August 2023

Changing Ofwat's charging rules to support the new developer services framework

Ofwat

About this document

We are consulting about changes to our new connection charging rules from April 2025. To complement the deregulation of certain aspects of developer services that we will implement as part of our price review 2024 (**PR24**), we propose measures that will offer protection to developer services customers for whom market choice is currently limited. We are also consulting on changes to our charging rules which support the existing developer services market, including infrastructure charges.

Our consultation relates to water companies wholly or mainly in England (**English companies**), for which we regulate developer charges through our new connection charging rules. Developer services for companies wholly or mainly in Wales (**Welsh companies**) are subject to a different regulatory regime and the issues we raise in this consultation do not currently apply to them.

Executive Summary

The way we regulate developer services is changing. As part of our 2024 Price Review, we are reducing our regulation of the provision of site-specific services. These are the contestable activities involved in connecting new homes to the water and wastewater network. We are removing these from the price control for water (in England) and wastewater (in England and Wales). We are making these changes to facilitate the development of competition in the developer services market.

We are consulting on proposals to amend our English New Connection Rules to complement the developer services market, to (i) ensure customers remain protected from abuses of market power; (ii) refine how companies set their infrastructure charges; and (iii) enable implementation of environmental incentives.

Our proposals include:

- Requiring companies to tether charges for typically uncontested sites to those of typically contested sites.
- Increasing transparency and supporting the market through a requirement to further unbundle charges for activities involved in service connections.
- Introducing two new scenarios for which companies will publish worked examples, to offer additional assurance to developer customers at sites not represented by existing scenarios.
- Providing enhanced guidance via our Regulatory Accounting Guidelines on how to allocate costs to developer services.
- Carrying out a market review prior to PR29, for companies to demonstrate how they support the developer services market.
- Requiring companies to set infrastructure charges taking account of differences between actual and forecast costs and revenues.

Parallel to this consultation, we are also proposing a common framework for environmental incentives in England, for implementation in April 2025. Our aim is to encourage greater water efficiency and more sustainable drainage across all types of new development.

The next steps following this consultation are as follows:

- To implement the provisions for site-specific developer services and the common framework for environmental incentives, we will undertake a statutory consultation on changes to our new connection charging rules for English companies. We would expect to undertake this in early 2024-25.

Responding to this consultation

The closing date for this consultation is 27 October 2023. We are allowing a longer consultation period than normal, because companies will be preparing their PR24 business plans for submission in early October, as well as responding to our other consultations, for example on the measures of experience performance commitments at PR24. Please email us at charging@ofwat.gov.uk with your response, or if you wish to discuss any aspect of this consultation, or to arrange a conversation on the issues we have raised.

We may publish responses to this consultation on our website at www.ofwat.gov.uk, unless you indicate that you would like your response to remain unpublished. Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with access to information legislation – primarily the Freedom of Information Act 2000 (FoIA), the General Data Protection Regulation 2016, the Data Protection Act 2018, and the Environmental Information Regulations 2004. For further information on how we process personal data please see our privacy policy.

If you would like the information that you provide to be treated as confidential, please be aware that under the FoIA there is a statutory Code of practice which deals, among other things, with obligations of confidence. In view of this, it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information, we will take full account of your explanation, but we cannot give an assurance that we can maintain confidentiality in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on Ofwat.

Table 1: Consultation questions

Number	Question
Q1	What are your views on our proposal to link charges for different types of development through the use of tether ratios? What are your thoughts on the use of ratios based on industry maximum figures, not average or median figures?
Q2	What are your views on option 5 that companies should individually charge for separate activities involved in making service connections? Do you agree with our proposal to implement via changes to the wording of the CTWE?
Q3	Do you have views on our proposals to add two new worked examples with the aim of providing additional protection for developments with limited choice? What are your views on suitable new scenarios?
Q4	Do you agree with our proposed general guidance for RAG2 regarding a fair allocation of all relevant overheads across ALL expenditure areas, including developer services?
Q5	Should RAG2 specify methods of overhead recovery for developer services? Are there any disadvantages to doing so? Are there any methods that you think would be appropriate to use across the industry that would drive consistency?
Q6	Do you agree that RAG2 could be extended to cover the recovery and allocation of overhead costs between developments with and without a mains requirement? Do you have any suggestions as to how this should be done?
Q7	What are your views on our proposal to carry out a market review prior to PR29?
Q8	What are your views on our proposal that companies include historical variances between expenditure and revenues in setting infrastructure charges?
Q9	Do you agree with our proposal to enable companies to take account of upsized infrastructure when setting infrastructure charges?
Q10	What are your views on our proposals relating to how we accommodate changes to the provision of income offset?

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1. Introduction

This consultation is about potential changes to our charging rules, which we issue under the Water Industry Act 1991 (**the Act**) as amended by the Water Act 2014. Specifically, we are consulting on potential changes to the Charging Rules for New Connection Services (English Undertakers) (**English New Connection Rules**), from April 2025. These changes comprise:

- Changes to complement the new framework for developer services that we will implement as part of our price review 2024 (**PR24**).
- Changes to the way companies set infrastructure charges, including to support environmental incentives.

We are also consulting on draft wording for our charging rules. If we decide to proceed with any of the changes we propose in this document, we will consult again, as required by the Act.

There are separate developer services charging regimes for companies wholly or mainly in England (**English companies**) and companies wholly or mainly in Wales (**Welsh companies**). In this document we consult on issues relevant currently to English companies only.

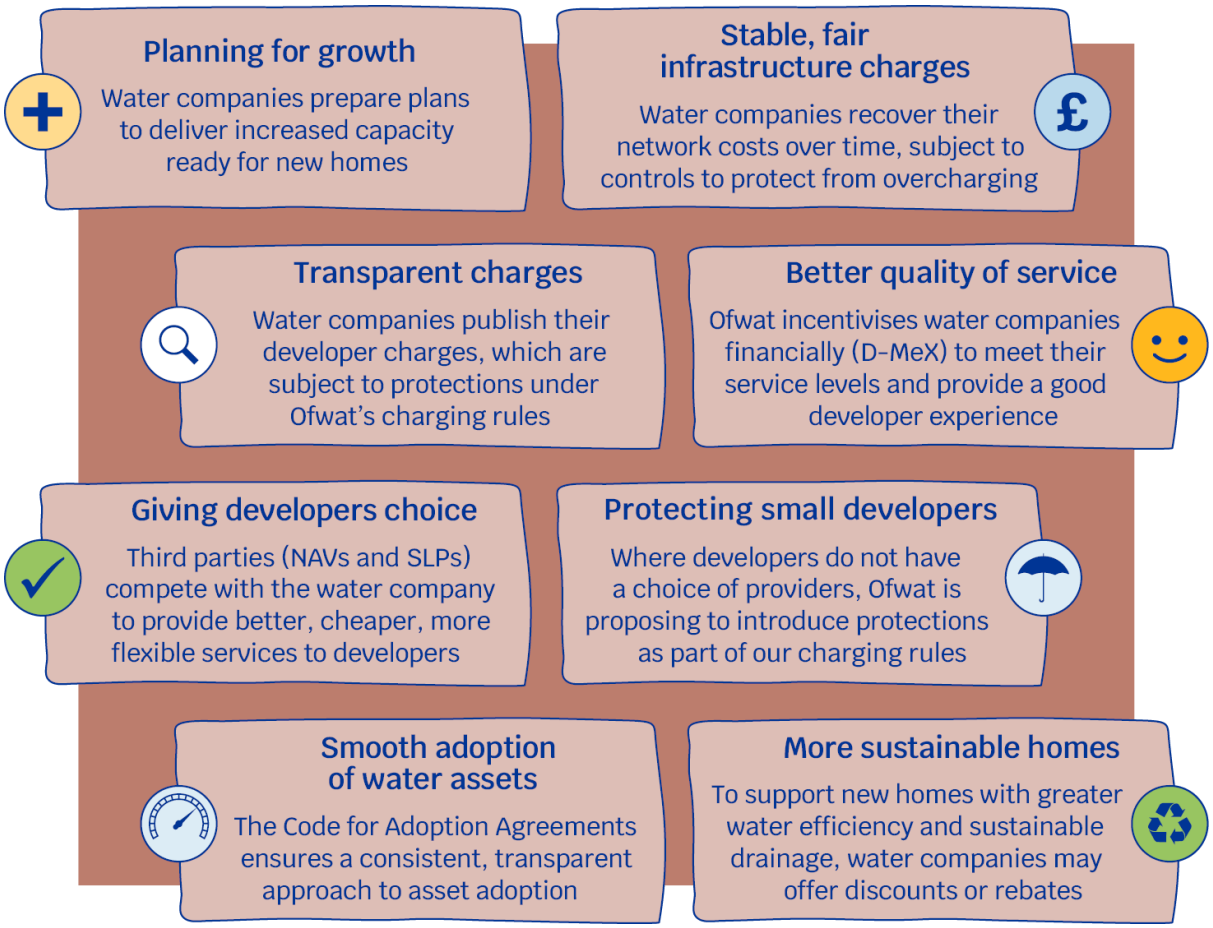
The rest of this document is structured as follows:

- In chapter 2 we set out the context for making the proposed changes.
- In chapter 3 we identify the options for changes to the charging rules, and enhancements to our regulatory reporting, to complement the PR24 framework.
- In chapter 4 we present other proposed changes to our charging rules.
- In Appendix 1 we set out drafts of the proposed amendments to our charging rules.

