W A CONSULTANCY LTD

technical & development services

The Competition & Markets Authority
25 Cabot Square
London
E14 4QZ

5th May 2020

Dear Sirs,

RE: Water & Sewerage Sector: Impact of PR19 FDs & the New Charging Arrangements

We welcome the opportunity to respond to the CMA's call for input and/or evidence following the rejection of Ofwat's PR19 Final Determinations by four Water and Sewerage Companies. Ever, since our involvement in the sector reforms starting some 7-years ago, and in the context of Developer costs, we have continued to raise questions and concerns about Ofwat's underlying objective(s) and motivation(s).

By way of introduction, TDS and WA Consultancy are two independent consultancy practices but who also work with other civil engineering consultants on an advisory and evidence share basis. In addition to providing advice and guidance to clients, our respective businesses deal with the design, construction and procurement of water and sewerage infrastructure on behalf of large developers/house builders, SMEs, and other consultants. As previous Technical Directors at major UK house building businesses our cumulative experience of water and sewerage matters, together with other areas of civil engineering practice, dates back to the early 1970's. Throughout our respective careers we have played an integral part in the development of legislation, regulation and guidance as the Water and Sewerage Sector started its evolution following the onset of the Water Act 1973. Cumulatively, we can demonstrate over 90 years of experience in House Building and the Utility Sector, mostly at senior executive level. In addition, our experience extends to legal and land acquisition due diligence matters and when called upon to do so, we have also engaged with Senior Officials in Government.

The co-author of this letter, Ray Farrow, is also a Director of an established and accredited Self-lay provider for water services, namely, Utilities Direct Ltd, and can therefore speak with authority on such matters.

For ease of reference we have opened our response with a short 'executive summary'.

Executive Summary

At the outset, (2013/14) one of our primary concerns related to a possible shift in market dynamics whereby Ofwat in being given an un-audited freedom to redefine who pays for what, would seek to introduce reforms that significantly increased developer costs as a means of reducing existing customer bills. Assurances were sought that this would not be the case, but reality has since confirmed otherwise and that our original perception and accompanying concerns were well founded.

In September 2017 Defra issued an update of the Government's Strategic Priority Statement (SPS) for Ofwat pursuant to Section 2A of the Water Industry Act 1991, as amended by the Water Act 2014. Moreover, this 'statement' followed the January 2016 Defra Statutory Guidance issued to Ofwat, and specific to the introduction of new Water Company charging rules/arrangements in April 2018.

Included amongst a cumulative number of 8 'priorities' and 'objectives' set out in the 2017 SPS were the following material, principal statements:

> "***Priority:*** *Ofwat should challenge the water sector to plan, invest* and operate to meet the needs of current and future customers, in a way which offers best value for money over the long term*".
>
> "***Objective:*** *Ofwat should challenge water companies to improve planning and investment to meet the wastewater needs of current and future customers*".
>
> "***Housing (Para 27)*** *– Ofwat should keep under review what it can do to make sure that company planning and delivery keeps pace with housebuilding and supports development across the country, taking account of its duty to contribute to the achievement of sustainable development*"*.

(* Our underlining for emphasis).

The collective view, and not just from the four Companies that have rejected Ofwat's PR19 FDs, is one of Ofwat having repeatedly failed in its duty to deliver on its obligations. Moreover, the evidence we have included in this submission creates a compelling question as to whether Ofwat has strayed into the realms of 'market manipulation' given the latest charging reforms are now heavily skewed towards reducing existing customer bills through the introduction of significant and inequitable increases in developer costs. In our opinion, this is a key area for detailed scrutiny by the CMA.

The expectation of Defra, Developer Customers, their Consultants and Advisors was that costs before and after the introduction of the new charging rules and charging arrangements would be clearly set out on a robust comparison basis to allow the Developer Community to make informed responses to any subsequent consultation. Similarly, and more importantly, to make informed commercial decisions when undertaking crucial land acquisition investments. This did not happen with Water UK representing the interests of Water and Sewerage Companies, whilst also advising Ofwat, steadfastly refusing to consider any aspect of historic charging being compared against the new charging arrangements.

