south east water

PR24 Redetermination

Response to the CMA's Provisional Determinations

11 November 2025

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1 Executive summary

Section 1: Introduction

1.1 This submission sets out our response to the CMA's Provisional Determinations (the **PD**). The PD is a lengthy and detailed suite of documents, and we are grateful to the CMA for the work it has carried out to date.

The CMA's PD recognises that SEW was not appropriately funded by Ofwat's PR24 FD to deliver a resilient service to our customers

1.2 Our Statement of Case (**SoC**) explained how Ofwat's PR24 FD was flawed in each of the price control building blocks. These flaws presented significant challenges to SEW individually and combine to leave us precariously positioned – needing everything to "go right" in AMP8 in order for us to deliver for our customers and address the threats to water security in our regions.[1]

1.3 In the PD, the CMA has taken a fresh look at some of the issues we raised and we welcome the CMA's scrutiny and independent view. Overall, the PD is a definite step in the right direction. Across all four of the key price review workstreams – base costs, enhancements, outcomes and risk & return – the CMA has recognised that the calibrations that Ofwat tabled last year were too stretching and has taken concrete action to right-size the funding we will receive in some areas to the improved outcomes that our business plan seeks to secure for our customers.

1.4 For example:

(a) **Base costs:** the CMA is right to conclude that under-delivery adjustments in respect of past delivery can only be justified on the basis of clear evidence, that regulators must tread carefully when making retrospective adjustments without convincing evidence of regulatory gaming, and that there is no such evidence to support adjustments at PR24.[2]

(b) **Enhancement costs:** we welcome the CMA's recognition that we should receive higher funding for demand management enhancement costs. This includes water efficiency, where the CMA accepts we are a high performer and that our proposed interventions are different from those of other companies, and other leakage activity, where the CMA recognises that Ofwat's unit costs are not a "*robust and reliable basis*"[3] for setting the allowances of high performers such as SEW.

(c) **Outcomes:** the CMA has correctly recognised that the Water Supply Interruptions (**WSI**) PCL for Disputing Companies generally should be set based on the median of the average levels of performance individual companies have actually achieved in recent years, and that for SEW this should also take account of company-specific factors, and that the risks SEW would face under a -2.0% RoRE collar would outweigh any incentive properties.[4]

(d) **Cost of capital:** the CMA is right to recognise the higher risk of the sector[5] and to seek to position the allowed return on equity logically next to those that investors can currently earn elsewhere, necessitating an increase in Ofwat's allowed return.

(e) **Frontier shift:** the CMA rightly recognises the need to change the longstanding regulatory approach of setting an ongoing efficiency target around 1% as this does not reflect the overwhelming evidence that the UK economy has not experienced productivity gains at that level in recent years, and that the water sector is unable to outperform the economy as a whole.

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1 SEW, March 2025, Statement of Case, Figure 1.1.
2 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.438.
3 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.642.
4 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraphs 6.266 and 6.296.
5 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 7, paragraph 7.11.

But the CMA's Final Report should do more to chart a clear pathway towards water security and resilience for our customers

1.5 The CMA's PD goes only around one quarter of the way to delivering the price control that we sought from the CMA in our SoC. This means that, while we are in a better position than we would have been had we accepted Ofwat's FD, we still have very limited room for manoeuvre in the face of the operational and financing challenges that we face as a business. There is still more for the CMA to do to address these real-world challenges and remove the unacceptable water security risks that our customers otherwise face in the short and longer term.

1.6 In particular:

(a) On **base cost allowances**, the CMA proposes to grant us an additional £39m, compared to the £129m uplift above Ofwat's FD we justified in our SoC. While we welcome the CMA's recognition that Ofwat's FD underfunded our efficient costs, a material funding gap of £90m remains. We address this further in Section 2 of this Response.

(b) On **enhancement cost allowances**, the CMA proposes to allow £60.6m of additional funding for specific schemes based on the evidence we have provided of need and cost efficiency. However, we are still faced with a material funding gap of £166.8m, significantly undermining our ability to deliver the service our customers want and are prepared to pay for as set out in Section 3 of this Response. It is critical that the CMA should complete its redetermination by engaging fully with the evidence which we have provided to support these schemes and by providing the funding required to secure delivery for our customers.

