

July 2019

Trust in water

# PR19 draft determinations

**Northumbrian Water – Accounting for past  
delivery actions and interventions**

## PR19 Draft Determinations: Northumbrian Water - Accounting for past delivery 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, the model the action relates to, 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. Table 1 also sets out any further interventions that are not resulting from an action which we are making as part of the draft determination.

Each action and further intervention that is not resulting from an action has a unique reference. The prefix 'NES' denotes the company Northumbrian 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. Actions whose numbers are preceded with a 'B' denote advised actions. Interventions not resulting from an action are preceded with a 'C' followed by a three digit code for the model the intervention is relevant to, and a two digit reference for the interventions in that model. The model codes are set out below.

Model	Code
ODIs	002
Land sales	003
WRFIM	005
Totex	006
Water trading	007
Residential retail	008
SIM	009
RCV adjustments feeder model	010
Revenue adjustments feeder model	011

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

**Table 1 – Northumbrian Water’s response to required actions and interventions for draft determinations**

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
Outcomes	NES.PD.A1	Required	<b>PR14 Outcome delivery incentives:</b> Northumbrian Water is required to remove the adjustment for the tax rate in the values reported in table App 27 and resubmit.	1 April 2019	Northumbrian Water provides table App27 with values not adjusted for tax.	No intervention required but action required by Northumbrian Water.	In its representations on the draft determinations the company should ensure that tables App5 (PR14 reconciliation – performance commitments) and App27 (PR14 reconciliation – ODI summary) reconcile, and both tables contain values that have not been adjusted for tax.
Outcomes	NES.PD.A2a	Required	<b>PR14 Outcome delivery incentives:</b> Northumbrian Water is required to update its forecast for 2019-20 performance to take account of the actual 2018-19 performance for all its performance commitments.  We expect the company to pay particular focus where we found the evidence provided in its business plan for the 2018-20 forecasts to be insufficient which was for:	15 July 2019	No company action required for the draft determination.	No intervention required.  We will review Northumbrian Water’s updated data before making any interventions for the final determination.	N/A
Outcomes	NES.PD.A2b	Required	W-C3: Water mains bursts (3-year average)	15 July 2019	As NES.PD.A2a	As NES.PD.A2a	As NES.PD.A2a
Outcomes	NES.PD.A2c	Required	W-C4: Leakage (Ml/d) Northumbrian area	15 July 2019	As NES.PD.A2a	As NES.PD.A2a	As NES.PD.A2a
Outcomes	NES.PD.A2d	Required	W-C5: Leakage (Ml/d) Essex & Suffolk area	15 July 2019	As NES.PD.A2a	As NES.PD.A2a	As NES.PD.A2a

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
Outcomes	NES.PD.A2e	Required	S-B5: Transferred drains and sewers - internal sewer flooding	15 July 2019	As NES.PD.A2a	As NES.PD.A2a	As NES.PD.A2a
Outcomes	NES.PD.A2f	Required	S-C1: Sewage treatment works discharge compliance (3-year average)	15 July 2019	As NES.PD.A2a	As NES.PD.A2a	As NES.PD.A2a
Outcomes	NES.PD.A2g	Required	W-B2: Overall drinking water compliance (3-year average)	15 July 2019	As NES.PD.A2a	As NES.PD.A2a	As NES.PD.A2a
Outcomes	NES.PD.A2h	Required	W-B1: Satisfaction with taste and odour of tap water	15 July 2019	As NES.PD.A2a	As NES.PD.A2a	As NES.PD.A2a
Outcomes	NES.PD.A2i	Required	W-B3: Discoloured water complaints (3-year average)	15 July 2019	As NES.PD.A2a	As NES.PD.A2a	As NES.PD.A2a
Outcomes	NES.PD.A2j	Required	W-C2: Properties experiencing poor water pressure (3-year average)	15 July 2019	As NES.PD.A2a	As NES.PD.A2a	As NES.PD.A2a
Outcomes	NES.PD.A2k	Required	S-B2: Properties flooded internally	15 July 2019	As NES.PD.A2a	As NES.PD.A2a	As NES.PD.A2a
Outcomes	NES.PD.A2l	Required	S-B4: Sewer collapses (3-year average)	15 July 2019	As NES.PD.A2a	As NES.PD.A2a	As NES.PD.A2a

