



South Staffs Water

incorporating



South Staffs Water
and Cambridge Water

Developer Charging
Reform Consultation

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1. Introduction – purpose of this document

In December 2016, Ofwat (the economic regulator of the water industry in England and Wales), published [rules](#) requiring water companies to review their charging arrangements for developers. These are the charges that developers and other customers pay water companies for new connections to the public water supply network and other infrastructure services.

Our new charging arrangements will come into effect on **1st April 2018**. They will apply to:

- developers¹;
- self-lay providers, or SLPs (what used to be called ‘self-lay organisations’, or SLOs)²; and
- new appointments and variations (NAVs)³.

This document gives all of our stakeholders the opportunity to review and comment on our charging proposals. It follows our successful consultation events, which we held in our South Staffs and Cambridge regions in November 2017. At these events we gained a clearer understanding of our customers’ requirements and the challenges they face in the area of connection charging. We have reflected the comments we received in this consultation and incorporated them in our future direction of travel.

Because we are continually striving to provide an effective service to all our customers – including developers, SLPs and NAVs – our proposals aim to be fair and reasonable to everyone who engages with our business.

We are seeking views on our proposals by **29th January 2018**. Please see section 7 for details on how to respond to this consultation.

¹ Any person or company that buys land and builds properties for domestic or commercial use.

² Any contractor that a developer uses to install new water mains or other pipework.

³ A ‘new appointment’ is made where a limited company is appointed by Ofwat to provide water and/or sewerage services for a specific geographic area. A ‘variation’ is where an existing appointed company (or ‘appointee’) asks Ofwat to vary its appointment so it can extend the area to which it provides services.

2. Developing charging rules – progress to date

2.1 Guidance from the Department for Environment, Food and Rural Affairs (Defra)

The Water Act 2014, which amended the Water Industry Act 1991, permitted Ofwat to set rules about charges for new connections. This is where an owner or occupier of a building or premises to which water is provided requires access to the existing public water supply network.

On 29th January 2016, Defra issued [charging guidance](#) to Ofwat. This guidance is structured around the key objectives of:

- fairness and affordability;
- transparency and customer-focused service;
- environmental protection; and
- stability and predictability.

Defra's guidance stated clearly that:

“It is right that developers should bear the costs associated with connections to, or adoption of, water and sewerage systems. Charges should ensure that the distribution of costs for new infrastructure between developers and current customers of water and sewerage companies is fair. Cross subsidy between developers and water customers should be limited.”

Therefore, any new charging framework should preserve the existing balance between developer customers and present bill payers.

2.2 Ofwat's charging rules

Following consultation in July 2016, Ofwat published its [final charging rules](#) in December 2016. These rules are principles-based, with a strong focus on:

- fixed charges;
- clear methodologies to support predictability; and
- transparency to support development.

The rules state that water companies can levy charges for both off-site water and sewerage infrastructure. Also, while they do not require companies to illustrate environmental price signals in their charges, they do allow them to offer incentives for sustainable solutions.

Given the water scarcity challenges we face across both our regions, we welcome the opportunity to implement guidelines for water efficiency incentives and to offer a more transparent charging mechanism to our customers.

2.3 Developing our charging proposals

We have taken a considered approach to developing our charging proposals following consultation with customers. These proposals comply with Ofwat’s rules and take advantage of the opportunities they provide to encourage development and sustainable economic growth in both our regions. We welcome reform in this area and have played a role at all stages of its development.

We have embraced Defra’s vision to shape their charging principles, and have welcomed directions from both Defra and Ofwat in developing our proposals. We have also been part of the work that Water UK has carried out on charging reform.

Below, we set out a detailed timeline of our activity.

