

April 2025

PR24 redeterminations

Overview of our response to the statements of case

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1. Introduction

- 1.1 **We stand by our PR24 determinations.** They were the product of a collaborative, transparent and thorough four-year process, built on over thirty years of regulatory expertise and experience. They were supported by regular and meaningful engagement with water companies, customers, and a wide range of other stakeholders. Throughout our review, we consistently listened to feedback and responded to it, adapting our approach in response to new evidence or information. Our determinations reflect our regulatory judgement in light of all this evidence, exercised in line with our statutory duties.
- 1.2 Our determinations delivered the **largest package of water sector investment since privatisation**, which we expect to drive tangible performance improvements and economic growth. At the same time, PR24 had a strong focus on ensuring customers do not pay for inefficiency, past underperformance or risky financing choices. This was particularly important given the cost of living challenges many customers are facing. Water companies are monopolies, and customers rely on us to protect them from the excessive prices and poor service that would otherwise be disincentivised by market competition.
- 1.3 We set a package that anticipated the challenges that will come with delivering the step up in investment. For example, it significantly increased the levels of risk protection for companies compared with PR19. And 12 of 16 companies, including three of the disputing companies, now stand to earn net rewards on performance commitments (PCs) over 2025–30 simply for achieving their performance forecasts.¹ We set the allowed return such that an efficient company has a reasonable prospect of earning the base allowed return, taking account of the **overall calibration of the package of risk and return**. There is significant evidence that investors continue to see the water sector as an attractive investment.
- 1.4 The disputing companies' statements of case include a **significant volume of new information**. Four of the five companies have increased their total expenditure requests, compared to their representations on our draft determinations. They also **focus selectively on specific areas of the determinations**: for example, raising concerns about individual PCs, without consideration of the wider outcomes package. However, at PR24 we were required, and now the CMA is required, not to be so selective: we had to set determinations in a manner best calculated to meet all our statutory duties. We also heard from 16 companies during the PR24 process – ten of which subsequently accepted their final determination – as well as thousands of customers and other stakeholders.

¹ [OF-OU-077] Ofwat, ODI Payment Calculator – with performance forecasts, January 2025, tab 'Output by Company (with ASM)'.

- 1.5 We support the CMA's efforts to ensure customers and other stakeholders can meaningfully engage with the redeterminations process, like they did at PR24. Unfortunately, we consider the disputing companies' submissions **fall well short of the level of transparency and ownership we would expect to see** as part of a business plan submission for a price review, to support such engagement. For example, they provide varying levels of detail around customer bill impacts, with only one clearly providing a proposed bill profile for 2025-30. Some have changed their requests from previous versions of their plans, but the impact of some of these changes on outcomes and bills is unclear. If the sector is to regain public trust, companies must be more open with customers and other stakeholders about their proposals.
- 1.6 In response to the CMA's request, **we consider there are areas that could be deprioritised** from the redeterminations. This can help the CMA achieve its overriding objective, by focusing on issues that will have the biggest impact. In identifying these areas, we have considered where we already have mechanisms or ongoing processes to address the issue, or where our approach has broad support from the sector. We continue to be committed to giving the CMA all the assistance we can throughout the redetermination process, to help deliver the best outcomes for customers and the environment.

2. Our submission

- 2.1 On 21 March 2025, Anglian Water, Northumbrian Water, Southern Water, Wessex Water and South East Water (the 'disputing companies') provided us with their statements of case to the CMA, in respect of their references of the 2025–30 price controls for redetermination.
- 2.2 The disputing companies provided a significant volume of new information in their statements of case. This includes material changes compared to previous versions of their business plans. In some cases, companies have resiled from the latest view of their business plan, which we used to set our final determinations, and reverted to their 'original' plan. In others, companies have introduced new expenditure items or changed their requests, such as asking for a higher allowed return than proposed in their business plan. Companies have also provided significant new evidence to support their view. On expenditure allowances alone, the disputing companies have raised around one hundred issues; on the allowed return on equity, companies have submitted nearly 600 pages along with over one hundred databook files.
- 2.3 Given the time available and the volume of new information submitted, we have not sought to address each individual argument in full. While we have aimed to address key points raised in the submissions, it has not been possible for us to provide our comprehensive consideration of all points raised in the statements of case, even when supported by our economic and academic consultants. To reduce the burden on the CMA, we have signposted to published documentation where possible. Our final determinations publications remain the fullest account of why we made our decisions at PR24.²
- 2.4 In their statements of case, the disputing companies ask the CMA to consider significant amounts of new material in a challenging timescale. Some have even indicated that further changes to their proposals may be necessary later in the process. We are happy to assist the CMA to develop ways in which this new information can be assessed in a way that ensures different perspectives are heard. We would welcome the opportunity to feed into the CMA's deliberations on this new material, for example through the submission of working papers.
- 2.5 One option to manage new information and potential changes to company proposals would be to set a cut-off date for considering new evidence, as set out in section 5 of this document.
- 2.6 We have focused our submissions into the following structure:
- this document, which covers key high-level issues;

² [OF-OA-032] Ofwat, Final determinations in the 2024 price review, December 2024.

- a document for each key policy area focusing on the thematic issues: expenditure allowances, outcomes, and risk and return; and
- a document for each disputing company, which summarises our PR24 final determination and responds to company-specific issues.

- 2.7 We have indicated in our documentation where we have set out new information. In the majority of instances, we have done so in response to new information that was raised in the statements of case.
- 2.8 In our introductory submission to the CMA, we stated that our response to the statements of case would expand on some of the points we made in that document.³ This overview document therefore sets out further detail on the approach we took to PR24 (section 3) and how we addressed the key challenges of affordability, deliverability and financeability (section 4).
- 2.9 The CMA has also asked us to identify the issues we consider it should prioritise in its redeterminations. In section 5, we list a number of issues that we think could be deprioritised, allowing the CMA to focus on the areas that will have the biggest impact on outcomes and bills. This will help the CMA meet a challenging timeline and achieve its overriding objective: namely, to dispose of redetermination references fairly, efficiently and at proportionate cost within the prescribed time periods.⁴
- 2.10 At the same time, we think it is important that the redeterminations do not focus only on issues raised by the disputing companies. We welcome that the CMA has recognised this by inviting views from third parties on what issues, beyond those raised by the companies, it should consider as part of its redeterminations. This is important as there are some material areas that the disputing companies may have been less inclined to raise, since our decisions in these areas may have been seen as relatively 'favourable' to them. We set out some examples in section 5.
- 2.11 Finally, the CMA also asked us to set out how we fulfilled our statutory duties at PR24. We set this out in the Annex to this document, as well as addressing some of the main respects in which we and the companies differ as to whether the duties have been met.

³ [OF-OA-033] Ofwat, Reference of the PR24 final determinations: Introductory submission to the CMA, March 2025, p. 1, para 1.2.

⁴ [OF-OA-082] CMA, Water References: Competition and Markets Authority Rules, December 2024, p. 7.

3. Our approach to PR24

- 3.1 The water sector is at a critical juncture. It has lost public trust, and must now work to regain it. There is a real need for companies to provide better services and deliver lasting environmental improvements.
- 3.2 Our PR24 final determinations provide the sector with the opportunity for transformation, delivering better outcomes for customers and the environment. We have allowed record levels of investment over the next five years, backed by stretching but achievable targets to turn around company performance. This investment will also help unlock critical new infrastructure across England and Wales, boosting local growth.
- 3.3 By 2030, we expect this investment to bring tangible improvements. But we are clear that increased spending alone will not deliver the change required. Water companies need to change their approach: to become more innovative, dynamic, and proactive. We expect to see them on the front foot and to tackle issues head on – not to blame weather, third parties or external factors. Companies are better placed than their customers to manage and plan for these factors. We are encouraged that some companies are starting to take a forward-thinking approach, and need to see more showing the same sense of urgency and action.

The PR24 process

- 3.4 We developed the 2024 price review with the above issues at the forefront of our thinking. In December 2020, we kicked off the PR24 process with a call for ideas that highlighted the future challenges and opportunities for the sector.⁵ These included protecting and improving the environment in the context of climate change; achieving public confidence and affordability in the face of cost pressures; innovating and collaborating to transform performance; and anticipating and adapting to uncertainty and change.
- 3.5 We then published further consultations to inform our development of PR24. These invited feedback on our initial ideas around various elements of the price review, including cost assessment, PCs, outcome delivery incentives (ODIs), and risk and return, which built on our approach at PR19. We also set up a number of working groups and workshops to allow us to engage with companies and other stakeholders. For example, our Cost Assessment Working Group met 16 times from April 2021 to May 2023, covering a range of topics to help us improve our approach.⁶ Input from companies and

⁵ [OF-OA-035] Ofwat, PR24 and beyond: Future challenges and opportunities for the water sector, December 2020.

⁶ [OF-CA-002] Ofwat, Cost Assessment Working Group, May 2023.

stakeholders to these consultations and workshops informed our draft PR24 methodology, published in July 2022.⁷

- 3.6 We refined our approach by taking account of responses to our draft methodology, publishing our final PR24 methodology in December 2022.⁸ This included setting out our 'early 'view' of the allowed return. Our methodology reflected continued stakeholder feedback around the need to deliver on all the challenges originally identified in our initial call for ideas. We introduced several new environmental PCs. We improved and expanded our approach to cost modelling, anticipating the much larger enhancement programme that would need to be assessed. We continued our Innovation Fund from PR19, and doubled it to £400 million in our final determinations. And we required companies to deal with future uncertainties through robust long-term adaptive planning.
- 3.7 Following companies' PR24 submissions in October 2023, we published our draft determinations for consultation in July 2024.⁹ Taking into account representations made by companies and stakeholders, we then published our PR24 final determinations in December 2024, bringing to a close the final stage of the four-year price review process.¹⁰
- 3.8 We received and considered a number of company submissions over the process, with total expenditure requests rising from £96 billion in October 2023 to £112 billion ahead of our final determinations. This included an unprecedented increase in requested expenditure in response to our draft determinations. We also recognised early on that some companies' plans risked not being fully consistent with statutory obligations, and worked closely with companies and other regulators to allow changes to business plans, with some materially updated just three months before our draft determinations.
- 3.9 Overall, the PR24 process included 18 different consultations, alongside workshops, working groups and regular engagement with companies, customers, consumer and environmental groups, investors, and political stakeholders.¹¹ Nearly 6000 queries have been received and sent between us and companies, allowing companies many opportunities to explain and justify their plans, and for companies to have sufficient understanding of our decisions to be able to engage meaningfully.
- 3.10 We listened to feedback and responded to it, adapting our approach in response to new evidence or information. We reflected on the learnings of the 2020-24 period in calibrating the balance of risk and return. For example, after reviewing outturn 2023-24 company performance data, we reevaluated the profile and level of stretch in our

⁷ [OF-OA-036] Ofwat, Creating tomorrow, together: consulting on our methodology for PR24, July 2022.

⁸ [OF-OU-002] Ofwat, Creating tomorrow, together: Our final methodology for PR24, December 2022.

⁹ [OF-OA-037] Ofwat, Draft determinations, July 2024.

¹⁰ [OF-OA-038] Ofwat, Final determinations, December 2024.

¹¹ [OF-OA-033] Ofwat, Reference of the PR24 final determinations: Introductory submission to the CMA, March 2025, pp. 8-10.

performance commitment levels (PCLs). We increased our expenditure allowances by £16 billion from draft to final determinations, taking into account stakeholder representations. And throughout the process, we refined and revised our assessment of the allowed return. We reacted to changing statutory requirements, and in some cases needed to assess multiple versions of company plans. And we continue to adapt: for example, we are introducing a new cost change process for critical cost items where there was insufficient certainty to include them in our final determinations.

- 3.11 However, PR24 was also built on a long-standing framework that has been refined and improved over time. We set our determinations using the 'totex and outcomes' approach first introduced at PR14, which provides flexibility in how companies deliver improvements. Our determinations were set by reference to a notional capital structure, reflecting the approach applied in our decisions and those of other economic regulators since privatisation. In setting the allowed return, we followed the peer-reviewed guidance and recommendations on estimating the allowed return published by the UK Regulators Network (UKRN).¹² The UKRN process involved extensive engagement between regulators and the CMA, as well as public consultation.
- 3.12 We carefully considered the CMA's PR19 redeterminations in our approach to PR24. In a number of ways, our PR24 methodology aligned with the CMA's approach at PR19. However, like the CMA panel, we consider each price review in the context of the statutory duties, strategic priorities and objectives from the UK and Welsh Governments, policy challenges, and available information at the time. We evolve our regulatory approach, recognising both the need to follow due regulatory process and that companies and investors value the transparency and predictability of regulatory decision making.
- 3.13 Some of the disputing companies criticise our determinations for, in their view, not sufficiently reflecting the PR19 redeterminations. For example, Northumbrian Water states, in relation to the allowed return, that 'unfortunately, Ofwat has readopted some of the earlier positions that the CMA previously found to be wrong'.¹³ The company implies that the approach to setting the allowed return in the PR19 redeterminations must be reflected in future price reviews. Alongside the other economic regulators, we considered carefully the approach adopted by the CMA in its PR19 redeterminations. Following careful consideration and consultation, we applied some elements of the PR19 redetermination approach, and did not apply other elements. In its determination of the RIIO-2 appeals, the RIIO-2 CMA group stated that, while the CMA PR19 redetermination contains highly relevant material, 'this does not mean that it sets down the unquestionable methodological best practice from which a sectoral regulator cannot depart, nor that subsequent findings of a sector regulator are automatically (or even

¹² [OF-RR-015] UKRN, UKRN guidance for regulators on the methodology for setting the cost of capital, March 2023.

¹³ [OF-OA-002] Northumbrian Water, Statement of Case, March 2025, p. 15, para 45.

presumptively) wrong if they differ from it'.¹⁴ In any case, many of Northumbrian Water's proposals themselves depart from the PR19 redeterminations.

- 3.14 We stand by our PR24 determinations. They are the product of a collaborative, transparent and thorough four-year process, which was in turn built on over thirty years of regulatory expertise and experience. Our approach was, and continues to be, evidence-led. Therefore, if companies present sufficient new evidence, and the CMA considers this evidence to be in the scope of its redeterminations, we will accept the case for an adjustment. Equally, it is consistent with our duties to assist the CMA by providing our view where the disputing companies' proposals are not in the interests of customers and the environment.

Fulfilling our duties

- 3.15 Our PR24 determinations reflect our statutory duties. These duties require us to set price controls in the manner we consider is best calculated to, in summary: further the consumer objective, secure that the functions of water companies are properly carried out, secure that the companies are able (in particular, by securing reasonable returns on their capital) to finance the proper carrying out of those functions, and further the resilience objective.¹⁵
- 3.16 The CMA has asked us to set out how we have fulfilled our statutory duties in reaching our final determinations.¹⁶ We set this out in the Annex to this document, as well as addressing some of the main respects in which we and the companies differ as to whether the duties have been met.
- 3.17 The disputing companies argue that we have either not met our duties, or have failed to give appropriate weight to particular duties. We consider these arguments are simply disagreements as to the merits of decisions that we made in our final determinations. Our determinations were the result of an exercise in regulatory judgement on complex multi-faceted decisions. This is recognised in the wording of the Water Industry Act 1991, which requires Ofwat to carry out its functions 'in the matter which...it considers

¹⁴ [OF-OA-039] CMA, RII0-2 Final determination Volume 2A: Joined grounds: Cost of equity, October 2021, p. 46, para 5.120. See also, [OF-RR-015] UKRN, UKRN guidance for regulators on the methodology for setting the cost of capital', March 2023, p. 8.

¹⁵ The general statutory duties for most of our work that we summarise here are set out in section 2 of the Water Industry Act 1991: [OF-OA-040] Water Industry Act 1991. We also have secondary duties including duties that require us to set price controls in the manner we consider is best calculated to, among other things, promote economy and efficiency on the part of companies, as well as contribute to the achievement of sustainable development. We must also act in accordance with the UK and Welsh Government statements setting out strategic priorities and objectives for Ofwat, known as strategic policy statements (SPSs). We are also required to have regard to the principles of best regulatory practice (including the principles under which regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed). We also have other duties, set out in [OF-OA-041] Ofwat, PR24 final determinations: Our approach, December 2024, pp. 4–9.

