

Paying for household water services

Charging for domestic water services on the basis of household rateable values will be illegal after 31 March 2000. A discussion paper prepared for the Public Utilities Access Forum by John E. Thackray analyses the existing system for billing consumers and considers the options for reform.

f More than half the average household water bill is for disposal of sewage and rainwater from properties and from roads. These costs are not proportional to the volume of water supply. Even for water supply, a high proportion of costs is for making the service available 24 hours a day, regardless of the volume of use.

f The current system of rateable value charges creates serious anomalies that are becoming increasingly unfair and unsupportable. Rateable values for similar size houses vary hugely from one area to another; flats are more highly rated than the corresponding accommodation in houses; and older properties are generally lower rated than newer homes even when they are larger and have higher capital values.

f Water-metering is not an economically viable alternative. Only one in ten homes are fitted with meters and no more than 50 per cent are forecast to be metered by the middle of the next century.

f Existing metered tariffs discriminate against low-income households who need above average amounts of domestic water, including those with young children or older people with incontinence problems or other disabilities requiring intensive water-use.

f Transferring the costs of highway drainage to general taxation would reduce household water bills by 10 to 15 per cent.

f The researcher concludes that two approaches to future charging for water can be seen as more practicable than others:

- basing charges on Council Tax band values would be the modern equivalent of rates. However, Council Tax bands bear even less relationship to household water costs than rateable values. The change would require legislation and consideration would need to be given to a system of rebates for low-income families as are currently available in Scotland.
- charging based on factors closely related to the cost of service provision - such as floor and garden area - would be relatively simple to calculate and make metering unnecessary for the majority of households. A 'Water Services Factor' system would not require legislation, would be low cost to install and make it possible for resulting changes in bills to be justified.

Background

Paying for water services, which used to be a relatively simple and uncontentious issue, has increasingly become the subject of acrimonious debate. Household bills have risen substantially, but unevenly. In England and Wales they have increased by more than double the general rate of inflation since 1989. Some households, including many with low incomes, have been hit much harder than others. Similar problems are emerging in Scotland and are foreshadowed in Northern Ireland. The same legislation that introduced the privatisation of water services in 1989 also makes the present system of calculating bills on the basis of rateable values (RV) for some 18 million homes in England and Wales illegal after 31 March 2000. The need for change was identified in a government White Paper in 1986, but 11 years later and very close to the deadline, very little progress has been made by the water companies and their regulator.

The current charging system

Current charges cover what are, in reality, four different water services provided to households: water supply, sewage disposal, rainwater disposal from buildings, and rainwater disposal from highways. There are two fundamentally different ways in which the cost of providing any one - or all four - of these services can be met:

- providing funds from local or national taxation;
- making direct or indirect charges on households and others.

The Water Act 1973 caused a major shift to paying for all of the water services through charges rather than through taxation in England and Wales. In addition, the 1989 legislation in which publicly-owned water companies were privatised, gave a government-appointed water regulator new and personal power to advise the companies how to charge individual households and sanctions to ensure that his advice is taken. The regulator has taken substantially different views on how legislation should be interpreted from those of his public authority predecessors. This approach is unique in the world. In Scotland similar changes are in process, but there is still an explicit public subsidy for sewage and rainfall disposal charges. In Northern Ireland there are no direct charges to households or small businesses for any of the four water services at present: costs are still primarily met from local taxation, supported in varying degrees by national taxation.

The component costs of water services

If customers are expected to pay for their water services through charges that reflect the costs of making these services available, it is essential to be as clear as possible about how those costs are built up. Hitherto there has been little in the way of published analyses of the separate costs of each major component of these services. However, an analysis making use of the detailed published accounts of one water company whose tariff structure best separates the charges for each of the four water services suggests that:

- Over half of the average household bill is for sewage and rainwater disposal services;
- Costs associated with local pipe networks account for half or more of total costs;
- The greater part of total costs is for making services available 24 hours a day, irrespective of actual use, and bears no proportional relationship to the volume of water consumed by individual households.

Options for future water charging

The study examined six alternative bases for water charges. These were assessed against a checklist of criteria:

Fairness - issues of affordability or social equity are intrinsically important for a basic, essential and monopoly service;

Broadly related to costs - costing cannot be precise but the present legislative framework requires charges to 'have regard to cost';

Practicability - some charging bases cost considerably more than others to install and operate;

Transparency - customers should be able to check the basis for their bills and budget on the basis of predictable charges;

Flexibility - charging bases need to be long term to be effective, but they also need to be simple to update and flexible in the face of change.

