

April 2025

PR24 redeterminations

# **Response to Wessex Water's statement of case**

# PR24 redeterminations – response to Wessex Water's statement of case

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# 1. Navigation assistance

- 1.1 To assist the Competition Markets Authority (CMA), Table 1.1 below shows where we have responded to the points raised in Wessex Water Services Limited's (Wessex Water) statement of case.
- 1.2 Many of the points raised by Wessex Water are responded to in the following documents:
- PR24 redeterminations – overview of our response to the statements of case;
  - PR24 redeterminations – expenditure allowances – common issues;
  - PR24 redeterminations – outcomes – common issues; and
  - PR24 redeterminations – risk and return – common issues.
- 1.3 This document starts with a brief description of Wessex Water, from our regulatory perspective, then sets out a summary of our Price Review 2024 (PR24) final determination.
- 1.4 If we consider that a point raised by Wessex Water in its statement of case is company-specific, and our response or CMA's considerations are unlikely to have a wider impact on other companies, or the whole sector, we set out our response in section 4 of this document. In order to further assist with navigation of our response to company-specific points, we provide a list of the points covered in each sub-section.
- 1.5 Our summary of the PR24 final determination for Wessex Water, and the remainder of this document, and the suite of documents comprising our response to the five statements of case, is generally structured around the building blocks of the price review: expenditure allowances, outcomes, and risk and return.

**Table 1.1 Navigation assistance**

Point in Wessex Water's statement of case	Statement of case (SoC) reference	For Ofwat's response, see:
Regulation and duties	Paragraph 2.3 Chapter 5	Annex to PR24 redeterminations – overview of our response to the statements of case document
Disinfection at water treatment centres	Paragraph 2.15 onwards Chapter 6 Annex A7	Paragraph 4.18 below and table 4.2 of this document Expenditure allowances – cost adjustment claims – section 12

Point in Wessex Water's statement of case	Statement of case (SoC) reference	For Ofwat's response, see:
Bioresources	Paragraph 2.19 onwards Chapter 7 Annex A8	Paragraph 4.17 and table 4.2 of this document Expenditure allowances – cost adjustment claims – section 11
Wholesale water base costs	Paragraph 2.28 onwards Chapter 8	Paragraph 4.16 and table 4.2 of this document Expenditure allowances – common issues – section 2 – wholesale water models
Phosphorus removal costs	Paragraph 2.37 onwards Chapter 9	Paragraph 4.1.13 and table 4.4 of this document Expenditure allowances – common issues – section 5
Allowed return	Paragraph 2.43 onwards Chapter 10	Section 4 of Risk and return – common issues
Bill impact	Paragraph 2.53 onwards	Section 7 of Risk and return – common issues
Business rates	Executive summary Chapter 2, Paragraph 2.52, 2.57 Chapter 8, para 8.51	Expenditure allowances – common issues – Business rates section

## 2. Introduction

- 2.1 Wessex Water is both a water undertaker and a sewerage undertaker. It serves 1.3 million household customers, and 75,000 business customers, across Dorset, Somerset, Bristol, most of Wiltshire and parts of Gloucestershire and Hampshire. Wessex Water is owned by YTL Corporation. As at 31 March 2024, YTL Corporation Berhad was 50.2% owned by Yeoh Tiong Lay & Sons Family Holdings Limited, with 49.8% owned by third-party shareholders.
- 2.2 We currently have an ongoing enforcement case for Wessex Water, relating to the whether it is operating its sewage treatment works in line with its environmental obligations.<sup>1</sup> In our latest water company performance report, we categorised Wessex Water as 'average'.<sup>2</sup> It has been in this category for four consecutive years.
- 2.3 In our most recent monitoring financial resilience report, we categorised Wessex Water as 'elevated concern', which means that we have identified some concerns or potential concerns with the company's long-term financial resilience that may require action to redress.<sup>3</sup>
- 2.4 We assessed the business plan it submitted in October 2023 against our quality and ambition assessment.<sup>4</sup> In our draft determinations, we categorised Wessex Water's plan as inadequate, as it did not meet our minimum quality expectations in the round.<sup>5</sup> We set the company a number of conditions to improve its plan. At final determinations, we determined that Wessex Water had made progress against most of its conditions and moved its plan out of the inadequate category.<sup>6</sup> However, we still had outstanding concerns, with the company having only partially met three of its six conditions, and having not met one other condition.

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<sup>1</sup> [OF-OA-055] Ofwat, Investigation into sewage treatment works and sewage networks, March 2022.

<sup>2</sup> [OF-OU-017] Ofwat, Water Company Performance Report 2023–24, October 2024, slide 8.

<sup>3</sup> [OF-OAA-003] Ofwat, Monitoring Financial Resilience report 2023–24, November 2024, p.7.

<sup>4</sup> [OF-OU-002] Ofwat, Creating tomorrow, together: our final methodology for PR24, December 2022, chapter 11.

<sup>5</sup> [OF-OA-042] Ofwat, PR24 draft determinations: Quality and ambition assessment summary, July 2024, p. 3, Table 1.

<sup>6</sup> [OF-OA-016] Ofwat, PR24 final determinations: Quality and ambition assessment summary, December 2024. p. 20.

### 3. Wessex Water: A summary of our PR24 final determination

- 3.1 In this section, we summarise what was included in our final determination in the three main areas of expenditure allowances, outcomes and risk and return, and provide more information on the key issues that arose between us and Wessex Water during the PR24 process.
- 3.2 The following table sets out the key metrics included in Wessex Water's February 2024 PR24 business plan submission to us, our draft determination, the company's representation on our draft determination and our final determination.
- 3.3 We provide an Appendix to this document that sets out more key data.

**Table 3.1 Summary of key metrics**

	Revised business plan (Feb 2024)	Draft determination	Company view (August 2024 representations)	Final determination
Totex, 2025-2030 (£million) (post frontier shift/RPEs)	5,579	3,699	5,086	4,231
PAYG rate (%)	30.30	30.90	33.60	38.20
Allowed return (%)	4.39	3.72	3.72	4.03
RCV run-off rate (%)	3.77	3.76	3.88	3.85
Allowed revenue, 2025-30 (£million)	3,850	3,083	3,846	3,632
Average bill per household customer, 2025-30 (£)	628	500	634	594

### Expenditure allowances

- 3.4 Wessex Water's totex allowance forms part of an in the round package that is stretching but achievable and is set at a level that ensures that customers only pay for efficient costs.
- 3.5 In our final determination, we allowed Wessex Water a total expenditure ('totex') allowance of £4.23 billion (after frontier shift/RPEs), an increase of £390 million

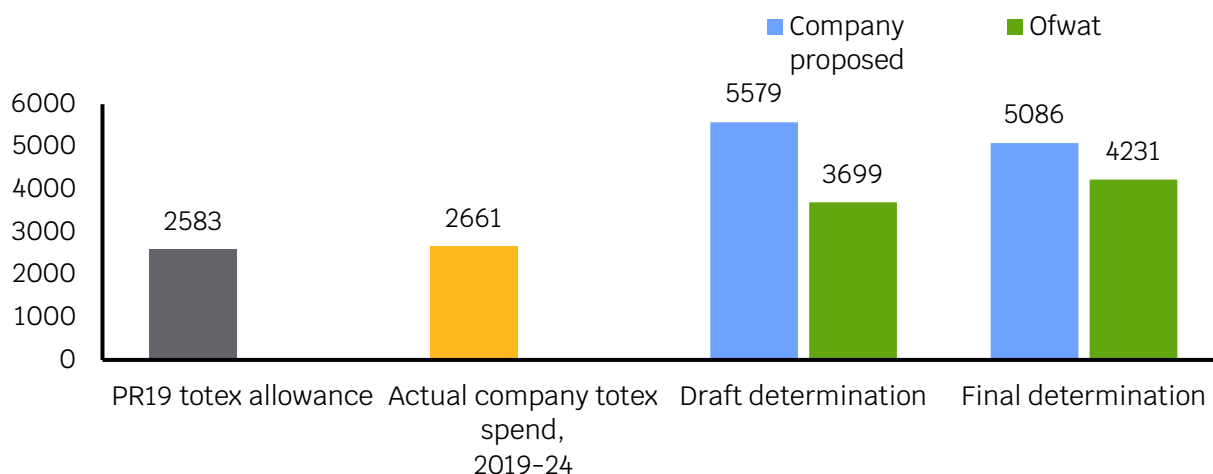
compared to our draft determination.<sup>7</sup> Table 3.2 shows the changes in the requested and allowed expenditure allowances during the PR24 process.

