

April 2025

PR24 redeterminations

# **Response to South East Water's statement of case**

## **PR24 redeterminations- response to South East 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 South East Water's statement of case.
- 1.2 Many of the points raised by South East 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 South East Water, from our regulatory perspective, then sets out a summary of our PR24 final determination.
- 1.4 If we consider that a point raised by South East 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 final 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.
- 1.5 Our summary of the PR24 final determination for South East Water, and the remainder of this document, and the suite of documents comprising our response to the five statements of case, are generally structured around the building blocks of the price review: expenditure allowances; outcomes; and risk and return.

**Table 1.1 Navigation assistance**

Point in South East Water's statement of case	Statement of case (SoC) reference	For Ofwat's response see
Base cost models	1.17a Table 1.1 4.9 onwards	Expenditure allowances – common issues- Section 2 – Wholesale water base models
Cost adjustment claims	1.17a Table 1.1	Expenditure allowances – common issues- Section 13- cost adjustment claims
Frontier shift	Table 1.1 4.83 onwards	Expenditure allowances – common issues -Section 6 – Frontier Shift
Mains renewals	1.17a 4.27a onwards	Expenditure allowances – common issues -Section 2 – Base expenditure allowances-



Point in South East Water's statement of case	Statement of case (SoC) reference	For Ofwat's response see
		subsection- Water main renewal costs adjustment
Metering	1.17a 4.27b	Expenditure allowances – common issues -Section 2 – Base expenditure allowances- subsection- Meter replacement
Water treatment works-level economies of scale	4.33a	Expenditure allowances – common issues- Section 13- cost adjustment claims
Network reinforcement	1.17a 4.33b	Expenditure allowances – common issues- Section 2 – catch-up efficiency challenge- subsection- Network reinforcement
Price control deliverables (PCDs)	1.11a 1.17a and b 4.14c 4.39 4.44 4.81	Expenditure allowances – common issues- Section 7 – Price control deliverables
Bowl water treatment works	1.17b Table 4.2 4.75a	This document – section- setting our enhancement allowance- subsection- Bowl water treatment works- Table 4.4, paragraph 4.66 onwards
Service reservoir upgrades	1.17b Table 4.2 4.76b	This document – section- setting our enhancement allowance- subsection -Service Reservoir capacity increases- Table 4.4 and paragraph 4.83 onwards
Southern Water water treatment works upgrade	Table 4.2 4.76c	This document – section- setting our enhancement allowance- subsection- Southern Water Treatment Works Upgrade (River Medway Scheme)- Table 4.4 and paragraph 4.90 onwards
Smart network	1.17b 4.80 Table 4.2	This document – section- setting our enhancement allowance- subsection- Smart Networks – Table 4.4, paragraph 4.22 and 4.39 onwards
Leakage	1.17b 4.76a	Expenditure allowances – common issues -Section 4 –

Point in South East Water's statement of case	Statement of case (SoC) reference	For Ofwat's response see
		Water enhancement expenditure allowances
Water efficiency	1.17b 4.76d	Expenditure allowances- common issues -Section 4- water enhancement expenditure allowances Demand (water efficiency)
Resilience interconnectors	1.17b Table 4.2 4.79	This document – section- setting our enhancement allowance- subsection- Resilience interconnectors – Table 4.4, paragraph 4.21 and 4.99 onwards
Cyber	Table 4.2 4.76f	This document – section- setting our enhancement allowance- subsection subsection –Cyber – Table 4.4, paragraph 4.190 onwards
SEMD	1.17b Table 4.2 4.76g	This document – section- setting our enhancement allowance- subsection –SEMD- Table 4.4, paragraph 4.21 and 4.156 onwards
WINEP – Raw water deterioration	Table 4.2 4.75d	Expenditure allowances – common issues- Section 4- Raw Water Deterioration- Nitrate This document- section- setting our enhancement allowance – subsection Raw Water deterioration – Table 4.4, paragraph 4.29 and 4.174 onwards
WINEP – Investigations	Table 4.2 4.76e	Expenditure allowances – common issues – Section 4 – WINEP water investigations
WINEP – Drinking water protected areas	Table 4.2 4.76h	This document – section- setting our enhancement allowance- subsection WINEP – Drinking water protected areas – Table 4.4, paragraph 4.18 and 4.197 onwards
Net zero	Table 4.2 4.75c	Expenditure allowances – common issues – Section 4 – Net Zero
Leakage – Other leakage activity	Table 4.2	Expenditure allowances – common issues – Section 4 – Water enhancement expenditure allowances

Point in South East Water's statement of case	Statement of case (SoC) reference	For Ofwat's response see
		This document – section- setting our enhancement allowance- subsection Smart Networks- Table 4.4, paragraph 4.19 and 4.41 onwards
Leakage – deep dive costs reallocated from Smart networks	Table 4.2 4.75e	This document – section- setting our enhancement allowance- subsection – Other companies delivered smart network improvements through base- Table 4.4, paragraph 4.19 and 4.52 onwards
Demand (Water efficiency initiatives)	Table 4.2	Expenditure allowances- common issues- Section 4- water enhancement expenditure allowances Demand (water efficiency)
Lead	Table 4.2 4.75b	This document – subsection Lead
Contingent allowance	1.11a 4.6d 4.37 4.47 onwards	This document – section- setting our enhancement allowance- subsection £50 million contingent resilience allowance- Table 4.4 and paragraph 4.124 onwards
Water supply interruptions PCL	1.20a 5.4a 5.11 onwards	PR24 redeterminations – outcomes – common issues, pp.21-25 (s.2)  This document –section- Delivering outcomes for customers and the environment – subsection Delivering outcomes for customers and the environment, Water Supply Interruptions- Table 4.10 and paragraph 4.215 onwards
Water supply interruptions collar	1.20a 5.4a 5.33 onwards	This document- section Delivering outcomes for customers and the environment- subsection- Water Supply Interruptions- Table 4.10 and paragraph 4.215 onwards
ODI regime	4.17 5.3a onwards	PR24 redeterminations Outcomes – common issues, pp. 26-33 (s.3)

Point in South East Water's statement of case	Statement of case (SoC) reference	For Ofwat's response see
C-MeX	1.20b 5.4b 5.39 onwards	This document – section Delivering outcomes for customers and the environment – subsection Delivering outcomes for customers and the environment, C-Mex- Table 4.10 and paragraph 4.209 onwards
PR19 penalty – non-household voids	1.21 5,10	This document- section Delivering outcomes for customers and the environment- subsection- Business voids performance commitments- Table 4.10 and paragraph 4.259 onwards
Imbalance in Ofwat's package	1.11c 6 7.33	Risk and return – common issues- Section 1- Balance of Risk- subsection- Overall Balance
Financial risk	1.11c onwards 1.12e onwards	Risk and return – common issues-Section 1-Balance of risk- subsection- Finance risk
Notional company	1.26 onwards 7.11 onwards Table 7.1 7.15	Risk and return – common issues- Section 3- Allowed return on Cost of debt- subsection- Embedded Cost of Debt
Cost of equity	1.23 6.12 onwards	Risk and return – common issues- Section 4- Allowed return on Equity- subsection- Equity beta
Cost of equity – aim up	Table 1.1	Risk and return – common issues- Section 4 -Allowed return on Equity- subsection- Choosing a point estimate
Cost of debt	1.24 6.32 onwards	Risk and return – common issues- Section 3- Allowed return on cost of debt- subsection- Embedded Cost of Debt
Cost of debt – company specific adjustment	1.24	Risk and return – common issues- Section 6- Company specific adjustments (SEW) This document- Section 4- Aligning Risk and return – common issues- subsection-

Point in South East Water's statement of case	Statement of case (SoC) reference	For Ofwat's response see
		Cost of debt company specific adjustment
Allowed return	7.1 onwards	Risk and return – common issues– Section 4– Allowed Return on Equity– subsection– Allowed Return and Total Market Equity
Aggregate sharing mechanism (ASM)	1.28	Risk and return – common issues– section 1 – Balance of Risk– subsection–Aggregate sharing mechanism and Calibrating the risk and return package for PR24
Outturn adjustment mechanism (OAM)	1.28	Risk and return – common issues– section 1 – Balance of Risk– subsection –Outturn Adjustment Mechanism

## 2. Introduction

- 2.1 South East Water is a water undertaker. It supplies water services to 2.3 million customers in the South East of England. South East Water Limited is the main operating company and is a wholly owned subsidiary of South East Water (Holdings) Limited. South East Water (Finance) Ltd is registered in the Cayman Islands and holds most of the debt raised by the Group. The company is owned by a consortium of investors comprising Utilities of Australia PTY Limited (as trustee of utilities trust of Australia) (50%– Australia), three entities of Desjardins cooperative financial group (25%– Quebec); Régime de rentes du Mouvement Desjardins (12.5%), Desjardins Financial Security Life Assurance Company (6.25%) and Certas Home and Auto Insurance Company (6.25%) and Natwest Pension Trustee Limited as trustee for the NatWest Group Pension Fund (25%– England).
- 2.2 In the latest Water company performance report 2023–2024, we categorise South East Water's performance as 'average'.<sup>1</sup> The company met the performance targets for four of the eight key performance indicators for water-only companies. During the PR19 period, we categorised the company's performance as 'average' in two years and 'lagging behind' in two years.
- 2.3 In our most recent Monitoring financial resilience report,<sup>2</sup> we categorised South East Water as 'Action Required', as we did in the previous year. This means company action is being taken or is required, and/or commitments have been made to strengthen long term financial resilience. In the report we set out that South East Water reported year-end regulatory gearing of 77.8% and ongoing financial pressures driven by factors including, impacts of its performance and operational challenges, additional capital expenditure and higher interest costs. On 13 November 2024 Moody's credit rating was downgraded to Baa3 (on review for downgrade), being the minimum for investment grade. Consequently, the company is now in cash lock-up under its licence and unable to pay a dividend without Ofwat's approval.
- 2.4 In November 2023 we opened an enforcement case investigating whether South East Water has failed to develop and maintain an efficient water supply system.<sup>3</sup> This relates to South East Water's poor performance on water supply interruptions, where the company was the worst performer in England and Wales in 2022–23 with an average interruption per household of 3 hours, 2 minutes and 21 seconds lost per property compared with its performance commitment level of 5 minutes and 45 seconds.
- 2.5 We assessed the business plan it submitted in October 2023 against our quality and ambition assessment. At draft determination we considered South East Water's plan as

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<sup>1</sup> [OF-OU-017] Ofwat, Water company performance report 23–24, October 2024, slide 8.

<sup>2</sup> [OF-OAA-003] Ofwat, Monitoring financial resilience 2023–24, p.7.

<sup>3</sup> [OF-SEW-007] Ofwat, Enforcement case into South East Water's supply resilience, November 2023.



'lacking ambition'.<sup>4</sup> Whilst the company's plan met our minimum quality expectations, it demonstrated a poor level of ambition in the round. As a result we set a financial penalty to South East Water that would apply if it did not provide an improved plan by final determinations. We set out to the company specific conditions to improve its plan. At final determinations, we determined that South East Water had made progress against all conditions set out and moved its plan out of the lacking ambition category.<sup>5</sup> To recognise the improvements made by the company since draft determination we did not apply a financial penalty at final determination, As set out in the Quality and ambition assessment chapter of our PR24 final methodology, the company was not eligible for a reward.<sup>6</sup> Whilst we still had some outstanding concerns across two conditions, we considered that these could be addressed outside of the quality and ambition assessment.

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<sup>4</sup> [OF-SEW-008] Ofwat, 'PR24 draft determinations: South East Water- Quality and ambition assessment appendix', July 2024.

<sup>5</sup> [OF-SEW-008] Ofwat, 'PR24 draft determinations- South East Water Quality and ambition assessment appendix', July 2024, p.2.

<sup>6</sup> [OF-OU-002] Ofwat, 'Creating tomorrow, together: Our final methodology for PR24', December 2022, p.150.

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

- 3.1 We summarise below what was included in our final determination in each of the three main building blocks of the price review: expenditure allowances, outcomes and risk and return and provide more information on the key issues that arose between us and South East Water during the PR24 process.
- 3.2 The following table sets out the key metrics included in South East Water's February 2024 PR24 business plan submission to Ofwat, 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)	1,995	1,373	2,104	1,821
PAYG rate (%)	43.38	49.1	43.38	46.3
Allowed return (%)	4.45	3.72	4.86	4.03
RCV run-off rate (%)		3.82	3.82	3.82
Allowed revenue, 2025– 2030 (£million)	1,662	1,462	1,782	1,679
Average bill per household customer, 2025–2030 (£)	273	241	291	274

### Expenditure allowances

- 3.4 In our final determination we allowed South East Water a total expenditure (totex) allowance of £1.8 billion (after frontier shift/ RPEs) for the period 2025–30. This is a 56% increase over its PR19 allowance (£1.1 billion) reflecting the step change across the sector. South East Water requested an 80% increase in its totex allowance relative to PR19 levels. We increased its wholesale costs allowances by £448 million between the



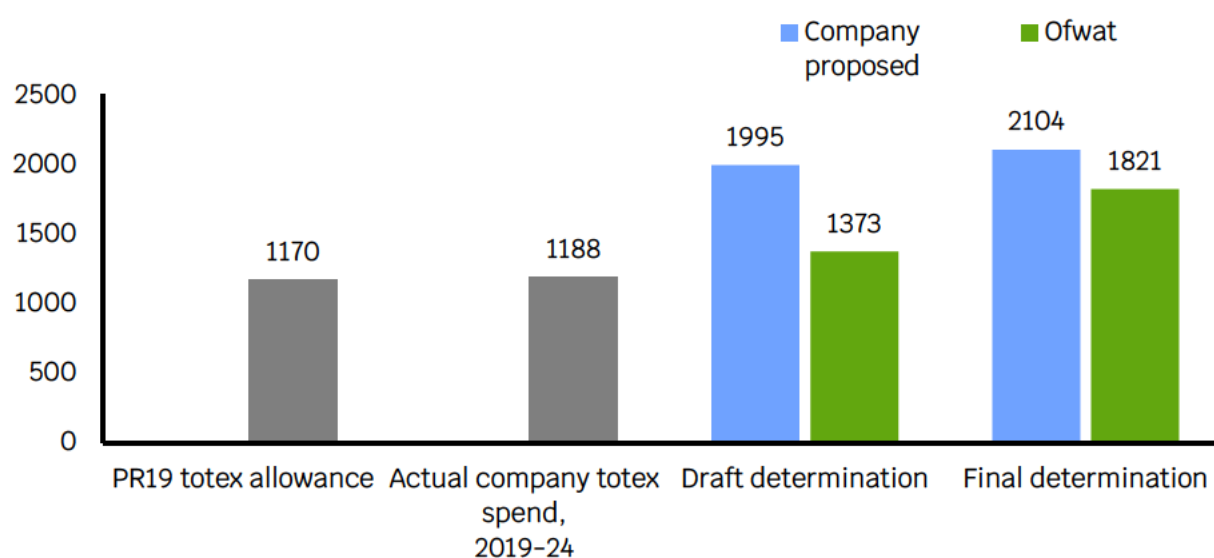
draft and final determination stages. However, we did not find the company's evidence to be sufficient and convincing to justify all of the upwards adjustments that it proposed. As shown in table 3.2, overall, cost gaps reduced from 12% to 7% for base expenditure and from 64% to 26% for enhancement expenditure between our draft and final determinations.

**Table 3.2: Final determination total expenditure allowances and previous stages of PR24 for South East Water £m (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 (£m)	FD (£m)	FD vs Rep (%)	FD vs Rep (£m)
Overall expenditure	1,170	1,995	1,373	2,104	1,821	-13	-282
Base expenditure	978	1,256	1,108	1,343	1,255	-7	-88
Enhancement expenditure	192	738	265	761	566	-26	-194

3.5 In the following chart, 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 South East Water £m (2022-23 prices)**



3.6 As part of its representation to our draft determination, South East Water proposed an increase in its totex to £2.1 billion. This included an £87 million increase in base expenditure, across business rates, cost adjustment claims and developer services cost requests. A further £23 million increase in enhancement expenditure was requested across water quality. By the time of the final determination in December 2024, we had

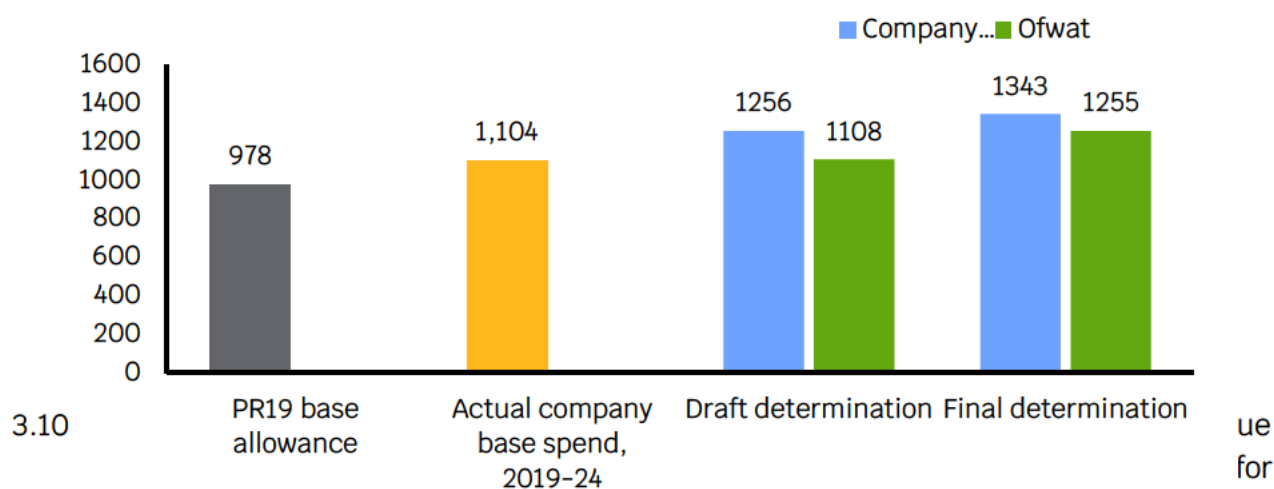
carried out further work to evaluate the robustness of our modelling results: South East Water's proposed expenditure remained 13% above what we consider to be its efficient costs as shown in table 3.2.

- 3.7 We consider that South East Water's final determination 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. Although challenging, we consider that the significant increase in allowance provided to South East Water compared with the current period, across base expenditure (28%, £276 million) and enhancement expenditure (195%, £569 million) provides sufficient funding for the company to meet the targets set in the round. We do not expect a company to meet all targets, however we consider that there are operational issues that South East Water must work through and provide a £228 million resilience allowance for the company.
- 3.8 Our PR24 final determination expenditure allowance is 13% below the £2.1 billion requested by the company in its August 2024 representation on the draft determination. This overall cost gap of £283 million is the second largest in percentage terms across the industry. South East Water has overspent its PR19 totex allowance by 16% between 2020–2024. It has underspent its PR19 enhancement expenditure allowance by 7% (£12 million).

## Base expenditure

- 3.9 Our final determination allowed South East Water £1.3 billion of base expenditure, as shown in table 3.2. This was an uplift of 13% (£147 million) from our draft determination. In February 2024, it submitted an amended business plan that included uplifts to its base expenditure request, specifically on business rates where it increased its request from £86.1 million to £91.5 million.

**Figure 3.2: Overview of base allowances for South East Water £m (2022–23 prices)**



network reinforcement expenditure, increasing the amount from £31 million to £44.5 million: it considered that our base model includes new activity via base cost model drivers that relate to "the provision to new customers of the current service level", not accounting for the higher rate of growth fully.<sup>7</sup> It considered that it should have received a network reinforcement cost adjustment on treatment work size given Thames Water and Southern Water received this adjustment and South East Water has sustained as high a rate of growth as Thames Water.<sup>8</sup> In our final determination we partially accepted this claim and provided the company with £32.2 million through the sector wide network reinforcement cost adjustment to support economic growth and new housing.<sup>9</sup> This allowance is £1.2 million higher than requested by South East Water in its October 2023 business plan.

- 3.11 In its representation the company decreased its request for an Economies of scale at water treatment works cost adjustment claim from £26.9 million to £25.1 million. In our final determination we partially accepted the company's claim and applied a £14.3 million cost adjustment. We applied this adjustment based on an alternative water base cost model that included economies of scale at water treatment works.<sup>10</sup>
- 3.12 In its representation on our draft determination, South East Water also set out different views on various sector wide adjustments including mains renewals, metering and net zero as they considered these gave allowances lower than required to meet output targets. The company also raised concern with the reallocation of costs from enhancement to base expenditure allowances, considering that historical cost and cost driver relationships may not adequately represent future needs and will leave the company underfunded across its enhancement cases. We maintained our approach from draft determination to final determination. We specifically reallocated costs from enhancement to base as the company failed to provide sufficient and convincing evidence to demonstrate their eligibility for enhancement allowances through a step change to a new, improved level of service. Nor did the company demonstrate that the proposed investment went beyond what we would reasonably expect a company to be doing already through its base expenditure allowance.
- 3.13 At representation South East Water broadly accepted our approach towards unmodelled costs: the company proposed that efficiencies should not be applied to these costs and increased its forecast of business rates.<sup>11</sup> Our final determination increased expenditure allowances versus draft determination: on energy we allowed £29 million versus £5.7 million at draft determination and on business rates £105 million versus £83.5 million at

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<sup>7</sup> [OF-SEW-009] South East Water, 'PR24 Draft Determination Response Executive Summary' (southeastwater.co.uk), August 2024, p.21.

<sup>8</sup> [OF-SEW-009] South East Water, 'PR24 Draft Determination Response Executive Summary' (southeastwater.co.uk), August 2024, p.21.

<sup>9</sup> [OF-OA-022] Ofwat, 'PR24\_final\_determinations: Expenditure allowances', December 2024, p.56.

<sup>10</sup> [OF-OA-022] Ofwat, 'PR24 final determination: Expenditure allowances', December 2024, pp.379–380.

<sup>11</sup> [OF-SEW-009] South East Water, 'PR24 Draft Determination Response Executive Summary' (southeastwater.co.uk), August 2024, p.22.

draft determination. We consider these allowances are appropriate and have taken into account increases in energy costs and supply chain costs from across the sector.

- 3.14 South East Water proposed alternative approaches to the sector wide adjustment on mains renewals throughout the price review process. We provided the company with a £29.3 million adjustment on mains renewals: we considered that the mains renewal rate provided at final determination (0.50%) will drive the company to deliver renewals and target improving its below average assets and increase asset health over the 2025-30 period by targeting condition grade 4 and 5 mains.<sup>12</sup> Within its representation the company considered that base expenditure allowances have not been enough to prevent deterioration in asset condition.<sup>13</sup> We do not agree with this as capital maintenance within base expenditure has increased by 3% per year in real terms since privatisation.<sup>14</sup>
- 3.15 At final determination, we set a frontier shift of 1%. South East Water requested 0.5% in its representation. We expect companies to innovate and take advantage of new technologies to become more cost efficient. We explain our rationale for the 1% frontier shift in 'PR24 final determinations: expenditure allowances'.<sup>15</sup>

## Enhancement expenditure

- 3.16 In the figure below we show South East Water's Water enhancement expenditure request in its February 2024 business plans and Ofwat's draft determination; and we show South East Water's proposed request within its representation to the draft determination and Ofwat's allowance at final determination.

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<sup>12</sup> [OF-OA-022] Ofwat, 'PR24 final determination: Expenditure allowances', December 2024, p.39.

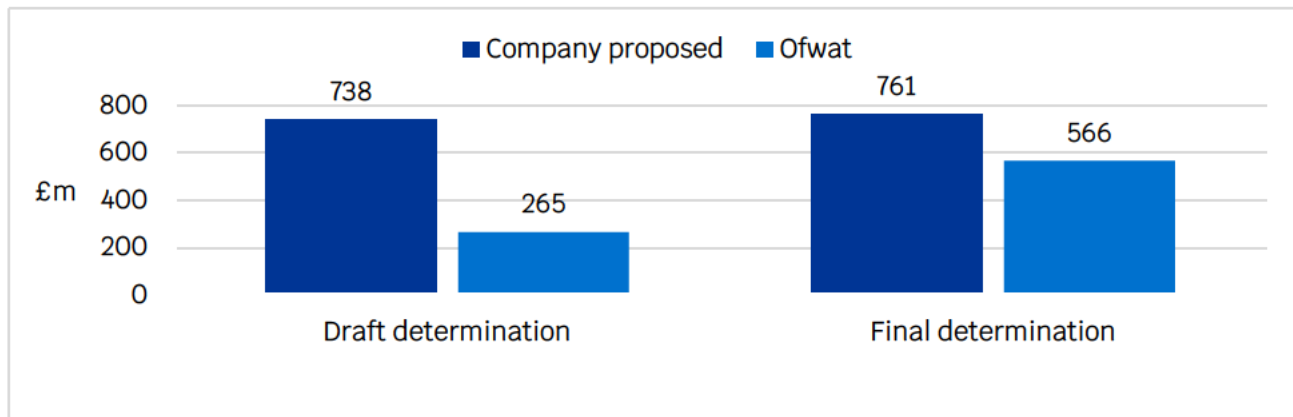
<sup>13</sup> [OF-SEW-009] South East Water, 'PR24 Draft Determination Response Executive Summary' (southeastwater.co.uk), August 2024, p.17.

<sup>14</sup> [OF-OA-022] Ofwat, 'PR24 final determination: Expenditure allowances', December 2024, p.83.

<sup>15</sup> [OF-OA-022] Ofwat, 'PR24 final determinations: expenditure allowances', December 2024, pp 261-268.



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



- 3.17 Our final determination allowed South East Water a water enhancement allowance of £566 million. This was 26% (£194 million) lower than South East Water's request in its representation to our draft determination. This negative cost gap has reduced significantly from our draft determination (£301 million gap), as we provide further allowances across: resilience, supply-demand balance, investigations, strategic resource options, metering, raw water deterioration and interconnectors. We use our judgement to give the company a higher allowance than requested because of the improved evidence put forward by the company which demonstrated a need for an increased allowance.
- 3.18 South East Water submitted an updated plan in February 2024. This contained a reduced request by £58 million for capital expenditure on major developments including construction and enhancement of infrastructure. This decrease is as a result of updated costs across projects and initiatives.<sup>16</sup>
- 3.19 Within its representation to our draft determination South East Water included a revised whole life cost proposal for delivering Broad Oak Reservoir (£362 million in the October 2023 plan and £1.1 billion in August 2024). It considered that this brings the cost in line with the industry and the lifespan of a reservoir.<sup>17</sup>
- 3.20 In November 2024 the company submitted a further enhancement request of £9 million for its PFAS programme. As part of our final determination, we include a notified item and propose to include PFAS in a cost change process with the possibility of in-period adjustments to price controls and an end of period reconciliation. We refer the CMA to our final determination for further details of the PFAS Uncertainty Mechanism.<sup>18</sup> Our assessment of the company's request of an additional £9 million for its PFAS

<sup>16</sup> [OF-SEW-010] South East Water, 'Latest information on our PR24 business plan', March 2024.

