

July 2019

Trust in water

PR19 draft determinations

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

PR19 Draft Determinations: SES 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 'SES' denotes the company SES 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 'SES' denotes the company SES 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 SES Water draft determination, please see the [draft determinations webpage](#).

Table 1 – SES 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	SES.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 in the outcomes areas ensuring a line of sight between risks to resilience and package of outcomes.	1 April 2019	SES Water has not implemented all relevant outcome actions associated with operational resilience, in particular those related to its bespoke resilience performance commitments.	Intervention required. The company should address any outstanding actions associated with operational resilience from the 'SES Water - Delivering outcomes for customers actions and interventions' tables, in particular those related to unplanned outage, mains repairs and its bespoke resilience performance commitment ('Risk of supply failures').	Refer to interventions described in the 'SES Water - Delivering outcomes for customers actions and interventions' tables regarding unplanned outage, mains repairs and its bespoke resilience performance commitment ('Risk of supply failures').

Test area	Action reference	Action type	Action	Date required	Summary of company response to action	Our assessment and rationale	Required interventions
	SES.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	SES 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
	SES.LR.A3	Required	The company should 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	SES Water has confirmed this commitment.	No intervention required. The company has complied with the required action.	N/A
	SES.LR.A4	Required	Please explain the steps the company and its Board are taking to maintain long term financial resilience in the context that a company specific adjustment to the cost of capital is not guaranteed by the PR19 methodology (or at a future price control) and set out the risk management/mitigation approaches that have been identified.	1 April 2019	<p>SES Water says that, whilst its cost of capital should reflect its efficient cost of finance, its Board has taken/will take necessary steps to maintain long term financial resilience. In particular, the company says that it has:</p> <ul style="list-style-type: none"> obtained a 'non-binding' undertaking of financial support from its two main shareholders; already taken decisive action to strengthen its equity position reducing gearing from 77% to around 60% by the start of 2020; reduced its net debt and high cost embedded debt, and is carrying out an ongoing review of financing options; and taken action on operational resilience to manage the risk of impacts on its business. <p>The company also states that in the event Ofwat does not allow the requested company specific adjustment, the Board will take the practical steps required to ensure the company remains financially resilient.</p>	<p>Intervention required.</p> <p>The company is responsible for maintaining its long term financial resilience and the company has provided a Board assurance statement that the plan is financeable on the actual capital structure.</p> <p>The company has carried out a financial restructuring which provides comfort about its ability to maintain its financial resilience and the company has confirmed the Board will take the practical steps to ensure the company remains financially resilient in the absence of a company specific cost of capital adjustment.</p> <p>However, further assurance is required about the steps the company will take to maintain its financial resilience in the context of the draft determination, which includes, for example, an updated view of the cost of capital, our assessment of efficient costs and our assessment of outcome delivery incentives.</p>	<p>The company should provide further detail and Board assurance about its plans to maintain its long term financial resilience in the context of our draft determination as referenced in action SES.LR.C1.</p> <p>We also note that the undertaking of financial support referenced by the company is in the form of a 'non-binding expression of intent'. We seek further assurance from the company's Board that this provides the support the company might require to maintain its financial resilience in extreme downside scenarios.</p>

Test area	Action reference	Action type	Action	Date required	Summary of company response to action	Our assessment and rationale	Required interventions
							In its future reporting, we expect SES Water to apply suitably robust stress tests in its long term viability statements in 2020-25.
	Advised actions	Advised	No advised actions.	N/A	N/A	N/A	N/A

Table 2 – Further interventions for draft determinations

Intervention reference	Our assessment and rationale	Interventions
SES.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.