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
Outcomes	NES.PD.A2m	Required	S-C2: Pollution incidents - category 3 (3-year average)	15 July 2019	As NES.PD.A2a	As NES.PD.A2a	As NES.PD.A2a
Residential retail	NES.PD.A3a	Required	<b>PR14 Residential retail:</b> Northumbrian Water is required to clarify what the correct number is in table R9 for retail revenue for unmetered water and wastewater customers in 2017-2018.	1 April 2019	The company clarifies that the correct retail revenue for unmetered water and wastewater customers in 2017-18 is £22.801 million and ensures consistency between table R9 and the submitted reconciliation model.	No intervention required. The company provides sufficient evidence in response to this action.	N/A
Residential retail	NES.PD.A3b	Required	<b>PR14 Residential retail:</b> Northumbrian Water is required to provide further clarity on the reasons for the difference between reforecast customer numbers and actual customer numbers in 2018-2019.	1 April 2019	The difference between actual and reforecast customer numbers in 2018-2019 is due to the forecast actual customer numbers figure being a more recent forecast.	No intervention required. The company provides sufficient evidence in response to this action.	N/A
Residential retail	NES.PD.A3c	Required	<b>PR14 Residential retail:</b> Northumbrian Water is required to also provide further evidence to back up the forecasts for metered wastewater-only customers in 2018-2019 and 2019-2020.	1 April 2019	Northumbrian Water provides evidence to support its forecasts by referring to consistency with WRMP data included in other business plan tables.	No intervention required. The company provides sufficient evidence in response to this action.	N/A
Residential retail	NES.PD.A3d	Required	<b>PR14 Residential retail:</b> Northumbrian Water is required to also provide further evidence to back up the forecasts for metered water-only customers in 2019-2020.	1 April 2019	Northumbrian Water provides evidence to support its forecasts by referring to consistency with WRMP data included in other business plan tables.	No intervention required. The company provides sufficient evidence in response to this action.	N/A

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
Residential retail	NES.PD.C008.01	Intervention not resulting from an action	N/A	N/A	N/A	<p>Intervention required.</p> <p>We are intervening to round Northumbrian Water's modification factor figures to two decimal places to ensure consistency with the '<a href="#">PR14 reconciliation rulebook</a>'.</p>	<p>We are rounding to two decimal places, modification factor figures for 2015-16 to 2019-20 associated with the following lines in business plan table R9:</p> <ul style="list-style-type: none"> <li>• unmetered water-only customer;</li> <li>• unmetered wastewater-only customer;</li> <li>• unmetered water and wastewater customer;</li> <li>• metered water-only customer;</li> <li>• metered wastewater-only customer; and</li> <li>• metered water and wastewater customer.</li> </ul> <p>Our interventions reduce the total residential retail revenue payment at the end of the 2015-20 period from - £0.180 million to - £0.176 million (2017-18 FYA CPIH deflated price base).</p> <p>Please see published draft determination residential retail revenue reconciliation model for Northumbrian Water.</p>
Residential retail	NES.PD.C008.02	Intervention not resulting from an action	N/A	N/A	N/A	<p>Intervention required.</p> <p>We are intervening to apply the appointee WACC as the discount rate to be used to provide a financing adjustment for the time value of money of the reward or penalty in line with the '<a href="#">PR14 reconciliation rulebook</a>'. This may be required if the materiality threshold for financing adjustment is exceeded.</p> <p>Our intervention ensures that there is no mismatch between the discount rate used and the revenue control to which it is applied.</p>	<p>For Northumbrian Water we are including a figure of 3.74% for the 'Materiality threshold for financing adjustment - Discount Rate.' This replaces the figure of 3.6% contained in Northumbrian Water's April 2019 submission.</p> <p>Our interventions do not result in any changes to the total residential retail revenue payment at the end of the 2015-20 period because the materiality threshold is not exceeded.</p> <p>Please see published draft determination residential retail revenue reconciliation model for Northumbrian Water.</p>
SIM	NES.PD.A4	Required	<b>PR14 Service incentive mechanism:</b> Northumbrian Water is required to provide more evidence to support the forecast trajectory in table R10.	1 April 2019	Northumbrian Water provides an explanation for its forecast trajectory in its response to action NES.PD.A4.	<p>No intervention required.</p> <p>The company provides sufficient evidence in response to this action.</p>	N/A

