

# Periodic review 2004

October 2003

Newsletter

## Setting water and sewerage price limits for 2005-10: Overview of companies' draft business plans

The PR04 Newsletter reports on the events, public statements, analysis and summaries that take place at key stages of the 2004 review of water company price limits.

At the start of phase two of the review process, we asked each company to develop a draft business plan, setting out its preferred strategy for the five years 2005-10. To help us make accurate comparisons, we also asked the companies for reference plans based on a set of common assumptions provided by Ofwat. The purpose of these reference plans was to give Ofwat an indication of the prospects for price limits of a range of quality and environmental outputs.

Each company published a summary of its proposals at the end of August. We are now working with the companies, the quality regulators and Government in preparation for the later stages of the review. Our views of their draft plans will enable companies to present better final plans next year.

It is too early to say what the outcome of the review will be. But hard choices will have to be made about the size of the expenditure programmes the companies are expected to carry out if we are to set price limits that are recognised by customers generally as appropriate and necessary.

There is a clear challenge to water companies to show that their plans represent value for money for the customer and that they are properly sharing the risks. And there is a clear challenge to the quality regulators seeking major water quality and environmental improvements to fully justify them.

Ministers will also have some difficult decisions to make on whether all of the proposed drinking water quality and environmental improvements are essential, and on the pace of delivery of those they agree are needed.

If the programmes of works that each company will be expected to deliver remain unchanged from those set out in the draft business plans then there can be little doubt that water bills will need to rise substantially.

The price limits that we set will need to be sufficient to allow each company to finance its obligations on a long-term and sustainable basis. But they shall be no higher than is necessary in order to protect the customers of these monopoly companies.

Most companies are proposing a significant increase in the first year of the new price limits and smaller

changes thereafter. Others are proposing a more even increase across the whole period. The majority of companies are seeking increases in average household water bills of 30% or more over the five years. Only one company is proposing a rise of less than 10% (Tendring Hundred). Rises in average household sewerage bills range from less than 20% (Thames, Wessex and Yorkshire) to 50% or more (United Utilities).

Taking all the companies' forecasts together, average water bills would increase by £32 in real terms between 2004-05 and 2009-10, and sewerage bills by £40 ( £72 in total). Improvements to water quality and the environment account for almost half of this increase, whilst companies' proposals for capital maintenance account for a further third.

### Key issues from the companies' draft business plans

The table below shows what is driving the changes in bills in England and Wales. For a more detailed account of the key issues, published in our document, 'Setting water and sewerage price limits for 2005-10: Overview of companies' draft business plans', [click here](#).

Average household bills in 2004-2005		£234
Less	(1) past efficiency savings and outperformance	(8)
	(2) scope for reduction through future efficiency improvements	(10)
Plus	(3) maintaining base services	37
	of which (a) changes in revenue	3
	(b) changes in operating costs	6
	(c) changes in capital maintenance	19
	(d) impact of taxation	9
	(4) maintaining security of supplies to all customers	12
	(5) the impact of improvements in services	41
	of which (a) drinking water quality	10
	(b) environment	26
	(c) service performance	5
Average household bill in 2009 – 2010		£306

### Next steps

We will be meeting each company in November or December 2003 to provide feedback on and discuss its draft business plan.

We will all need to test the priority and value of the proposed improvements. Our early analysis shows that there will be hard choices to make if we are to limit the cost pressures faced by companies and set price limits that are affordable. Unless the scale and pace of the proposed outputs are changed, customers will face very significant increases in bills in order to pay for them.

**Here is a timetable highlighting key events in the price review timetable.**

The project is being managed in four phases:

**Phase 1 - Complete**

**Phase 2 - Assessment of draft business plans and market research**

**Phase 3 - Decisions and determinations**

**Phase 4 - Implementation of price limits and evaluation of price review**

Phase 1	15-Oct-02	Publish our proposed approach – ‘Setting price limits for 2005-10: framework and approach’
	Oct-02	Publish consultation on draft business plan reporting requirements.
	Nov-02	Publish results of joint market research into customers’ views
	14-Jan-03	Consultation on ‘Setting price limits for 2005-10: framework and approach’ ends.
	21-Jan-03	Ministers issue initial guidance on the possible quality programme for 2005-10 and other issues (March 2003 for Wales).
	27-Mar-03	Publish our final approach – ‘Setting water and sewerage price limits for 2005-10: Framework and approach’.
Phase 2	Aug-03	Companies submit their draft business plans to us and publish summaries of these, including their proposed price limits.
	Today	We are providing an overview on issues emerging from companies’ draft business plans.
	Dec-03	We submit advice on company draft business plans to Ministers.
	Jan-04	Ministers give their principal guidance on the required quality programme.
Phase 3	Apr-04	Companies submit their final business plans.
	Jul-04	We consult on draft determinations of the price limits the companies will need.
	Sep-04	Ministers have the opportunity to fine-tune their decisions on required quality programmes.
	Nov-04	We publish the final price limits.
Phase 4	Apr-05	New price limits come into effect.

*The approach papers, ‘Setting water and sewerage price limits for 2005-10: Framework and approach’, and ‘Overview of companies’ draft business plans’ are available on our website, together with other relevant documents.*

For further information contact [enquiries@ofwat.gsi.gov.uk](mailto:enquiries@ofwat.gsi.gov.uk)

This is the third in a series of newsletters that we will publish to keep you informed about the key stages of the price review.