<sup>17</sup> [OF-SEW-009] South East Water, 'PR24 Draft Determination Response Executive Summary', August 2024, p.23.

<sup>18</sup> [OF-OA-022] Ofwat, 'PR24 Final Determinations: Expenditure Allowances', December 2024, p.208.

programme can be found under 'Raw Water Deterioration – PFAS' later in this document. As recommended within our PR24 redetermination- overview of our response to the statements of case document, we would support the CMA deprioritising expenditure allowances associated with PFAS that would be eligible for our cost change process.<sup>19</sup>

- 3.21 Our final determination provides £566 million enhancement expenditure allowances for South East Water's proposed £761 million enhancement programme. This is three times the size of its PR19 £192 million enhancement allowance. The largest components of the cost gaps relate to resilience, leakage and demand. At final determination we applied a cost efficiency challenge to South East Water's proposals where we concluded that South East Water had considered limited options and had not provided sufficient and convincing evidence that its higher costs were efficient.
- 3.22 In addition to its enhancement allowance, our final determination introduced an additional £50 million contingent allowance for the company to use through the 2025–30 period to improve its resilience subject to certain requirements. We considered this to be the most appropriate approach as we recognised that the company may require additional investment during the 2025–30 period and provide supportive evidence within the 'setting our enhancement allowances' section of this document.<sup>20</sup>
- 3.23 We introduced price control deliverables (PCDs) to hold companies to account for the outputs and outcomes that they propose to deliver and to return money to customers if companies do not deliver these in full. Our final determination includes 19 PCDs for South East Water.

## Delivering outcomes for customers and the environment

- 3.24 South East Water's final determination included targets that we consider are both achievable and stretching. We further support this through incentives that link

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<sup>19</sup> Ofwat, PR24 redeterminations – overview of our response to the statements of case, (Ofwat.gov.uk), April 2025, p.29.

<sup>20</sup> [OF-OA-022] Ofwat, PR24 Final determination: Expenditure allowances, December 2024, p.224.

performance with financial returns and improve its reputational standing, so customers receive an uninterrupted service.

- 3.25 In our latest Water company performance report 2023–24, South East Water was categorised as 'average' and did not achieve top performance categorisation across any areas of service delivery.<sup>21</sup> South East Water did not meet its leakage target in 2023–24 and had a poorer performance than in the previous year (2022–23), whilst six companies did meet the target performance commitment level in 2023–24. On water supply interruptions, South East Water remains one of the worst performers across the sector. Four companies met the water supply interruptions performance commitment level throughout the period in 2023–24.<sup>22</sup> Through our ongoing enforcement case, we continue to challenge South East Water to improve its supply resilience and minimise supply interruptions to its customers. As mentioned above, overall, the company has underspent its enhancement allowance during the 2020–24 period by 7% (£11 million).<sup>23</sup>
- 3.26 We assessed that, should South East Water achieve its forecasted performance commitments as submitted in its representation on our draft determination, the company would stand to earn a net outperformance payment over 2025–30 of £3.2 million.<sup>24</sup> We consider the final determinations outcomes package to be a fair bet. and that
- 3.27 We consider the company's proposed performance commitment levels were of low to moderate ambition and do not go far enough in some cases to fully support views proposed by customers of uninterrupted service, improved water security and resilience across its region. Within its representation to our draft determination the targets proposed by South East Water across water supply interruptions, per capita consumption, repairs to burst mains and biodiversity remained among the lowest across the sector.
- 3.28 In South East Water's representation to our draft determination, it raised concerns with the common performance commitment level on water supply interruptions and the company specific collar. Our final determination set a common level of 5 minutes per property. The company proposed a performance commitment level of 10 minutes and 15 seconds per property. We consider that alongside the enhancement expenditure provided to South East Water, this target, although stretching, is achievable and necessary so that customers are able to receive an uninterrupted service.
- 3.29 The overall outcomes package for South East Water provides it with an opportunity to outperform but also improve on its current performance, as mentioned above. We

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<sup>21</sup> [OF-OU-017] Ofwat, 'Water company performance report 2023–24', (Ofwat.gov.uk), October 2024, p.6.

<sup>22</sup> [OF-OU-017] Ofwat, 'Water company performance report 2023–24', (Ofwat.gov.uk), October 2024, p.30.

<sup>23</sup> [OF-OU-017] Ofwat, 'Water company performance report 2023–24', (Ofwat.gov.uk), October 2024, p.33.

<sup>24</sup> [OF-OU-077] Ofwat, PR24-FD-OC36-ODI-payment-calculator-with-performance-forecasts-v2.xlsx, January 2025.

reiterate that common performance commitment levels are set at a level that we expect an efficient company to deliver for its customers and the environment.

- 3.30 Our final determination includes protections for the company from the impact of extreme underperformance. We applied underperformance deadbands for all companies across the ten common performance commitments. For South East Water our final determination set a wider collar on its water supply interruptions (-2% RoRE) compared to the rest of the sector (-1% RoRE), as a result of the company's historical poor performance. This collar was set to incentivise the company to make the improvements that we expect of it: further detail on our decision is provided within our final determination.<sup>25</sup>

## Aligning risk and return

### Risk and Return

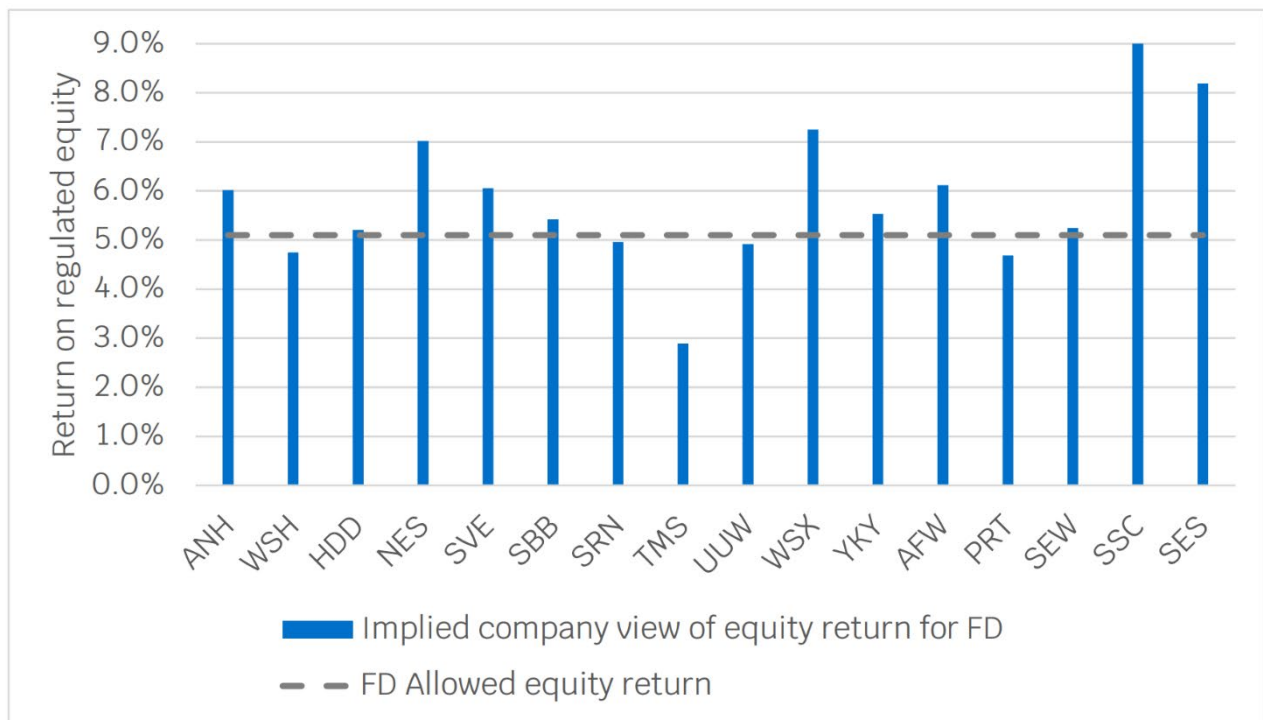
- 3.31 We consider that our final determination for South East Water provided a reasonable balance of risk and return.
- 3.32 To illustrate, we have adjusted South East Water's central view of outturn equity returns set out in its representation to reflect changes in our final determination. These include 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 5.2% for South East Water. As shown in figure 3.5 below this is in line with the base equity return. This analysis excludes other changes made to the risk package since draft determinations, including changes to how we apply 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.

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<sup>25</sup> [OF-OA-017] Ofwat, 'PR24 final determinations: Delivering outcomes for customers and the environment', February 2025, p.87.



**Figure 3.4: Indicative company view of regulated equity returns under the final determinations.<sup>26</sup>**



3.33 We assessed that South East Water's overall balance of incentives was skewed slightly to the upside at -4.8% to +5.1%.

3.34 In South East Water's October 2023 business plan it used its own view of the allowed return of 4.45%. This was amongst the highest across the sector and considerably higher than the allowed return set out in our PR24 final methodology (3.29%). We did not consider that South East Water provided sufficient and convincing evidence as to why its position on the allowed return would be reasonable.

3.35 We increased our allowed return at draft determinations from 3.29% to 3.72% (real, CPIH). This reflected increases in the cost of finance, as well as our decision to apply an allowed return on equity that was towards the upper end of our range. South East Water's representation on our draft determination argued for a higher allowed return range of 4.19% to 4.82%. In response to a query on the WACC<sup>27</sup> underpinning its proposed bills profile it argued for a higher range of 4.53% to 5.20% (reflecting its view of required correction for asymmetric risk and CSA), with a midpoint of 4.86%. This

<sup>26</sup> [OF-OA-019] Ofwat, 'PR24 final determinations: Aligning risk and return – appendix', December 2024.

<sup>27</sup> [OF-SEW-011] OFW-PR24 – Query response – OFW-REP-SEW-075 .msg – All Documents.

range and point estimate are both higher than our final determination figure of (4.03%).<sup>28</sup>

- 3.36 Our final determination did not accept South East Water's request for a company-specific adjustment (CSA) to its overall cost of debt of 30bps, to reflect its view that it faced structurally higher debt costs due to being an infrequent issuer of debt. We expected high quality and compelling evidence from the company that its proposed uplift reflected higher costs due to its small size, and that its evidence showed customers supported funding the cost of this uplift through higher bills. We judged that the company did not satisfy either of these criteria. Further detail on our decision is provided within our Aligning risk and return appendix of the final determination.<sup>29</sup>

## Financeability

- 3.37 Our final determination assessed that South East Water's final determination was financeable on the basis of the notional company, and that it will be able to raise the necessary levels of debt and equity to deliver the required investment.
- 3.38 To support financeability and to maintain a reasonable gearing level, our final determination included an equity injection for South East Water of £132 million, and we allowed £3.2 million for issuance costs. We allowed for dividends of £191 million (4% yield).<sup>30</sup> The financial ratios under our final determination are consistent with the target credit rating for the notional company. Post financeability revenue provides further headroom in financial metrics.

## Actual company structure

- 3.39 South East Water reported gearing of 77.8% at 31 March 2024. South East Water's business plan stated a target credit rating of Baa2/BBB for the actual structure which is below the notional target set in our decision. The business plan included a proposed £55 million fresh equity injection, a dividend yield of 1.2% and gearing of 74.5% in 2030.
- 3.40 In its representation to our draft determination, South East Water was required to provide additional board assurance and a financial resilience plan, with evidence of investor support to demonstrate how it will take forward its responsibility to maintain financial resilience.<sup>31</sup> In its representation South East Water proposed £75-125 million in

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<sup>28</sup> [OF-OA-019] Ofwat, 'PR24 final determinations: Aligning risk and return', December, 2024.

<sup>29</sup> [OF-OA-021] Ofwat, 'PR24 final determinations: Aligning risk and return- allowed return appendix' (ofwat.gov.uk), December, 2024, pp.106-111.

<sup>30</sup> [OF-OA-020] Ofwat, 'PR24 final determinations: Aligning risk and return appendix 1', December 2024, p.70, Table 8.

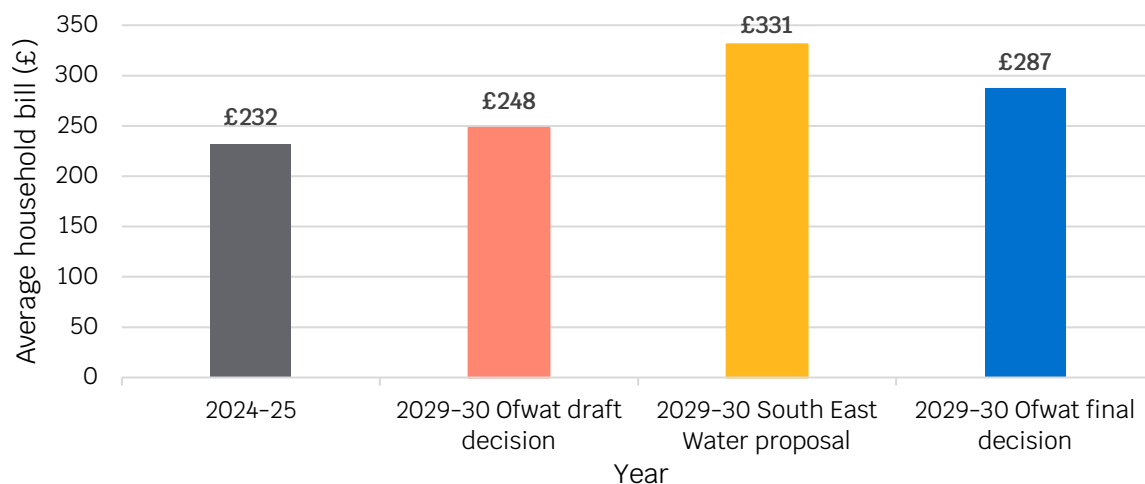
<sup>31</sup> [OF-SEW-008] Ofwat, 'PR24 draft determinations: South East Water- Quality and ambition assessment appendix', (Ofwat.gov.uk), July 2024, p.3.

fresh equity and the full restriction of dividends over the 2025–30 period with an aim to reduce gearing to under 70%, subject to the terms of the final determination and an appropriate calibration of risk and return.<sup>32</sup>

- 3.41 South East Water remains subject to ongoing monitoring and engagement of its financial resilience, as it has been categorised as 'Action required' in our Monitoring financial resilience report for two consecutive years.<sup>33</sup> We consider that South East Water needs to take steps to support its long term financial resilience and we discuss the issues concerning South East Water's financial resilience in further detail in the 'Risk and return – common issues document'.<sup>34</sup>

## Affordability

**Figure 3.5: Average household bills for South East Water, 2024–25 and 2029–30, before inflation**



- 3.42 The PR24 final determination results in an increase in average household bills of £55 (24%) from 2024–25 to 2029–30 for South East Water customers, before inflation, compared with the company's proposed £99 (43%) increase.<sup>35</sup>
- 3.43 In South East Water's October 2023 business plan the company proposed zero shareholder support for customers struggling to pay, resulting in the company being ranked as the least ambitious on affordability across the sector.<sup>36</sup>

<sup>32</sup> [OF-SEW-009] South East Water, 'PR24 draft determination response – executive summary', August 20024, p.22.

<sup>33</sup> [OF-OA-066] Ofwat, 'Monitoring Financial Resilience Report 2023–24', November 2024, p.7.

<sup>34</sup> Ofwat, PR24 redeterminations – risk and return – common issues, April 2025, Section 9.

<sup>35</sup> Our decision is for the revenue companies can collect through bills, not the average bills per customer – the latter is a forecast.

<sup>36</sup> [OF-SEW-008] Ofwat, 'PR24 draft determinations: South East Water- Quality and ambition assessment appendix', (Ofwat.gov.uk), July 2024, p.2.

3.44 In its representation to our draft determination, South East Water included shareholder support: this was a condition that needed to be met in order for the contingent penalty in our quality and ambition assessment to be removed. Total funding from shareholders for affordability support is forecast as 0.04% of South East Water's return on regulated equity, which at the final determination was the third lowest of all the water companies.<sup>37</sup> Shareholders also put forward a £1.5 million contribution towards debt matching and other affordability schemes which remains the fourth lowest across the sector. The company committed to doubling support over the period and plans to increase the percentage of customers on social tariffs from 6% to 10% over the 2025-30 period.<sup>38</sup> The majority of the financial support will come from a levy on customers to provide a cross subsidy: the company's social tariff offer is fully funded by other customers.

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<sup>37</sup> [OF-OA-048] Ofwat, 'PR24 draft determinations: Summary of water companies' published plans for affordability for 2025-30', (Ofwat.gov.uk), December 2024, p.10, Table 1.3.

<sup>38</sup> [OF-OA-048] Ofwat, 'PR24 draft determinations: Summary of water companies' published plans for affordability for 2025-30', (Ofwat.gov.uk), December 2024, p.9, Table 1.2.

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

### Introduction

- 4.1 If we consider that a point raised by South East 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 (section 4.1); outcomes (section 4.2); and risk and return (section 4.3).
- 4.3 In the fulfilling our duties appendix to our PR24 redetermination– overview of our response to the statements of case we explain how our PR24 final determinations reflect our statutory duties. It also provides our response to any specific comments about our duties, made by companies in statements of case, including those from South East Water.

### Expenditure allowances

- 4.4 At final determination, South East Water received 87% of the total expenditure that it had requested in its representation on the draft determination.
- 4.5 While South East Water's statement of case largely focuses on the areas of cost challenge at final determinations, it has increased its overall cost request by £129 million since its response to our draft determination, largely in base expenditure (from £1.3 billion to £1.4 billion). In enhancement the increase is from a combination of the company requesting its resilience request in full despite our inclusion of a £50 million contingent allowance. South East Water also requests the closure of nearly all cost gaps across base expenditure (including modelled allowances and cost adjustment claims) and enhancement requests.
- 4.6 At final determination we assessed the expenditure allowance in the round and provided South East Water with higher allowances than it requested in several areas of enhancement expenditure (supply-demand balance, strategic resource options, metering). These are not highlighted in its submission to CMA.

- 4.7 Table 4.1 shows the changes to South East Water's proposed expenditure amounts, and our allowances between its original PR24 business plan, our draft determination, its representation on our draft determination, our final determination and its statement of case. Since February 2024, the company's total expenditure request has increased by £238 million or 12%.

**Table 4.1: Cost gap at final determination by area (five-year period, after frontier shift/RPEs, 2022-23 prices)**

	Company view (February 2024) totex (£m)	Company view (August 2024) totex (£m)	Final determination (£m)	Statement of case (£m)	Cost gap FD vs SoC (£m)
Total expenditure	1,995	2,104	1,821	2,233	-412
Base expenditure	1,256	1,343	1,255	1,428	-173
Enhancement expenditure	738	761	566	805	-239

## Setting our base allowances

- 4.8 At final determination our base expenditure allowances were 14% more than the company has spent over the last five years and 28% more than its PR19 allowance.
- 4.9 In its statement of case, South East Water raises the following issues in relation to our base cost assessment:
- 4.10 **Water base cost models** – South East Water states its concerns with some of the selected cost drivers and model specifications. Firstly, the inclusion of length of mains as a scale variable in the treated water distribution models. It considers this does not appropriately capture costs associated with population growth and proposes the inclusion of the number of properties variable in half of the models. Secondly, the company considers that weighted average complexity is unintuitive when modelled in logarithms. Thirdly, the company proposes that average pumping head and booster per length of mains network topography variables should both be included in the same models, rather than in separate models.
- 4.11 **Economies of scale at water treatment works** – South East Water considers that the final determination assessment of its cost adjustment claim was only partial in scope. This is because it focused only on the water resources plus models and omitted the impact on wholesale water models. The company commissioned a report to review our assessment and submits this as new evidence to support its case.

- 4.12 **Mains renewal cost adjustment** – South East Water disagrees with our approach to determining what base buys, but it is unclear which view the company supports.<sup>39</sup> It also asks the CMA to allow a higher efficient unit cost for mains renewals due to operating conditions faced by the company, including congested road, high regional wages and a high density of regions categorised as sensitive areas. The company provides no additional evidence to support its request.
- 4.13 **Meter replacement cost adjustment** – South East Water disagrees with our approach to holding companies to account for PR19 under-delivery. It states that it has spent its PR19 allowance and there was not a PCD or set requirement for companies to deliver the mains renewals activity specified in their business plans. The company asks the CMA to remove this adjustment from its allowed adjustment. It also asks for an increase in the unit cost of replacement based on its bottom-up cost assessment.
- 4.14 **Network reinforcement** – South East Water asks the CMA to recalculate its adjustment using its preferred approach to calculating the implicit allowance and removing the efficiency challenge applied at final determination. The company considers that the approach taken to calculating the implicit allowance overstates what base buys, and that costs in the South East are higher than other regions which means that a median unit cost is not suitable to assess cost efficiency in network reinforcement.
- 4.15 **Frontier shift** – South East Water proposes a frontier shift adjustment of 0.5% per year compared to our adjustment of 1.0% per year.
- 4.16 Each of these issues has potential cross company impacts and so are discussed in detail in the Expenditure allowances – common issues document and Expenditure allowances – cost adjustment claims and Expenditure allowances – addressing asset health appendices. We provide a brief outline of our response in the following table.

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<sup>39</sup> To support its submission, the company submitted a report, [OF-CA-048] 'Oxera – Base cost adjustments and cost adjustment claims', which states that "As with the other post-modelling adjustments, the implicitly funded level of activity should be based on the full benchmarking period – not an arbitrary set of years.", p. 7.



**Table 4.2: Key issues in setting base allowances**

Base expenditure area	Change to FD allowance (£m)	Ofwat response	Document reference
Water base models	45	We consider the decisions to include length of mains as the scale driver in the treated distribution models, modelling weighted average complexity in logarithms and using average pumping head and booster per length of mains in different models continue to be appropriate based on the extensive company engagement and consideration given to these issues throughout the PR24 process.	Expenditure allowances – common issues Section 2 – Wholesale water base models
Economies of scale at water treatment works – cost adjustment claim	12	<ul style="list-style-type: none"> <li>• We consider our decision remains appropriate based on the new information provided.</li> <li>• We accepted the unique circumstances faced by South East Water, Southern Water and Wessex Water in terms of operating a high number of water sources per population (top three companies), meaning they could not benefit from economies of scale in water treatment. We also agreed this was unlikely to be captured by variables in the base cost models.</li> <li>• We developed an independent view of the value of the cost adjustment by including a water weighted average treatment size (water-WATS) variable in all the water resource plus base cost models. The company requests an additional allowance based on also including the water-WATS variable in the wholesale water base cost models.</li> <li>• We only included the water WATS variable in the water resources plus models for the purpose of calculating the cost adjustment as this is where we expected the water-WATS variable to have the largest impact (ie it primarily affects water treatment costs). We do not consider it is appropriate to also include the variable in the wholesale models due to poor statistical performance.</li> </ul>	Expenditure allowances – cost adjustment claims Section 13
Mains renewal cost adjustment	72	<ul style="list-style-type: none"> <li>• We disagree with the company's approach to determining what base buys.</li> <li>• We do not consider there to be a clear rationale for calculating what base buys on the last five years, and have concerns with the incentives this could create. We consider it is most appropriate to use the historical period used to set base expenditure allowances to ensure that customers do not pay twice.</li> <li>• The company also does not identify company specific factors that are driving the company's unit cost of renewals above that of other companies.</li> </ul>	Expenditure allowances – common issues Section 2 – cost adjustment claims

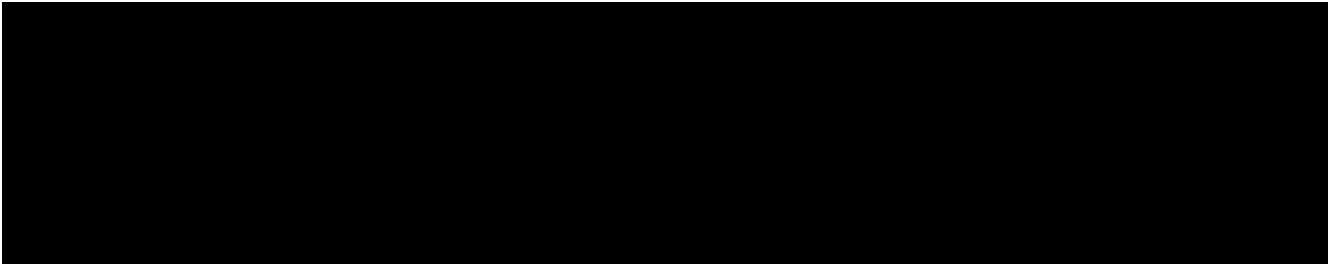


Meter replacement cost adjustment	15	<ul style="list-style-type: none"> <li>It is appropriate to hold companies to account for historical under-delivery to ensure that customers do not pay twice.</li> <li>At PR19, there was a 0.4% sector cost gap between allowances and business plan requests. We therefore consider that companies were sufficiently funded to deliver renewals as set out in their business plans, and therefore that customers should not pay twice for companies failing to do so.</li> <li>The company has not provided compelling evidence to demonstrate why its efficient unit cost of replacement is greater than other companies. It provides no evidence to support its bottom-up cost assessment. It also received an adjustment that is greater than what it requested in its original business plan submission.</li> </ul>	Expenditure allowances – common issues Section 2 – cost adjustment claims
Network reinforcement	10	<ul style="list-style-type: none"> <li>We consider the £32.2 million network reinforcement sector wide adjustment awarded to the company continues to be appropriate.</li> <li>The implicit allowance is triangulated between two approaches and the unit cost efficiency challenge incorporates a 20% cap as opposed to using the industry median unit cost, which would have led to a cost challenge of 54.8% instead of 20%.</li> </ul>	Expenditure allowances – common issues Section 2 – cost adjustment claims
Frontier shift	19	<ul style="list-style-type: none"> <li>We continue to consider a 1% per year frontier shift adjustment is appropriate.</li> <li>This is consistent with recent CMA and UK regulatory decisions 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>	Expenditure allowances – common issues Section 6
Total	173		

## Setting our enhancement allowances

4.17 South East Water requests additional enhancement expenditure allowances in the following areas, largely reflecting cost challenges in our final determinations:

4.18 **Water WINEP** – WINEP Investigations and Drinking Water Protected Areas where South East Water raise that the cost efficiency challenge was arbitrary and did not take full account of the evidence. South East Water request that its enhancement cost allowances are adjusted to fill the cost gaps left by PR24 final determinations.

