



The voice for water consumers  
Llais defnyddwyr dŵr

# **CCW's submission the Competition and Markets Authority on Southern Water's statement of case**

**22 April 2025**

## 1. Introduction

- 1.1 The Consumer Council for Water (CCW) is the statutory consumer organisation representing household and non-household water and sewerage consumers in England and Wales.
- 1.2 We welcome the opportunity to submit evidence to the Competition and Markets Authority (CMA) on Southern Water (SRN's) statement of case which sets out the company's arguments and evidence in its request for a redetermination of Ofwat's final determination for 2025-30.
- 1.3 In this submission we also offer additional evidence and commentary to assist the CMA in its redetermination and to provide important context for the consideration of cost and financing allowances that are central to the dispute between SRN and Ofwat.

## 2. Executive Summary

- 2.1 SRN argues that it is facing unprecedented investment requirements, notably a proposed £8.5 billion capital programme (including over £3 billion for environmental projects) over 2025–30. This is framed as a generational opportunity to improve environmental outcomes (eg reducing river abstraction, enhancing wastewater treatment and cutting storm overflows and pollution) while meeting statutory and performance obligations.
- 2.2 However, Ofwat's annual Service Delivery reports<sup>1</sup> show that SRN has consistently been one of the poorest performers in the sector and CCW's research shows it has the second lowest level of customer trust and satisfaction in the sector<sup>2</sup>.
- 2.3 CCW's research also shows that SRN customers has the lowest level of satisfaction with customer service<sup>3</sup> and with aspects of sewerage service<sup>5</sup>. SRN is also among the lowest in terms of customer satisfaction with the fairness and affordability of water and wastewater charges<sup>6</sup>. Any redetermination by the CMA needs to deliver outcomes that will help turn around the company's poor performance and negative customer opinion.

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<sup>1</sup> See 2023-24 Ofwat Service Delivery Report [here](#)

<sup>2</sup> As shown in CCW annual Water Matters surveys. See 2024 report [here](#).

<sup>3</sup> By customers who'd contacted Southern Water in the last 12 months

<sup>4</sup> [Customer contact matters: Insights from Water Matters 2024](#)

<sup>5</sup> [Environment matters: Insight from Water Matters 2024](#)

<sup>6</sup> [CCW Water Matters 2024 - what are the findings telling us? report](#)

- 2.4 The company's business plan for 2025-30 also received the lowest level of household customer acceptability (44%) and only 11% of customers found SRN's proposed bill increase to be affordable<sup>7</sup>.
- 2.5 Any increase in bills on top of the 53% (before inflation) already allowed for in Ofwat's FD will place additional pressure on customers already struggling to pay and will certainly further reduce customers' trust and satisfaction with the company if there are no additional tangible outcomes.
- 2.6 In the context of any increase, the CMA's assessment must account for what customers expect to receive as service and environmental improvements in 2025-30 and beyond. It must also increase the affordability support the company offers to assist customers at risk of water poverty. CCW expects the CMA to ensure the redeterminations show customers that costs are fair, are efficient and allow the company to deliver customer expectations.
- 2.7 Any bill increases resulting from the redeterminations must be clearly linked to measurable improvements in service reliability and environmental protection, rather than just providing additional funds without clear benefits.

### **3. Our submission**

#### **Cost allowances**

##### Base costs

- 3.1 Although CCW cannot assess the technical merits of either SRN's or Ofwat's approaches to base cost benchmarking and modelling, we believe there is a customer-focused context that the CMA must consider in its assessment of this dispute. In its redeterminations, customers would expect the CMA to remove any poorly evidenced expenditure, inefficient costs and any proposed costs for activities that have been funded previously.
- 3.2 Customers should be assured that the latest evidence on asset deterioration, climate risks, and independent cost assessments inform decisions on efficient costs they need to pay to ensure delivery of services that will improve and become more reliable, turning around the company's poor performance.

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<sup>7</sup> This research has not been published by Southern Water but is available to the CMA on request

- 3.3 Evidence that SRN customers prioritise the asset reliability that base cost allowances should deliver comes from multiple sources, including:
- The company's customer research - SRN's engagement activities, such as a long-term customer panel, surveys and focus groups, when triangulated, consistently show that customers place high importance on a reliable water supply<sup>89</sup>
  - Independent consumer research - CCW reports also indicate strong customer demand for asset reliability<sup>10</sup>
- 3.4 Together, these sources suggest that SRN customers see asset reliability as essential to their everyday service, making it a critical factor in investment and regulatory decisions over the next several years.
- 3.5 Customers should have confidence that the allowances set through the CMA's redetermination sufficiently mitigate operational risks - such as service failures - while balancing costs fairly between current and future customers. Addressing asset health now is crucial to preventing higher costs for customers in the long run. To align with customer priorities, it should explicitly link the adequacy of asset maintenance funding to the outcomes that matter most to customers particularly service reliability.

