

July 2019

Trust in water

PR19 draft determinations

**Northumbrian Water – Securing long-term
resilience actions and interventions**

ofwat

www.ofwat.gov.uk

PR19 Draft Determinations: Northumbrian Water – Securing long-term resilience 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 '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 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 '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. Intervention numbers are preceded with a 'C'.

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

Test area	Action reference	Action type	Action	Date required	Summary of company response to action	Our assessment and rationale	Required interventions
Securing long-term resilience	NES.LR.A1	Required	The company should ensure that its common and bespoke performance commitments associated with operational resilience are clearly defined, sufficiently demanding for the 2020 to 2025 period and the long term, and supported by the right incentives. We expect the company to satisfy the relevant actions set out in relation to the outcomes areas ensuring a line of sight between risks to resilience and the package of outcomes.	1 April 2019	Northumbrian Water has not implemented all relevant outcome actions associated with operational resilience, in particular those related to bespoke resilience performance commitments.	Intervention required. The company should address any outstanding actions associated with operational resilience from the 'Northumbrian Water - Delivering outcomes for customers actions and interventions' tables, in particular those related to unplanned outage, mains repairs and its bespoke resilience performance commitments (Delivery of resilience enhancement programmes for water,	Refer to interventions described in the 'Northumbrian Water - Delivering outcomes for customers actions and interventions' table regarding unplanned outage, mains repairs and its bespoke resilience performance commitments (Delivery of resilience enhancement

Test area	Action reference	Action type	Action	Date required	Summary of company response to action	Our assessment and rationale	Required interventions
						wastewater and cyber improvements).	programmes for water, wastewater and cyber improvements).
	NES.LR.A2	Required	The company should provide a commitment that it will, by 22 August 2019, prepare and provide to us an action plan to develop and implement a systems based approach to resilience in the round and ensure that the company can demonstrate in the future an integrated resilience framework that underpins the company's operations and future plans showing a line of sight between risks to resilience, planned mitigations, package of outcomes and corporate governance framework.	1 April 2019	Northumbrian Water has confirmed its commitment to complete the action by 22 August 2019.	No intervention required. The company has complied with the required action.	N/A
	NES.LR.A3	Required	The company should also provide a commitment to work with the sector to develop robust forward looking asset health metrics and provide greater transparency of how its asset health indicators influence its operational decision making.	1 April 2019	Northumbrian Water has confirmed this commitment.	No intervention required. The company has complied with the required action.	N/A
	NES.LR.A4	Required	The company shall explain the steps it has taken/will take in response to its consultant's view that improvements should be made to ensure that the business adopts an integrated approach to its resilience arrangements.	1 April 2019	Northumbrian Water provides a response to its consultant's recommendations and says that the required action plan (action NES.LR.A2) will address issues around the adoption of an integrated approach to resilience.	No intervention required. The company has complied with the required action.	N/A
	NES.LR.A5	Required	Please explain how the company has taken account of the risks associated with its current credit ratings of BBB+ (negative) and its targeted ratings of BBB+/Baa1 for the period from 2020 to 2025.	1 April 2019	Northumbrian Water says it has an overarching financial objective of retaining its existing investment grade credit ratings of BBB+/Baa1. It says it has assessed the financeability of its business plan in this context. Northumbrian Water considers that its capital structure provides sufficient flexibility to deal with significant adverse events having stress tested key financial metrics.	No intervention but action required. The company has provided the required explanation, however we expect the company to provide further Board assurance on its long term financial resilience in the context of action NES.CR.L1.	See action NES.CR.L1

Test area	Action reference	Action type	Action	Date required	Summary of company response to action	Our assessment and rationale	Required interventions
	NES.LR.A6	Required	The company has noted the possibility of additional equity investment as a financial risk mitigation measure. Please explain the steps and risk management approaches the company has taken to ensure equity will be available if such support is required.	1 April 2019	Northumbrian Water says that, whilst its financial risk mitigation includes the possibility of equity retention through application of the Board's flexible dividend policy, its business plan did not make reference to the possibility of additional equity investment. The company also sets out that it has committed bank facilities for back up liquidity.	No intervention required. The company has provided the required explanation.	N/A
	Advised actions	Advised	No advised actions.	N/A			

Table 2 – Further interventions for draft determinations

Intervention reference	Our assessment and rationale	Interventions
NES.LR.C1	The Board assurance on actual and notional financeability and financial resilience in the revised business plan was provided on the basis of the assumptions made in the business plan, prior to any interventions we have made in the draft determination and our updated view of the cost of capital. There is evidence of further downward pressure on the cost of capital in very recent market data which will be considered for our final determination.	We expect companies to provide further Board assurance, in their responses to the draft determination, that they will remain financeable on a notional and actual basis, and that they can maintain the financial resilience of their actual structure, taking account of the reasonably foreseeable range of plausible outcomes of their final determination, including evidence of further downward pressure on the cost of capital in very recent market data as we discuss in the 'Cost of capital technical 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.

Ofwat
Centre City Tower
7 Hill Street
Birmingham B5 4UA

Phone: 0121 644 7500
Fax: 0121 644 7533
Website: www.ofwat.gov.uk
Email: mailbox@ofwat.gov.uk

July 2019

© Crown copyright 2019

This publication is licensed under the terms of the Open Government Licence v3.0 except where otherwise stated. To view this licence, visit nationalarchives.gov.uk/doc/open-government-licence/version/3.

Where we have identified any third party copyright information, you will need to obtain permission from the copyright holders concerned.

This document is also available from our website at www.ofwat.gov.uk.

Any enquiries regarding this publication should be sent to us at mailbox@ofwat.gov.uk.