2017	July - September	- Initial scoping and drafting of consultation document into charging mechanisms
	September	- W/c 25 th : Draft consultation document released for initial comment to developers, SLOs and key stakeholders
	October	- W/c 16 th : Revised consultation published on company websites with email update for response
	2 nd November	- South Staffs Water event forum held in Walsall to discuss consultation in detail
	23 rd November	- Cambridge Water event forum held in Cambridge to discuss consultation in detail
	December	- Full review of all consultation feedback from customers and stakeholders
2018	January	- Release of second consultation document based on customer feedback – including priced scenarios for preferred charging mechanism - Full review of all responses from customers and stakeholders by end of January 2018
	February	- Publication of new charging approach published on company websites before end of February 2018.

In addition, our consultation events in November 2017 gave us the opportunity to understand our customers’ views on the new charging framework. The main feedback we received at these events was a preference for a ‘cost per plot’ approach to charging. We have taken this into account in this consultation. We have also published the feedback from the events on our [website](#).

The data analysis we have carried out has also informed our site-specific **cost per plot** proposal. We consider that carrying out this comprehensive analysis ensures that our proposals maintain the broad balance of charges.

3. Our current charging mechanism

Below, we have outlined our existing charging mechanism. This is to help all our stakeholders understand the changes we are proposing – and the rationale behind these proposed changes.

3.1 Maintaining the broad balance of charges

Within the existing charging framework, we are entitled to recover any reasonably incurred costs, so that our existing customer base does not cross-subsidise the capital expenditure required to enable new customers to connect to our network.

3.2 New connection charges

Within the existing charging framework, we are entitled to recover any reasonably incurred costs for delivering a new connection. These are charged per plot, and are typically in the range of £350 to £1500 per plot depending on the scale of the works required to connect the properties.

3.3 Infrastructure charges

Within the current charging framework, the infrastructure charge is a fixed value within operating licences conditions. Currently Ofwat review this number each year, however this is currently £365 per plot.

3.4 Site-specific infrastructure

When a main is requisitioned a charge is calculated by the water company using a methodology that takes into account future income that we will receive. This is known as Discount Aggregate Deficit (DAD) calculation. These costs are allocated per development at present, and can vary significantly from £1,000 to in excess of £1m depending on the scale of the works required.

