

23 December 2013

Dear Regulator,

I am writing to let you know about a change that Ofwat is making to our PR14 delivery plan. In addition, following on from the Information Notice we published in November - '[2014 price review – companies' compliance with statutory obligations](#)', I am also seeking your organisation's views on whether there are any outstanding material issues that have arisen since business plans were submitted and which affect companies' compliance with statutory obligations (for example new enforcement action).

Given the change we are making to our PR14 delivery plan (which I explain below), we need to bring forward the date of response to this letter from 1 March 2014 to 14 February 2014. It is important that we receive a response by this new date so that our Board can take any new information into account before making decisions on whether individual companies pre-qualify for enhanced status.

### **Change to PR14 delivery plan**

Since 2 December, we have been busy analysing the business plans and accompanying data. Our teams' initial analysis has highlighted a number of areas where we require further information. It has also shown that companies' views on risk and reward are not in alignment with market evidence for the water sector.

For these reasons we are going to extend our query process and remove default tariffs from the risk based review. In addition we are also going to introduce a change to our process, which will work as follows:

- On January 27 we will publish guidance on risk and reward.
- We propose to pre-qualify companies for enhanced status if their business plans pass our tests for outcomes, costs and affordability and demonstrate robust board assurance. The pre-qualification results and reward for enhancement will be published on 10 March.
- At this point we will invite the Boards of pre-qualifying companies to accept our published guidance on the risk and reward. If they do they will gain enhanced status. If they don't they will be classified as standard.

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The remaining companies will receive the outcome of the risk based review on 4 April as planned.

Further information, including an updated plan is also available on our [website](#).

## **Compliance with statutory obligations**

On 12 November we published an Information notice - '[2014 price review – companies' compliance with statutory obligations](#)'. This note confirmed our approach, first set out in our published methodology, to assessing whether companies' plans appropriately demonstrate compliance with statutory obligations. This made it clear that companies must meet their current and future statutory obligations.

This notice explained that we expected the environmental and drinking water quality regulators to highlight in each Customer Challenge Group (CCG) report whether or not a company had provided adequate assurance that it will meet its future statutory obligations. I would like to take this opportunity to thank you for providing your views via these reports and the very important roles you played as members of the CCGs.

The information notice also explained that we recognise the status of issues may change during our risk based review. For example, another regulator may decide to take enforcement action against a company for its current performance. For this reason we committed to write to each regulator that has specific enforcement action powers in December to:

- Identify those companies that state their plan allows full compliance with statutory obligations; and
- Ask each regulator to confirm to us that since each company submitted their plan there are no new or outstanding enforcement (or other material) issues that have come to light relating to those companies.

All 18 companies that submitted their business plans on 2 December have stated that their proposed plan will ensure compliance with statutory obligations. We still need to consider in more detail the level of assurance provided – including Board assurance and the views of the environmental and drinking water quality regulators – to determine whether companies have provided adequate assurance in order to pass our risk based review tests.

Before making recommendations to our Board on whether individual companies pre-qualify for enhanced status, we would like to know of any unresolved issues that you are aware of - for any company - which are:

- material and which could affect their compliance with statutory obligations; AND

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- which have come to light since business plans were submitted (meaning your organisations were therefore not able to raise them in the CCG forum).

Before you flag this to us, I would be grateful if you could speak to the relevant company in the first instance. This will give the company the chance to respond to your concern. If this does not resolve the issue, then I would be grateful if you could write to me and explain what the issue is by 14 February 2014.

Given the tight timetable we cannot commit to reflect any new information received in our risk based review tests for companies that are classified as standard or resubmission. For these companies there will be further opportunities for the other regulators to engage after we publish the results of the risk based review on 4 April and before companies submit revised versions of their plans by 27 June. Resubmission companies will require fresh engagement with their CCG and a statement to accompany their resubmitted plan. If a company classified as standard decides it is not appropriate to engage their CCG and makes revisions to its plan that could affect compliance with statutory obligations, then we will expect a statement from the relevant environmental and water quality regulators to accompany their revised plan.

Clearly for companies likely to pre-qualify for enhanced status, we will commit to take your response into account before making final recommendations to our Board. We will not classify a company as enhanced if it fails to adequately demonstrate that its plan will meet its future statutory obligations.

If you have any questions about this process I would be grateful if you could contact your Portfolio Lead.

Finally may I take this opportunity to thank you for your on-going support and I wish you and your staff a happy Christmas.

Yours sincerely,

**Sonia Brown**  
**Chief Regulation Officer**

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