¹⁶ [OF-OA-034] CMA, Water References: Competition and Markets Authority Guide, December 2024, p. 19.

is best calculated' to meet the various objectives and duties set out in subsections (2A) and (3) of section 2 of that Act.

- 3.18 We recognise that the CMA will also be exercising its judgement in its redeterminations, and it may be that it reaches a different view to our final determination on certain points. That would simply reflect the nature of the complex decisions that are taken in reaching a final view on each company's determination and the new information before the CMA.
- 3.19 Given the necessity of regulatory judgement, there are various aspects of our determinations where there were a range of reasonable approaches for the decision we arrived at. Where the impact of differences between us and the disputing companies would be relatively small, we would support deprioritising such issues, to help achieve the CMA's overriding objective. We identify in section 5 where we consider there are opportunities to focus the CMA's decisions on areas that have the biggest impact on customers.
- 3.20 We welcome that the disputing companies have also expressed a desire to focus the redeterminations process. However, there are some areas that the disputing companies may have been less inclined to suggest should be prioritised, as our decisions in these areas may have been seen as relatively 'favourable' to them, or new information may have emerged that is less favourable than that which informed our decisions. This imbalance further supports the case for prioritising issues with the biggest impact, bearing in mind the 'in the round' nature of our determinations.

Our PR24 framework

- 3.21 At PR24, we aimed to set a package that included efficient and justified expenditure allowances, stretching but achievable PCs, and a fair balance of risk and return.
- 3.22 In a sector consisting of natural monopolies, our price review aims to replicate some of the conditions companies would face if they operated in a competitive market. To remain competitive, companies in such a market would need to continually innovate and find efficiencies, improve service to customers, and manage a number of internal and external risks, with the ultimate aim of realising returns to investors. Left unchecked, investors and management of monopoly companies would face weak incentives to keep bills low, improve service, innovate, manage risks, and make certain strategic investments.
- 3.23 In a competitive market, customers would tend to choose water companies that provide better service for a lower price. However, household customers in England and Wales do not have this choice. It is therefore important that we set price controls on the basis of an efficient company with a notional capital structure. This is a company that is

efficient, achieves a reasonable level of return through a good level of operational and financial performance, and maintains a capital structure that supports long-term financial resilience and allows it to access finance on reasonable terms as and when it is required.

- 3.24 A company that is inefficient, delivers poor service, and fails to appropriately manage risk would find, in a competitive market, that its revenues and returns fall. This is because customers would switch to other companies. In the absence of this choice, our price controls protect customers from having to pay for inefficiency, poor performance or risky financing choices simply because they have no other option. We consider that customers should only pay for the efficient notional company.
- 3.25 PR24 therefore had a strong focus on ensuring customers do not pay for inefficiency, past underperformance or risky financing choices, consistent with the consumer objective, and our duties in the round. This is important at any price review, so that risk and return is appropriately allocated between customers and companies over the long term. It was particularly important at PR24, given the cost of living challenges many customers are facing. While customers and other stakeholders tended to support increased investment, there is no evidence of support for inefficient investment or unjustified returns to shareholders. We received consistent feedback that customers should not be asked to 'pay twice' for improvements already funded in previous determinations, or to pay for companies to address past non-compliance issues.
- 3.26 We made adjustments to our allowances to prevent customers paying twice for improvements that should have been delivered in previous price control periods, or were already covered by base expenditure allowances. We did not provide funding for regaining compliance with permit conditions. And we set our allowed return, and carried out our financeability assessment, using a notional capital structure. If the sector is to regain public trust, it must not ask its customers to pay for inefficient, risky or poor management decisions made by the 'actual company'.
- 3.27 Moreover, there are clear opportunities to outperform our determination and earn additional investor returns. This has been recognised by companies that have identified scope for outperformance in 2025-30, and/or whose investors have provided support through injecting new equity (see paragraphs 4.31 and 4.34).
- 3.28 At the same time, we fully recognise that the costs of operating are not the same for each company. For this reason, we included flexibility in our assessment to allow for such costs. We included a number of cost drivers in our benchmarking models that explained some differences in efficient expenditure between companies, such as – for base models – scale, treatment complexity and population density. Where companies provided evidence of unique, exogenous circumstances driving higher costs, in line with our assessment criteria, we made adjustments to the benchmarked allowance. For example, we considered cost adjustment claims and carried out deep dive engineering

assessments. We also invited input on whether it was more appropriate for PCLs to be company-specific, rather than common. And we made uplifts to the allowed return on debt for small companies, where this was supported by customers.

- 3.29 Some of the disputing companies argue that our PR24 framework did not enable sufficient consideration of their individual company circumstances. However, these arguments can be disentangled into two categories. Firstly, whether our determinations sufficiently accounted for factors outside of company control: we address their specific arguments elsewhere in our response to the statements of case. Secondly, whether customers should pay for inefficiency, poor performance or risky financing decisions. For the reasons set out above, we strongly consider adjusting for all of the latter would not be in the interests of customers and the environment.

An evidence-based approach

- 3.30 As a regulator of regional monopolies, we inevitably face the issue of information asymmetry. Water companies have a better understanding of the activities they directly manage, how much improvements will cost, and the potential for improvements in their performance. To incentivise companies to reveal this information to us – and as in previous price reviews – we offered financial rewards and penalties at PR24 to incentivise high-quality and ambitious business plan submissions. The information revealed is important for our comparative analysis, allowing us to challenge all water companies' cost estimates and performance forecasts.
- 3.31 Wessex Water sets out that 'information asymmetry concerns...are not borne out by evidence', arguing this is the case because 'the industry has not substantively and persistently out-earned the WACC historically'.¹⁷ While we agree that the 2020–24 period has been a challenging period, as set out in our 'risk and return – common issues' document, median total shareholder return has averaged 8.5% across the sector in the 2020–24 period, and 10.6% in the 2015–20 period. There is evidence of significant real equity outperformance prior to this. But even if Wessex Water was correct about historical returns, its argument does not consider the impact of our price review regime, which partially mitigates the asymmetry issue by incentivising companies to reveal information. If it did not do this, there would be a greater risk of setting allowances that are too high and targets that are not stretching enough, leading to windfall profits and poorer service.
- 3.32 Since companies hold the information we require to conduct a price review, the burden of proof lies with the company. We set clear expectations that companies provide sufficient and convincing evidence – or, where we considered the evidence bar should be set higher, compelling evidence – to support their business plans. For example, if companies cannot provide sufficient and convincing evidence for additional

¹⁷ [OF-0A-004] Wessex Water, Statement of Case, March 2025, p. 79, para 9.71.

expenditure allowances, it raises concerns that proposals are poorly developed and costed. In expenditure areas where we have robust cost benchmarks, we require compelling evidence to adjust allowances, as companies need to justify why these benchmarks are not appropriate for their circumstances. We provided guidance in our PR24 methodology on the criteria we would use to assess company evidence, such as for cost adjustment claims, enhancement investments, and bespoke PCs.

- 3.33 However, we faced some challenges at PR24 relating to the quality of the information provided by companies. Three business plans, including those provided by Southern Water and Wessex Water, failed to meet our minimum quality expectations by the draft determinations stage of the process.¹⁸ In some cases, we needed to assess multiple versions of company plans, with some companies submitting new information, including consultancy reports, late in the process. There were also cases where new information was submitted too late for us to have reasonably been able to consider it fully and reflect it in our final determinations.
- 3.34 In some cases, we concluded in our PR24 determinations that allowing investment to improve service was in the interests of customers and the environment, even though we retained concerns around the quality of evidence provided. For example, we provided South East Water with an allowance of £228 million for resilience enhancement.¹⁹ We recognised that the company's poor performance indicated a residual risk that additional investment may be needed during 2025–30. To manage this residual funding risk, we provided a contingent allowance of £50 million. We deemed this allowance necessary as a result of the company's failure to properly evidence its proposed investments. This is contrary to claims made by some disputing companies that our regime is set up to minimise expenditure allowances and customer bills.
- 3.35 In their statements of case, the disputing companies have now presented significant amounts of new information and evidence that was not available to us during the price review process. Four of the five companies have increased their total expenditure requests compared to their representation on our draft determination; the remaining company, Wessex Water, has reverted to its original, higher, business plan proposal for water base expenditure. Some disputing companies have even indicated that further changes to their proposals may be necessary later in the redeterminations process.²⁰
- 3.36 We have identified that new submissions relevant to the allowed return on equity alone amount to nearly 600 pages, accompanied by over one hundred databook files. While we have aimed to address key points raised in the submissions, it has not been possible for us to provide our comprehensive consideration of all points raised in the statements of case, even when supported by our economic and academic consultants. In a number

¹⁸ [OF-OA-042] Ofwat, PR24 draft determinations: Quality and ambition assessment summary, July 2024, pp. 7–11.

¹⁹ [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, February 2025, pp. 224–227.

²⁰ [OF-OA-002] Northumbrian Water, Statement of Case, March 2025, p. 16, para 53; and OF-OA-003 Southern Water, Statement of Case, March 2025, p. 51, para 81.

of instances, it has been necessary to request additional information from the firms representing the interests of the disputing companies, where information was not provided in initial submissions or was not fully transparent. We consider it a fundamental expectation that information on which our determinations are made should be transparent and accessible to a range of stakeholders. Where information does not meet these expectations, or where new information is provided at a late stage in the overall price review process, we consider there should be a high bar in determining the weight that should be placed on it for the purposes of setting a determination. Points that are not addressed in our response should not be interpreted as our tacit agreement to those made in the statements of case, and we reserve the right to make further representations on this information to the extent that it is relied upon for setting a redetermination.

- 3.37 We have concerns with the quality and selectivity of information presented to the CMA by the disputing companies in relation to the allowed return. Three companies are proposing an allowed return on equity that is higher than proposed in their representations to the draft determinations, driven partly by their decision to step back from parts of their evidence base that point to a lower figure, and reflecting requests for a greater 'aim up' of the allowed return.
- 3.38 We do not agree with the implication that we have failed to reflect all the available evidence in reaching our determination of the allowed return. We understand and have taken into account that the available evidence for each cost of capital parameter spans a wide range. We have engaged with arguments put forward on all elements of the allowed return. In reaching our estimate, we have also taken into account the considerable weight of evidence pointing to a cost of capital lower than we have allowed. In our 'risk and return – common issues' document, we set out for example, evidence that:
- our point estimate for the risk-free rate could be lower if we placed weight on 10 year RPI-linked gilt yields (rather than just the 20 year) – in line with our 10–20 year CAPM horizon;
 - some estimators of historical total market return (TMR), and evidence of serial correlation, support a range of TMR estimates below our 6.83% point estimate from final determinations;
 - our embedded cost of debt allowance is close to the industry average, despite higher actual gearing and weaker actual credit ratings than our notional company benchmark; and
 - the treatment of inflation in our determination process provides scope for financing outperformance where (as currently) inflation is above the Bank of England's 2.0% inflation target.
- 3.39 All disputing companies have pointed to the higher capex in relation to the regulatory capital value (RCV) at PR24, relative to PR19. However, we have also taken into account

that the scale of capex is not exceptional relative to UK price controls generally. We have directly addressed the challenges associated with the increased investment programme and past performance through the recalibration of the risk and incentive package at PR24. And while companies have underperformed on operational incentives during 2020-24, this must be considered alongside collective outperformance on financing costs and the positive impact of inflation during the same period (see paragraphs 4.30 and 4.33).

- 3.40 The disputing companies argue that they require an allowed return of up to 4.58%, well above our final determination of 4.03%. However, based on the factors above, an allowed return on capital up to one percentage point lower than our final determination would be just as credible a reflection of the available parameter evidence and would not require us to depart fundamentally from the methodology we consulted and decided on.
- 3.41 Other companies that have accepted our final determination have recognised the work we have done to consider all the available evidence. A submission from Pennon Group notes that we 'took a proportionate, evidence-based approach' to determining the allowed return.²¹ This, it states, resulted in an 'appropriate balance between risk, affordability and investor return' based on a 'level of engagement [that] was extensive and unprecedented in our experience'. Consistent with the advice from our advisors CEPA, Pennon's submission concludes that our overall package is consistent with a valuation that allows it to continue to raise capital, as confirmed by its recent £490 million equity raise.
- 3.42 The disputing companies' estimates reflect a selective presentation and interpretation of the cost of capital evidence. The evidence presented undermines the considerable analysis and debate that we, the companies and other stakeholders have carried out over the four years from publishing our initial call for ideas in December 2020 to our final determinations in December 2024.
- 3.43 To set expenditure allowances and stretching but achievable PCLs, we mitigate information asymmetry using cross-company benchmarking models. We benefit significantly from having 16 companies in the water sector to use as comparators, which is higher than in other regulated monopoly sectors. Benchmarking allows us to compare historical and forecast costs and service levels across companies, to estimate an efficient cost or an appropriate target level.
- 3.44 Some of the disputing companies argue our cost assessment was over-reliant on econometric benchmarking models. However, we consider using benchmarking models as our primary tool for setting expenditure allowances across multiple companies is the most appropriate approach. Top-down models are vital as they can capture interactions

²¹ [OF-OA-043] Pennon Group, PR24 Redetermination – Third Party Submission, April 2025.

and trade-offs between different costs, reducing the risk of setting an unachievable cost challenge, and enable consistency of approach across companies.

- 3.45 Our models produce robust results that align with engineering and economic rationale. Internal and external engineering experts played an integral role in model development so that the models have a clear engineering rationale and capture the key cost drivers that explain differences in efficient expenditure between companies and over time. As we explain in our 'expenditure allowances – common issues' document, we undertook a number of exercises in recognition that no model is perfect, including cost adjustments and deep dive assessments. We also made adjustments where future costs are likely to be different to those incurred in the past, for example on energy and phosphorus removal. Individual econometric models will rarely attract universal acceptance across all companies, as by definition not all companies will turn out above or at our benchmark.
- 3.46 Some of the disputing companies propose alternative cost assessment approaches that may be practical for their specific circumstances, but may not be proportionate or effective if they were applied across the sector. Companies who accepted their final determination have not raised concerns with our cost drivers, and changes in cost drivers will impact the allowances for all disputing companies and potentially all companies if reflected in benchmarks for PR29.²² As at PR24, we will continue to consult and engage with companies and stakeholders on our framework ahead of the next price review.

²² In its submission to the CMA, Pennon Group states it does not consider suggestions to adopt new cost drivers, or exclude 'proven variables', are appropriate. See [OF-OA-043] Pennon Group, PR24 Redetermination – Third Party Submission, April 2025.

4. Key issues

- 4.1 In our introductory submission, we set out that the key challenges at PR24 are affordability, deliverability and financeability.²³ We stated that the disputing companies were most likely to draw attention to the last one of these challenges. This is borne out by the statements of case.
- 4.2 It continues to be important to be duly mindful of these key challenges of affordability, deliverability and financeability. We were required, and now the CMA is required, to set the PR24 determinations in a manner best calculated to meet all applicable statutory duties: in particular, to further the consumer objective, to secure that the functions of the companies are properly carried out, to secure that the companies are able (in particular, by securing reasonable returns on their capital) to finance the proper carrying out of those functions, and to further the resilience objective. We address each of the three key challenges in this chapter.
- 4.3 The selectiveness of the statements of case underlines the importance that all stakeholder voices continue to be heard during the redeterminations process.
- 4.4 In their statements of case, some of the disputing companies cited acceptability research which indicated customer support for their original business plan.²⁴ We agree it is important that the customer voice is heard. However, this research did not see customers consider bill impacts alongside the proposed investments. When we and CCW commissioned research on the draft determinations, 75% of customers found the proposed investments acceptable, but this reduced to 58% when they considered the proposed bill changes.²⁵ Bill increases in our final determinations were higher than in our draft determinations, and the disputing companies would like to increase bills significantly higher than that, which is likely to further reduce customer support for company plans.
- 4.5 We heard from customers and consumer representatives throughout the price review process. For example, around 700 people attended our 'Your water, your say' sessions in July 2024, with nearly 120 responding to our subsequent survey. Over 100 individual members of the public made formal representations on our draft determinations, and we received around 17,000 emails as a result of campaigns. Common topics included concerns about bill increases, approaches to tackling environmental issues such as 'forever chemicals' and storm overflows, and company performance.