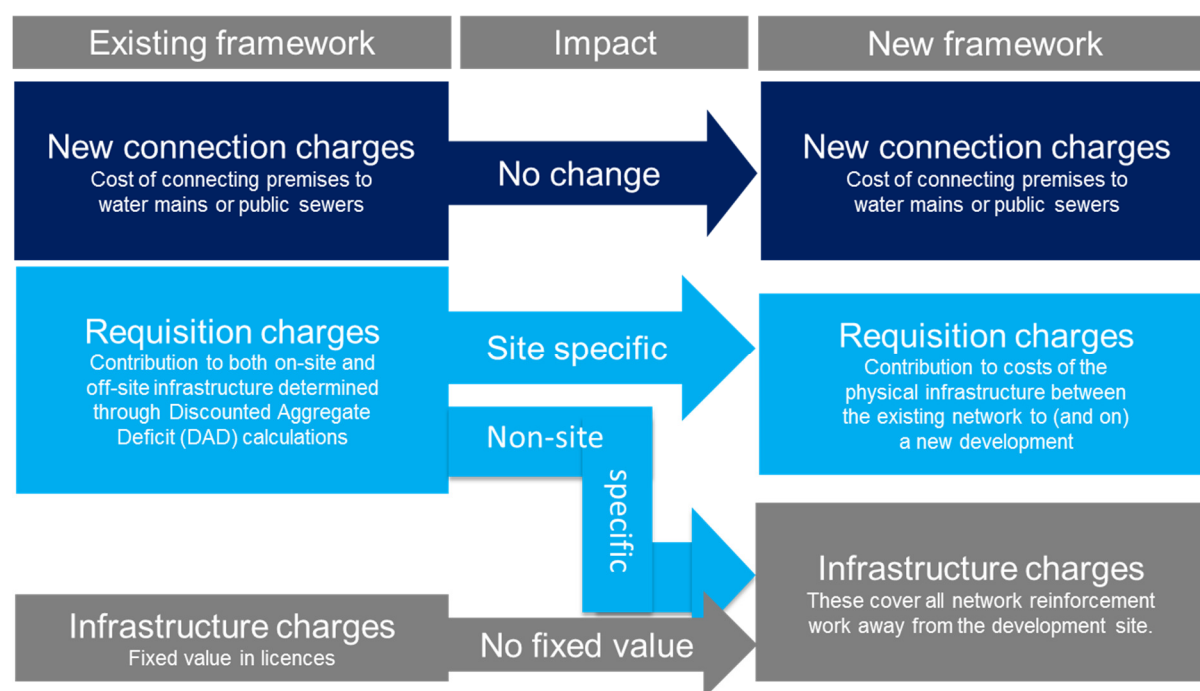
3.5 Off-site-specific infrastructure

Currently, any off-site infrastructure which relates to a new development has a capital contribution after the DAD calculation by the customer. This aspect of the charge is also allocated on a per development basis, and can vary significantly depending on the scale of the reinforcement works required to supply to

development. The range here can be from zero, up to £3m plus where significant works are required.

This capital contribution is paid at the same time a customer provides acceptance of their development estimate.

Figure 1. Summary of changes to charging framework



4. Our proposal

We propose implementing the following framework from 1st April 2018.

4.1 Maintaining the broad balance of charges

The Ofwat rules dictate that the broad balance of charges should be maintained, so within the future charging framework we are required to recover any reasonably incurred costs to ensure that existing customers continue not to be disadvantaged by the connection of new customers.

4.2 New connection charges

We intend to publish our charges to enable customers to determine the likely cost of their new water connections. Non-standard scope is captured in section 4.8.

4.3 Infrastructure charges

Under Ofwat’s new charging framework, infrastructure charges will fund the construction of the off-site reinforcement works required to support new development.

It will apply equally to developers, SLPs and NAVs, and will replace the existing off-site reinforcement requisition charge.

Our proposed cost per plot water infrastructure charge will be **£325**

In developing our new approach, we carried out research to establish the types and volumes of developments likely to be undertaken in the next five years. This has enabled us to assess the reinforcement works that will be required, which we have calculated using the cost per plot approach that our customers have said they prefer.

To ensure the correct balance of charges is maintained, we propose to monitor actual development and reinforcement works infrastructure spend and potentially recalculate each year.

4.4 Site-specific requisition charge

Our proposed site-specific requisition charge uses outturn cost data to determine this cost, which will also be provided on a cost per plot basis.

Where the customer approaches us directly for water, the proposed cost per plot site-specific requisition charge will be **£167**

We have looked at historical project data for completed schemes and have established the contribution on a cost per plot basis for mains requisition projects with on-site infrastructure only.

4.5 SLPs

We recognise that SLPs offer customers an important alternative for providing water infrastructure to serve their developments.

For SLPs, we propose to calculate the asset value (AV) payment on the basis of the inverse cost from the discounted site-specific requisition charge (outlined in section 4.4 above).

Again, we have calculated this AV payment on a cost per plot basis and this is **£612**

Scheme costs will include those relating to:

- network analysis;
- modelling; and

- point of connection.

They will also include those costs relating to any feasibility studies carried out, and will be applied consistently regardless of the type of application.

We intend to publish our SLP application service level performance, using Water UK's service level agreement (SLA) criteria. This supports our view is that all customers are equal. We also intend to introduce a specific application form for SLPs during 2018.

We are open to completing works on behalf of SLPs. For example, where the existing water main is located on the opposite side of a dual carriageway, the SLP can engage us to complete the works on their behalf if they choose to. The reasonable costs of this work will be deducted from the asset value.

As this is contestable work, we would not suggest that this should be compulsory in any way. But it provides SLPs with further options should they wish for us to complete such works.

4.6 NAVs

As with SLPs, we recognise NAVs as an important customer group, and propose to offer them a service package that is equivalent to those we would provide to any other customer.