2. Context

In this chapter we explain our charging rules, our PR24 approach to developer services, and set out the rationale for the changes we are considering. This sits within the wider framework by which the water sector supports the supply of new homes, as outlined in Figure 1.

Figure 1: The water sector's framework for supporting the supply of new homes



2.1 Our charging rules

Ofwat issues rules for how companies should set and present their charges. Our power to do so is set out in the following sections of the Act:

- **English New Connection Rules** (**ENCR**) are issued under sections 51CD, 105ZF and 144ZA and apply to the provision of new connections and related services.

- **Wholesale Charging Rules** (**WCR**) are issued under sections 66E and 117I and apply to wholesale charges (for English and Welsh companies) and wholesale connection charges (for English companies).
- **Charges Scheme Rules** (**CSR**) are issued under sections 143(6A) and 143B, and apply mainly to household services. However, infrastructure charges, which companies apply in relation to new connection services, are also issued as part of the Charges Scheme Rules, because of the way the Act confers powers on companies to charge for their functions.

We updated the CSR with effect from April 2023 to explicitly allow companies to implement charging trials and to require companies to reflect general charging principles when setting charges.

We updated the ENCR and WCR with effect from April 2022, to simplify our rules, removing duplication and adding clarity. We also published a new Common Terms and Worked Examples (**CTWE**) document and introduced a requirement on companies to use standardised terms in their charging arrangements for developer services and publish worked examples that show the charges that would be incurred under six different scenarios[1] as set out in the CTWE. These worked examples help simplify and clarify the detailed array of charges for different activities that comprise developer services. They also promote greater consistency between companies in how they present their developer charges and communicate with customers.

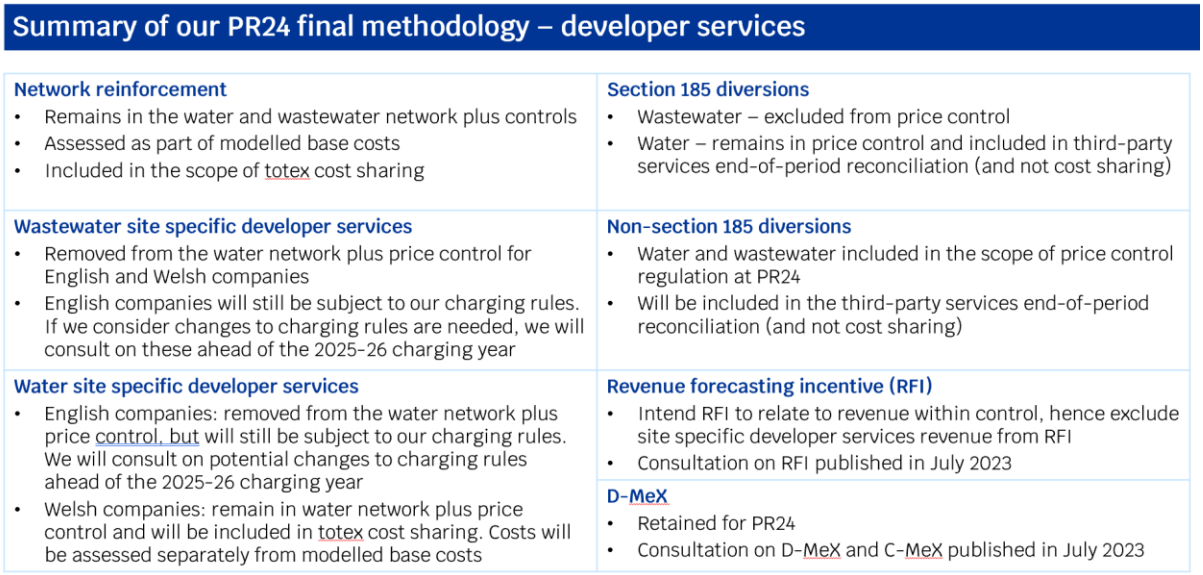
2.2 PR24 changes to the developer services framework

We published our final methodology for the price review 2024 (**PR24**) in December 2022. In this, we confirmed the changes we are making to how we regulate developer services.[2] We summarise the new framework in Figure 2.

We are making these changes to facilitate the development of competition in the developer services market. This includes removing regulation where it is no longer required and focusing regulation in areas where it will provide most benefits to developer services customers.

[1] The scenarios are explained in our Common Terms and Worked Examples document, and published by the English companies in their Charging Arrangements. They represent the typical activities for a single connection, a small development (10 properties in a block of flats), a medium size development (50 properties) and a large development (200 properties). For both the medium and large size developments there are two scenarios, one with excavation done by the company, and one with it done by others.
[2] PR24 Final Methodology – Appendix 3 Developer services - Ofwat.

Figure 2: Summary of PR24 framework for developer services



Source: Ofwat PR24 Final Methodology – Appendix 3, Developer Services

The main change we have made is the removal of site-specific developer services from the water network plus price control for English companies (except diversions under section 185 of the Act), and from the wastewater network plus price control for English and Welsh companies. Site-specific services include making new connections, providing water mains and sewers, and diversions under section 185 of the Act. Site-specific work is mostly contestable and can be provided by the incumbent, a new appointee, or a self-lay provider (**SLP**). SLPs and new appointees may provide faster, more responsive services and lower prices than incumbents. They can also sometimes provide developer services across utilities, reducing coordination issues.[3]

By making this change we can reduce the risk of cost cross-subsidy with household customers and subsequent market distortions and remove the need for complex cost assessment and reconciliation mechanisms.

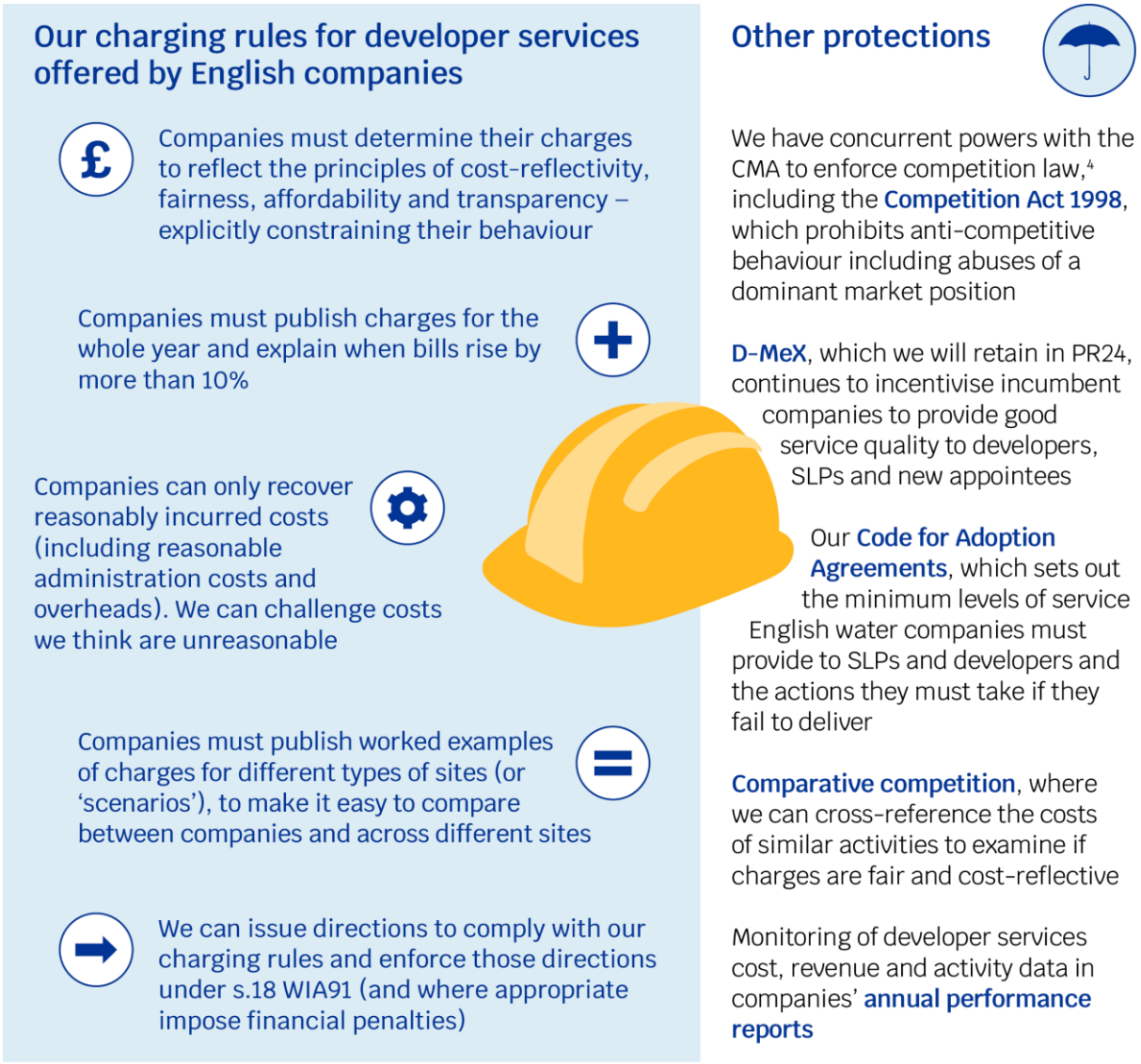
2.3 Existing protection for developer services customers