- 4.19 **Supply demand balance** – Leakage and Demand Management (Water Efficiency)  
South East Water requests the full £43.1 million allowance for its 'other leakage activity' (i.e. non-mains renewal), stating it is in its customers' interests.
- 4.20 For the demand (water efficiency) activities the company requests a funding allowance of £40.2 million, which represents a reduction of £13.5 million from its business plan request of £53.7 million. This change results from a revised cost estimate derived by South East Water since our PR24 final determination.
- 4.21 **Resilience and security** – resilience (resilience interconnectors, smart networks, Bewl water treatment works, river Medway water treatment works, service reservoir capacity), SEMD (alternative water supply) and cyber.
- 4.22 For smart networks the company is asking to fund the full request of £48.1 million, including the resilience request of £36.8 million, and a leakage request for £11.3 million that we allocated from resilience. The company disagrees with our assessment that the £48.1 million investment should be covered by base allowances and disagrees with our cost reallocations to leakage.
- 4.23 For Bewl the company is requesting the CMA to accept the full funding of £27 million to upgrade the site. The company disagrees with our assessment on the need for enhancement and has provided additional narrative relating to the need. It disagrees with the £50 million contingency mechanism that Ofwat have made available for resilience which can be used for Bewl where appropriate evidence is submitted.
- 4.24 For service reservoirs the company is requesting the full funding of £34 million compared to the allowance of £25 million. It disputes our assessment on cost efficiency and provides new costing evidence for the £34 million in its statement of case.
- 4.25 For resilience Interconnectors the company is asking to close the full cost gap of £38 million. The company disagrees with our adjustment which excluded investment for previously funded activities, and with our allocation of seven schemes from supply interconnectors to resilience interconnectors.
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- 4.27 **Water quality improvements** – This includes company requests under lead, PFAS and nitrates. On **Lead** South East Water resubmits all costs under 'Other lead reduction related activity' that were challenged at final determination, representing a total of

£24.3 million. This includes costs related to large scale stop tap surveys, lead sampling and lead trial holes at 5% of properties, etc. On **PFAS** South East Water resubmits the costs for a scheme previously raised at final determination which was deferred to our 'PFAS Reopener' – Beenhams Heath WTW (£3.4 million) and inclusion two new PFAS schemes at Forstal Water Treatment Works (£4.8 million) and five Catchment Studies (£4.2 million). This represents a total request of £12.4 million, £9 million more than requested for final determination. On **Nitrates** South East Water requests that we remove the 10% cost efficiency challenge for the Cookham Dean WTW scheme (–£1.4 million). However, we provided the company with a higher nitrate allowance at final determinations than requested as the other four schemes were more efficient than our cost benchmark (+£1.5 million). This results in an overall increase in the company request compared to final determination (+£2.9 million). This gives an overall increase in the water quality request of around £12 million.

- 4.28 **Other enhancements** – net zero South East Water requested a net zero enhancement funding allowance totalling £12.6 million. This funding covers two Ozone upgrade schemes totalling £4.4 million, and one transport focused scheme totalling £8.2 million. None of these schemes were approved at final determination as they did not pass the eligibility criteria set out in our PR24 methodology.
- 4.29 Most of these issues could have cross company implications and so are discussed in the 'PR24 redeterminations- expenditure allowances – common issues' The following issues are company specific and are discussed in this document:
- Water resilience
  - SEMD – Alternative Water Supplies/ Emergency Planning
  - Lead
  - Raw water deterioration – PFAS
  - Cyber
  - Drinking water protected areas
- 4.30 South East Water also raises concerns on our shallow dive efficiency challenge. However, this is not part of their overall requested cost increase. We provide our response to this issue in the 'PR24 redeterminations- expenditure allowances – common issues'.
- 4.31 The following table sets out the enhancement expenditure requests from the company, and our final determination allowances, including a comparison with amounts requested in the company's statement of case.

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

Enhancement expenditure area	Company view (February 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	96	97	82	-15	96	14
Supply/Demand balance and metering	227	236	160	-75	212	52
Resilience and security (w)	363	337	266	-70	387	121
Water quality improvements	57	88	72	-17	101	29
Other water enhancement areas	13	13	0	-13	13	13
Total water enhancement allowance	756	770	580	-190	809	229

4.32 The following table provides additional navigation assistance for CMA. It sets out each of the key enhancement issues raised in South East 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 reference
Resilience interconnectors	38	This is an existing issue. The company has not provided sufficient and convincing evidence for the need for enhancement. We have concerns the investment overlaps with PR19 and base. The company requests to use a modelled approach but does not provide reliable or comparable model drivers.	"PR24 redeterminations – response to South East Water statement of case", section 4

Smart Networks	37 <sup>40</sup>	This is an existing issue. The company has not provided sufficient and convincing evidence for the need for enhancement. We have concerns the investment overlaps with base. The company does not provide a structured narrative explaining its choices nor does it proposed investment result in a step change in performance.	"PR24 redeterminations – response to South East Water statement of case", section 4
Bewl water treatment works	27	This is an existing issue. The company has not provided sufficient and convincing evidence for the need for enhancement. The company does not clearly articulate why the upgrade is required in light of AMP7 improvements at Bewl nor does it adequately explain why the AMP8 investment at [REDACTED] will not sufficiently improve resilience.	"PR24 redeterminations – response to South East Water statement of case", section 4
Service Reservoir capacity increases	9	This is an existing issue with new evidence. The company has provided new evidence which partially addresses concerns we set out within our final determination. We continue to have concerns regarding the cost as the company relies upon the cost of new service reservoirs to estimate its cost for proposed increases in capacity at existing service reservoirs.	"PR24 redeterminations – response to South East Water statement of case", section 4
Southern Water Treatment Works Upgrade (River Medway Scheme)	7	This is an existing issue. The company has not provided sufficient and convincing evidence that its costs are efficient. Based on the evidence solely provided by Southern Water under the five-site strategy, we cut the spending request. We proportionally allocate cost challenges from Southern Water to South East Water so they have funding to meet required contributions of 25%. We continue to consider that South East Water would be accountable for overspend.	"PR24 redeterminations – response to South East Water statement of case", section 4
Leakage	36	This is an existing issue. The company stated that the use of SES Water's unit cost for higher performing companies is inappropriate. We still consider a unit rate of £2.057m per Ml/d is sufficient for companies to deliver other leakage activities. No further evidence is provided why higher performers need a higher rate and why South East Water's rate is efficient.	"PR24 redeterminations – expenditure allowances – common issues", section 4

<sup>40</sup> Excluding £11.300 million that was reallocated and assessed in leakage.



<b>Demand</b>	16	This is an existing issue. The company has not provided sufficient and convincing evidence that its proposed high unit costs are justified for its proposed programme. We therefore continue to consider that efficiency challenge remains appropriate to protect customers.	"PR24 redeterminations – expenditure allowances – common issues", section 4
<b>Lead</b>	17	This is an existing issue. The company has not provided sufficient and convincing evidence its large-scale dig survey approach to identify lead pipes is necessary. We therefore continue to consider that challenging the need for enhancement for this part of its lead strategy is required to protect customers.	"PR24 redeterminations – response to South East Water statement of case", section 4
<b>Raw water deterioration</b>	12	<p>This is an existing issue.</p> <p>PFAS – The company has not provided evidence of DWI endorsement/ tracking of scheme delivery in the form of a site-specific notice for Beenhams Heath WTW. The scheme has been deferred to our PFAS Reopener.</p> <p>Nitrate – The company has not provided sufficient and convincing evidence of costing methodology and third party benchmarking for the Cookham Dean WTW scheme. 10% challenge has been applied.</p>	<p>"PR24 redeterminations – response to South East Water statement of case", section 4</p> <p>"PR24 redeterminations – expenditure allowances – common issues", section 4</p>
<b>WINEP investigations</b>	12	This is an existing issue. The company has not provided supporting benchmarking or sufficient and convincing evidence of exogenous factors to fully justify why its costs are so much higher than other companies. We continue to consider that our benchmark approach with deep dives on cost outliers is appropriate. We have reflected the additional complexity of South East Water's actions in our allowance and maintain that a 20% adjustment is appropriate and necessary to protect customers.	"PR24 redeterminations – expenditure allowances – common issues", section 4
<b>WINEP – Drinking water protected areas</b>	2	This is an existing issue. The company has not provided evidence on cost efficiency in the form of activity cost breakdown or benchmarking for the 15 schemes included in its DrWPA programme. We therefore continue to consider that a 10% cost	"PR24 redeterminations – response to South East Water statement of case", section 4

		efficiency challenge remains appropriate to protect customers.	
Cyber	2	This is an existing issue. The company disputes our 5% cost efficiency challenge to its cyber security funding, citing three third-party assurance reports as evidence of efficient costs. Our assessment found that these reports do not provide sufficient and convincing evidence of cost efficiency—none directly address cyber-related costs or offer suitable benchmarking. As a result, we maintain that our modest 5% adjustment is appropriate and necessary to protect customers, given the company's continued failure to demonstrate that its proposed costs are efficient.	"PR24 redeterminations – response to South East Water statement of case", section 4
SEMD	1	This is an existing issue. We maintain our 10% challenge of costs in this area. The company has not provided sufficient and convincing evidence of bottom-up costing and benchmarking for all costs pertaining to alternative water supplies.	"PR24 redeterminations – response to South East Water statement of case", section 4
Net zero	13	This is an existing issue. We maintain our decision on not allowing funding through the Net Zero Challenge Fund for the three schemes submitted by the company. The two Ozone upgrade schemes continue to be outside the eligibility criteria for the fund, because they are not primarily driven by net zero. We maintain that the electrification of the company's fleet should be funded from base cost allowance. However, we introduced a sector wide base cost adjustment for net zero to support with the costs of supporting infrastructure and heating.	"PR24 redeterminations – expenditure allowances – common issues", section 4
Frontier shift	12	This is an existing issue. We continue to consider a 1% per year frontier shift adjustment is appropriate. 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%. 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.	"PR24 redeterminations – expenditure allowances – common issues", section 6

<b>Total</b>	239 <sup>41</sup>		
<b>Other issues</b>			
<b>Shallow dive efficiency</b>		We continue to apply the shallow dive efficiency challenge for low materiality (<£10 million schemes). The % challenge is based on the efficiencies of multiple expenditure models and is applied using the same method for all companies.	"PR24 redeterminations – expenditure allowances – common issues", section 9
<b>£50 million contingent resilience allowance</b>		We continue to consider that the contingent resilience allowance for South East Water is appropriate. Based on the resilience evidence it has submitted in its representations to draft determinations, the ex-ante resilience allowances we have set are appropriate. The mechanism is clear and objective, submissions require compelling evidence and can be linked to schemes previously disallowed at final determinations. The mechanism is an opportunity for the company to address concerns we had over the need for resilience enhancement at final determinations.	"PR24 redeterminations – response to South East Water statement of case", section 4

## Resilience enhancement

- 4.33 In our PR24 methodology we set out that resilience enhancement investment can be requested to manage increasing risks, or changing acceptance or acceptability of risk, from hazards that are beyond company control and not covered by other enhancement areas (for example, increasing risk of source water pollution, river or coastal flooding).<sup>42</sup>
- 4.34 In our PR24 final methodology we excluded providing allowances to manage existing risk and to address the failure of assets managed through maintenance, as these should be managed through base costs allowances.<sup>43</sup> We stated that investment should be prioritised and promoted based on an understanding of the current level of risk, how this would change under the proposed investment, and how this compares to the risk appetite of customers and the company's board. Companies should also have addressed

<sup>41</sup> Numbers may not add due to rounding.

<sup>42</sup> [OF-CA-001] Ofwat, 'PR24\_final\_methodology\_Appendix\_9\_Setting\_Expenditure\_Allowances.pdf', December 2022, p.48.

<sup>43</sup> [OF-CA-001] Ofwat, 'PR24\_final\_methodology\_Appendix\_9\_Setting\_Expenditure\_Allowances.pdf', December 2022, pp.51-56.



any actions identified in their PR19 resilience action plans. We expect companies to continue offsetting the in-period impacts of climate change through base allowances.<sup>44</sup>

- 4.35 Based on our assessment of the need for enhancement (focused on concerns with base overlap and customers double funding), optioneering and cost efficiency we made an allowance of £87 million for South East Water to deliver water production and treated storage upgrades and £90 million to deliver improved interconnectivity.<sup>45</sup> For our final determination we provided an allowance of £228 million in response to the company's request of £295 million.
- 4.36 We recognised that the company's poor performance indicates a residual risk that additional investment may be needed during 2025–30. However South East Water was unable to appropriately evidence the need for this additional investment as part of the price review process. To manage this residual funding risk, the £228 million total allowance included a contingent allowance of £50 million for South East Water.<sup>46</sup> This contingent allowance is available to South East Water within AMP8 subject to the company evidencing that it is spending its enhancement allowances; its resilience programme is on target and that the company presents a submission identifying resilience schemes to be delivered with an appropriately evidenced case for additional resilience investment.<sup>47</sup> The contingent allowance will allow the company to address issues in the 2025–30 period, protecting customers' interests and promoting long-term resilience. Further details on the issues raised by the company, and our analysis of the contingent allowance, can be found further down in this cost resilience section.
- 4.37 The overall allowance for the company is the second highest in the sector across resilience and resilience interconnector cost models.<sup>48 49</sup> Table 4.5 below shows a scheme level summary of assessed (the value the company proposed) and our PR24 final determination allowances.

**Table 4.5: Water production and treated water assessed and allowed values**

Programme	Scheme Description	Assessed Value £ million	Allowances £ million
Resilience	Smart Water network (company level)	36.806	0.000
	Resilience improvements at Tonbridge, Pembury, Bewl WTWs	34.644	7.959
	Improved resilience at Barcombe WTW	45.428	45.428

<sup>44</sup> [OF-CA-001] Ofwat, 'PR24\_final\_methodology\_Appendix\_9\_Setting\_Expenditure\_Allowances.pdf', December 2022, p.52.

<sup>45</sup> [OF-OA-022] Ofwat, 'PR24 final determinations: Expenditure allowances', December 2024, p.226.

<sup>46</sup> The individual allowances of £87 million for water production and treated storage upgrades, £90 million for interconnectivity and £50 million of contingent allowance do not add up to £228 million due to rounding.

<sup>47</sup> [OF-OA-022] Ofwat, 'PR24 final determinations: expenditure allowances', December 2024, pp.226–227.

<sup>48</sup> [OF-CA-147] Ofwat, PR24-FD-CA31-Water-Resilience-enhancement-expenditure-model\_redacted.xlsm, tab "Allowance".

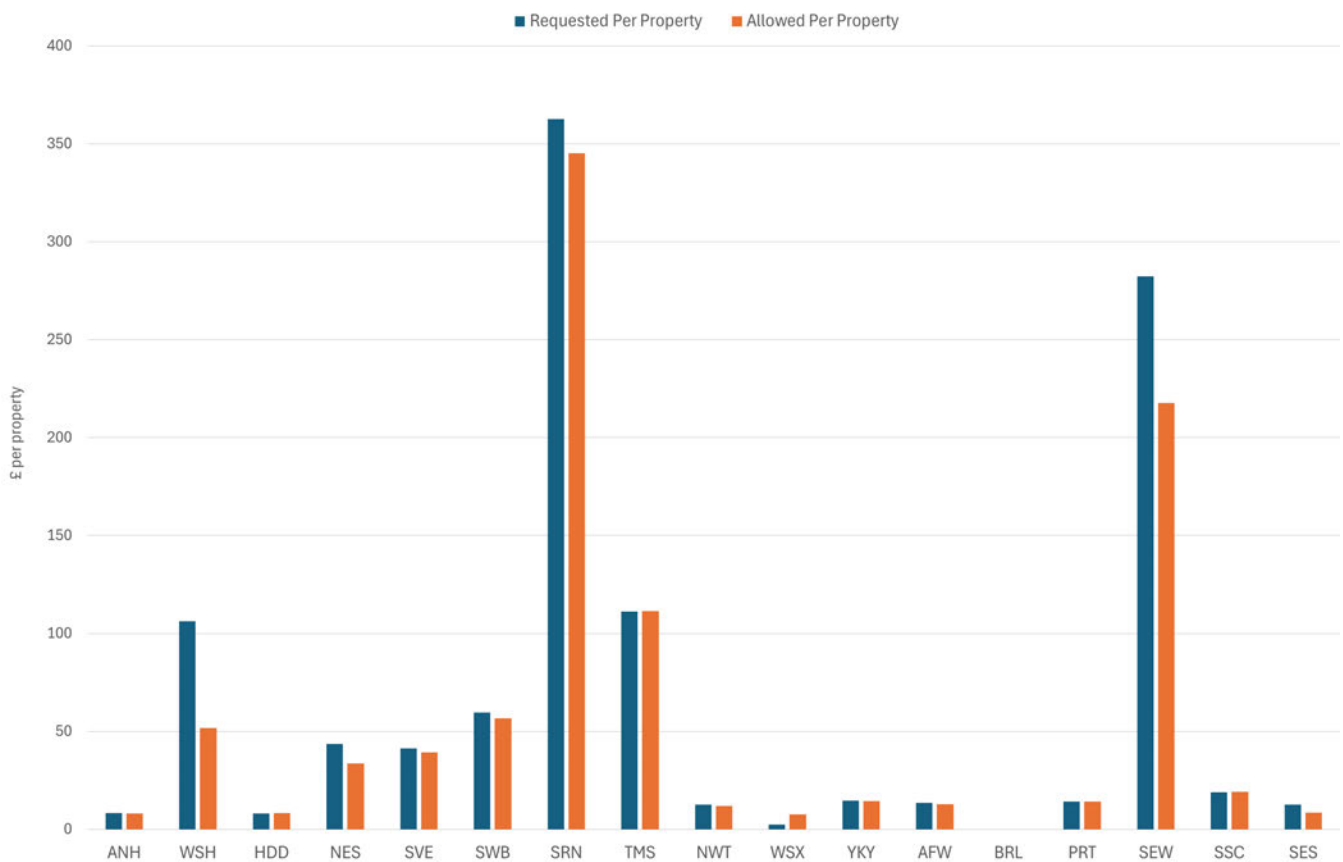
<sup>49</sup> [OF-CA-279] Ofwat, PR24 final determinations: Water resilience interconnectors v3, tab "Allowance", December 2024.

	Contribution to Southern Water for improvements at [REDACTED] WTW (River Medway scheme)	15.450	8.684
	Resilience improvement of five service reservoirs in Kent	26.179	19.242
	Two service reservoirs in Sussex	7.835	5.759
<b>Resilience interconnectors</b>	As submitted (nine schemes)	41.177	23.924
	Allocated from supply interconnectors (seven schemes)	87.608	66.504
<b>Climate Change Resilience Uplift</b>	At draft determinations we allowed £5.500 million uplift for climate change. In its representations it forwent the allowance <sup>50</sup>	0.000	0.000
<b>Total</b>		<b>295.127</b>	<b>177.500</b>
<b>Resilience contingency funding</b>	Additional funding is available for future submissions related to resilience or resilience interconnectors	0.000	Up to 50.000
<b>Total including contingency funding</b>		<b>295.127</b>	<b>Up to 227.500</b>

4.38 We also highlight in Figure 4.1 that on a per property basis, both the request and the allowance is the second highest in the sector and more than double that of the third place company.

<sup>50</sup> [OF-SEW-013] Ofwat, Query response OFW-REP-SEW-069.

**Figure 4.1 Per property resilience costs including contingent allowance**



## Smart Networks

### Final determinations

4.39 The company requested an allowance of £48.106 million for the purposes of creating a smart water network, which they propose to include:

- Pressure sensors;
- Chlorine residual monitors;
- Service reservoir inlet and outlet meters;
- Trunk main meters;
- Telemetry updates; and
- Network monitoring and analysis software.

4.40 In our final determination we assessed, in a deep dive, the proposed investment and we did not provide any allowance for the proposed investment. It was our view that the

company did not provide sufficient and convincing evidence to demonstrate the need for this scheme to be allowed as enhancement.

### Issues raised by disputing company

4.41 In its statement of case,<sup>51</sup> the company raises two issues with our assessment, namely it disagrees with:

- Our reallocation of £11.3 million from resilience to leakage associated with pressure sensors and acoustic leakage sensors.
- Our conclusion that there is overlap with base costs for its smart network activities.

### Our assessment

4.42 Having reviewed the arguments brought forward by the company in its statement of case and revisiting our final determination we consider there could be a case to include an allowance (of between £2.098 million and £9.753 million, see Figure 4.2 below) relating the installation of meters on trunk mains. This would relate to new requirements in leakage reporting in AMP8 which requires companies to adopt a flow balance approach to monitoring trunk mains leakage.<sup>52</sup> Had the company presented the investment relating to trunk mains meters for this purpose earlier we are likely to have included an allowance for this in our final determination.

4.43 We continue to consider that the company does not provide sufficient and convincing evidence to demonstrate that the remaining request for smart network investment should be allowed through enhancement expenditure.

### Reallocation of £11.3 million to leakage

4.44 The company disagrees with our reallocation of costs relating to pressure and acoustic leakage sensors to leakage. Our reallocation was based on rejection of its resilience enhancement case (due to insufficient evidence), and we looked to see if we could include an allowance relating to these items within leakage enhancement.

4.45 We assessed these claims within leakage enhancement as a deep dive. The deep dive did not identify clear leakage benefits associated with the proposed benefit and therefore no allowance was included. Within Annex G Paragraph 397 the company states it did not include a defined MI/d leakage benefit within its submission, nor did it for other secondary benefits.

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<sup>51</sup> [OF-OA-005] South East Water, 'PR24 Redetermination – Statement of case', March 2025, paragraph 4.75 (e), p.57.

<sup>52</sup> [OF-OA-017] Ofwat, 'PR24 final determinations: Delivering outcomes for customers and the environment', December 2024, p.116.

4.46 As the company does not set out the benefits of its proposed investment, we do not find it provided sufficient and convincing evidence that it is efficient and requires customer funding. Within its statement of case it still does not quantify any secondary benefits.

4.47 Overall, we conclude it was appropriate to reallocate the proposed investment in acoustic leakage sensors and pressure sensors through our leakage assessment, after the company failed to show need for this investment in resilience. Had the company presented a structured business case, clear need and provided details of benefits it is more likely we would have provided an allowance for this investment.

### **Overlap with base for proposed smart network upgrade**

4.48 We continue to consider that the smart network upgrade should be covered by base expenditure as: it is consistent with the definition of base spending, other companies have delivered smart network improvements through base, it does not deliver a step change in performance and does not provide an evidenced case for the proposed option and benefits.

### **Base expenditure**

4.49 We continue to consider that the smart network upgrade should be covered by that this base expenditure because:

- it is consistent with the definition of base spending;
- other companies have delivered smart network improvements through base; and
- it does not deliver a step change in performance.

4.50 Even if we considered that this type of investment meets the enhancement criteria, South East Water does not provide sufficient and convincing evidence to support its proposed investment or the chosen option within its statement of case.<sup>53</sup> The company claims to have considered several options to identify the smart network design which would benefit customers the most. The company presents the support for its "full" smart network as near universal with no support for a "more basic" smart network within its statement of case. In its October 2023 business plan submission<sup>54</sup> the company states that "stakeholders felt divided whether a full or basic system was preferable".

### **Consistent with base expenditure definition**

4.51 We expect the maintenance and replacement of assets and systems used in the production and supply of water to modern equivalent standards to be delivered through base allowances. We define base expenditure as the routine, ongoing costs that water

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<sup>53</sup> [OF-CA-195] South East Water, 'South East Water PR24 RD – Annex G – Enhancement costs', March 2025, paragraph 402, p.90.

<sup>54</sup> [OF-SEW-014] South East Water, SEW41 Resilience, October 2023, p.4.

companies incur to maintain their current level of service. This includes the costs associated with operating, maintaining, and renewing existing assets. The proposed schemes failed to provide sufficient and convincing evidence to demonstrate their eligibility for enhancement allowances through a step change to a new, improved level of service; nor to demonstrate that the proposed investment went beyond what we would reasonably expect a company to be doing already.

### **Other companies delivered smart network improvements through base**

- 4.52 The company states in its statement of case that it is "unaware of any Ofwat funding for base or enhancement at PR14 or PR19 which has been explicitly targeted for a smart network".<sup>55</sup> This is correct. However, other companies have successfully delivered smart networks through the maintenance and replacement of existing assets. The company does not explain why it has been unable to do the same. The way that base allowances are modelled means that the base spent by others on this activity in the past is incorporated into the modelled outputs.
- 4.53 Within our call for evidence on innovative examples of smart network through base allowances we received examples from most companies. Examples we were given include the following.
- 4.54 Affinity Water developing an artificial intelligence tool which combines flow, pressure and other network data to understand network events. They tied this with hydraulic modelling to predict locations of non-visible leaks on their distribution network.
- 4.55 Southern Water installed 24,000 sewer level monitors at risk points across its wastewater network to identify emerging sewer blockage issues and installed pressure monitoring on higher risk rising mains to identify pressure surges which can result in bursts.
- 4.56 South West Water developed a smart water system to predict, control and self-configure the clean water network to reduce supply interruptions, manage supply pressures,

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<sup>55</sup> [OF-CA-195] South East Water, South East Water PR24 RD – Annex G – Enhancement costs, March 2025, paragraph 399(d), p.89.



ensure water quality, reduce energy use and maintain continuous service for our customers.

- 4.57 Portsmouth Water used smart pressure sensors combined with machine learning software to enable them to use micro pressure fluctuations to identify network bursts and leaks.
- 4.58 All the above examples of smart networks have been achieved through these companies' base expenditure.

