

April 2019

Trust in water

PR19 draft determinations: South West Water – Securing cost efficiency actions and interventions

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Following our initial assessment of plans, we categorised two types of actions for fast-track companies:

- agreed actions that fast-track companies committed to implement to ensure that their plans meet the threshold for fast-track status; and
- required actions for companies which in general were required for draft determinations (or final determinations for some aspects of past delivery).

Table 1 below sets out the agreed and required actions, a summary of the company's response to the action, our assessment of the company's response, and any further interventions we are making as part of the draft determination.

Each action has a unique reference. The prefix 'SWB' denotes the company South West Water. The central acronym references the test area where the action has been identified, please see the 'PR19 draft determinations: Glossary' for a key of these acronyms. Actions whose numbers are preceded with an 'A' denote agreed or required actions.

Table 2 below sets out any further interventions that are not resulting from an action, which we are making as part of the draft determination.

Each further intervention that is not resulting from an action has a unique reference. The prefix 'SWB' denotes the company South West Water. The central acronym references the test area where the action has been identified, please see the 'PR19 draft determinations: Glossary' for a key of these acronyms. Intervention numbers are preceded with a 'C'.

For all other documents related to the South West Water draft determination, please see the [draft determinations webpage](#).

Table 1: South West Water's response to required actions and interventions for draft determinations

Test area	Action reference	Action type	Action	Date required	Summary of the company's response to the action	Our assessment and rationale	Interventions
Securing cost efficiency	SWB.CE.A1	Agreed	For actions on cost efficiency thresholds, see data table below.	N/A	South West Water accepts the outcome of our view of efficient costs at the initial assessment stage.	No intervention required.	N/A
	SWB.CE.A2	Agreed	South West Water should propose a performance commitment related to Knapp Mill new water treatment works. The company proposes significant investment to deliver Knapp Mill new water treatment works, which requires	10am, 11 February 2019	See response within 'South West Water - Delivering outcomes for customers actions and interventions'.		

Test area	Action reference	Action type	Action	Date required	Summary of the company's response to the action	Our assessment and rationale	Interventions
			customer protection for efficient delivery via an underperformance payment.				
	SWB.CE.A3	Agreed	South West Water should propose a performance commitment related to Alderney new water treatment works. The company proposes significant investment to deliver Alderney new water treatment works, which requires customer protection for efficient delivery via an underperformance payment.	10am, 11 February 2019	See response within 'South West Water - Delivering outcomes for customers actions and interventions'.		
	SWB.CE.A4	Required	WaterShare as applied to unconfirmed environmental investments: The company states (in response to query SWB-IAP-CE-002) that environmental investments are "one element of uncertainty that will be included within the WaterShare mechanism. WaterShare has been in place since PR14 and will continue to track and report expenditure against the WINEP items included in the business plan. Any differences will be transparently reported and shared with customers." So that we may take an independent view of these differences, please provide breakdowns of the c.£41m of expenditure included for the 110 Amber schemes in your company's WINEP3 i) by scheme and ii) between lines in tables WS2 and WWS2.	10am, 11 February 2019	The company provided a scheme by scheme cost breakdown of South West Water's WINEP schemes that remain at amber status by line in tables WWS2 and WS2. They explain that the number of Amber schemes reduced from 110 following Defra decisions on UWWTD and Bathing Water Investigation drivers prior to the submission of the business plan on 3 September 2018.	No intervention required	N/A

Table 2: Further interventions for draft determinations

Intervention reference	Our assessment and rationale	Interventions
<p>SWB.CE.C1</p>	<p>We propose to intervene on the transition expenditure relating to the Knapp Mill water treatment works scheme as the company did not provide sufficient evidence why it would be efficient to bring this activity forward.</p>	<p>We are not allowing the transitional expenditure given on Business plan table WWS10 Line 13, 14 and 40 relating to the Knapp Mill WTW.</p>
<p>SWB.CE.C2</p>	<p>We consider that the proportion of developer services expenditure that is assumed recoverable from developers should be the same across all companies unless there is specific evidence in the company business plans to the contrary.</p> <p>Water</p> <p>New developments: Company business plan forecasts suggest an industry average recovery rate for new developments of 48%. Six companies (including all 3 fast track companies) are forecasting a negative infrastructure charge as the income offset is greater in absolute terms than the infrastructure charge. In 2020 new charging rules for developer services (England only) mean that the income offset is now applied to the infrastructure charge. We said in Charging Rules for New Connection Services (December 2018) that in the transition to the new charges regime, that companies should take reasonable steps to ensure that the existing balance of charges between developers and other customers prior to the implementation of the new rules should be broadly maintained.</p> <p>For the purposes of determining an appropriate industry position, we have capped the amount of income offset such that it cannot exceed the infrastructure charge for the 6 companies referred to above. This is because we do not recognise this as being consistent with the balance of charges under the pre-2020 regime. This gives a revised average rate of 66% which we have applied.</p> <p>New connections: We expect recovery rates for new connections to be close to 100%. We therefore assume 100% cost recovery for new connections.</p> <p>Diversions:</p> <p>Our expectation is that diversion activities are fully recoverable by companies. We will apply a 100% assumption for diversions recovery rates.</p> <p>Wastewater</p>	<p>We are intervening to use our forecast of the proportion of developer services expenditure that is assumed recoverable from developers:</p> <p>Water</p> <p>New developments: 66%</p> <p>New connections: 100%</p> <p>Diversions: 100%</p> <p>Wastewater</p> <p>New developments: 100%</p> <p>Diversions: 100%</p>

Intervention reference	Our assessment and rationale	Interventions
	<p>New developments: Our expectation, based on previous price reviews, is that recovery rates for wastewater should be close to 100%. Of the 11 WaSCs, 8 state that they will recover 100%, including South West. We therefore assume a recovery rate of 100%.</p> <p>Diversions: Our expectation is that diversion activities are fully recoverable by companies. We will apply a 100% assumption for diversions recovery rates.</p>	
SWB.CE.C3	<p>Our adjustments to base and enhancement expenditure will impact operating and capital expenditure differently. We therefore propose to adjust the opex and capex split in each control to reflect the adjustments agreed with the company to base and enhancement expenditure in each control. In base expenditure, we retain the opex and capex expenditure splits provided by the company in its submission. We assume all enhancement expenditure we allow is capital expenditure.</p>	<p>We are intervening to adjust the opex/capex split in each control to reflect the adjustments we have agreed with the company to base and enhancement expenditure.</p>
SWB.CE.C4	<p>Our adjustments will impact different programmes within totex differently. The five-year profile of expenditure provided in the company submission by South West Water is reasonable and therefore we propose to profile our totex allowance over the five-year period based on this profile.</p>	<p>We are intervening to apply South West Water's five-year totex profile to our totex allowance.</p>

Ofwat (The Water Services Regulation Authority) is a non-ministerial government department. We regulate the water sector in England and Wales. Our vision is to be a trusted and respected regulator, working at the leading edge, challenging ourselves and others to build trust and confidence in water.

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