



OFWAT BOARD

Meeting held on Thursday 23 January 2014 (by telephone conference)

Members in attendance

Chairman:

Jonson Cox

Chief Executive:

Cathryn Ross

Non-executive directors:

Penny Boys

Wendy Barnes

Chris Burchell

Catherine Farnish

Robin Paynter Bryant

Martin Lawrence

Catherine Waddams

Executive directors:

Sonia Brown

Richard Khaldi

Keith Mason

In attendance:

Noel Beale

(Director of Legal Services) – all items

Dan Mason

(Assistant Board Secretary) – minutes

David Black

(Director of Economics)

Graham Taylor

(City Advisor)

Antony Cook

(PwC)

Stuart Cook

(PwC)

Nick Forrest

(PwC)

Claire Simpson

(Strategic Assistant to the Chief Regulation Officer)

Mathew Stalker

(Principal Economist)

1. PR14 risk and reward pre-qualification guidance

- 1.1 The Executive presented to the Board a number of proposals around issues to be included within the forthcoming risk and reward guidance, which is to be published on 27 January.

- 1.2 In particular, the Executive presented to the Board a recommendation on the strategic range for the weighted average cost of capital (WACC), further to discussions at the November and December Board meetings.
- 1.3 The Board agreed to the proposed range, noting that the range had been derived from appropriate market observations and regulatory precedent.
- 1.4 The Board discussed the issue of financeability. The Board noted Ofwat's statutory duty to enable efficient companies to finance their functions on the basis of a notional capital structure. The Board also noted that responsibility rests with the companies to manage their businesses – including through the use of the additional levers available to them in this price review – to secure financeability.
- 1.5 The Executive presented to the Board a recommendation around the appropriate point estimate for the Appointee level WACC to be included in the risk and reward guidance. The Executive noted that the figure proposed was different to that included within the recommendation paper, and that this was a result of further analysis that had been undertaken. In particular, the Executive highlighted that arriving at a point estimate within the range would contain an element of expert regulatory judgement, and that this should be considered within the context of the benefits it is intended to drive. The Executive also noted to the Board the assumptions made around tax when arriving at the proposed WACC.
- 1.6 The Board agreed to the proposed point estimate and acknowledged that this includes an element of judgement. The Board also noted that the proposed point estimate of the appointee level WACC, in conjunction with the latest available evidence on outcome delivery incentives, allowed scope for outperformance.
- 1.7 The Executive updated Board on emerging thinking around the level of the retail household margin. As a result, the Executive proposed a change within the specific range for the retail household margin. The Board agreed to delegate decision making authority to the Chief Regulation Officer for this issue, noting the implications for the wholesale WACC.
- 1.8 The Executive presented a proposed approach to Board around the consideration of companies who are seeking a small company premium. The Board agreed to the proposed approach.
- 1.9 The Board discussed the proposed communications and engagement strategy around the publication of the risk and reward guidance. The

Board in particular noted the importance of the input from Customer Challenge Groups in this process.

2. Any other business

2.1 There was no other business.

Dan Mason
23 January 2014