### **Lack of step change in performance**

- 4.59 In its statement of case the company states the "investments we need to make now represent a clear step-change".<sup>56</sup> However, even with the proposed resilience investment, South East Water is forecasting to deliver the second worst water supply interruptions performance across England and Wales at 8 minutes per customer property. This is a significant improvement on current performance, which is over 44 minutes per property reported in 2023-24, and in 2019-20 the company reported a water supply interruptions value of 10 minutes. However, it is still double the 2025-30 target, 5 minutes, that we set for all water companies. The company claims that this is due to challenges from climate change and changing demand patterns post Covid-19.<sup>57</sup> These challenges are not unique to South East Water and similar failures in interruptions to supply have not been seen across other companies impacted by these factors. We continue to consider that the smart networks expenditure should be covered by base expenditure and does not deliver a step change in performance beyond that expected to meet the existing supply interruptions performance commitment of 5 minutes per customer property. We note that even after the proposed improvements the duration of supply interruptions experienced by customers is still expected to be higher than it was in 2019-20.

### **Lack of sufficient evidence to support proposed investment**

- 4.60 Within our deep dive we found the company did not provide sufficient and convincing evidence to support the proposed investment. Its main evidence was a series of reports combined into a very long single PDF document.<sup>58</sup> We were unable to find any structured narrative from the company whereby it builds the case for the proposed smart network investment. The document contains 165 pages relating to smart water networks but is mainly comprised of a 145 page UKWIR report titled "Smart metering and smart networks for leakage management". This report is not specific to South East

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<sup>56</sup> [OF-CA-195] South East Water, South East Water PR24 RD – Annex G – Enhancement costs, March 2025, paragraph 400, p.90

<sup>57</sup> [OF-CA-195] South East Water, South East Water PR24 RD – Annex G – Enhancement costs, March 2025, paragraph 399(a), p.88.

<sup>58</sup> [OF-SEW-015] South East Water, SEW06 Collated reference documents – Companywide, October 2023.

Water and we have not found that South East Water refer to this document to support its proposed smart network investment.

- 4.61 The collated reference document also contains costing information for different components of its smart network. This includes different options which are available as shown in Figure 4.2.

**Figure 4.2: South East Water smart network capital expenditure**

**CAPEX Costs**

Scheme	Optimistic (-10%)	Total Cost	Pessimistic (+10%)
Pressure Sensors	£ 3,400,000	£ 3,777,000	£ 4,155,000
Acoustic Leakage Sensors	£ 5,693,000	£ 6,325,000	£ 6,958,000
Chlorine Residual Monitors Scenario 1 (50% new Hydrant)			
Scenario 1 (50% new Hydrant)	£ 4,347,000	£ 4,830,000	£ 5,313,000
Scenario 2 (25% new Hydrant)	£ 3,835,000	£ 4,261,000	£ 4,688,000
Service Reservoir Outlet Meters	£ 5,193,000	£ 5,770,000	£ 6,347,000
Inlet Reservoir Meters			
Scenario 1 (with Magnetic Flow Meter)	£ 7,957,000	£ 8,841,000	£ 9,726,000
Scenario 2 (with Ultrasonic Strap-on Meter)	£ 1,416,000	£ 1,573,000	£ 1,731,000
Strategic Trunk Main Meters			
Scenario 1 (with Magnetic Flow Meter)	£ 8,778,000	£ 9,753,000	£ 10,729,000
Scenario 2 (with Ultrasonic Strap-on Meter)	£ 1,889,000	£ 2,098,000	£ 2,308,000
PRISM Telemetry Updates	£ 79,000	£ 87,000	£ 96,000
Aquasuite Tool			
Scenario 1 (Alert only)	£ 1,627,000	£ 1,807,000	£ 1,988,000
Scenario 2 (Alert + Find)	£ 4,879,000	£ 5,421,000	£ 5,964,000
Smart Water Network Total	£ 40,324,000	£ 44,804,000.00	£ 49,285,000

- 4.62 Nowhere within the company's business plan does it set out benefits associated with each option. Nor does it explain the decision-making process and how the company reaches its preferred option for this investment and why it represents best value for customers. In each case it opts for the most expensive solution with no narrative. It does not explain anywhere why there is no overlap with maintenance and replacement of existing assets and makes no adjustment based on the incremental cost of smart network assets compared to traditional non-smart assets.
- 4.63 Overall, we conclude that given the poor performance of South East Water over 2020 to 2025 that there is no step change in resilience performance being provided to customers by its plan with its proposals delivering a level of supply interruptions that is still double the target we have set and more than any other English or Welsh water company. The company does not present a case for its smart network investment, rather it provides a series of documents without any references or a structured narrative.
- 4.64 We consider it could be appropriate to include an allowance relating to meters for trunk mains for the purpose of changes to AMP8 reporting requirements for leakage, not resilience as the company has included within its business plan. We cover this further in our assessment of leakage. The company presents two technologies, magnetic flow meter and ultrasonic strap on meter. These are costed by the company's consultant at

£9.753 million and £2.098 million respectively. The company opted for the more expensive magnetic flow meter within its business plan but did not explain why it opted for this over the less expensive ultrasonic strap-on meters.

- 4.65 Should the CMA not wish to consider this expenditure as leakage enhancement as part of its redeterminations we are happy to consider this as part of the £50 million contingent funding. This is as set out in our reply to its query regarding the contingent allowance.<sup>59</sup> We would expect the company to fully justify its choices, for example its choice of trunk mains metering technology, within any request.

## Bewl water treatment works

### Final determinations

- 4.66 Within the company's business plan it included a request for investment at its Bewl water treatment works (WTW). Within its 2023 business plan the company included investment to add an additional process stream to increase the output of Bewl WTW by [REDACTED], from [REDACTED] to [REDACTED]. The company requested an allowance of £26.685 million for this upgrade.

- 4.67 At PR19 we allowed customer funding for the company to increase the site output by [REDACTED] from [REDACTED] to [REDACTED]. This was to address an invasive non-native species risk at Darwell reservoir which resulted in the need to end an existing [REDACTED] transfer from Darwell to its Hazard's Green WTW. In our final determination we assessed in a deep dive the proposed Bewl WTW upgrade and we did not provide any allowance for the proposed investment as the company did not provide sufficient and convincing evidence to demonstrate the need for this scheme.<sup>60</sup> In particular the company did not provide sufficient and convincing evidence relating to the scope or feasibility of the scheme nor did it provide evidence to demonstrate the requirement for a further increase in site output once its AMP7 upgrade was complete.

### Issues raised by disputing company

- 4.68 In its statement of case the company raises two issues with our assessment, namely that we have misunderstood the need for the Bewl WTW upgrade and have wrongly assumed that the additional capacity, delivered at Bewl WTW in AMP7, can provide additional headroom.<sup>61</sup> The company provides additional narrative within its statement of case relating to need but it does not address all the issues we highlighted with regard to evidence within our final determination.<sup>62</sup>

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<sup>59</sup> [OF-SEW-066], Ofwat, OFW-FD-SEW-002, January 2025.

<sup>60</sup> [OF-CA-147], Ofwat, PR24-FD-CA31-Water-Resilience-enhancement-expenditure-model\_redacted, tab 'SEW\_3\_WTW'.

<sup>61</sup> [OF-OA-005] South East Water, South East Water – statement of case, March 2025, paragraph 4.75 (a), p.55.

<sup>62</sup> [OF-CA-195] South East Water, SEW – PR24 RD – Annex G – Enhancement costs, March 2025, pp. 2–9.

## Our assessment

4.69 We acknowledge the arguments brought forward by South East Water in its statement of case with respect to this scheme. However, we continue to consider that the company does not provide sufficient and convincing evidence to demonstrate the need for the enhancement investment proposed at Bewl WTW.

## Company evidence

4.70 For other water treatment works' investment South East Water provides either a feasibility report, as in the case for Pembury and Tonbridge WTWs, or a strategic site study, as it did for Barcombe WTW. For its Bewl WTW investment, it has not provided either of these documents. These documents helped us understand both the proposal and the need for the investment, and we included allowances for these three investments within our final determination. Within a query<sup>63</sup> we requested the company provide any additional information, such as an engineering feasibility study, but the company was only able to provide concept design outputs which did not contain information to support the need for this investment.

4.71 The schematics the company has provided<sup>64</sup> only show a partial representation of the network, for example they do not include Hazards Green WTW. This makes it difficult to understand the company explanation of the requirement in light of the current configuration and post-AMP7 delivery position.

## AMP7 Bewl upgrade

4.72 As part of our PR19 final determination we allowed the company an enhancement allowance to increase output at Bewl from [REDACTED]. The company states that its AMP7 [REDACTED] upgrade at Bewl is a "direct replacement" of a raw water transfer from Darwell Reservoir to Hazards Green WTW.<sup>65</sup> It then states that the 2022 peak demand event showed that Hazards Green WTW required [REDACTED] of raw water from Darwell Reservoir. This compares to the transfer of [REDACTED] from Darwell Reservoir to Hazards Green WTW. This suggests that [REDACTED] of additional headroom may be available from delivery of the PR19 Bewl upgrade. The company does not explain why this is not the case. The company has not been able to sufficiently address our concerns that the AMP7 upgrade not will improve resilience in peak demand events, such as those experienced in 2022. The company has not presented sufficient and convincing evidence to demonstrate the need for the proposed AMP8 investment.

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<sup>63</sup> [OF-SEW-016] South East Water, OFW-OBQ-SEW-116, February 2024.

<sup>64</sup> [OF-CA-195] South East Water, SEW – PR24 RD – Annex G – Enhancement costs, March 2025, pp. 7–8, figures ANG5, ANG6 and ANG7.

<sup>65</sup> [OF-CA-195] South East Water, SEW – PR24 RD – Annex G – Enhancement costs, March 2025, p.4, para 16– 17.



## Proposed AMP8 upgrade

4.73 In AMP8 the company presented a further investment at Bewl from [REDACTED]. When we queried the company<sup>66</sup> it stated that the increase of [REDACTED] in AMP8 output from Bewl WTW would allow the company to reduce its [REDACTED] WTW transfer by [REDACTED], with the remaining [REDACTED] being used to improve resilience at Cranbrook Service Reservoir, which it describes as "having interruptions during various severe weather events" and also Goudhurst WTW, Kingsnorth strategic transfer and resource zone 2 in Sussex. The company does not explain how improvements at Bewl WTW will increase resilience at either Goudhurst or Kingsnorth, what historical issues have been experienced at these sites or what type of event they require additional resilience for. This implies that the needs case effectively rests on the reduced reliance on [REDACTED] and unstated resilience issues at other locations.

## River Medway Scheme – [REDACTED] upgrades

4.74 The company has a commercial agreement in place with Southern Water whereby it has a 25% share in the River Medway pumped storage scheme. Under this scheme the company is entitled to a 25% share in the overall scheme yield. This can be taken as either raw water from Bewl reservoir or from [REDACTED]. Under the terms of this agreement the company is required to contribute to 25% of any capital costs spent on [REDACTED]. Within its business plan it includes a request for £15.450 million which represents its share for the works proposed by Southern Water. The actual allowance for this scheme is smaller but continues to reflect the 25% of capital costs that the company is liable for, this is discussed later in the document.

4.75 Within a response to our query<sup>67</sup> it states "the current [REDACTED] transfer from Southern Water at [REDACTED] has proved over recent years to be unreliable", although it provides no evidence to support this statement. Within the company's statement of case it does not mention improved reliability but states the location of Bewl is more useful in improving resilience. Within annex G paragraph 269 South East Water states that the water from [REDACTED] is a key source for its Maidstone area and is part of its resilience planning. Overall, this gives a confusing view of what the company is planning to do and why, undermining confidence in its enhancement cost.

4.76 In our final determination we allowed £27.903 million for upgrades to [REDACTED] split between £21.137 million to Southern Water and £6.766 million for South East Water (who provide a 25% capital contribution to the site). Southern Water proposes to increase peak week production capacity of [REDACTED] WTW from [REDACTED] to [REDACTED] by 2031. The company does not explain why it is not feasible to use these improvements to

<sup>66</sup> [OF-SEW-017] and [OF-SEW-018] Ofwat, Query responses OFW-REP-SEW-021 and OFW-REP-SEW-048.

<sup>67</sup> [OF-SEW-017] Ofwat, Query response: OFW-REP-SEW-021.

improve resilience to its supply areas nor does it present any options to show it has considered this.

- 4.77 The company does not explain why proposed improvements in resilience cannot be achieved with the planned investment at [REDACTED] in AMP8. It states that its proposed AMP8 investment at Bewl will enable them to fill the distribution network more quickly but does not explain what impact increased output as a result of the AMP8 investment at [REDACTED] would have on filling the network or the impact reducing the [REDACTED] transfer would have on this.
- 4.78 Overall we do not consider that the company provides sufficient evidence to be confident its proposed AMP8 Bewl investment is needed and cannot be achieved through other means. We continue to consider that the company has not shown that the additional treatment capacity is needed and does not present a joined up approach to managing investment and water available in Bewl WTW and [REDACTED] WTW.

## General Issues

- 4.79 Additionally, the company does not present any additional evidence which would be useful to inform our final determination. For example, it does not specify the return period of the 2022 peak demand which would enable us to understand on average how frequently the company would experience these conditions. Nor does South East Water explain what level of resilience to peak demand events the company's proposed upgrades would deliver which would help improve our confidence that the proposed investment will address the situation it faced in 2022.

## Conclusion

- 4.80 We consider the company has not provided sufficient and convincing evidence. The company does not:
- Convincingly address our concerns that the AMP7 Bewl upgrade will improve resilience sufficiently to cope with peak demand events, such as those experienced in 2022.
  - Fully explain what impact the investment at [REDACTED] will have on its supply resilience and why it considers the planned investment will not sufficiently improve the company's resilience to peak events.
  - State what level of resilience the investment will deliver.
- 4.81 Given this lack of evidence, we cannot be confident that there is a need for proposed investment.
- 4.82 Should the company remedy these shortcomings and show that there is no additional headroom from its AMP7 improvements at Bewl and quantify the [REDACTED] investment impact on resilience in comparison to its proposed Bewl AMP8 investment it would be



appropriate for the company to look to use its contingent funding allowance to progress with its proposed investment.<sup>68</sup>

## **Service Reservoir capacity increases**

### **Final determinations**

4.83 In its business plan, South East Water requested investment at six service reservoirs to increase treated storage capacity by 50.5 Ml. The company requested an allowance of £34.014 million. In our final determination we undertook a deep dive assessment of the proposed service reservoir upgrades and raised concerns on cost efficiency and applied a 26.5% adjustment to submitted cost. In particular, the company did not provide sufficient and convincing evidence why the requested costs had increased by 36% during the business planning process. This resulted in an allowance of £25.000 million.<sup>69</sup>

### **Issues raised by disputing company**

4.84 In its statement of case<sup>70</sup>, South East Water raises a number of issues with our assessment, namely that it does not consider we have appropriately taken into account the additional evidence which it provided on the service reservoir costs and we have not understood the basis for increasing its cost proposal within the draft determination representation.

### **Our assessment**

4.85 Ofwat acknowledges the arguments brought forward by the company in its statement of case with respect to this scheme and we note the company has provided additional evidence that was not available at the time of the final determination. This new evidence addresses information we requested in response to the company's draft determination representations. Had this information been available at that time we would have reached a different outcome.

4.86 Within its statement of case the company includes new information relating to the number of data points used in the benchmarking and clarifies that the benchmarking is based upon 22 new service reservoir projects<sup>71</sup>. We welcome the clarification on the data points. The company also provides an additional report<sup>72</sup> from its benchmarking consultants. This report provides further detail of the benchmarking which has been

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<sup>68</sup> [OF-OA-022] Ofwat, 'PR24 final determinations: Expenditure allowances', December 2024, chapter 9.

<sup>69</sup> [OF-CA-147] Ofwat, 'PR24-FD-CA31-Water-Resilience-enhancement-expenditure-model\_redacted', December 2024, PR24CA31 – W-Resilience – SEW\_5\_SerRes and SEW\_2\_SerRes.

<sup>70</sup> [OF-OA-005] South East Water, 'PR24 Redetermination Statement of Case', March 2025, p.57.

<sup>71</sup> [OF-CA-195] South East Water, 'SEW – PR24 RD – Annex G – Enhancement Costs', March 2025, p.55.

<sup>72</sup> [OF-SEW-019] South East Water, 'Modelling Methodology & Service Reservoir Costs', March 2025.

undertaken and also provides additional information regarding increasing cost trends, although we note this only provides a qualitative description of increasing costs.

- 4.87 We continue to have concerns over the comparability of the datapoints and therefore the benchmark with the proposed upgrades to the size of service reservoirs. The company's proposed investment is expanding storage capacity at existing service reservoirs. However, the benchmark is based on building new service reservoirs. We would expect service reservoir upgrades to be lower cost than entirely new service reservoirs. Upgrades to existing service reservoirs present opportunities for cost savings on the installation of items such as telemetry, pipes, instrumentation, power supply and electrical equipment. The company does not explain why they do not take account of this.
- 4.88 While the company includes what it terms as a 6% stretch efficiency<sup>73</sup> this represents efficiency in delivery of the scheme and is not relevant to the reduced scope of increasing storage at service reservoirs compared to constructing a new service reservoir.
- 4.89 Overall, this new information increases confidence in the company's costs compared to what was available at the time of our final determination. Had this information been available at the time of the final determination we would likely have applied a challenge of 10% on cost efficiency, on each proposed service reservoir investment, to reflect that the company does not present evidence to demonstrate they have taken account of scope differences between increasing storage and building a new service reservoir.

## **Southern Water Treatment Works Upgrade (River Medway Scheme)**

### **Final determination**

- 4.90 In its representations South East Water requested £15.451 million and we allowed £8.684 million for a contribution to the [REDACTED] upgrade.
- 4.91 Southern Water has 75% ownership of [REDACTED], whilst South East Water owns the remaining 25%. At representations we assessed Southern Water's submission, South East did not submit evidence for this scheme.
- 4.92 We allowed £26.073 million to Southern Water to upgrade [REDACTED]. To calculate South East Water's 25% contribution to [REDACTED] we divided £26.073 million by three to get £8.684 million.

### **Issues raised by disputing company**

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<sup>73</sup> [OF-SEW-020] South East Water, 'SEWDD2a PR24 Draft Determination Cost Assessment', July 2024, Section 1.4.1.

4.93 In its statement of case the company rejected our approach to proportionally allocate Southern Water's adjustment to South East Water. The company raises the following issues:

- South East Water has no control over the costs, because the site is managed and owned by Southern Water.
- Funding for [REDACTED] WTW was covered through base at PR19, but now there is an unfunded step change in requirements to address DWI enforcement orders.
- South East Water cannot fund overspend from PR24 base expenditure because it is already stretched or ring fenced.

## Our assessment

4.94 We respond to each point in order:

4.95 South East Water is in management control of [REDACTED] WTW because 25% of the site supply goes to, and is paid for by, South East Water customers. As such it can influence the costs of the work and it could have supported the request for funding at [REDACTED] WTW but relied on Southern Water to evidence the claim for investment. Based on the evidence solely provided by Southern Water we cut the spending request. Proportional allocation of cost challenges was reasonable in this case.

4.96 We assessed PR19 base totex allowances and found that together with the PR24 uplift, there was sufficient funding to address the 2018 DWI estimated mandated capex of £39.551 million (uplifted to 2022-23 prices). This estimate is for activities to address the legal instrument, and covers contributions from Southern Water and South East Water. See paragraph our response to Southern Waters statement of case<sup>74</sup> for further information. At PR19 Southern Water requested £38.678 million in base (in 2022-23 prices) for [REDACTED]. This implies that South East Water submitted £12.893 million base in base at PR19 to cover the 25% contribution (in 2022-23 prices). At PR19 South East Water received a 1% cost challenge to its wholesale base requests, and Southern Water received a 7.6% cost challenge to its wholesale base request.<sup>75</sup> The PR19 allowance sufficiently funded South East Water to contribute 25% of required funds for maintenance to Southern Water. Both companies have been sufficiently funded, collectively, to address the DWI estimate of £39.551 million. In our response to Southern Water we also raised cost efficiency concerns with its PR24 request, and concerns that activities have been previously funded where DWI deadlines are pushed back into the 2025-30 period. These two concerns are the basis for cost challenges for Southern

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<sup>74</sup> Ofwat, 'PR24 redeterminations – response to Southern Water's statement of case', section 4, "Resilience enhancement at [REDACTED] water treatment works".

<sup>75</sup> [OF-CA-020] Ofwat, PR19-final-determinations-Securing-cost-efficiency-technical-appendix.pdf, p. 167, table A1.2, "Base Costs £m".

Water. It is logical to apportion these cost challenges from Southern Water to South East Water if the investments are for the same business case.

- 4.97 While we support companies to address DWI notices through enhancement, additional funding above this is only approved where there is a quantified step change improvement. Regulatory escalation from a DWI notice to a DWI Final Enforcement Order does not justify a step up to enhancement funds. Any additional requests for enhancement for this reason is considered previously funded. Both Southern Water's and South East Water's customers funded maintenance at the site through PR19 base (activities that were stipulated in the original DWI notice). There was no customer protection attached to this funding at the time, and we challenged part of the PR24 enhancement on this basis (that it was previously funded). In our final determinations we have allowed a 25% contribution which funds South East Water's requirements to contribute to the uplift. South East Water should remain accountable for any overspend and benefit from underspending. The company also benefits from cost sharing with customers. Setting allowances based on South East Water's full request, or setting a true up mechanism sets a perverse incentive which does not benefit customers supplied by [REDACTED] in the boundaries of South East Water zones. The remedies that the company has proposed gives no financial incentive for South East Water to address any outstanding issues at [REDACTED].
- 4.98 In addition, in its statement of case South East Water states that Southern Water has a higher cost sharing rate of 62.5% compared to South East Water which is 50%<sup>76</sup>. The company should clarify this statement. Its assumptions on this calculation seem incorrect. South East Water states that this is because Southern Water has 50% cost sharing on 75% overspend and 100% cost sharing on the 25% passed through to South East Water (50% $\times$ 75% plus 100% $\times$ 25% gives the 67.5%). South East Water states it has a cost sharing rate of 50%. The cost sharing rates for both companies are the same. Southern Water bears the risk on its share of the costs and South East Water bears the risk on its share of costs.

## Resilience interconnectors

### Final determination

- 4.99 Resilience interconnectors represent an area with material enhancement cost within the company's resilience and security investment requests. Resilience interconnectors are where companies identify additional interconnectivity in water supply networks as a solution to resilience risks. These are separate to the water available for use (WAFU) supply benefit of supply interconnectors. We assess these separately to other resilience

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<sup>76</sup> [OF-CA-195], South East Water, 'SEW – PR24 RD – Annex G – Enhancement Costs', March 2025, p.59, paragraph 279.

claims whilst still applying the enhancement assessment criteria through the deep dive approach.

4.100 In its draft determination representations, South East Water requested £41.177 million for nine resilience interconnectors schemes ("SEW\_1"). In our assessment we allowed £23.291 million funding for nine schemes and partially challenged three. The company also requested £87.608 million for seven supply interconnectors schemes which we reallocated to resilience interconnectors ("SEW\_2"). In our assessment we include an allowance of £66.504 million. We partially challenged one interconnector scheme and rejected three. We carried out a deep dive assessment on all proposed investment<sup>77</sup>.

**Table 4.6: Breakdown of cost challenges for enhancement resilience interconnectors**

Scheme breakdown	Enhancement requested (£m)	Enhancement allowed (£m)	Challenge as a % of request	Ofwat Views
Total programme	128.785	90.428	29.8%	
SEW_1 - Total	41.177	23.924 <sup>78</sup>	41.9%	
SEW_1 - Ashford supply resilience	20.585	4.537	78.0%	PR19 non-delivery
SEW_1 - Row Dow/Kemsing transfer	3.420	2.736	20.0%	Base drivers (climate change)
SEW_1 - Groombridge reinforcement	2.606	2.085	20.0%	Base drivers (climate change)
SEW_1 - Telham SR	2.662	2.662	0.00%	
SEW_1 - [REDACTED] to Halling systems	[REDACTED]	[REDACTED]	[REDACTED]%	
SEW_1 - Windover SR	1.086	1.086	0.00%	
SEW_1 - Tonbridge to Bloodshots MR	0.690	0.690	0.00%	
SEW_1 - Kilnwood supply SPoF	2.806	2.806	0.00%	

<sup>77</sup> [OF-SEW-021] Ofwat, PR24-FD-CA94-Water-Resilience-interconnectors-v3, tabs "SEW\_1" and "SEW\_2", March 2025.

<sup>78</sup> The current allowance in [OF-SEW-021] "PR24-FD-CA94-Water-Resilience-interconnectors-v3" is £23.921 million. On review, the allowance should be £23.924 million. This discrepancy is due to a rounding error.

Scheme breakdown	Enhancement requested (£m)	Enhancement allowed (£m)	Challenge as a % of request	Ofwat Views
SEW_1 – Thanington WTW to Dunkirk	6.486	6.486	0.00%	
SEW_2 – Total	87.608	66.504	24.1%	Reallocation to supply interconnectors
SEW_2 – Surrey Hills to fleet	43.694	26.596	39.1%	Misallocation and PR19 non-delivery
SEW_2 – Oakhanger to Alton	2.713	0.000	100.0%	Misallocation and unquantified single point of failure risk
SEW_2 – Darnley Driver booster	1.167	0.000	100.0%	Misallocation and base drivers (population growth)
SEW_2 – Poverty Bottom	0.126	0.000	100.0%	Misallocation and originally considered driven by base factors, new information since has been provided
SEW_2 – Greywell to Swaineshill	12.433	12.433	0.00%	Misallocation
SEW_2 – Ewshot to Itchel	5.173	5.173	0.00%	Misallocation
SEW_2 – Greywell to Whitedown	22.302	22.302	0.00%	Misallocation

## Issues raised by disputing company

4.101 In its statement of case South East Water raises three key issues with our assessment.

It disagrees with our allocation of seven schemes from supply interconnectors into resilience interconnectors.<sup>79</sup> It also disagrees with our assessment of PR19 base overlap on the basis it has substituted PR19 schemes and delivered equivalent outcomes and our justification that customers should not pay twice.<sup>80</sup> The company also has issues with the other base adjustments where we have identified base drivers in our assessment for the need for enhancement.<sup>81</sup>

<sup>79</sup> [OF-CA-195], South East Water, SEW – PR24 RD – Annex G – Enhancement Costs, March 2025, p. 20.

<sup>80</sup> [OF-CA-195], South East Water, SEW – PR24 RD – Annex G – Enhancement Costs, March 2025, pp. 22–24 and pp. 27–29.