(c) On **frontier shift**, the evidence we have provided supports a target of 0.5% (rather than 0.7% as provisionally decided by the CMA).

(d) On **outcomes**, we welcome the CMA's acceptance that Ofwat's -2% RoRE penalty collar is not justified, and that a company-specific PCL for SEW which takes into account our performance is warranted. However, as set out in Section 5 of this Response, the PCL proposed in the PD remains excessively stretching.

(e) On **risk and return**, we welcome the CMA's increase in the Cost of Equity from 5.10% to 5.90%. However, we ask the CMA to consider the full range of evidence on observable returns available from other assets and make an additional upwards adjustment to ensure that the flow of capital into the sector is not impeded, as set out in Section 6 of this Response.

1.7 As the CMA works towards its Final Report, it should focus on a series of additional, targeted interventions to fully recognise the efficient costs that we will incur when delivering our plan, provide for challenging but achievable performance targets, and allow us to make a return that is competitive versus the returns that are currently available elsewhere.

Opportunities for strengthening the Final Report

1.8 One of the strengths of the PD was the CMA's willingness to approach key 'building blocks', like the costs benchmarking work, the assessment of the rate of frontier shift in the water industry and the estimation of the cost of capital, with a genuinely fresh pair of eyes. In other parts of the PD, however, the write-up contains less independent analysis on the part of the CMA than we had expected. In some areas, a large proportion of the page count is due to detailed summaries of submissions made by main and third parties, with comparatively light sections setting out the CMA's own assessment.

1.9 In places, the PD also either exhibits a significant degree of deference to Ofwat's view or does not fully engage with the evidence we have submitted (in some cases failing to accurately assess or recognise what evidence has been provided). To assist the CMA's task in the remaining time, this Response clearly sets out where evidence has previously been provided.

1.10 This can be seen in particular in relation to **enhancement costs**, where the CMA has largely maintained Ofwat's FD position, for example disallowing requested funding for resilience interconnectors on the basis of alleged PR19 under-delivery despite: (i) the inconsistency of this approach with the CMA's approach to under-delivery adjustments in base; and (ii) SEW's ability to show both that we overspent our allowances in PR19 and that the PR19 investments we made delivered greater customer benefits. Similarly, the PD declines funding for Bewl WTW, citing the absence of a network-level explanation of the current and future need for additional capacity, which we can provide, and which is included in this Response. The need for these schemes to deliver the resilience improvements our customers support and value was a significant driver of our decision to seek a CMA Redetermination.

1.11 Furthermore, in relation to **base costs,** the PD proposes to continue with the approach of assessing the implicit allowance ('what base buys') based on the full historical modelling period, rather than the benchmarking period, without engaging with our submissions as to why this is wrong.

1.12 In some areas, the PD falls back on Ofwat's FD approach rather than basing its view on first principles, on the basis that SEW has not provided *"sufficient and convincing evidence"* that our requested costs are efficient.[6] We are disappointed that the CMA did not highlight any cost efficiency concerns set out in the PD during our main party hearings or in RFIs and give us an opportunity to respond prior to adopting this position in the PD. There are also a number of areas where the CMA has not taken account of evidence that has already been submitted. For example, on our service reservoirs enhancement case the CMA states we did not provide externally assured evidence that our costs are efficient. However, this was provided in the original ChandlerKBS report submitted with our SoC. This Response addresses each of the specific points raised by the CMA in the PD with a view to further justifying the efficiency of our proposed costs and we would welcome an opportunity to discuss these areas with the CMA and to address any further queries that may arise.

1.13 The PD also suggests some reticence on the part of the CMA in terms of assessing evidence and asserting its own view on schemes and cost efficiency. Whilst we appreciate that the CMA does not have significant internal engineering expertise, we consider that the CMA's Final Report should go further in using the CMA's contracted engineering consultants, WRc. There are also instances where the PD does not seem to take WRc's views properly into account, e.g. where they support the need and efficiency of our proposed investments. In addition, there are areas where further technical input would be of use to the CMA – such as validating the needs case for our Bewl WTW enhancement scheme.

