

April 2019

Trust in water

**PR19 draft determinations:
United Utilities – Aligning risk and
return 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 'UW' denotes the company United Utilities 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 'UW' denotes the company United Utilities 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 United Utilities Water draft determination, please see the [draft determinations webpage](#).

Table 1: United Utilities' 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
Aligning risk and return	UW.RR.A1	Required	For the assessment of notional financeability, the proposed dividend yield for the notional company exceeds the real cost of equity on a blended CPIH:RPI basis. The company should revise the dividend yield (and associated dividend growth) for the notional company to reflect the real CPIH:RPI blended cost of equity of 4.52%. The company should reconsider the level of the PAYG adjustment and provide more	10am, 11th February 2019	United Utilities has reduced the dividend yield for the notional company in line with the blended CPIH:RPI cost of equity of 4.52% and reassessed financeability. This has resulted in a lower adjustment to PAYG rates to address the notional financeability constraint.	No intervention required. United Utilities has complied with the action. We accept the evidence provided in relation to the financeability constraint and apply the revised PAYG adjustment proposed by	N/A

Test area	Action reference	Action type	Action	Date required	Summary of the company's response to the action	Our assessment and rationale	Interventions
			evidence to justify its choice of RCV run-off rates.		United Utilities has also provided further convincing evidence to support its proposed RCV run off rates.	United Utilities in our draft determination. We accept the RCV run off rates proposed by United Utilities and apply these in our draft determination.	

Table 2: Further interventions for draft determinations

Intervention reference	Our assessment and rationale	Interventions
UUW.RR.C1	United Utilities' approach to PAYG rates is to recover in each year an amount equivalent to operating costs. The Ofwat view of totex has a different profile of operating and capital expenditure. Using the company's PAYG rates would result in PAYG revenue not being consistent with the approach stated in the business plan.	We are intervening to amend the PAYG rates across all wholesale controls to reflect the mix of operating and capital expenditure in our view of efficient costs in the draft determination. The changes maintain the company's stated approach for PAYG of recovering operating costs.
UUW.RR.C2	In our draft determination summary, we note that the RoRE risk ranges shown in Table 5.1 and Figure 5.1 reflect our interventions and, in particular, that we have included the RoRE risk ranges for ODIs shown in Table 2.3 of the summary document.	The company should provide an updated view of RoRE risk ranges at P10/P90 confidence levels in light of our draft determination. For this purpose, the company should apply its view on the interactions between individual ODI risks in arriving at an overall risk range for ODIs. Calculations should be carried out using the App26 rows on the F-Inputs tab of the draft determination financial model, with values read off the model dashboard. The company's updated view should be provided in its response to the draft determination.
UUW.RR.C3	United Utilities' approach to other income includes an element representing of losses on the disposal of fixed assets. In our determinations we ensure that assets are funded when they are purchased and so it is not appropriate to provide further additional funding on disposal. Using the company's approach would mean that customers are potentially paying twice for assets purchased by the company.	We are intervening to amend the forecast 'other income' to adjust the forecast to exclude the impact of losses on the disposal of fixed assets.

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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