**Table 3.2 Overview of final determination total expenditure allowances and previous stages of PR24 for Wessex Water (five-year period, after frontier shift/RPEs, 2022–23 prices)**

Five-year total	BP Oct 23 (£m)	BP Jan/Feb 24 (£m)	DD (£m)	Rep Aug 24 (£m)	FD (£m)	FD vs Rep (%)	FD vs Rep (£m)
Overall expenditure	5031	5,579	3,699	5,086	4,231	-17	-855
Base expenditure	2425	2,696	1,996	2,530	2,183	-14	-347
Enhancement expenditure	2606	2,883	1,703	2,556	2,048	-20	-508

3.6 In Figure 3.1, we show how PR24 expenditure proposals and allowances compare to PR19 expenditure allowances and the most recent actual expenditure levels.

**Figure 3.1 Overview of totex allowances for Wessex Water, £m (2022–23 prices)<sup>8</sup>**



3.7 As part of its representation on our draft determination, Wessex Water reduced its total expenditure request to £5.09 billion, from £5.58 billion in its updated business plan

<sup>7</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, December 2024, p. 2.

<sup>8</sup> Actual company totex spend data provided by companies in their yearly APR submissions, converted to 2022–23 price base. Includes wholesale water, sewage, bioresources and retail. Excludes grants and contributions.

submitted in February 2024.<sup>9</sup> This included a £214 million reduction in its phosphorus removal enhancement request and a £198 million reduction in its base expenditure request. By our final determination in December 2024, we had carried out further work to evaluate the robustness of our modelling results. We introduced the concept of engineering outliers, where we provided an uplift to reflect unique scheme-specific characteristics. We also provided uplifts to the company's base allowance for mains renewals and network reinforcement. However, even after these changes, Wessex Water's request remained 17% above what we considered to be its efficient costs.<sup>10</sup>

- 3.8 Wessex Water's business plan put forward cost estimates that appeared out of step with the rest of the sector. We found that the company had not provided sufficient and convincing evidence to justify all the higher costs that it proposed. On base expenditure, we concluded that accepting the capital maintenance cost adjustment claim, without any commitment to additional outcomes or outputs, would effectively allow customers to pick up inefficient costs.<sup>11</sup> On enhancement expenditure, while we took additional measures ahead of our final determinations to account for outlier schemes, the overall conclusion was that Wessex Water put forward inefficient cost estimates across a number of key areas. The overall cost gap of £854 million in our final determination was the second largest across the industry, as a proportion of requested investment.<sup>12</sup>

## Base expenditure

- 3.9 We allowed Wessex Water £2.2 billion in base expenditure. Our PR24 base expenditure allowance for Wessex Water is 10% (£206 million) higher than its PR19 allowance and 2% (£38 million) higher than its actual spend in 2019–24, as shown in Figure 3.2.<sup>13</sup>

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<sup>9</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, December 2024, p. 2.

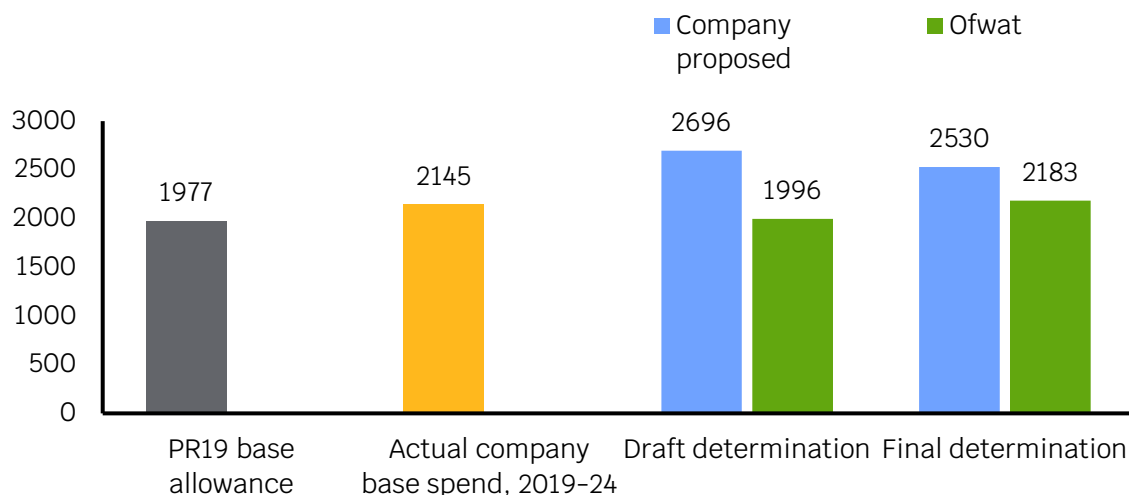
<sup>10</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, December 2024, p. 385.

<sup>11</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, December 2024, p. 34.

<sup>12</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, December 2024, p. 385.

<sup>13</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, December 2024, p. 377.



**Figure 3.2: Overview of base allowances for Wessex Water, £m (2022–23 prices)<sup>14</sup>**

- 3.10 Our final determination base expenditure allowance is 9% higher than the allowance we made at draft determination.<sup>15</sup> This is mainly due to updates we made to: our energy cost adjustment; our allowance for business rates; our sector-wide mains renewals adjustment; applying a new sector-wide network reinforcement adjustment; and applying an economies of scale at water treatment works adjustment.
- 3.11 At draft and final determinations, we partially accepted Wessex Water's cost adjustment claim for the ongoing costs of nature-based solutions (£19 million of £35 million requested).<sup>16</sup>
- 3.12 In its August 2024 draft determination representation, Wessex Water put forward a cost adjustment claim worth £494 million for capital maintenance, which superseded three claims made in its original business plan.<sup>17</sup> Our rejection of this claim effectively accounts for the entire base expenditure gap at final determination, which is £346 million.
- 3.13 Wessex Water stated that this cost adjustment claim for capital maintenance reflected the difference between its own bottom-up analysis of base expenditure – which it argued was the most appropriate way to estimate base requirements – and Ofwat's draft determination allowance.<sup>18</sup> The company argued that our approach, which is primarily based on benchmarking using econometric models, has historically

<sup>14</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, December 2024, p. 382.

<sup>15</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, December 2024, p. 377.