<sup>81</sup> [OF-CA-195], South East Water, SEW – PR24 RD – Annex G – Enhancement Costs, March 2025, pp. 21–22 and pp. 26–27.



## Our assessment

### Re-allocation from supply interconnectors

- 4.102 We allocated the investment (£87.608 million) associated with the seven interconnectors in the company's SEW\_2 programme from supply interconnectors to resilience interconnectors at both draft and final determination. The company failed to submit sufficient and convincing evidence these schemes provided a supply benefit aligned with water resources planning.
- 4.103 Key to this case is that, regardless of whether the investment was assessed as a supply or resilience interconnector, we would make the same adjustments for PR19 funding and base overlap as we did in the final determination. The allocation and assessment make no impact here. However, we respond to the allocation challenge raised by the company.
- 4.104 Schemes in WRMPs are expected to deliver quantified water available for use (WAFU) benefits to a company's zonal supply demand balance. The supply demand balance is calculated by companies at a water resource zone level in their WRMPs. Where companies face a deficit (ie forecast demand is higher than forecast supply) companies identify options (ways to increase supply or reduce demand) to improve the balance. The calculation of WAFU is the supply side availability and undertaken at a water resource zone level.
- 4.105 This is described in the joint Ofwat, Environment Agency and Natural Resources Wales Water Resources Planning Guideline.<sup>82</sup> The zonal supply is usually calculated by companies using system simulation behavioural models. These are relatively simplified versions of the company system including raw water sources, connections and demand centres. Demands are ramped up until a demand centre cannot be sourced with water anymore. The resultant supply level is deemed the current amount of supply at a water resource zone level.
- 4.106 Although South East Water claims that these schemes deliver zonal WAFU, it also describes them as sub-zonal. The company has used much more detailed modelling to generate small scale deficits under different conditions and added these to the zonal scale calculations used elsewhere in the WRMP. This mixing of methodologies is not an

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<sup>82</sup> "You can present options that do not provide specific supply-demand balance benefits but offer wider resilience benefits or meet specific legislative requirements that form part of your best value plan. These options can be presented as part of your WRMP, however will need to be discussed with Ofwat for inclusion in the business plan process...To be considered for supply demand balance enhancement funding, a scheme should have some benefit to one or more components of the supply-demand balance. For example, through providing deployable output or reducing outage." Ofwat, Environment Agency, Natural Resources Wales, Water resources planning guideline – GOV.UK, updated April 2023.

approach taken by other companies. The company then presents these summed sub-zonal deficits and benefits of sub-zonal interconnectors in WRMP data tables.

- 4.107 It is important for the WRMP process that the need (scale of deficit) is consistently calculated as the options and their WAFU benefits are compared on an assumed like for like basis. They all provide addition water or reduce demand under the same conditions (e.g. drought level, zonal).
- 4.108 It is only South East Water that claims to struggle to justify investment at a sub-zonal level due to the WRMPs guidance. We have engaged with the company on several occasions about the perceived issues it has with the WRMP and business plan submission process. We have provided steer to the company on how best to approach its WRMP modelling, and alternative routes to request this type of funding. We have suggested to the company that its water resource zones may need splitting, or that these schemes are actually to improve resilience or are environmental investment (to address Water Framework Directive issues).<sup>83</sup>
- 4.109 South East Water's uses the example of an abstraction loss at a site due to WINEP to explain how its sub-zonal deficits are generated. This loss of source would impact the zonal modelling as described above and therefore align with WRMP processes. As a result, we are concerned about how the company approaches its WRMP modelling.
- 4.110 We acknowledge that some companies identify localized issues caused by abstraction licence reductions driven by WINEP, which don't impact zonal WAFU, but then appropriately request funding via the Water Framework Directive (WFD) enhancement line. Where it was evident that a South East Water scheme had another valid enhancement driver, such as WFD, we assessed it on its individual merits and in many cases these schemes are funded in full (for example Ewshot to Itchel interconnector was solely driven by impacts of abstraction reductions). This also ensured consistency with how we treated similar schemes from other companies.
- 4.111 Some schemes are more comparable with schemes covered under resilience, and unrelated to the supply demand balance, at either a zonal or sub-zonal level. For example, we had concerns over the need for enhancement relating to the Oakhanger to Alton scheme. The company proposes to extend the water main to address a single point of failure risk to Basingstoke.<sup>84</sup> The Bloodshots to Darnley drive scheme is an upgrade to larger variable speed pumps that address a single point of failure hazard at a service reservoir.<sup>85</sup> Other companies (Dŵr Cymru, Anglian Water and Affinity Water)

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<sup>83</sup> This includes a letter on Accelerated infrastructure delivery – water resilience schemes sent on 26 May 2023, and two calls post PR24 draft determinations on 1 August 2024 and 12 August 2024.

<sup>84</sup> [OF-CA-195] South East Water, 'SEW – PR24 RD – Annex G – Enhancement costs', March 2025, p.21.

<sup>85</sup> [OF-CA-195] South East Water, 'SEW – PR24 RD – Annex G – Enhancement costs', March 2025, p.22.

submitted schemes addressing single points of failure hazards through resilience,<sup>86</sup> therefore our reallocation ensures a like for like assessment of costs and evidence.

- 4.112 The company states that if the supply interconnector model implies its schemes are efficient it should get the modelled allowance. We tested the cost efficiency of interconnectors assessed in the WFD and resilience interconnector enhancement areas using the supply interconnector model. This was a test to support our assessment – noting our preference for benchmarking where possible. However, we note in the final determination we removed these data points from the supply interconnector model due to concerns with size and benefit comparability with other datapoints in the model.<sup>87</sup>
- 4.113 Supply interconnector schemes are benchmarked based on WAFU benefit measured over a dry year annual average scenario. This will be lower than pipeline capacity, which is used to size the pipe costs that are included in the WFD and resilience interconnector lines. Using a higher value for the benefit (eg pipeline capacity) in the model would naturally result in higher modelled allowances and implied efficiency of schemes tested within them. The supply interconnector schemes are also likely to have higher costs as this is the sustainable replacement of water in one zone from another – and its clear its balanced in zonal models and data tables. We applied the test consistently to all companies and no other disputing company has stated that the model should be used to set allowances. We have not applied a cost efficiency challenge on South East Water's resilience interconnector schemes, we only challenged the need for enhancement.<sup>88</sup>

### Interaction with PR19 funding and delivery

- 4.114 At PR24 we made a 78% adjustment to South East Water's Ashford scheme (from a request of £20.585 million) and a 39.1% adjustment to the Surrey Hills to Fleet scheme (from a request of £43.694 million) to remove overlaps with previously funded schemes. It is not appropriate for customers to pay twice for the same outcome.
- 4.115 In its statement of case the company disagrees with these adjustments. It claims to have overspent at a programme level and achieved the same outcomes for customers at PR19. The company does not agree with Ofwat adjusting PR24 allowances by removing overlaps with PR19 funding. It states that this is effectively setting a price control deliverable on a retrospective basis since the allowances were not ringfenced, or the schemes were not specified in price control deliverables at PR19.<sup>89</sup>
- 4.116 The company states that the PR19 adjustment for its Ashford scheme is flawed as the PR19 scheme is not the same. The PR19 scheme was to bring supply from the north-

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<sup>86</sup> [OF-CA-147] Ofwat, 'PR24-FD-CA31-Water-Resilience-enhancement-expenditure-model\_redacted.xlsm', tab "Scheme level costs".

<sup>87</sup> [OF-OA-023] Ofwat, 'PR24 final determinations: Enhancement cost modelling appendix', December 2025, p.142.

<sup>88</sup> [OF-CA-279] Ofwat, 'Water- Resilience Interconnectors: enhancement expenditure model', February 2025, tabs "SEW\_1" and "SEW\_2".

<sup>89</sup> [OF-CA-195] South East Water, 'SEW- PR24 RD- Annex G- Enhancement Costs', March 2025, p.23.

east from Canterbury into Ashford, this delivers the same outcome to supply resilience as the PR24 Ashford scheme. It states that it has not delivered the PR19 scheme because it was not the best long-term solution. At PR24 the company is requesting funding to deliver an equivalent outcome which is to bring supply from the northwest into Ashford, from Butler water treatment works.<sup>90</sup> Our 78% adjustment to the Ashford supply resilience scheme is therefore to account for underspend and non-delivery of this overlapping scheme from PR19. The PR19 allowance was £13.600<sup>91</sup> million (2017-18 prices), and the company has not spent this on the Canterbury to Ashford scheme. South East Water states that it used the £13.600 million funding for the Butler water treatment works and the Wellwood to Potters main. Both these schemes were already funded at PR19 which is why we adjusted for PR19 underspend at Ashford.<sup>92</sup> The Wellwood to Potters main also had an attached bespoke end of period financial ODI, equivalent to a PCD at PR24.<sup>93</sup> We removed £13.600 million PR19 underspend for Ashford plus 18% to convert to 2022-23 prices, totaling £16.048 million.

4.117 We have also adjusted for base overlap on the Surrey Hills to Fleet scheme. South East Water states this adjustment is flawed because its PR19 underspend was redirected to solutions with equivalent outcomes.<sup>94</sup> The Surrey Hills to Fleet PR19 funding was to deliver 14Ml/d to the Basingstoke area by 2025. It states the budget was spent on environmental monitoring of the Blackwater Estuary to determine if it can find a route and acceptable pipe sizing.<sup>95</sup> This is a different geographical area to Basingstoke and does not deliver equivalent outcomes to supply resilience such as Mld benefits. The company was funded £17.140 million at PR19 and has underspent by £14.490 million (both in 2017-18 prices). South East Water states that differences in spending do not matter at a scheme level as it has overspent at a programme level. However South East Water has not provided sufficient and convincing evidence that spend has been redirected to more effective solutions achieving equivalent or better outcomes (ie risk reduction). The programme level overspend is based on its view of resilience and growth expenditure combined, with the overspending on the growth programme. The 39.1% adjustment is from removing £14.490 million underspend plus 18% to convert (using CPIH index) to the 2022-23 price base, totaling £17.098 million. From the £2.650 million the company has spent at PR19 (17.140-14.490) it provides costing for only £400,000 of its scope, it is not clear what the remaining £2.250 million was spent on (which is £2.655 million in 2022-23 prices).

<sup>90</sup> [OF-CA-195] South East Water, 'SEW- PR24 RD- Annex G- Enhancement Costs', March 2025, p.28.

<sup>91</sup> [OF-SEW-012] Ofwat, Query response: OFW-OBQ-SEW-124.

<sup>92</sup> [OF-SEW-012] As confirmed in query OFW-OBQ-SEW-124, table 1, in the following quote: " funding for these schemes has been used on the Butler WTW, the Wellwood to Potters main and the modelling work required to define the new strategy".

<sup>93</sup> [OF-CA-280] Ofwat, 'PR19 final determinations- Consolidated PR19 final determinations: South East Water- Outcomes performance commitment appendix', December 2023, p.122.

<sup>94</sup> [OF-CA-195] South East Water, 'SEW- PR24 RD- Annex G- Enhancement Costs', March 2025, p.91.

<sup>95</sup> [OF-SEW-012] Ofwat, Query response: OFW-OBQ-SEW-124, table 1, quote " Budget spent has been on environmental monitoring of the Blackwater SSSI to determine if we can find a route and acceptable pipe sizing.".

4.118 We acknowledge that under our totex and outcomes frameworks companies are able to use their expenditure allowances to meet their outcomes in a flexible way. However, this should not come at the expense of asking customers to pay twice for previously funded improvements. Despite being given adequate opportunity, South East Water has not demonstrated that its proposed PR24 enhancements do not overlap with previously funded PR19 investments which deliver similar outcomes.<sup>96</sup>

### Need for enhancement adjustments

4.119 At PR24 we made adjustments to five other schemes because the company had not justified the need for enhancement. The five schemes were: Row Dow, Groombridge, Darnley, Poverty Bottom and Oakhanger. At Row Dow and Groombridge we challenged 20% of the respective requests of £3.420 million and £2.606 million. For Darnley, Poverty Bottom and Oakhanger we rejected in full the need for an enhancement uplift, from respective requests of £2.713 million, £1.167 million and £0.126 million.<sup>97</sup>

4.120 We had concerns that the Row Dow and Groombridge schemes were to address hazards caused by extreme weather events, which other companies address through base allowances. Both interventions at these sites include upgrading booster pumping stations and laying or reinforcing new mains. We had some concerns that there was not sufficient and convincing evidence that the investment is already covered by base allowances. We made a top-down adjustment of 20% on our assessment of the need for enhancement. We continue to consider that upgrading the pumping stations should typically be covered through base maintenance allowances. South East Water provides no additional evidence in its statement of case to justify the need for an enhancement uplift.

4.121 The Darnley scheme is to increase pump capacity to meet predicted increases in peak demands. Investment to address growth in demand is covered by base allowances (via the increase in the scale parameters in the base cost models). The company does not provide any additional evidence on why this investment is not covered by base allowances.

4.122 The Poverty Bottom scheme includes £126,000 for rezoning a sub-zone and installing motorized valves. South East Water states this is due to abstraction sustainability reductions associated with chalk stream protection.<sup>98</sup> In its representations of the PR24 draft determinations, the company did not identify which sites would have these reductions. We rejected the claim at final determinations because there was a lack of evidence there was a need for enhancement expenditure. In its statement of case, it states the groundwater sources at Poverty Bottom, Cow Wish and Rathfinney have

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<sup>96</sup> [OF-CA-001] Ofwat, 'Creating tomorrow, together: Our final methodology for PR24 – Appendix 9 Setting expenditure allowances' December 2022, pp.25-26.

<sup>97</sup> [OF-CA-279] Ofwat, 'Water- Resilience interconnectors: enhancement expenditure model', February 2025, tabs: "SEW\_1", "SEW\_2" and "Scheme level assessment".

<sup>98</sup> [OF-CA-195] South East Water, 'SEW – PR24 RD – Annex G – Enhancement costs', March 2025, p.22.

sustainability reductions with a potential loss of more than 3.7 Ml/d between 2030–40. The impact of the abstraction reduction and timing are still presented in uncertain terms. If the schemes were required for 2030 then we would have expected the company to have confidence in the requirements by now. We accept this evidence for the need for enhancement because it clarifies in its statement of case which sites will be impacted by the abstraction reductions.<sup>99</sup>

4.123 At PR24 final determinations we had concerns over the need for enhancement for the Oakhanger to Alton scheme. The scheme is to extend the water main to address a single point of failure risk to Basingstoke.<sup>100</sup> There was no quantified risk assessment for the likelihood of the single point of failure risk. In terms of its preferred solution to extend the water main, there was also no optioneering and cost efficiency evidence provided. In its statement of case the company states that the single point of failure risk is linked to the loss of Lasham WTW from March 2030, which is a consequence of abstraction reductions. As the company provides no quantified risk assessment we continue to reject the need for enhancement for this scheme.

## **£50 million contingent resilience allowance**

### **Final determination**

4.124 To address residual risk that additional resilience funding is required during 2025–30 we allowed £50 million contingent funding to the company. This was subject to South East Water proving it is spending its ex ante enhancement allowances, and demonstrating its resilience programme is on target.<sup>101</sup> In our final determinations we said the funding is contingent on the following requirements:

- South East Water submits a fully justified case for schemes that delivers agreed investment to our satisfaction. We will return the £50 million, in full or in part, to customers if it fails to meet this criteria in its submission.
- It must be requested no earlier than November 2026.
- The proposal must include an associated PCD.

4.125 In a query response<sup>102</sup> we provided additional guidance on how approval for contingent funding would work, in practice.

### **Issues Raised by Disputing Company**

4.126 The company raises five issues in relation to the contingent allowance.

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<sup>99</sup> We still highlight that this should be presented as a WFD enhancement investment (as there is no zonal supply demand balance impact) as other companies have done at PR24.

<sup>100</sup> [OF-CA-195] South East Water, 'SEW – PR24 RD – Annex G – Enhancement costs', March 2025, p. 21.

<sup>101</sup> [OF-OA-022] Ofwat, 'PR24 final determinations-Expenditure allowances', December 2024, pp.226–227.

<sup>102</sup> [OF-CA-276] OFW-FD-SEW-002, January 2025.



- 4.127 The company states that it is not clear if the contingent allowance can be linked to previously disallowed schemes (such as Bewl water treatment works) or if it must be schemes to address new risks.<sup>103</sup>
- 4.128 The company states that there should not be a requirement that the current delivery plan is on track, and that if a new scheme is needed, efficient and deliverable, we should accept the scheme irrespective of the delivery status of other resilience schemes.
- 4.129 The company states that substantial new evidence would not be available by November 2026, in addition to what had been submitted already. It further states that if the company waits later in the AMP to submit its request the window for AMP8 delivery would become impractically narrow.
- 4.130 The company states that the time required to submit the required information and analysis followed by a four month review creates risk of delay.
- 4.131 The company states that the CMA should either increase ex ante allowances, or contingent allowances put in place that are "fit for purpose" which is described as "clear, objectively understood, transparent, proportionate and targeted standards". The company states this should include a focus on ensuring "predictability and coherence, adaptability and efficiency, minimising regulatory burden and avoiding unnecessary costs".<sup>104</sup>

## Our Assessment

- 4.132 **Bewl water treatment works.** We included the contingent allowance for South East Water given our concerns over the quality of the evidence provided in the company's resilience cases submitted at draft determination representations, which made it unclear whether additional investment was required. The contingent allowance is not intended to address the overall water enhancement cost gap. It relates only to resilience investment. We have clarified in a query response the contingent allowance can be linked to previously disallowed schemes such as Bewl.<sup>105</sup> Where we have stated concerns over Bewl, the company should provide compelling evidence to address these concerns.
- 4.133 **Requirement on delivery of enhancement programme.** The contingent allowance should not distract South East Water from delivering its substantial PR24 enhancement and resilience expenditure programmes. We therefore expect the company to submit its contingent funding request no earlier than November 2026. This will provide the

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<sup>103</sup> [OF-OA-003] South East Water, 'SEW – PR24 RD – Statement of Case – CONFIDENTIAL', March 2025, p.47.

<sup>104</sup> [OF-OA-003] South East Water, 'SEW – PR24 RD – Statement of Case – CONFIDENTIAL', March 2025, p.49.

<sup>105</sup> [OF-CA-276] Ofwat, Query response: OFW-FD-SEW-002, January 2025.

company with sufficient opportunity to demonstrate that it is spending its enhancement allowances and the delivery of its resilience programme is on track.<sup>106</sup>

- 4.134 **Availability of evidence for assessment.** South East Water needs to demonstrate that any additional resilience investment through the contingent allowance meets the same enhancement investment criteria as other PR24 investment of need, best option, cost efficiency and customer protection. We consider that November 2026 provides the company with sufficient time to develop sufficient and convincing evidence to justify the additional expenditure.
- 4.135 **Risk of delay.** We consider that November 2026 provides the company sufficient time for the company to provide appropriate evidence to support its proposed investment. We consider that our assessment deadline of four months, commencing once all required information is received, provides a realistic timeframe for us to carry out a focused assessment on its resilience request. We encourage the company to make its submission as early as possible after November 2026 to avoid delaying investment.
- 4.136 **Approach to contingent allowance.** We consider that our approach to setting a contingent allowance, balances the risks of not providing the company with sufficient investment for resilience, with the need for the company to provide adequate justification for that investment. We consider that our criteria meet the principles of good regulatory practice<sup>107</sup> and that we should not reduce the standard of evidence we should apply to this investment. We do not consider that providing additional ex ante allowances would be appropriate based on the quality of evidence submitted at draft determination representations and in the statement of case.

## Lead

### Final determinations

- 4.137 The UK Government SPS for Ofwat states that “safe, clean drinking water is vital for public health and the wellbeing of our society. The Government supports action by the industry to trial approaches to reducing exposure of lead to customers from drinking water, from a public health perspective”.<sup>108</sup>
- 4.138 The lead standard in drinking water is 10 ug/l in England and Wales, although the Welsh Government ambition is to achieve levels as low as reasonably practicable, which is considered to be 5 ug/l.<sup>109</sup> The DWI's normal point of compliance measurement for these

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<sup>106</sup> [OF-CA-278], Ofwat, 'PR24 final determinations: Delivery plan guidance March 2025', pp.27-38.

<sup>107</sup> [OF-CA-281] Better-Regulation-Task-Force-Principles-of-Good-Regulation, 2003.

<sup>108</sup> [OF-SEW-040] Department for Environment, Food & Rural Affairs, 'Policy Paper – February 2022: The Government's Strategic Priorities for Ofwat', March 2022.

<sup>109</sup>[OF-SEW-041] European Union, DIRECTIVE (EU) 2020/2184 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL OF 16 DECEMBER 2020 ON THE QUALITY OF WATER INTENDED FOR HUMAN CONSUMPTION (RECAST), 2020.

standards is the customer's cold kitchen tap<sup>110</sup>, referred to as 'consumer's taps' in legislation.

- 4.139 Reducing exposure to lead in drinking water can be achieved by either removing lead from the system through pipe replacements (or relining) or treating water with orthophosphate to reduce plumbosolvency (lead leaching). When companies replace a lead communication pipe it only meets the enhancement need in this area if it is for water quality (ie lead reduction) purposes, despite other benefits, such as leakage or addressing pressure issues. As part of the trials as referenced in the UK Government SPS some companies propose lead supply pipe (either external only or external and internal) replacements to remove lead piping before the compliance point at targeted properties (i.e. customers and/or schools/nurseries) or other trials to reduce lead below the current standard of 10 ug/l.
- 4.140 In our final determination we provided benchmark allowances for the replacement/ relining of lead communication and supply pipes.<sup>111</sup> South East Water requested £24.320 million for 'other lead reduction related activities' not associated with our modelled allowance for communication and supply pipes.
- 4.141 We shallow dived elements associated with lead sampling, lead locator spatial assessment, phosphate disengagement trial and associated on-costs, and made an allowance of £6.264 million applying a shallow dive efficiency factor of 10%.<sup>112</sup>
- 4.142 We deep dived elements associated with stop tap and trial hole physical surveys, and associated on-costs of £17.360 million. As part of the assessment, we raised concerns on investment need, best option and cost efficiency and applied a 100% adjustment.<sup>113</sup> Table 4.7 below summarises South East Waters lead programme, highlighting the company was provided with an above ask allowance for 'External Supply Pipes' of £0.678 million based on the 368 of the assets South East Water proposed to replace/ reline in as part of its AMP8 programme.

**Table 1.7 showing a summary of South East Water's lead programme in terms of area, units, request and allowance<sup>114</sup>**

<sup>110</sup> [OF-SEW-042] Department for Environment, Food & Rural Affairs, 'The Water Supply (Water Quality) Regulations 2016 for England and The Water Supply (Water Quality) Regulations 2018 for Wales, 2018.

<sup>111</sup>[OF-OA-022] Ofwat, 'PR24 Final Determinations- Expenditure Allowances', December 2024, Section 3.7.2 Lead, pp.211-216.

<sup>112</sup> [OF-SEW-043] Ofwat, 'Water- Lead: enhancement expenditure model', December 2024, sheet:Other lead reduction worksheet.

<sup>113</sup>[OF-SEW-043] Ofwat, 'Water- Lead: enhancement expenditure model', December 2024, sheet: SEW\_Lead surveys'.

<sup>114</sup> [OF-SEW-043] Ofwat, 'Water- Lead: enhancement expenditure model', December 2024, sheet: Allowance.

Lead Request Area	Units (No.)/ Length (m)	Cost Request (£m)	Cost Allowance (£m)
Comms Pipes	0/ 0	0	0
Internal Supply Pipes	0/ 0	0	0
External Supply Pipes	368/ 2,024	0	0.678
Other Lead Reduction Activity	N/A	24.320	6.264

4.143 Our concerns on the lead survey, sampling and associated elements were that they went beyond the requirements of the Strategic Priority Statement issued by Defra<sup>115</sup> which was to trial approaches to reducing exposure of lead to customers from drinking water. We consider that the stop tap, trial hole elements and associated on-costs do not reduce water quality risks to customers and that there is insufficient evidence provided by the company to demonstrate a step-change in service level delivered.

4.144 In addition, we raised concerns that South East Water's metering programme provided opportunities to assess lead risk in a proportion of communication/ supply pipes – however the company provided no assessment of this and that the use of lead locator/prediction models would allow lead surveys and stop gap trials to be targeted.

4.145 There was a lack of evidence on cost calculations/ key assumptions and external assurance of scheme costs raising concerns with cost efficiency. The company also designates all scheme costs under 'Other lead reduction activity' costs as capex enhancement. Ofwat would disagree with this designation, it is more appropriate to classify costs as opex enhancement as work such as stop tap surveying, sampling, trial hole and programme management costs are day-to-day activities and not tangible capital assets with a lifespan greater than a year.

### Issues raised by disputing company

4.146 In its statement of case, the company raises three issues with our assessment based on the need, best option and cost efficiency criteria.<sup>116</sup>

- Under investment need, South East Water states that the Defra SPS supports the work being undertaken and disputes Ofwat's interpretation of work not being a 'trial' as it is industry-leading and new.

<sup>115</sup> [OF-SEW-040] Defra Policy Paper – February 2022: The Government's Strategic Priorities for Ofwat, February 2022.

<sup>116</sup> [OF-CA-195] South East Water, SEW- PR24 RD- Annex G- Enhancement Costs, March 2025, pp.11-14.

- In terms of best option, South East Water raises a concern on Ofwat's support for 'Lead Predictor Models', stating that it is a common approach and not effective at accurately locating lead which leads to inefficiencies, lead risk to population and does not provide sufficient resolution to support phosphate disengagement.
- South East Water also raise concerns on the 'shallow dive' efficiency challenge applied to lead related enhancement requests <£10 million. This will be addressed separately as the outcome is relevant to multiple areas of expenditure.<sup>117</sup>

## Our assessment

4.147 We continue to consider that South East Water has not justified the stop tap and trial hole physical surveys and that we should apply the shallow dive adjustment to South East Water's other lead costs.

4.148 Firstly, regarding investment need, we do not consider a lead survey to be a 'trial' approach and therefore it is not consistent with the Defra Strategic Priority Statement.<sup>118</sup> Stop-tap surveys and trial holes are both well-established methods for the identification of lead in the water industry. The 'industry-leading' or 'new' element is only relevant to the intention to identify all lead service pipes within the area served. We do not consider there is a need to survey all company and service pipes (971,000 properties and 893,00 stop taps) is an appropriate approach to be necessary to identify lead.

