient and economical system of water supply and to ensure such arrangements have been made ... for maintaining, improving, and extending the water undertaker's water mains and other pipes".

Provided that the undertakers before complying with a requisition under this section- may require the owner to undertake to pay in respect of each year a sum amounting to one-eighth of the expense of providing and laying the necessary mains (less any amounts received by the undertakers in respect of water supplied, whether for domestic or non-domestic purposes, in that year from those mains)" (S37 WIA 1991)

The statutory duty placed on all water and sewerage companies to provide the necessary water and sewerage infrastructure to meet the needs of a growing population is unequivocal. It is the Developer Community that responds to the demand for increased housing provision through the risk-based investments that it makes. It therefore remains a critical customer, singularly dependent on the statutory duties and obligations placed on all water and sewerage companies and who maintain an overarching statutory obligation.

Moreover, the almost solus contribution that new homeowners make to the asset and income growth of water and sewerage companies has been recognised by Legislators for over 70 years - we see no reason why this should not continue. In addition, the intent that lay behind the requisition process, especially for sewers, and as a result of the coming into force of the Water Act 1973, was effectively recognition that Sewerage Companies had failed in their statutory duties to effectually drain their area. As such, until the reforms recently introduced by Ofwat, Developers only paid a small contribution, reduced by the income stream derived from new home domestic water and sewerage charges.

If income offsets were questionable in any way, then the 1973 Act, and subsequent iterations of water and sewerage legislation would surely have dealt with the matter. Crucially, there is nothing in the Water Act of 2014 that repeals the continuance of income offsets. On the face of it we appear to have an example of Ofwat using its now considerable powers to better favour the commercial interests of water and sewerage companies at the Developer's expense. Gifting of perpetual income generating assets is an unprecedented commercial arrangement and therefore, if fair and reasonable charges are to prevail, income offsets should not only be allowed to prevail but increase.

Charges for Strategic Assets – Given the statutory duties and obligations placed on all water and sewerage companies pursuant to Section 37 *et al* and Section 94 of the Water Industry Act 1991 this should not even be considered as a fair and equitable inclusion within Developer Service charges. See also our earlier comments regarding how 'in consequence' Developer contributions can be fairly, accurately, and transparently determined. Furthermore, any such imposition would also necessitate a change in primary legislation.

Q3 – What environmental incentives should water companies be offering developers and NAVs? We are interested in examples of good practice. How can we better support this?

3.1 Developers have been committed to delivering improved environmental and sustainability standards in new housing for several years. For example, significant reductions in surface water discharge on sites that have had a previous use, and which had large impermeable footprints. However, since the charging reforms were introduced in 2018, sewerage company discounts of infrastructure charges for reduced surface water discharge to existing public sewers, (when given) have been wholly unrepresentative of the betterment created. In our opinion, further work is required in this area to establish a discount mechanism that is more appropriate rather than the current subjective approach being applied by sewerage companies.

- 3.2 Similar issues arise when it comes to water supplies to sites that have had a former use and connected to existing water infrastructure. Certain water companies, aka Yorkshire Water, refuse to give water infrastructure credits. In one instance involving a recently decommissioned hospital site, not only are infrastructure credits not being given but having presented unequivocal evidence that the site is undergoing a change of use to new housing will result in a much lower water use, Yorkshire Water not only refused to accept the evidence presented but insisted highly questionable off-site network reinforcement must be undertaken. (It is reported options for dispute resolution are under consideration).
- 3.3 Ofwat has once more referred to the role that rainwater harvesting, and greywater recycling can play. Leaving aside the wider public health/CDM issues, both concepts come with a high energy/carbon footprint. Moreover, UK Government policy is moving towards embodied carbon as the likely carbon assessment metric, i.e., a whole life carbon approach that captures both operational and embodied carbon. If crystallised, this will render RWH and greywater recycling very unattractive options. Neither Ofwat nor Frontier Economics appear to be aware of the Government's emerging carbon reduction policy and how this could impact on the concept of larger discounts from water companies for water efficient fittings. Therefore, advocating such a simplistic approach without fully understanding the wider implications and repercussions is counterintuitive, in addition to not being part of the foundation that defines effective incentives.
- 3.4 Environmental incentives that are well considered and effective are welcome but conversely, the 'nitrate' issue briefly referred to by Ofwat on page 16 of the consultation needs to be addressed by sewerage companies as part of their statutory duties and obligations under S94. Nitrate contribution from the urban environment is around 25% of total nitrate loading – the Agricultural Industry being the major polluter. It is noteworthy that Ofwat has avoided intervening in resolving the issues that have effectively embargoed the construction of c. 12,000 new homes in those planning authorities in and around the Solent. Moreover, for commercial expediency, Developers are being coerced into paying to the Wildlife Trust a financial offset up to c.£6000/dwelling just to get sites underway but this is neither appropriate nor sustainable. (The Frontier Economics Report is also silent on such an important issue). In essence, the Developer Community is being put under commercial duress to make a payment to the Trust in order to be able to implement a planning consent. The alternative is a myriad of private wastewater treatment plants associated with each development proposal. Moreover, this latter solution may not necessarily receive planning consent or meet the requirements of the EA's Environmental Permitting Regime when it comes to treated effluent quality. (There is a recent planning appeal decision whereby the Planning Inspector dismissed an appeal for a site in the south of England on the grounds of uncertainty, namely, that a private wastewater treatment plant may not necessarily continue to operate as it should). Clearly, urgent intervention action by Ofwat is needed, having previously penalised Southern Water to the tune of £126M for serious breaches of its S94 obligations specific to WWTWs.
- 3.5 Ofwat make no mention of the benefits arising from more sophisticated meter reading technology, i.e., advanced AMR. First conceived by a major house builder and working collaboratively with United Utilities, truly smart metering on a large pilot site in Cheshire has made a fundamental difference to consumer attitudes to water use. First indications point to significant reductions in daily water use (c. 20%) but definitive evidence to this effect is awaited.
- 3.6 The Developer Community has been at the forefront of developing training alongside BPEC for operatives/contractors who provide service connections. The focus was very much on improved construction quality and specification to reduce service pipe leakage. It is disappointing to note that after 7 years of effort, water company reluctance to adopt/endorse improved working practices in this regard is continuing. How can Ofwat improve the take up of such important initiatives?
- 3.7 In terms of other initiatives, we would advance the following suggestions:

- Agricultural Industry – a commitment to better water use efficiency/recycling.
- Why not consider/introduce tariff structures in domestic water and sewerage bills that encourage and reward customers who use less water? This could be particularly effective in ensuring Developer introduced lower water use initiatives continue after a new home has been sold/occupied.
- Compulsory water use labelling is already progressing as part of the Government's Future Home Standard – Developers are actively involved in the initiative.
- Incentivise the installation of water meters, together with lower personal water use within the existing housing stock and within other building typologies.
- Consider smart water systems beyond RWH and greywater recycling.
- Given the pressure to reduce personal water use, re-consider the hydraulic design standards for adoptable foul sewers. Peak flows of 4000 litres/dwelling are no longer representative.
- Consider the role of AI in the detection of leaks – it has a growing pedigree of success in the USA but there is little to note here in the UK.
- Allow sewerage companies to adopt all SuDS infrastructure
- Sewerage Companies must be encouraged not put barriers in place that fetter the adoption of roads constructed with permeable paving – aka clause B5.1.14 of the current DCG for adoptable sewers.
- Encourage sewerage companies to evaluate the potential for strategically located natural attenuation schemes – ref: S21 Water Act 2014
- Working collaboratively with the Developer Community, undertake dedicated research to evaluate all aspects of extraneous surface water entering foul/combined sewers, including the volumetric contribution from leaking water assets.

4 CONCLUDING COMMENTS

Positive and beneficial reform is always welcome, but this consultation continues to raise concerns. The loss of income offset in our opinion and that of our clients is unfair and unjustified.

The Frontier Economics Report effectively confirms that current charging arrangements are in disarray, whilst being predicated on a concept that is at best ambiguous or at worst, non-existent i.e., the so-called balance of charges. Moreover, it is not that the issues articulated in this response, including how any 'balance' is to be defined and financially determined have not previously been flagged to Ofwat since before April 2018. It is a matter requiring critical attention.

The perception of many in the Development Community remains that of a Regulator that says it is committed to engagement with key customers and industry representatives but in reality, it continues to ignore what the Development Community says/needs in preference to enhancing water and sewerage sector commercial interests. For example, the reforms that came into being in April 2020 were diametrically opposite what the Developer Community needed – why was such an important customer ignored after Ofwat had been advised accordingly?

Developers are committed to improved environmental sustainability and will continue to do so. However, the water and sewerage sector must be seen to be making its own positive contribution rather pass the baton of mitigation to the Developer Community. This appears to be the underlying theme of this consultation. Tackling leakage more effectively and responsively is also paramount,

likewise ensuring what developers have to pay for is fair and representative as well as being cost reflective.

Both Ofwat and water and sewerage companies have to come to terms with what is realistically achievable in an environment of competing and challenging objectives/requirements and the impact of escalating costs. Moreover, the naïve expectation that cost doesn't matter as it comes off the land value is a flawed concept at a time when land value capture is expected to pay for so much. In reality, there are key parts of the UK where the concept will not work, i.e., where land values are already low, contaminated land remediation is expensive and project viability is under serious threat due to other social engineering demands imposed by Local Planning Authorities.

We are in this together, but Ofwat needs to start listening to Developer Customers and respond much more effectively to their needs and expectations.

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