<sup>16</sup> [OF-CA-230] Ofwat, Base cost adjustment claim feeder model – Wessex Water, December 2024, tabs 'WSX\_CAC1' 'WSX\_CAC2', 'WSX\_CAC4' and 'WSX\_CAC5'.

<sup>17</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, December 2024, p. 377.

<sup>18</sup> [OF-WSX-001] Wessex Water, WSX-M02 – Summary of Wessex Water's response to Ofwat's PR24 draft determination, August 2024, p. 7.

underfunded companies. It therefore argued that £494 million was required to 'catch up' on historical shortfalls, as well as provide a sufficient allowance for future capital maintenance.

- 3.14 The claim did not meet a number of the assessment criteria set out in our methodology.<sup>19</sup> For example, Wessex Water did not provide evidence of any outputs the additional expenditure would deliver. This meant we would not have been able to hold the company to account for improved outcomes from the cost adjustment. Accepting the claim risked customers paying twice while receiving nothing additional in return. The company also failed to demonstrate what factors outside of its control were driving the forecast increase in capital maintenance expenditure requirements.
- 3.15 We also do not consider the evidence provided at representation supports Wessex Water's arguments regarding historical 'underfunding'. Our analysis indicates that Wessex Water has underspent on totex between PR99 and PR19.<sup>20</sup> Based on information provided by the company during the PR24 process, Wessex Water's assets generally did not appear to have deteriorated in asset condition since 2010.<sup>21</sup> An exception to this was water mains, for which we provided an uplift of £23 million to Wessex Water's base allowance.<sup>22</sup> Several companies stated during the PR24 process that they have maintained asset condition to date with base expenditure allowances.<sup>23</sup>
- 3.16 Some changes to Wessex Water's base expenditure allowances between PR19 and PR24 reflect improvements we made to our weighted average population density variables at PR24 and a data input error in PR19. Wessex Water did not acknowledge that it provided water services in Poole when completing a density data request.<sup>24</sup> This meant Wessex Water's PR19 wholesale water base cost allowance was around £60 million higher than it should have been (in 2022–23 prices). We have not clawed this back, but have ensured that this error has not persisted into PR24 through the development of our refined weighted average population density variables.

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<sup>19</sup> [OF-CA-230] Ofwat, Base cost adjustment claim feeder model – Wessex Water, December 2024, tabs 'WSX\_CAC1' 'WSX\_CAC2', 'WSX\_CAC4' and 'WSX\_CAC5'.

<sup>20</sup> [OF-CA-230] Ofwat, Base cost adjustment claim feeder model – Wessex Water, December 2024, tabs 'WSX\_CAC1' 'WSX\_CAC2', 'WSX\_CAC4' and 'WSX\_CAC5'.

<sup>21</sup> [OF-CA-230] Ofwat, Base cost adjustment claim feeder model – Wessex Water, December 2024, tabs 'WSX\_CAC1' 'WSX\_CAC2', 'WSX\_CAC4' and 'WSX\_CAC5'.

<sup>22</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, December 2024, p. 39, Table 4.

<sup>23</sup> For example, Severn Trent Water commented that although the data may indicate a deterioration in condition for some assets, it has maintained its assets over time. United Utilities also commented that it has maintained stable asset performance and condition over time.

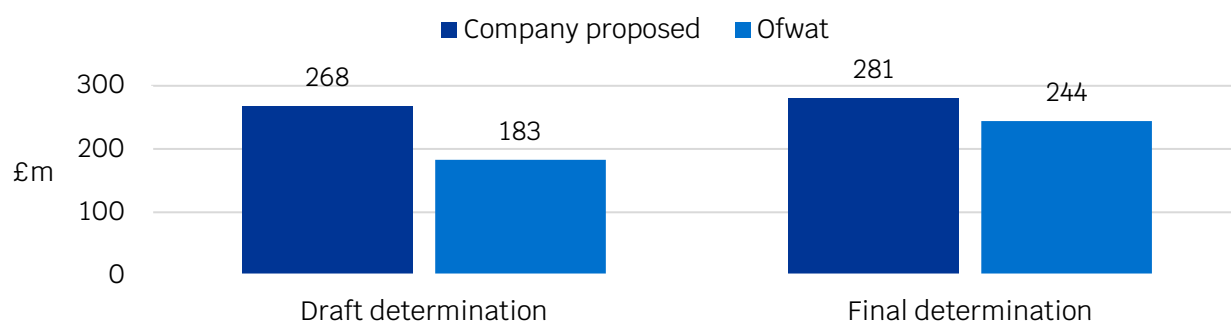
<sup>24</sup> Ofwat, 'PR24 redeterminations – expenditure allowances – common issues', April 2025, section 2.

## Enhancement expenditure

3.17 We allowed Wessex Water £2.0 billion as enhancement expenditure at final determination.<sup>25</sup> This followed a £327 million reduction in the allowance requested by the company between business plan submission and draft determination representation. Ninety-two percent of the £508 million enhancement cost gap for Wessex Water is within the wastewater price controls.<sup>26</sup> The vast majority of the gap is attributable to the company's performance in our econometric benchmarking models, rather than the outcome of deep dive assessments of enhancement claims.<sup>27</sup> Wessex Water's proposed costs appeared comparatively inefficient in many of our largest models, without sufficient justification. This continued to be the case after accounting for engineering outlier schemes.

## Water

**Figure 3.3: Water enhancement requests and allowances, draft and final determination (after frontier shift/RPEs)**



3.18 Our final determination allowance for water enhancement is £244 million. As shown in Figure 3.3, this is 13% (£37 million) lower than Wessex Water's request in its draft determination representation.<sup>28</sup> This negative cost gap reduced significantly between draft determination and final determination, primarily because we increased our allowances for raw water deterioration, cyber and leakage. The remaining gap is primarily due to:

- **Leakage:** We allowed £8 million of a £23 million request.<sup>29</sup> We set a higher unit rate for relatively good performers on leakage, such as Wessex Water (£2.1 million per

<sup>25</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, December 2024, p. 384, Table 54.

<sup>26</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, December 2024, p. 384, Table 54.

<sup>27</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, December 2024, pp. 377-378.

<sup>28</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, December 2024, p. 384.

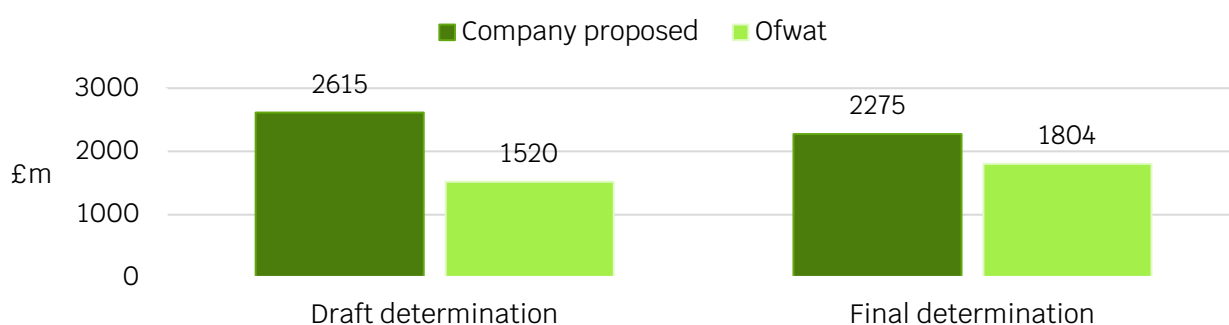
<sup>29</sup> [OF-OU-081] Ofwat, PR24 final determinations: Enhancement costs aggregator model, December 2024, tab 'Water – post adj total'.