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
SIM	NES.PD.C009.01	Intervention not resulting from an action	N/A	N/A	N/A	Intervention required.  We are intervening to adjust Northumbrian Water's household retail revenue as a result of its SIM performance from 2015-16 to 2018-19.	We are intervening to set the service incentive mechanism adjustment to +2.07% of household retail revenue, which is £6.228 million (2017-18 FYA CPIH deflated price base) in total over the period. We further explain how we calculate this in the 'Accounting for past delivery technical appendix'.
Totex	NES.PD.A5a	Required	<b>PR14 Totex:</b> Northumbrian Water is required to update the value for transitional expenditure in 2014-15 to match actual spend.	1 April 2019	Northumbrian Water updates the value for water transitional expenditure but does not update the value for sewerage transitional expenditure in its business plan table WWS15.  However, the company includes this correct value for sewerage transitional expenditure in its totex reconciliation model submitted on 1 April 2019.	No intervention required  We are using the value for sewerage transitional expenditure taken from the company's totex reconciliation model.	N/A
Totex	NES.PD.A5b	Required	<b>PR14 Totex:</b> Northumbrian Water is required to provide a more detailed explanation to support its forecasted performance for years 2018-19 and 2019-20 in tables WS15/WWS15 and the model.	1 April 2019	Northumbrian Water provides a detailed explanation to support its forecast performance in its 'Action tracker – NES' document.  The company's performance is driven by increased operating costs due to adverse weather conditions and also by increased chemicals prices.	No intervention required.  The company provides sufficient evidence in response to this action.	N/A
WRFIM	NES.PD.A6	Required	<b>PR14 Wholesale revenue forecasting incentive mechanism:</b> Northumbrian Water is required to use June 2018 update version of the model to calculate the adjustments.	1 April 2019	Northumbrian Water uses the June 2018 update version of the model to calculate the WRFIM adjustments.	No intervention required.  The company provides sufficient evidence in response to this action.	N/A

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
Water trading	NES.PD.C007.01	Intervention not resulting from an action	N/A	N/A	N/A	<p>Intervention required.</p> <p>We are intervening to disallow the water trading export incentive claim for the trade with Thames Water. The principles of the water trading incentives policy were set out at PR14. The policy intent of the incentives was to encourage new transfers of water between water companies. In order to be able to claim water trading incentives, the 'PR14 methodology' set out a requirement for companies to have an Ofwat-approved trading and procurement code in place consistent with those principles. Northumbrian Water has an Ofwat approved trading and procurement code, 'Northumbrian Water - trading and procurement code' consistent with the water trading incentives policy set out at PR14 which we approved on 12 February 2018. However, the net effect of the water trade with Thames Water is to implement a reduction in the amount of water that that is exported from Thames Water to Northumbrian Water under a modification of a pre-existing bulk supply agreement with Essex and Suffolk Water. Therefore, the incentive claim for this water trade is inconsistent with the criteria set out in the trading and procurement code which requires a new export agreement and with the policy intent of the water trading incentives as set out in the PR14 methodology to encourage new water transfers. Therefore, we are intervening to disallow the claim.</p>	Our interventions reduce the total PR14 water trading revenue payment at the end of the 2015-20 period from £7.088 million to £0 million (2017-18 FYA CPIH deflated price base).



Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
All models	NES.PD.A7	Required	<b>PR14 reconciliations:</b> Further to the actions we have set out to address our concerns over the evidence provided in its business plan for the individual reconciliations, we will require the company to refresh all of its PR14 reconciliations to replace its 2018-19 forecast performance with 2018-19 actual performance and update the evidence for its forecast 2019-20 performance taking into account of the actual 2018-19 performance.	15 July 2019	No company action required for the draft determination.	No intervention required. We will review Northumbrian Water's responses to its actions and further information provided for all the PR14 reconciliation models before making any further interventions for the final determination.	N/A
Revenue adjustments	NES.PD.C011.01	Intervention not resulting from an action	N/A	N/A	N/A	Intervention required. We are standardising the discount factor used to profile revenue adjustments. Companies can choose to apply revenue adjustments either in the first year, or, spread over a number of years in the 2020-25 period to minimise the impact on bills or to generate a bill profile that is appropriate for its customers. We consider the wholesale WACC is an appropriate discount factor as this is a measure of the time value of money that is consistent with the price control framework. We are not intervening in Northumbrian Water's choices for profiling revenue adjustments in 2020-25.	We are using our view of the wholesale WACC (3.09%) as the discount factor to preserve the net present value of the outperformance or underperformance payments due when spreading adjustments over the period..