4.149 South East Water also references an internal target to be lead-free by 2050, highlighting the proposed approach to lead surveys/ data collection is necessary to meet this target. This is an internal goal with no regulatory oversight and therefore there is no method of holding the company accountable in the instance of non-delivery. The company also suggests minimal replacement of lead service pipes (excluding a number of external supply pipes) within the same AMP. The goal to be lead-free surpasses the intentions of the SPS.

4.150 South East Water references the DWI Chief Inspectors Report 2022<sup>119</sup> as providing support for the proposed approach to lead surveys – "South East Water proposes to survey all service pipes (communication and supply) within the company area, this will provide a wealth of information which can be used for future targeted work on replacements." Whilst this statement provides some support, it was made independently of knowledge of a significant enhancement request, or company identifying synergies, opportunities or smarter approach at eliciting this data.

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<sup>117</sup> [OF-OU-070] Ofwat, 'PR24 redeterminations – expenditure allowances – common issues', April 2025, p.283.

<sup>118</sup> [OF-SEW-040] Defra, Policy Paper – February 2022: The Government's Strategic Priorities for Ofwat.

<sup>119</sup> [OF-SEW-044] Drinking Water Inspectorate, Drinking Water 2022– A report by the Chief Inspector of drinking water' 2022, p.18.



- 4.151 South East Water also references the wording in DWI's AMP8 Lead Strategy Undertaking to support this approach – "Conduct a survey of all company and service pipes to determine composition and the location of lead pipes in AMP8".<sup>120</sup> Although this wording supports elements of the scheme, it is unclear whether the intention was that customers would be supporting this via significant enhancement allowances. We recommend the CMA to engage with DWI to discuss this further, as the costs and benefits may not have been made clear. It also appears that the requirement to survey all service pipes is unique to South East Water. Surveying all service pipes to assess for lead appears excessive. This does not appear to reflect that the installation of lead pipework has been banned for properties since 1970.<sup>121</sup>
- 4.152 South East Water states that it is not possible to identify lead pipes when undertaking metering, as suggested by Ofwat, as lead identification and metering are separate activities. It states that most meter replacements are 'screw-in' jobs not exposing pipework, visual identification is difficult/ inaccurate and onsite tests for lead are not available. We continue to consider that metering presents an opportunity for the company to improve its understanding of lead risk where practical, without the need for a significant enhancement request. For context, South East Water renewed a total of 44,043 meters over its household and non-household properties between the five reporting years from 2019–20 to 2023–24.<sup>122</sup> If opportunities had been sought to examine and reduce lead risk during these activities, it would likely reduce the need for significant allowance requests for lead surveys moving forward. To further add to this point, South East Water has committed to install over 275,000<sup>123</sup> smart meters at its household properties in the 2025–30 period. If this programme was to be combined with lead spatial assessment highlighting lead risk areas on the network, it would reduce the need for customers to cover costs for extensive lead surveys.
- 4.153 Furthermore, other companies have identified and proactively replaced lead during other network activities (e.g. mains replacement, leakage), therefore we do not fully accept South East Water's points on why this has not been done alongside their metering programme. Further, the DWI AMP8 Lead Strategy Undertaking for South East Water, includes a reference to "Opportunistic replacement of lead pipes during mains replacements", which supports the point that 'other network activities' can be used as a means to understand and reduce lead risk.
- 4.154 On best option, the company raises concerns with our support for lead predictor models. South East Water states that while this is a common approach, continuing to use this approach does not give the industry an opportunity to move on from it. We continue to consider that lead predictor models are a well-established, reliable,

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<sup>120</sup> [OF-SEW-045] Drinking Water Inspectorate, 'South East Water Limited – AMP8 Lead Strategy (SEW-2023-00016)', April 2024.

<sup>121</sup> [OF-SEW-046] Drinking Water Inspectorate, 'Lead in Drinking Water'.

<sup>122</sup> [OF-SEW-047] Ofwat, 'Meter renewals cost adjustment model', December 2024, Worksheets: 'Household rates' & 'Non-household rates'.

<sup>123</sup> [OF-SEW-048] South East Water. Water Resources Management Plan 2025 to 2075, pg.124.



efficient method for identifying likely areas of lead service pipe within a supply system. We acknowledge it should be used in coordination with lead surveys to be fully effective.

4.155 Lastly, South East Water is an outlier in terms of allowance request, despite other companies having similar undertakings agreed with DWI. The defining element of South East Water's AMP8 Lead Strategy Undertaking is the reference to survey all service pipes – other elements however will largely be the same e.g. conduct phosphate disengagement trial, lead and regulation 27 risk assessments and to keep company strategy on public health with respect to lead under review. Table 4.8 below summarises the allowance request for 'Other Lead reduction activity' by company, highlighting the scale of allowance request from South East Water.

**Table 4.8: showing the allowance request by companies for 'Other Lead reduction activity'<sup>124</sup>**

Company	Totex request (£m)
ANH	1.350
WSH	0.000
HDD	1.778
NES	0.000
SVE	7.550
SWB	0.000
SRN	0.000
TMS	8.625
NWT	0.000
WSX	0.000
YKY	0.000
AFW	0.000
BRL	0.000
PRT	0.000
<b>SEW</b>	<b>24.320</b>
SSC	0.000
SES	0.652

## Security and Emergency Measures Direction (SEMD) – Alternative Water Supply (AWS)/ Emergency Planning

### Final determination

4.156 Under section 208 of the Water Industry Act 1991, the Secretary of State and Welsh ministers can give English and Welsh water companies directions in the interests of

<sup>124</sup>[OF-SEW-043] Ofwat, 'Water- Lead: enhancement expenditure model', December 2024, sheet: Allowance.

national security (for water and wastewater assets) or for the purpose of mitigating the effects of any civil emergency.**Error! Bookmark not defined.**

4.157 Transposed from the requirements outlined in the section 208, the Security and Emergency Measures Direction 2022<sup>125</sup> outlines requirements on water companies to prepare alternative water supplies to maintain a minimum supply in the event of piped water supply failure. The intention behind this legislation is to maintain a continuous supply of water to mitigate the effects of civil emergencies. [REDACTED]

[REDACTED] This can include providing water to customers through tankering, bowzers or bottled water.

4.159 In our final determinations, we allowed £10.858 million out of a request of £12.064 million after applying a 10% adjustment due to concerns over cost efficiency through our deep dive assessment process. We applied a cost challenge as South East Water did not provide sufficient detail of a bottom-up approach to demonstrate scheme element costs are efficient.<sup>127</sup>

### Issues raised by disputing company

4.160 In its statement of case, the company raised three main issues<sup>128</sup> with our deep dive assessment approach and the resultant application of a 10% cost efficiency challenge.

4.161 Firstly, South East Water states why the scheme is required and that it has concerns it is unable to meet its alternative water supply requirements under Security and Emergency Measures Direction 2022 with the 10% challenge. It states that following seasonal weather events impacting on water supply, [REDACTED]

The company

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<sup>125</sup> [OF-SEW-049] UK Public General Acts, 'Water Industry Act 1991: Section 208 The Security And Emergency Measures (Water And Sewerage Undertakers And Water Supply Licensees)' Direction 2022, 4.(4)(b).

<sup>128</sup> [OF-CA-195] South East Water, 'SEW- PR24 RD- Annex G- Enhancement Costs', March 2025, pp.46-47.

references a Security and Emergency Measures Direction DWI Undertaking in support of this.<sup>129</sup>

4.162 Secondly, in response to our cost efficiency concerns, South East Water states that it has assessed scheme costs via a bottom-up approach – "We have used a bottom-up approach to estimate the costs of the scheme, based on CAPEX for vehicles and building procurement".<sup>130</sup>

4.163 And finally, South East Water states that elements of the alternative water supply are bespoke and as such are unable to be benchmarked<sup>131</sup>. South East Water states that its unit cost database does not have detailed information on all costs within the scheme and that there are limited comparable schemes for benchmarking.<sup>131</sup>

## Our assessment

4.164 We consider that our cost efficiency challenge of 10% at final determination continues to be justified.

4.165 Firstly, regarding investment need, we acknowledge that the investment is required under Security and Emergency Measures Direction 2022. As such we did not apply a challenge to costs based on the justification of need. [REDACTED] companies, which makes South East Water an outlier in the industry [REDACTED] <sup>133</sup> to improve its supply system and its ability to respond to incidents associated with recent winter and summer demand events that led to repeated widespread impacts on service to customers. We note that having such a significant spend on operational responses to incidents could duplicate with other areas of company requests for resilience (e.g. interconnectivity and service reservoir storage). We make no adjustment for this however as the need for investment is understood in both areas, despite the potential overlap.

4.166 Secondly, South East Water has not provided evidence that addresses the concerns we raised at final determination in relation to cost efficiency. On bottom-up costing, the company provides a table which sets out the value and proportion each element of the work represents as part of the expenditure request. It also lists the method of cost assurance<sup>134</sup> used for each element. See table below.

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<sup>130</sup> [OF-CA-195] South East Water, 'SEW- PR24 RD- Annex G- Enhancement Costs', March 2025, p.46.

<sup>131</sup> [OF-CA-195] South East Water, 'SEW- PR24 RD- Annex G- Enhancement Costs', March 2025, p.47.

<sup>133</sup> [OF-SEW-054] Ofwat, 'Enforcement case into South East Water's supply resilience', November 2023.

<sup>134</sup> [OF-CA-195] South East Water, 'SEW- PR24 RD- Annex G- Enhancement Costs', March 2025, pp.46–47 Table ANG13.

**Table 4.9: Overview of South East Water AWS allowance request, including Ofwat opinion on the level of assurance provided.**

Equipment/ Area	Value (£ million)	% of Requested Allowance <sup>135</sup>	Cost Assurance Process	Ofwat Opinion
Tankers and trailers	██████	██████	██████████	Sufficient assurance
Building/construction	██████	██████	██████████ ██████████	Sufficient assurance
OPEX	██████	██████	██████████ ██████████	Insufficient assurance
Other (4x4 vehicles, welfare vehicles, curtainsiders, Arlington tanks and storage)	██████	██████	██████████ ██████████	██████████ ██████████

4.167 South East Water provides vendor evidence of quotes for tankers following our query October 2024 after final representation.<sup>136</sup> This additional evidence assisted us to reassess the 20% cost efficiency challenge applied at draft determination and contributed to the reduced 10% challenge at final determination.

4.168 The 10% was still deemed necessary as only a portion of 'Other' costs were assured by vendor quotes. However, the remainder was solely assured via company expertise – this is not independent or externally benchmarked. Further, it is uncertain what the proportion of the 16.4% is assured by vendor quotes, see table above.

<sup>135</sup> [OF-CA-195] South East Water, 'SEW- PR24 RD- Annex G- Enhancement Costs', March 2025, pp.46-47, Table ANG13.

<sup>136</sup> [OF-SEW-055] Ofwat, Query response: OFW-REP-SEW-046, October 2024

- 4.169 South East Water only benchmarked 8.5% of the requested expenditure, for building/ construction elements. This is the same information provided in its representations to draft determinations. The company could have undertaken benchmarking exercises with other water companies and equipment suppliers in the provision and mix of alternative water supply arrangements, including opportunities for cost efficiency through procurement unit discounts and delivery scheduling.
- 4.170 The largest proportion of costs relates to operating expenditure, which represents 52.5% of the requested allowance. The company states that cost-benefit analysis was used to provide a resilient service at the lowest cost. However cost benefit analysis does not equate to cost efficiency nor is it a surrogate for external and independent assurance or cost benchmarking.
- 4.171 We accept that South East Water's case to provide alternative water supply arrangements is bespoke and note that it is an outlier in the industry due to the uplift in % population covered by alternative water supply provision. This uplift follows recent managerial and operational responses to events and may not be necessary for customers to fund if the company had behaved differently. However, the basic practices, equipment, resources and the operational management response to provide alternative water supply arrangements to supply water to customers are not in themselves bespoke.
- 4.172 In general, we consider the components of an alternative water supply strategy as being relatively easy to benchmark as they will be comparable across companies (e.g. purchase, storage and delivery of bottled water and purchase of water tankers). This means the company should be able to present sufficient and convincing evidence that its costs are efficient.
- 4.173 The company has not demonstrated sufficiently that costs are efficient, as it has only referenced cost-benefit analysis and internal expertise to demonstrate cost assurance for some elements of this scheme. We consider that a 10% cost efficiency challenge remains appropriate to protect customers.

## **Raw Water Deterioration – PFAS**

### **Final determination**

- 4.174 Per and Polyfluoroalkyl Substances (PFAS) refers to a large collection of over 4000 chemicals, increasing scientific information has emerged about them over recent years. The measures to meet PFAS requirements are uncertain and companies are required to undertake investigation work (e.g. sampling) this period to better understand risks, costs and solutions.



- 4.175 To reflect this uncertainty, Ofwat included a notified item in our final determinations – referred to as the 'PFAS Reopener' or 'PFAS Uncertainty Mechanism'.<sup>137</sup> This allows companies to claim for any 'material' increase in expenditure relating to treatment interventions at a works, beyond the costs and work which we allowed in the final determination. If following PFAS investigation work, companies need to deliver schemes in the 2025-30 period required by a new DWI instrument given on after 20 December 2024, they are able to submit these costs to the PFAS Reopener for consideration. It will then be determined whether costs can be claimed and whether they are to be claimed in period or at the end of the period. This approach will cover the seven PFAS related schemes that did not meet our criteria at final determination, totalling £210 million from four different companies.
- 4.176 In its representation to the draft determination, South East Water requested £17.824 million relating to addressing PFAS. This request comprised of PFAS Investigations and a Granular Activated Carbon treatment scheme at one site.
- 4.177 We allowed £14.380 million for PFAS Investigations and deferred £3.444 million to the in-period 'PFAS Reopener'. The deferred portion pertained to Beenhams Heath WTW for Granular Activated Carbon treatment to be installed at the site to treat PFAS. This scheme was deferred as it did not have an associated 'site specific' legal instrument from DWI to support the need for investment, track delivery and enforce delivery at the time.<sup>138</sup>

### Issues raised by disputing company

- 4.178 South East Water raises three issues with our assessment.
- 4.179 Firstly, that Beenhams Heath WTW being deferred to our 'PFAS Reopener' has been incorrectly applied. The company states that the change in DWI guidance has recategorised the need for intervention at this site, the legal undertaking for 'AMP8 PFAS Strategy' is referenced<sup>139</sup> as supporting the need for intervention specifically at this site.
- 4.180 Secondly, the company identifies two new allowance requests which were not submitted to Ofwat previously. These requests relate to Forstal WTW at a cost of £4.8 million<sup>140</sup> and five catchment studies at a total cost of £4.2 million. The company references a letter sent on 18 November 2024 to Ofwat highlighting the proposed schemes following the submission of its draft determination representation. It states

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<sup>137</sup> [OF-OA-022] Ofwat, 'PR24 Final Determinations– Expenditure Allowances', December 2024, pp.209–211.

<sup>138</sup>[OF-SEW-056] Ofwat, 'PR24-FD-CA33 Water Raw water deterioration enhancement expenditure model redacted v3', December 2024, Worksheet: 'SEW (PFAS)'.

<sup>139</sup>[OF-SEW-057] South East Water, 'AMP8 PFAS Strategy (SEW-2023-00015)'.

<sup>140</sup> [OF-CA-195] South East Water, 'SEW- PR24 RD- Annex G- Enhancement Costs', March 2025, p.34, para 145.

they were not included originally owing to the short window between updates to DWI guidance on PFAS and draft determination representation submission.

4.181 Thirdly, the company raises concerns relating to our 'PFAS Reopener' regarding the uncertainty of receiving an allowance for schemes submitted via this process.

## Our assessment

4.182 We acknowledge the issues brought forward by South East Water, however we maintain our approach of deferring the original PFAS treatment scheme to the 'PFAS Reopener' as set out in our final determination.<sup>141</sup> Our approach was not to apply challenges to PFAS related schemes, provided they either had a site specific legal instrument or they were for PFAS investigation costs.<sup>142</sup>

4.183 The purpose of ensuring a site specific legal instrument is present is to confirm the DWI has reviewed, assessed and endorsed necessary schemes. This provides protection to customers in instances of non-delivery (as DWI can pursue enforcement action) and enables the progress of the scheme to be tracked by the DWI and through our price control deliverable process.

4.184 The purpose of allowing PFAS investigation costs was to allow companies to understand their PFAS risk more comprehensively to develop schemes to submit to the 'PFAS Reopener' where and when appropriate.

4.185 The scheme relating to Beenhams Heath WTW is not explicitly covered in the legal undertaking 'AMP8 PFAS Strategy', therefore not only is it less protected from non-delivery than if a site-specific instrument was present, however there is also less scrutiny, endorsement and visibility from the DWI on the scheme. The reason for deferring this scheme to the 'PFAS Reopener' was to provide the company with an opportunity to engage and follow due process with the DWI on the scheme.

4.186 We recommend that the newly requested £4.8 million for Forstal WTW is also deferred to the 'PFAS Reopener'. This is to allow due process to be followed, properly develop the scheme in consultation with the DWI and also so Ofwat is able to make an assessment of the costs.

4.187 We are unable to comment on whether an allowance should be made for £4.2 million relating to five catchment studies, as the company has not attached a referenced document in its statement of case<sup>143</sup> for Ofwat to review.

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<sup>141</sup>[OF-SEW-056] Ofwat, [REDACTED], December 2024, Worksheet: 'Representation Overview'.

<sup>142</sup> [OF-OA-022] Ofwat – December 2024, PR24 Final Determinations, Expenditure Allowances, p.210

<sup>143</sup> [OF-SEW-058] AtkinsRéalis, 'PR24 Additional Scheme – PFAS Removal Scheme, reference 216440-012 / 7.2 / RP / 094', October 2024.

- 4.188 At final determination ten water companies supported the inclusion of a PFAS Uncertainty Mechanism.<sup>144</sup> It is our intention to apply the same criteria to PFAS related spend for the 'PFAS Reopener' as we did at final determination. This will include having a site specific notice to demonstrate investment need and DWI endorsement, in addition to other evidence required for best option, cost efficiency and customer protection.<sup>145</sup> We recommend South East Water engages with DWI as early as possible, including for any schemes raised that have not previously been put forward.
- 4.189 The concerns relating to PFAS schemes raised by the company in its statement of case are unfounded, as these schemes are captured as part of our 'Cost Change Process' and therefore we have recommended these issues be deprioritised by the CMA.<sup>146</sup>

## Cyber security

### Our final determinations

- 4.190 In our final determinations we made allowances for all companies drinking water supply and distribution services to meet their obligations under the Network and Information Systems (NIS) Regulations 2018<sup>147</sup> and the requirements to be resilient against [REDACTED]

- 4.191 We allowed South East Water £27.865 million out of a request of £29.331 million after applying a modest 5% adjustment due to concerns over cost efficiency through our deep dive assessment process. We applied a cost efficiency challenge as the company did not provide evidence of satisfactory third-party assurance of its proposals as required in our PR24 final methodology.<sup>150</sup>

### Issues raised by disputing company

- 4.192 In its statement of case, South East Water states that it does not agree with our 5% adjustment and notes three related third party assurance assessments that were undertaken as evidence that the cost efficiency challenge should not be applied:<sup>151</sup>

- Firstly, that the company cost curves were subject to a benchmarking exercise by ChandlerKBS;

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<sup>144</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure-allowances, December 2024, p.208.

<sup>145</sup> [OF-CA-001] Ofwat, 'PR24\_final\_methodology\_Appendix\_9\_Setting\_Expenditure-Allowances.pdf', December 2022, Section: A1.1 Enhancement assessment criteria, pp.154-159.

<sup>146</sup> Ofwat, PR24 redeterminations – overview of our response to the statements of case', April 2025, p.28. s.5.

<sup>147</sup> [OF-SEW-060] Department for Digital, Culture, Media & Sport, 'The NIS Regulations 2018', January 2023.

<sup>148</sup> [OF-SEW-061] National Cyber Security Centre, 'Cyber Assessment Framework', April 2024.

<sup>149</sup> [OF-SEW-062] Drinking Water Inspectorate, 'Drinking Water Standards and Regulations',

<sup>150</sup> [OF-CA-001] Ofwat, 'PR24\_final\_methodology\_Appendix\_9\_Setting\_Expenditure-Allowances.pdf', December 2022, pp.155-156, A1.1.3 Cost efficiency.

<sup>151</sup> [OF-OA-005] South East Water, 'PR24 Redetermination – Statement of Case', March 2025, p.60.

- Secondly, that the company unit database and methodology was updated and reviewed by Faithful+Gould; and
- Finally, that the company cyber assessment framework 2024 was assured by AtkinsRealis.

## Our assessment

4.193 We continue to consider that our PR24 final determination cyber security allowance for South East Water is appropriate. The company has not provided sufficient and convincing evidence that its proposed costs are efficient. We applied a 5% cost efficiency challenge in our final determinations, which we consider to be a modest adjustment given the evidence presented.

4.194 The ChandlerKBS, PR24 benchmarking report,<sup>152</sup> makes no reference to cyber enhancement proposals. The report is based on three project types: interconnectors, nitrate removal and service reservoirs. These three project types bear no resemblance for those in the cyber claim so cannot be used as proxy evidence of efficiency. Therefore, it does not provide sufficient and convincing evidence that the cost estimates are efficient (for example using similar scheme outturn data, industry and/or external cost benchmarking).

4.1.181 Faithful+Gould (the company's quantity surveyors), Unit Cost Database (UCDB) – Guidance Notes Update<sup>153</sup> makes no reference to cyber related assets and does not appear to be suitable to demonstrate that the unit cost database is appropriate for cyber related investments. This does not provide satisfactory evidence that the cost estimates are efficient.

4.195 South East Water states AtkinsRealis conducted an independent review and assurance audit of the company's 2024 Cyber Assessment Framework (CAF)<sup>154</sup> This provides observations and recommendations regarding the contributing outcomes of the CAF to achieve and demonstrate an appropriate level of cyber resilience and does not comment on costs or provide evidence of cost efficiency in itself.

4.196 We stated in our draft determination that the company's standard of evidence for cost efficiency was not sufficient and convincing. South East Water has had adequate opportunity to provide appropriate assurance. However, the company has still not provided specific evidence that its cyber activities are efficient. In its statement of case, it continues to rely on the same external reports which are either poor proxies or unrelated to costs or cost efficiency.

We therefore continue to consider

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<sup>152</sup> [OF-SEW-063] South East Water, 'SEW124. PR24 DDR – ChandlerKBS Benchmarking Report', August 2024.

<sup>153</sup> [OF-SEW-064] South East Water, 'SEW.G003. SEW, Unit Cost Database – Guidance Notes Update', February 2023.

<sup>154</sup> [OF-SEW-065] South East Water, 'SEW.G0004. SEWDD2e24 SEW CAF AR Audit Letter', May 2024.

a 5% cost efficiency challenge remains appropriate to protect customers. We consider this challenge to be modest relative to the cost efficiencies potentially available to the company.

## Drinking water protected areas

### Our final Determinations

4.197 Drinking Water Protected Areas (DrWPA) is an enhancement activity listed in WINEP/NEP to implement catchment schemes to prevent deterioration or to make improvements following a deterioration in water quality to avoid an increase in the level of water treatment.

4.198 In the final determination, we applied a 10% adjustment to South East Water's WINEP DrWPA programme through a deep dive assessment. This resulted in a final determination allowance of £16.981 million for DrWPA (£18.868 million requested in its draft determination representation).

### Issues raised by disputing company

4.199 In its statement of case, South East Water states that the cost efficiency challenge for DrWPA was arbitrary and 'Ofwat has not taken full account of our evidence'.<sup>155</sup>

### Our assessment

4.200 In its draft determination representation South East Water requested £18.868 million to cover 15 schemes included in its WINEP for DrWPA enhancement activity. Following a deep dive assessment,<sup>156</sup> we applied a 10% adjustment for 'cost efficiency', resulting in an allowance of £16.981 million.

4.201 In the draft determination we had concerns that the need was not fully evidenced in terms of overlaps with base expenditure. We also had concerns on 'best option for customers' and 'cost efficiency'. Therefore, we had applied a 30% adjustment in the draft determination.

4.202 In its representation on the draft determination the company provided some additional evidence to help address our concerns on overlap with base expenditure and 'best option for customers', meaning that on balance we considered it appropriate to remove our challenge on these areas for the final determination.

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<sup>155</sup> [OF-OA-005] South East Water, South East Water statement of case, March 2025, p. 60 (paragraph 4.76 (h)).

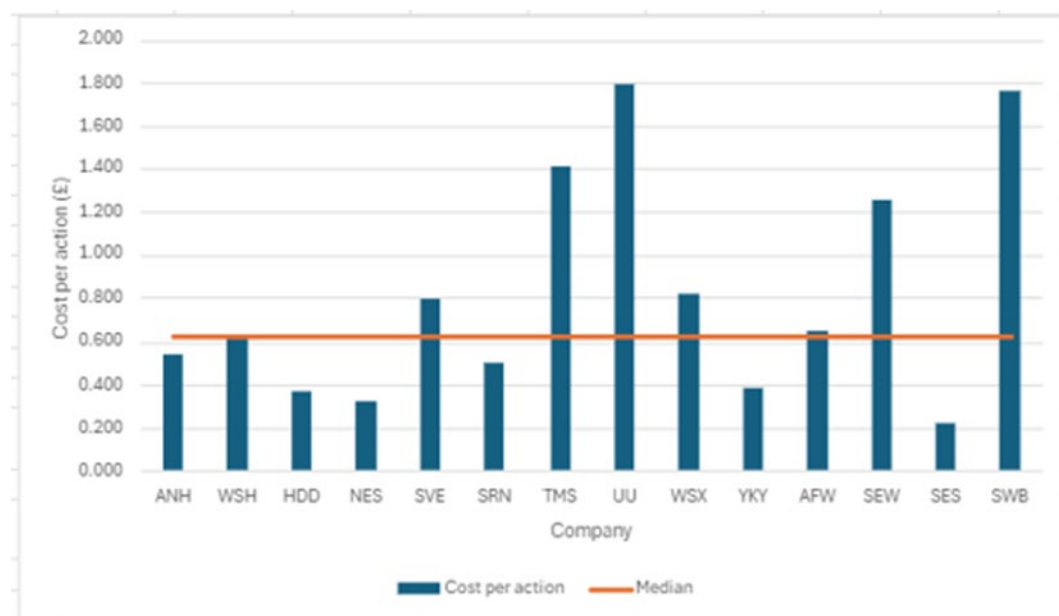
<sup>156</sup> [OF-SEW-004] Ofwat, PR24 final determination: Water Drinking water protected areas enhancement expenditure model, December 2024, Deep dive\_SEW tab.



