



Driscoll 2  
Ellen Street  
Cardiff, CF10 4BP  
Telephone: 02920 028 711  
Website: [iwnl.co.uk](http://iwnl.co.uk)

Charging Team  
Ofwat  
Centre City Tower  
7 Hill Street  
Birmingham  
B5 4UA

By email only to: [Charging@ofwat.gov.uk](mailto:Charging@ofwat.gov.uk)

27<sup>th</sup> October 2023

Dear Ofwat

**Re: Changing Ofwat's rules to support the new developer services framework**

I am writing to you on behalf of Independent Water Networks Limited ("IWNL"), part of the BUUK Infrastructure group of companies, in response to your consultation on changing Ofwat's rules to support the new developer services framework. IWNL welcomes the opportunity to respond to this consultation and this letter sets out a summary of our views on Ofwat's proposals. The BUUK group of companies also operates independent gas and electricity licensees and have built up extensive knowledge of working with developers to connect new utility networks over more than 25 years operating in those markets. We are keen to ensure that learnings from developments in the competitive frameworks for providing connections to utility networks are considered by Ofwat in developing these changes to support the new developer services framework. More specifically, as a NAV working closely with both developers and self-lay partners, IWNL has a keen interest in the outcomes of this consultation and are pleased to be able to provide Ofwat with our feedback in this area.

The development of competition and choice for customers is something which is exceptionally important for IWNL and the customers that we serve. In general we are supportive of the provisions that Ofwat are seeking to put in place to support the new developer services framework and we have provided detailed answers to Ofwat's questions in Annex 1 of this letter. However, there are some areas which we would like to highlight as having, in our view, particular importance to the development of the framework and the rules supporting the framework.

In order to meet government targets for housebuilding there will be a need for fast and agile connections to utility networks to be provided. It is imperative that changes to the developer services framework are congruent with this approach and that connections to water networks does not act as a blocker to the development of such homes. We think that there is a significant part to play for competition and the competitive provision of connections to new networks and we welcome the steps which Ofgem has taken in removing some of the developer services from the price control framework to recognise this development.

We think that it is important that Ofwat recognise that the provision of new water networks, in particular, the contestability of providing those networks is still developing and is likely to continue to develop. It is important that any changes which are put in place now do not do anything to inhibit or restrict this development. For example, the use of tether ratios may provide a simple and clear way to restrict increases in costs for sites which are not typically contested, but we are concerned that their blanket application may reduce the future contestability of those sites. We think that it is important for Ofwat to draw this distinction and to allow for agility and changes within the rules to take into account developments of this nature.

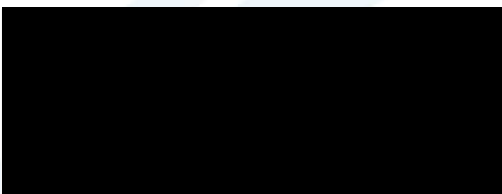
We believe that the competitive market review which Ofwat are referencing in this consultation is likely to play a key role in ensuring the development of the market in the interest of customers and we would urge Ofwat to consider a broad scope for this review to ensure that all areas which affect the contestability are captured. These areas are likely to be far wider than the scope of the connection charging rules.

IWNL have been engaging with Ofwat and water companies on the development of appropriate processes and content of NAV charges through Ofwat's Bulk-Supply Working Group. This work has largely failed to deliver the necessary changes and improvements required to support the NAV market and we recognise that this is, in part, because charges are outside of the price control. We are concerned that removing the developer services from the price control may have the unintended consequence that Ofwat do not have sufficient controls to enact necessary changes or interventions where it is required to ensure that the market operates as intended. The provision of water connections is an essential component for any development, and it is imperative that nothing within the way that this market operates inhibits the timely provision of connections and networks. We would welcome some assurance from Ofwat that they will retain the necessary controls to be able to act on issues and concerns that arise in the market quickly and decisively.

We have previously responded to Ofwat's consultation on the development of the environmental incentives, and we believe that more clarity is required on the outcomes from that consultation than has been provided in the development of the charging rules relating to income offset. We know that it is important for water networks to play a role in ensuring creating and retaining environmental value and in doing so water networks will need to work with developers. We would welcome this clarity being forthcoming from Ofwat so that we are able to work with our developer customers and ensure that they are prepared for changes to the way that they will be incentivised to develop homes.

Please find our detailed responses to Ofwat's decisions in the appendix of this letter and please do not hesitate to contact me should you wish to discuss our response.

Yours Sincerely



Keith Hutton  
**Group Regulation Director**

## **Appendix 1 – Answers to Ofwat Consultation Questions**

***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 the use of ratios based on industry maximum figures, not average or median figures?***

We are generally supportive of the proposal to link charges for different types of development insofar as it provides protection to customers where there is generally no competition. We do however believe that there should be scope for competition to develop in those areas. The use of tether ratios means that the total costs for providing connections to customers where there is generally no competition is constrained to the extent that it may mean that competition is unable to develop in those areas. We recognise that this is a broad, and relatively straight forward way to limit increase to costs faced by customers in those areas and we also understand that there is a need for this protection for customers. Ultimately, we believe that the development of competition in those areas is likely to provide the best protection to customers in the long run and we believe that this is more likely to be given the space to develop under Option 3 where a regulated margin would provide the headroom for competition to develop and to better serve connection customers.

