Northern Ireland Assembly

COMMITTEE FOR REGIONAL DEVELOPMENT

OFFICIAL REPORT
(Hansard)

Water and Sewerage Services (Amendment) Bill

11 November 2009

NORTHERN IRELAND ASSEMBLY

COMMITTEE FOR REGIONAL DEVELOPMENT

Water and Sewerage Services (Amendment) Bill

---

11 November 2009

Members present for all or part of the proceedings:
Mr Fred Cobain (Chairperson)
Miss Michelle McIlveen (Deputy Chairperson)
Mr Cathal Boylan
Mr Willie Clarke
Mr Tommy Gallagher
Mr Danny Kinahan
Mr Raymond McCartney
Mr Ian McCrea
Mr Brian Wilson

Witnesses:

Mr Adrian Arbuthnot	)	Department of Finance and Personnel
Mr Richard Pengelly	)	

The Chairperson (Mr Cobain):
The meeting will consist of two evidence sessions; one from the Department of Finance and Personnel (DFP), and one from the Northern Ireland Public Service Alliance (NIPSA). Included in members' packs is a letter from NIPSA — which the Committee looked at during its meeting on 4 November — detailing its concerns about the Bill, and requesting an opportunity to give evidence to the Committee. No written submissions have been received from either DFP or NIPSA.

I remind witnesses and those in the Public Gallery that the session is being recorded by

Hansard, and, therefore, mobile phones must be switched off completely and not running on silent.

With us today is Richard Pengelly and Adrian Arbuthnot. Richard, perhaps you can make your presentation and then I will open up the meeting to questions.

Mr Richard Pengelly (Department of Finance and Personnel):
The Committee has helpfully forwarded me a list of some of the issues that it wants to explore. Given that time is short, perhaps we could move straight to the questions rather than delay proceedings with a long opening statement.

The Chairperson:
Yes, that would be helpful.

The Department for Regional Development (DRD) is asking the Committee for permission to extend the period of the non-payment of water rates. As you know, the non-payment period runs out on 31 March 2010, and the Department needs additional powers from 1 April 2010. To give the Committee a feel for the background to that, can you give us some indication of the financial outcomes if the Department exercises that position?

Mr Pengelly:
The power that will be conferred by the Bill is an enabling power, and, as such, does not preclude the introduction of water charges at some point. However, any previous plans by the Executive to introduce water charges were on a phased basis. The original plan would have had full charging in place at a designated point in time, but that will no longer be the case.

You asked about the financial implications. A key point is that expenditure plans exist only up to 2010-11. Therefore, we can talk with any certainty about numbers only until then. Beyond that there needs to be a further Budget process and further work with DRD and Northern Ireland Water (NIW) to quantify the precise cost implications.

We are going backwards to go forward. The three-year Budget, which was approved by the Executive and the Assembly in January 2008, covered the period 2008-09 until 2010-11, and assumed that the phased introduction of water charges would be in place from April 2009.

Subsequently, in November 2008, the Executive decided to defer water charges. The cost implications for 2009-2010 were dealt with as part of the in-year monitoring process.

We are at the stage in which, in reality, water charges will not be in place in 2010-11, and that has as much to do with logistical reasons as it does with the Executive's position. Indeed, the Executive have still to debate that issue.

The financial implications for 2010-11 for current expenditure will be £120 million, and, for capital investment, £93 million. That is revenue that we had assumed would be available and which will not be because water charges are not in place. In the absence of charging, the financial implications will be of that magnitude rolling forward into 2011-12 and beyond. Until the Budget process is refreshed, we do not have those funds.

I know that DRD has talked about a figure of about £1 billion during the period 2010-13. That is internal work that the Department has done based on NIW's business plan; however, as yet, it has not formally presented us with a figure.

The Chairperson:
The introduction of water charges was to be done through a phased process, beginning with one-third charging, two-thirds charging and then full charging. Do you know how much the subsidy for the one-third and two-thirds charging was?