#### Enhancement costs

- 3.6 CCW cannot assess the relative merits of either Ofwat's or SRN's approach to enhancement cost modelling, but the CMA should recognise that customers support what the enhancement costs should deliver in its redetermination. The business plan shows that the two overwhelming priorities for customers (based on a triangulation of various sources of evidence) are service resilience and reducing pollution<sup>11</sup>. These are the two main outcomes the enhancement programme should deliver.

#### Past cost allowances

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<sup>8</sup> See [Southern Water's business plan 2025-30](#) page 48

<sup>9</sup> See [Southern Water's business plan annex SRN003](#)

<sup>10</sup> [CCW's research on understanding customer priorities \(February 2025\)](#) places leakage as the 3<sup>rd</sup> highest priority. [CCW and Ofwat research on customer preferences for PR24 \(April 2022\)](#) placed water supply interruptions as one of the highest priorities, with leakage ranked 'medium'.

<sup>11</sup> [Southern Water Business Plan 2025-30](#) page 48

- 3.7 SRN claims there has been chronic underfunding allowed over decades, which has led to the need to invest an extra £585 million above the allowed base cost to maintain its wholesale water asset base.
- 3.8 While there is evidence of overspending since 2020<sup>12</sup>, it is important to recognise that if companies overspend, then the costs are shared between company and customers.
- 3.9 It is not necessarily the failure to allow adequate cost allowances that has led to the company's poor performance because:
- The reasons for some of the overspend in the more recent years are related to energy costs and input prices following wider economic events, as Ofwat's reports confirm<sup>13</sup>.
  - Ofwat's approach is based on a notional efficient company model using industry median performance. SRN's higher spending could partly be due to internal inefficiencies rather than genuine regulatory underfunding.

### **Performance Commitments and Outcome Delivery Incentives (ODIs)**

- 3.10 CCW considers the set of Performance Commitments in the final determination to be a fair reflection of where the company needs to improve and reflect customer priorities. We disagree that this represents an overly harsh downside risk as the associated targets need to incentivise companies to invest in both immediate service improvements and long-term infrastructure resilience to meet customer expectations.

### **Price Control Deliverables (PCD)**

- 3.11 In principle, CCW supports PCDs as a way of giving customers and stakeholders transparency in what companies will deliver, when and at what cost. PCDs should expose failure, delays or under/over performance and allow bodies such as CCW, customers and stakeholders to scrutinise and challenge companies' delivery. PCDs will act as an incentive for

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<sup>12</sup> See [2023-24 Ofwat Service Delivery Report](#) page 30, which shows 60% cumulative overspend in wholesale water expenditure since 2020, while page 31 shows a 32% cumulative overspend in wholesale wastewater expenditure.

<sup>13</sup> See [2023-24 Ofwat Service Delivery Report](#) page 29

companies to deliver what is a significantly large investment programme in 2025-30. On this basis PCDs should be retained.

- 3.12 However, we would support some flexibility to prioritise investments where they are most needed. The regulatory regime for PCDs should allow companies to produce new compelling evidence of any risks or possible alternative solutions that were not available at the time determinations are made, that justifies a modification to PCDs. This will help ensure customers' money returns value, by addressing the highest risks, while retaining transparency and a strong incentive to deliver.

### **True-ups and cost uncertainties**

- 3.13 The redetermination must ensure that external cost uncertainties are not shifted onto customers without careful consideration. SRN (and indeed all companies) should absorb some of these risks through improved operational efficiency and prudent risk management, and not automatically pass uncertain cost allowances on to customer bills, especially during a price control period that is already placing a heavy burden on customers' bills.
- 3.14 A balance needs to be established so that customers are not overpaying for what are cost uncertainties during 2025-30, while avoiding a potential 'bill spike' for customers in 2030-31 due to an excessive number of upward costs true-ups.

