

## Foreword

This report sets out my determinations of price limits for the water and sewerage companies in England and Wales from April 2005 to March 2010. They have been prepared in accordance with all of my statutory duties. They are the product of careful collective consideration within Ofwat. They are therefore referred to throughout this report as 'our' determinations. The non-executive advisory directors on the Ofwat Board have been party to the process and they support the outcome.

We have made judgements about what resources each company needs to finance and carry out its functions properly, assuming that it improves its efficiency year by year in line with our efficiency factors. We have taken account of the interests of customers and of the wider environment. Although the price limits run only to 2010, we have reflected in them the need for the water industry to continue to provide essential water services for the foreseeable future.

We have taken as our starting point each water company's final business plan. In reaching our view we have been helped by the guidance given by the Secretary of State for Environment, Food and Rural Affairs for England and the Welsh Assembly Government for Wales; by research jointly undertaken with other stakeholders on customers' views and priorities and submissions from the WaterVoice Committees; by work undertaken by the Drinking Water Inspectorate, the Environment Agency, English Nature and the Countryside Council for Wales on the outputs required of the companies; by the work of the independent reporters for each company; and by the reports of a number of consultants commissioned by Ofwat and by other stakeholders.

We published for consultation our draft determinations in August so that the companies and other stakeholders could consider them and make their representations. I met each WaterVoice Committee and each company to understand their concerns. Ministers provided final guidance, endorsing the inclusion of some discretionary work for England and confirming the exclusion of further work in Wales. The quality regulators, the Environment Agency, English Nature and the Drinking Water Inspectorate have had full access to our detailed decisions to enable them to help us clarify future work programmes.

We have considered all of the representations made on our draft determinations and have taken them, together with the most up-to-date factual information available to us, into account in our final determinations.

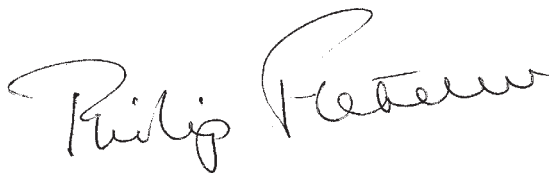
We judge that an increase in price limits is essential to maintain the progress in service quality and performance which has already been achieved and to make the further advances required. The price limits are as high as they need to be to enable each company to provide these services. But they are no higher than they have to be for customers, who in general have no choice about their supplier. Our price limits have been prepared on a consistent basis, but do take account of each company's circumstances and accordingly vary considerably from one company to another.

In general terms we are content with the strategies proposed by companies. However, following scrutiny and challenge we consider that the companies have in general tended to overestimate the costs of their strategies and underestimate the scope for further improvements in efficiency. This challenge explains why we have been able to determine price limits that are only around two-thirds of the increase that companies sought.

In conducting the review, we have adopted a transparent process. We have followed the methodological approach that we set out in March 2003. We have explained our reasoning in general terms in this report, supplemented by a confidential, detailed report that we have provided to each company.

Inevitably during 2005 to 2010 there will be new challenges to meet. Each company's licence has provisions for interim price limit reviews in cases where there are specific material changes in circumstances that are not reflected in our determinations. We have taken a neutral stance on interim price reviews, neither allowing contingencies in price limits for future changes nor setting our assumptions and expectations at levels that presuppose the need for interim reviews.

Each company must decide by 1 February 2005 if it wants me to refer its determination to the Competition Commission for redetermination. Whether or not a reference is made to the Competition Commission, our determinations will apply to the charging year beginning 1 April 2005. The Competition Commission would review all the available evidence in reaching its own determinations, which could lead to changes to the price limits we set for those companies that appeal.

A handwritten signature in black ink, reading "Philip Fletcher". The signature is written in a cursive, flowing style with a large initial 'P'.

**Philip Fletcher**  
**Director General of Water Services**