Mr Pengelly:
I do not have the exact figure.

The Chairperson:
The figure that you mentioned of about £100 million does not bear any relation to what the Department is telling us about the full implications of non-charging.

Mr Pengelly:
Is that by reference to the £1 billion?

The Chairperson:
No. The Department has not mentioned the figure of a £100 million subsidy for Northern Ireland

Water to cover the complete non-charging of water. We were told that that subsidy would be about £250 million.

Mr Pengelly:

The assumption was that one-third charging would be in place in 2009-2010; two-thirds charging in 2010-11; and full charging in 2011-12. That was the original plan. Another complication about 2010-11 is that, in parallel with the phased introduction of water charges, there was to have been an offset to the regional rate, because there was to have been full recognition of the contribution to water and sewerage charges through the regional rate. The decision not to introduce water charging would have reduced the regional rate, but the regional rate will not now be reduced in 2010-11, as was originally planned.

The Chairperson:

Sorry, explain that to me. Will there be no reduction in the regional rate in 2010-11?

Mr Pengelly:

No, because that reduction was to recognise and offset the introduction of water charging. It was to have recognised the contribution to water charges made through the regional rate. If water charging is not in place in 2010-11, there need not be a reduction that year.

The Chairperson:

I do not think that the public will understand that sleight of hand, Richard. I thought that the Minister of Finance and Personnel told everyone that they were going to be £161 better off, which was the notional amount that they pay for water in the regional rate.

Mr Pengelly:

The average contribution to water through the regional rate is about £160 per household.

The Chairperson:

A lot of people were told that they were going to be better off by that amount. No one mentioned that if water charges were not introduced that the £160 saving would be taken back off them. When was that decided?

Mr Pengelly:

It was part and parcel that at the point that water charges were introduced, there would be a reduction in the regional rate offset by that introduction, so the two were very much paired.

The Chairperson:

Therefore, are you saying that no water charging equals no rate reduction?

Mr Pengelly:

Yes.

The Chairperson:

OK. That clears that up. Those are the financial issues. What about the negotiations that the Department is having with the Treasury about VAT and the reclassification of Northern Ireland Water? What are the financial implications of those issues?

Mr Pengelly:

VAT is not a Treasury matter; rather, it is an issue between Northern Ireland Water and Her Majesty's Revenue and Customs. We are not engaged in that at all. That is an issue involving DRD and Northern Ireland Water. They periodically update my Department on that.

The Chairperson:

So, it is not a Treasury issue?

Mr Pengelly:

That is correct; it is a matter for Revenue and Customs. The classification is determined by the Office for National Statistics (ONS). The original classification as a Government-owned company (Go-co) was predicated on charging being applied. A Go-co must generate its own revenue stream, which was fine when water charging was planned. With the deferral of charging, ONS revisited that and determined that Northern Ireland Water was not a Government-owned company; it is, effectively, a non-departmental public body (NDPB). That will remain the case unless and until the introduction of water charging.

The Chairperson:

What are the financial implications of that?

Mr Pengelly:

The main issue involves what we call non-cash costs — the cost of capital and depreciation. The cost of capital is by far the most significant element of that. In parallel, the Treasury has reviewed the overall public expenditure framework, and from 1 April 2010, it is abolishing cost of capital. Therefore, after 31 March 2010 that issue goes from being very significant to disappearing. Although the classification exposes Northern Ireland Water to cost of capital, because that issue is being abolished by the Treasury —

The Chairperson:

Are there any residual costs up until 2010?

Mr Pengelly:

The previous agreement was that the Treasury would absorb the cost of capital implications for 2009-2010.

The Chairperson:

Therefore, are there no financial implications at all involved in reclassification?