ML/d rather than £1.4 million per ML/d). However, Wessex Water put forward a unit cost for non-mains renewals activity that was four times higher than our benchmark, without sufficient justification.

- **Supply:** We allowed £10 million of a £16 million request.<sup>30</sup> We applied a challenge to Wessex Water's proposed adaptive pathway schemes, as following a deep dive assessment we had concerns that the investment was inefficient.

## Wastewater

**Figure 3.4: Wastewater enhancement requests and allowances, draft and final determination (after frontier shift/RPEs)**



3.19 As shown in Figure 3.4, our final determination allowance for wastewater enhancement is 21% (£471 million) lower than Wessex Water's request in its representation on our draft determination. This negative gap is smaller than the 42% cost gap between the company's original business plan and our draft determination. This gap decreased primarily because Wessex Water reduced its request by £340 million in its representation on the draft determination, particularly in the areas of phosphorus removal and Industrial Emissions Directive (IED). We further reduced the gap by increasing allowances for nitrogen removal, IED and sludge cake storage.

3.20 The largest reason for the wastewater enhancement negative cost gap is in the area of phosphorus removal. In this area, we allowed £630 million of a £916 million request.<sup>31</sup> We found that Wessex Water's cost estimates were generally inefficient compared to other companies. This was after we had made further adjustments for schemes that we viewed to be more costly to deliver from an engineering perspective, such as schemes that upgrade to tight phosphorus permits (<0.25mg/l) and schemes that have a biological treatment component. We note that most companies have more experience

<sup>30</sup> [OF-OU-081] Ofwat, PR24 final determinations: Enhancement costs aggregator model, December 2024, tab 'Water – post adj total'.

<sup>31</sup> [OF-OU-081] Ofwat, PR24 final determinations: Enhancement costs aggregator model, December 2024, tab 'Waste – post adj total'.

with phosphorus removal upgrades compared to other enhancement areas, due to the large PR19 enhancement programme. Therefore, companies should be able to forecast PR24 expenditure requirements more precisely than other enhancement areas. We assigned equal weights to historical and forecast models in our assessment. The implied allowances for Wessex Water were much lower when using the historical models. This approach, along with not applying any catch-up efficiency challenge, may have been favourable to Wessex Water, as in other settings such as base costs, where we used historical data only to set efficient allowances.

## Delivering outcomes for customers and the environment

- 3.21 Wessex Water's final determination includes targets that are achievable yet stretching, supported by incentives that link performance with expected financial returns and reputational standing.
- 3.22 We considered Wessex Water's performance commitment forecasts in its February 2024 business plan were relatively unambitious.<sup>32</sup> As set out in Table 3.3, compared to the rest of the sector, Wessex Water has tended to perform relatively well on key performance commitments in the 2020–24 period. In 2023–24, Wessex Water met the performance targets for 7 of the 12 performance indicators reported in our water company performance report.<sup>33</sup>
- 3.23 In its representation, Wessex Water increased the stretch for a number of performance commitments. However, the August 2024 version of its business plan would see the company fall to the middle of the pack on most measures, and even to the lower quartile on some. At final determination we have therefore pushed the company to deliver better outcomes for customers on some measures, while the common performance commitment levels (PCLs) on other measures are less stretching than the company proposed.

**Table 3.3 Wessex Water actual performance 2020–24 versus company 2029–30 forecasts for key performance commitments**

Performance commitment	2020–24 Wessex Water average actual performance	Proposed 2029–30 PCL, Wessex Water representation on our draft determination
Water supply interruptions	Upper quartile	Lower quartile

<sup>32</sup> [OF-WSX-004] Ofwat, PR24 draft determinations: Wessex Water – Quality and ambition assessment appendix, July 2024, p. 1.

<sup>33</sup> [OF-OU-017] Ofwat, Water Company Performance Report 2023–24, October 2024, p. 6.

<b>Leakage</b>	Upper quartile	Middle
<b>Per capita consumption</b>	Middle	Middle
<b>Repairs to burst mains</b>	Lower quartile	Middle
<b>Internal sewer flooding</b>	Upper quartile	Middle
<b>Storm overflows</b>	Upper quartile	Lower quartile
<b>Total pollution incidents</b>	Middle	Middle
<b>Sewer collapses</b>	Upper quartile	Middle

- 3.24 We assess that, if Wessex Water achieved its own performance commitment forecasts as submitted in its representation on our draft determination, the company would stand to earn a net outperformance payment over 2025–30 of £1.7 million over the 2025–30 period.<sup>34</sup> On outcomes, Wessex Water's determination may therefore be considered favourable to the company. This analysis does not include C-MeX, D-MeX and BR-MeX, since these metrics are operated on a relative basis, rather than by setting a performance commitment level.
- 3.25 Our final determination also protects Wessex Water from the impact of extreme underperformance. We applied underperformance deadbands for all companies for four performance commitments and for Wessex Water, we applied collars to 14 of its 16 other financial performance commitments.<sup>35</sup> At the same time, we applied caps to 12 performance commitments, to mitigate the impact of extreme outperformance on bills, and outperformance deadbands to two.

## Aligning risk and return

### Risk and return

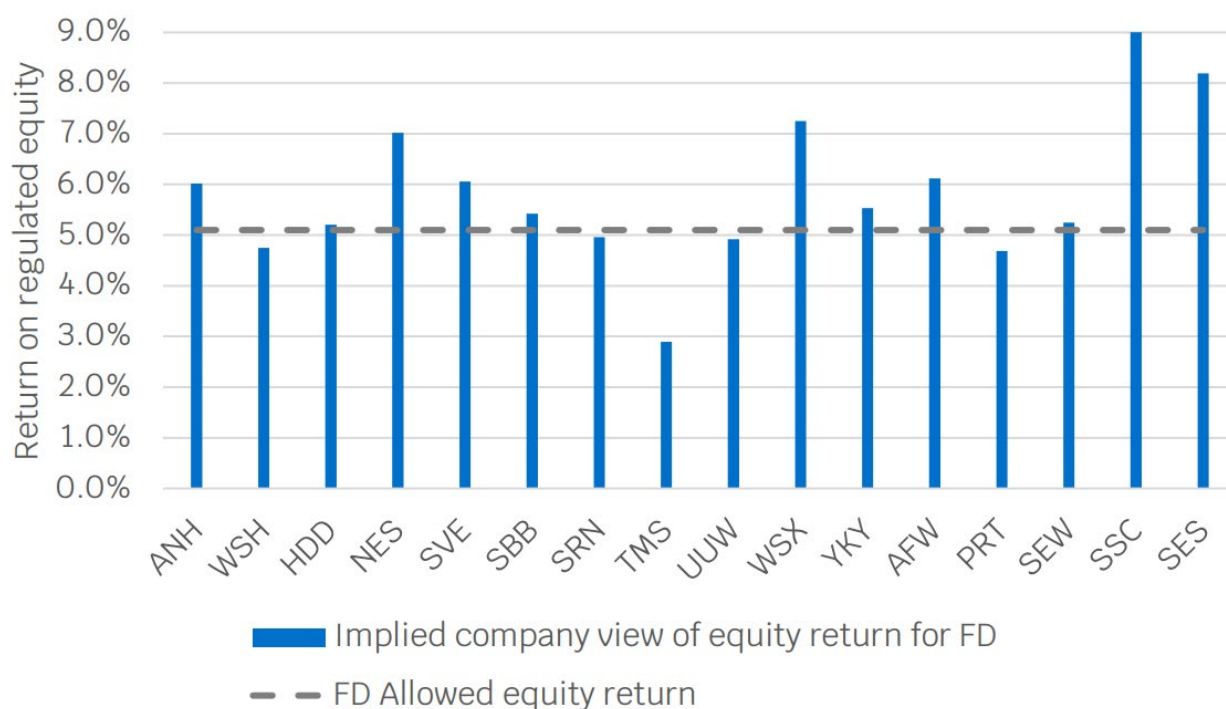
- 3.26 We consider that our final determination for Wessex Water provided a reasonable balance of risk and return.
- 3.27 To illustrate the balance of risk and return our final determination provides, in Figure 3.5 we have adjusted Wessex Water's central view of outturn equity returns set out in its representation to reflect changes in our final determination. These include changes to expenditure allowances, the outcomes package and the allowed return. Presenting these results against the allowed base equity return of 5.1% in our final determinations, we come to an indicative central view of over 7% equity return for Wessex Water. This is