Scheme costs will include those relating to:

- network analysis;
- modelling; and
- point of connection.

They will also include those costs relating to any feasibility studies carried out, and will be applied consistently regardless of the type of application.

When we receive a request from a NAV, we will report our performance using Water UK's service level agreement (SLA) criteria. This supports our view is that all customers are equal. We also intend to introduce a specific application form for NAVs during 2018.

As the on-site infrastructure is installed by the NAV, it is outside of this charging framework. But we will offer the same income offset to NAVs that we provide to developers and SLPs. We illustrate this in more detail in section 5.

Ofwat has recently concluded a [study](#) of the NAV market. Any action that Ofwat takes as a result of this study or its work on applying income offsets could affect our charging proposals for NAVs. We will monitor these developments to ensure we continue to offer our NAV customers an equivalent service to that offered to developers and SLPs.

4.7 Non-standard work

We intend to provide a fixed charge for works wherever possible. But there are certain to be circumstances outside our control where this will not be possible or helpful. In such cases, the works can become complex and unpredictable, and additional costs are incurred both in terms of the work we carry out and in terms (occasionally) of payments – for example, to a third party.

To ensure that we align with Defra’s charging principles, we consider there to be a balance between fixed charges and fairness. Given that elements of non-standard work are unpredictable and highly variable in cost, we think that simply passing these costs on when they arise is the fairest option for our customers.

The elements of non-standard exceptions are as follows.

- Where the consent of the Crown or an undertaker protected by Section 183 and Schedule 13 of the Water Industry Act 1991 are required.
- Where there is contaminated land.
- Where the connection works are carried out in a dual carriageway.
- Where Lane Rental is imposed by a local authority.
- Where we are required to complete a road crossing.
- Where we are required to complete a bicycle lane crossing.
- Where construction of a water booster station or water pumping station (with or without land to accommodate it) are required.
- Where the requisitioned main may cross or impinge upon a dual carriageway, motorway or river.

5. New charging framework – examples

Within this section, we set out eight examples developments (four in the South Staffs region and four in the Cambridge region), comparing the current charging rules to the proposed new charges which will take effect from the 1 April 2018.

To aid understanding, we have also set out two of the examples in more detail. Note that these examples exclude connection charges which are not affected by the change in rules and all unit costs have been rounded to nearest £.

5.1 South Staffs region – five-plot development

In this example, it is assumed that the proposed development is for five properties which will all be built within one year. The cost of the on-site work is £8,000.

5.1.1 Mains requisition (direct to water company)

Under the **current charging rules**, if we carry out all of the work, we would charge the developer based on the DAD calculation (which works out at a charge of £358) with a fixed infrastructure charge of £365 per property connected (that is, $£365 \times 5$ properties = £1,825).

Therefore, the total amount the developer pays is $£358 + £1,825 = £2,183$.

Under the **new charging rules**, we calculate a cost per plot (which is the same for all developments) rather than the DAD calculation. We have worked this out by reviewing the historic average cost per plot over the last five years and is estimated at £779 per plot. An income offset is then applied, again based on the historic split over the past five years, which is 78.5%. Therefore, the cost per plot is $£779 \times (100\% - 78.5\%) = £167$.

Under the **new charging rules**, the infrastructure charge is now based on the projected costs of off-site reinforcement over the next five years. We have based this on expected developments (taken from local plans) and developer enquiries. This has been estimated at £8.4 million, which when divided by the 25,937 expected connections gives a charge of £325 per plot.

Therefore, the developer would now pay $(£167 + £325) \times 5 = £2,460$.

5.1.2 SLP

Under the **current charging rules**, if an SLP carries out all of the work, we would pay an asset payment based on the DAD calculation (which works out at a payment of £7,647). This would be offset by a fixed infrastructure charge of £365 for each property connected (that is, $£365 \times 5$ properties = £1,825).