Customers with limited market choice, as well as SLPs and new appointees for whom incumbents provide some services (such as checking designs and processing applications), will not be wholly unprotected once developer services are removed from the price control. Our current charging rules will still apply to developer services

[3] Ofwat, Review of incumbent company support for effective markets, August 2020, pp. 30-31.

offered by English companies and there are other protections that sit alongside our charging rules. We summarise these in Figure 3.

Figure 3: Existing protections for developer services customers



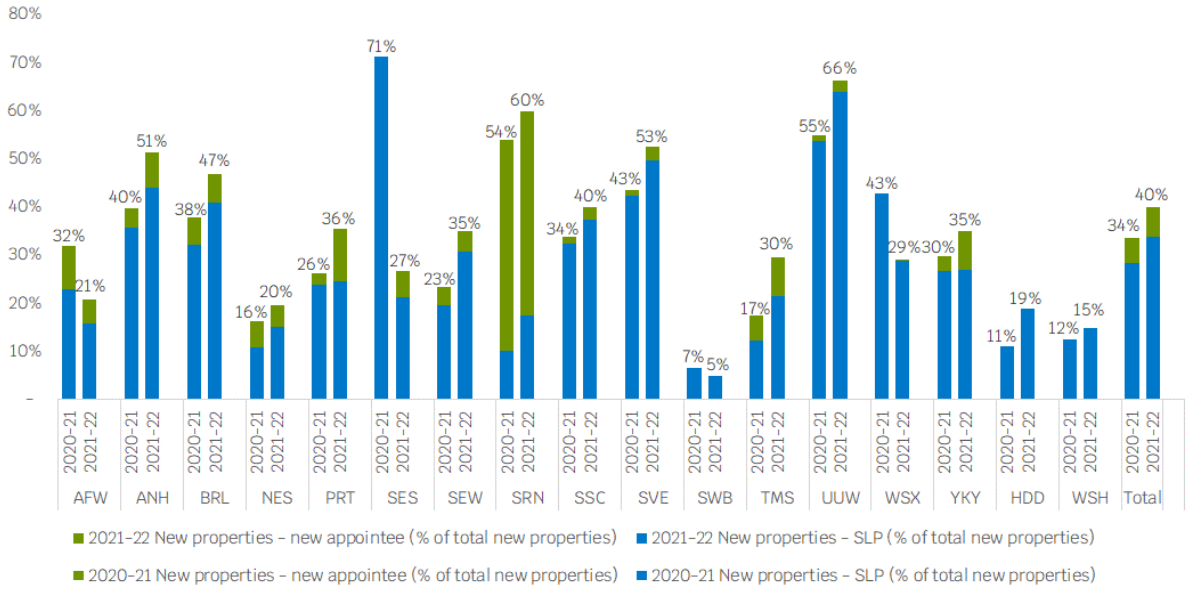
2.4 Why propose additional protection?

We explained in our Final Methodology that competition in the provision of developer services is prevalent in some companies' areas and for certain types of development

[4] In relation to commercial activities connected with the supply of water or provision of sewerage services, under section 31 WIA91.

but is not present everywhere. Figure 4 shows the extent to which SLPs and new appointees compete with incumbents to make new connections.

Figure 4: Properties connected by SLPs and new appointees 2020-21 to 2021-22 (% of total new properties connected)



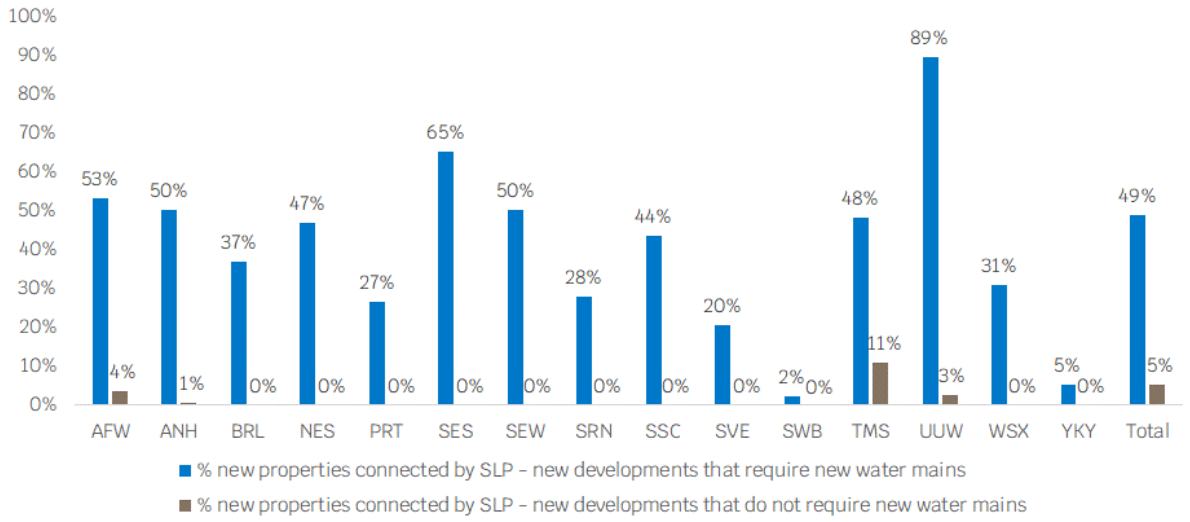
Source: Ofwat analysis of annual performance report data in 2020-21 and 2021-22.

We recognise that competition is not widespread across all segments of the market. In 2021-22, around 160,000 new properties were connected to the water network.[5] Around 50% of these new properties were on development sites that did not require new water mains.

- There are relatively high levels of competition for development sites that require new water mains (see Figure 5). SLPs connected almost half of all new properties connected to the water network on development sites that required new water mains in 2021-22. Developer services customers' needs and interests will be protected by competition, charging rules and competition law. We do not intend to introduce additional protections for this market segment.
- But the level of competition remains low for development sites that do not require new water mains (see Figure 5). For example, on these sites, only 5% of new properties were connected to the water network by SLPs in 2021-22.

[5] Based on Ofwat analysis of granular 2021-22 developer services data (financially closed new developments). Financially closed new developments are where no further site-specific developer services work is expected on the development site, and all invoices for the services provided have been paid.

Figure 5: Percentage of new properties connected by SLPs in 2021-22 (financially closed new developments)



Source: Ofwat analysis of granular 2021-22 developer services data (financially closed new developments)

With site-specific developer services removed from the price control, companies no longer have the constraint that they do not benefit financially by overcharging developers, SLPs and new appointees. We said in the Final Methodology that it would not be appropriate to exclude all water site-specific developer services from the price control without introducing alternative regulatory protections for market segments that currently have low levels of competition. We also said that additional protection could include limits on increases in published charges through our charging rules to sit alongside the requirement for both published and bespoke charges to be cost reflective.[6]

Our approach to the provision of additional protection for customers is consistent with our rationale for removing site-specific developer services from the price control. It balances our desire to remove regulation where it is no longer needed, reducing cross-subsidy and market distortions, with the need to guard against abuses of market power. We want to avoid constricting the growth of the developer services market while affording protection to those market segments (and market participants, including SLPs and new appointees) where market choice is currently limited. We envisage these additional protections would act like a safety net, supplementing rather than replacing existing protections. We outline the options for additional protection in chapter 3.