Option 1: household metering

As the 31 March 2000 deadline has grown closer for the ending of water charging based on rateable values, the water services regulator and many of the water companies have focused on metering as the

preferred new charging base. Yet information from the water companies confirms that only one in ten homes are fitted with meters and suggests that no more than 50 per cent are likely to be metered by the middle of the next century. Meter installation is costly and the environmental gains through reduced domestic water use are very limited and often achieved through poorer households reducing their water use. There is evidence that metered tariffs already discriminate unfairly against certain types of low-income household which need above-average amounts of domestic water. These include households with young children and older people with incontinence or other problems causing above average need for laundry. Metering provides a poor fit with the 'fairness' criterion unless much more sophisticated and administratively costly tariffs could be introduced than are currently available. There is a different case which could be made for metering heavy use of water for gardening. By law this is a non-domestic use. Appropriate tariffs would be easier and cheaper to operate if it could be metered separately from the home's main domestic supply.

Option 2: extending the use of Rateable Values (RVs)

Extending the use of rateable values is increasingly impracticable as they have ceased to be maintained and kept up to date by the Valuation Office. A large and increasing number of properties simply do not have a valid RV. The RV base is, in any case, known to contain many serious anomalies from the point of view of water-charging, with flats being more highly rated than corresponding accommodation in houses and older properties having lower RVs than newer properties - even when they are larger and have higher capital values. Although some families and others with low incomes live in older, lower RV property, others live in newer social housing which is relatively highly rated. RV is now twice outdated even as a local government tax base. It fails the test of flexibility and cannot be said to offer a long-term solution.

Option 3: use of Council Tax Band Values (CTBV)

Some water companies favour a move to using Council Tax Band Values as a basis for household water, sewage and rainwater charges in England and Wales. In terms of social fairness, council tax band values would score worse than RV because of the relatively high weighting of charges to lower value housing. However, because it is more up to date than RV it does contain fewer anomalies. Charges based on CTBV and income from them would be predictable for both customers and companies. But their link with water service costs would not be

transparent - not least because of the problem of variability between England and Wales and between regions, and having too few bands and the high thresholds between them. Fairness would also require a rebate and discount system comparable with the one used for Council Tax itself. This is currently used for water services in Scotland. New legislation would be needed to permit the use of CTBV for water-charging

Option 4: Water Service Factors (WSF)

This approach would mean every household being given a number to replace RV - the Water Service Factor - on which its bill would be based each year. The WSF would be based on features broadly related to water service requirements and the long-term cost of making services available, such as gross floor area, standard spacing between properties, garden area, and roof and car-parking areas. The likely cost of measuring WSF for every home and introducing charges is estimated at around £10 per property, which compares very favourably with the costs of installing metering in existing homes of between £100-£200 per property. In addition, it would have very much lower operating costs, once established, comparable with those for the RV-based system and around £28 per year per property less than the annual costs of funding and operating metered systems. But even at £10 per property the one-off cost would be less than the extra operating costs of water-metering which recur each year. Moving to WSF would produce some major changes in water bills, with inevitable 'winners' and 'losers', but these would be less than for a move to CTBV. A charging system using WSF would, in the long run, meet the requirement to broadly reflect costs while being transparent and predictable for customers.

Two further possibilities were examined - Option 5: household licence fees and Option 6: household size and appliance counts - but both were considered to have too many drawbacks to be viable.

Finally the study proposes a Unified Tariff Structure which identifies the key cost components in the bill for each service: customer billing and contact; network and availability; volume of use; peak load. This structure could in principle be used with any viable tariff base.

Paying for highway drainage

The study concluded that if the cost of highway drainage was to be transferred back to general taxation instead of direct charges to consumers, household water bills could be reduced by 10-15 per cent. Such a move would ease the problems of

transition to Water Services Factors or any other new tariff structure and would represent a significant saving for low-income households.

Longer term policy issues

The water regulator - water industry regulation in the UK was traditionally a local or regional responsibility exercised by a board of local authority and special interest representatives. In England and Wales, this arrangement was abolished in 1989 and replaced by a single, national regulator. At the same time, customers effectively lost the right to appeal through the courts against decisions on charging policy. Key policy issues of regulator interpretation and approach need to be addressed and it would be timely to launch a review of the structure and mechanism of water service regulation.

Fairness of charging policies - several issues of fairness are shown to have been inadequately addressed within the present framework of paying for water services. Most especially since water service costs cannot be allocated precisely and domestic water use by more affluent customers is not especially sensitive to pricing there is a case for placing a duty on water service companies to operate reasonable cross subsidies which broadly favour those least able to pay while still having a general regard to cost. Reviewing this and other issues of equity may point to the need for changes in regulatory principles and institutions - and their basis in law.

About the study

The paper was based on the results of studying 95 publicly available references and research reports, informal discussion with practitioners, contact with the water companies by letter and confidential questionnaire, and a review of the author's own files and experiences over 23 years in developing and implementing the radical changes in charging policy required by the Water Act 1973 and numerous consultancy assignments on water services tariff policy development and change both in the UK and overseas.

Further information

The full report, *Paying for Household Water Services from 1 April 2000: From problems to solutions* is available from Sean Creighton, Secretary, Public Utilities Access Forum, c/o Agenda Services, 18 Ridge Road, Mitcham, CR4 2ET, Tel/fax: 0181 640 1814 (price £10 plus £1 post; cheques should be made payable to PUAUF).

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