Mr Pengelly:

Not for cost of capital. The main implication of the classification is the creation of some flexibility. What scores in the Executive's Budget for a Go-co is the amount of money that DRD would pass to Northern Ireland Water. As a non-departmental public body, what scores is the amount of money that Northern Ireland Water spends on providing services. There is significantly more flexibility in that, as a Go-co, the company could build up some reserves that would provide it with the flexibility to deal with exceptional circumstances. As an NDPB, even if it accumulates reserves, at the point that it spends them it would have an effect on public expenditure.

The Chairperson:

Basically, there are no financial implications.

Mr Pengelly:

Now that we have addressed the cost of capital —

The Chairperson:

Are there any physical costs to Northern Ireland?

Mr Pengelly:

The balance between current expenditure and capital expenditure changes, but in global terms, it is broadly the same. There are some tweaks around the margins, but —

The Chairperson:

Are we talking about what happens around the margins? We are not —

Mr Pengelly:

We are not talking about fundamental change. The linked issue is the asset valuation, that is, the valuation of Northern Ireland Water's asset base.

The Chairperson:

Was it £700 million, and we are now up to £5 billion?

Mr Pengelly:

It was £6 billion when it was an agency, before it became Northern Ireland Water. At that point, it was classified as a Go-co. In technical terms as an agency, the asset base had to be valued by reference to depreciated replacement costs, that is, how much it would cost to recreate the water and sewerage infrastructure. As a Go-co, the model is valued by how much cash the assets can generate, which is the charging stream. It originally reduced, at the point of the creation of Northern Ireland Water, to £850 million. That has crept up to approximately £1 billion because of the investment programme that has been put in place.

My colleagues in DRD who are accountants, and who are examining that issue, are still confident that the £1 billion valuation is correct. We still the view the classification as an NDPB as an interim measure. We do not want to carry out a wholesale revaluation of Northern Ireland Water until there is a formal Executive consideration of the way forward for the company. My DRD colleagues are content that, in accounting terms, the £1 billion remains valid.

The Chairperson:

Is the Treasury happy with that?

Mr Pengelly:

We have not discussed the issue in detail with the Treasury. There is no need to seek Treasury approval at this time. The valuation is one that the Northern Ireland Water and DRD accounting officers came to, and which is subject to audit.

The Chairperson:

I want to be absolutely clear about that. Are you saying that the Treasury has not been consulted about any of this?

Mr Pengelly:

That is correct. The work that is being done is undertaken in the context of the framework that was established by the Treasury.

The Chairperson:

So, there has been no direct contact with the Treasury?

Mr Pengelly:

There is no need. We would speak to the Treasury only to seek an exemption.

The Chairperson:

I just wanted to get the point absolutely clear that there have been no discussions with the Treasury.

Mr Pengelly:

The last discussion involving the Treasury and Northern Ireland Water took place around November 2008, when the Treasury agreed to pick up the burden of the cost of capital. There has been no direct engagement since then.

The Chairperson:

OK. Good.

Mr Gallagher:

I want to look to April 2010 and onwards, and to the possibilities that the legislation might cater for. We can go on as we are, or make a decision to introduce direct charging. If charges were to be introduced in April 2010, how would they be set? Would it be at the one-third level or the two-thirds level, since we are a year late? Could charges be set at the full value? Links were being made between the two levels anyway. There is the possibility of a rates discount in lieu of customer charges. If charges are brought in at that level in April 2010, will there be a corresponding discount in the rates from April 2010?

Mr Pengelly:

The short answer is that the decision on when and how to introduce water charges in the future is for the Executive to determine. The Executive have not yet received a paper. Looking backwards —

Mr Gallagher:

Many things are happening in the background. The Minister for Regional Development has not ruled that out, and the Minister of Finance and Personnel indicated that he cannot run his Department without the introduction of water charges.

Mr Pengelly:

I cannot say for certain what the Executive may do in the future. However, I can clarify the clear principles that the Executive established in January 2008 when they took the decision to introduce water charges. One principle was that the move to water charging would happen on a phased basis. Given that, it is exceptionally unlikely that we will move from no charging to full charging. The transition would be managed over a period of years. The Executive will determine whether to charge one or two thirds of the full charge or whether to extend the phasing period.