4.203 Although the company provided additional evidence, we still had concerns on cost efficiency. Following a query [OFW-REP-SEW-038<sup>157</sup>] South East Water presented a snapshot of the cost sheet it uses across its WINEP programme and an example for an investigation scheme.

4.204 South East Water did not provide detailed cost sheets for the DrWPA Implementation and No Deterioration schemes which the company was requesting expenditure for under the DrWPA business plan line. The company did not provide new evidence in the form of activity cost breakdown or evidence of benchmarking for these schemes which was raised in the draft determination deep dive assessment.<sup>158</sup> This would have been useful evidence given the company's request was high compared to other companies (refer to Figure 4.3 below). Therefore, for the final determination we retained our draft determination approach and applied a 10% adjustment for 'cost efficiency'.<sup>159</sup>

**Figure 4.3: Cost per action of company's DrPWA final determination expenditure requests<sup>160</sup>**



<sup>157</sup> [OF-SEW-006] Ofwat, Query response OFW-REP-SEW-038.

<sup>158</sup> [OF-SEW-005] Ofwat, PR24 draft determination: Water Drinking Water Protected Areas enhancement expenditure model, June 2024, Deep dive\_SEW tab.

<sup>159</sup> [OF-SEW-004] Ofwat, PR24 final determination: Water Drinking water protected areas enhancement expenditure model', December 2024, 'Deep dive\_SEW' tab.

<sup>160</sup> [OF-SEW-004] Graph taken from Ofwat, PR24 final determination: Water Drinking protected areas enhancement expenditure model', December 2024, 'Modelled costs' tab. We tested companies' requests against

4.205 The company has not provided any additional evidence of cost efficiency as part of its statement of case. We therefore continue to consider that a 10% cost efficiency challenge remains appropriate to protect customers.

4.206 In Annex G,<sup>161</sup> South East Water states that the cost challenge increases the probability of it incurring a non-delivery penalty as each catchment scheme is subject to a non-delivery Price Control Deliverable (PCD). At draft determination South East Water proposed investment did not meet the materiality threshold for PCDs (materiality threshold of 1% of the company's relevant total expenditure). In its representation on our draft determination South East Water revised its proposed investment, meeting the materiality threshold for PCDs.<sup>162</sup>

4.207 South East Water meets the materiality threshold for a PCD and we continue to consider that a PCD should be applied to the expenditure.

## Delivering outcomes for customers and the environment

4.208 South East Water's proposed an unambitious set of performance commitments when compared to other companies. We stretch the company to meet these targets, so all customers are able to receive an uninterrupted service. We consider the targets achievable coupled with the enhancement expenditure allowance that it has been provided.

**Table 4.10: Navigation of key issues in outcomes**

Point in South East Water's statement of case	Statement of case (SoC) reference	For Ofwat's response see:
Water supply interruptions PCL	1.20a 5.4a 5.11 onwards	PR24 redeterminations – outcomes – common issues, April 2025, pp. 21-25 (s.2)  This document- subsection Delivering outcomes for customers and the environment, Water Supply Interruptions
Water supply interruptions collar	1.20a 5.4a 5.33 onwards	This document- subsection Delivering outcomes for customers and the environment, Water Supply Interruptions

the median unit cost benchmark per action. This was to support identifying which companies to deep or shallow dive, or particular outliers. It was not used to set allowances.

<sup>161</sup> [OF-CA-195] South East Water, South East Water PR24 Redetermination: Annex G Enhancement costs, March 2025, pp. 72 (s.2.7).

<sup>162</sup> [OF-OA-022] Ofwat, PR24 final determinations: Expenditure allowances, February 2025. p.308-309 (Materiality testing).

ODI regime	4.17 5.3a onwards	PR24 redeterminations – outcomes – common issues, April 2025, pp. 26–33 (s. 3)
C-MeX	1.20b 5.4b 5.39 onwards	This document- subsection Delivering outcomes for customers and the environment, C-Mex

## C-MeX

### Performance commitment level

#### Final Determination

4.209 At PR24, we set the C-MeX performance commitment – a measure of customer experience – on a common basis.<sup>163</sup> We found that there are no clear reasons for why customers should expect differences in customer services between companies. This means customers can expect the same standard of customer service regardless of where they are in the country.<sup>164</sup>

#### Company statement of case

4.210 South East Water states that the C-MeX methodology contains regional bias, which – in its view – unfairly penalises the company due to its geographical location in the South East of England. It argues that customers satisfaction scores vary across different regions in the UK, and that our surveys do not sufficiently account for these differences.<sup>165</sup>

4.211 The company provides evidence from the regional UK Customer Satisfaction Index (UKCSI) scores, which compares national averages with South East average. According to South East Water, this evidence suggests that UKCSI scores are lower in the South East compared to other regions.<sup>166</sup>

#### Our response

4.212 From the evidence provided by South East Water, it is not clear that there is a significant difference between the two datasets. The average difference is 0.4% across the 5 years and as low as 0.2% in one year. For some sectors, such as insurance and

<sup>163</sup> [OF-SEW-003] Ofwat, Customer-measure-of-experience-C-MeX-PC-definition-2, December 2024 (republished March 2025).

<sup>164</sup> [OF-OA-017] Ofwat, PR24 final determinations: Delivering outcomes for customers and the environment, December 2024 (republished February 2025), p.236.

<sup>165</sup> [OF-OA-005] South East Water, South East Water Statement of Case, March 2025, p.74.

<sup>166</sup> [OF-OA-005] South East Water, 'South East Water Statement of Case, March 2025, p.75.

public services, the difference between the national and South East averages is very small at <0.1%.

4.213 It is also true that correlation does not prove causality, where the differences could be caused by other regional impacts. For example, it does not account for poorer performing organisations.

4.214 South East Water proposes to use regional UKCSI averages to set the performance benchmark (PCL). This would have the effect of having different PCLs for different companies. We do not consider that customers in different regions of the England and Wales should experience different standards of customer service so we do not support this proposal. CCW has a similar view – that '.... it is the company's job to turn this situation round. There should be no change in the company's target on customer service experience, as every company has circumstances that are unique to it and give it a disadvantage in some way.'<sup>167</sup> Having a company-specific target for C-MeX would also have the effect of reducing sample sizes and risks the performance benchmarks being more volatile.

## **Water supply interruptions**

### **Final determination**

#### **Performance commitment definition and performance commitment level**

4.215 At PR24, we set PCLs at a common level of 5 minutes across all years of the 2025-30 period for all companies. We expected companies to deliver this performance from their total expenditure allowances.<sup>168</sup> We considered this represented a stretching yet achievable common PCL target. The performance commitment measures average number of minutes lost per customer for the whole customer base for interruptions that lasted three hours or more. Further detail on setting the PCL and why we consider this PCL to be achievable but stretching for the sector as a whole is provided in section 2 of the 'PR24 redeterminations – outcomes – common issues' document.<sup>169</sup>

### **Company statement of case**

4.216 South East Water states that Ofwat has set a PCL that 'is overly stretching for many companies, and in the case of South East Water, fails to take into account a feasible

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<sup>167</sup> [OF-OU-045] CCW, CCW's submission the Competition and Markets Authority on South East Water's statement of case, p. 6.

<sup>168</sup> [OF-OA-017] Ofwat, PR24 final determinations: Delivering outcomes for customers and the environment, December 2024 (republished February 2025), p.87.

<sup>169</sup> Ofwat, PR24 redeterminations – outcomes – common issues, April 2025, pp. 21-25 (s.2).

level of performance given our current circumstances and the characteristics of our region.<sup>170</sup>

4.217 It challenges our approach to setting the common PCL as being inconsistent with decisions across the wider outcomes framework.

4.218 The company provides the following reasons why it should have a company-specific PCL for water supply interruptions:

- its current and industry water supply interruption performance levels are significantly higher than the 5 minutes PCL target;
- increasing frequency and severity of extreme weather events;
- increased demand for its water following the Covid-19 pandemic;
- interconnectivity factors; and
- investment to improve headroom will not realise the majority of the benefits until the final years of the 2025–30 period.<sup>171</sup>

4.219 South East Water considers that its reasons for a company-specific PCL are as compelling as the reasons provided by United Utilities in relation to internal sewer flooding, which we accepted in our final determinations.

4.220 South East Water proposes an adjusted company-specific PCL for the 2025–30 period using the following methodology:

- estimating a level of performance that reflects the lack of operational headroom, without extreme weather and 2025–30 enhancement schemes, which equates to performance of 24.5 minutes per year;
- adding impact of extreme weather at the P50 level, which increases the PCL by 9 minutes per year on top of the 24.5 minutes per year; and
- accounting for the benefits of 2025–30 enhancement schemes, which improves performance by 25.81 minutes by 2029–30.

4.221 Using the results from above, it recommends an alternative water supply interruptions PCL, which it rounds to the nearest minute as an 'efficiency and ambition stretch'.<sup>172</sup> We compare South East Water's water supply interruption PCL proposal to the PCL in our final determinations in table 4.11.

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<sup>170</sup> [OF-OU-027] South East Water, Annex F – Outcomes and Water Supply Interruption, March 2025, p.6.

<sup>171</sup> [OF-OU-027] South East Water, Annex F – Outcomes and Water Supply Interruption', March 2025, p.7.

<sup>172</sup> [OF-OA-005] South East Water, PR24 Redetermination Statement of Case, March 2025, p.72.



**Table 4.11: South East Water's water supply interruptions PCL: company recommendation versus Ofwat's final determination (hh:mm:ss)**

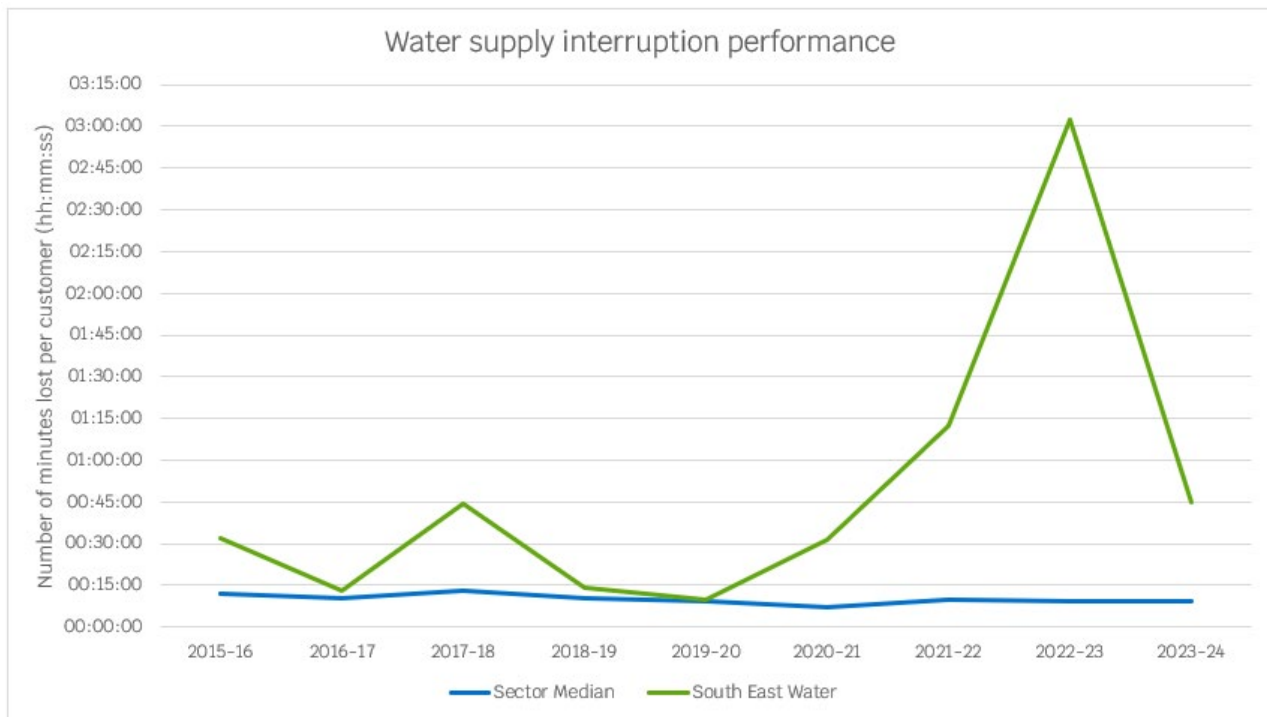
	2025-26	2026-27	2027-28	2028-29	2029-30
South East Water proposal	00:33:00	00:30:00	00:29:00	00:24:00	00:08:00
Ofwat final determination	00:05:00	00:05:00	00:05:00	00:05:00	00:05:00

## Our response

- 4.222 We do not consider that the CMA should adopt the changes that South East Water proposes to the water supply interruptions PCLs. The company fails to provide compelling evidence that we should depart from our approach on exclusions in relation to water supply interruption performance. We discuss this in more detail below.
- 4.223 South East Water provides a considerable amount of information about its historical and future performance in relation to water supply interruptions. It also includes new information in its statement of case that has not previously been provided as part of the determination process. However, we note the PCL that South East Water is recommending for its customers, would mean that it can expect to receive a level of service on average 509% worse than the 2023-24 sector median in the first four years of the 2025-30 period. We are currently investigating South East Water in connection with its duty to develop and maintain an efficient water supply system, including for its consistently poor performance in this area.<sup>173</sup>
- 4.224 We recognise that the PR24 PCL is a challenging target for poorer performing companies, such as South East Water. South East Water's performance for water supply interruptions has been worse than the median performer in each of the least nine years and generally by a large amount, as shown in the figure below.

<sup>173</sup> [OF-OU-046] Ofwat, Ofwat launches investigation into South East Water's supply resilience, November 2023.

**Figure 4.4: South East Water supply interruption performance since 2015-16 compared to the sector median<sup>174</sup>**



4.225 While the sector median has gradually improved over the period, from 12 minutes in 2015-16 to 9 minutes 18 seconds in 2023-24, South East Water has failed to improve over the period. Its performance has been particularly poor during the past three years. It ranks last out of all 17 companies for average water supply interruption performance over the period 2021-22 to 2023-24. This is despite stating, in its PR19 business plan, that the company will aim to reach 5 minutes 30 seconds in 2020-21 and down to 4 minutes by 2024-25.<sup>175</sup>

4.226 In our final determinations we set out that "... we do not consider that it is appropriate to have exclusions for factors that are outside a company's control."<sup>176</sup> We do not consider making exclusions relating to extreme weather for water supply interruptions acceptable as companies can mitigate the impact on customers of weather events through how they prepare for and respond to such events. We have set out why we do not consider that it is appropriate to have general exclusions in place for exogenous factors, such as weather events in section 6 'Approach to exclusions' of 'Ofwat, PR24 redeterminations – outcomes – common issues' document. In relation to South East Water specifically, Ofwat's reviews of previous severe weather incidents have found that South East Water has failed to adequately prepare. For instance, the review of water

<sup>174</sup> [OF-OU-026] Ofwat, PR24-FD-CA-13-Water supply interruptions model, December 2024.

<sup>175</sup> [OF-OU-049] South East Water, 2020 to 2025 Business Plan, December 2019, p.67.

<sup>176</sup> [OF-OA-017] Ofwat, PR24 final determinations: Delivering outcomes for customers and the environment, December 2024 (republished February 2025), p.13, p. 86-87, and p. 148.

companies' response to the 'Beast from the East in June 2018' found that South East Water's plans 'were not sufficiently robust to enable it to deal with the situation that the company was actually confronted with'.<sup>177</sup> In addition, the freeze thaw event in December 2022 was exacerbated by South East Water's lack of preparedness. For example, South East Water had neither optimised its available storage, nor was it optimising the output from its available treatment works.<sup>178</sup>

4.227 We also note that a neighboring company subject to the same climatic conditions, Affinity Water, is able to deliver upper quartile performance in water supply interruption times. More generally, 10 companies are forecast to deliver or outperform a performance of 5 minutes by 2025–26 and 14 companies by 2029–30.<sup>179</sup> This suggests companies can effectively plan and invest to better deal with extreme weather to reduce water supply interruptions.

4.228 We acknowledge South East Water's challenge that the approach we have taken differs from that for setting PCLs for total pollution incidents and internal sewer flooding. We also recognise that only 4 companies met the supply interruption PCL in 2023–24 and sector median outturn is closer to 9 minutes. However, for water supply interruptions, we consider this is a performance commitment where the sector needs and has opportunity to prioritise improvement for customers in the short term. We consider that historical performance and company forecasts support delivery of a 5 minutes performance level by efficient and effective companies. We discuss this in more detail in the 'PR24 redeterminations – outcomes – common issues' document.<sup>180</sup>

4.229 As stated in our water company performance report 2023–24, 'customers have told us that water supply interruptions have a high impact on them, particularly longer duration ones'.<sup>181</sup> CCW highlights in its response to South East Water's statement of case 'reliable water supply is a top priority, so customers would expect an ambitious target to drive tangible improvement in return for the bill increase'.<sup>182</sup> The importance of good performance on water supply interruptions is high priority for customers. Furthermore, research commissioned by Ofwat and the CCW has highlighted that water supply interruptions is of significant concern to South East Water household customers. For instance, supply issues in June 2023 resulted in issues 'such as schools and businesses that had to shut, care homes sending residents in vulnerable circumstances to stay with relatives, and reports of animals in danger of death by dehydration'.<sup>183</sup> Almost all participants in the research were disappointed by South East Water's management of

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<sup>177</sup> [OF-OU-047] Ofwat, Letter to South East Water about the review of the freeze/thaw incident, June 2018.

<sup>178</sup> [OF-OU-048] DWI, Consolidated review of the widespread loss of supplies arising from the freeze/thaw event affecting England in December 2022, May 2023.

<sup>179</sup> Note Hafren Dyfrdwy have been excluded from this comparison due to the scale of the company.

<sup>180</sup> Ofwat, PR24 redeterminations – outcomes – common issues, April 2025, pp. 21–25 (s.2).

<sup>181</sup> [OF-OU-017] Ofwat, Water company performance report 2023–24, October 2024, p.18.

<sup>182</sup> [OF-OU-045] CCW's submission the Competition and Markets Authority on South East Water's statement of case, p.2.

<sup>183</sup> [OF-OU-050] Blue Marble, 'Research into incident response: June 2023 water supply interruption in the South East Water region', November 2023, slide 6.

the incident and its failure to learn from previous interruption incidents. In addition to this, we highlight in our 2023 report 'Prepare Better, Perform Better – Cold Weather Events', that South East Water particularly 'requires improvements in its planning and preparedness' including improvement in its provision of bottled water in response to loss of supply.<sup>184</sup>

## Company specific issues

4.230 We do not consider that the train usage data provided by South East Water is sufficient to demonstrate that it is particularly affected by hybrid working arrangements.

4.231 In fact, in a report produced by Europe Economics (commissioned by Ofwat) on the impacts of Covid-19 on per capita consumption (PCC), it concludes that the ongoing impact of additional working from home impact on PCC for South East Water is 2.0%, with the sector impact at 1.8%, in the scenario it considers most plausible in its analysis.<sup>185</sup> As such, we do not consider that South East Water is significantly impacted from the impacts of Covid-19 above and beyond other water companies.

4.232 Moreover, the regional PCC data provided by the company demonstrates that while there was an increase in PCC in the year of the Covid-19 pandemic, this has been followed by successive reductions in the years 2021-22, 2022-23 and 2023-24 across all South East Water regions.<sup>186</sup> While we recognise that the data from 2020-2025 uses a new leakage reporting methodology, and is thus not directly comparable to 2015-2020 data, the reduction in PCC in the last three years demonstrates that shifting consumption patterns following the Covid-19 pandemic has not resulted in a sustained increase in PCC.

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<sup>184</sup> [OF-OU-051] Ofwat, 'Prepare Better, Perform Better – Cold Weather Events', January 2023.

<sup>185</sup> [OF-OU-052] Europe Economics, 'Impacts of COVID-19 on PCC -Revised', November 2024, p.56.

<sup>186</sup> [OF-OU-053] South East Water, 'Annex D – Supporting Information', March 2025, p.28.

**Table 4.12: South East Water regional PCC data**

Year	Sussex	West	Kent
2015-16	156.79	172.22	151.87
2016-17	148.22	160.34	143.49
2017-18	150.01	156.94	141.32
2018-19	150.49	160.27	142.75
2019-20	149.40	155.11	142.60
2020-21	164.09	173.15	158.73
2021-22	155.85	162.33	157.17
2022-23	151.75	149.78	149.32
2023-24	143.67	143.04	143.48

4.233 In figure 'AND11: SEW's step change in actual peak demand compared to WRMP19', there are only three incidents over the last five years where demand exceeds their WRMP19 peak week forecasts and only in one of these incidents is there a large associated water supply interruptions (2022-23).<sup>187</sup> In addition to this, in figure ANF7: SEW – average monthly operational headroom by region, over the last 7 years, the average monthly operational headroom has only dropped below 0% three times.<sup>188</sup> Reviewing the evidence provided suggests that a lack of headroom is not a major driver of serious supply incidents especially given headroom rarely falls below 0%.

4.234 We disagree that South East Water's infrastructure interconnectivity should mean that its Kent and Sussex regions should continue to perform significantly more poorly than its Western region. Given the company has been in its current form for 18 years, it has had sufficient time and allowances to plan and implement better interconnectivity in the regions it serves. As noted above, its previous business plans resolved to do just that.

4.235 In figure ANF9 provided by the company, which maps serious incidents and sub-zonal interconnectivity, we note that 40% of serious incidents still occur in regions with high sub-zonal interconnectivity.<sup>189</sup> This indicates there are other strategies the company can undertake outside of interconnectivity to reduce water supply interruptions that are within management control.

4.236 As part of the PR19 final determinations, South East Water was provided with an allowance of £41.8 million in its base allowance for intra-zonal investment schemes to meet local increases in demand resulting from new housing development and to ensure supply demand balance.<sup>190</sup> In addition to this, we allowed the company £10.9 million

<sup>187</sup> [OF-OU-053] South East Water, Annex D – Supporting Information, March 2025, p.25.

<sup>188</sup> [OF-OU-027] South East Water, Annex F – Outcomes and Water Supply Interruption, March 2025, p.31.

<sup>189</sup> [OF-OU-027] South East Water, Annex F – Outcomes and Water Supply Interruption, March 2025, p.37.

<sup>190</sup> [OF-SEW-001] Ofwat, PR19 final determinations: South East Water – Cost efficiency additional information appendix, December 2019, p.2.



enhancement expenditure to improve water resilience as part of the PR19 determinations.<sup>191</sup> This was to mitigate critical mains failures and to invest in water treatment works. Examples of investments allowed included the mitigation of a critical main from Arlington water treatment works, mitigating mains failures between Wellwood service reservoir and Potters corner and cross-connection between the treatment streams and upgrade of the high lift pump station on treatment stream one at Barcombe water treatment works.

4.237 Despite the allowances provided, we have seen South East Water's performance deteriorate over the 2020–24 period. Its performance will likely have been exacerbated by the non-delivery of the strategic main to bring supply from the north-east from Canterbury into Ashford and the Surrey Hills to Fleet interconnector that were provided allowances at PR19.

4.238 We disagree that the company cannot take operational changes to improve performance in the short term and can only improve through enhancement expenditure. For instance, in South East Water's service commitment plan, the company has already identified several actions it will undertake to improve performance in the short term.<sup>192</sup> This includes increasing the number of tankers and increasing treatment capacity. With many of these projects due to be complete before the end of the 2025–26 period, we should see the benefits of these schemes reflected in the supply interruption performance.

4.239 We also notice other water companies such as Severn Trent Water, improving its performance over time. In their latest annual performance report, the company cites the "growth of the network response team and trunk main repair team" has been a key driver of their positive performance. The company also points to other strategies it has been implementing to improve both leakage and supply interruptions such as a 'calm network' approach.<sup>193</sup>

4.240 We consider that South East Water has failed to provide the same level of evidence as provided by United Utilities in relation to internal sewer flooding to receive a company-specific PCL.<sup>194</sup> These tests assess:

- does the company provide compelling evidence that performance **is impacted by regional specific factors** that are not covered in the base cost models used to set allowances and are outside of management control; and
- does the company provide compelling evidence to demonstrate it **is taking reasonable and appropriate action** to improve performance in this area.

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<sup>191</sup> [OF-SEW-002] Ofwat, PR19 final determinations: South East Water final determination, December 2019, p.37.

<sup>192</sup> [OF-OU-085] South East Water, Service Commitment Plan, 2023, p.18.

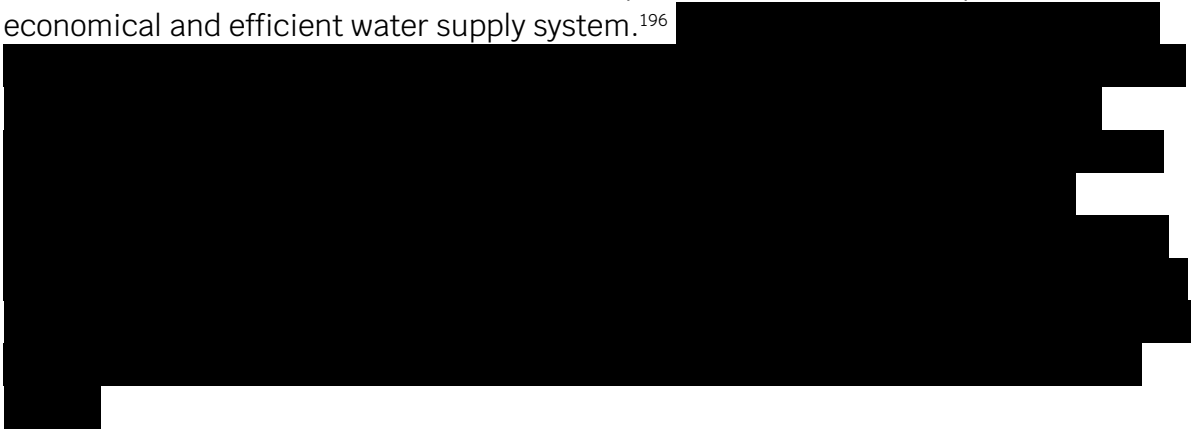
<sup>193</sup> [OF-OU-086] Severn Trent Water, Annual performance report 2023, p.52.