<sup>31</sup> [OF-OU-077] Ofwat, ODI Payment Calculator – with performance forecasts, January 2025, tab 'Output by Company (with ASM)'.

<sup>35</sup> [OF-SRN-009] Ofwat, PR24 final determinations: Key Dataset 1: Outcomes data, December 2024.

well in excess of the base equity return and only South Staffs Water and SES Water have a higher figure in our analysis. This analysis excludes the further risk protections for companies added since draft determinations, including changes to how we apply price control deliverables (PCDs), the introduction of new notified items, and a new bespoke interim determination process, all of which we would expect to reduce downside risk for companies.

**Figure 3.5 Indicative company view of regulated equity returns under the final determinations<sup>36</sup>**



- 3.28 Our view is that efficient companies have a reasonable prospect of earning the base allowed return on equity. We assessed that Wessex Water's overall balance of incentives in our final determination was slightly skewed to the upside, at -5.0% to +5.1%.
- 3.29 In its October 2023 business plan, Wessex Water used an allowed return of 4.45%.<sup>37</sup> This was one of the highest proposed rates in the sector and materially higher than our 'early view' of 3.29%. The company's proposed allowed return on equity was, at 6.25%, higher than the upper bound of its advisors' cost of equity range (5.7%), which used the same June 2023 data cut-off.<sup>38</sup> We did not consider that Wessex Water's plan provided compelling evidence for its departures from our approach to setting the allowed return.

<sup>36</sup> [OF-OA-020] Ofwat, PR24 final determinations: Aligning risk and return – appendix, December 2024, p. 9, Figure 4.

<sup>37</sup> [OF-WSX-002] Wessex Water, WSX02 – An overview of our business plan, October 2023, p. 223.

<sup>38</sup> [OF-WSX-002] Wessex Water, WSX02 – An overview of our business plan, October 2023, p. 227.



- 3.30 In our draft determinations, we set an allowed return of 3.72%.<sup>39</sup> This reflected increases in the cost of finance, as well as our decision to apply an allowed return on equity that is towards the upper end of our range, to support the increased levels of investment in 2025–30. Wessex Water's representation on our draft determination proposed an increased rate of 4.58%. We set an allowed return of 4.03% in our final determination. The increase reflected targeted changes to our methodology, as well as market data suggesting a higher cost of finance.
- 3.31 Our final determination also accepted Wessex Water's proposal to change its policy regarding cost recovery rates from the approach in its business plan.<sup>40</sup> The company had originally proposed to recover capitalised infrastructure renewals expenditure over time through RCV run-off, but changed its approach in its draft determination representation to recover at least part of this expenditure in-period. This increased the company's revenue allowance for 2025–30, compared to the approach applied in our draft determination. Despite this being a material change from Wessex Water's original business plan, we accepted the new approach as it was consistent with our PR24 methodology.

## Financeability

- 3.32 We assessed that Wessex Water's final determination was financeable on the basis of the notional company, such that it will be able to raise the necessary levels of debt and equity to deliver the required investment. To support financeability and to maintain reasonable gearing levels, our final determination included an equity injection for Wessex Water of £512 million, with a £13 million allowance for issuance costs, and allowed for dividends for the notional company of £485 million (4% yield).<sup>41</sup> The financial ratios assessed in our final determination support credit ratings that are well within the investment grade at a target credit rating of at least Baa1/BBB+.
- 3.33 Wessex Water did not use our notional capital structure to underpin either its business plan or draft determination representation. It applied a gearing level of 60%, rather than the 55% signalled in our PR24 methodology, as it considered that we set the notional gearing level too low. Our view is that there is a stronger role for equity in the notional capital structure than used in our recent determinations. This reflects the need for the sector to maintain adequate levels of financial resilience, to support the sector to raise necessary levels of finance, reflecting also the level of revenue at risk from the incentive package that will apply for the 2025–30 period. Further, the high level of

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<sup>39</sup> [OF-OA-021] Ofwat, PR24 final determinations: Aligning risk and return – allowed return appendix, July 2024, p. 5.

<sup>40</sup> [OF-OA-019] Ofwat, PR24 final determinations – Aligning risk and return, December 2024, p. 30, footnote 18.

<sup>41</sup> [OF-OA-021] Ofwat, PR24 final determinations: Aligning risk and return appendix, December 2024, p. 71, Table 8.



inflation that has occurred in the 2020–25 period would enable a company with the notional capital structure to reduce gearing levels naturally to 55% or below by the start of the 2025–30 period. We explain these issues further in our 'risk and return – common issues' document.

## Actual company structure

- 3.34 Our view is that efficient companies have a reasonable prospect of earning the base allowed return on equity. We assessed that Wessex Water's overall balance of incentives in our final determination was slightly skewed to the upside, at –5.0% to +5.1%.<sup>42</sup>
- 3.35 Wessex Water reported gearing of 69% at 31 March 2024.<sup>43</sup> The company's business plan stated a target credit rating of Baa1/BBB+ for the actual capital structure, which is in line with the notional target set in our final determination. The business plan proposed no new equity and payment of no dividends.
- 3.36 In its response to our draft determination, we required Wessex Water to provide additional Board assurance and a financial resilience plan, with evidence of investor support. The company's response reconfirmed its proposal for a full restriction of dividends in the 2025–30 period. However, taking account of the scale of the investment programme, the company provided insufficient evidence to convince us that it will be able to maintain sufficient headroom in the event of downside risks and achieve its target credit rating. Wessex Water remains subject to targeted ongoing monitoring and engagement on its financial resilience, as it was categorised as 'Elevated Concern' in our monitoring financial resilience report.<sup>44</sup> We continue to consider the company may need to reconsider its approach to maintaining financial resilience in the context of our final determination and other factors external to the decision.