²³ [OF-OA-033] Ofwat, Reference of the PR24 final determinations: Introductory submission to the CMA, March 2025, pp. 1-4, paras 1.5-1.13.

²⁴ For example, [OF-OA-002] Northumbrian Water, Statement of Case, March 2025, p. 6, para 4; [OF-OA-005] South East Water, Statement of Case, March 2025, p. 5, para 1.9.

²⁵ [OF-OA-044] Impact Research, Draft Determination Research 2024, p. 4.

- 4.6 Many customers argued they should not pay to address infrastructure issues where maintenance had already been funded through bills, or for companies to resolve non-compliance issues. Nor should they 'pay twice' for improvements already funded in previous determinations. These principles were a strong focus for us in setting our determinations. Should the CMA set companies higher expenditure allowances than in our final determinations, an option would be to adjust PCLs so that customers receive better service in return for paying higher bills, and to put in place mechanisms to protect customers against late delivery or non-delivery, such as price control deliverables (PCDs).
- 4.7 As with our 'Your water, your say' sessions, we are open to funding an independent Chair to facilitate direct engagement between the CMA and customers during the redeterminations process.

Affordability

- 4.8 Our research has found that one in five bill payers are currently struggling to afford their water bill.²⁶ Two in five said they would find the proposed bill in our draft determinations difficult to pay.²⁷ This was based on an average bill increase of 21% for water and wastewater companies from 2024-25 to 2029-30, and our analysis suggests that, on average, the four disputing water and wastewater companies are seeking an increase of between 42% and 46% in their statements of case.²⁸ It follows that a very significant proportion of customers are likely to find it difficult to pay the bill proposed by the disputing companies.
- 4.9 In this context, it is crucial that customers, consumer representatives and other stakeholders are able to meaningfully engage with the redeterminations process. We strongly support the CMA's requirement for companies to explain the impact of their requests on current and future customer bills.²⁹ The disputing companies' statements of case set out varying levels of detail around bill impacts. Only one disputing company has clearly set out a bill profile for 2025-30 in its statement of case, and Southern Water did not provide a bill estimate. Where we have identified bill profiles, we present them in Table 1.1.
- 4.10 We have also found it difficult to estimate bill impacts based on companies' requests, as in some cases companies were not clear about the expenditure allowances or the

²⁶ [OF-OA-045] Ofwat, Cost of living: wave six – water customers' experiences, December 2024.

²⁷ [OF-OA-044] Impact Research, Draft Determination Research 2024, p. 4.

²⁸ As set out below, it is unclear whether the uplifts stated by Anglian Water and Southern Water represent an increase to our final determination % bill increase or an increase to our final determination bill figure, so we present a range that includes both. South East Water's draft determination included an 8% bill increase from 2024-25 to 2029-30, and it requests an increase of around 47% in its Statement of Case. We do not include South East Water here because its bill figure does not include the cost of wastewater services and so is not directly comparable.

²⁹ [OF-OA-034] CMA, Water References: Competition and Markets Authority Guide, December 2024, p. 19, para 4.4.

allowed return they were seeking. This falls well short of the level of transparency and ownership we would expect to see as part of a submission for a price review, where we would also ask each company to accompany its business plan with an assurance statement on behalf of the company's Board to demonstrate the company has challenged and satisfied itself on the contents of the plan, and that the Board owns and is accountable for the submission.

Table 4.1 Bills presented in the statements of case (£, 2022-23 prices)³⁰

Company	2024-25	2025-26	2026-27	2027-28	2028-29	2029-30
Anglian Water ³¹	491	-	-	-	-	695-714 [*]
Northumbrian Water ³²	422	463	518	523	528	545
Southern Water	420	-	-	-	-	- ^{**}
Wessex Water ³³	508	575 [*]	645 [*]	658 [*]	658 [*]	658 [*]
South East Water ³⁴	232	-	-	-	-	341

^{*} Estimated based on other information provided in the statement of case, see footnote.

^{**} Southern Water did not provide any bill details in its statement of case

- 4.11 Water bills need to rise to fund record investment. However, bills should be no more than they need to be. There is no evidence of customer support for inefficient investment or unjustified returns to shareholders.
- 4.12 Some disputing companies imply we have focused unduly on keeping bills low at previous price reviews, and that this has led to underinvestment. However, PR19 sector base expenditure allowances were only 0.4% less than companies requested, and PR14 wholesale total expenditure allowances were only 1% less than companies requested.³⁵ This does not support the view that we have applied overly stretching cost efficiency challenges and prioritised keeping water bills low at previous price reviews.

³⁰ 2024-25 bill values are populated from [OF-OA-014] Ofwat, PR24 final determinations: Our approach, December 2024, pp. 33-34, Table 3, based on company business plan data. Anglian Water stated the impact of its Statement of Case would be a 13.06% uplift by 2029-30. It is unclear whether this uplift represents an increase to our final determination % bill increase or an increase to our final determination bill figure, so we present a range that includes both. Northumbrian Water set out a bill profile for 2025-30. Southern Water did not provide a bill estimate. Wessex Water provided a line graph from which values have been manually estimated. South East Water provided an estimate of the bill impact in 2029-30, but no bill profile for 2025-29.

³¹ [OF-OA-001] Anglian Water, Statement of Case, March 2025, p. 21, para 75.

³² [OF-OA-002] Northumbrian Water, Statement of Case, March 2025, p. 17, Figure 1.

³³ [OF-OA-004] Wessex Water, Statement of Case, March 2025, p. 12, Figure 1.

³⁴ [OF-OA-005] South East Water, Statement of Case, March 2025, p. 11, Table 1.1. The bill for South East Water does not include the cost of wastewater services.

³⁵ [OF-CA-020] Ofwat, PR19 final determinations: Securing cost efficiency technical appendix, December 2019, p. 167, Table A1.2; [OF-OA-046] Ofwat, Setting price controls for 2015-20: Final price control determination notice: policy chapter A3 – wholesale water and wastewater costs and revenues, December 2014, p. 4.

- 4.13 Further, our price review methodology does not aim for a particular level of customer bills. The level of bills is a product of the components on which the determination is based, which in turn contribute towards the company's revenue allowance. At PR19, the key drivers of the reduction in bills were the reduction in the allowed return on capital – reflecting prevailing market conditions – and retail costs, as well as an increase in customer numbers.
- 4.14 At PR24, there were elements of our final determinations where we could have reasonably chosen an option that would have reduced bills in the short term, but elected not to. For example, we used a point estimate for the allowed return on capital at the top of our range of reasonable estimates to support investment and investor confidence. However, a different reading of the evidence at the time could have supported a lower point estimate. Our consultants, CEPA, considered a figure of 4.75% as their point estimate for return on equity was more appropriate, compared to our 5.10%.³⁶
- 4.15 We could also have capped expenditure allowances where our models provided a higher allowance than what the company requested. For example, Anglian Water received an enhancement allowance £111 million higher for the wastewater network plus controls than it stated it required.³⁷ Northumbrian Water's water enhancement allowance is £10 million higher than requested and its retail allowance is £11 million higher.³⁸ This means customers pay for allowances that are higher than what companies stated they needed. However, we chose not to cap allowances at a price control level, as this can help incentivise companies to reveal efficiencies at future price reviews.
- 4.16 Further, it is the nature of benchmarking models that, at a granular level, some individual allowances will be higher than requested, and some will be lower. Aggregating and triangulating multiple models increases confidence that overall allowances are sufficient, and where benchmarking is unsuitable or unachievable, we use deep or shallow dives where appropriate. We took an in-the-round approach to expenditure allowances and satisfied ourselves that the overall allowances for each expenditure area, and for the company as a whole, were likely to be sufficient for the company to deliver its programme. Some of the disputing companies request higher enhancement allowances in some areas, without suggesting corresponding areas in which the models may have been 'favourable' to the company and where downward adjustments could be appropriate. Therefore, where the CMA is minded to set higher allowances in particular areas, one option would be to make downward adjustments in other areas.

³⁶ [OF-OA-047] CEPA, PR24 Cost of Equity, December 2024.

³⁷ [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, February 2025, p. 384, Table 54.

³⁸ [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, February 2025, pp. 384-385, Tables 54 and 55.

4.17 As part of our PR24 methodology, we called on companies to support customers to pay their bills, using social tariffs and other methods.³⁹ The disputing companies highlight measures they are taking to support customers who are struggling to pay their bill. While we welcome this support, it will mostly be funded through cross-subsidy from other customers, which can place pressure on affordability. To help third parties engage with the redeterminations process, we would welcome clarity on how much the disputing companies' shareholders propose to commit financially to affordability support measures. Our analysis of company business plans at final determinations showed that, on average, shareholder funding for affordability support measures was 0.17% of return on regulated equity (RoRE); four of the disputing companies proposed significantly less than this.⁴⁰ The CMA may consider ensuring that companies can be held to account for shareholder commitments. We do not agree with Southern Water's proposal to part-fund social tariffs through underperformance payments, which would effectively mean customers not on social tariffs are inadequately compensated for poor performance.

Deliverability

4.18 Our PR24 determinations quadrupled allowances for enhancement investment compared to PR19, to £44 billion across the sector. Companies are likely to face challenges in delivering this significant step up. If the sector is to regain public trust, it is critical that it delivers – and is seen to deliver – the schemes that customers are funding.

4.19 Some have struggled to deliver the PR19 programme, with the disputing companies having underspent their enhancement allowance in 2020–24 by 7% to 28%.⁴¹ Across the sector, the underspend is £1.7 billion on a £10.7 billion allowance. We have seen examples in the 2020–25 period where companies have not delivered enhancement schemes they promised, or where they will be delivered later than planned. This includes:

- Anglian Water's internal interconnection programme, where as of February 2024 it forecast delivery of less than half the agreed capacity by the original date in 2025, and is not planning to deliver some schemes at all;⁴²

³⁹ [OF-OU-002] Ofwat, Creating tomorrow, together: Our final methodology for PR24, December 2022, p. 156, Table 11.4.

⁴⁰ Anglian Water (0.06%), Southern Water (0.09%), Wessex Water (0.01%) and South East Water (0.04%). Northumbrian Water's figure was 0.23%. See [OF-OA-048] Ofwat, Summary of water companies' published plans for affordability for 2025–30, December 2024, p. 10.

⁴¹ Anglian Water (18%), Northumbrian Water (28%), Southern Water (26%), Wessex Water (16%) and South East Water (7%). See [OF-OA-049] Ofwat, Data for the Water Company Performance Report 2023–24, October 2024, tab 'Enhancement Data'.

⁴² [OF-OA-050] Ofwat, Outcome delivery incentives model 24/25 – Anglian Water, December 2024, tab 'Override_Additional info'.

- Northumbrian Water's improvements to its Howden wastewater treatment works, where the company is forecasting a 60-month delay to the growth elements of the scheme;⁴³
- Southern Water's delivery of long-term supply-demand schemes, with only two of 10 schemes now expected to be completed by the original date in 2027, and four schemes either cancelled or delayed indefinitely;⁴⁴ and
- Wessex Water's full to flow treatment WINEP requirements at its Avonmouth wastewater treatment works, where it secured an extension from the Environment Agency from 2025 to 2028.⁴⁵

4.20 Further, Southern Water has requested additional allowances to deliver water resilience and supply schemes that it had committed to deliver, and was funded for, in the 2020-25 period. As explained in our 'response to Southern Water's statement of case' document, this includes rebuilding a water treatment works that it committed to Defra would be complete by February 2024.

4.21 Given the learnings from PR19 and likely delivery challenges at PR24, our PR24 determinations included a number of measures to protect customers from late delivery or non-delivery, and to increase transparency. This included introducing price control deliverables (PCDs) to incentivise companies to deliver schemes on time.

4.22 We have used versions of PCDs in a number of our previous determinations. At PR19, we set bespoke PCs to incentivise delivery of particular schemes, such as Anglian Water's internal interconnection programme. PCDs are also used in other sectors, such as energy. At PR24, we expanded these incentives to encourage companies to deliver the outputs that customers are paying for. While this will bring an additional administrative burden to companies and Ofwat, we consider this is proportionate compared to the overall scale of investment and need to protect customers. PCDs also offer additional opportunities for companies to enhance returns, by rewarding on-time delivery.

4.23 In response to our draft determinations, stakeholders generally supported the introduction of PCDs. British Water, which represents the industry supply chain, argued that companies need to spend more consistently across the price review period, and to deliver schemes at greater pace, rather than backloading programmes. We have encouraged this by introducing time incentives on PCDs, as well as extending our transitional expenditure programme to both 2023-24 and 2024-25, so that companies could make an early start on their PR24 programmes. We are continuing to work with the sector to further develop our approach to monitoring delivery of PR24, with the first draft delivery plans due for submission in May 2025. We consider it is vital that we have

⁴³ [OF-OA-051] Ofwat, Outcome delivery incentives model 24/25 – Northumbrian Water, December 2024, tab 'Override_Additional info'.

⁴⁴ [OF-OA-052] Ofwat, Outcome delivery incentives model 24/25 – Southern Water, December 2024, tab 'Override_Additional info'.

⁴⁵ [OF-OA-053] Ofwat, 'Outcome delivery incentives model 24/25 – Wessex Water', December 2024, tab 'Override_Additional info'.

tools to incentivise and hold companies to account to deliver the investment they have promised.

- 4.24 As set out in our introductory submission, there are increasing concerns about how water companies are performing. These concerns are evident from customer research, our monitoring of company performance, and our enforcement cases. We have ongoing enforcement activities with all the disputing companies,⁴⁶ and in the last two years Anglian Water, Southern Water and South East Water have been categorised as 'lagging behind' in our Water Company Performance Report.⁴⁷
- 4.25 In some areas, company performance is unacceptable. We expect to see companies take an innovative and proactive approach to solving the problems facing the sector. Record investment alone will not deliver the sustained improvements to services and the environment needed to rebuild public trust. We are clear that changes in company culture are essential for lasting change. Too often, we hear that shortcomings are due to weather, third parties or external factors.
- 4.26 It is disappointing to see this continue in some of the statements of case. For example, South East Water attributes its past performance to the effects of climate change, customer behaviour, and regulation, and states that 'there is a high likelihood that our customers will continue to experience significant interruption events' under the final determination.⁴⁸ Anglian Water states that 'underfunding' and 'unachievable performance expectations' under its PR19 redetermination set by the CMA caused delays in delivery and a deterioration in performance.⁴⁹ Southern Water argues that it should not receive financial penalties for poor performance where it is caused by severe weather.⁵⁰ We consider it is crucial that companies plan for and react effectively to the effects of severe weather, as they are better placed than customers to manage its impact. We included urban rainfall in most of our wastewater base models to reflect company-specific impacts, as well as providing uplifts to enhancement allowances for improving resilience to climate change.

⁴⁶ For Northumbrian Water, we have consulted on an enforcement order and penalty for failing to comply with its responsibilities to deal with wastewater, and for failing to effectively plan and manage those responsibilities: see [OF-OA-054] Ofwat, Thames, Yorkshire and Northumbrian Water face £168 million penalty following sewage investigation, August 2024. Anglian Water and Wessex Water are under investigation for the same issue: see [OF-OA-055], Investigation into sewage treatment works and sewerage networks, March 2025. We are monitoring the steps Southern Water is taking to achieve compliance following our enforcement action in 2019 and assessing if any further action is required: see [OF-OA-056] Investigation into Southern Water's wastewater treatment sites and the company's reporting of relevant compliance information to us, October 2019. We are also investigating whether South East Water has failed to develop and maintain an efficient water supply system and to plan and manage that statutory responsibility: see [OF-SEW-007] Enforcement case into South East Water's supply resilience, November 2023.

⁴⁷ [OF-OU-017] Ofwat, Water Company Performance Report 2023-24, October 2024; [OF-CA-080] Ofwat, Water Company Performance Report 2022-23, September 2023.

