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Sent via email

Ofwat  
PR24 consultation  
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To whom it may concern,

### **WRSE response to Ofwat's draft determinations**

Water Resources South East (WRSE) is the regional group for South East England.

The regional plan we have prepared has directly informed the Water Resources Management Plans (WRMPs) of six water companies - Affinity Water, Portsmouth Water, SES Water, South East Water, Southern Water and Thames Water.

Our regional plan and the companies' WRMPs are fully aligned and identify the investment needed to secure water supplies for the future. Together, they will address the forecast one billion litres per day shortfall in water supplies by 2035 and the 2.7 billion litres per day shortfall that could develop by 2075.

This is being driven by the joint challenges of population growth, climate change, the need to increase the region's resilience to severe drought, and the need to align with government expectations. Furthermore, it plans to replace up to 1.3 billion litres of existing abstractions by 2050 to help enhance our rivers and streams.

Our response to the draft determination is focused on the decisions that could impact the delivery of the regional plan, which presents the best value solution for customers in South East England. The next 10 years will set the foundations for meeting the significant water resources challenge we face over the next 50 years.

Our regional plan has been developed through extensive modelling and scenario planning, using advanced technical methods to ensure it is robust. It has identified the optimum combination of schemes whilst addressing both demand and supply challenges, ensuring the

timeframe in which schemes need to be delivered, does not compromise the security of our water supplies and achieves the policy targets set by the government.

We have worked closely with regulators, stakeholders and companies to develop a highly integrated plan of action to meet these challenges, which ensures resources are shared, rather than developing new resources unnecessarily. However, this strategy depends on the timely delivery of new water resources schemes as well as ambitious reductions in leakage and customer consumption at a scale not seen before.

Achieving this requires a significant increase in funding, the vast majority of which will be enhancement expenditure, as it is delivering a step-change in performance to meet new government policies and a higher level of resilience for both the environment and customers. It is essential that the funding needed for water resources is appropriately funded in AMP8 so that our water security is not compromised.

When producing the regional plan, we developed a resilience framework to ensure the plan supports the government's resilience duty. Part of the framework requires companies to assess and develop cost-efficient sub-water resource zone (WRZ) interconnector schemes that:

- Help meet companies' supply duties
- Enable companies to implement short-term licence reductions identified through their statutory Water Industry National Environment Programme (WINEP) process by moving water from another source in the zone, or
- Provide the infrastructure to move water across a zone from one bulk supply point to a new bulk supply point.

These WRMP facilitation schemes are critical to some zones, and we therefore request that Ofwat ensures that these sub-water resource zone improvements are included in the final determination.

### **Strategic Resource Options (SROs)**

We welcome that Ofwat has continued to fund the major Strategic Resource Options (SROs) identified in the regional plan.

The Regulators' Alliance for Progressing Infrastructure Development (RAPID) process introduced at PR19 brought much-needed focus and consistency to the development of these schemes that are critical to the plan and the ability of the companies to meet their statutory duties and environmental obligations in the future.

We also support Ofwat's decision to include more schemes in the RAPID process. However, we note no enhancement funding has been allocated to deliver the requirements of Gate 1 and limited funding has been allocated for Gate 2 for new SROs.

We would encourage Ofwat to reconsider its judgement on the allocation of funding for the new SRO schemes as we consider that allowances should be considered as enhancement spend, consistent with previous judgements.

Ofwat appears to expect companies to fund these early development costs primarily from base expenditure, rather than considering it enhancement, which is at odds with Ofwat's own definition<sup>1</sup> of base expenditure:

*Base expenditure: routine, year-on-year costs, which companies incur in the normal running of their business to provide a base level of good service to customers and the environment and maintain the long-term capability of assets.*

If companies and third parties are now expected to progress schemes to a significantly greater level of detail, this could have significant consequences and disincentivise the development of catchment solutions or new innovative ideas.

We would therefore suggest a continuation of the current process, but in parallel with an option development framework. This would clearly set out the expected design standard, including environmental assessment, that a scheme would need to be progressed to under baseline activities, ready for the planning process.

We have already set out a draft proposal which we have recently shared with RAPID and the All Company Working Group (ACWG) for consideration. We believe this would provide the clarity required for all parties while providing a practical solution as to what should be funded as baseline or enhanced expenditure.