We believe the evidence enclosed, elements of which support the responses made by each of the Companies who have rejected Ofwat's PR19 FD, will be of concern to the CMA.

Main Response/Evidence Submission

For the record we wish to express to the CMA our serious concerns over the way Ofwat has used ONS Household Formation Data to evaluate growth and new connections for 2020 – 2025. This is not only reiterated by the four Companies that have referred their PR19 Final Determinations to the CMA but by all Companies. Slavish reliance on ONS data is a fundamental error on Ofwat's part and one which has a profound effect on all Company PR 19 FDs, as evidenced by the following statement:

> ***"This funding gap arises because Ofwat:***
>
> ***(a) used ONS trend-based projections for its forecasts, which are implausibly low relative to Local Authority forecasts, and inconsistent with current outturn data"***
>
> (Anglian Water - Page 150 of their PR19 Rebuttal Statement)

Whilst Bristol Water also make the following comment in para 477 of their statement. In addition, they too have confirmed the fact that the ONS data relied upon by Ofwat is from 2016 and therefore unrepresentative of actual new connections achieved during AMP 6:

> ***"Indeed, the ONS's official methodology itself makes clear that its data should not be used as a reliable forecast for growth, but rather as a trend-based starting point for analysis. Specifically, it states:***
>
> ***"Household projections are not forecasts and generally take no account of policy or development aims that have not yet had an impact on observed trends".*** (Bristol Water)

In addition, we are obliged to raise with the CMA a series of water and sewerage related issues that indirectly affect the PR19 Final Determinations, in addition to raising doubt about the competence of Ofwat in the discharge of their regulator duties when it comes to Developer Services and specifically, the veracity of the Charging Rules and Charging Arrangements.

As we reach the final stages of the Water and Sewerage Sector reforms, together with the onset of AMP 7 in April 2020, we are compelled to write to the CMA in relation to the following:

1. **Ofwat's PR19 Final Determinations and the significant and concerning variations between Ofwat's and the Company's forecast of new connections in the ensuing five years, i.e. 2020 to 2025.**

2. **The New Charges being imposed on Developers under Ofwat's Charging Rules and Company Charging Arrangements.**

In addition to the above, we have closed our submission by providing a series of bullet-points identifying a number of intrinsic, important related issues and concerns we firmly believe the CMA should investigate as an integral part of its current review.

1. Ofwat's PR19 Final Determinations and the significant and concerning variations between Ofwat's and the Company's forecast of new connections in the ensuing five years.

1.1 Attached are two comparison schedules compiled from Ofwat's PR19 Final Determinations. The first (Schedule 1)defines the considerable and concerning difference in the forecast of new connections, i.e. submitted Water and Sewerage Company evidence-based forecasts versus those crystallised by Ofwat in respective FDs.

1.2 The second (Schedule 2) shows the monetised consequences that result. In addition, see later sections of this submission relating to costs/charges in general and which our Clients and the Developer Community in general will have to pay over the ensuing period. The shortfall in infrastructure investment is considerable – a concern echoed not just by Developers and Consultants but by almost all Water and Sewerage Companies during our recent and ongoing dialogue with them. Whilst only four Companies have taken the decision to formally reject Ofwat's dictated imposition, there is sector-wide consensus and disquiet that we now have a serious issue of under-investment.