⁴⁸ [OF-OA-005] South East Water, Statement of Case, March 2025, pp. 3-6, paras 1.3-1.4, 1.12.

⁴⁹ [OF-OA-001] Anglian Water, Statement of Case, March 2025, p. 1, para 4.

⁵⁰ [OF-OA-003] Southern Water, Statement of Case, March 2025, pp. 41, 82, paras 45, 138.

- 4.27 Expenditure allowances and service expectations are linked to each other. At PR24, we improved the link between cost allowances and service expectations, so that we set targets that could be achieved by efficient companies with expenditure allowances. However, this does not mean increased spending inherently results in improved performance. Based on the 2019–24 period, we found no evidence to suggest that cost efficient companies perform poorly on outcomes.⁵¹ Similar findings were revealed in our analysis at PR19 and the CMA's PR19 redeterminations.⁵² Companies can achieve performance improvements by implementing better practices. Providing inefficient allowances risks disincentivising companies from making these changes.
- 4.28 Our PR24 determinations set stretching but achievable targets for each company. We highlight that Northumbrian Water, Wessex Water and South East Water stand to earn net outperformance payments over 2025–30 simply for achieving the PCLs they forecast in their representations. Overall, this is the case for 12 of 16 companies in the sector.⁵³ The four companies that forecast net penalties – Anglian Water, Southern Water, Thames Water and Yorkshire Water – have all been categorised as 'lagging behind' in at least one of our last two Water Company Performance Reports.⁵⁴ We consider it is right that poor performers financially compensate their customers for their performance and are incentivised to improve for customers and the environment.

Financeability

- 4.29 Our PR24 determinations recognised that the step up in investment will require companies to raise significant amounts of debt and equity finance. Our determinations allow efficient companies to maintain a credit rating that is well within the investment grade at Baa1/BBB+, and include a range of protections that are designed to support efficient companies to raise finance on reasonable terms.
- 4.30 Reflecting on company performance in the 2020–24 period, and the need to support companies to deliver increased levels of investment in 2025–30, our PR24 determinations significantly increased the range and scope of risk and uncertainty mechanisms compared with PR19.⁵⁵ The effects of the recalibration of the risk and return package must be considered alongside other requests to adjust cost allowances

⁵¹ [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, February 2025, pp. 276–281.

⁵² [OF-OA-057] Ofwat, PR19 final determinations: Overall stretch on costs, outcomes and cost of capital policy appendix, December 2019, pp. 36–48; [OF-CA-013] CMA, Anglian Water Services Limited, Bristol Water plc, Northumbrian Water Limited and Yorkshire Water Services Limited price determinations: Final report, March 2021, p. 29, para 74.

⁵³ [OF-OU-077] Ofwat, ODI Payment Calculator – with performance forecasts, January 2025, tab 'Output by Company (with ASM)'.

⁵⁴ [OF-OU-017] Ofwat, Water Company Performance Report 2023–24, October 2024; [OF-CA-080] Ofwat, 'Water Company Performance Report 2022–23', September 2023.

⁵⁵ The scale of risk protections at PR24 is extensive, so this document provides an inexhaustive summary. We set out a more comprehensive list in [OF-OA-019] Ofwat, PR24 final determinations: Aligning risk and return, December 2024, pp. 15–17.

or revisit the allowed return. Around 55% of total wholesale expenditure will be covered by reconciliation adjustments related to external input price factors, compared to 30% at PR19. This is in addition to:

- indexation of the RCV (in line with general inflation), and indexation of the cost of new debt;
- expansion of cost sharing mechanisms to cover more areas of expenditure than at PR19, and generally making rates more favourable for companies, such as 25% sharing rates for schemes included in enhanced engagement and the large scheme gated process;
- the inclusion of new, and separate, aggregate sharing mechanisms for outcomes and costs;
- an outturn adjustment mechanism for outcomes, which would be triggered if there was a significant shift away from anticipated sector-level returns;
- uncertainty mechanisms for cost items including cyber security and the removal of 'forever chemicals' (PFAS) from drinking water, providing for additional allowances if new requirements in those areas arise, and a process for additional base cost allowances, if required, to maintain and improve asset health;
- gated allowances for larger complex investment projects, where we will provide further funding after companies have developed final designs and we are confident in their costings; and
- a significant extension of the direct procurement for customers (DPC) and specified infrastructure projects regulations (SIPR) regimes, to fund 27 major projects under a commercial model, removing the risk of delivery of those large schemes from the regulated companies.

4.31 The record levels of equity raised by the sector, with over £5 billion of equity raised in the 2020-25 period (equivalent to 5% of the RCV), and the significant levels of debt issuance raised over the last two years, provide evidence that investors continue to see the sector as an attractive investment. Since our final determinations, further evidence of investor support has emerged, for example:

- Southern Water announced that it will raise £900 million of committed equity to support its 2025-30 investment programme.⁵⁶ This is greater than the £650 million proposed in its representation on our draft determinations;⁵⁷
- South East Water raised £75 million equity in December 2024. While this was to improve the company's liquidity position, as highlighted by Moody's in a recent ratings assessment, this was additional to the £75 million to £125 million equity that its investors had already proposed as necessary to support investment in 2025-30;⁵⁸

⁵⁶ [OF-RR-004] SW (Finance) I PLC, 'Corporate Update', February 2025.

⁵⁷ [OF-OA-020] Ofwat, PR24 final determinations: Aligning risk and return – Risk and return appendix, p. 85, Table 11.

⁵⁸ [OF-OA-005] South East Water, Statement of Case, March 2025, p. 26, para 2.55.

- South West Water did not consider equity financing to be necessary in either its business plan or its draft determination representation.⁵⁹ However, the group carried out a rights issue in January 2025, successfully raising £490 million of new equity;⁶⁰ and
- Affinity Water confirmed that its investors have entered into a legally binding and unconditional agreement to inject £150 million equity into the company before 31 March 2026.⁶¹

- 4.32 Further evidence that our final determinations represent a reasonable balance of risk and return can be observed in the trading value of listed companies. Our assessment of the Market-to-Asset Ratios is that they have averaged 8% in the period January to March, close to the long-run premium of 10%. SES Water was acquired by Pennon in January 2024 at a reported premium of 6%. Previous private water company transactions in June and July 2022 indicated premia of 44% and around 50% for the Bristol Water and Northumbrian Water transactions. These premia were well in excess of the then current trading premia of the listed water companies of 21–22%.
- 4.33 Since our final determinations, we observe that companies have, overall, been able to issue debt in the sterling markets at a cost in line with the rate implied by the PR24 benchmark index, taking account of the benchmark adjustment in our final determination. This is despite those companies' credit ratings and financial resilience not being in line with what we would expect if they had the notional structure.⁶²
- 4.34 We have also seen evidence of listed companies forecasting to outperform their PR24 determinations. Severn Trent Water announced it was anticipating net operational outperformance of over £300 million in 2025–30, resulting from ODIs and PCDs.⁶³ South West Water announced it is targeting real RoRE returns of 7% in 2025–30, which would represent material outperformance of the base allowed return.⁶⁴ Pennon Group's submission to the CMA argues that our allowed return was appropriate and supported the company to raise the new equity mentioned above, which 'clearly signals investor confidence in the regulatory package'.⁶⁵
- 4.35 Further, the recent history of realised returns in the sector is more nuanced than that presented by the disputing companies. In particular, inflation is a part of the investor return and it would be incorrect for it not to be recognised in assessing overall investor

⁵⁹ [OF-OA-058] Ofwat, PR24 draft determinations: Aligning risk and return – Risk and return appendix, p. 63, Table 13; [OF-OA-020] Ofwat, PR24 final determinations: Aligning risk and return – Risk and return appendix, p. 85, Table 11.

⁶⁰ [OF-OA-059] Pennon Group PLC, Launch of c.£490m Rights Issue, January 2025.

⁶¹ [OF-RR-003] Affinity Water Finance PLC, Final determination acceptance and planned equity injection, February 2025.

⁶² These issuances were made by Wessex Water, Yorkshire Water and Affinity Water between January and March 2025. We set out further detail in our 'risk and return – common issues' document.

⁶³ [OF-OA-060] Severn Trent PLC, Severn Trent Capital Markets Day, March 2025.

⁶⁴ [OF-OA-061] Pennon Group, Investor Summary: PR24 Final Determinations, January 2025, p. 3.

⁶⁵ [OF-OA-043] Pennon Group, PR24 Redetermination – Third Party Submission, April 2025.

returns over time. In consultation with the sector, we developed the total shareholder return metric, which aims to capture the full effect of the returns generated by equity investors over time, taking account of all elements of out- and under-performance on real returns as well as the inflationary component of the return.

- 4.36 Over 2020-24, the median total shareholder return for the sector was 8.5%, taking account of the effects of inflation, financing and operational performance: in total, seven companies reported total shareholder returns in excess of 10% over 2020-24, six companies reported total shareholder returns below 5%. In 2015-20, median reported total shareholder return was 10.6%.
- 4.37 The disputing companies have been selective in their use of information to support their arguments on the allowed return. The submissions request material increases to the allowed return on equity, but make little to no reference to elements of our approach to setting the allowed return that provide an overall benefit to companies. We set out examples in our 'risk and return – common issues' document, but for example, there is only cursory reference to the benefits that companies receive from the treatment of inflation in our assessment of the allowed return. On 30 October 2024, the Office for Budget Responsibility's (OBR) Economic and Fiscal Outlook referenced an updated long-run wedge CPIH-CPI wedge of 0.4 percentage points.⁶⁶ This wedge is materially greater than the zero wedge that was included in our final determinations, and was published at a time beyond which it would have been possible to consult on the implications for our final determinations. It is however a matter that should be considered both for setting the allowed return on debt and the allowed return on equity, particularly in a context where the disputing companies are requesting that new information should be assessed in determining the allowed return on equity. We have not identified that companies have referenced this for consideration in their statements of case.
- 4.38 Equity investors benefit from high inflation where fixed-rate debt is in place. With CPIH at 3.4% (as of March 2025), these benefits could continue into the 2025-30 period.⁶⁷ Further, companies with RPI-linked debt accrue benefits where CPIH outpaces RPI, as is currently the case (with RPI at 3.2%).⁶⁸ As of 31 March 2024, the vast majority of the disputing companies' debt was fixed-rate or indexed to RPI.⁶⁹ In their statements of case, the disputing companies failed to engage with the beneficial effects of inflation to equity investors in the context of an inflation-indexed regulatory regime, to the detriment of their overall assessment of the balance of risk. Reflecting these factors, we would welcome a reassessment of the treatment of inflation in setting the allowed

⁶⁶ [OF-OA-062] Office for Budget Responsibility, Economic and fiscal outlook, October 2024, p. 38, Box 2.3.

⁶⁷ [OF-OA-063] Office for National Statistics, Consumer price inflation, UK: March 2025, April 2025, section 1.

⁶⁸ [OF-OA-063] Office for National Statistics, Consumer price inflation, UK: March 2025, April 2025, section 7.

⁶⁹ [OF-OA-064] Ofwat, Monitoring Financial Resilience report 2023-24 charts and underlying data, November 2024, tab 'Borrowings'.

return, as a necessary addition to the position set down by companies on the allowed return in their statements of case.

- 4.39 Since we set our final determinations, there has been a material increase in turbulence in the financial markets. This has resulted in a more uncertain financial outlook for the world, with most recent forecasts pointing to lower expectations for economic growth. Water companies are largely insulated from these effects, as a result of the provision of an essential service with significant regulatory protections in place, including indexed allowed returns and revenue reconciliation mechanisms. These factors support their relatively low equity betas and their position as a defensive stock in an investment portfolio.
- 4.40 Index-linked gilt yields, a key input to the allowed return on equity, have risen significantly since our final determinations. While the relatively higher stability of index-linked gilts at the time of our draft and final determinations persuaded us to not index it, our PR24 methodology signalled that we likely would have decided differently if we had experienced the levels of volatility seen since the final determination.⁷⁰ We would accordingly welcome the CMA considering whether its redetermined allowed return on equity should be an indexed allowance to increase the confidence that it is accurate and can reflect prevailing interest rate conditions over 2025-30.
- 4.41 We assessed that our determinations were financeable for an efficient company with the notional capital structure. All of the disputing companies have adopted capital structures that depart materially from the notional structure. Four of the disputing companies forecast average gearing of at least 70% in 2025-30, which exceeds the level we consider is consistent with the need for companies to maintain long-term financial resilience. Anglian Water's credit risk is impacted by the level of debt maintained in its holding company structure. Southern Water is rated below investment grade by Moody's and its capital structure has been characterised by borrowing above the regulated company and the use of financial derivatives to manage its cash flows. South East Water has maintained a credit rating that has been lower than the level targeted in our financeability assessment for the last two decades. And in our latest Monitoring Financial Resilience Report, Southern Water and South East Water were classified as 'Action Required', with Northumbrian Water and Wessex Water in our 'Elevated Concern' category.⁷¹
- 4.42 A notional capital structure has been used in regulatory determinations since privatisation, in water and other regulated sectors. Companies are able to deviate from the notional structure, but they, rather than customers, should bear any risks of doing so. Setting our determinations by reference to a notional structure is important for setting expectations about the risk and return balance, and is consistent with our

⁷⁰ [OF-OA-065] Ofwat, Creating tomorrow, together: Our final methodology for PR24: Appendix 11, Allowed return on capital, December 2022, p. 18.

⁷¹ [OF-OA-066] Ofwat, Monitoring Financial Resilience report 2023-24, November 2024, p. 7.

statutory duties. The evidence arising from the challenges posed by companies with the weakest levels of financial resilience, and the more recent actions taken by the credit rating agencies, further supports our view that gearing levels that exceed 70% may not be sustainable in the long term.

- 4.43 The disputing companies refer to recent changes to the assessment of the water sector by credit rating agencies. Our final determinations took account of the changes to guidance published by the credit rating agencies in November 2024, to the extent they were relevant to the notional company, and while being aware of the potential impact on customers. We note that sector-wide actions since our final determinations reflect the credit agencies' assessment of the impact of negative public sentiment on regulatory and political expectations, rather than our final determinations. Fitch Ratings set out that it considered our final determinations 'provided a reasonable outcome for most UK water companies'.⁷² Updates to individual credit ratings for the disputing companies since our final determinations are also driven by company-specific issues that are outside of the price control determinations, as set out in our 'risk and return – common issues' document.
- 4.44 It is critical that price determinations are not opportunities for customers to pay to address companies' actual financial resilience issues. For example, South East Water argues it is unable to attract new equity to achieve a 'more modest' level of gearing, and that its 'actual financial position' is not independent of the regulatory process.⁷³ As set out in our 'risk and return – common issues' document, South East Water paid a large dividend in the 2020–24 period to enable its shareholders to repay an outstanding loan owed to the regulated company. Our view is that the challenges brought about to South East Water's ability to raise equity are the result of its past financing choices and its ongoing performance challenges. Nonetheless, we welcome the £75 million of equity into the company in December 2024, and the additional equity injection proposed that is in the range of £75–125 million.
- 4.45 Similarly, Southern Water argues that our assessment of financeability should consider a notional company that does not achieve the base return.⁷⁴ This would effectively see the efficient notional company adopt some actual company characteristics, namely that Southern Water has delivered relatively poor operational performance for an extended period of time. The company has maintained weak levels of financial resilience, which has led it to maintain a credit rating that is in the sub-investment grade and other credit ratings that are weakly positioned in the investment grade category. The company has been the subject of a distressed sale and is in the process of delivering a turnaround in its operational performance. We do not consider it appropriate that the characteristics of an actual company's poor performance, whose consequences should

⁷² [OF-RR-045] Fitch Ratings, Fitch on UK Water, Rating approach for AMP8, March 2025, p. 3.

⁷³ [OF-OA-005] South East Water, Statement of Case, March 2025, p. 91, paras 7.37–7.41.

⁷⁴ [OF-OA-003] Southern Water, Statement of Case, March 2025, p. 91, para 206.

rightly sit with equity investors, should form the basis on which a determination should be set.