Furthermore, the Executive took a clear decision to fully recognise the existing contribution to the provision of water and sewerage services through the regional rate. When water and sewerage charges are introduced, there was to be a compensating reduction of about £160 per household to the domestic regional rate.

Mr Gallagher:

Perhaps I did not pick you up correctly; I thought that you said that the rates are already fixed for

April 2010 to March 2011? Can they be changed?

Mr Pengelly:

The Assembly passes a piece of legislation annually in January or February that strikes the rate. The Executive have planned for that as part of the Budget process. In January 2008, the plan was to offset the reduction in the regional rate, because water charges were supposed to be in place in 2010-11. However, the legislation for that year needs to go through in early 2010. Given that there are no water charges, the compensating reduction is not required. That will not impact on household bills or the amount of money that is available to the Executive for public services; we will remove a plus and a minus to leave a neutral position.

The Chairperson:

Have you taken the notional figure of £161 reduction in the regional rate back in? That will not cover the costs of Northern Ireland Water. Who will cover the shortfall?

Mr Pengelly:

The Executive will need to find that shortfall.

The Chairperson:

How much is the shortfall?

Mr Pengelly:

I do not know the exact figure. However, I think that, in broad terms, the full cost of water and sewerage services per household is in the region of £330. A recognised contribution of about £160 is made through the regional rate. The Executive will need to find the difference.

The Chairperson:

It will be even more than that, because if you put the money back into the regional rate, people who claim passport benefits will pay nothing. They will pay something towards water charges. How much will they pay?

Mr Pengelly:

There is a differential impact at household level. The £160 per household translates into about £109 million of total revenue. That £109 million, which is the existing contribution through the regional rate, will not cover the full cost of running Northern Ireland Water. The balance would have been funded through charging.

The Chairperson:

It is about £200 million?

Mr Pengelly:

Yes, that is the ballpark figure. Given that charging is not in place, the Executive need to make a contribution.

The Chairperson:

A contribution of £200 million.

Mr Pengelly:

I quoted £120 million and £93 million because a subsidy was intended to be in place in 2010-11 to account for the lack of full charging. Those two figures represent the additional provision that is needed to reach that sort of figure.

The Chairperson:

You said that charging will be phased in. Even if we charge one third of the overall charge, people who are on passport benefits will not pay anything.

Mr Pengelly:

That is right.

The Chairperson:

Therefore, not everyone will pay regional rates, but everyone will pay water charges. The Executive need to find £200 million or more.

Mr Pengelly:

In the context of no charging, that is correct.

Mr Kinahan:

I am not sure that I fully understand. How much lead-in time is required before charging can be introduced? Is it a year or six months?

Mr Pengelly:

I think that it will take between six months to a year; however, that is really a question for Northern Ireland Water and DRD, because will they manage the introduction.

Mr B Wilson:

I have been trying to reconcile the figures that you provided with the previous figures that we received, and I am beginning to get clarification. You said that the Executive's current expenditure in 2010-11 will be £120 million plus £93 million and that they will get £109 million in revenue from the regional rate. Therefore, had the original plan been in place, would the total revenue for 2010-11 be £109 million plus the amount generated from two-thirds charging?

Mr Pengelly:

It is much easier to talk in broad terms. In 2010-11, the sums of £120 million and £93 million for current expenditure and capital investment respectively relate to the ongoing running costs of Northern Ireland Water and a capital investment programme. It costs approximately £300 million to run Northern Ireland Water. Therefore, the plan was for two-thirds charging to be in place by 2010-11 to generate approximately £200 million in revenue and for the Executive to provide £100 million in existing financial cover.

Mr B Wilson:

Is that revenue from the regional rate?