> ***"Ofwat's unsatisfactory approach to growth therefore compromises Anglian's ability to meet its statutory obligations and is inconsistent with Ofwat's duties to secure long-term resilience, further the consumer objective, secure that water companies can finance the proper carrying out of their statutory functions, and contribute to the achievement of sustainable development. It is also inconsistent with the Government's SPS to ensure that delivery keeps pace with housebuilding and supports development across the country. While many regions are adversely affected, Anglian is one of the most disadvantaged, given the region's growth requirements".*** (Our underlining for emphasis).
>
> ***"Furthermore, the Final Determination also risks Anglian's ability to facilitate Government and Local Authority plans for home building in addition to the future growth pressures not reflected in the Anglian Plan such as those associated with the proposed Oxford-Cambridge (OxCam) corridor"*** (Anglian Water Rebuttal Statement Chapter E2 – Growth)

1.3 Ofwat's slavish reliance on ONS Data for growth and new connections is totally inappropriate and constitutes a major error on their behalf. What is most disturbing is that in raising the matter with Ofwat they declined our offer to share with them the information contained in Schedules 1 and 2, labelling it as 'antagonistic'. Consistent with our concern, the rebuttal submissions presented to the CMA by Anglian Water, Yorkshire Water and Bristol Water respectively, advise that ONS household projection data, as used by Ofwat, is neither appropriate nor is it a reliable and accurate source to determine the projected number of future new connections. Likewise, crucial investment decisions that have a direct impact on housing delivery. Moreover, ONS data carries a specific 'health warning' and counsels that it should not be used in the manner relied upon by Ofwat. The ONS data is also dated (2016) and does not account for Government policy to deliver 300,000 new homes each year, with a house building industry already on target to meet this policy requirement by 2025, despite the current unprecedented times we find ourselves in. Likewise, ONS data fails to reflect the housing-related decisions already made by Central and Regional Government regarding HS2 and the Northern Powerhouse, respectively.

1.4 MHCLG net new home completion data is more reliable and representative as this provides the means for determining annual, net new home completion payments from Central Government to each local authority. We have had this conversation and engaged in e-mail correspondence with both Ofwat and Water UK but there has been a tacit reluctance on their part to listen to what experienced developer customers, consultants, planning consultants, and indeed others have been saying. Likewise, to properly consider the supporting evidence we have provided. Moreover, when time and precious resources have been spent to provide accurate and representative data the approach taken by Ofwat, including their ill-informed consultants, is anathema to both effective engagement and business planning. Furthermore, it leaves us to conclude that Ofwat had already pre-determined their decision based exclusively on purist economics, whilst maintaining a preference for shareholder interest(s) at the expense of targeted and responsive infrastructure investment.

1.5 As a result of Ofwat's light touch regulatory approach, we have already seen certain Water and Sewerage Companies free to return to the exercise of their monopoly privileged position by putting developers under commercial duress to meet any shortfall in infrastructure funding by whatever subjective means possible. In our view, and the views of many, including several Water and Sewerage Companies, monopoly privileged businesses need more prescriptive regulation and control, not the converse.

1.6 The reality of Ofwat's PR19 Final Determinations will likely lead to delays if not partial paralysis in the house building industry arising from the imposed restrictions on infrastructure investment. The lack of adequate investment in the provision of water and sewerage infrastructure will clearly undermine the ability of Companies to even fulfil their statutory obligations under S37 and S94 of the Water Industry Act 1991 – a fundamental and concerning point made in each Company's rebuttal statement. (Anglian Water have identified a £318 million funding shortfall – this is of serious concern, especially if shortfalls of this comparative magnitude are replicated across the Water and Sewerage Sector).

> ***"Anglian's Plan included £660 million to meet housing and population growth requirements in its region and £60 million to reduce sewer flooding and low-pressure incidence on its network (total £720 million). The FD allows just £402 million, leaving Anglian underfunded by £318 million for growth, reducing sewer flooding and low pressure due to:***
>
> ***(i) Ofwat's use of Office for National Statistics (ONS) trend-based projections, which are implausibly low relative to local authority forecasts and current outturn data;***
>
> ***(ii) Ofwat's approach to modelling growth costs, which for the sector, adds around £4.5 billion of growth (and other) expenditure into its unadjusted base costs models. Anglian considers these models unfit for assessing growth expenditure needs: …."***
>
> (Para 481 of the Anglian Water Rebuttal Statement)

1.7 The negative comments made by Anglian Water, Yorkshire Water and Bristol Water in their respective PR19 rebuttal statements are not unexpected. Moreover, both have cited Ofwat's very perceptible disregard of developer customer needs and expectations - an experience we have frequently encountered in our dealings with Ofwat and Water UK. It also raises the compelling question as to whether Ofwat really understand the equitable function of Water & Sewerage Company Developer Services Departments and the importance to future housing delivery.