From this would also be deducted any non-contestable costs (for example, mains commissioning costs). In this example, we have assumed that there are £1,000 of such costs.

Therefore, the total amount we would pay to the SLP is $£7,647 - £1,825 - £1,000 = £4,822$.

Under the **new charging rules**, we calculate a cost per plot (which is the same for all developments) rather than the DAD calculation. As set out above, the cost per plot is £779. An income offset is then applied based on the historic split over the past five years, which is 78.5%. Therefore, the cost per plot is $£779 \times 78.5\% = £612$.

Under the **new charging rules**, the infrastructure charge is now based on the projected costs of off-site reinforcement over the next five years. As set out above, this charge is £325.

From this would also be deducted any non-contestable costs (for example, mains commissioning costs). In this example, we have assumed there are £1,000 of such costs.

Therefore, we would now pay the SLP $(£612 - £325) * 5 - £1,000 = \underline{£435}$.

5.1.3 NAV

Under the **current charging rules**, in a NAV development, we would not carry out any of the on-site works (including any non-contestable work). Because of this, a NAV would not receive an income offset as there would not be any mains requisition costs to offset against it. So, the NAV would be charged a fixed infrastructure charge of £365 per property connected (that is, $£365 * 5$ properties = £1,825).

Therefore, the total amount a NAV would pay is £1,825.

Under the **new charging rules**, the same income offset received by SLPs would be applied to NAVs, which is calculated at £612 per plot.

Under the **new charging rules**, the infrastructure charge is now based on the projected costs of off-site reinforcement over the next five years. As set out in section 5.1.1 above this charge is £325.

Therefore, we would now pay the NAV $(£612 - £325) * 5 = £1,435$.

5.2 Cambridge region – 1,000-plot development

In this example, we have assumed that the proposed development is for 1,000 properties at a build rate of 100 a year. The cost of the on-site work is £500,000.

5.2.1 Mains requisition (direct to water company)

Under the **current charging rules**, if we carry out all of the work, we would charge the developer based on the DAD calculation (which works out at a charge of £72,632) and then a fixed infrastructure charge of £365 for each property connected (that is, $£365 * 1,000$ properties = £365,000).

Therefore, the total amount the developer pays is $£72,632 + £365,000 = £437,632$.

Under the **new charging rules**, we calculate a cost per plot (which is the same for all developments) rather than the DAD calculation. We have worked this out by reviewing the historic average cost per plot over the last five years and is estimated at £779 per plot. An income offset is then applied, again based on the historic split over the past five years, which is 78.5%. Therefore, the cost per plot is $£779 * (100\% - 78.5\%) = £167$.

Under the **new charging rules**, the infrastructure charge is now based on the projected costs of off-site reinforcement over the next five years. We have based this on expected developments (taken from local plans) and developer enquiries. This has been estimated at £8.4 million, which when divided by the 25,937 expected connections gives a charge of £325

Therefore, the developer would now pay $(£167 + £325) * 1,000 = £492,000$.

5.2.2 SLP

Under the **current charging rules**, if an SLP carries out all of the work, we would pay an asset payment based on the DAD calculation (which works out at a payment of £427,368) and this would be offset by a fixed infrastructure charge of £365 for each property connected (that is, $£365 * 1,000$ properties = £365,000).

From this would also be deducted any non-contestable costs (for example, mains commissioning costs). In this example, we have assumed there are £50,000 of such costs.

Therefore the total amount we would pay to the SLP is $£427,368 - £365,000 - £50,000 = £12,368$.

Under the **new charging rules**, we calculate a cost per plot (which is the same for all developments) rather than the DAD calculation. As set out above, the cost per plot is £779. An income offset is then applied based on the historic split over the past five years, which is 78.5%. Therefore, the cost per plot is $£779 * 78.5\% = £612$.

Under the **new charging rules**, the infrastructure charge is now based on the projected costs of off-site reinforcement over the next five years. As set out above, this charge is £325.