1.14 The PD proposes to deprioritise issues where the CMA expects them to be addressed in a reasonable period through alternative means.[7] The CMA says that it has *"sought clarity as required on the likelihood and nature of the alternative route before reaching our provisional decisions."*[8] Examples of this approach include:

(a) **Asset health**, which the CMA has broadly deferred to Ofwat's Asset Health Roadmap process.[9]

(b) **Bewl WTW** enhancement investment, where the CMA states that concerns relating to the needs case could be resolved under Ofwat's contingent allowance mechanism rather than during the Redetermination process.[10] We disagree that Bewl should be relegated to the contingent allowance, for the reasons set out in Section 3 of this Response.

6 See for example CMA, October 2025, Provisional Determinations, Volume 1, Chapter 5, paragraph 5.571 (service reservoirs); 5.593 (smart network); 5.605 (WINEP investigations); 5.646 (other leakage activity); 5.663 (leakage – smart network).
7 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 3, paragraph 3.20.
8 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 3, paragraph 3.25.
9 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.236.
10 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.561.

(c) **PFAS interventions**, which the CMA has deferred to Ofwat's PFAS uncertainty mechanism under the cost change process.[11]

(d) **Lead replacement** enhancement investment, where the CMA rejects our funding request linked to our legally binding undertaking agreed with the DWI, observes that a DWI change control process exists, and encourages us to work with Ofwat and the DWI to agree an alternative lead reduction strategy.[12] See further Section 3 of this Response, which explains our progress to date on this issue. If a revised undertaking cannot be agreed in time, the CMA's Final Report should specify an 'in-period adjustment' mechanism to ensure that our allowances match our legal obligations.

(e) **PCDs**, where the PD cites the recommendation of the Independent Water Commission (**IWC**) for government to develop a more robust and flexible PCD framework as context for its proposal not to make the changes for PR24 requested.

1.15 We are concerned that the PD approach in these areas leaves us exposed to the consequences of a mismatch between performance and our legal obligations on the one hand, and the inadequate funding in Ofwat's FD on the other hand. In this regard, we note that the IWC highlighted that *"the current arrangements, in which the EA, NRW and the DWI set the requirements that determine much of water company costs, and the economic regulator subsequently determines the revenues companies can receive from water bills to cover those costs, can and does generate tension, complexity and can lead to sub-optimal outcomes"*.[13] We request that where the CMA proposes to defer issues to other regulatory processes, it sets clear parameters around how and when those processes must address them (or otherwise introduce uncertainty mechanisms to ensure that we are not exposed to unfunded obligations which are legally binding, contrary to the interests of our customers).

1.16 Another inevitable consequence of relying on other processes to address issues (such as Ofwat's change process or the resilience contingent allowance) is further delays to the delivery of crucial projects. As these projects can deliver greater customer benefits if approved sooner, we urge the CMA to prioritise timely decisions to the greatest extent possible.

1.17 Together, these issues mean that the CMA's PD leaves SEW with an overall totex funding gap of 11% (£238m),[14] with even larger percentage gaps remaining in key areas for water security. As such, it does not address the key resilience issues we identified in our SoC and will not enable us to adequately address the challenges we face, contrary to the interests of our customers.

1.18 We sought a redetermination from the CMA because we firmly believed that Ofwat had failed to meaningfully engage with the engineering evidence we provided to support our business plan. We are concerned that the CMA does not follow the same path. We recognise the challenges an economic regulator will face in forming views on our proposed engineering solutions because they are not immersed in the day to day operational running of our business. However, taking a cautious approach of denying funding where there is any uncertainty on the CMA's part has material adverse consequences for our customers. We are convinced, based on the comprehensive work we have undertaken to evidence this position, that all of our proposed schemes (and particularly Bewl) must be delivered in AMP8 to improve water security for our customers. Even if we are wrong on timing, and customers could potentially wait for the next AMP for these solutions to be delivered, it seems to us that this is a far riskier approach to take, with a much greater downside, than the risk of bills being slightly higher in this AMP to deliver the solutions our customers need and clearly supported. We therefore urge the CMA to reconsider the evidence in the round and to give us the benefit of the doubt by making appropriate trade-offs and by materially reducing the significant funding gap which remains – our customers will be the ones that benefit from the CMA taking this approach.