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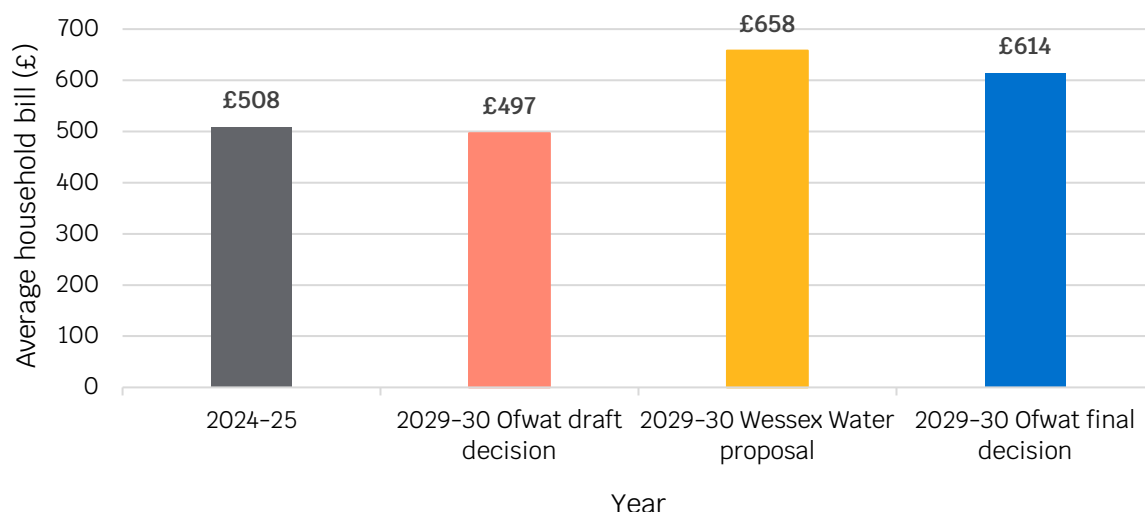
<sup>42</sup> [OF-WSX-005] Ofwat, PR24 RoRE, December 2024, tab 'FD'.

<sup>43</sup> [OF-WSX-003] Wessex Water, Wessex Water: Annual Performance Report 2023–24, July 2024, p. 24.

<sup>44</sup> [OF-OAA-003] Ofwat, Monitoring Financial Resilience Report 2023–24, November 2024, p. 7.

## Affordability

**Figure 3.6 Average household bills for Wessex Water, 2024-25 and 2029-30, before inflation<sup>45</sup>**



3.37 Our final determination saw an increase in average household bills of £106 (21%) from 2024-2025 to 2029-30 for Wessex Water customers, before inflation.<sup>46</sup>

3.38 Wessex Water plans to increase social tariff provision from 3% of households in 2020-25 to 7% in 2025-30. The company plans to use £39 million of cross-subsidy from other customers to help customers repay debts by matching their payments. It has explained that this scheme is not funded by shareholders but is part of the customer agreed cross-subsidy that also funds social tariffs. Wessex Water has committed to a shareholder contribution of £1 million from shareholders for affordability support. This is forecast to represent 0.01% of Wessex Water's Return on Regulated Equity, which at the final determination was the second lowest shareholder contribution of all water companies.<sup>47</sup>

<sup>45</sup> Proposal reflects the wholesale allowed return on capital (4.58% real, CPIH) proposed by the company as an alternative to the allowed return in our draft determination. The bill has been capped using profiling to be no more than a 30% increase in bills from the 2024-25 value.

<sup>46</sup> Our decision is for the revenue companies can collect through bills, not the average bills per customer – the latter is a forecast.

<sup>47</sup> [OF-OA-048] Ofwat, Summary of water companies published plans for affordability for 2025-30, December 2024, p. 10, Table 1.3.

## 4. Wessex Water: Our response to its statement of case

### Introduction

- 4.1 If we consider that a point raised by Wessex Water in its statement of case is company-specific, and our response or CMA's considerations are unlikely to have a wider impact on other companies, or the whole sector, we set out our response in the following section of this document. In order to further assist with navigation of our response to company-specific points, we provide a list of the points covered in each sub-section.
- 4.2 We organise this section around the building blocks of the price review: expenditure allowances, outcomes, and risk and return.
- 4.3 Wessex Water has been focused with the issues that it sets before the CMA, while at the same time reserving the right to raise additional issues as the process progresses. In the appendix to our 'overview of our response to the statements of case' document, we explain how our PR24 final determinations reflect our statutory duties. We also respond to specific comments about our duties, made by companies in statements of case, including those from Wessex Water.
- 4.4 Wessex Water states the bill impact of its requests would be a 38% increase from 2024-25 to 2029-30, but – similarly to its business plan – asks that the CMA uses financial levers to defer some impacts to future periods and keep the increase to 30% or below.
- 4.5 Wessex Water criticises our quality and ambition assessment (QAA) for, in its view, incentivising companies to minimise base costs. It also implies that the QAA incentivised it to put forward a plan that was not financeable, by penalising companies for not using our 'early view' allowed return. However, it does not ask the CMA to consider the QAA within its redetermination and we consider this to be an area that can be deprioritised from the redeterminations (see section 5 of this document).

### Expenditure allowances

- 4.6 At final determination, Wessex Water had an overall cost gap of 17%, or £855 million. This reflected a reduction of £493 million in the requested costs from the company, as well as an increase in its allowance of £532 million. The costs of its schemes were generally considered inefficient when compared to other companies.

4.7 As shown in Table 4.1, the company has requested an additional £739 million compared to our final determination. We estimate this means the company has reduced its requested allowance by £116 million compared to its draft determination representation. The CMA may want to request updated business plan data tables from the company, which signposts changes from its representation on the draft determinations.

**Table 4.1 Cost gap at final determination by area (after frontier shift and real price effects, 22-23 prices)**

	Company view (February 2024) (£m)	Company view (August 2024) (£m)	Final determination (£m)	Statement of case (£m)	Cost gap FD vs SoC (£m)
<b>Total expenditure</b>	5,579	5,086	4,231	4,970	-739
<b>Base expenditure</b>	2,696	2,530	2,183	2,668	-485
<b>Enhancement expenditure</b>	2,883	2,556	2,048 <sup>48</sup>	2,302	-254

## Setting our base allowances

4.8 Our base expenditure allowance at final determination totalled £2.2 billion. This was 10% more than its PR19 allowance, and 2% more than the company has spent over the last five years. However, it was 14% less than what the company requested in its draft determination representation, which was explained by our decision to not allow the company's capital maintenance cost adjustment claim.

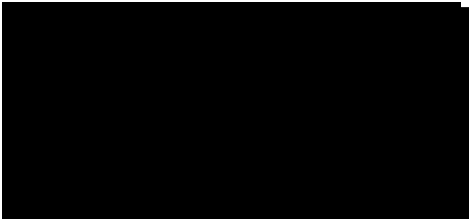
4.9 We note that Wessex Water's PR19 wholesale water base cost allowance was around £60 million higher than it should have been (in 2022-23 prices). This was due to a data input error. Wessex Water did not acknowledge that it provided water services in Poole when completing a population density data request at PR19. We have not clawed this money back but have ensured that this error has not persisted into PR24 through the development of our refined PR24 weighted average population density variables.

4.10 In its statement of case, Wessex Water has raised four issues in relation to our base cost assessment:

<sup>48</sup> This represents the published final determinations allowance. Post final determinations corrections have determined that this figure should be increased by £45 million.

