

July 2019

Trust in water

PR19 draft determinations

**Anglian Water – Securing cost efficiency
actions and interventions**

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PR19 Draft Determinations: Anglian Water – Securing cost efficiency actions and interventions

Following our initial assessment of plans, we categorised two types of actions for slow-track and significant scrutiny companies:

- required actions for companies which in general were required for draft determinations (or final determinations for some aspects of past delivery); and
- advised actions for companies to do by a specific date but that are not required for our draft determinations.

Table 1 below sets out the required and advised 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 'ANH' denotes the company Anglian Water. The central acronym references the test area where the action has been identified, please see the 'PR19 draft determinations: Glossary' for a key to these acronyms. Actions whose numbers are preceded with an 'A' denote required actions and actions whose numbers are preceded with a 'B' denote advised 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 'ANH' denotes the company Anglian Water. The central acronym references the test area where the action has been identified, please see the 'PR19 draft determinations: Glossary' for a key to these acronyms. Intervention numbers are preceded with a 'C'.

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

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

Test area	Action reference	Action type	Action	Date required	Summary of company response to action	Our assessment and rationale	Required interventions
Securing cost efficiency	ANH.CE.A1	Required	<p>We provide our view of efficient costs for the company along with our reasoning. We expect it to address areas of inefficiency, or lack of evidence, in the revised business plan. Where appropriate, we expect it to withdraw investment proposals if either:</p> <ul style="list-style-type: none"> • the need for investment is not compelling; or • there is no need for a cost adjustment claim beyond our existing cost baseline. 	1 April 2019	<p>The company requests expenditure levels significantly higher than they incurred historically, and has not substantially changed or revised the requested levels since our initial assessment of business plans.</p> <p>It retained the two cost adjustment claims submitted at initial assessment of plans for sludge transport costs and maintaining frontier leakage performance, which we rejected and partially accepted at initial assessment of plans respectively.</p> <p>It has provided substantial evidence to support its view of costs, some of which was not submitted in time for us to fully assess for the draft determination. We</p>	<p>Intervention required.</p> <p>Much of the wholesale cost reduction is due to a reduced scope (for example removing metaldehyde treatment) rather than improved cost efficiency.</p> <p>The company did not respond to our efficiency challenge in its resubmitted costs.</p> <p>We review the company responses and incorporate these into our assessment for draft determination. To ensure customers pay only for efficient costs we continue challenge these costs for all areas.</p>	<p>We provide our view of efficient costs for the company along with our reasoning.</p> <p>We expect the company to continue to address areas of inefficiency and lack of evidence.</p>

					will consider the late submissions as we complete our final determination.	We recognise that Anglian Water has made additional submissions in this area including cost adjustment claims after 1 April 2019. These were not submitted until significantly after the date when we could review them sufficiently to take them into account for draft determinations. However, we will consider them in our final determination.	
ANH.CE.A2	Required	There is significant investment proposed in delivering the internal interconnection programme and therefore the company is required to propose an outcome delivery incentive in order to ensure customer protection for efficient delivery. The company should provide evidence to justify the level of the performance commitment and the outcome delivery incentive rates proposed, in line with our Final Methodology. We expect to receive evidence of customer support for outperformance payments, where proposed, and that the incentive rates proposed are reflective of customer valuations.	1 April 2019	The company proposes to use an 'end of AMP' mechanism to return expenditure associated with the interconnector programme, in the event that certain solutions are not required. The company does not present this mechanism in the form of a new bespoke performance commitment but states an intention to work with Ofwat after the initial assessment of plans submission to finalise the detail of this mechanism to be in the final determination.	Intervention required. We assess the additional information provided by the company in the submission and intervene to give the company a bespoke performance commitment PR19ANH_39 – Internal interconnection programme to provide customer protection in this area (our decision is described in 'Anglian Water – Delivering outcomes for customers actions and interventions').	Company to provide response to the revised performance commitment in its representation to the draft determination.	
ANH.CE.A3	Required	Strategic regional solution development - We have identified from the plans that at least one strategic supply solution is required over the next 5-15 years to secure drought resilience in the south-east. The strategic regional solution development allocation is to allow the delivery of consistent and transparent investigations, planning and development of strategic options with the overall aim of optimum solutions being construction ready by 2025. The company's allocation is made on the basis of having clear deliverables and customer protection for the gated delivery of the development of an eastern regional solution/transfer. The following actions are required to ensure the efficient delivery of this development programme. <ul style="list-style-type: none"> • In conjunction with the other companies involved, jointly propose methods for collaborative working including setting up the joint working group for individual schemes, and how consistent assumptions and decisions will be made within these groups and between them. • Provide more detail on the gated process, the deliverables, timings and expenditure allocations at each gate. • Propose outcome delivery incentive-type mechanisms to allow allocated funding to be recovered by customers in the event of the scheme not progressing through 	1 April 2019	The company's strategic regional water resources submission includes a joint statement by six companies via Water Resources South East. This joint statement considers: the principles for joint working; timing of the gateways; increased detail of the work between the proposed gates; the principles of a change protocol to manage changes to schemes in the proposal and to change the current list of schemes when required; development of the principles of an outcome delivery incentive type mechanism to allow funding to be recovered by customers in the event of the scheme not progressing and for the non-delivery or late delivery of outputs. In an addendum to the joint statement, submitted on 3 May 2019, the same companies specify key principles for a 'hybrid approach' outcome delivery incentive mechanism. Anglian Water also submit a summary of costs and solution specific reports for the Affinity Water transfer and reservoir, and Grand Union Canal to Affinity Water transfer.	Intervention required. We have assessed the revised submissions (both joint and company specific) to intervene for the draft determinations. This includes updates to cost allowances for this development programme, gate delivery updates and the end of period reconciliation mechanism to protect customers. The detailed assessment and rationale is provided in the 'Strategic regional water resource solutions appendix'.	Company to present joint solutions consistently with solution partners and clearly set out the costs related to strategic regional water resource solutions in its representation to the draft determination.	