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11 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 3, paragraph 3.45.
12 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.688.
13 Independent Water Commission, July 2025, Final Report, paragraph 330.
14 This figure excludes the £50m contingent allowance (adjusted for frontier shift and RPEs).

This Response clearly sets out the key changes needed in each area to improve the service to our customers

1.19 In this Response, we ask the CMA to take another look at a targeted list of issues where we think the PD has not fully considered the full suite of evidence that we put to CMA in the first stage of its work and/or not yet alighted on a suitably balanced set of price control arrangements. There remains adequate time within the prescribed statutory period to do so and ensure that we can deliver for our customers in AMP8.

1.20 In considering this targeted list of issues, we urge the CMA to step back and assess the overall stretch in the package on a holistic basis across costs, outcomes, PCDs and the allowed return, as evidenced by our submissions in Section 7 of this Response on the negative skew and excessive downside risk resulting from the PD package. For example, if the CMA opts not to allow funding for particular enhancement schemes, those decisions should be reflected in its evaluation of the appropriate PCLs on ODIs.

1.21 This Response clearly sets out the key changes needed, and which are supported by our customers. The remedies we set out in our SoC were equivalent to an increase in the average 2029-30 customer bill of £54 versus Ofwat's Final Determination, which is consistent with the overall bill proposals tested with our PR24 business plan and which were supported by 71% of our customers, one of the highest levels of customer support in the South East region. The customer bill impact from the remedies set out in this Response is in line with the bill impact set out in our SoC.

Section 2: Base Costs

1.22 Overall, we welcome the CMA's recognition that our efficient base costs are higher than allowed for in Ofwat's PR24 FD, and there are several areas where the PD approach represents an improvement over Ofwat's, including:

(a) a basic recognition that Ofwat's models omitted some of the factors that drive costs in our region;

(b) the inclusion of an allowance for differences in regional wage levels;

(c) better modelling of the effect that topography has on costs;

(d) a willingness to account for economies of scale at water treatment works (**WTWs**);

(e) an overarching concern that the spread of efficiency scores in Ofwat's PR24 decision was too wide;

(f) an appreciation that the question of whether to use an upper quartile (**UQ**) benchmark, or some alternative benchmark level of spend, has to be looked at in the context of the comfort or discomfort that the CMA feels with the overall shape of its allowances and its confidence in the base cost models; and

(g) an ultimate conviction that the level of funding awarded to SEW in the PD provided by Ofwat in its PR24 FD materially understated our efficient cost requirements.

1.23 We maintain that once targeted improvements are reflected, the PD models would support the efficiency of the £1,300m base cost funding request we made in our SoC, which is the level of funding we need to operate and maintain our network. Our request to the CMA is that the Final Report ensures that our base costs are funded at this level.

1.24 More specifically, if the CMA is minded to broadly maintain the PD approach to base costs in the Final Report, there are several steps the CMA should take to improve the assessment:

(a) The PD approach to 'what base buys' for mains renewal and meter replacements wrongly assesses the average activity undertaken by the industry in the full modelling period

(2012–24). This should be corrected by assessing the implicit allowance using the benchmarking period (2020–24);

(b) The CMA should revisit how the effects of real input price inflation are reflected in base costs, and revert to a standalone allowance for Real Price Effects (**RPEs**); and

(c) If LASSO is retained to select drivers for base cost models, then the approach should incorporate more expert judgement on the reasonableness of the models, their consistency with operational expectations, and the allowances they produce.