From this would also be deducted any non-contestable costs (for example, mains commissioning costs). In this example, we have assumed there are £50,000 of such costs.

Therefore, we would now pay the SLP $(£612 - £325) * 1000 - £50,000 = \underline{£237,000}$.

5.2.3 NAV

Under the **current charging rules**, if an NAV carries out all of the work, we would not undertake any of the on-site works (including any non-contestable work). Because of this, a NAV would not receive an income offset as there would not be any mains requisition to offset it against. So, the NAV would be charged a fixed infrastructure charge of £365 for each property connected (that is, $£365 * 1,000$ properties = £365,000).

Therefore, the total amount a NAV would pay is £365,000.

Under the [new charging rules](#), the same income offset received by SLPs would be applied to NAVs, which is calculated at £612 per plot.

Under the [new charging rules](#), the infrastructure charge is now based on the projected costs of off-site reinforcement over the next five years. As set out in section 5.1.1 above this charge is £325.

Therefore, we would now pay the NAV $(£612 - £325) * 1000 = £287,000$.

The table in section 5.3 below summarises some more worked examples to demonstrate how our proposed new framework compares with the existing one. We have used the infrastructure charges for 2017/18 to build up the costs in these examples.

5.3 New charging spectrum

Region	South Staffs				Cambridge			
	5 plots	10 plots	100 plots	1,000 plots	5 plots	10 plots	100 plots	1,000 plots
Number of plots	5 plots	10 plots	100 plots	1,000 plots	5 plots	10 plots	100 plots	1,000 plots
Build rate	5/year	3/year	20/year	100/year	5/year	3/year	20/year	100/year
Cost of on-site work	8,000	25,000	50,000	500,000	8,000	25,000	50,000	500,000
Mains requisitions								
Current charging								
DAD	358	10,852	2,178	61,636	1,197	12,784	2,644	72,632
Infra charges	1,825	3,650	36,500	365,000	1,825	3,650	36,500	365,000
Total cost to developer	2,183	14,502	38,678	426,636	3,022	16,434	39,144	437,632
New charging								
Cost per plot	167	167	167	167	167	167	167	167
Total on-site costs	837	1,675	16,749	167,493	837	1,675	16,749	167,493
Total off-site contribution (infra charge)	1,627	3,253	32,533	325,333	1,627	3,253	32,533	325,333
Total cost to developer	2,464	4,928	49,283	492,826	2,464	4,928	49,283	492,826
Change in cost to developer	281	(9,574)	10,605	66,190	(558)	(11,506)	10,139	55,194

Region	South Staffs				Cambridge			
	5 plots	10 plots	100 plots	1,000 plots	5 plots	10 plots	100 plots	1,000 plots
Build rate	5/year	3/year	20/year	100/year	5/year	3/year	20/year	100/year
Self-lay provider								
Current charging								
Asset payment	7,647	14,152	47,823	438,364	6,807	12,222	47,357	427,368
Less non-contestable costs	(1,000)	(2,700)	(10,000)	(50,000)	(1,000)	(2,700)	(10,000)	(50,000)
Less infra charges	(1,825)	(3,650)	(36,500)	(365,000)	(1,825)	(3,650)	(36,500)	(365,000)
Total net payment to SLP	4,822	7,802	1,323	23,364	3,982	5,872	857	12,368
Self-lay provider								
New charging								
Allowance per plot	612	612	612	612	612	612	612	612
Total on-site allowance	3,058	6,115	61,154	611,544	3,058	6,115	61,154	611,544
Less non-contestable costs	(1,000)	(2,700)	(10,000)	(50,000)	(1,000)	(2,700)	(10,000)	(50,000)
Less off-site contribution (infra charge)	(1,627)	(3,253)	(32,533)	(325,333)	(1,627)	(3,253)	(32,533)	(325,333)
Total net payment to SLP	431	162	18,621	236,211	431	162	18,621	236,211
Change in cost to SLP	4,391	7,640	(17,298)	(212,847)	3,551	5,710	(17,764)	(223,843)

