

July 2019

Trust in water

PR19 draft determinations

**Dŵr Cymru – Securing cost efficiency
actions and interventions**

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PR19 Draft Determinations: Dŵr Cymru – 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 'WSH' denotes the company Dŵr Cymru. 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 'WSH' denotes the company Dŵr Cymru. 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 Dŵr Cymru draft determination, please see the [draft determinations webpage](#).

Table 1: Dŵr Cymru'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	WSH.CE.A1	Required	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: 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	The company proposes slightly reduced base expenditure in comparison to its September 2018 business plan. The company proposes expenditure to catch-up with the sector on leakage, supply interruptions, pollution incidents and water quality contacts about the acceptability of water. The company retained the three cost adjustment claims submitted in its original plan, one of which we rejected and two partially accepted at initial assessment of plans, and submitted a new cost claim for	Intervention required. Although reduced in comparison to its September 2018 business plan, the company's costs are greater than our efficient view, particularly in the wastewater network plus and residential retail price controls. The company's proposed expenditure to catch-up with the sector on leakage, supply interruptions and pollution incidents is not permitted. We challenge a significant proportion of the company's proposed expenditure to catch-up customer contacts	We provide our view of efficient costs for the company along with our reasoning. We expect the company to continue to address areas of inefficiency and lack of evidence.

					Welsh language service costs at draft determinations.	about the acceptability of water. We make partial allowances for the two cost adjustment claims retained from the September 2018 business plan and reject the third. We do not make an allowance for the new cost claim for Welsh language services.	
WSH.CE.A2	Required	There is significant investment proposed in the delivery of the reservoir safety programme and therefore the company is required to propose a specific 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 has complied with the action by proposing a bespoke performance commitment for the delivery of its reservoir safety enhancement programme.	No intervention required. Interventions which relate to the suitability of the bespoke performance commitment PR19WSH_BI6 –Delivery of our reservoirs enhancement programme will be carried out through the Outcomes framework. (our decision is described in ‘Dŵr Cymru r – Outcomes performance commitment appendix’).	N/A	
WSH.CE.A3	Required	1) U_IMP6 schemes - When applied to the 4,953m3 storage volume reported in line 10 of table WWS4 the proposed unit cost formula would result in the company retaining £0.273m (about 5%) of the £5.749m totex requested for these schemes in table WWS2. Given that the storage schemes are all scheduled to be delivered in year 5 and therefore the risk of abortive expenditure is minimal the company should justify this proposed level of retention. 2) WFD_IMPg schemes - The proposals to replace unconfirmed schemes with others of equal value rather than return money to customers is inconsistent with the proposed approach for unconfirmed UWWTD schemes and does not meet our PR19 Methodology requirement for a cost adjustment mechanism. We note the similarity of approach to that proposed for any unconfirmed NEP schemes, but that the policy the company cites to justify the approach, i.e. Welsh Government's expectation that any headroom in AMP7 created by the removal of Amber schemes will be filled by bringing forward other schemes from AMP8, is not relevant in England. Accordingly, the company should explain its proposed approach for these schemes in England, provide evidence of customer support for it, or submit revised proposals. 3) The company should identify for Amber NEP schemes included in its AMP7 investment programme, the total costs included for each and the lines within table WWS2 and, if applicable, table WS2 (capex and opex) to which these costs have been allocated.	1 April 2019	1) The company states that the status of all schemes with a U_IMP6 driver in the most recent release of WINEP (in March 2019) had changed to ‘Green’ and that therefore there is no longer a need for a cost adjustment mechanism for this driver. 2) The company accepts that the circumstances resulting from the removal of ‘Amber’ schemes from WINEP differ to the situation in Wales and now propose to return the totex relating to cancelled ‘Amber’ WFD_IMPg schemes to customers. 3) The company provides a table showing all ‘Amber’ NEP schemes included in its proposed AMP7 investment programme, the forecast costs and the lines in tables WS2 and WWS2 to which they are allocated.	No intervention required. Though the company's proposals align with Welsh Government's expectation that any headroom in AMP7 created by the removal of Amber NEP schemes will be filled by bringing forward other schemes from AMP8, at £0.42m we consider the potential associated totex to be non-material, As such we do not require it to be subject to the same cost adjustment mechanism as will apply to unconfirmed Amber WINEP schemes.	N/A	

	WSH.CE.A4	Required	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.	1 April 2019	The company states that no investment for the treatment of metaldehyde is included. The company does flag an emerging metaldehyde issue in the Whitborne WTW catchment. The company has reviewed and submitted a risk assessment, which includes other pesticides, to the DWI.	No intervention required for Draft Determination but further action needed by the company. We accept that no expenditure is included for metaldehyde. We note that any decision by the DWI for Whitborne WTW catchment will not require expenditure specifically for metaldehyde.	Company to provide evidence to confirm DWI agreement with its submitted plans/ revised undertakings.
	Advised actions	Advised	No advised actions	N/A			

Table 2: Further interventions for draft determinations

Intervention reference	Our assessment and rationale	Interventions
WSH.CE.C1	<p>Your submission IAP Response. Ref B2.23.WSH.CE.A1. Storage schemes in the network to reduce spill frequency at CSOs IAP response requested investment of £34m to deliver unspecified schemes relating to CSOs with a high frequency of spilling. Your response to our query WSH-DD-CA-006 did not provide any further material information relating to how the scope and value of this programme was arrived at. Further to this we understand that NRW will specify the scope of this programme during 2020. Therefore due to the remaining uncertainty on cost we require that an uncertainty mechanism be set in addition to the current unit cost mechanisms that you have proposed for NEP amber scheme to ensure customers are protected.</p> <p>We have allowed the investment in our draft determination and will make an adjustment to this allowance at the end of the control period considering the delivered programme. We will apply a unit cost formula that is based on our current cost benchmarking models and our WINEP/NEP programme level cost challenge. The unit cost is taken as the marginal cost to provide additional schemes to that already within our allowance.</p> <p>The unit cost model uses as a variable the effective storage volume (cu.m). The unit costs coefficients may be subject to change as a result of further submission and representations prior to final determination.</p> <p>The effective storage volume is equal to the total vol. of storage commissioned as part of the conventional CSO scheme or the equivalent storage volume that would have been necessary should an alternative approach not have been followed. Such alternative approaches include, for example, working with a range of stakeholder in the catchment to improve surface water management.</p>	<p>We are intervening to set an efficient unit costs for schemes as specified by NRW to address to frequently spilling CSOs. The unit costs is, Allowed totex (£m) = 0.00122 per meter cubed of equivalent storage volume.</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.

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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