### **Resilience and risks with extreme weather events**

- 3.15 SRN has been allowed £627 million in its final determination to increase the resilience of its assets, including from the effects of power outages and extreme flooding<sup>14</sup>.
- 3.16 The Ofwat final determination should not be increased in a way that transfers the full financial burden of extreme weather risks to customers, when effective asset management measures could mitigate some of these risks. However, as part of the appeals process, CCW would value an assessment of whether Ofwat has made the right balance between serving the needs of customers now and in the future. Customers should not bear the higher long-term costs resulting from deferred investments.

### **Financeability**

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<sup>14</sup> See page 17 of [Southern Water's PR24 final determination](#)

3.17 The Weighed Average Cost of Capital (WaCC) directly impacts how much water companies can recover through revenues, and it is a key driver of bills. Given the recent path of economic indicators, including interest rates and inflation, the CMA's redetermination presents an opportune time to review Ofwat's WaCC methodology, assumptions and potential impacts.

3.18 To inform the CMA's assessment, CCW has commissioned an independent report from MCC Economics (included as an appendix with our submissions). The report analyses whether Ofwat's view of the WaCC is a reasonable central estimate in the context of the overall risk/return framework. MCC's report considers (a) the methodology adopted (b) the data used and (c) the regulatory judgement applied.

3.19 Key findings in the report:

- Ofwat's PR24 final determinations lean toward the upper bounds of WaCC components. This may overstate the returns required for a notionally efficient water company.
- Ofwat's principle that companies bear the risk of deviating from the notional structure was not consistently applied. Risk has been shifted from shareholders to customers.
- Ofwat included data from companies with high gearing and low credit ratings. These conditions stem from shareholder decisions, not market pressures.
- Regarding embedded debt, Ofwat relied on actual debt issuance, including inefficiently financed companies. For new debt, Ofwat added a 30bps benchmark adjustment without sufficient justification.
- Ofwat's beta values may be overstated. MCC advocates for lower beta values and suggests using alternative models better volatility representation.

3.20 Based on this analysis and evidence, MCC Economics recommends:

- Setting a lower WaCC consistent with market evidence and notional company efficiency. MCC estimates the WaCC could have been 1.08% lower, saving £5.4 billion over 5 years - that's £41 per household per year.

- Allocating risks to companies rather than customers to avoid rewarding inefficient financial structures at customers' expense.

### Gearing

- 3.21 High gearing increases companies' financial risk and ultimately exposes customers to higher costs. As of 31 March 2024, SRN's gearing at 72%<sup>15</sup> is substantially higher than Ofwat's notional benchmark of 55% for PR24. The company is also categorised as needing a higher level of financial monitoring in Ofwat's assessment of financial resilience<sup>16</sup>.
- 3.22 As part of its redetermination, the CMA should assess whether SRN's gearing is sustainable in the long term. CCW questions whether a more balanced approach to capital financing would protect customers from the risks of volatile borrowing costs particularly in the current uncertain economic outlook

### **Customer engagement – evidence of priorities and expectations**

- 3.23 SRN carried out a substantial amount of research and customer engagement to support the development of its business plan. CCW is satisfied that the company carried out good quality research that considered a balance of informed and uninformed views and included representation of different customer groups by drawing together different kinds of samples and triangulating the results.
- 3.24 Overall, CCW is satisfied that SRN's business plan reflected the priorities of its customers, and we wish to see the CMA's redeterminations drive outcomes that address this.
- 3.25 However, Ofwat's price determinations have not been explicit in how it used customer evidence in its decisions. In our response to Ofwat's draft determination we noted that:
- Outside of the brief mention within the quality assessment summary, there was little explanation of the extent to which Ofwat has assessed the level of customer engagement and challenge of the business plan, or how it may have influenced its draft determinations.

<sup>15</sup> Page 27 of [Southern Water's Annual Performance Report 2023-24](#)

<sup>16</sup> As per [Ofwat's 2023-24 'Monitoring Financial Resilience Report'](#)



- Given the scale of research and engagement that took place to inform the company's business plan, summarising this effort in a few lines sends a signal that customers' views have not been adequately considered by Ofwat.

3.26 The final determination did not provide any new evidence to convince us how Ofwat took into consideration customer's views. The CMA's redetermination should be more explicit in how evidence from customers has influenced decisions.

### **Customer acceptability and affordability**

3.27 CCW commissioned quantitative research to test the package of bill changes, service improvements and investments in Ofwat's draft determination for customer acceptability and affordability<sup>17</sup>. This included surveys with a sample of 488 of SRN's household customers.