Region	South Staffs				Cambridge			
	5 plots	10 plots	100 plots	1,000 plots	5 plots	10 plots	100 plots	1,000 plots
Build rate	5/year	3/year	20/year	100/year	5/year	3/year	20/year	100/year
NAV								
Current charging								
Non-contestable costs								
Total off-site contribution (infra charge)	1,825	3,650	36,500	365,000	1,825	3,650	36,500	365,000
Total net charge to NAV	1,825	3,650	36,500	365,000	1,825	3,650	36,500	365,000
New charging								
Non-contestable costs								
Total off-site contribution (infra charge)	1,627	3,253	32,533	325,333	1,627	3,253	32,533	325,333
Income Offset	(3,058)	(6,115)	(61,154)	(611,544)	(3,058)	(6,115)	(61,154)	(611,544)
Total net (payment) to NAV	(1,431)	(2,862)	(28,621)	(286,211)	(1,431)	(2,862)	(28,621)	(286,211)
Change in cost to NAV	3,256	6,512	65,121	651,211	3,256	6,512	65,121	651,211

5.4 Water efficiency opportunities

We are facing considerable water resources pressures in both our regions – mainly because of population growth and an increased number of connected properties. We are committed to providing water efficiency standards to all our customers, and consider that developers can play their part when designing and constructing new homes and buildings.

When new homes are built in the UK, developers must comply with Part G of the Building Regulations 2010. This states that any new homes must be built to provide no more than 125 litres of water per person per day (l/p/d). In addition, The Building Research Institute (BRE) has established recognised energy ratings for new developments – the [Home Quality Mark](#) (HQM) for housing and the [Environmental Assessment Method](#) (BREEAM) for high-rise residential developments.

We propose incorporating these ratings into our charges framework. So, if a developer commits to water efficiency levels of 100 l/p/d in each new-build development, for example, we would provide the following incentives.

- A 25% reduction in the applicable infrastructure charge for HQM-accredited properties.
- A 10% reduction in the applicable infrastructure charge for BREEAM-accredited properties with a 'Very Good' rating.
- A 25% reduction in the applicable infrastructure charge for BREEAM-accredited properties with an 'Excellent' rating.
- A 40% reduction in the applicable infrastructure charge for BREEAM-accredited properties with an 'Outstanding' rating.

There is a [water calculator](#) available to help developers select the most water efficient products to be installed in new properties and evaluate the total l/p/d. We think this should help them achieve our 100 l/p/d target.

We are committed to supporting developers to help them to build more water-efficient properties now and in the future. That said, we recognise that there may be conditions where customers remove water-efficient products or devices. So, we do not intend to recoup incentivised infrastructure charges if the customer chooses to remove any of the installations. This assessment will be carried out at the point of connection.

6. Transitional arrangements

We recognise that transitional arrangements are crucial when changing the way we charge customers. We are aware that moving to a new framework may cause uncertainty for developers, SLPs and NAVs – particularly in relation to buying land or developing a site.

From 1st April 2018, if an agreement has not been finalised and signed, we will use the new charging framework, given that it would be the only mechanism to charge from.

If you have applied and paid for a new water main, but the work has not yet begun by 1st April 2018, then we will make a replacement offer under the new charging framework, subject to agreement.

7. Communicating with us

We will be finalising our new charging framework over the next few months, and welcome your feedback to this consultation as an important stage in our plans for our networks moving forward.

You can email your responses to Developerforum@south-staffs-water.co.uk or post them to:

Developer Forum Feedback
South Staffordshire Water plc
Green Lane,
Walsall
WS2 7PD

The closing date for this consultation is **29th January 2018**.

Note: In developing this consultation, we have carried out considerable detailed historical data analysis, which could be subject to additional refinement. At the time of writing, we have not completed our assurance. This means that some of our assumptions cannot be taken as absolute at this stage.