Section 3: Enhancement costs

1.25 We were pleased to see that the PD supports increased allowances for several of our enhancement cases, including: one **resilience interconnector scheme** (Poverty Bottom); our **service reservoirs** scheme; to reflect an update to our 2024/25 leakage PCL baseline; our **leakage smart technology** scheme; **funding for PFAS investigations**; and partial acceptance of our funding requests on **other leakage costs** and **water efficiency (demand) costs**.

1.26 Working towards the Final Report, the CMA should revisit the PD in a number of areas where desired evidence has either already been provided or is clearly set out in this Response. A full account is given in Section 3, but the key issues are:

(a) In relation to **resilience interconnectors**, the CMA should remove its under-delivery adjustments, reflecting the evidence we provide on the benefits delivered to customers by the alternative investments we made during AMP7, and for consistency with the approach to under-delivery adjustments in base. The evidence shows that our alternative schemes in PR19 delivered between £2.57 and £26.77 of customer benefits for every £1 spent and collectively delivered more significant customer benefits than the originally proposed schemes would have delivered (at only £3.27 of customer benefits for every £1 spent). Ofwat's PR19 framework was deliberately flexible to allow exactly this kind of re-prioritisation and to penalise a company retrospectively for using the framework as designed is wholly inappropriate. A decision to maintain Ofwat's under-delivery adjustments would also necessarily impact our ability to deliver other elements of our investment programme, as they go beyond any feasible cost efficiency savings.

(b) In relation to **Bewl**, we have addressed the PD challenge of providing a network-level explanation of the current and future need for additional capacity. The CMA should take into account the evidence on our needs case submitted with this Response (and in previous submissions), and allow our requested up-front funding in full, rather than relegating the scheme to the uncertain contingent allowance. The contingent allowance is intended to address future risks, whereas Bewl addresses a clear and immediate need. It is not in customers' interests to delay a decision on this investment until 2027, when implementing the scheme can deliver clear and much-needed customer benefits sooner. The CMA taking a decision on this now will mean [redacted] customers are at a lower level of supply risk for a period of 12 months.

(c) In relation to **our smart network investment**, the CMA should place more weight on WRc's confirmation that smart network investment constitutes a "step change", and take into account our evidence on the step-change our programme represents and the lack of overlap with base activities.[15]

1.27 More broadly, this Response addresses remaining concerns with the cost efficiency of our leakage unit costs, leakage smart sensors, and water efficiency investments. We also explain why we disagree with the PD conclusions on our WINEP investigations, and why the PD conclusion on our service reservoir upgrades does not take account of the evidence we have already provided, which justifies our requested funding in full.

[15] CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.595.

1.28 The PD proposal that two schemes be deprioritised for funding in the Redetermination process on the grounds that they will be addressed via separate processes should also be revisited:

(a) In relation to **lead reduction**, we agree with the CMA that we find ourselves in an untenable situation of misalignment between regulators, of the kind highlighted in the IWC's findings. We are exploring solutions with Ofwat and the DWI, but in the event it is not possible to agree an amended undertaking prior to the CMA's Final Report, the CMA should introduce an 'in-period adjustment' mechanism to ensure we are not left with an unfunded legal obligation (with regard to either the current or a future revised undertaking), which is not in customers' interests.

(b) In relation to **PFAS interventions**, the PD proposes to deprioritise two intervention schemes on the basis that they will be eligible for Ofwat's PFAS reopener. However, Ofwat RFI responses indicate that this is not in fact the case due to the triviality threshold which Ofwat proposes to apply, and consequently these legally mandated schemes should not be deprioritised and should be funded in full.

1.29 Finally, we ask that the CMA make a simple change and amend the mains renewal PCD so that the target applies at the end of the AMP, rather than annually, and allow a reasonable degree of movement between different categories, which we suggest being set at 25%. This would allow us to optimise our programme over time while ensuring that the full programme is delivered, reducing overall costs in the interests of customers and reintroducing some flexibility into an otherwise constrained programme. We also set out our views on the design of the contingent allowance.