[6] PR24 Final Methodology – Appendix 3 Developer services - Ofwat, page 12.

2.5 Environmental incentives

In our June consultation on environmental incentives[7] we included proposals to enable companies to recover revenue from developers via a new component of the infrastructure charge. This will allow water companies to fund environmental incentives. We also proposed to introduce guidance, issued under the charging rules, to provide common terms and conditions and promote consistency across companies in terms of technical standards or methodologies.

That consultation closed on 1 August and we continue to review all responses. We raise potential changes to our rules in this document for completeness, so we can present the full suite of rule changes we are considering, but any changes we might make to our rules will be subject to our consideration of responses. We set out our proposals in chapter 4 and draft wording in Appendix 1.

2.6 Other support for the developer services framework

As the developer services market grows, both we and companies can deepen our understanding of the interaction between our charging rules and their provision of developer services. We use insights from our wider work, as well as feedback from companies and other stakeholders on this interaction, to consider how we might improve our charging rules to reflect the maturing market.

In this consultation we propose changes to our existing charging rules to improve the ongoing operation of the developer services market, through the way companies set infrastructure charges and manage variances between forecast and actual costs and revenues. We set out the proposals in chapter 4.

[7] Consultation on environmental incentives to support sustainable new homes – Ofwat.

3. Complementing the PR24 approach – options

In this chapter we look at how we might provide additional protection for those developer services customers that do not have a real alternative to the incumbent water company for providing developer services. We particularly focus on those customers that do not require new water mains. We set out options for protecting these customers as well as options for supporting the market, which will benefit all customers. We describe how we assess the options, before proposing a way forward. We also explain what further measures we might take in due course if our approach for protecting customers proves to be insufficient.

3.1 Options for additional protection

In our PR24 Draft Methodology we suggested that additional protection could be a restriction on companies to increase developer charges [only] in line with the consumer prices index including housing costs (CPIH).[8] Eight respondents commented specifically on this suggestion.

- Yorkshire Water suggested setting a maximum net margin for new connections-related revenues for smaller developments.
- Wessex Water, Northumbrian Water, United Utilities, South East Water, Yorkshire Water and Welsh Water opposed a CPIH-based cap on increases because charges could become non-cost reflective.
- Affinity Water was cautious but not opposed to using CPIH.
- South Staffs Water suggested a price cap for different types of site-specific charges and supported the use of CPIH.
- United Utilities suggested tying prices for small developments to those for larger developments.

We have considered these responses carefully, along with other potential options that could protect customers for whom market choice is limited, and which we would implement via changes to our charging rules. These options are summarised below.

- Option 1 – Capping developer charges.
- Option 2 – Capping increases in developer charges to CPIH.
- Option 3 – Capping net margin for revenue related to new connections on small developments.

[8] PR24 Final Methodology – Appendix 3 Developer services - Ofwat, page 3.

- Option 4 - Requiring companies to tether charges for typically uncontested sites to those of typically contested sites.
- Option 5 – Requiring companies to unbundle charges for activities involved in service connections.
- Option 6 – Introducing two new scenarios for which companies will publish worked examples.

3.2 Options to support the wider developer services market

We said in our PR24 Final Methodology that we plan to develop more detailed cost allocation guidance ahead of the 2025-26 charging year on how companies should allocate costs between developments that require new mains and developments that do not require new mains.[9] We identify this as option 7, below.

We also said companies will continue to provide us with cost and revenue data and we will consider how best to target those data requests to maximise our understanding of the market while minimising burden on companies. We will use the information submitted by companies, and our engagement with the wider stakeholder base, to monitor the development of the market. We are keen to observe how developers, SLPs and new appointees respond to our deregulation of certain aspects of developer services and we will take careful interest in how companies play their part in supporting competition. We summarise these activities as option 8, below, which we see as being complementary to the other options we have identified.

- Option 7 - Provide enhanced guidance via our Regulatory Accounting Guidelines (**RAGs**) on how to allocate costs to developer services.
- Option 8 - Carry out a market review prior to PR29, in which companies will demonstrate how they support the developer services market.

3.3 Framework for assessing the options

We set out the framework we have used to identify and assess the options for additional protection in Figure 6. It builds on the framework we used in our PR24 Draft Methodology to assess the options for our approach to deregulating some aspects of

[9] PR24 Final Methodology – Appendix 3 Developer services - Ofwat, page 12.

the provision of developer services. It is also consistent with the UK Government's Strategic Policy Statement (**SPS**) which includes expectations for Ofwat to:

- promote greater collaboration between incumbents and their new connections customers, particularly on large-scale developments;
- improve fairness and transparency in incumbents' charging arrangements and further promote sustainability and environmental protections; and
- consider how its regulatory framework can enable water and wastewater services to support government's ambitions to increase housing supply, in line with our duty to contribute to the achievement of sustainable development.

Figure 6: Developer services option assessment framework

1. Protects customers
• Reduces likelihood of monopoly pricing • Facilitates transparent, stable and predictable developer charges
2. Facilitates competition
• Promotes open market and reduces barriers to entry • Encourages cost reflective charging between different types of development
3. Regulatory simplicity
• Simple design, easily understood • Proportionate and targeted
4. Regulatory burden
• Easy to implement and operate • Facilitates third party scrutiny

3.4 Option assessment

It is important that any option to protect customers complements the existing framework (explained in chapter 2) but also supports the developer services market and allows companies to retain ownership of their charges.

We consider **option 1 (capping charges)** would be a be a retrograde step. We no longer approve charges, and this option would mean we would have to assess the appropriate level of charges, in effect approving charges and undermining our principles-based charging rules. We would not know what the right charge should be for each activity provided by each company, and capping prices would remove companies' responsibility to do so. It would be a heavy administrative burden on us.

We acknowledge the concerns raised by some companies with **option 2 (capping increases to CPIH)**. We would need to ensure companies could recover efficient costs, which might require some 'get-out' clause if material costs occurred that would otherwise mean companies would breach the limit on charge increases. This option would also risk charges diverging from costs over time, with the requirement for some sort of periodic reset of charges to the correct cost-reflective level. It would be not be a straightforward option for us or for companies to design and implement.

Option 3 (capping net margins) could be either a straight cost pass-through (zero margin) or cost-plus pass-through (positive margin). It would likely require detailed cost information and it would not directly limit price increases or encourage cost-efficiency. It may also encourage companies to re-allocate costs from the contested to uncontested market.

Under **option 4 (tethering charges)** we would seek to harness the power of competition for typically contested sites and apply it to typically uncontested sites, in order to constrain increases in charges. This option would be simpler to implement than other options and would allow companies to recover costs. It would not preclude increases in charges but it would encourage companies to limit such increases or risk losing market share at contested sites.

Options 5 and 6 are different to options 1 to 4, in that they do not seek to directly limit the charges or increases in charges. **Option 5 (unbundling charges)** would promote greater transparency of charges, enabling greater scrutiny of charges by interested stakeholders, particularly those on small developments for whom service connections comprise the majority of the total charge. Bo so doing this option would help to deter companies from re-allocating costs between contested and uncontested sites. **Option 6 (new worked examples)** would see a wider range of worked examples representing typically uncontested sites, enabling those customers to compare their actual charges with those from a typical scenario. This option would also provide a richer data set to support monitoring of the market and would be relatively straightforward to implement.

We said in our PR24 Final Methodology that we would carry out **option 7 (additional cost allocation guidance)**. We say more on this in section 3.5.4.

In our view, **option 8 (market review exercise)** will provide us and the wider sector with a useful assessment of how our deregulation of certain aspects of the developer services market is working. It will also enable us to form a judgement about the effectiveness of competition as a constraint on incumbents' market power.

3.5 Proposed way forward

We propose a combination of price protection and additional regulatory reporting and scrutiny. Our proposed options are summarised as follows.

- Option 4 - Require companies to tether charges for typically uncontested sites to those of typically contested sites.
- Option 5 - Increase transparency through a requirement to further unbundle charges for activities involved in service connections.
- Option 6 – Introduce two new scenarios for which companies will publish worked examples, to offer additional assurance to developer customers at sites not represented by existing scenarios.
- Option 7 - Provide enhanced guidance via our Regulatory Accounting Guidelines (**RAGs**) on how to allocate costs to developer services.
- Option 8 - Carry out a market review prior to PR29, in which companies will demonstrate how they support the developer services market.

We provide more detail on each of these options below.

3.5.1 Option 4 - Tethering charges

Our charging rules are principles-based, creating a framework in which companies have flexibility to innovate in how they calculate and present their charges and offer better customer services. We do not want to constrain this flexibility unduly.

Under this option, we propose to protect developer customers who do not directly benefit from competition by tethering their charges to the charges for the customers that benefit from competition.