- 4.11 **Wholesale water base costs** – Wessex Water questions the robustness of the wholesale water econometric models. The company suggests that the models do not capture the full complexity of water company operations and provides new analysis to try and demonstrate that the models lead to counterintuitive outcomes under different scenarios. The company asks the CMA to accept its revised bottom-up wholesale water base costs of £892 million. We estimate the company has increased its request by around £95 million from its draft determination representation.
- 4.12 **Bioresources capital maintenance cost adjustment claim** – Wessex Water asks the CMA to consider new evidence related to a £108 million cost adjustment claim to deliver improvements across its sludge treatment centres. The company states this was requested in its draft determination representation. However, the evidence submitted in its statement of case is new and was not assessed for our final determinations.
- 4.13 **Water treatment disinfection improvements** – Wessex Water states the need for additional investment to upgrade disinfection treatment methods at specific sites in line with guidance produced by the World Health Organisation (WHO) and ongoing engagement with the DWI. This investment is valued at £47 million. The company states this was requested in its draft determination representation. However, the evidence submitted in its statement of case is new and was not assessed for our final determinations.
- 4.14 **Business rates** – Companies have received new information since final determinations from the Valuation Office Agency (VOA). Wessex Water has increased its business plan request by £16.2 million. We have provided an updated model assessment of business rates liabilities based on this new information. As explained in our 'overview of our response to the statements of case' document, this is an area that we consider the CMA could deprioritise.
- 4.15 Wessex Water also raises concerns with our overall approach to setting base expenditure allowances; the mains renewals sector wide adjustment and associated PCD; and our 1% per annum frontier shift efficiency challenge.
- 4.16 Each of these issues has potential cross-company impacts and so are discussed in detail in the 'expenditure allowances – common issues', 'expenditure allowances – cost adjustment claims' and 'expenditure allowances – addressing asset health' documents.

**Table 4.2: Base expenditure allowances – key issues raised by Wessex Water**

Base expenditure area	Change to FD allowance (£m)	Ofwat response summary	Document reference
<b>Water base models</b>	244	<ul style="list-style-type: none"> <li>We engaged extensively with water companies when developing the econometric models used in our final determination.</li> <li>Wessex Water has previously expressed concerns with the models. But it did not propose alternative solutions or variables to mitigate these concerns. Nor did it provide evidence to rebut the chosen models, such as that submitted in its statement of case.</li> <li>We followed a rigorous and robust process to developing the econometric models, but we accept that no model is perfect.</li> <li>We encouraged companies to submit cost adjustment claims if they think the models do not capture their company specific factors. Wessex Water did not do so.</li> </ul>	Expenditure allowances – common issues – section 2 – wholesale water models
<b>Bioresources capital maintenance claim</b>	178	<ul style="list-style-type: none"> <li>Additional information is required to assess the need for a cost adjustment, and the cost efficiency of requested costs.</li> <li></li> </ul>	Expenditure allowances – cost adjustment claims – section 11
<b>Disinfection improvements</b>	47	<ul style="list-style-type: none"> <li>We agree the proposed investment is not funded through base expenditure allowances.</li> <li>But it is unclear why these proposed disinfection upgrades at water treatment works were not put forward as part of the established industry DWI PR24 programme.</li> <li>We suggest Wessex Water follows due process for the assessment of these needs and associated requirements by engaging with the DWI in the first instance and agreeing to appropriate legal instruments.</li> <li>If the investment is supported with legal instruments, and additional expenditure allowances are provided, it would be</li> </ul>	Expenditure allowances – cost adjustment claims – section 12

		important to hold the company to account through a price control deliverable.	
<b>Business rates</b>	16	<ul style="list-style-type: none"> <li>Companies have received new information since final determinations from the Valuation Office Agency. We have provided an updated assessment of business rates liabilities based on this new information.</li> <li>All companies should have received new information. We consider that whatever approach the CMA applies, it should apply to all disputing companies.</li> </ul>	Expenditure allowances – common issues – section 2 – unmodelled costs
<b>Total</b>	485		
<b>Other issues</b>			
<b>High-level approach to base cost assessment</b>		<ul style="list-style-type: none"> <li>We sought to build on and improve upon our PR19 approach to assessing base expenditure at PR24.</li> <li>We consider we delivered against this aim with the improvements to our econometric models, and the introduction of six forward looking sector-wide cost adjustments.</li> <li>Moving forward, we are open to considering alternative approaches to assessing base costs at future price reviews.</li> <li>This includes a more bottom-up assessment of costs. However, it is important that companies understand the extensive data and assurance requirements such an approach is likely to come with. We discuss this further in our 'expenditure allowances – addressing asset health' document.</li> </ul>	Expenditure allowances – addressing asset health at PR24
<b>Mains renewal adjustments/ PCD</b>		<ul style="list-style-type: none"> <li>We allowed the company an additional £23.3 million to increase main renewals and improve asset condition over the 2025–30 period.</li> <li>The company disagrees with our approach to determining what base buys but does not express its preferred approach. We consider it is most appropriate to use the historical period used to set base expenditure allowances so that customers do not pay twice.</li> <li>It is also appropriate to hold the company to account for undertaking these renewals, and delivering an improvement in condition, through a PCD.</li> </ul>	Expenditure allowances – common issues – section 2 – cost adjustment claims
<b>Frontier shift</b>		<ul style="list-style-type: none"> <li>We continue to consider a 1% per year frontier shift adjustment is appropriate,</li> </ul>	Expenditure allowances – common issues – section 6

		<p>rather than the 0.5% per year frontier shift challenge proposed by the company.</p> <ul style="list-style-type: none"> <li>• This is consistent with recent CMA and UK regulatory decisions on frontier shift and is in the middle of CEPA's recommended range of 0.8% to 1.2%.</li> <li>• That considers both pre and post financial crisis productivity growth and other relevant factors such as the most recent OBR productivity growth forecasts; embodied technical shift; and the step-change in investment over the 2025-30 period, which should facilitate a 'learning by doing' productivity effect.</li> </ul>	
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## Setting our enhancement allowances

- 4.17 Wessex Water was generally considered to be an inefficient company in terms of its enhancement costs. We allowed £2.0 billion at final determination, leaving the company with a negative cost gap at final determination of 18% or £463 million (post frontier shift). Wessex Water has reduced its costs further within its statement of case but still requests an additional £254 million over that allowed in the final determination.
- 4.18 This request entirely relates to phosphorus removal, where Wessex Water raises issues with the phosphorus removal benchmarking model, including specification, robustness and capture of all relevant factors. Following our final determinations, Wessex Water submitted a query to us which set out that five of its schemes have sufficiently strong engineering rationale and unique characteristics to be considered as engineering outliers. These five schemes are part of the 11 schemes Wessex Water has identified as having the largest cost gaps in its statement of case.<sup>49</sup> We assessed the new evidence presented in Wessex Water's statements of case for each of these schemes. Consistent with our response to its query,<sup>50</sup> we consider Wessex Water has not demonstrated unique circumstances relating to these schemes. We are confident that the models capture the key cost drivers, and the models are robust. Wessex Water also suggests that less weight should be placed on the historical models. We continue to consider that at least equal weight should be placed on historical models, as forecasts can be impacted by risk aversion and the pricing in of uncertainty.
- 4.19 We provide a more detailed response to this issue in our 'expenditure allowances – common issues' document, as it is a cross-cutting issue and could impact on other disputing companies.

<sup>49</sup> [OF-OA-004] Wessex Water, Statement of case, March 2025, pp. 267-271, Table A13-1.

<sup>50</sup> [OF-CA-090] Ofwat, Query response: OFW-FD-WSX-022\_Ofwat response, February 2025.



4.20 Wessex Water also asks the CMA to correct for an error on growth at sewage treatment works. We have previously confirmed to Wessex Water that this will be corrected as part of our blind year reconciliation process. As set out in our 'overview of our response to the statements of case' document, we would support the CMA deprioritising adjustments already agreed with companies to correct unambiguous errors in our final determinations.