			<p>each gate and for the non-delivery or late delivery of outputs.</p> <p>Intervention updates and clarifications:</p> <p>We sent clarification of our expectations for information relating to this action that we expected information submitted on 1 April to be as accurate and complete as possible, but accepted that given the timescales and joint working implications this may be in draft form. However, we wanted clarity on the costs relating to strategic regional water resource solutions and the solutions this relates to be summarised by 12 April, with the final information covering the action by 3 May.</p>				
	ANH.CE.A4	Required	<p>We note the company's proposal that 10% of the costs of any Amber WINEP scheme for which ministers do not confirm the need, be retained by the company to cover any initial spend made prior to the decision not to proceed with the scheme. The company should submit evidence to justify this scale of retention and identify what actions the company is taking / intends to take to minimise the possibility of abortive expenditure and why this risk could not be eliminated with appropriate scheduling. To further inform our view of the reasonableness of the company's proposal it should provide assumed expenditure profiles (capex and opex) for each of the Amber schemes included in its investment plan and give a breakdown of this expenditure between the lines in business plan tables WS2 and WWS2.</p>	1 April 2019	<p>The company provides a forecast capital and operating expenditure profiles for all Amber schemes as requested together with a breakdown of expenditure between the lines in business plan tables WS2 and WWS2.</p>	<p>Intervention required.</p> <p>We did not find the arguments put forward in support of the proposed 10% retention for cancelled Amber schemes compelling, nor that the potential benefits to customers outweigh the disadvantages. As a result we reject this proposal.</p>	<p>We provide our view of the unit rates to be used in the cost adjustment mechanism.</p>
	ANH.CE.A5	Required	<p>There may be significant impacts in terms of investment or type of investment as a result of the metaldehyde ban. The company should investigate and agree with the DWI the scale and timing of any potential changes compared to its submitted plans. Significant changes and uncertainty may require an outcome delivery incentive to protect customers in the instance of expenditure not being required. Should the company propose a performance commitment and outcome delivery incentive, the company should provide evidence to justify the level of the performance commitment and the outcome delivery incentive rates proposed, in line with our Final Methodology. We expect to receive evidence of customer support for outperformance payments, where proposed, and that the incentive rates proposed are reflective of customer valuations.</p>	1 April 2019	<p>The company has revised its submission in relation to the metaldehyde treatment required to support its internal interconnection programme. The company has removed the metaldehyde treatment requirement from its schemes reducing requested totex by £47.4 million. The company has also removed the product substitution payments for farmers from its catchment management programme, reducing requested totex by a further £20.8 million.</p>	<p>No intervention required for draft determination but further action needed by the company.</p> <p>We accept the revisions and assess the revised expenditure.</p>	<p>Company to provide evidence to confirm Drinking Water Inspectorate agreement with its submitted plans/revised undertakings and that no metaldehyde specific treatment or product substitution costs are included in the requested allowance.</p>
	Advised actions	Advised	No advised actions	N/A			

Table 2: Further interventions for draft determinations

Intervention reference	Our assessment and rationale	Interventions
<p>We explain our approach to cost assessment, including the allowances we set for each control, assumption on revenue recovery from grants and contributions, opex-capex split and totex profiling, in 'Securing cost efficiency technical appendix'. We set out other company specific interventions, and the allowances we set for each control, in section 3 of the company's draft determination summary and its cost efficiency appendix.</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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