1.8 Table 1 below identifies the considerable shortfall in new wastewater connections over AMP 7 (2020 -25) for each Water and Sewerage Company, Welsh Water excluded:

Company	**Ofwat F/Cast**	**WaSC F/Cast**	**%age Shortfall**	**Comments**
Anglian Water	118,035	218,345	**45%**	Area of considerable growth
Northumbrian Water	21,054	49,543	**58%**	
United Utilities	77.095	137,580	**44%**	Area of considerable growth – Northern Powerhouse
Southern Water(1)	86,766	113,136	**23%**	Area of considerable growth
South West Water	27,179	36,124	**25%**	
Thames Water	260,933	330,117	**21%**	Area of considerable growth
Wessex Water	51,063	64,514	**21%**	
Yorkshire Water	55,286	107,103	**48%**	Area of growth – Northern Powerhouse
Severn Trent	135,060	184,970	**27%**	Area of growth - HS2

(Table 1)

(1) Additional issue in Southern Water involving Wastewater treatment breaches (Nitrates) and the falsification of WwTW treatment records – additional S94 investment crucial to housing delivery and to redress historic under-investment in WwTWs and the public sewerage network in general.

1.9 Whilst Table 2 identifies the considerable shortfall in new water connections:

Company	Ofwat F/Cast	WaSC/WoC F/Cast	%age Shortfall	Comments
Anglian Water	94,275	191,101	**51%**	Area of considerable growth
Northumbrian Water	59,930	91,181	**34%**	
United Utilities	79,946	140,319	**45%**	Area of considerable growth – Northern Powerhouse
Southern Water	47,405	64,962	**27%**	Area of restrictions & high demand
South West Water	37,515	46,895	**20%**	
Thames Water	174,563	225,962	**23%**	
Wessex Water	24,692	33,832	**27%**	
Yorkshire Water	55,854	109,792	**49%**	Area of growth – Northern Powerhouse
Affinity Water	66,143	87,468	**24%**	
Bristol Water	23,996	29,914	**20%**	Area of growth
Portsmouth Water	10,520	11,359	**7%**	
SES Water	12,605	12,629	**>1%**	
South East Water	45,630	51,783	**12%**	
South Staffs Water	20,333	30,946	**34%**	
Severn Trent	122,923	153,973	**20%**	Area of growth – HS2
Totals	873,330	1,282,116		**Shortfall of 408,786 connexions**

(Table 2)

Taking even the total forecast connections, as submitted by Water and Sewerage Companies, this only represents an average of 256,423 connections to new homes in each year. The only conclusion that can be drawn is the approach taken by Ofwat will have serious repercussions for housing delivery throughout AMP 7 given the imposed restrictions on infrastructure investment.

1.10 Having finally obtained Ofwat's PR19 FDs it became necessary for us to seek clarification by making a formal request to Ofwat under the FOI regulations as to whether their total connection numbers identified were specific to new housing. Ofwat's staggering response was that their forecast:

(a) Included a range of building typologies, <u>including non-residential and commercial</u>

(b) No percentages of building typologies had been determined and ….

(c) Companies had not been requested to provide such crucial information, despite its underlying relevance and importance to the calculation of charges, typically the network reinforcement component of the now combined infrastructure charge.

This leaves the spectre of a house building industry contributing to new connection costs that are subsidising others and not in direct consequence and/or related to new residential development. Likewise, the prospect of skewed infrastructure charges that include for network reinforcement that is not specific to new residential development. The only way to resolve this matter is by the disclosure of robust evidence but sector reluctance to do so is seriously undermining what little trust and confidence may exist.