We welcome an allowance for the continued development of the Severn Thames Transfer, which is one of many adaptive solutions in our regional plan. However, we were surprised that another adaptive solution, Beckton water recycling, didn't receive any allowances to continue its development from a design and consenting perspective.

These adaptive solutions need to be progressed further if, for some reason, other schemes in the regional plan cannot be delivered. These alternative schemes will enable us to adapt the regional solution should we face more challenging scenarios in the future, particularly if more water needs to be returned to the environment than is currently projected under the Environment Agency's Environmental Destination policy.

## **Demand reduction**

Key to securing the region's water resources over the next 10 years is the successful delivery of 850 million litres of water by reducing leakage and both household and business customers' consumption.

The ambitious reductions in leakage, per capita consumption (PCC) and business demand set out in our plan align with the government's target set out in the Environmental Improvement Plan (EIP). Achieving them requires action from water companies and the government to enable customers to make sustainable changes to their water use.

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<sup>1</sup> PR24 and beyond: Final guidance on long-term delivery strategies; Ofwat, April 2022.

Ofwat, in its consultation response to the regional plan, highlighted that there are some very challenging targets for companies to achieve which will require customers to play their part.

The South East companies have trail-blazed water metering with meter penetration reaching more than 80 per cent across the region. Likewise, they have made provision for an accelerated smart meter rollout, either to replace existing meters or install new ones.

The costs for replacement meters are easier to estimate compared to the costs of new installations that have not previously been metered, which are typically a more complicated process, more expensive to install and therefore harder to forecast. If companies are to meet their future PCC targets, these more difficult installations must be adequately allowed for in the final determination, otherwise, companies will fall short of their targets and the security of supplies will be at risk.

We urge Ofwat to review the average cost models that it has used for meter installations. Ofwat uses two econometric models to calculate smart metering allowances, one model for new installations and another for meter upgrades. The average cost models balance the cheap installations with the more expensive installations.

For companies which are starting their metering installation programmes, this conceptually makes sense as they can balance the cheaper installations with the more expensive installations. However, as companies near the end of their installation processes, meter installations are typically more expensive for a range of reasons, not least because the easier and cheaper installations have already been completed.

We consider that with some minimal alterations and explanatory factors, the meter installation unit cost models could be adjusted to better reflect meter installation costs against current meter penetration rates. A similar approach could also be taken for water efficiency and leakage, the costs for which could be adjusted based on several external factors.

We would also suggest that a meter unit cost approach for non-household meters is included in the suite of average cost models, as these meters are typically larger and have different installation costs than household meters.

The PCC profiles outlined in the regional plan and company WRMPs include savings associated with government policy interventions. We consulted on these interventions and savings during the development of the regional plan and used a government intervention strategy which aligned with the commitments set out in the EIP. A breakdown of these savings is provided in the regional plan, but for clarity, we expect that the Defra interventions would save three litres per person per day (l/p/d) by 2030 and up to 24 l/p/d by 2050.

We consider that the PCC targets for companies should be adjusted to reflect their activities alone and not those of the government. Alternatively, Ofwat could make an allowance for South East company targets during the next AMP period, based on the government interventions that have been put in place. For example, if the government interventions have not been delivered, then the PCC targets should be adjusted to take account of this.

In developing our regional plan, we have built on past regulatory decisions and followed best practice. It was for this reason that our non-household demand forecast included input from government economic growth factors, as well as recognising that some service sectors' growths are influenced by population and/or property growth rates.

An estimation of non-household growth built on a trend-based analysis alone, as used by Ofwat in its draft determination, will not support government growth ambitions. Therefore, Ofwat should reconsider the use of its non-household forecast and base it on the forecasts included in the company WRMPs, which aligned with the Water Resources Planning Guideline (WRPG), that Ofwat co-authored.

### **Conclusion**

We are concerned about the significant cost reductions made by Ofwat in the Draft Determinations and urge it to consider the evidence provided by companies so that essential schemes are appropriately funded, as shortfalls in funding, not just efficient costs, increase the risk of non-delivery of these schemes

We hope our consultation feedback is useful; we would be more than happy to discuss any of the points we have raised in more detail.

Our key consideration in making this representation is to ensure customers and the environment in the South East continue to receive high-quality and resilient water supplies, which meet government expectations and put the correct foundations in place for future generations, all at a fair price.

Yours faithfully,



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