4.46 As noted above, it is a long-standing principle that the actual company structure is a matter for companies and their investors to manage, within the context of the determination, the licence and general company law. It remains an important principle that companies and their investors bear the consequences of past financing decisions, even where these endure over multiple determination periods, as amending the allocation of risk and return would risk passing equity risk onto customers.

4.47 Finally, it is important that revisions to the final determination are made only where it is fair and reasonable to do so based on the underlying evidence. [REDACTED]

[REDACTED] Northumbrian Water's RCV (£5.44 billion as at 31 March 2024) is larger than the combined RCV of the water companies in the Pennon Group (£5.15 billion as at 31 March 2024). However, Pennon successfully raised a greater amount of equity (£490 million) in January 2025 than proposed by Northumbrian Water in its draft determination representation (£400 million). South West Water's operational performance (as measured by RoRE) was lower than Northumbrian Water's in the 2020-24 period. Overall, this evidence does not suggest that the equity return is insufficient to support the provision of new equity; rather, that Northumbrian Water is seeking to enhance its ability to generate returns through the redetermination process.

5. Looking ahead

- 5.1 The statements of case cover a wide range of issues, and the disputing companies have provided a significant volume of information. This includes new expenditure items, changes to previous requests, and new evidence. As requested by the CMA, we have extended the deadline for the CMA to report to up to 12 months from the date of the reference. However, we recognise the CMA will endeavour to carry out the work in less than 12 months if possible.⁷⁶

Areas for deprioritisation

- 5.2 In order to achieve the challenging timeline, we support the CMA's approach to consider which issues 'would have the largest effect on customer prices and other outcomes' in assessing whether issues may be deprioritised from its redeterminations.⁷⁷ Along with the disputing companies, we were asked to highlight areas that could be deprioritised from the redeterminations. We have identified a number of areas that could be deprioritised, allowing the CMA to focus on issues that will have the biggest impact. In identifying these areas, we have considered where we already have mechanisms or ongoing processes to address the issue, or where our approach has broad support from the sector. These include:

- quality and ambition assessment;
- retail price control;
- base cost models;
- adjustments from past performance;
- business rates;
- notional capital structure;
- asset health;
- expenditure allowances associated with PFAS, cyber security, the large schemes gated process, major project development costs and Havant Thicket that would be eligible for our cost change process;
- PCLs and ODIs for total pollution incidents; and
- adjustments agreed with companies to correct unambiguous errors in our final determinations.

- 5.3 We would support the CMA deprioritising redetermination of the **quality and ambition assessment (QAA)**. Northumbrian Water and Southern Water confirmed that the QAA is not in scope of their appeals.⁷⁸ Anglian Water and Wessex Water both raised concerns

⁷⁶ [OF-OA-067] CMA, Water PR24 price redeterminations, April 2025.

⁷⁷ [OF-OA-034] CMA, Water References: Competition and Markets Authority Guide, December 2024, p. 13.

⁷⁸ [OF-OA-002] Northumbrian Water, Statement of Case, March 2025, p. 41, para 134; [OF-OA-003] Southern Water, Statement of Case, Annex 3: Areas of the Final Determination that are not in Dispute, March 2025, p. 544, para 1.

with how the QAA was implemented, but neither raised any actions relating to the QAA in their statements of case. We do not think there are any benefits of redoing the QAA as part of the redeterminations process. It was designed to incentivise high quality and ambitious price review submissions, so redoing the assessment after the submissions have been made would be of limited value.

- 5.4 We would support the CMA deprioritising redetermination of the **retail price control**. The disputing companies have not raised substantial concerns in this area. Southern Water, Wessex Water and South East Water confirm that the retail price control is not in the scope of their appeals and could be deprioritised (although Southern Water has asked the CMA to update its bad debt allowance to reflect any changes in wholesale bills).⁷⁹ Northumbrian Water did not raise any actions for the CMA in relation to the retail price control. However, Anglian Water has asked the CMA to update the retail models to reflect the most recent forecast data.⁸⁰ This would require data from all companies, and any change in allowances would impact on all the disputing companies – including those companies that are not challenging the final determinations in this area. Our final determination retail allowance for Anglian Water was only 2% (£13 million) less than it requested. We therefore do not think that updating the retail models should be a high priority.
- 5.5 We would support the CMA deprioritising redetermination of the **base cost models**. Our base cost models have been developed over many years in consultation with water companies and other stakeholders, as set out in our 'expenditure allowances – common issues' document. Our approach to assessing base expenditure builds on the approach used at PR19, which was mostly followed by the CMA in its PR19 redeterminations (for example, the CMA made a minor change to wastewater base cost models). Companies broadly supported our proposed approach to setting base expenditure allowances at PR24, with relatively minor comments received. Further, Northumbrian Water set out that the base models are not in scope of its appeals.⁸¹ While some of the other disputing companies highlight where they consider that alternative cost drivers should be used in the benchmarks, other companies have not raised concerns with these cost drivers. Changes in cost drivers will impact the allowances for all disputing companies, and potentially all companies if reflected in benchmarks for PR29. Given the broad support from the sector for our base models and the potentially significant impact of changing them on the disputing and other companies, we think there is an opportunity to deprioritise this area.
- 5.6 We would support the CMA deprioritising redetermination of **adjustments from past performance**. Four of the disputing companies did not include any PR19

⁷⁹ [OF-OA-003] Southern Water, Statement of Case, Annex 3: Areas of the Final Determination that are not in Dispute, March 2025, p. 544, para 1; [OF-OA-004] Wessex Water, Statement of Case, March 2025, p. 9, Table 1; [OF-OA-005] South East Water, Statement of Case, March 2025, p. 11, para 1.33.

⁸⁰ [OF-OA-001] Anglian Water, Statement of Case, March 2025, p. 14, para 43.

⁸¹ [OF-CA-055] Northumbrian Water, 'Statement of Case, Appendix 1: Supporting information', March 2025, p. 2, Figure 2.

reconciliations in the scope of their appeals. South East Water is disputing our application of underperformance payments for its PR19 'voids – business properties' PC.⁸² Many of South East Water's points relate to policy decisions at PR19, which the company accepted as part of the PR19 package. We do not think it is in customers' interests to reopen specific elements of previous price reviews without reconsidering the overall balance of risk. Given the significant volume of material that will need to be considered as part of these redeterminations, we think the CMA should focus on decisions that were made in relation to PR24, rather than decisions that companies could have challenged as part of a redetermination reference five years ago. A high bar should be applied before retrospectively re-opening past price review decisions, given the importance of certainty and stability in relation to final determination decisions. While South East Water argues that we should have accounted for the impact of Covid-19 on its performance on non-household voids, we concluded in our final determinations that this would not be in customers' interests, as the company was unable to quantify the impact of Covid-19 in the evidence it provided.⁸³ The company has not provided any further evidence in its statement of case. Further, the issue concerns only a £3.9 million payment in the context of a £1.7 billion five-year revenue allowance for South East Water. We therefore think there is an opportunity to deprioritise this area.

- 5.7 We would support the CMA deprioritising redetermination of expenditure allowances associated with **business rates**. Anglian Water, Northumbrian Water and Wessex Water have asked the CMA to update allowances based on the latest valuations from the Valuation Office Agency.⁸⁴ All companies should have received draft rateable values in February 2025, but negotiations are ongoing and rateable values will not be confirmed until the summer. In our final determinations, we included reasonable forecasts of business rates, and to reflect the level of uncertainty we also applied 10:10 cost sharing rates. This means that, if business rates turn out to be higher than our allowances, companies will be able to recover 90% of the additional costs at PR29. Given that the rates forecasts are still uncertain, and that companies will be able to recover the majority of any additional costs at PR29, we think there is an opportunity for the CMA to deprioritise these costs.
- 5.8 We would support the CMA deprioritising redetermination of the **notional capital structure**. We set notional gearing at 55% in our final methodology in 2022, having previously signalled that a lower level of notional gearing may be appropriate in our draft methodology and in our discussion document in 2021.⁸⁵ This provided companies

⁸² [OF-OA-005] South East Water, Statement of Case, March 2025, p. 67, para 5.10.

⁸³ [OF-OA-068] South East Water, Statement of Case, Annex I – PR19 reconciliation NHH voids, March 2025, p. 1, para 3.

⁸⁴ [OF-OA-001] Anglian Water, Statement of Case, March 2025, p. 14, para 43; [OF-OA-002] Northumbrian Water, Statement of Case, March 2025, p. 157, Figure 53; [OF-OA-004] Wessex Water, Statement of Case, March 2025, p. 206, para 1.8.

⁸⁵ [OF-OA-036] Ofwat, Creating tomorrow, together: consulting on our methodology for PR24, July 2022, p. 96; [OF-OA-069] Ofwat, PR24 and beyond: Discussion paper on risk and return, December 2021, p. 2.

with the opportunity to better align their capital structures with the notional gearing level of 55%, should they have wished to, supported by the impact of high inflation on regulatory gearing for those companies with fixed-rate debt, such as assumed for the notional company. Further, while Southern Water and Wessex Water have asked the CMA to reconsider the reduction to notional gearing from the level at PR19,⁸⁶ four companies, including one of the disputing companies, either accepted or did not challenge the proposed level of notional gearing in their representations to our draft determinations. Our approach to setting the level of notional gearing is consistent with the UKRN, which sets out that 'the notional gearing assumption should reflect the regulator's assessment of the balance of risks facing the regulated company, a wide range of benchmarks on gearing levels and overall regulatory policy objectives, not just that of the actual company (or companies) in question'.⁸⁷

5.9 We would support the CMA deprioritising redetermination of **asset health allowances**. All the disputing companies raised funding for asset health as an issue in their statements of case. In our final determinations, we said that we would gain greater insight into the condition of a wider range of assets before PR29. We stated we would assess if there are any sector-wide asset condition issues that need to, and can be, addressed ahead of PR29 and whether additional funding above what we allowed at PR24 is required. This work has already begun.⁸⁸ We are collecting asset condition data from companies, and plan to make decisions on the necessary additional allowances by December 2026. We will also ensure that companies can access any additional revenue ahead of PR29 if required. The approach needs to be applied across the sector and will be developed iteratively in consultation with the industry to ensure a common understanding. We expect all companies to be able to challenge our decisions on asset health by referring either future determinations or required licence modifications to the CMA.⁸⁹ As we are engaging with the sector and plan to have a process that will allow all companies to evidence the need for additional asset health expenditure, and a mechanism that will allow them to access additional funding in-period if required, we think there is an opportunity for the CMA to deprioritise this area.

5.10 We would support the CMA deprioritising redetermination of expenditure allowances associated with **PFAS, cyber security, the large schemes gated process, major project development costs and Havant Thicket** that would be eligible for our cost change process. South East Water has asked the CMA to include £9 million of additional costs relating to PFAS,⁹⁰ and Southern Water has asked for the CMA to reduce the materiality threshold for all notified items to 2% of turnover, which would require a

⁸⁶ [OF-OA-003] Southern Water, Statement of Case, March 2025, p. 91, para 205; OF-OA-004 – Wessex Water, Statement of Case, March 2025, p. 90, para 10.12.

⁸⁷ [OF-RR-015] UKRN, UKRN guidance for regulators on the methodology for setting the cost of capital, March 2023, p. 5.

⁸⁸ We set out further detail on this work in [OF-CA-011] Ofwat, Enhancing Asset Health Understanding Workstream, March 2025.

⁸⁹ Companies operating mainly in Wales need to agree to licence modifications. English companies can refer a modification to the CMA.

⁹⁰ [OF-OA-005] South East Water, Statement of Case, March 2025, p. 46, para 4.46.

licence modification.⁹¹ In our final determinations, we set out our intention to introduce a new in-period adjustment mechanism for critical cost areas where costs were still uncertain at the time of our determinations.⁹² These changes will require licence modifications, which require full consultation. We signalled our intent in our final determinations, and have since engaged with water companies and other key stakeholders to develop an approach. We expect to formally consult on the changes in July, and plan to have it in place for the mechanism to operate in 2026, 2027 and, where appropriate, 2028, with possible changes in price controls from April 2027. This will allow companies to access revenue associated with these areas in-period if needed, or receive a commitment that it will be funded at the next price review. As already signalled in our final determinations, we expect the materiality threshold for possible in-period price control changes to be 2% of turnover for each item (calculated in the same way as for a standard interim determination). Given that we are developing this process for all companies, including the disputing companies, we think there is an opportunity for the CMA to deprioritise these costs from the redeterminations, as companies will have another route to access funding ahead of the next price review, if needed. Companies would be able to appeal our decisions on licence modifications and under our proposals we expect them to be able to refer our decisions on any interim determinations to the CMA.

- 5.11 We would support the CMA deprioritising redetermination of **PCLs and ODIs for total pollution incidents**. Reporting changes being proposed by the Environment Agency and Natural Resources Wales are expected to affect all companies, including disputing companies, from 2026. We plan to consult, in line with our change control process, to determine whether there is sufficient reason to reset relevant aspects of the PC. Given the uncertainty involved and the redetermination timescales, we propose that our consultation process runs its course, and consider there is an opportunity for this to be deprioritised. We set out further details in our 'outcomes – common issues' document.
- 5.12 Finally, we would support the CMA deprioritising adjustments agreed with companies to correct **unambiguous errors in our final determinations**. For example, Wessex Water requests that the CMA adjusts for an error relating to its allowance for growth at sewage treatment works.⁹³ As set out in the respective final determination notification documents, we will adjust for unambiguous errors in allowed revenue within our blind year reconciliation process, through the revenue forecasting incentive (RFI) formula.⁹⁴ We aim to complete this by December 2025. Where unambiguous errors have been confirmed, we have recorded them in our PR24 final determinations change log.⁹⁵

⁹¹ [OF-OA-003] Southern Water, Statement of Case, March 2025, p. 297, para 3.

⁹² [OF-OA-015] Ofwat, PR24 final determinations: In-period adjustments, December 2024.

⁹³ [OF-OA-004] Wessex Water, Statement of Case, March 2025, p. 8, Table 1.

⁹⁴ For example, [OF-OA-081] Ofwat, Notification of the PR24 final determination of price controls for Wessex Water Services Limited, December 2024.

⁹⁵ [OF-OA-075] Ofwat, PR24 final determinations change log, April 2025.

Where the disputing companies raise unambiguous errors that we have not agreed, we respond in the respective company-specific documents.

Other areas for consideration

- 5.13 We think it is important that the redeterminations do not focus only on issues raised by the disputing companies. We welcome that the CMA has recognised this by inviting views from third parties on what issues, beyond those raised by disputing companies, it should consider as part of its redeterminations.⁹⁶ Third-party submissions to the CMA from Pennon Group and CCW highlight there are a range of views on areas both raised and not raised by the disputing companies.⁹⁷
- 5.14 Some disputing companies' arguments selectively focus on specific areas of disagreement. However, it is difficult to consider specific issues within our determinations in isolation. This is for two key reasons:
- our determinations are based on interlinked 'building blocks': for example, the level of expenditure allowances is inextricably linked to the service levels a company can be expected to achieve, and the overall balance of risk and return must account for all the elements that make up that balance; and
 - given the comparative nature of how we set expenditure allowances and PCLs across the sector, adjustments to one company's determination can often also impact other companies'. For example, modelled expenditure allowances are set with reference to sector-wide efficiency benchmarks: changes to this benchmark can therefore impact all companies' determinations (or, in the case of the PR24 redeterminations, all disputing companies' determinations).
- 5.15 While the disputing companies have narrowly framed some issues as company-specific, such issues may, for the above reasons, require consideration on a more cross-cutting basis. We welcome the CMA's approach to be mindful of whether specific issues impact on other parts of the redeterminations.⁹⁸ For elements of the determinations where this is not the case, we support prioritising issues to help achieve the CMA's overriding objective, as we set out above.

⁹⁶ [OF-OA-067] CMA, Water PR24 price redeterminations, April 2025.