<sup>194</sup> [OF-OU-061] We provide detail of our assessment of United Utilities evidence and our decision in the PR24 company specific outcomes appendix. PR24 final determination: United Utilities – Outcomes appendix.



4.241 It is appropriate to set a high evidential bar for deviating from a common performance level where it will result in targets being set at a lower level of performance in that region. This is because, in our outcomes regime, it will result in customers potentially paying outperformance payments or not receiving underperformance payments despite receiving a lower level of service than those in other regions. A similar view is expressed by CCW in its response to South East Water's statement of case "the company should be challenged and sufficiently incentivised to improve in an area of service where they are comparatively poor performers and where customers place a high level of priority".<sup>195</sup>

4.242 It is important to note that South East Water is currently under investigation by Ofwat. This investigation relates to whether the company has failed to develop and maintain an economical and efficient water supply system.<sup>196</sup>



4.243 Based on our assessment of South East Water's PR24 statement of case, we do not consider the evidence the company provides to be compelling. The company fails to demonstrate it has implemented activities to improve performance including investment planning, operational resilience and how it can act in the short term to improve for its customers. In addition to this, the company has not demonstrated it has undertaken adequate root cause analysis to account for its poor performance. As such, we do not consider it supports or justifies application of company-specific PCLs for water supply interruptions. Therefore, we do not recommend any changes from our final determinations. We consider a common PCL for Water Supply Interruptions should apply to South East Water of 5 minutes over the 2025–30 period.

## **Risk Protections**

### **Final determination**

4.244 At PR24, we set a company specific collar for South East Water at -2% RoRE and at -1% RoRE for all other companies. We maintained this position since draft determinations in July 2024 given South East Water's poor performance and low resilience to external

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<sup>195</sup> [OF-OU-045], CCW's submission the Competition and Markets Authority on South East Water's statement of case, p.6.

<sup>196</sup> [OF-OU-046] Ofwat, Ofwat launches investigation into South East Water's supply resilience, November 2023.

<sup>197</sup> [OF-OU-054] More information regarding the minded to process can be found in Ofwat's Statement of policy with respect to financial penalties pursuant to section 22A of the Water Industry Act 1991.

factors. We considered a wider collar is necessary to incentivise the company to deliver the improvements expected of it, especially given the importance of this performance commitment to customers.<sup>198</sup>

## Company statement of case

- 4.245 South East Water states that our general approach of calibrating a wider collar of -2% RoRE, which is intended to better balance risk while preserving incentives for companies to improve performance, is not effective when poor performance is driven by underlying structural issues.<sup>199</sup>
- 4.246 South East Water also states that the magnitude of its resilience issues cannot be resolved through operational changes. It suggests that while wider collars may incentivise improved performance where issues can be addressed through lower-cost operational changes, this is not the case where performance is driven by underlying structural issues that need to be addressed using enhancement schemes.
- 4.247 On this basis, South East Water considers its company-specific collar of -2% RoRE to be overly punitive. It argues that, when combined with the PCL, the company-specific collar exposes it to disproportionate risk – particularly given that its resilience issues cannot be easily addressed through operational changes.
- 4.248 In light of this, South East Water proposes introducing a collar of -0.5% RoRE, stating that this would be aligned with the collars applied to other performance commitments that are considered important to customers, such as storm overflows and bathing water quality.

## Our response

- 4.249 We do not consider South East Water has provided compelling evidence in its statement of case that supports its proposal to tighten the collar for water supply interruptions to -0.5% RoRE. We note that in South East Water's response to our draft determinations, the company proposed aligning its collar with that of other companies at -1% RoRE.<sup>200</sup> As such, this is a new proposal from the company with a new rationale in its statement of case.
- 4.250 We do not consider South East Water's proposal to apply a 0.5% collar appropriate. Caps and collars are calibrated to balance protecting companies and customers from excessive ODI payments, while maintaining incentives for companies to improve their performance. For the specific performance commitments mentioned by South East

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<sup>198</sup> [OF-OU-055] Ofwat, PR24-final-determinations: South-East-Water – Outcomes appendix, December 2024, section 2.1, p.6.

<sup>199</sup> [OF-OA-005] South East Water, PR24 Redetermination Statement of Case, March 2025, p.72.

<sup>200</sup> [OF-OA-017] Ofwat, PR24 final determinations: Delivering outcomes for customers and the environment, December 2024 (republished February 2025), p.91.

Water, we set the collar at – 0.5% according to our final methodology criteria that these are both new at PR24.<sup>201</sup> This is not the case for water supply interruptions, which is a well-established performance commitment.

4.251 We do not agree with the company's statement that improvements in performance can only be achieved through resolving the company's long term structural issues.<sup>202</sup> As we discuss in the section above, the company should look to understand its root causes and also improve performance operationally in the short term to reduce supply interruptions for its customers. We maintain our view that, given South East Water's continuous poor performance issues and low resilience to external factors, a wider –2% RoRE collar compared to –1% for the rest of the sector at PR24 is necessary to incentivise it to deliver the improvements expected of it over 2025–30.<sup>203</sup> We justify this further below.

4.252 Water supply interruptions is a key area that South East Water needs to improve on. Figure 4.5 shows that South East Water has consistently underperformed against the industry median and other poor performers. During the first four years of PR19, the three poorest performers are Hafren Dyfrdwy, Southern Water and South East Water (with South East Water ranking last).<sup>204</sup> Southern Water performed in line with the industry median until 2022 and Hafren Dyfrdwy's performance has now returned to industry median after a peak in 2020–21, where the spike in performance was largely a result of a single point of failure in relation to the Wrexham trunk main, which the company is being funded to improve at PR24.<sup>205,206</sup>

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<sup>201</sup> [OF-OU-004] Ofwat, Creating tomorrow, together: Our final methodology for PR24– Appendix 8 Outcome delivery incentives, December 2022, pp. 62–63.

<sup>202</sup> [OF-OA-005] South East Water, PR24 Redetermination – Statement of Case, March 2025, p.73.

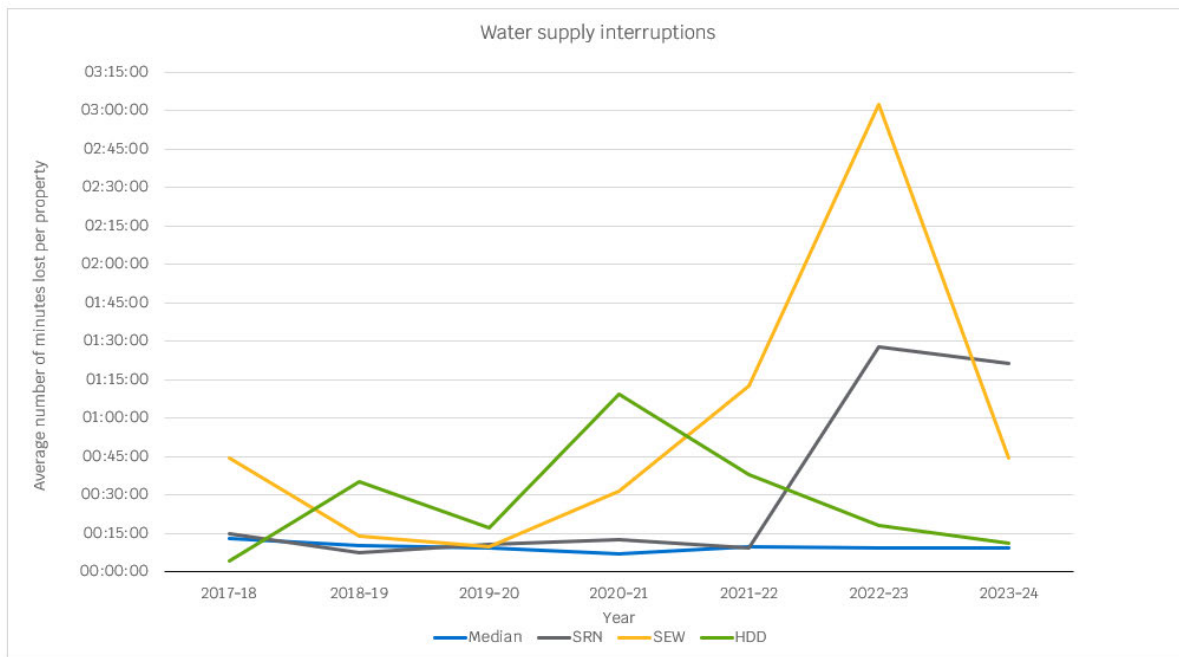
<sup>203</sup> [OF-OU-055] Ofwat, PR24–final–determinations: South-East-Water – Outcomes appendix, December 2024, Section 2.1, p.6.

<sup>204</sup> [OF-OU-017] Ofwat, Water company performance report 2023–24, October 2024, p.19.

<sup>205</sup> [OF-OU-0113] Hafren Dyfrdwy, PR24: draft determination representations: PCs and ODIs, August 2024, p.11.

<sup>206</sup> [OF-OU-020] Ofwat, PR24: Final determinations Hafren Dyfrdwy, Outcomes appendix, December 2024, p.12.

**Figure 4.5 – South East Water Southern Water and Hafren Dyfrdwy: Water supply interruption performance since 2015-16 compared to the sector median<sup>207</sup>**



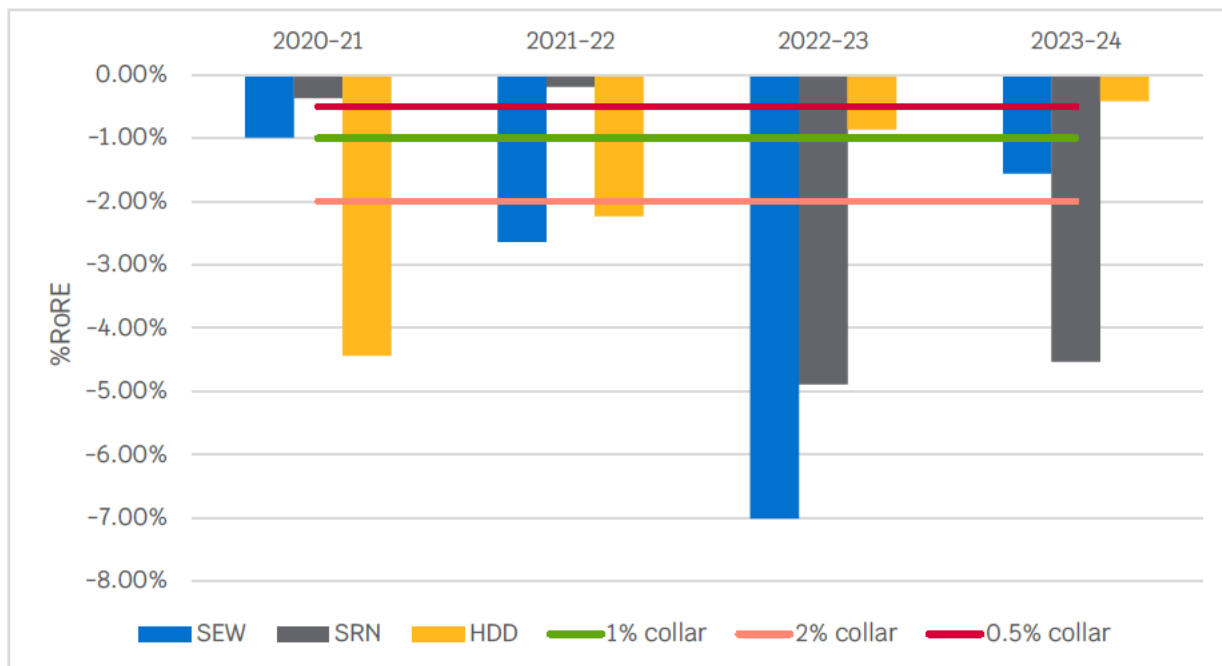
4.253 Figure 4.6 highlights, based on historical performance for these companies the impact of setting a collar at different levels. The figure shows the -2.0% collar set at PR24 for South East Water, the -1.0 RoRE collar we have set for all other companies and South East Water's proposed -0.5% RoRE collar.<sup>208</sup> We consider that once a collar is hit, the financial incentive to minimise the number and duration of supply interruptions is diminished, as the company cannot receive any additional ODI penalties for further deterioration in performance.

4.254 While the company has proposed a collar of -0.5% RoRE, we consider that even the -1% RoRE collar set for all other companies would not maintain incentives for South East Water. Figure 4.6 shows that South East Water is the only company that would breach a collar of -1% RoRE in all years.

<sup>207</sup> [OF-OU-113] Ofwat, 'PR24-FD-CA13-Water-supply-interruptions (additional internal analysis)', April 2025.

<sup>208</sup> At PR19, for common and comparable bespoke performance commitments, we set collars as a multiple of the 2020-21 performance commitment level and used this collar for all years of the period.

**Figure 4.6 South East Water, Southern Water and Hafren Dyfrdwy: Water Supply Interruption ODI payments 2020–24 in (%RoRE) <sup>209</sup>**



4.255A collar of -0.5% RoRE and -1% RoRE corresponds to underperformance of around 10 and 20 minutes respectively. South East Water's average actual performance over 2020–2024 was 76 minutes compared to the common PCL target of 5 minutes for 2025–2030 at PR24. Performing at this level would represent underperformance of 71 minutes, more than 50 minutes beyond the 1% collar. In contrast, Southern Water (2020–21 and 2021–22) and Hafren Dyfrdwy (2022–23 and 2023–24) demonstrated the ability to perform within the -1% collar in PR19. Therefore, setting a collar at -1% RoRE in line with other companies would significantly reduce South East Water's incentive to improve its performance regarding water supply interruptions benchmarked against its historical levels.

4.256The -2% RoRE collar further incentivises the step-change in performance that is needed to provide resilience against this measure into future price control periods. If the company faces underperformance payments only to a -0.5% or -1.0% RoRE collar over 2025–30, there is a risk that it does not take all the steps it can to make operational improvements in the shorter term that are necessary to sustain longer term resilience.

4.257 Overall, we consider the following factors justify the need to maintain strong financial incentives on South East Water's performance for water supply interruptions:

- the company's poor historical performance;
- the impact of this on customers; and

<sup>209</sup> [OF-OU-113] Ofwat, 'PR24-FD-CA13-Water-supply-interruptions (additional internal analysis)', April 2025.

- the ongoing investigation relating to whether the company has failed to develop and maintain an economical and efficient water supply system justify the need to maintain strong incentives in this area for South East Water.<sup>210</sup>

4.258 As such, we consider maintaining both the final determination PCL and a wider collar of -2% RoRE, alongside the PCDs, are in the interests of customers and the environment over the 2025-30 period.

## Business voids performance commitment

### Final Determination

4.259 At PR24 we made no interventions to remove underperformance payments relating to South East Water's PR19 performance commitment to improve performance related to its void performance commitment.

### Statement of Case

4.260 In its statement of case to the CMA, South East Water asks for the £3.9 million underperformance payment related to its Voids performance commitment (PC) to be removed.<sup>211</sup>

4.261 South East Water claims Ofwat took an "inconsistent approach" to setting PCLs and ODIs at PR19, also raising issues about the retail market design and relative performance. Regardless of our views on these points, such arguments are not relevant and are, in our view, out of scope of the redetermination.

### Our response

4.262 Having reviewed the company's statement of case, we consider it provides little new evidence of relevance to its case and, based on the available information, our decision at PR24 not to intervene remains appropriate. We respond to two broad points the company makes in its statement of case below.

4.263 The first broad point is that a number of issues raised in the statement of case are not relevant to deciding whether to intervene or not.

4.264 South East Water accepted the PR19 final determination and the overall package and relative risks and opportunities it contained. The voids performance commitment was part of this package. In accepting the determination, it was accepting the performance commitment definition, performance commitment levels and outcome delivery incentive payments set. It was accepting that it was being asked to deliver the PC

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<sup>210</sup> [OF-OU-046] Ofwat, 'Ofwat launches investigation into South East Water's supply resilience', November 2023.

<sup>211</sup> [OF-OA-005] South East Water, 'PR24 Redetermination – Statement of Case', March 2025, p. 55, para 5(iii).



within the framework and design of the business retail market and that its PC was bespoke and different to voids related commitments other companies accepted in their final determinations. The redetermination should only relate to the PR24 final determination, not decisions made, and accepted by the company, at PR19 final determination. It should not be an opportunity for the company to unpick a single element of the PR19 final determination it disagrees with five years after the performance commitment was accepted as part of that overall determination.

4.265 The second broad point is that the context and evidence to support an intervention is different from the per capita consumption performance commitment, justifying a different outcome.

4.266 We were clear for both the per capita consumption performance commitment<sup>212</sup> and South East Water's voids performance commitment<sup>213</sup> that companies were expected to work to improve performance and that we would require sufficient and convincing evidence in order to consider a case to intervene.

4.267 This is an important principle because neither performance commitment includes provisions to exclude any elements of performance. A decision to intervene therefore must consider and balance the interests of different stakeholders and recognise that removing the underperformance payments ultimately places all the risk on customers – they pay more than they otherwise would have despite not receiving the expected benefits of improved performance.

4.268 We consider there is a clear difference between the two performance commitments. For the per capita consumption PC, companies (including work South East Water jointly commissioned) and Ofwat produced a range of evidence that considered the impact of COVID-19 on consumption. Overall, this allowed a reasonable quantifiable estimate of the impact of Covid-19 on PCC to be produced, including differentiating between the direct impact of COVID-19 during restrictions and the lower impact in later years.

4.269 In contrast, as was the case in PR24, South East Water's statement of case does not provide empirical evidence to quantify the impact of the pandemic on the voids PC. It hasn't provided evidence as to how any impact might have changed over time, nor has it provided evidence to show that the payments it wants removed relate only to the

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<sup>212</sup> We first mentioned this in our July 2021 "Consultation on changes to per capita consumption performance commitments and our November 2021 "Consultation on changes to per capita consumption performance commitments – our decision on reporting performance and ODI timing". We reiterated our expectations in the draft and final determinations Sector Overview of in-period outcome delivery incentives for 2021-22 and 2022-23, in our IN22/01, IN23/03 and IN24/01, which set out our expectations for monopoly company annual performance reporting for 2021-22, 2022-23 and 2023-24 and in our PR24 draft and final determinations Accounting for Past Delivery Appendix.

<sup>213</sup> We first mentioned this in South East Water's draft and final determinations for in-period outcome delivery incentives for 2020-21. We reiterated these expectations and requests for evidence in the queries OFW-OBQ-SEW-129, OFW-OBQ-SEW-141 and OFW-REP-SEW-005 which we sent to the company during the PR24 price review.

impact of COVID-19, not other factors (which would not form part of the case to be considered).

4.270 This is an important difference given that performance and payments are calculated differently for each PC. Per capita consumption is calculated using a three year average, meaning an impact on performance in any one year also affects performance (and associated payments) in the following two years as well. This contrasts with South East Water's voids PC where performance and payments are based on a single year and do not affect performance or payments in later years.

4.271 Table 4.13 shows South East Water's performance across the five years.

**Table 4.13: South East Water's performance against its PCL <sup>214</sup>**

Year	Performance against PCL of 8.1%
2020-21	10.6%
2021-22	10.24%
2022-23	10.29%
2023-24	10.54%
2024-25	10.50% (forecast)

4.272 The stated purpose of the PC was to incentivise the company to reduce the number of non-household void properties, benefiting customers because fewer voids can lead to fairer charges between customers and lower bills for customers already paying. South East Water's customers have not seen any of the stated additional benefits this PC was intended to provide. Yet the company seeks an intervention that removes all risk for its performance in every year and asks customers to pay more than they otherwise would. This is despite, as explained above, the company not providing evidence that quantifies the impact it claims COVID-19 had on this PC, nor how this impact changed over time (noting that the performance in 2024-25 is close to three years after restrictions were lifted).

## Aligning risk and return

4.273 We consider the issues raised by South East Water around risk and return should be considered thematically. Therefore, the issues outlined below are all addressed in the 'PR24 redeterminations – Risk and return-common issues'.

<sup>214</sup> See cell F22 of Tab 3A of South East Water's ODI performance models for 2020-21, 2021-22, 2022-23, 2023-24 and 2024-25 for actual performance each year. See "Consolidated PR19 final determinations: South East Water – Outcomes performance commitments appendix for PCL each year.

**Table 4.14: Key issues in risk and return**

Point in South East Water's statement of case	Statement of case (SoC) reference	For Ofwat's response see:
Imbalance in Ofwat's package	1.11c 6 7.33	Risk and return – common issues- Section 1- Balance of Risk- subsection- Overall Balance
Financial risk	1.11c onwards 1.12e onwards	Risk and return – common issues-Section 1-Balance of risk- subsection- Finance risk
Notional company	1.26 onwards 7.11 onwards Table 7.1 7.15	Risk and return – common issues- Section 3- Allowed return on Cost of debt- subsection- Embedded Cost of Debt
Cost of equity	1.23 6.12 onwards	Risk and return – common issues- Section 4- Allowed return on Equity- subsection- Equity beta
Cost of equity – aim up	Table 1.1	Risk and return – common issues- Section 4 -Allowed return on Equity- subsection- Choosing a point estimate
Cost of debt	1.24 6.32 onwards	Risk and return – common issues- Section 3- Allowed return on cost of debt- subsection- Embedded Cost of Debt
Cost of debt – company specific adjustment	1.24	Risk and return – common issues- Section 6- Company specific adjustments (SEW) This document- Section 4- Aligning Risk and return – common issues- subsection- Cost of debt company specific adjustment
Allowed return	7.1 onwards	Risk and return – common issues- Section 4- Allowed Return on Equity- subsection- Allowed Return and Total Market Equity
Aggregate sharing mechanism (ASM)	1.28	Risk and return – common issues- section 1 – Balance of Risk- subsection-Aggregate

		sharing mechanism and Calibrating the risk and return package for PR24
<b>Outturn adjustment mechanism (OAM)</b>	1.28	Risk and return – common issues– section 1 – Balance of Risk– subsection –Outturn Adjustment Mechanism

### Cost of Debt- Company specific adjustment

4.274 South East Water continues to claim that it should receive an uplift to its allowed return on debt to reflect its status as an infrequent issuer. A report by KPMG proposes a point estimate of 30bps consistent with its prior representations in the PR24 process.<sup>215</sup> We continue to consider it has not demonstrated it faces higher costs due to being an infrequent issuer, and has not provided compelling evidence that its customers support funding the higher cost of its uplift, thus failing both criteria to be allowed an uplift according to our PR24 CSA policy. Further detail is set out in Section 6 of the 'Ofwat response to statement of case: Risk and return' document.

<sup>215</sup> [OF-SEW-067] KPMG, 'PR24 cost of debt: analysis of the infrequent issuer premium: a report prepared for South East Water', March 2025.



## Affordability

**Table 4.15: South East Water's bill increases for AMP8 (£)216**

South East Water	2024–25	2025–26	2026–27	2027–28	2028–29	2029–30	5yr avg.
Final determination	£232	£260	£268	£275	£280	£287	£274
Statement of case	232					341 <sup>217</sup>	

4.275 In its statement of case South East Water proposed a revised impact on customer bills, as shown in table 4.15 this will see an increase in bills with a bill impact change from final determination of £287 to £341. The company has not provided Ofwat the profiles of bills over the period.

4.276 If each of the additional asks from South East Water in its statement of case are agreed, this would result in an increase to the customers bills of (19%) £54 by 2029–30. The company stated a key priority of its customers throughout the price review included affordability and concluded that 71% of its customers considered its business plan as acceptable.<sup>218</sup> However, South East Water has not since provided further information on the affordability and acceptability of its increased request confirming if customers accept a further increase on bills.

4.277 Within South East Water's statement of case the company proposed a wider range of affordability support for customers, however these remain the same measures as proposed within the company's representation on the draft determination. Earlier in this document we mentioned that total funding from shareholders for affordability support is forecast as 0.04% of South East Water's return on regulated equity which at the final determination was the third lowest of all the water companies.<sup>219</sup>

4.278 The company proposed that 10% of customers will be on social tariffs by 2029–30 versus a sector average of 9%. We consider the support proposed by South East Water are in-line with what other companies have proposed across the sector.<sup>220</sup>

<sup>216</sup> 2024–25 bill values are populated from [OF-OA-011] Ofwat, 'Our final determinations for the 2024 price review: Sector summary', December 2024, p. 21, based on company business plan data. South East Water provided an estimate of the bill impact in 2029–30, but no bill profile for 2025–29.

<sup>217</sup> [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.

<sup>218</sup> [OF-OA-005] South East Water, Statement of Case', March 2025, p.31.

<sup>219</sup> [OF-OA-048] Ofwat, 'PR24 draft determinations: Summary of water companies' published plans for affordability for 2025–30', (Ofwat.gov.uk), December 2024, p.10, Table 1.3.

<sup>220</sup> [OF-OA-048] Ofwat, 'PR24 draft determinations: Summary of water companies' published plans for affordability for 2025–30', (Ofwat.gov.uk), December 2025, p.10, Table 1.3.

## 5. Areas for deprioritisation

- 5.1 In its statement of case, South East Water lists aspects of our final determination that it 'does not consider.....to be in dispute'.<sup>221</sup> It is not challenging any enhancement expenditure allowances where our final determination accepts the company's scheme costs (before efficiency challenges), the retail price control, the form of the control for wholesale water, costs sharing rates and PAYG and RCV rates (acknowledging that the CMA may consider these as part of its financeability assessment and update as necessary).
- 5.2 In response to the CMA's request, we have suggested in our PR24 redetermination- overview of our response to the statements of case document that the CMA could deprioritise the redetermination of a number of the PR24 price review building blocks.<sup>222</sup> We include the retail price control.
- 5.3 As such, we do not agree with some of the suggestions made by South East 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 PR24 redetermination- overview of our response to the statements of case, 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>221</sup> [OF-OA-005] South East Water, Statement of Case, March 2025, section 1.33, p.11.

<sup>222</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 Southern Water's business plan. This appendix provides further detail of the calculation of the final determination where we made a number of interventions to Southern 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) £	240.94	291.38	274.09
Average bill growth (%)	8	31	24
Allowed return (%)	3.72	4.19 to 4.82	4.03
RCV Growth (%)	12.7	39.5	28.5
Dividend yield (%)	2	2.1	4.1
ACICR simple (ratio)	1.75	1.85	1.73
ACICR weighted (ratio)	1.76	1.85	1.73
FFO/net debt simple (%)	9.9	9.9	9.8
FFO/Net debt weighted (%)	9.9	9.9	9.8
Run off rate (%)	3.82	3.82	3.82
Post financeability revenue adj (£m)	36.3	44.6	35.9

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