1.11 Ofwat's likely defence is that the April 2020 market reform(s) are to facilitate increased sector competition through NAVs, i.e. the NAV market will make up any shortfall in Ofwat's forecast of new connections. We disagree with such an assumption on the most compelling of grounds, namely, the NAV appointment process can be considered anti-competitive in its own right given the process and procedures that have to be adhered to and the time it takes to issue a licence, i.e. in excess of 4 months. This has little if any synergy with the land acquisition due diligence process and undermines effective competition. We have raised this issue with Ofwat and Water UK several times over with our suggestion of working collaboratively to resolve the issue having been effectively rebutted. Moreover, in the 16 months ending April 2020 a mere 68 NAV licences (as identified on the Ofwat register) have been issued - and to just two NAV businesses. Of these, only 18 relate to the provision of water infrastructure. By comparison, licences issued in the energy sector far exceed those issued by Ofwat by several orders of magnitude – see Ofgem list of licences. NAVs are welcome but their ability to make up a significant deficiency in water connections is a heroic aspiration on the part of Ofwat given the lack of NAV competition and an underlying lack of enough critical mass.

1.12 In summary, we are very much of the opinion that the CMA need to look beyond the PR19 FDs to judge if Ofwat has acted as an effective Industry Regulator. Similarly, can they be considered to have fully discharged their statutory obligations? We are not alone in believing there are significant shortcomings on the part of Ofwat, some of which were first identified in the Gray Review of 2011.

2. The New Charges being imposed on Developers under Ofwat's Charging Rules and Company Charging Arrangements.

2.1 The legal requirement of the Water Act 2014 was for Ofwat to produce Charging Rules consistent with the principles set out in Defra's statutory guidance and thereafter for companies to produce compliant Charging Arrangements. Moreover, one of the fundamental requirements was to ensure that developer charges before and after 1st April 2018 effectively remained the same but not by relying on inexplicable and unjustified cross-subsidising when legitimate reductions in cost were the outcome. (Defra's view was that the reforms should result in a reduction in Developer costs for water and sewerage infrastructure provision).

> ***" ….. the range of initiatives underway are intended to improve the developer service experience by providing improved customer service, increased competition, more choice and transparency in the market. These in turn are expected to lead to cheaper, better, and more innovative services for all developers".***
>
> (Sarah Hendry - Director, Floods & Water, Defra – in correspondence November 2017)

2.2 The rationale for this basic requirement arose from initial concerns expressed to Government by House Builders regarding the fairness and transparency of charges *per se*. From the evidence we hold and can provide in addition to that enclosed, it is evident that Ofwat have not only failed to respect this requirement but have also failed to undertake any form of due diligence assessment of each Company's charges. This has been confirmed following our 2020 FOI requests made to Defra and CC Water, respectively. The unfairness of the present charges has been further exacerbated by Ofwat's most recent Charging Rule reforms that came into force from 1st April 2020 and evidenced in the Anglian Water rebuttal statement below:

> ***"As part of its DD Representation, Anglian revised its forecast for site-specific costs to remove £50.4 million associated with asset payments to self-lay providers. This reflected changing rules for charging for new infrastructure prohibiting these payments".***
>
> (Para 377 of the Anglian Water Rebuttal Statement)

The consequence of this imposed change by Ofwat will result in house builders and/or developers in the Anglian Water area alone having to pick up an additional cost of £50.4m during AMP7. **If these costs are consistent across the remaining Water and**

Sewerage Companies, the cumulative additional cost burden for house builders and developers will be circa £0.50 billion.

2.3 We have enclosed an earlier inter-company cost schedule that compares each Company's charges for the year 2018/19 – (Schedule5). These charges were introduced on a unilateral basis on 1st February 2018 and became effective on 1st April 2018. They contain alarming differences in costs that have little in the way of evidential justification. These differences have persisted despite earlier acknowledgement by Ofwat.