⁹⁷ [OF-OA-043] Pennon Group, PR24 Redetermination – Third Party Submission, April 2025; [OF-OA-070] CCW, CCW's submission to the Competition and Markets Authority on Anglian Water's statement of case, April 2025; [OF-OA-071] CCW, CCW's submission to the Competition and Markets Authority on Northumbrian Water's statement of case, April 2025; [OF-OA-072] CCW, CCW's submission to the Competition and Markets Authority on Southern Water's statement of case, April 2025; [OF-OA-073] CCW, CCW's submission to the Competition and Markets Authority on Wessex Water's statement of case, April 2025; [OF-OU-045] CCW, CCW's submission to the Competition and Markets Authority on South East Water's statement of case, April 2025; [OF-OA-074] MCC Economics & Finance, A review of Ofwat's PR24 Final Determination WACC allowance: a report for CCW, April 2025.

⁹⁸ [OF-OA-034] CMA, Water References: Competition and Markets Authority Guide, December 2024, p. 13.

5.16 Given the information asymmetry between companies and regulators, as well as taking account of the views from third parties, it is also important for the CMA to consider material areas where our decisions may be seen as 'favourable' to the companies. We have already set out some examples in this document, and summarise key areas below:

- **Risk protections.** Our PR24 determinations significantly increased the levels of risk protection compared with PR19 (see paragraph 4.30);
- **'Aiming up'.** To set the allowed return on capital, we used a point estimate at the top of our range to support investment and investor confidence. However, there were reasonable arguments for choosing a rate at the midpoint, including the significant evidence that investors continue to see the sector as an attractive investment. For example, our consultants, CEPA, preferred a figure of 4.75% as their point estimate for return on equity, compared to our 5.10% (see paragraph 4.14);
- **Performance commitments.** 12 of 16 companies stand to earn net outperformance payments over 2025–30 for achieving the PCLs they forecast in their representations on our draft determinations (see paragraph 4.28);
- **Expenditure allowances.** We moderated the scale of our enhancement cost challenge by reducing the scale of our deep and shallow dive efficiency challenges, using median benchmarks, and assigning equal weights for historical and forecast data for enhancement expenditure. We could also have capped expenditure allowances where our models provided a higher allowance than what the company requested (see paragraph 4.15);
- **Inflationary benefits.** Equity investors benefit where inflation outturns above the 2.0% Bank of England inflation target and companies have fixed-rate debt in place. With CPIH at 3.4% (as of March 2025), these could bring benefits into the 2025–30 period (see paragraph 4.38). Further, the updated long-run CPIH-CPI wedge referenced by the OBR's Economic and Fiscal Outlook is materially greater than the zero wedge included in our final determinations. To the extent there are methodological changes to setting the allowed return compared with our determination, we consider this is a matter that should be taken into account (see paragraph 4.37); and
- **Allowed return on equity indexation.** We chose not to pursue an indexation approach, but likely would have decided differently if we had experienced the levels of volatility seen since the final determinations (see paragraph 4.40). Indexation could now provide the fairest outcome to customers and investors, reflecting the incentive that market changes to the risk-free rate has brought on company decisions to request a redetermination (see our 'risk and return – common issues' document).

5.17 Information asymmetry applies even more acutely where the disputing companies cite changes in parameters or circumstances since our final determinations that they argue have increased costs or risk. We and the CMA inevitably have limited awareness of any recent changes that have worked in the companies' favour. For example, we have not identified that the statements of case set out the issue referenced above on inflationary

benefits. We consider the information set out in the papers from our economic advisers (CEPA)⁹⁹ and academic advisers (Mason, Robertson and Wright)¹⁰⁰ that accompany our submission should be given due consideration and weight in any redetermination of the allowed return.

- 5.18 One option to manage new information and potential changes to company proposals would be for the CMA to set a cut-off date for using new evidence to inform the redeterminations. Alongside deprioritisation of issues such as those we suggest above, this could help achieve the CMA's overriding objective. Since we set our final determinations, there has been a material increase in turbulence in financial markets. Particularly given this context, it is far from certain that more recent data will necessarily result in a better determination for the 2025–30 period. There would be a number of potential options for a cut-off date, including limiting the information used to set the redeterminations to that which was available to us when we set our PR24 final determinations in December 2024.
- 5.19 We underline our continued commitment to giving the CMA all the assistance we can throughout the redetermination process, to help it achieve its overriding objective and deliver the best outcomes for customers and the environment.

⁹⁹ [OF-OA-083] CEPA, Supplementary evidence on the cost of equity: response to statements of case, April 2025.

¹⁰⁰ [OF-OA-084] Mason, Robertson and Wright, A report on allowed return issues in disputing companies' statements of case, April 2025.

A1 Fulfilling our duties

Introduction

A1.1 We have explained throughout the PR24 process¹⁰¹ how our decisions reflect both our statutory duties and the UK and Welsh Government statements setting out strategic priorities and objectives for Ofwat – known as strategic policy statements (SPSs).¹⁰² Nevertheless, for ease of reference, we start by setting out what these duties comprise and how we fulfilled those duties when reaching our final determinations.

A1.2 We then turn, in the sections of this Annex that follow, to some of the main respects in which our and the companies' views differ as to whether the duties have been met, namely:

- time frame (short term v long term and the impact on future customers;
- cost allowances versus outcomes;
- the financing duty and financeability; and
- the growth duty.

A1.3 The companies allege that we have not met our duties (and/or have failed to give appropriate weight to, or to have regard to, particular duties) on a wide range of issues. These include, for example, whether the level at which the allowed return should be set is sufficient to secure reasonable returns on capital,¹⁰³ whether cost allowances suffice to enable companies to fulfil the proper carrying out of their functions, promote growth and meet the resilience objective¹⁰⁴ and whether aspects of our outcomes package meet the consumer objective.¹⁰⁵

A1.4 It is neither helpful nor accurate to characterise each such disagreement as a failure to meet our statutory duties. Rather, these are simply disagreements as to the merits of decisions that we made in our final determinations. Throughout PR24, we have been motivated by all of our statutory duties, protecting customer interests and finding the right outcome in light of our duties in the round. This includes looking to the long term, securing that companies are able to earn a reasonable return to finance the proper carrying out of functions and secure resilience and the taking of steps to meet needs for water and sewerage services. It is wholly consistent with our duties that our final

¹⁰¹ [OF-OU-002] Creating tomorrow, together: Our final methodology for PR24, December 2022 and [OF-OA-014] PR24 final determinations: Our approach, December 2024.

¹⁰² [OF-OU-002] Creating tomorrow, together: Our final methodology for PR24, December 2022. Ofwat set out four key ambitions for the review in the final methodology: increase focus on the long term; deliver greater environmental and social value; reflect a clearer understanding of customers and communities, and drive improvements through efficiency and innovation.

¹⁰³ [OF-OA-005] South East Water, Statement of Case, March 2025, p. 9, para 1.23 and [OF-OA-001] Anglian Water, 'Statement of Case', March 2025, p.193. para 734.

¹⁰⁴ [OF-OA-004] Wessex Water, Statement of Case, March 2025, p. 30, para 5.13.

¹⁰⁵ [OF-OA-003] Southern Water, 'Statement of Case', March 2025, p. 385, para 95.

determinations secure that customers do not pay more than a company's efficient costs or what it should cost an efficient company to raise finance. We do not consider it appropriate in light of our duties to adopt a general principle that customers of poorly performing companies should suffer a lower level of service, or systematically pay more for the same level of service that will be provided by the rest of the sector.

A1.5 Our final determinations were made in light of all relevant circumstances including our experience of the sector and the evidence submitted to us and carefully and conscientiously considering all of our duties. They were the result of an exercise of regulatory judgement.

A1.6 We focus in this annex on the duties relevant to England, or English water companies, because none of the disputing companies serve areas in Wales.

The duties

A1.7 In performing our functions as a public body, Ofwat is subject to a range of statutory duties and strategic policy considerations, as summarised below.

A1.8 Sections 2 and 3 of the Water Industry Act 1991 (as amended) (the Act) place a number of statutory duties on Ofwat.

A1.9 Our statutory duties under section 2(2A) of the Act require us, in summary, to set price controls in the manner we consider is best calculated to:

- further the consumer objective, to protect the interests of consumers, wherever appropriate by promoting effective competition;
- secure that water companies (water and sewerage undertakers) properly carry out their functions (previously referred to by the CMA as the functions duty);
- secure that water companies are able (in particular, by securing reasonable returns on their capital) to finance the proper carrying out of those statutory functions (previously referred to by the CMA as the financing duty);
- secure that business retailers (water supply licensees and sewerage licensees) properly carry out their licensed activities and statutory functions (previously referred to by the CMA as the licence duty); and
- further the resilience objective, to secure the long-term resilience of water companies' water supply and wastewater systems and to secure that they take steps to enable them, in the long term, to meet the need for water supplies and wastewater services.

A1.10 Subject to those 'primary' duties, we are, under section 2(3) of the Act, required to set price controls in the manner we consider is best calculated to:

- promote efficiency and economy by companies;

- secure that no undue preference or discrimination is shown by companies in fixing charges, or in relation to the provision of services;
- secure that consumers' interests are protected where companies sell land;
- ensure that consumers' interests are protected in relation to any unregulated activities by companies; and
- contribute to the achievement of sustainable development.

A1.11 Such duties have been previously referred to by the CMA as the secondary duties.

A1.12 We are also required, under section 2(4) of the Act, to have regard to the principles of best regulatory practice (including the principles under which regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed).

A1.13 We also have general environmental and recreational duties in section 3 of the Act when formulating or considering any proposals relating to any functions of a water company. These include duties under section 3(2) of the Act to:

- exercise any power conferred with respect to the proposals to further the conservation and enhancement of natural beauty and the conservation of flora, fauna and geological or physiographical features of special interest;
- have regard to the desirability of protecting and conserving buildings, sites and objects of archaeological, architectural or historic interest; and
- take into account any effect on the beauty or amenity of any rural or urban area or on any such flora, fauna, features, buildings, sites or objects.

A1.14 Subject to the duties imposed by section 3(2) of the Act, pursuant to section 3(3) of the Act, we have duties in relation to such proposals to:

- have regard to the desirability of preserving for the public any freedom of access to areas of woodland, mountains, moor, heath, down, cliff or foreshore and other places of natural beauty;
- have regard to the desirability of maintaining the availability to the public of any facility for visiting or inspecting any building, site or object of archaeological, architectural or historic interest; and
- take into account any effect which the proposals would have on any such freedom of access or on the availability of any such facility.

A1.15 Further, we are subject to other general environmental duties, including:

- to take such action as we consider appropriate to further the objective of the conservation and enhancement of biodiversity in England through the exercise of

functions in relation to England (section 40 of the Natural Environment and Rural Communities Act 2006);¹⁰⁶

- in exercising any of our functions, to have regard to the requirements of the Habitats Directive (92/43/EEC) and the Wild Birds Directive (2009/147/EEC) (regulation 9(3) of the Conservation of Habitats and Species Regulations 2017)¹⁰⁷ so far as they may be affected by the exercise of those functions;
- in exercising functions so far as affecting a river basin district, to have regard to the river basin management plan for that district and any supplementary plan (regulation 33 of the Water Environment (Water Framework Directive) (England and Wales) Regulations 2017);¹⁰⁸ and
- in exercising or performing any functions in relation to, or so as to affect, land in a protected landscape, to seek to further the purpose of conserving and enhancing the natural beauty of the protected landscape and, in relation to some protected landscapes, other purposes including conserving and enhancing the wildlife and cultural heritage of the protected landscape.¹⁰⁹

A1.16 In discharging our environmental duties, we work closely with other regulators who oversee related aspects of environmental and water resource management, such as the Environment Agency and the Drinking Water Inspectorate. Our close collaboration with these regulators supports more effective and co-ordinated oversight. We have worked, and continue to work, with these regulators so that we have a good understanding and overview of the inter-related regulatory requirements.

A1.17 From 21 May 2024, we have also been under a duty to have regard to the desirability of promoting economic growth pursuant to the Deregulation Act 2015.¹¹⁰ In performing this duty, we must consider the importance for the promotion of economic growth of exercising any regulatory function in a way that ensures that regulatory action is taken only when needed and any action taken is proportionate.¹¹¹ We must also have regard to the statutory guidance issued by the UK Government which includes a non-exhaustive list of behaviours of smarter regulation that regulators should ensure they exhibit.¹¹²

¹⁰⁶ [OF-OAA-013] Natural Environment and Rural Communities Act 2006.

¹⁰⁷ [OF-OAA-014] Conservation of Habitats and Species Regulations 2017.

¹⁰⁸ [OF-OAA-015] Water Environment (Water Framework Directive) (England and Wales) Regulations 2017.

¹⁰⁹ The duties summarised here are set out in [OF-OAA-007] the Countryside and Rights of Way Act 2000, section 85 (in relation to land in areas of outstanding natural beauty), of [OF-OAA-008] the National Parks and Access to the Countryside Act 1949, section 11A (in relation to land in a National Park) and [OF-OAA-009] Norfolk and Suffolk Broads Act 1988, section 17A (in relation to land in the Broads).

¹¹⁰ See [OF-OAA-010] The Economic Growth (Regulatory Functions) (Amendment) Order 2024. We note that consistent with the exclusion of Ofwat's competition functions from the growth duty, the CMA has not been named as an organisation subject to the growth duty. Further, the scope of the Order is limited to Ofwat's regulatory functions in England, excluding regulatory functions so far as exercisable in Wales, if or to the extent that the function relates to matters which are devolved Welsh matters.

¹¹¹ [OF-OAA-011] Deregulation Act 2015, section 108.

¹¹² [OF-OAA-001] Department for Business & Trade, Statutory guidance: Growth duty, 21 May 2024.

A1.18 We must also have regard to the public sector equality duty imposed by the Equality Act 2010.

A1.19 Pursuant to s12(3) of the Act, the CMA is to apply the principles which apply, by virtue of Part 1 of the Act, to determinations we have made. Notably, various duties to which we had regard in making our final determinations, including the growth duty, apply to us by virtue of requirements that sit outside Part 1 of the Act and the CMA will need to consider if they apply independently to the CMA when carrying out its redeterminations, noting that the CMA has not had the specific growth duty extended to it.

The strategic priorities

A1.20 We are also required under section 2A of the Act to set price controls for the disputing companies in accordance with the statement of strategic priorities and objectives of the UK Government. The UK Government's statement (SPS), published in February 2022, set the following priorities:¹¹³

- protecting and enhancing the environment;
- delivering a resilient water sector;
- serving and protecting customers; and
- using markets to deliver for customers.

A1.21 The CMA's Water References Guide states, '...the relevant SPS complements the Authority's existing statutory duties. The Authority's statutory duty is to carry out its functions in accordance with the relevant SPS and to that extent it may prioritise certain work areas over others. The expectation is that the regulated water industry will reflect the priorities and objectives in its strategic direction'.¹¹⁴ We have clearly explained how the final determinations support the achievement of the SPS priorities.¹¹⁵

Future changes

A1.22 Some Disputing Companies refer in their Statements of Case to future changes to our duties. Anglian Water, South East Water and Southern Water for example,¹¹⁶ refer to the duty in section 10 of the Water (Special Measures) Act 2025¹¹⁷ when exercising or performing relevant functions, to have regard to the need to contribute towards

¹¹³ [OF-OAA-005] Defra, The government's strategic priorities for Ofwat, February 2022.

¹¹⁴ [OF-OAA-002] CMA, Water References Competition and Markets Authority Guide – CMA205, December 2024, p. 11, para. 3.4.

¹¹⁵ [OF-OA-012] UK Government priorities and our 2024 price review final determinations, December 2024.

¹¹⁶ [OF-OA-001] Anglian Water – Statement of Case, March 2025, p. 49, para 191. [OF-OA-005] South East Water, Statement of Case, March 2025, p. 56, para 4.75(c) and [OF-OA-003] – Southern Water Statement of Case, March 2025, p. 51, Annex 2, paras 17–19.

¹¹⁷ [OF-OAA-021] Water (Special Measures Act) 2025, section 10.

achieving compliance by the UK government with the environmental target duties in section 1 of the Climate Change Act 2008 (UK net zero emissions target); and in relation to the areas of English companies, section 5 of the Environment Act 2021 (other environmental targets). The duty set out in section 10 of the Water (Special Measures) Act 2015 did not apply to us at the time of our PR24 final determinations. We do not yet know when this duty will come into force (and therefore whether it will be applicable to any redeterminations) as the date will be specified in commencement regulations that have not yet been made (as noted in a footnote in Anglian Water's Statement of Case¹¹⁸). Despite the new duty not being in force, in line with the UK government's SPS, we challenged English companies during PR24 to deliver against applicable targets set under the Environment Act 2021 and, consistent with the SPSs from both the UK and Welsh governments, have supported the sector to progress towards achieving net zero.