We would aim to achieve this by employing maximum unit cost ratios, based on the worked example scenarios presented by companies for scenarios 1, 2, 4 and 6.

- Scenario 1 – single connection
- Scenario 2 – 10 connections, small development, block of flats
- Scenario 4 – 50 connections, medium development, excavation by company
- Scenario 6 – 200 connections, large development, excavation by company

We propose to tether charges as follows:

- Divide the total costs for developer customers for each scenario by the number of properties to provide a **unit cost per connection** for each scenario (Table 2).

- Compare the unit costs for scenarios 4 and 6 against the unit cost for scenarios 1 and 2, which gives a **tether ratio** (Table 3).
- Introduce a charging rule that requires **the tether ratios not to exceed certain levels.**

Table 2 - Unit costs per connection for companies, 2023-24, £

Company	Scenario 1	Scenario 2	Scenario 4	Scenario 6
Anglian Water	3,075	1,145	2,292	1,986
Northumbrian Water	2,505	911	1,578	1,402
Northumbrian (Essex)	2,081	873	1,825	1,585
Severn Trent	3,531	1,314	1,920	1,571
Southern Water	2,041	1,200	3,410	2,643
South West Water	3,510	1,328	4,558	3,697
Thames Water	6,760	1,783	4,398	3,793
United Utilities	1,721	618	1,798	1,533
Wessex Water	3,804	1,909	3,775	3,387
Yorkshire Water	3,471	903	1,868	1,608
Affinity Water	3,613	1,010	2,604	2,252
Bristol Water	1,908	731	2,442	2,049
Portsmouth Water	1,985	647	1,677	1,468
South East Water	2,709	1,124	1,979	1,737
South Staffs Water	2,026	964	1,524	1,223
SES Water	1,644	1,131	2,273	1,899
English companies Average	2,899	1,099	2,495	2,114
Minimum	1,644	618	1,524	1,223
Maximum	6,760	1,909	4,558	3,793
Median	2,607	1,067	2,216	1,818

Source: Ofwat analysis of companies' 2023-24 charging arrangements

We have removed income offset from the total charges in companies' worked examples, to ensure a more valid cross-comparison of unit costs. Only some companies currently offer income offset, and from April 2025 companies will not be able to offer income offset for any new agreements.

We do not propose a tether ratio specifically for charges for SLPs and new appointees. Incumbents provide fewer services to them than to developers, and we would ordinarily expect the charges to be the same irrespective of whom they apply to. It seems relatively straightforward for SLPs and new appointees to be able to monitor these

charges and challenge any significant differences between charges to them and other customers. (See also option 5 regarding unbundling of charges.)

Table 3 – Tether ratio for English companies, 2023-24.

Company	Scenario 1 to scenario 4	Scenario 1 to scenario 6	Scenario 2 to scenario 4	Scenario 2 to scenario 6
Anglian Water	1.3	1.5	0.5	0.6
Northumbrian Water	1.6	1.8	0.6	0.7
Northumbrian (Essex)	1.1	1.3	0.5	0.6
Severn Trent Water	1.8	2.2	0.7	0.8
Southern Water	0.6	0.8	0.4	0.5
South West Water	0.8	0.9	0.3	0.4
Thames Water	1.5	1.8	0.4	0.5
United Utilities	1.0	1.1	0.3	0.4
Wessex Water	1.0	1.1	0.5	0.6
Yorkshire Water	1.9	2.2	0.5	0.6
Affinity Water	1.4	1.6	0.4	0.4
Bristol Water	0.8	0.9	0.3	0.4
Portsmouth Water	1.2	1.4	0.4	0.4
South East Water	1.4	1.6	0.6	0.6
South Staffs Water	1.3	1.7	0.6	0.8
SES Water	0.7	0.9	0.5	0.6
English companies Average	1.2	1.4	0.5	0.5
Minimum	0.6	0.8	0.3	0.4
Maximum	1.9	2.2	0.7	0.8
Median	1.3	1.5	0.5	0.6

Source: Ofwat analysis of companies' 2023-24 charging arrangements

We summarise our proposed approach below and in Figure 7. We propose:

- To set four maximum tether ratios which companies must ensure their charges comply with. This ensures developments represented by scenarios 1 and 2 are both protected.
- For a single set of ratios to apply to all companies, rather than setting individual ratios for each company. This is more easily monitored by developers and other interested stakeholders.
- To set tether ratios based on industry maximums, rather than average or median figures. We are not looking to use this approach as an 'efficiency challenge',

requiring those companies with above average tether ratios to reduce their charges. Instead, we see this as additional protection, allowing companies to retain ownership of their charges and have flexibility to set charges that reflect their own costs.

- For those companies who have tether ratios below the maximum tether ratios, we would not expect to see ratios rise quickly to meet the maximums, and companies would need to explain to us any substantial changes in ratios.

Figure 7: Illustration of maximum tether ratios

	To Scenario 4	To Scenario 6
Ratio of Scenario 1	1.9	2.2
Ratio of Scenario 2	0.7	0.8

With this approach, companies would still be able to set individual charges for each activity within the provision of developer services and change those charges from year to year maintain cost-reflectivity. But the overall constraint would help give customers confidence that charges for all types of development were appropriate. This approach has some similarities to that outlined in rule 14 of the Charges Scheme Rules, which links metered and unmetered charges.[10]

Q1) What are your views on our proposal to link charges for different types of development through the use of tether ratios? What are your thoughts on the use of ratios based on industry maximum figures, not average or median figures?

3.5.2 Option 5 – Further unbundling of charges

There are lots of activities involved in the provision of site-specific developer services, including:

- those needed to make **service connections** (such as installing meters, boundary boxes and service pipes, laying additional pipework, traffic management, excavation and reinstatement, and design and administration); and
- those involved in **laying mains** (including laying mains, chlorination, washouts and sampling, trial holes and additional valves).

[10] "Charges for services provided to domestic premises must be fixed so that the average difference between metered charges and unmetered charges only reflects any differences in the costs of, and the additional benefits of, the provision of one service relative to the other."

In the Common Terms and Worked Examples (**CTWE**) document published by Ofwat, the template for each scenario itemises each different activity that companies can charge for. It also requires companies to include all relevant charges when presenting worked examples, where they are not included in the connection charges. Our analysis of companies' charging arrangements shows that almost all of them bundle some of the charges together, such as administration, application and design fees, the cost of meters and boundary boxes, charges for traffic management, labour and other materials. For example, Figure 8 shows that for scenario 1, most companies bundle some charges, to varying degrees.[11]

Figure 8: Bundling of company charges for scenario 1 of worked examples

	Pre-construction Charges			Construction Charges			
	Application Fee	Admin Fee	Design Fee	Connection fee*	Pipework - Road	Traffic Management	Meters
Unit	£	£	£	Per connection	Per metre	Per TM usage	Per connection
Company							
Anglian Water							
Northumbrian Water							
Northumbrian Water - Essex							
Severn Trent							
South West Water							
Southern Water							
Thames Water							
United Utilities Water							
Wessex Water							
Yorkshire Water							
Affinity Water							
Bristol Water							
Portsmouth Water							
South East Water							
South Staffs Water							
Sutton & East Surrey							
Key: Yellow = bundled charge	**Red = Charge not included**					*including assumed pipework allowance	

Source: Ofwat analysis of companies' 2023-24 charging arrangements

Although companies are required to set charges that are cost-reflective for every activity, bundling makes it more difficult for us and other stakeholders to monitor the

[11] All companies include a minimum amount of pipework in the connection charge.

different charges being applied to activities on contested and uncontested sites, and for charges to SLPs and new appointees.

Companies may find it convenient to bundle charges for some activities. They may find it easier to present bundled charges to customers. However, bundling means there is less transparency about the costs of each activity and whether charges are properly cost reflective. In turn this can make it more difficult to scrutinise the charges for SLPs and new appointees: it is important that these charges are fair to support the developer services market, thereby giving developers a choice of suppliers. In addition, the costs for bundled activities on smaller, uncontested sites and compare with charges for the same or similar activities at larger sites where competition is stronger.

Under this option **companies would publish charges for the separate activities involved in making service connections** and itemise these in the worked example templates provided in the CTWE. We would implement this by amending this paragraph on page 11 of the CTWE, under the section "Guidance for Water Companies", removing the text highlighted in strikethrough.

"For all scenarios, when presenting worked examples:

- Assume typical soil type for your region, that there is no rock and the land is not contaminated.
- Include all charges for activities and materials expected in an average job in the surface type being used
- Include all relevant ancillary charges, such as (but not limited to) application and design fees, any other administrative fees charged to developer customers for delivering the service, and meter costs and installation ~~(where not included in the Connection Charges)~~."