2.4 Similarly, a series of more recent schedules (2020) (Schedules 3 and 4) that drill down into the detail of the principal cost(s) and charges payable by developers. These too have been compared on a strict like for like basis. We are confident the CMA will be concerned at the significant variation in cost for identical infrastructure provision/specification(s). This information has been shared with Ofwat, who have shown no interest in investigating the underlying reasons and/or justification for such significant variation(s).

2.5 At no time has Ofwat ensured that either their own consultation(s) or indeed those instigated by each Company, included transparent cost information, supported by robust evidence. Moreover, costs and charges have been introduced on a specifically timed, unilateral basis, without any effective customer consultation, in addition to being presented in an evidential vacuum. This has raised many comments and concerns by the Developer Community as well as us regarding possible anti-competitive practices and/or behaviour within the Water and Sewerage Sector.

2.6 Since 2013, our two consultancies have been engaged in an evidenced-based evaluation of the market reforms progressively introduced by Ofwat. Sector engagement has not been without its difficulties and frustrations, especially when trying to get Ofwat to fully understand the needs and expectations of house builder customers on a fair, equitable, and transparent basis. Principal to these reforms was a need to build sector trust and confidence in a part of the utility sector that is overly expensive and which has frequently come under the customer spotlight for relying on its monopoly privileged position to the extent that it can be considered (in part) to have been anti-competitive.

2.7 From the outset, Defra's intention was made clear in that sector trust and confidence will only be restored, if not enhanced, if Ofwat ensure companies provide robust cost/financial evidence to support their new charging arrangements. Instead, we have experienced a light touch regulatory approach that has been anathema to the concept. Regrettable as it is to say, this fundamental need for transparency has been betrayed by the sector refusing to disclose such information. This is despite repeated requests to do so. Moreover, Defra called upon Ofwat to issue a Regulatory Impact Assessment as part of its Charging Rules/Arrangements consultation in 2017 – it was never provided and therefore denied the Developer Community, Self-lay businesses and NAVs the opportunity to be informed, together with the means to provide wholesome comment. The defence has been that the sector needs to be wary of the rules on competition concerning such disclosure, but we find this to be a somewhat groundless reason to either redact or refuse to disclose crucial evidence.

2.8 As the reforms have progressed the need to maintain cost neutrality has been especially important but it is clear that Ofwat have discounted any such approach and used their interpretation of the legislation, and the remit handed to them, to significantly increase developer costs - a comment that has been made by several peer group consultants.

Similar comments have been made by a number of Water and Sewerage Companies who have readily admitted that they occupy the middle ground of trying to introduce fair and equitable charges for developers against the economic and unrealistic constraints that are being imposed by Ofwat. For example, one Company has made it quite clear that from April 2020, developer costs will increase by around £1000/dwelling – other Companies have repeated such comments but without necessarily reporting a monetary value. (As an aside, the cumulative cost of Gas, Electricity and Superfast Broadband provision for a new residential dwelling is significantly less than the increase in cost, as advised by the Company concerned).

2.9 The perception of Developers, Consultants and indeed some of the Water and Sewerage Companies themselves, is that Ofwat are approaching matters from an economist's perspective and one that effectively preserves the largesse of excessive shareholder returns rather than the fundamental importance of ensuring there is sufficient investment to meet the Government's housing objectives. There is already evidence of a return by certain Companies, aka Southern Water and Dwr Cymru, using their monopoly position to leverage additional and inequitable funding from a developer community put under commercial duress to accept inequitable terms and conditions for the provision of water and sewerage infrastructure.

2.10 In our seminal discussions (2013/14) Defra confirmed that one of their principal expectations of the charging reforms, likewise the future direction of PR19, would see developer costs reduce. Likewise, that companies would have financial headroom to enable timely investment in water and sewerage infrastructure to meet the Government's housing objectives. From the evidence we have painstakingly collected over the past three years, part of which is enclosed with this letter, our experience is the complete opposite and to a significant extent in terms of increased Developer costs.