A1.23 The UK and Welsh governments have also set up an independent review into the water sector (known as the Independent Water Commission,¹¹⁹ led by Sir Jon Cunliffe). Certain disputing companies refer to this review in their Statements of Case, sometimes to suggest that it supports their view that our approach to its final determinations was flawed. However, the Commission's review is forward-looking and will make recommendations to the Government to reform the water sector in England and Wales rather than address the final determinations. The terms of reference state that: 'To ensure a stable investment climate, the commission will not make recommendations that impact the live Price Review 24 process'.¹²⁰ It will report in summer 2025. The UK and Welsh governments will then respond and consult on the recommendations that they intend to take forward.

Our approach to our duties and strategic priorities

A1.24 There are five important points to which we submit the CMA should have particular regard when considering how to apply the duties set out above.

A1.25 First, as the CMA observed in the redeterminations following PR14 and PR19, there is no hierarchy among the principal duties: 'the primary duties are equally important and are intended to complement one another. They should not be applied in isolation. The secondary duties are subordinate to, or subject to, the primary duties but are still legal requirements that must be taken account of'.¹²¹ The CMA reflects this in its Water References Guide, which observes that the 'the legislation does not set out any

¹¹⁸ [OF-OA-001] Anglian Water, 'Statement of Case', March 2025, p. 49, para 192, footnote 64.

¹¹⁹ [OF-OAA-006] Defra, The Call for Evidence: Independent Commission on the Water Sector Regulatory System, February 2025.

¹²⁰ [OF-OAA-004] Independent commission on the water sector regulatory system terms of reference, October 2024.

¹²¹ [OF-CA-136] Competition and Markets Authority, Final Report Competition and Markets Authority, March 2021, p. 62, para 2.84.

hierarchy of the primary duties, nor that they should affect any other obligation of the Authority to comply with any other duty, such as the Growth Duty'.¹²²

A1.26 It follows that the role of Ofwat – and, in turn, of the CMA – is not to ascertain whether a set of bright-line tests has been met. Rather, this is an exercise of regulatory judgement, in which the regulator considers all of its duties and the objectives set out in the Act and other legislation, acts in accordance with the SPS, and takes a view on the evidence in light of those considerations and its own experience and expertise. The requirement for the exercise of judgement is clear in the wording of the Act: section 2 requires Ofwat to perform the primary and secondary duties set out in that section 'in the manner which...it considers is best calculated' to meet the various objectives.

A1.27 The section 2 duties are not a checklist of tests that Ofwat (or now the CMA) must meet. Such an approach would be overly simplistic and fails to comprehend that the Ofwat and in turn, the CMA, must consider all relevant factors in the round, in view of all its duties.

A1.28 Second, and relatedly, as well as requiring an exercise of judgement, the duties are not mutually exclusive. The objectives in the Act and in the SPS inter-connect to support the regulation of the water sector. Contrary to what the disputing companies suggest, it is not a case of having to choose between promoting one objective over another. For example, while Anglian Water suggests that we have promoted the consumer objective, in the form of lower bills over the financing duty,¹²³ we consider that the consumer objective is not met simply through bills that reflect efficient and justified costs but also through, among other things, having resilient and compliant water infrastructure that serves customers and the environment.

[REDACTED] we consider that efficiency is part of the proper carrying out of company functions (for the purposes of both the functions and financing duties) and the interests of customers (for the purposes of the consumer objective).

A1.29 Third, in reaching our decisions, we were entitled – indeed, required as a matter of public law¹²⁵ – to take into account a wide range of relevant considerations. The companies are selective as to which considerations they emphasise to the CMA. The

¹²² [OF-OA-034] Water References Competition and Markets Authority Guide, CMA205, December 2024, p. 11, para 3.4.

¹²³ [OF-OA-001] Anglian Water, Statement of Case, March 2024, paras 194, 318, 734.

¹²⁵ The same requirement to have regard to all of the relevant circumstances is also reflected in the wording of Condition B of the companies' licences [OF-OAA-012], which provides that Ofwat 'shall' determine price controls 'having regard to all the circumstances which are relevant in the light of the principles which apply by virtue of Part I of the Act in relation to the Water Services Regulation Authority's determinations, including, without limitation, any change in circumstance which has occurred since the last Periodic Review or which is to occur': see paragraph 8 of Condition B for South East Water [OF-OAA-016] and paragraph 9 of Condition B in the licences for Anglian Water [OF-OAA-018], Northumbrian Water [OF-OAA-017], Southern Water [OF-OAA-020] and Wessex Water [OF-OAA-020].

CMA has the discretion to determine which issues it prioritises during the redetermination process. However, it is required to undertake a thorough evaluation of all relevant evidence and considerations in respect of the matters that fall to be determined.

A1.30 Fourth, it follows that each determination by us is highly fact- and context-specific. While there are some general aspects of prior Ofwat or CMA decisions (for example, the CMA's observations referred to above as to the weighting of the various duties) which may be useful starting points for consideration by us (and the CMA) and to which we have given due weight, each determination is a fresh decision which is not bound by previous determinations or re-determinations, as acknowledged by the CMA in its PR19 Final Report.¹²⁶ Each determination was taken in the light of the most recent evidence available to us and each reflects our evolving views on issues such as costs of capital, econometric modelling techniques and incentivising performance improvements, formed in consultation with the companies and other relevant stakeholders through the process of the development of the methodology for, and implementation of, the price review. In making its determinations, the CMA will have before it information that was not available to us at the time of our final determinations in addition to our reasons and evidence supporting our financial determinations. The CMA may decide to have regard to some or all of that information and will decide how much weight should be attached to each element. It may be that the CMA, after considering all of the information and circumstances, reaches a different view on certain points to that which we reached. That is simply a reflection of the nature of the many (and complex) decisions that are taken in reaching a final view on each company's price controls. It does not detract from the fact that we have given careful and conscientious consideration to our statutory duties in making our final determinations.

A1.31 Finally, as regards the SPS, companies (in particular South East Water and Anglian Water) suggest that we have given insufficient weight to the SPS priorities or have interpreted them too narrowly.¹²⁷ Such suggestions are ill-founded. As set out above, Ofwat – and the CMA – must have regard to all the objectives, duties and priorities set out in the Act and the SPS and reach a decision in the round. We have acted in accordance with the SPS alongside our duties as demonstrated by, among other things: our engagement with other regulators to understand and respond to environmental priorities; our encouragement of long-term planning and improved performance while including safeguards for customers and enhanced monitoring; and our encouragement of innovation and competition.

¹²⁶ [OF-CA-136] CMA, Final Report_CMA_March_2021, p. 98, para. 3.20 'However, we are not bound by the decisions of other Groups in past redeterminations and appeals, where facts, issues and arguments are likely to have differed. We have made our decisions in light of the breadth of relevant evidence.' Certain disputing companies are critical of our approach to prior decisions, see for example [OF-OA-002] Northumbrian Water, Statement of Case, March 2025, Appendix 1 to para 24.

¹²⁷ [OF-OA-005] South East Water, Statement of Case, March 2025, p. 56, para 4.75(b)(ii).

A1.32 We turn now to the challenges made to the performance of Ofwat's duties.

Time frame (short term v long term and the impact on future customers)

A1.33 Certain disputing companies complain that our focus in PR24 was unduly short term.¹²⁸ In doing so, these Disputing Companies make sweeping criticisms.

A1.34 For example, Anglian Water alleges that we have, 'failed to demonstrate long term thinking', 'failed to place appropriate weight on long term considerations', citing what it sees as prior decisions to prioritise low prices (allegedly leading to lack of investment), and 'lack of adequate funding for long term solutions means that companies are forced to increase expenditure on short term less costly solutions, rather than focus on long term sustainable development to the benefit of customers'.¹²⁹

A1.35 South East Water asserts 'Ofwat's proposals are also inconsistent with securing that SEW takes steps for the purpose of enabling it to meet, in the long term, the need for the supply of water to consumers (i.e. Ofwat's resilience duty) and are unnecessary and disproportionate, contradicting Ofwat's resilience and growth duties'.¹³⁰

A1.36 Wessex Water alleges the final determinations are set 'at a level that does not allow Wessex Water to earn a reasonable rate of return to finance its assets and investments in a manner consistent with long-term resilience' and that Ofwat's approach therefore 'negatively impacts both our ability to invest sustainably in a manner that would allow us to properly carry out our functions and, over the long run, consumer welfare, in breach of the Duties'.¹³¹

A1.37 The complaints, whether implicit or explicit in the companies' submissions, amount to suggestions that we have failed to meet our consumer objective, in that we have taken a narrow view and/or inappropriately short-term view of the objective that failed to consider properly both the interests of existing and future consumers as the objective requires;¹³² and we have otherwise undermined or failed to meet others of our duties by our failure to focus on the long term, namely the resilience, financing and sustainable development duties.

A1.38 Such complaints are imprecise and ill-founded. We did not have any overriding short-term aim as the companies claim. Indeed quite the contrary, our approach to, for

¹²⁸ [OF-OA-001] Anglian Water, Statement of Case, March 2025, paras 82, 103, 318, 330, 366, 654, 734; [OF-OA-004], Wessex Water, Statement of Case, paras 8.2-8.3 and [OF-OA-005] South East Water, Statement of Case, March 2025, paras 1.12, 4.54, 6.4-6.7.

¹²⁹ [OF-OA-004] Wessex Water, Statement of Case, March 2025, p. 32, para 5.26.

¹³⁰ [OF-OA-005] South East Water, Statement of Case, March 2025, p. 48, para 4.54.

¹³¹ [OF-OA-004] Wessex Water, Statement of Case, March 2025, p.32, para 5.26.

¹³² [OF-OA-040] Water Industry Act section 2(5A).

example the level of gearing in our notional company (see our Risk and Return document¹³³) and allowances for significant capital investment (see our Costs document¹³⁴) demonstrate that long term resilient companies and infrastructure were a feature of our decisions, as part of taking a view of our duties as a whole. The companies' submissions are erroneously reductive to suggest that the choices available to us (and now, therefore, to the CMA) are between achieving short-term savings and delivering long-term investment.

A1.39 Taking first how we have considered the consumer objective for both current and future customers. Two critical questions we consider in our decisions are whether the expenditure proposed by the companies is no more than it needs to be, including that it is efficient, and whether that expenditure should be directed to more immediate operational issues or developing/taking forward longer-term investment. Spending on projects that is higher than necessary means higher costs to customers in the short term without improvements to service in the long term. Our statutory objective (and that of the CMA) to protect the interests of future, as well as existing, consumers does not immunise the companies against the need to demonstrate the efficiency of, and justification for, their proposed expenditure.

A1.40 Indeed, as set out earlier in this document, given affordability challenges, demonstrating that allowances are efficient and well justified is vital. This is not just about affordability for existing customers: one of the reasons why it is important for us to scrutinise whether claimed expenditure is efficient is that once expenditure allowances become 'built into' a company's regulatory capital value (RCV), that expenditure will be paid for not only by current customers, but by future customers potentially for many decades to come. Thus, customers both now and in future are entitled to expect that they should fund only expenditure allowances that are efficient and well justified and our approach during the PR24 process of considering both existing and future customers in our judgements is entirely consistent with the consumer objective (and other duties).

A1.41 Turning then to the resilience and financing duties as well as sustainable development. In enacting the resilience duty, Parliament was plainly concerned to encourage long-term planning by both us and water companies. The resilience objective, though placed on Ofwat as part of its suite of statutory duties, is in practice directed as strongly at the companies themselves as at Ofwat (and now the CMA). The second limb of the objective is expressly framed in these terms – 'to secure that undertakers take steps for the purpose of enabling them to meet, *in the long term...*' (emphasis added). It includes in particular promoting 'the taking by them of a range of measures to manage water

¹³³ PR24 redeterminations – risk and return common issues.

¹³⁴ PR24 redeterminations – expenditure allowances – common issues.

resources in sustainable ways, and to increase efficiency in the use of water and reduce demand for water...'.¹³⁵

A1.42 Our consideration of resilience pre-dates the implementation of an express resilience objective and is integral to our final determinations. Record levels of expenditure allowances have been permitted precisely to promote both short term operational resilience and long term resilience. Therefore it is incorrect to suggest that we have not furthered the resilience objective. The requirement on us to secure long term resilience, including sustainability does not entail an obligation on us to accept companies' proposed expenditure plans uncritically without assessing their efficiency or requiring that they are supported by adequate evidence. Companies cannot appeal to 'resilience' or 'sustainability' as a means of avoiding the need to undertake appropriate planning and investment. As set out above, learning lessons from the delivery of schemes in PR19 and taking into account the deliverability challenges in PR24, we have supported increased allowances with risk protections and protections around delivery to secure that allowances are appropriately targeted and to incentivise delivery of resilient, sustainable development.

A1.43 The financing duty is inherently prospective. Certain of the companies seek to undermine our discharge of the financing duty by making submissions to the effect that PR24's short-term focus undermines their ability to finance their functions.¹³⁶ We disagree. The regulatory regime strongly supports companies to invest and raise the finance they need to deliver the investment required to properly carry out their functions. PR24 is an evolution of approaches that have been in place for many price reviews and underpin the aim of supporting investment over the long term. Key consistent features of the regime include regulatory independence, five yearly determinations, reopeners and uncertainty mechanisms and indexed returns. Ofwat's evidence¹³⁷ shows that contrary to the submissions of the disputing companies, the water sector continues to attract investment:

- over £5 billion of equity has been raised in the 2020-25 period to support the sector to deliver – this is material at c.5% of RCV, hugely outstripping any period since privatisation and achieved at a time when the allowed return has been at an historically low level in real terms;
- over £0.5 billion of that equity was raised in the period since PR24 representations and was not envisaged in those representations; and
- companies have, since PR24 final determinations announced commitments to provide an additional £400 million of equity not referenced in representations,

¹³⁵ [OF-OA-040] Water Industry Act section 2(2DA)(b).

¹³⁶ [OF-OA-003] Southern Water, Statement of Case, March 2025, p. 218, para 15. [OF-OA-005] South East Water, Statement of Case, March 2025, p. 48, para 4.54. [OF-OA-001] Anglian Water, Statement of Case, March 2025, paras 82 and 318. [OF-OA-003] Southern Water, Statement of Case, March 2025, introduction para 35, executive summary paras 1, 55, 5 and 66, Chapter 3 para 50, Chapter 7 paras 4 and 14-15, 610-611. [OF-OA-002] Northumbrian Water, Statement of Case, March 2025, p. 81, para 271.

¹³⁷ PR24 redeterminations – risk and return – common issues.

with a minimum £1 billion expected to be raised this financial year. Listed companies continue to trade at premia to their MAR, with average premia of 8% in the months of January to March 2025, which compares with the long term premia (22 years) of 10%.

Cost allowances versus outcomes

A1.44 The disputing companies complain, expressly or implicitly, that the performance requirements imposed on them are out of balance relative to their allowances and/or that Ofwat has retrospectively applied assumptions to performance and or use of allowances in PR19 that result in the imposition of unrealistic or unreasonable performance commitments or allowances, amounting to a breach of Ofwat's duties, in particular the financing duty.¹³⁸

A1.45 For example, Anglian Water states, 'At PR24, Anglian is once again expected to achieve unrealistic performance improvements or face excessive penalties, without being funded to do so' and 'Critically, while Ofwat made cuts to our base funding request it also placed considerably higher (and unevidenced) expectations of what can be funded from base expenditure, leading to disallowed enhancement cost requests and a lack of funding to efficiently deliver customer outcomes.'¹³⁹ South East Water advances a similar complaint: 'Ofwat's cost allowances significantly underfund our efficient costs and mean that in practice we will not be able to deliver the performance that our customers want... [a final determination] which leads to this outcome is inconsistent with Ofwat's statutory duties.'¹⁴⁰ Northumbrian Water states that, 'Ofwat's FD24 does not reflect a robust consideration of the risk in the settlement in the round. When the settlement is compared to current expenditure levels and service improvement rates, FD24 is, once again, unlikely to be achievable for the average or median performer in the sector.'¹⁴¹

A1.46 The essence of such complaints is that in the final determinations Ofwat's funding was less generous than they would like. As demonstrated by the quotations above, the point may be couched in the language of breach of statutory duties (for example, as a breach of the financing duty) but is simply a disagreement with the exercise of our judgement on the merits.