Q2) What are your views on option 5 that companies should publish individual charges for separate activities involved in making service connections? Do you agree with our proposal to implement via changes to the wording of the CTWE?

3.5.3 Option 6 – Introducing new worked example scenarios

Currently, companies are required to publish worked examples for six different scenarios. These scenarios differ in terms of the number of connections to be made, whether the site requires new mains, and whether the company or a third party carries out the excavation and reinstatement. Although they have only been in effect since April 2022, they provide a useful benchmark for comparing the cost of carrying out certain connection scenarios.

With site-specific developer services removed from the price control, and customers with limited market choice potentially at risk from overcharging, we are considering revising the CTWE document to show worked examples of more scenarios, or different scenarios, which could help mitigate against this.

In our PR24 final methodology, we concluded that we would consider additional protection for customers at sites that did not require new mains as competition is limited. However, only two of the six scenarios involve sites where new mains are not required. **We propose to introduce two new worked example scenarios.** We seek views on what typical scenarios for developments with limited market choice would be. For example:

- a housing development of 5 properties that does not require new mains.
- a housing development of 25 properties that does not require new mains.

Having two new scenarios will ensure the worked examples cover a broader range of developer services customers with limited market choice. Our analysis shows that the majority of development sites that do not require new mains connect 25 properties or fewer. The new scenarios would give those customers more confidence about the charges they could face and provide us with more evidence of the charges that companies levy for customers facing limited market choice.

We do not consider the addition of new worked examples would significantly increase regulatory burden for companies, as they would be similar to existing examples for which the template is already established. Also, with the removal of site-specific services from the price controls from April 2025, we do not think this is the right time to remove any worked examples. Instead, we would use the data provided by the publication of worked examples since April 2022 as part of our evidence base to support our market review, which we discuss in more detail in section 3.5.5.

If we proceed with our proposal to introduce two new worked example scenarios, they will not be within the scope of option 4 (tethered charges). However, we may bring them within scope at a later date if we consider it necessary to do so to protect those customers.

Q3) Do you have views on our proposals to add two new worked examples with the aim of providing additional protection for developments with limited choice? What are your views on suitable new scenarios?

3.5.4 Option 7 – Enhanced cost allocation guidance

It is important that companies allocate overheads and other costs correctly between site-specific developer services (outside the revenue control) and network reinforcement (within the revenue control), as well as to different activities within developer services.

The findings from the SIA Partners study[12] show that companies take very different approaches to cost allocation. This leads to differences in companies' charges for developer services and makes it challenging to compare charges between companies. SIA Partners reported the following:

- The significant variation in charges for developer services may in part be due to an inconsistent definition of overheads across the companies, as well as different interpretations of the elements of costs that it is reasonable to recover, with some companies not recovering costs such as central overheads. Most companies include some form of central overhead covering office space, IT, and back-office support functions such as finance. Costs for administration and design contribute to the provision of service but are to an extent fixed regardless of output. Some companies define and report these as overheads whilst others keep them as separate direct costs and there is significant overlap between them.
- There was significant variation in how companies reported overheads in the quantitative analysis. We found that five companies did not have any separate overheads, instead including them in construction rates. Despite all 15 companies using external contractors to some degree, only five companies had separately identifiable contractor overhead costs. One company had separate overheads related to the storing of materials. One company told us that they reported overhead costs as a balancing item in the RFI, applying them as a final step in the calculation to make up the difference with charges.
- Each company uses a different methodology for applying overheads. For example, some companies apply a flat fee to service connection costs, but others apply a percentage uplift. Some companies have a complex structure of direct and indirect overheads applied differently to different cost elements, which is not simple to breakdown and understand.

To mitigate this, we could:

- prescribe one or more approaches that companies must use to recover overheads;

[12] SIA Partners Connection Charges Analysis – Final Report - Ofwat.

- or leave companies to decide their own approach but require them to demonstrate that their recovery of overheads is cost reflective.

Companies will be required to give us more data on costs and revenues as part of our PR24 framework for developer services.

In the APR we currently specify the following tables focused on developer services:

- 2E – developer services revenues
- 4N – developer services water totex
- 4O – developer services wastewater totex
- 4P – non-price control diversions totex

In the PR24 business plans we require the following tables.

- DS1 – developer services revenues (England and Wales)
- DS2 – developer services water totex (England and Wales)
- DS3 – developer services wastewater totex
- DS4 – new connections, properties, mains
- DS5 – Network reinforcement costs
- DS6 – Network reinforcement cost drivers

Our final version of PR24 business plan tables includes a revised DS1e to support our new framework for developer services.

- We have changed the terminology from “grants and contributions” to “developer services revenue”.
- We removed the water resources section, as most companies report zero in these lines of the APR.
- Revenue included in the scope of price control regulation should be captured in lines DS1e.1 to DS1e.9 (water) and DS1e.15 to DS1e.19 (wastewater).
- Revenue outside of the scope of price control regulation should be captured in lines DS1e.10 to DS1e.12 (water) and DS1e.20 to DS1e.22 (wastewater)
- We have included additional lines to enable companies to report revenue and expenditure associated with environmental incentives.

Our current regulatory accounting guidelines (**RAG**)[13] do not specify in detail how companies should allocate and recover overheads for developer services.

[13] Guideline for the table definitions in the annual performance report - Ofwat and RAG 2.09 – Guideline for classification of costs across the price controls - Ofwat.

Reflecting on the SIA Partners findings, we are satisfied that in general companies are including overhead costs for developer services activities. For those instances highlighted by SIA Partners**, we propose to add a general principle to RAG2** that would ensure that central and departmental overheads should be added to all capital programme activities (that is base, enhancement and developer services) in a fair manner with no discrimination according to the investment area.

SIA Partners also observed the greatest variation in overhead costs to be for the larger development scenario. This is in part due to the overhead allocation being based on a percentage uplift. There were also differences due to whether activities were delivered in-house or by using contractors.

Most companies would be used to dealing with contractor financial arrangements as part of their general maintenance and enhancement activities and that they would incur contractor overheads costs even if they are not as transparent as the companies own costs would be. That said it could be beneficial to have prescribed methods of overhead allocation for developer services activities in order to gain consistency across the industry and to create a possible solution for future extended disaggregation (see below). This could include, say a requirement to use a flat rate for all connections, or perhaps a blended application of allocation to each development and to each connection.

Q4) Do you agree with our proposed general guidance for RAG2 regarding a fair allocation of all relevant overheads across ALL expenditure areas, including developer services?

Q5) Should RAG2 specify methods of overhead recovery for developer services? Are there any disadvantages to doing so? Are there any methods that you think would be appropriate to use across the industry that would drive consistency?

RAG2 does not distinguish between developments that do and do not require new mains. We said in our PR24 final methodology that we plan to develop more detailed cost allocation guidance ahead of the 2025-26 charging year on how companies should allocate costs between developments that do and do not require new mains. We will consider what additional guidance we may provide to complement the new approach to developer services.

We will consider how to take that work forward separately. However, as part of this consultation, we seek initial views on the recovery of overheads and the allocation of costs between developments that do and do not require new mains.

Q6) Do you agree that RAG2 could be extended to cover the recovery and allocation of overhead costs between developments with and without a mains requirement? Do you have any suggestions as to how this should be done?

3.5.5 Option 8 – Market review

The developer services market is complex. In practice, currently we consider there is a set of regional markets, in which each of the companies competes with SLPs and new appointees to serve developer customers for contestable activities, while retaining a provider of last resort function and providing non-contestable services. In addition, some SLPs, new appointees and developer customers operate in more than one company's region, creating supra-regional markets.

We want to remove regulation where it is no longer needed, but we also need to ensure customers are protected where competition is unable to do so. We need to measure how companies and developer customers respond to our new approach, to judge the effectiveness of competition as a constraint on companies' use of market power. We want to understand how companies support developer customers and how developers, SLPs and new appointees view the market and the opportunities available to them to compete and procure cost-reflective services.

We propose to review the effectiveness of developer services market prior to PR29. We will engage with developer customers, new appointees, SLPs and companies about how they operate in the market, what opportunities they seek, what barriers they may face to success. We propose to look at sites that do and do not require new mains, and potentially other market segments. We propose to produce a report that sets out our findings and what we consider to be appropriate, proportionate and effective next steps.

We will consider separately the scope of that exercise, but we would welcome views in response to this document about what aspects of the market we could examine.

Q7) What are your views on our proposal to carry out a market review prior to PR29?

3.6 Possible further protections

We said in the PR24 Final Methodology that we will reconsider the effectiveness of competition as a constraint on incumbents' market power at PR29 if we observe

revenues exceeding costs over time.[14] We may also decide to introduce further measures to protect customers, before PR29. Options may include (but are not limited to) one or more of the following:

- An Ofgem-style 'competition test', requiring companies to demonstrate that effective competition exists in their areas.
- Referral to the CMA for a market investigation.
- Carrying out an investigation under the Competition Act 1998.