We believe that using the industry maximum figures goes some way to mitigate this issue as it allows the most headroom in charges for typically uncontested sites and allowing water companies to retain ownership of how they set charges may also allow competition to develop.

***Q2. What are your views on options 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?***

We are supportive of Ofwat's proposal to unbundle charges and require companies to provide individual itemised charges and costs. We agree with Ofwat that this increases the transparency and ability to scrutinise the individual costs which we believe is in the wider interests of 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?***

We are supportive of the requirement to introduce two new specific worked example scenarios. Again, we believe that this is likely to increase transparency and the ability for customers to be able to understand that costs which they are likely to face in requesting a connection to the water network.

We do not have any specific comments on the worked examples which should be included.

***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?***

Yes, we agree with the proposed general guidance, as a minimum, regarding a fair allocation of overhead recovery for all areas. Given that some areas of developer services are not to be included in the water network plus price control it is important that overheads are fairly and reflectively allocated for these areas to ensure that the wider customer bases is not at risk of subsidising developer services whilst also ensuring that the overheads included in charges for developer services

are reflective and equally protect connecting customers and do not inhibit the development of competition in those areas.

If overheads are incorrectly allocated, then there is the real risk that they are allocated within the price control and so the wider customer base is paying for those costs which should be more accurately charged as part of the connection costs to customers. This cross-subsidy would also unduly reduce the costs charged to developer customers by incumbents which would have negative impacts on the development of competition. Conversely, if the overheads allocated to developer services are higher than would be cost reflective then it would follow that water companies may risk overcharging those customers to the benefit of the wider customer base.

***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?***

We believe that, given the existing discrepancies which have been identified and are discussed in the consultation paper, it would be beneficial for RAG2 to define the approach for overhead cost allocation. We do not foresee any disadvantages in doing this.

We do not have a specific preference or recommendation for use in this context but we believe that overhead allocation should be based on a hybrid of both expenditure and volume of work to ensure cost reflectivity. I.e. we do not believe that there is a single drive which should determine overhead allocation and it is important that several factors are considered in developing a common method.

***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?***

We believe that this should be a consideration to distinguish between developments which require a mains and those which do not require a mains. The nature of the work undertaken and the level of overhead attributable to those types of developments is likely to be different and so a fair and reflective overhead allocation method would need to draw that distinction.

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

We are fully supportive of a review of the competitive market for developer services. There are several factors which will impact on the development, or otherwise, of competition in a given area and market segment and we recognise the need for Ofwat to be able to define the scope of the review to be able to take into account all of these factors so we agree that this should be a separate exercise.

We believe that some of the areas which are likely to influence the development of competition, particularly in relation to NAVs, are:

- The ease of getting a connection from an existing water company to develop a new site;
- The cost of non-contestable services and the extent to which those services are cost reflective and are applied equally to the incumbent operator's own connections business;

- The ability of an SLP or NAV to operate in the region including the possible market penetration available in that region and the ability to serve customers (developer and end users) economically
- The revenues margins available to NAVs operating water networks being commensurate with the costs incurred and the costs which would be incurred if the incumbent operated that network as a stand-alone business.
- The provision of emergency response contract by the incumbent in a given region.

There are likely to be other factors and a market review will be a significant piece of work so we believe that it is important to set out the scope properly and thoroughly at the start of any work. We would welcome further engagement with Ofwat on this matter when they are seeking to set out this scope in detail.

We note that Ofwat have referenced Ofgem's competition review in your consultation document and we believe that there are significant lessons to be learned from this review. As part of our group of companies we also operate independent distribution network operators (IDNO) and played an active role in the development of this review. Our main point from this review would be to ensure that the scope of any review is able to accurately assess the development of competition in the market, is not too prescriptive in how it achieves this purpose and is not too wedded to the differentiation of market segments, noting that markets do not always develop in predictable ways. We would welcome further engagement on this area and would be happy to discuss in more detail our experience of Ofgem's review with the relevant teams within our groups of companies.

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

We support the proposal to include historical variances between expenditure and reviews in setting future infrastructure charges. Although we recognise that there is a desire for developers to have predictable charges with low levels of volatility, we do not believe that this should be at the expense of other customer groups and we do not believe that this need is more important than the general need for cost-reflective charging for infrastructure.

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

We agree with the changes to be able to take into account upsized infrastructure in setting infrastructure charges.

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

We do not have any comments on the proposals relating to how Ofwat intend to accommodate the agreed changes in the context of this consultation but we would, however, refer Ofwat to the response that we submitted to the consultation on introducing environmental incentives to address our wider views on the rollout of environmental incentives