3.28 This revealed that:

- 49% of customers found the draft determinations' proposed bill increases unaffordable.
- 65% found the package of investment and service delivery improvements were acceptable.
- After being reminded of the bill increase, customers were asked again if they found the package acceptable, and this figure dropped to 47%.

3.29 There is a +9% difference in the average bill increase between the Draft and final determinations, so it is likely that a higher proportion of customers will find the revised bill difficult to afford. This would be exacerbated further by the impact of any further bill increase in a redetermination. Despite this, it is likely that they would still broadly support what the package should deliver.

3.30 In this context, whatever changes are made to address cost allowances, the CMA's redeterminations must retain the outputs for customers and the environment that the final determination set to ensure customers can see tangible benefits from bill increases.

3.31 SRN's business plan says that customers are willing to pay up to £7 more cross subsidy to support a social tariff (£20 per year in total), which means they can maintain support for the 158,000 customers that will be receiving the tariff by 2025.

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<sup>17</sup> [CCW draft determination testing research \(November 2024\)](#)

- 3.32 Overall, the scale of the bill increases (the largest in the sector) and the very low level of customers who found the plan affordable means that the proposed increase in affordability support is inadequate. SRN's business plan shows estimated that 152,000 customers will be left in water poverty by 2030<sup>18</sup>. That was based on a 2030 average bill of £681 - the Ofwat final determination is a bill of £642 before inflation.
- 3.33 At the time of the revised business plan (February 2024) the company estimate of those expected to remain in water poverty at 2030 was 199,000. This is more than the 158,000 the company forecasts will receive support by 2030. As the statement of case proposes a further bill increase, the volume of customers in water poverty will increase if this is approved, so the support proposed will not be sufficient. The CMA has an opportunity to require the company to go further to support people struggling to pay their bills.
- 3.34 CCW supports companies funding (or 'topping up') funds for affordability support from shareholders or parent companies and would welcome Southern doing so to align with other companies that provide this (eg Severn Trent, United Utilities).
- 3.35 We do not agree with SRN's argument that additional social tariff funding should be provided from future ODI penalties. ODIs are designed as performance incentives, so redirecting penalties to other purposes could:
- Dilute the deterrent effect of penalties
  - Reduce accountability for delivering service standards
- 3.36 This could be seen as helping the vulnerable at the expense of holding the company to account for poor performance. Directing ODI penalties to the social tariff is, in effect, adding to the cross subsidy as wider customers will not see any benefit in terms of a reduced bill or additional work - and this is done without them agreeing it.
- 3.37 This could set a precedent leading to companies becoming indifferent to penalties, knowing they can reallocate the funds to socially "acceptable" uses. It also would keep the funding in

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<sup>18</sup> As shown in [this data table](#) submitted as part of Southern's PR24 Business Plan (tab SUP15)

the business, and potentially reduce debt costs, causing a further deterrent to performing well.

- 3.38 The increased bills that SRN seeks carries a risk of more SRN customers falling below the water poverty threshold by 2030. The plan does not sufficiently show how the company will address this risk as the social tariff support is unlikely to meet the potential demand for assistance significantly.
- 3.39 In CCW's engagement with the company, it signalled its aim to be proactive at identifying customers who are struggling to pay. While this is a positive move, it needs to offer better assistance given the proposed bills and water poverty forecast.

### **Other issues**

#### Customer Experience (C-MeX) measures

- 3.40 CCW is disappointed that, despite extensive engagement with Ofwat, an additional metric to measure customer complaint volumes is not part of the proposed range of C-MeX components in the final determination or a standalone incentive.
- 3.41 Our annual complaints reports<sup>19</sup> show a continued increase in customer complaints across the sector in the last three years. High volumes of complaints are evidence of a poor experience by many customers and can be an indicator of more fundamental problems.
- 3.42 Measures of customer satisfaction alone may not adequately incentivise companies to resolve customer issues first time to prevent complaints and address the causes of complaints. Ofwat has shown how companies C-MeX performance has worsened over the current price control period<sup>20</sup>. As such, the CMA's redetermination is an opportunity for the Authority to include a separate performance commitment and ODI on the volume of complaints.

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<sup>19</sup> [Household customer complaints report 2024 - CCW](#)

<sup>20</sup> Ofwat's annual C-MeX reports show SRN's performance has declined from 74.6 points in 2020-21 to 66.87 points in 2023-24.

## **Enquiries**

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