We may also decide to revisit whether options 2 and 3, explained earlier in section 3.1, would be worth implementing. If we were to pursue one or more of them, we would engage with companies and other stakeholders first. Therefore, we do not intend to go into further detail about these potential options in this document.

[14] PR24 Final Methodology – Appendix 3 Developer services - Ofwat, page 12.

4. Other proposed changes to our new connection charging rules

In this chapter we set out other changes we propose to make to our English New Connection Rules, to enable implementation of environmental incentives and to refine how companies set infrastructure charges, notably so that the calculation takes account of include historical variances between expenditure and revenue.

Our proposed changes are driven by external and internal feedback and experience and will improve the way companies set and present their charges, and consequently lead to better outcomes for customers. In the rest of this chapter we set out the rationale for each proposed change and in Appendix 1 we provide the detail of our draft wording of each rule change.

4.1 Supporting environmental incentives

We explained in chapter 2 our June consultation on environmental incentives proposal that each company will need to collect revenue from the developer of every site in its area in order that environmental incentives can be funded from within the developer community. We proposed in our consultation that the revenue for environmental incentives is collected as a new environmental component within the infrastructure charge, although we also considered that we could introduce a separate charge. We also proposed to introduce guidance, issued under our charging rules.

Subject to responses to that consultation and our subsequent decisions, we would implement our proposals by

- Introducing new rule 51, to require companies to offer environmental incentives in accordance with guidance issued by Ofwat.
- Amending rule 52 to include reference to the ability to account for previous under- or over-recovery of infrastructure charge revenue.
- Amending rule 53, to include reference to the environmental component.

We set out a draft of the proposed new rules in Appendix 1.

4.2 Taking account of historical variances in setting infrastructure charges

We refer to Rule 52 of our ENCR as "the 5-year rule". It states:

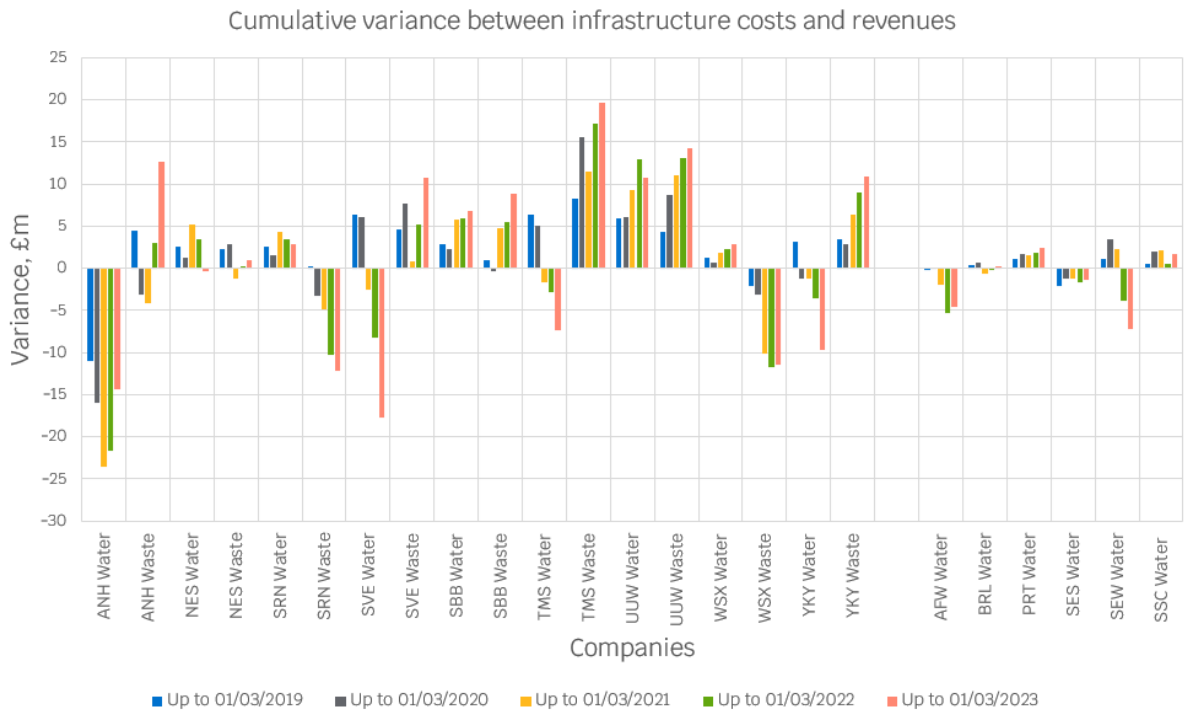
> "Infrastructure Charges must be determined in accordance with the principle that the amount of such charges will over each period of five consecutive Charging Years ending on 31 March 2023 and, thereafter, on 31 March in each subsequent year cover the costs of Network Reinforcement that the relevant undertaker reasonably incurs, less any other amounts that the relevant undertaker receives for Network Reinforcement, and before the application of any Income Offset."

In our charging rules consultation in June 2021 we noted our interpretation of the 5-year rule, given that it was issued for the first time in April 2018. We said companies should set their infrastructure charges each year on the basis of their forecast of likely costs and likely number of connections over the following five years (i.e., on a wholly forward-looking basis). We said setting infrastructure charges using both retrospective consideration of the variance between forecast and actual costs and revenues, as well as forecasts of likely costs and revenues, was not consistent with the 5-year rule.

In our subsequent consultation in August 2021, we recognised there was a mixed response to the details we provided. Some respondents supported our approach; others commented that they will review their approach in line with our clarification; and some expressed concerns, with different levels of severity. We concluded that there was a need for greater consideration of the issues raised, notably the balance between the desire for developers to have stable predictable charges and to have charges that reflect cost, as well as the interaction with annual reporting and with PR24. We said we would consider the issues further and revert to stakeholders in due course.

Figure 9 shows that all companies report variances between revenue they collect from developers and costs incurred in network reinforcement. Some variation is inevitable, given the bulky nature of investment and the time-lag between needing to incur costs and subsequently collecting revenue from infrastructure charges when properties are connected. For some companies, variance appears to be relatively stable over time, for others variance is growing (either negatively or positively) year on year. For several companies, variances are large, indicating significant under- or over-recovery of costs from developers. Under the current interpretation of the 5-year rule, companies have no way of balancing these variances through changes to infrastructure charges.

Figure 9: Cumulative variance between infrastructure costs and revenue



Source: Ofwat analysis of table 2K of companies' APRs.

We have listened to developers, companies and others about setting infrastructure charges. We have looked again at the issues raised by respondents to our consultations, as part of our process to revise how we regulate developer services, as well as the changes to our wider regulatory framework.

- Our October 2021 decision to disallow companies to offer income offset (a discount which has no convincing economic rationale).
- Our PR24 decision to remove the Developer Services Reconciliation Adjustment mechanism and the potential consequences if companies over- or under-recover network reinforcement revenue from developers.
- Our PR24 decision to remove site-specific developer services from the network plus price controls.
- Our decision that environmental incentives be self-funded by the developer community and the need to ensure companies are able to set charges that comply with our charging principles, including stability and predictability, as well as being able to manage any difference between forecast and actual revenue (see our June 2023 consultation on environmental incentives).
- The extent of variance reported by companies in Table 2K of their Annual Performance Reports (**APRs**).

Consequently, **we propose that companies set infrastructure charges taking account of historical variances between expenditure and revenue when setting infrastructure**

charges. We consider this would be more consistent with our revised developer services framework. We propose to implement this through changes to rule 52 of our ENCR, to include reference to historical imbalances. We set out a draft of the proposed amended rule in Appendix 1.

Q8) What are your views on our proposal that companies include historical variances between expenditure and revenues in setting infrastructure charges?

4.3 Setting infrastructure charges - upsizing

When we refer to 'upsizing' we mean the practice carried out by companies of installing more capacity than is immediately required to satisfy demand for new connections, in anticipation of needing to meet future demand. It is usually more cost effective to do this than to install additional capacity in the future, because the provision of upsized infrastructure typically results in a smaller cost per unit of capacity provided. Consequently, the customers that make the requisitions (now and in the future) are likely to pay less than if the upsizing was not undertaken.

Thames Water raised an issue with us that our definition of Network Reinforcement refers to "capacity in earlier mains or sewers" but the 5-year rule requires a forward forecast of "costs incurred". Thames Water said this would appear to prohibit taking into consideration "costs incurred" historically, which is what would happen with the installation of an upsized earlier main or sewer. Consequently, the costs of future capacity would not be recoverable from developers who would benefit from that upsized capacity.