¹³⁸ [OF-OA-005] South East Water, Statement of Case, March 2025, paras 4.8 and 5.4 and [OF-OA-003] Southern Water, Statement of Case, March 2026, p. 420, para 35, [OF-OA-004] Wessex Water, Statement of Case, March 2025, para. 5.14, 5.26, 8.2, 8.29 and 10.1.

¹³⁹ [OF-OA-001] Anglian Water, Statement of Case, March 2025, para 1(7).

¹⁴⁰ [OF-OA-005] South East Water, Statement of Case, March 2025, p. 35, para 4.8. Para 1.12 also refers to the combined impact of a number of elements, such as ODIs and a lack of flexibility in how allowances could be spent, leading to an unsustainable level of risk.

¹⁴¹ [OF-OA-002] Northumbrian Water, Statement of Case, section 5, p. 108.

A1.47 First, unlike the companies, we are positioned to take an expert, independent, and objective view of the entire sector, utilising representations and benchmarking evidence from all individual companies (including at least ten companies that are not contesting their final determinations). We can also assess historical performance across the sector and compare company performance, drawing on decades of regulatory intelligence. Although we rely significantly on companies to provide information about their business plans, we possess substantial experience in understanding how cost allowances have impacted performance across various indicators.

A1.48 We have drawn on this experience and information to calibrate each of the companies' performance commitment levels (PCLs) as a package, to be both stretching and achievable. During this redetermination, the CMA will apply its own perspective and experience to address the disputing companies' complaints about the balance between performance requirements and allowances, which is entirely appropriate.

A1.49 Second, the disputing companies' complaints about incentives for under- and overperformance must be viewed in the light of the actual outcomes that are being incentivised and, again, the distribution of upside and downside risk across the package. Companies are motivated to concentrate their challenges on aspects of the package they find excessively burdensome, areas where they perform poorly, and to downplay performance commitments where they might outperform. This strategy aims to secure more attainable performance targets and reduce potential negative impacts. The CMA will be aware, therefore, that the companies' submissions amount to an attempt to unpick selected parts of the package without necessarily considering it in the round.

A1.50 Third, as set out in our Outcomes- Common issues document,¹⁴² our final determinations contained an integrated and flexible application of risk protections, alongside increased levels of risk protections for companies, such that we consider that criticisms that we have failed to consider the level of risk being undertaking or have failed to fund companies for the level of risk, are unfounded. Our use of: risk protections on individual performance commitments to mitigate the effects of extremes in performance; the aggregate sharing mechanism (ASM) to further limit payments at extreme ranges; and the outturn adjustment mechanism (OAM) to adjust returns across all companies if sector-wide performance turns out to be materially different from expectations, all contribute to package being balanced overall.

A1.51 Finally, objections to the final package on grounds of retrospectivity are misconceived.¹⁴³ It is an integral part of the exercise of regulatory judgement that we may look at cogent evidence of considerations from the past, present and future (as

¹⁴² PR24 redeterminations – outcomes – common issues.

¹⁴³ [OF-OA-005] South East Water, Statement of Case, March 2025, p. 39, para 4.26 and p. 61, para 4.79. [OF-OA-002] Northumbrian Water, Statement of Case, March 2025, pp. 444-448, para 426.

discussed above) to best inform our decisions. In particular, it is open to us to take into account any under delivery from previous price review periods when assessing the need to provide additional allowances in the future. This was also a matter on which third parties encouraged us to focus to ensure that customers did not pay twice. Therefore, we reject any suggestion that we have retrospectively imposed requirements on companies or that we have done so arbitrarily as set out further in our Costs document.¹⁴⁴

The financing duty and financeability

A1.52 All of the disputing companies argue that we failed to satisfy the financing duty.

Wessex Water says 'The allowed return is too low, and the expected return is lower still. As a result, we do not consider the Final Determination meets Ofwat's Duties.'¹⁴⁵

Southern Water alleges 'In sum, the allowed return on equity fails market tests and the allowed return on debt does not provide for efficient debt costs. The consequence is that there is a low incentive for investors to allocate new capital to the water sector.

This means that the allowed return is not financeable and therefore Ofwat has not met its finance duty.'¹⁴⁶ South East Water states 'Overall, the PR24 FD is not financeable or deliverable. The allowed return is objectively too low for equity investors and

undermines debt financing and there is insufficient headroom to allow SEW to manage risk'.¹⁴⁷

A1.53 Our financing duty is to: 'act in the manner that [Ofwat] considers best calculated...to

secure that companies holding appointments...as relevant undertakers are able (in particular by securing reasonable returns on their capital) to finance the proper

carrying out of those functions'.¹⁴⁸ The opening words of the duty confirm Ofwat's

inherent discretion: performance of the duty requires the exercise of our regulatory judgement, as it now (in this process) requires the exercise of judgement by the CMA).

We consider that the disputing companies' arguments that the financing duty have not been met are simply disagreements with the exercise of this inherent discretion. We

continue to consider that our final determinations represent a reasonable exercise of our regulatory judgement and would highlight the following four points regarding the

disputing companies' criticisms of our consideration of the financing duty.

A1.54 Firstly, some disputing companies conflate the financing duty with a company-specific

'financeability' analysis. It is either said or strongly implied that these two things should be equated, so that if a company appears to be under some pressure, then Ofwat must

be in breach of its financing duty. For example, South East Water asserts: 'The

financeability test is an overall cross-check of the regulatory determination when taken

¹⁴⁴ PR24 redeterminations – expenditure allowances – common issues.

¹⁴⁵ [OF-OA-004] Wessex Water, Statement of Case, March 2025, p. 242, para 5.14.

¹⁴⁶ [OF-OA-003] Southern Water, Statement of Case, March 2025, p. 416, para 13-14.

¹⁴⁷ [OF-OA-00] South East Water, Statement of Case, March 2025, p. 5, para 1.11(d).

¹⁴⁸ [OF-OA-040] Water Industry Action section 2(2A)(c).

as a whole. It arises out of Ofwat's duty to secure that water companies can – through securing reasonable returns on their capital – finance the proper undertaking of their statutory functions...The conclusion our Board reached when it reviewed the FD in the round is that both the allowed return and the level of cashflows over a five-year period impede – rather than support – our access to financial capital and give us less financial resilience than we ought to have in the face of possible future shocks'.¹⁴⁹

A1.55 Other disputing companies have chosen to characterise the duty as the 'Financeability Duty' or 'Investibility'.¹⁵⁰ This language is never used in the Act. This characterisation seeks to reconstitute the financing duty as a pass or fail test, editing out the need for regulatory judgement that is made explicit in the statutory language. There is no basis for this approach in the statute. It is misconceived, and it would be inappropriate for the CMA to adopt it.

A1.56 Secondly, each of the disputing companies has requested a significant increase in the base allowed return than that which has been accepted by at least ten companies who are raising finance on the basis of our final determinations, supporting the sector and our final determinations being 'investible'. In any event, we do not accept that our final determination for any of the disputing companies was in breach of the financing duty.

A1.57 Thirdly, the criticisms do not amount to substantiated reasons why our approach is unsound. We provided adequate funding for an efficient company with a notional capital structure. Consistent with our previous determinations (and those of the CMA), we consider our financing duty alongside our other duties, including our secondary duty to promote economy and efficiency, that is a proper discharge of our duty in a way that ensures objectivity and neutrality as between different organisational or funding models.

A1.58 Finally, companies cannot, by pointing to our financing duty, divest themselves of the responsibility that they themselves bear for ensuring their own financial resilience. Invoking the existence of the financing duty cannot absolve a company of the need to take responsibility for its own performance against its performance commitment levels or for the consequences of its chosen capital structure. Customers do not have the ability to affect a company's decisions regarding capital and financing. Therefore, companies must take responsibility for their own capital and financing structures and bear the consequences of their decisions within the context of the determination, their appointments and company law. Relaxing that position would pass equity risk from investors to customers contrary to the well understood position of price determinations,

¹⁴⁹ [OF-OA-005] South East Water, Statement of Case, March 2025, p. 85, para 7.4–7.5.

¹⁵⁰ [OF-OA-001] Anglian Water, Statement of Case, March 2025, introduction to Chapter D and paras 186, 194, 318, 365, 402, 563, 622, 654, 655 and 698. [OF-OA-005] South East Water, Statement of Case, March 2025, paras 1.12, 1.26–1.28, 7.31–7.32 and [OF-OA-003] Southern Water, Statement of Case, March 2025, Executive Summary paras 65–66 and Chapter 1 paras 24, 28, 189–191 and 239–241.

significantly harming customers' interests and having the effect of shifting the costs associated with equity risk from equity investors to customers.

A1.59 Notably, our Monitoring Financial Resilience Report 2023–24¹⁵¹ sets out concerns regarding all of the disputing companies. Two of these companies (Southern Water and South East Water) are categorised as 'action required'. South East Water is a company that is underperforming, is carrying a high level of debt in its capital structure and has a weak credit rating. The company needs to strengthen its balance sheet, even taking account of the £75m equity injected in December 2025 in response to the comment Moody's made about South East Water's poor levels of liquidity. Northumbrian Water and Wessex Water are 'elevated concern' and Anglian Water, despite its 'standard' assessment, has a credit rating that is impacted by the challenges associated with its holding company financing arrangements. Through the requests for re-determination companies are seeking to shift equity risk to customers either by improving financial resilience at extra customer cost, or enhancing the value of existing equity. Accepting company requests to amend the risk and return balance to satisfy challenges that are underpinned by the actual levels of financial resilience, or poor company performance, could undermine the principles that have been in place over the long term that underpin the allocation of risk and return between customers and companies.

The growth duty

A1.60 As the economic regulator of the water sector, efficiency and productivity, which are the foundations for economic growth, are part of all our regulatory activities but since 21 May 2024 and as set out above,¹⁵² the government has extended to us the specific growth duty. The Growth Duty Statutory Guidance makes clear that due deference is given to our specific expertise, and the range of duties and objectives to which we are subject, providing that: 'Regulators are independent and are experienced and best placed to balance their own decision-making on duties. Decisions on growth will involve a consideration of a regulator's other duties, for example relating to environmental or consumer protection (such as online safety), and there may be a need to balance multiple objectives.'¹⁵³

A1.61 Therefore, consistent with our other duties, consideration of the growth duty forms part of our exercise of our regulatory judgement in considering all duties in the round. While it is for the CMA to determine the extent to which it considers economic growth as part of its assessment, even in the absence of the specific growth duty, growth was already relevant to our duties in Part 1 of the Act, including through our duty to have regard to

¹⁵¹ [OF-OAA-003] Ofwat, Monitoring Financial Resilience Report 2023–24', November 2024.

¹⁵² [OF-OAA-011] Deregulation Act 2015 section 108. Applicable to the exercise of most regulatory functions, including the conduct of price reviews. The duty does not apply to any regulatory function so far as exercisable in Wales if or to the extent that the function could be conferred by provision falling within the legislative competence of the Senedd Cymru (section 109(3)(c) of the [OF-OAA-011] Deregulation Act 2015).

¹⁵³ [OF-OAA-001] Department for Business & Trade, Statutory guidance: Growth duty, May 2024, p. 8.

the principles of best regulatory practice (including the principles under which regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed).

A1.62 Anglian Water, South East Water and Southern Water have suggested that we have failed to comply with our growth duty (in addition to the resilience and financing duties, see above) because they consider that the final determinations risk them being unable to attract the level of investment we require the sector to secure in PR24 which will prevent investment to drive economic growth in the disputing companies' areas of appointment.¹⁵⁴

A1.63 Such suggestions are fundamentally misconceived.

A1.64 First, economic growth plainly underpins the final determinations. Each of the three building blocks of our final determinations in PR24 (outcomes, expenditure, and risk and return) has an impact on growth and our decisions across each have been taken having regard to the desirability of promoting economic growth.¹⁵⁵ The key challenges at PR24 of affordability, deliverability and financeability are also clearly relevant to economic growth:

- Affordability of essential services supports customers being able to improve growth in the wider economy. Our final determinations allow companies to only charge fair prices to customers for a given level of service, ensuring that customers do not pay more than is required, freeing up money to be spent in other areas of the economy.
- Investment in and delivery of modern, efficient and effective infrastructure, such as clean water and effective sewerage, is essential for economic growth and our final determinations purposefully allow efficient levels of expenditure, where it meets government requirements or will create value for customers.¹⁵⁶ In addition to the investment through PR24, we have continued to evolve our regulatory approach to support the development of major infrastructure projects, the costs of which are allowed for in the final determination¹⁵⁷ and the inclusion of which is required by the Environment Agency and Defra to protect the environment and to plan for future water resources and wastewater services for customers and businesses, including for new housing developments and businesses.

A1.65 Our final determinations also promote productivity and innovation by including incentives for companies to innovate to reduce costs or improve service further. We also

¹⁵⁴ [OF-OA-001] Anglian Water, Statement of Case, March 2025, para 29, introduction to Chapter D, paras 402 and 654, [OF-OA-005] South East Water, Statement of Case, March 2025, paras 1.12 4.54 and [OF-OA-003] Southern Water, Statement of Case, Executive Summary at para 66 and at Chapter 7 paras 14-15, 611 and 625.

¹⁵⁵ [OF-OA-014] Ofwat, PR24 final determinations: Our approach, December 2024, p. 6.

¹⁵⁶ [OF-OA-014] Ofwat, PR24 final determinations: Our approach, December 2024, p. 6.

¹⁵⁷ Our portfolio of 30 major projects is detailed in [OF-OA-030] Ofwat, PR24 final determinations: Major projects development and delivery, December 2024.

fund innovation directly through our innovation fund, which doubled in size to £400 million in PR24, having seen the PR19 innovation fund successfully support over 90 innovation initiatives.

A1.66 Second, the companies rely on vague and bare assertions, unsupported by evidence. Various of the complaints include that 'PR24 FD results in an overall level of risk that is unsustainable ... contrary to Ofwat's statutory duties (including its new growth duty)',¹⁵⁸ 'the increased risk profile associated with this huge increase in enhancement investment, even after Ofwat's mitigations, has not been adequately reflected in the rate of return. Ofwat has therefore failed to discharge its financeability, resilience and growth duties'¹⁵⁹ and 'An unfinanceable allowed return creates a regulatory barrier to investment and therefore Ofwat has also not met its growth duty'.¹⁶⁰ Such arguments are untenable, suggesting incorrectly that increased investment equates to growth, and amount to no more than thinly veiled complaints that our funding was less generous than the companies would like. Investment in the wrong projects, badly spent investment or providing investment funding that is not required, can mean less growth when compared to the alternative, including no investment.

A1.67 Third, such assertions disregard the regulatory judgement inherent in, and indeed demanded by, the performance of the duty. As above, the decisions reached by Ofwat were arrived at in full pursuit of our applicable duties and objectives and following comprehensive consideration of the evidence and expertise at hand, consistent with the guidance on this specific duty: 'An effective regulator will set a strategy that strikes the right balance between competing pressures or duties, informed by an understanding of what approach might best support sustainable growth'.¹⁶¹

¹⁵⁸ [OF-OA-005] South East Water, Statement of Case, March 2025, p. 5, para 1.12.

¹⁵⁹ [OF-OA-001] Anglian Water, Statement of Case, March 2025, p. 112, para 402.

¹⁶⁰ [OF-OA-003] Southern Water, Statement of Case, March 2025, p. 69, para 66.

¹⁶¹ [OF-OAA-001] Department for Business & Trade, Statutory guidance: Growth duty (21 May 2024), p. 8.

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We regulate the water sector in England and Wales.**

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