**Table 4.3: Enhancement cost gaps (before the application of frontier shift and real price effects)**

Enhancement expenditure area	Company view (Feb 2024) (£m)	Company view (August 2024) (£m)	Final determination allowance (£m)	Cost gap at FD (£m)	Statement of case request (£m)	Cost gap to SoC (£m)
Water WINEP	44	42	38	-4	38	0
Supply/Demand balance and metering	153	161	133	-28	133	0
Resilience and security (w)	29	23	24	1	24	0
Water quality improvements	35	57	53	-4	53	0
Other water enhancement areas	8	5	0	-4	0	0
Total water enhancement allowance	269	288	249	-38	249	0
Storm overflows	514	571	580	9	580	0
Nutrients	1357	1,134	820	-315	1074	-254
Other WINEP (ww)	341	271	235	-36	235	0
Resilience and security (ww)	75	22	9	-13	9	0
Growth at sewage treatment works	130	176	122 <sup>51</sup>	-54	122	0
Industrial emissions directive	181	117	76	-41	76	0
Other enhancement areas (ww)	63	49	8	-41	8	0
Total wastewater enhancement allowance	2,660	2,340	1,851	-490	2,105	-254
Total enhancement allowance	2,929	2,328	2,100	-528	2,354	-254

<sup>51</sup> This represents the published final determinations allowance. Post final determinations corrections have determined that this figure should be increased by £46 million.

4.21 The following table provides additional navigation assistance for CMA. It sets out each of the key enhancement issues raised in Wessex Water's statement of case, a summary of our response, and the location of our more detailed response.

**Table 4.4: Key issues in setting enhancement allowances**

Enhancement expenditure area	Change to FD allowance (£m)	Ofwat response	Document
Phosphorus removal	254	This is an existing issue with new evidence. Wessex Water raises issues with the phosphorus removal benchmarking model, including specification, robustness and capture of all relevant factors. We are confident that the models capture the key cost drivers and the models are robust. The company also suggests that less weight should be placed on historical expenditure. We continue to consider that our phosphorus removal models are robust and reflect the most important engineering cost drivers. We continue to consider that at least equal weight should be placed on historical expenditure, as forecasts can be impacted by risk aversion and the pricing in of uncertainty.	Expenditure allowances – common issues – section 5

## Delivering outcomes for customers and the environment

4.22 Wessex Water does not include any issues relating to outcomes in its statement of case and explicitly accepts our use of deadbands, caps and collars for the suite of performance commitments (PCs). Wessex Water also accept in the round the PCLs and outcome delivery incentives (ODIs) for the measures of experience PCs (customer (C-MeX), developer (D-MeX) and business retail (BR-MeX)) in the round.

4.23 We consider that Wessex Water has not highlighted any specific concerns with the PCLs as it is confident of outperforming them over the 2025-30 period. The performance commitment forecasts that Wessex Water included in its February 2024 business plan we considered were unambitious. These were replaced in its representation on our draft determination by slightly more ambitious targets, although these would still see the company's performance fall to the middle of the pack on most measures, and even to the lower quartile on some.

4.24 While the company disagrees with the high-level approach to setting ODI rates and a number of PCLs, these do not feature within the statement of case, although it does indicate it is happy to provide additional information on these topics at a later date.

## Aligning risk and return

4.25 We consider the issues raised by Wessex Water around risk and return should be considered thematically. Therefore, we address all the issues below are in our 'risk and return – common issues' document.

**Table 4.5: Key issues in risk and return**

Point in Wessex Water's statement of case	Statement of case (SoC) reference	For Ofwat's response, see:
<b>Allowed return</b>	2.43 onwards Chapter 10	Section 4 of Risk and return – common issues
<b>Bill impact</b>	2.53 onwards	Section 7 of Risk and return – common issues

## Affordability

**Table 4.6 Wessex Water average household bills, 2024–30 (£)**

Wessex Water	2024–25	2025–26	2026–27	2027–28	2028–29	2029–30	5yr avg.
<b>Final determination</b>	508	575	585	594	603	614	594
<b>Statement of case</b>	508	575*	645*	658*	658*	658*	639

4.26 As shown in Table 4.6, average bills have risen considerably in Wessex Water's statement of case compared to our final determination, with the 5-year average bill being £44 higher under the statement of case compared to the final determination. The company provided a line graph in its submission, from which we have manually estimated average bill figures in Table 4.6.<sup>52</sup>

4.27 Wessex Water also states that, should the CMA adopt all requests in the statement of case, the bill increase would be 38%, but request that this is capped at 30% using financial levers.<sup>53</sup>

<sup>52</sup> [OF-OA-004] Wessex Water, Statement of Case, March 2025, p. 12, Figure 1.

<sup>53</sup> [OF-OA-004] Wessex Water, Statement of Case, March 2025, p. 12, para 2.55.

## 5. Areas for deprioritisation

- 5.1 In its statement of case, Wessex Water states that 'we consider it appropriate not to focus our Statement of Case on these areas', setting out a list that includes: base costs – wholesale wastewater, some enhancement expenditure allowances (growth at sewage treatment works, IED, leakage, supply side schemes, resilience), retail costs, PCLs and ODIs, price control deliverables (except for PCDs on base expenditure), the delayed delivery cashflow mechanism, the scope of uncertainty, and 'downside skew in the overall RoRE range'.<sup>54</sup>
- 5.2 It also sets out 'areas we are willing to accept in the round'. This includes enhancement cost deep dive and shallow dive approaches, costs sharing rates, use of deadbands, caps and collars within the outcomes framework, and the measures of experience.<sup>55</sup>
- 5.3 In response to the CMA's request, we have suggested in our 'overview of our response to the statements of case' document that the CMA could deprioritise redetermination of a number of the PR24 price review building blocks.<sup>56</sup> We include the retail price control and the PCLs and ODIs for the total pollution incidents PC.
- 5.4 As such, we do not agree with some of the suggestions made by Wessex Water for deprioritisation from the CMA redetermination process. We reflect that both the PR24 price review process itself and the redetermination process undertaken by the CMA feature significant asymmetries, as discussed in the 'overview of our response to the statements of case' document, including a likelihood that companies have not proposed areas for redetermination where the potential outcome could lead to a less 'favourable' outcome.

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<sup>54</sup> [OF-OA-004] Wessex Water, Statement of Case, March 2025, p. 12, para 2.45, Table 1.

<sup>55</sup> [OF-OA-004] Wessex Water, Statement of Case, March 2025, p. 14, para 2.48, Table 2.

<sup>56</sup> Ofwat, 'PR24 redetermination – Overview of our response to the statements of case', April 2025, section 5.

## A1 Appendix 1: Key financial metrics

A1.1 The main body of this document sets out the key interventions that we made to Wessex Water's business plan. This appendix provides further detail of the calculation of the final determination, where we made a number of interventions to Wessex Water's business plan and/or draft determination representation position. Further detail on the interventions are set out in our documentation.

**Table A1.1: Key financial metrics**

	Draft determination	Company view (August 2024 representation)	Final determination
Average bill (2025-30) £	499.96	634.09	594.21
Average bill growth (%)	-2	31	21
Allowed return (%)	3.72	4.58	4.03
RCV Growth (%)	34.5	50.3	35.9
Dividend yield (%)	2	2.1	4.1
ACICR simple (ratio)	1.75	1.88	1.73
ACICR weighted (ratio)	1.73	1.70	1.73
FFO/net debt simple (%)	9.7	9.6	9.9
FFO/Net debt weighted (%)	9.6	8.3	9.8
Run off rate (%)	3.76	3.88	3.85
Post financeability revenue adj (£m)	24.2	36.6	35.0

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