We agree that rule 52 and the definition of network reinforcement are mutually inconsistent. **We propose to amend rule 52 to include reference to costs already reasonably incurred.** We set out a draft of the proposed amended rule in Appendix 1.

Q9) Do you agree with our proposal to enable companies to take account of upsized infrastructure when setting infrastructure charges?

4.4 Income offset and balance of charges

In our October 2021 decision we disallowed the ability for companies to offer income offset from April 2025 and signalled our intent to remove rule 19 of our ENCR that companies should maintain at pre-2018 levels the balance of charges that developers and other customers pay to cover the costs of new development.

In March 2023, South Staffs Water queried whether the disallowance of income offset applies to existing agreements as well as new agreements, given that some developments may take years to be fully built-out.

In our May 2023 guidance to companies on submitting PR24 business plan tables, we clarified that

- the ability to offer income offset for English water companies is removed from April 2025 onwards for new agreements; but
- we would not expect companies to enter into any new agreements in the remainder of AMP7 that would require them to make any payments in connection with income offset after April 2025.

This means we propose to make the following consequential changes to our ENCR.

- Remove rule 19, relating to the balance of charges.
- Amend rules 5, 52, 55 and 57 to refer to income offset only in connection with existing agreements.
- Amend rule A1 in Appendix 1, removing references to the balance of charges.

We set out a draft of the proposed amended rules in Appendix 1.

Q10) What are your views on our proposals relating to how we accommodate changes to the provision of income offset?

4.5 Where our existing charging rules are sufficient

In February 2022 and in its response to the PR24 Draft Methodology, Thames Water raised another issue with our definition of Network Reinforcement and how to recover the costs of upsizing.

> "We understand that the current definition of network reinforcement in the New Connections charging rules requires the incumbent water company to be able to link any network reinforcement spend specifically to a developer's application. This means that network reinforcement spend can only be applied to developer projects that are sufficiently mature (that is to say, they are sufficiently developed so that the Developer will have submitted an application for water connections). This does not allow for longer term planning with regards to Network Reinforcement. Specifically, it prevents the additional demand from future schemes, which are planned but with no live connection application to be considered in making Network Reinforcement investment decisions…Any large developments with long build outs (20+ years in some cases) will include "capacity ahead of need". This

> "investment ahead of need" cannot be treated as Network Reinforcement (and thereby funded through Infrastructure Charges), and must therefore be funded through Household and Non Household charges."

We clarified our view of Thames Water's interpretation of our charging rules in the PR24 Final Methodology.

> "We also note Thames Water's interpretation of the definition of network reinforcement in our charging rules. More specifically, Thames Water consider they can only record costs against network reinforcement if it can be linked to a developer's application. We consider Thames Water's interpretation is too narrow. Incumbent companies can set infrastructure charges to recover the costs of network reinforcement from all foreseeable developer applications. We will consider how companies should keep track and report the costs and revenues over successive regulatory periods ahead of the business plan table Phase 3 update scheduled for February 2023."

We do not consider any amendments to our charging rules are necessary to address this issue. And we have clarified in PR24 business plan table guidance that costs of network reinforcement from all foreseeable developer applications should be reported under infrastructure network reinforcement.[15]

[15] Ofwat, PR24 business plan table guidance part 8: Developer services, May 2023.

5. Next steps

The closing date for this consultation is 27 October 2023. Please email us at charging@ofwat.gov.uk with your response, or if you wish to discuss any aspect of this consultation, or to arrange a conversation on the issues we have raised.

We will consider all responses carefully and, if appropriate, prepare revisions to the rules upon which we will consult as required by the relevant sections of the Act in due course. Our aim is to issue revised rules in 2024, in good time for companies to implement them as they prepare charges and related documents for the 2025-26 charging year.

Appendix 1 Draft changes to our charging rules

In table 4 we set out the changes we are considering making to the charging rules, explained earlier in this document. In this table, ENCR means English New Connection Rules. We do not include the proposal to introduce two new scenarios (option 3) which we explain in section 3.5.3, as this would not require a change to our charging rules. Instead, we would work with the companies to agree a change to our CTWE document.

Text in red font is what we propose. Text in strikethrough font is current text which we propose to replace with red text.

Table 4: Changes we are considering making to our charging rules

Consultation Reference	Potential wording	ENCR Reference
Section 4.4	"Income Offset" means a sum of money, that may be offered by the Undertaker, against the Infrastructure Charges, in recognition of revenue likely to be received by the relevant undertaker in future years for the provision of: i. supplies of water to the premises connected to a Water Main; or ii. sewerage services to the premises connected to a Sewer, only under or in connection with any agreement entered into before 1 April 2025. "Income Offsetting" shall be construed accordingly.	Rule 5
Section 4.1	"**Environmental component**" means a sum of money charged by an undertaker to a developer for each water and / or wastewater service provided to a property connected to the undertaker's network for the first time, for the purpose of funding the undertaker's Environmental Incentives.	Rule 5
Section 4.1	"**Environmental Incentive**" means a payment or payments to a developer to promote water efficiency and sustainable drainage.	Rule 5
Section 3.5.1	"Tether ratio" means the ratio of unit costs calculated by reference to the total costs published by each undertaker for their worked examples, in accordance with the document entitled "Common Terms and	Rule 5

	Worked Examples – English New Connection Rules" published by Ofwat.	
Section 3.5.1	Undertakers must set requisition and connection charges in such a way that the Tether Ratio for each scenario in the worked examples published by them in accordance with the document entitled "Common Terms and Worked Examples – English New Connection Rules" published by Ofwat does not exceed the maximum Tether Ratios set by Ofwat and published in the same document.	Rule 18A
Section 4.4	Not used. ~~In setting charges in accordance with the present rules, undertakers should take reasonable steps to ensure that the balance between contributions to costs by Developers and other customers prior to 1 April 2018, is broadly maintained. Section 3 of Annex A to the Government's Charging Guidance to Ofwat published in January 2016 lists the charges under which Developers contribute costs relevant to this rule. For the avoidance of doubt, Income Offset also needs to be included. An undertaker may only depart from this general requirement where (and to the extent that) this is rendered necessary by circumstances providing clear objective justification for doing so. Any such justification must be clearly identified in any Charging Arrangements prepared pursuant to these rules.~~	Rule 19
Section 4.1	Infrastructure charges and Environmental Incentives ~~Income Offsetting~~ (English undertakers)	Heading before para 50
Section 4.1	~~Not used.~~ Each undertaker whose area is wholly or mainly in England must offer environmental incentives in their Charging Arrangements, using where appropriate the terms as defined at Rule 5 and those set out in the document published by Ofwat entitled "Guidance for Environmental Incentives – English New Connection Rules".	Rule 51
Section 4.3 Section 4.4	Infrastructure Charges must be determined in accordance with the following principle: • that the amount of such charges will over each period of five consecutive Charging Years beginning on 1 April 2025 ~~ending on 31 March 2023~~ and, thereafter, on 1 April~~31 March~~ in each subsequent year cover the costs of Network Reinforcement that the relevant undertaker reasonably incurs, (or has already reasonably	Rule 52

	incurred, in the case of additional capacity in any earlier Water Main or Sewer that will fall to be used in consequence of the provision or connection of a new Water Main or Sewer within the relevant 5-year period), before the application of any Income Offset and in calculating these costs the undertaker must: • take into consideration both the number and relevant costs arising in consequence of new connections in the undertaker's own area, and in the areas served by New Appointees with whom the undertaker has an agreement for bulk supplies of water or bulk discharge, less any other amounts that the relevant undertaker receives for Network Reinforcement; and • adjust for any under-recovery or over-recovery of infrastructure charge revenue in previous Charging Years which has not already been adjusted for in the calculation of any previous infrastructure charge.	
Section 4.1	Charging Arrangements must include a clear methodology explaining how Infrastructure Charges and the Environmental Component have been calculated.	Rule 53
Section 4.4	In setting Infrastructure Charges an undertaker must not provide for an Income Offset under or in connection with any agreement entered into from April 2025~~may (but is not required to) provide for an Income Offset. Each undertaker has discretion as to the methodology to be applied to calculate Income Offset~~.	Rule 55
Section 4.4	In making Charging Arrangements, each relevant undertaker must ensure that: …(d) the Charging Arrangements clearly explain the methodology to be applied for determining any Income Offset under or in connection with any agreement entered into before April 2025.	Rule 57
Section 4.4	ii. confirming that the company has appropriate systems and processes in place to make sure that the information contained in the Charging Arrangements, and the additional information covered by this annex is accurate~~; and iii. explaining how the present balance of charges between Developers and other customers is broadly maintained~~.	Annex Para A1

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

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