2.11 It is clear to us and indeed other engineering consultants, Ofwat has erred, either by going far beyond their remit or in mis-interpreting the statutory guidance issued by Defra to Ofwat in January 2016. That said, a second FOI request made to Defra and CC Water has confirmed no audit has been undertaken to test whether Ofwat's Charging Rules and Company Charging Arrangements comply with Defra's statutory guidance. The sole arbiter in this respect, is the water and sewerage sector itself and as such can hardly be considered as an aid to transparency.

2.12 There has been much talk by Ofwat of maintaining a so-called 'balance of charges', but this has never been articulated or defined by Ofwat in monetary terms. Likewise, what falls to be defined as a cost-reflective charge and the components of such a charge. Furthermore, any 'balance of charges', if it ever existed, now has a new benchmark, i.e. one that directly favours the commercial interests of Water & Sewerage companies. The statutory guidance issued to Ofwat could not have been clearer, namely, the need for fair, transparent, evidence-based, cost reflective charges. In our opinion these basic requirements have not been met.

2.13 During discussions with Ofwat we have continued to rase concerns about the effect that the market reforms will have on both Self-lay businesses and developer costs. Paragraph 377 of the Anglian Water rebuttal statement and referred to earlier, makes for very concerned reading. This statement alone crystallises the very point we have repeatedly made to Ofwat that the market reforms will not only undermine the benefits of competition delivered through self-lay businesses but will shift significant costs onto developers. Moreover, these costs will not be reduced whilst income off-sets are set at low, inconsequential, and unrepresentative levels when compared to the statutory provisions that previously existed in the Water Industry Act 1991.

2.14 The direction taken by Ofwat, which will impose even more cost onto developers, has the cumulative effect of lowering the charges paid by the general bill payer. With cost neutrality being assured by Defra from the outset and as a *de minimis* expectation/outcome, we find the current charging regime manifestly inequitable.

2.15 Much of what Ofwat has instigated since 1st April 2018 and supposedly in *de facto* compliance with Defra's statutory guidance, appears without any credible supporting cost evidence. Defra's clear expectation was that Ofwat would provide a Regulatory Impact Assessment as part of its consultation process for this very purpose, but this remains conspicuous by its absence. Costs and the market reforms in general are now clearly skewed towards preserving if not enhancing the commercial interest of the Water and Sewerage Sector.

2.16 As can be seen from the comparisons enclosed, these neither constitute a balance of charges, whatever defines this 'balance of charges' in monetary terms, nor can many of these charges be considered cost reflective. From a Developer Customer perspective, we have a confused picture – a sentiment privately echoed by nearly all Water and Sewerage Companies. Sector comments have also been made as to whether Ofwat have enough understanding of Developer Services Departments, having taken the line of least resistance by leaving each Company to interpret Ofwat's Charging Rules as they see fit. In many respects, the reforms have been regressive rather than progressive. Moreover, with the sector able to self-certify compliance with Ofwat's Charging Rules through Company Board Assurance Statements rather than an unbiased, independent audit, raises many questions concerning anti-competitive behaviour and practices, perhaps even to the point of being a cartel.

2.17 In summary, paragraph 710 of the Anglian Water Rebuttal Statement, repeated verbatim below, speaks for all water and sewerage companies in addition to justifying the many concerns we have raised in this submission.

> ***"However, Ofwat's approach means that net totex has been underestimated by £47.4 million (as Ofwat assumed higher contributions from developers). This makes it even harder for Anglian to outperform the cost-sharing incentive than would otherwise be the case".***

3. Other Related Matters That Merit Investigation by the CMA due to Ofwat Charging Rules

The series of bullet-points that follow relate to issues we believe the CMA should also consider investigating in full and which are a direct consequence of Ofwat's Charging Rules:

- The significant variation in charges between Companies and their divergent approach for identical work – regional variations are accepted but not to the degree our evidence has revealed.