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
N/A	NES.PD.B1	Advised	<p>Northumbrian Water should produce and provide additional evidence that it has identified:</p> <ul style="list-style-type: none"> <li>the drivers of its performance past and current outcomes performance, including financial and reputational performance commitments;</li> <li>lessons learnt from good and poor past and current performance;</li> <li>the performance gap between current performance and proposed performance in the 2020-25 business plan; and</li> <li>measures to ensure deliverability of the 2020-25 business plan.</li> </ul>	24 May 2019	The company provides further evidence to support the deliverability of its plan.	<p>No intervention required.</p> <p>Because our deliverability concerns were not substantial in this area, and so we set an advised action, we will conduct a risk-based review of the company's response to the action and will determine the need for further interventions for the final determination.</p>	N/A
N/A	NES.PD.B2	Advised	<p>Northumbrian Water should produce and provide an action plan that sets out:</p> <ul style="list-style-type: none"> <li>how Northumbrian Water will continuously monitor performance against PR14 and PR19 performance commitments, including how this relates to section 3 of the Annual Performance Report and what evidence it will look for beyond itself and the sector;</li> <li>how Northumbrian Water will identify drivers of performance and lessons learnt from both good and poor performance;</li> <li>how Northumbrian Water will identify measures to improve performance and integrate these into its business; and</li> <li>how Northumbrian Water will ensure that this is a continuous rather than one-off process.</li> </ul>	24 May 2019	The company provides an action plan as requested.	<p>No intervention required.</p> <p>Because our deliverability concerns were not substantial in this area, and so we set an advised action, we will conduct a risk-based review of the company's response to the action and will determine the need for further interventions for the final determination.</p>	N/A

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
N/A	NES.PD.B3	Advised	<p>Northumbrian Water should produce and provide additional evidence that it has identified:</p> <ul style="list-style-type: none"> <li>the drivers of incidents performance and customer communication and support performance during and after major incidents, pollution incidents and where statutory and licence obligations enforced by the EA/NRW, DWI and Ofwat have not been met;</li> <li>lessons learnt from good and poor past and current performance;</li> <li>the performance gap between current performance and proposed performance in the 2020-25 business plan; and</li> <li>measures planned or already in place to ensure deliverability of the 2020-25 business plan.</li> </ul>	24 May 2019	The company provides further evidence to support the deliverability of its plan.	<p>No intervention required.</p> <p>Because our deliverability concerns were not substantial in this area, and so we set an advised action, we will conduct a risk-based review of the company's response to the action and will determine the need for further interventions for the final determination.</p>	N/A

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
N/A	NES.PD.B4	Advised	<p>Northumbrian Water should produce and provide an action plan that sets out:</p> <ul style="list-style-type: none"> <li>• how Northumbrian Water will continuously monitor incidents performance and customer communication and support during and after major incidents and deliver targets set by the EA/NRW in the Environmental Performance Assessment (EPA), by DWI and by Ofwat's regulations , including what evidence it will look for beyond itself and the sector;</li> <li>• how Northumbrian Water will identify drivers of performance and lessons learnt from both good and poor performance;</li> <li>• how Northumbrian Water will identify measures to improve performance and integrate these into its business; and</li> <li>• how Northumbrian Water will ensure that this is a continuous rather than one-off process.</li> </ul>	24 May 2019	The company provides an action plan as requested.	<p>No intervention required.</p> <p>Because our deliverability concerns were not substantial in this area, and so we set an advised action, we will conduct a risk-based review of the company's response to the action and will determine the need for further interventions for the final determination.</p>	N/A

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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