Mr Pengelly:

Of the £200 million in revenue from charging, £100 million is the offset from the regional rate and about £100 million is from additional bills to households. Even if there is no charging in 2010-11, that £100 million Executive contribution will already have been made. Given that the regional rate has not been reduced, we are still receiving that revenue. That leaves a balance of about £120 million, which is the additional subsidy that needs to go to Northern Ireland Water that year.

Mr B Wilson:

What about the capital costs?

Mr Pengelly:

Some of the revenue from charging would have been used to cover the capital investment programme. Therefore, there is a need for revenue because charging is not in place. It is hugely technical. Part of the water bill covers non-cash costs for operating costs that do not have a cash outflow so that that money is available to finance capital investment. It is easier if we focus on the current expenditure side to get a sense of what is happening.

Mr McCartney:

The Bill has been described to the Committee as a technical Bill. Does the Bill interfere with or have any implications for the procedure to provide funding to the company?

Mr Pengelly:

The Bill is technical in nature, because it provides the legislative authority for DRD to continue to make a payment to Northern Ireland Water in the absence of charging. The substantive consideration for the Executive and the Assembly is whether charging should be in place. The Executive made a formal decision in November 2008 not to proceed with charging. There has not been a formal consideration of the position for 2010-11; however, given that it is November 2009, it will not be logistically possible to have bills in place for 2010-11. That is a financial issue.

The Executive have been discussing the financial position for 2010-11 over the past couple of weeks. Making good that shortfall is one of the key considerations for the Executive. There will be a Budget process next year, and the question over the introduction of water charges will once again be a substantive issue for the Executive to consider and to work through with members at Assembly Committees and plenary sessions.

Mr McCartney:

The Bill, as framed, will not —

Mr Pengelly:

It certainly will not preclude the introduction of water charges.

Mr McCartney:

What I am trying to say is that you do not wake up one day and decide that the only thing to do as a result of the Bill is —

Mr Pengelly:

No, not at all.

Mr McCartney:

Are you, therefore, saying that the Executive makes that decision?

Mr Pengelly:

Absolutely.

Mr McCartney:

If the Bill is agreed to, is there any timeline for when a decision on VAT must be made, or is that an issue that the water company must consider?

Mr Pengelly:

That is something about which the water company is speaking to Revenue and Customs.

The Chairperson:

I want to make sure that we are absolutely clear about this: is it too late to charge for water in 2010-11? Are we past that stage?

Mr Pengelly:

That is what colleagues in DRD tell us.

The Chairperson:

That is what they tell us also. I wanted to get that absolutely clear. Will the Bill give power to the Executive to introduce water charges in 2011-12?

Mr Pengelly:

Yes.

The Chairperson:

This is all hypothetical, and we are not holding you to this. Do you think that it is unlikely that in 2011-12, the Department will go from no charging to full charging?

Mr Pengelly:

Based on what the Executive have done in the past, I think that that is correct.

The Chairperson:

So, will it probably be a phased approach?

Mr Pengelly:

Yes.

The Chairperson:

If it will be a phased approach, we are talking about more than £200 million. Say we charge one third, two thirds and then the full amount, which could be in 2014-15 or 2015-16. In the first instance, if the plan that as set out is adopted in 2011-12, which is to charge one third and then two thirds, will the Department or the Executive provide two thirds of the costs of water, with the third coming from customers?

Mr Pengelly:

Yes.

The Chairperson:

Would that be more than £200 million?

Mr Pengelly:

Yes.

The Chairperson:

Is the capital cost on top of that?

Mr Pengelly:

Yes.

The Chairperson:

If there is no water charging, will the notional figure of £161 that is deducted from the regional rate be recharged?

Mr Pengelly:

Yes. That has continued to be charged. It was originally due to be offset in 2009-2010. That was the first year that water —

The Chairperson:

Is it correct that if there is no water charging, there will be no reduction in the regional rate?

Mr Pengelly:

That is correct.

The Chairperson:

OK. Thank you very much.