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By email

Ian McAulay
Chief Executive Officer
Southern Water

8 December 2021

OFFICIAL

Dear Ian,

Strategic regional water resource solutions: Standard gate one final decision for Southern Water

I am writing to inform you of our final decisions in respect of the following strategic regional water resource solutions:

- West Country South Sources and Transfers
- West Country South Southern Water Transfer
- Thames to Southern transfer

The RAPID partner regulators would like to thank Southern Water for submission timeliness, its collaborative approach and positive engagement which has helped drive the quality and speed of progression of these solutions.

This letter should be read in conjunction with the final decision documents for each of these solutions, which are published alongside this letter. Both this letter and the final decision documents are published on our website on 8 December 2021.

The solution sponsors and other interested parties had the opportunity to respond to the draft decisions during the representation period, which followed the publication of the draft decisions on 14 September 2021. We have taken all relevant representations into account in making our final decisions.

The table below summarises the elements of our final decisions in respect of the Southern Water-sponsored solutions. Further details are contained in the accompanying final decision documents.

Final decision summary in respect of Southern Water-sponsored solutions

Recommendation item	West Country South Sources and Transfers	West Country South Southern Water Transfer	Thames to Southern transfer
Solution sponsors	South West Water, Wessex Water and Southern Water	South West Water, Wessex Water and Southern Water	Thames Water, Southern Water
Should further funding be allowed for the solution to progress to gate two?	Yes – Poole effluent recycling and transfers No – Roadford reservoir pumped storage and transfer	Yes – Poole effluent recycling and transfers No – Southern Potable Water Transfer	Yes
Is there evidence all expenditure is efficient and should be allowed?	Yes	Yes	Yes
Delivery incentive penalty?	No	No	No
Is there any change to partner arrangements?	No	No	No
Is there a need for a remediation action plan?	No	No	No

Solutions' progress and funding

Funding is allowed for options within the West Country South Sources and Transfers and West Country South Southern Water Transfer solutions to continue to be developed to standard gate two.

The following options are to continue to be investigated:

- Poole effluent recycling and transfers

The following options are not to continue to be investigated as part of the RAPID gated process:

- Roadford reservoir pumped storage and intra-regional transfer
- Southern potable water transfer

Further funding is not allowed for these options due to the high investment required for a low water resource benefit under a 1 in 500 drought scenario involving a transfer of over 200km.

The source element (Roadford reservoir pumped storage) has approved funding via Ofwat’s green economic recovery decisions. The intra-regional transfer element (Roadford transfer from South West Water to Wessex Water) is small in size and local scale and we therefore consider it is not strategic in nature and should not continue in the RAPID gated process. This option element can be progressed as part of business-as-usual through water resources management planning and business planning.

To reflect this reduced solution scope, we will halve the Final Determination gate two allowance for both solutions.

As set out in the PR19 final determination, any money spent during the gate one assessment stage on these options can be claimed at PR24.

We will also combine West Country South Sources and Transfers and West Country South Southern Water Transfer solutions into a single solution. The two solutions are intrinsically interdependent, with either solution becoming unfeasible if they both do not progress. Combining the two solutions also brings potential working and reporting efficiencies; the solutions both have the same solution sponsors, under which the same teams work on both solutions. The combined solution will be named ‘Poole effluent recycling and transfers’.

The combined solution's total allowance and gate allowances will be formed by combining the two solutions’ reduced allowances and gate allowances from the final determination. We have also decided to merge the gate one and gate two allowances. The allowances for the Poole effluent recycling and transfers are shown below.

Poole effluent recycling and transfers - total allowance and gate allowances (£million 2017-18 prices)

Gate allowance		Gate 1	Gate 2	Gate 3	Gate 4	Total
		10%	15%	35%	40%	100%
Original funding allowance	West Country South Sources and Transfers - Poole effluent recycling - Roadford reservoir pumped storage and transfer	0.55	0.83	1.93	2.21	5.52
	West Country South Southern Water Transfer - Southern Raw Water transfer - Southern Potable Water transfer	0.40	0.59	1.39	1.58	3.96

	Total	0.95	1.42	3.32	3.79	9.48
50% funding adjustment from gate two	New combined solution - Poole effluent recycling and transfers	n/a	0.71	1.66	1.90	4.74
Merge gate one and gate two allowances	New combined solution - Poole effluent recycling and transfers		0.80	1.66	1.9	4.74

Our decision to merge the gate one and two allowances also applies to your accelerated gate solutions (Desalination and Water recycling) and to West Country North Sources but not to Havant Thicket direct pipe, which joined the gated process at gate one and so did not have a gate one allowance. This results in the following allowances being available at gate two:

- Thames to Southern transfer - £3.12m
- Desalination - £7.42m
- Water recycling - £6.09m

Evidence of efficient expenditure

For West Country South Sources and Transfers and West Country South Southern Water Transfer we determine that all expenditure of £0.496 million for the former and £0.282m million for the latter is efficient and appropriate, and we allow it in full. This reflects final and reconciled costs information provided during the representation period.

For the Thames to Southern transfer we determine that all expenditure of £0.628 million is efficient and appropriate, and we allow it in full. This reflects final and reconciled costs information provided during the representation period.

Submission quality

Our overall classification of the submissions for West Country South Sources and Transfer, West Country South Southern Water Transfer and Thames to Southern transfer is that they are "Good (meets expectations)".

Application of penalty to total efficient gate spend

The largest penalty across a company's suite of solutions is applied to the company's total gate one allowed efficient expenditure. For Southern Water, this results in a potential delivery incentive penalty of 10% of its efficient expenditure, which was the incentive penalty applied to the desalination and water recycling solutions at accelerated gate one.

Southern Water had the opportunity to avoid the incentive penalty through provision of a remediation action plan for the desalination and water recycling solutions by 31 March 2021 and delivery of the action plan in full by 26 July 2021. We have received Southern Water's remediation action plan and will make a decision regarding whether it was delivered in full at accelerated gate two.

Remediation

A list of remediation issues is provided in the Appendix to each final decision document divided into priority actions, actions and recommendations. Priority actions are those that should have been completed at gate one and must now be addressed on a short timescale in order to make sure a solution stays on track.

We have not identified any priority actions in respect of West Country South Sources and Transfers, West Country South Southern Water Transfer or Thames to Southern transfer and therefore Southern Water does not need to submit a remediation action plan for these solutions.

Should you have any questions about this letter or final decisions, please e-mail rapid@ofwat.gov.uk and someone from the team will be in touch.

Once again, Ofwat would like to thank Southern Water for the work that it has carried out over the gate one period

Yours sincerely,

David Black
Interim Chief Executive Officer

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