- The reduction in income offsets, supposedly to reflect the new income stream from new homeowners has been significantly reduced to be less than 2 years income on average when previously this was set at 12 years. A consequential and additional cost that will have to be borne by Developers. The schedules attached identify the paucity of water company income offsets at a time when average domestic water and sewerage bills are around £413/property and the related income-generating asset that developers construct are gifted to incumbent companies free of charge.

- Developers must now pay the full cost associated with requisitioned water and sewerage infrastructure. The original legislative mechanism resulted in developers paying around 15% of the total cost of the works in recognition of a Water and Sewerage Company's statutory obligations pursuant to S37 and S94 of the Water Industry Act 1991. Current Water and Sewerage Company approaches have serious implications for developer cash flow, especially the adverse effect on ROCE/ROA when high value requisitions are involved.

- We have genuine concerns about the continuing role of Self-lay businesses – we have identified one instance where the Water Company cost for a simple water connection appears to have been cross-subsidised to deter self-lay competition. At the cost quoted, no self-lay business can complete but Ofwat refuse to intervene. What we have exposed are increasingly low Company connection and main-laying costs that are unrepresentative to the extent that competition from self-lay businesses is effectively neutered.

- We remain concerned about the role of Water UK as a solus Water and Sewerage sector trade association tasked by Ofwat to prepare sector guidance and policy relating not just to the market reforms involving the Charging Arrangements but also the Codes for Adoption Agreements. We seriously question whether this is acceptable from a competition rules perspective, especially when Developer Customer consultation has not exceeded 2% of the Developer Community, inclusive of its consultants. Moreover, during the reforms and at key stages in the engagement process, we believe the Home Builders Federation has also been excluded.

- How network reinforcement has been determined and how this has influenced the combined infrastructure charge remains an unknown. Ofwat remain disinterested in terms of presenting adequate and robust evidence in this regard.

- Aligned to the previous bullet-point we have identified clear and unacceptable inconsistencies when it comes to water and sewerage asset capacity modelling. On the one hand certain companies say there is a consistent approach taken by all companies, conversely, others say that there are various methods. Whatever approach is being taken our evidence shows that in some instances overly conservative and quite subjective modelling criteria is being applied, but once again Ofwat have no desire to intervene. It is very evident that companies are free to choose whatever methodology they like in terms of demonstrating minimum available network capacity to justify maximum developer funded network reinforcement, either as a direct cost or through skewed infrastructure charges.

- Ofwat lack consistency in their approach to site specific issues that become the subject of a formal determination. This a key area that needs to be investigated. Moreover, waiting years for the outcome of a determination is not conducive to fair and equitable charging. Likewise, developers being forced to resolve disputes in the Courts because there is no effective dispute resolution process.

- Questions have also been raised regarding what assurances do we have that Water and Sewerage Company term contractors are not ‘price ringing’ as part of the tendering process. Some of the rates for main laying cited by certain water and sewerage companies and evidenced in our submission appear to be unrepresentative when compared to Developer procured sewerage infrastructure through a competitive tendering process.

- On 6th February 2020 Water UK announced that average household water and sewerage bills will reduce by £17 in 2020/21. With 27.8 million households in England and Wales the cumulative reduction could be around £473m. Given the impact of Ofwat’s PR19 FDs, together with Ofwat’s commitment to allow company profits and shareholder returns to be maintained at present levels, it is only the Developer Community that can be called upon to make up any shortfall through reformed costs and charges, This may be a somewhat crude calculation but it nonetheless supports much of what we have committed to in this submission.

The severity of the situation compels us to draw these issues to the attention of the CMA.

Given the evidence we hold and which we are willing to share, we believe a more detailed forensic analysis is required by the CMA. Therefore, we are quite willing to meet with the CMA to discuss in more detail the information we have provided.

Yours sincerely,

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