

July 2019

Trust in water

# PR19 draft determinations

**Northumbrian Water – Targeted controls,  
markets and innovation actions and  
interventions**

**0 f w a t**

[www.ofwat.gov.uk](http://www.ofwat.gov.uk)

## PR19 Draft Determinations: Northumbrian Water– Targeted controls, markets and innovation 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   |
|---|------------------|-------------|---|---------------|--|---|--|
| Targeted controls, markets and innovation | NES.CMI.A1       | Required    | The proposed split of fixed and variable revenues for the bio-resources revenue control has not been sufficiently evidenced, particularly where cost lines are partly incremental and partly fixed. We are also intervening to ensure that the bioresources revenue adjustment is set on a broadly comparable basis to avoid setting revenue controls that may distort the development of trades. We will set out our view in the draft determinations based on the updated tables Bio1, Bio3 and Bio4. We will treat the funding of the 2020 RCV (run-off, returns and tax) as fixed for these purposes, along with revenues to recover local authority rates; some fees; and a proportion of direct and indirect costs of bioresources treatment and transport. | 1 April 2019  | We issued an industry query response in March 2019 setting out further details about the broad approach to be followed consistent with the methodology that would be applied to the fast track companies. Northumbrian Water adjusted the split in its April 2019 submission. Northumbrian Water sets out its approach, along with other companies and we have reviewed this evidence. | Intervention required.<br><br>We are intervening because our assessment of the companies’ business plans revealed an inconsistent approach between companies in their calculation of the bioresources revenue requirements to recover fixed and variable costs. This resulted in a wide range of suggested splits between the fixed and variable revenue component. As with fast track companies, a consistent approach to the fixed/variable split is essential to ensure that | We are intervening to set the level of the split between fixed and variable costs. Our detailed approach is set out in ‘Our methodology for the classification of bioresources costs’. |

|  |            |          |   |              |  |  |     |
|--|------------|----------|---|--------------|--|--|-----|
|  |            |          |   |              |  | the company is correctly remunerated by our modified average revenue control for outturn sludge volumes that differ from its original forecasts.   |     |
|  | NES.CMI.A2 | Required | The company should provide a commitment to provide a detailed work programme by end August 2019 to assure us that the company will deliver appropriate drainage and wastewater management plans. The programme should ensure that the company can prepare and consult on its first drainage and wastewater management plan no later than the summer of 2022 to enable revised plans to be prepared in early 2023 to inform PR24 business plans. | 1 April 2019 | The company has provided a commitment in its 1 April 2019 submission.  | No intervention required.  | N/A |
|  | NES.CMI.A3 | Required | The company should explain the steps that Essex and Suffolk water is taking to engage with other companies in the south east around the development of strategic water resource options. We are intervening to disallow the water trading export incentive claim, where the net effect of the trade is to implement a reduction in the amount of water that could be imported from Thames Water rather than a net increase in exports.          | 1 April 2019 | The company has provided an appropriate response. The response covered: <ul style="list-style-type: none"> <li>• how they engage with neighbouring companies on a bilateral basis and as part of regional groups in general;</li> <li>• their recent agreement with Thames Water since their business plan was originally submitted;</li> <li>• provided details of engagement of three other trades they are exploring with Anglian Water; and</li> <li>• Steps to remove obstacles that would prevent their export of water from Kielder Reservoir.</li> </ul> | No intervention required.<br><br>As noted elsewhere, the company's 2015 agreement with Thames Water is not eligible for the Water Trading Incentive. If their new trade with Thames Water is of a similar nature then this too may not be eligible for any Trading Incentive at PR24. That said, we will consider any application on its merits at PR24. | N/A |
|  | NES.CMI.A4 | Required | The company should updates its bid assessment framework document to provide greater clarity on the information requirements on bidders and the process for appeals.   | 15 July 2019 | Northumbrian Water provides greater clarity on the information requirements on bidders through its strategic sourcing procurement process. In sets out its dispute resolution process, which includes is appeals process.  | No intervention required.  | N/A |
|  | NES.CMI.A5 | Required | For DPC, the company is required to provide further evidence to support the decisions that determined why some schemes were not suitable for DPC. The list of schemes and the required evidence is detailed in 'Northumbrian Water: Direct procurement for customers detailed actions'.   | 1 April 2019 | The company provided a high level summary of the key elements of the Howdon Sewage Treatment Works scheme including the key deliverables and projected scheme costs.<br><br>The company did not provide a Net Present Value analysis comparing the DPC option for Derwenthaugh   | No interventions required.<br><br>The decision by the company that the Howdon Sewage Treatment Works expansion scheme was less suitable for DPC was supported by some convincing information.  | N/A |

|  |            |         |   |              |   |   |     |
|--|------------|---------|---|--------------|---|---|-----|
|  |            |         |   |              | <p>versus in-house delivery for the Howdon expansion.</p> <p>The company's assessment of this scheme concluded that it should not be further considered using a DPC process.</p>  | <p>There was insufficient evidence on comparative evaluation for the construction of a new works, at Derwenthaugh, to confirm this as not viable. In addition, the decision not to include a Net Present Value as requested did not support the case that this option was unsuitable for a DPC process.</p> |     |
|  | NES.CMI.B1 | Advised | <p>The company should provide further information on potential bioresources trades with other companies.</p> <p>The company should consider how it can collaborate with other companies to maximise the opportunities for research to address common challenges (eg leakage detection, water efficiency and wastewater treatment processes) rather than companies progressing research independently.</p> <p>The company should consider the opportunities for partnerships in delivering sustainable drainage solutions.</p> | 1 April 2019 | <p>The company states that it is investigating the potential for long-term treatment contracts for bioresources arising from neighbouring water and sewerage companies, particularly those located relatively close to one of its AAD centres, for example with Yorkshire Water.</p> <p>The company is very active in collaboration and has either set up, or participates in, a large number of groups and organisations. There is little evidence of outputs from these meetings or investing significant resources and/or time in collaborating on shared challenges to come up with innovative solutions. There is no evidence of what resources have been invested in collaborative projects.</p> <p>The company provided appropriate evidence regarding partnership working to deliver sustainable drainage solutions. We also note their commitment to build on their existing approach.</p> | <p>No intervention required.</p> <p>We remain concerned that the company is not maximising the opportunities available from collaborating to address common challenges. We will promote innovation in the sector as part of our on-going work on innovation.</p>  | N/A |

**Table 2: Further interventions for draft determinations**

| Intervention reference | Our assessment and rationale | Interventions |
|------------------------|------------------------------|---------------|
| N/A                    | N/A                          | 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.

Ofwat  
Centre City Tower  
7 Hill Street  
Birmingham B5 4UA

Phone: 0121 644 7500  
Fax: 0121 644 7533  
Website: [www.ofwat.gov.uk](http://www.ofwat.gov.uk)  
Email: [mailbox@ofwat.gov.uk](mailto: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](http://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](http://www.ofwat.gov.uk).

Any enquiries regarding this publication should be sent to us at [mailbox@ofwat.gov.uk](mailto:mailbox@ofwat.gov.uk).