Section 4: Frontier shift

1.30 We welcome the CMA's recognition that a 'standard' 1% per annum productivity growth assumption is no longer tenable in light of the UK economy's disappointing recent productivity performance.

1.31 In calculating its estimate of frontier shift, the CMA's Final Report should: (i) place weight on actual recent UK productivity growth data; and (ii) take into account the fact that total factor productivity (**TFP**) data incorporates both cost reductions and quality improvements, which in the case of water are separately reflected in service targets in the Outcomes package. Both of these factors support a frontier shift estimate below 0.7%, and consistent with the evidence we have previously submitted, the final figure should be 0.5%.

Section 5: Outcomes

1.32 We welcome the CMA's recognition in the PD that there is no merit in setting the WSI collar at -2% of RoRE, and that the WSI PCL should reflect SEW's company-specific circumstances, though we disagree with the CMA's provisional decision not to take into account our submissions on the demand and headroom conditions we face. We also welcome the CMA's recognition that the PD outcomes package is negatively skewed by c. 20bps, consistent with the risk analysis submitted.[16]

1.33 The proposal to adopt our DDR WSI PCL, however, represents a target that is too stretching, is not a PCL that we can reasonably be expected to achieve, and exposes us to a significant level of downside risk. It also fails to fully reflect the impact of severe weather. This Response sets out two alternative approaches of: (i) uplifting the PD common PCL to reflect our region-specific issues, using more conservative assumptions on the impact of our enhancement schemes; or (ii) amending our DDR proposal to reflect the impact of severe weather. We then apply a cross-check of assessing our year-to-date WSI performance for 2025-26. Taken in the round, this evidence suggests a range for our starting WSI PCL between 18 minutes and 33 minutes.

[16] CMA, October 2025, Provisional Determinations, Volume 4, Chapter 8, paragraph 8.66.

Section 6: Allowed return

1.34 We welcome the new analysis that the CMA has provided in the PD, including in particular its willingness to stand back and consider whether the CAPM Cost of Equity (**CoE**) is sufficient to attract new investment in view of the returns on offer elsewhere, and to revisit the degree of aiming up required to ensure that investors are sufficiently incentivised to invest record levels of capital in the sector.

1.35 We ask that the CMA continue to stand back and update its CoE point estimate to reflect a top-down view of the required return for equity investors. The evidence shows that the PD CoE of 5.90% offers a thin premium compared to corporate bonds for bearing cost, performance, financing and political/regulatory/reputational risks. A broader set of cross-checks support a higher CoE.

1.36 In relation to the PD CAPM analysis, we think that too much weight has been given to low-end values for each of the RFR, TMR and beta, skewing the mid-point of the CMA's CoE range downwards. The CMA should revise its PD position and base its RFR estimate solely on index-linked gilts, use a measure of the ERP which is consistent with the chosen RFR estimate, and select a beta estimate which recognises that investor perceptions of sector-specific risk have increased since PR19.

1.37 The CMA should also revise its estimate of the future CPIH inflation to 2.1% to be consistent with the OBR's latest five-year economic forecasts. In relation to its proposal not to apply a company-specific adjustment to the cost of debt, the CMA should revisit its provisional conclusion that such an adjustment is not justified based on the evidence we submit that the greater point-in-time risk we face is systematic in nature and non-diversifiable.

1.38 On the cost of debt more broadly, we encourage the CMA to reconsider the approaches that it has applied in calculating the cost of debt, which include technical flaws and risk understating the allowance.

Section 7: Risk and financeability

1.39 We welcome the CMA's recognition that the sector faces higher risk in AMP8. However, the CMA's PD does not take sufficient steps to ensure that its cost allowances, outcome targets and allowed return translate into a genuinely 'fair bet'. Indeed, the PD risk and financeability analysis incorporates errors which lead to understating a significant downside risk for a notional company operating in our region, which is inconsistent with maintaining financial resilience.

1.40 The CMA should seek to remedy these risks by correcting the clear error in the CMA's assessment of 'what base buys', providing base and enhancement costs allowances and an outcomes package in line with our SoC, providing an allowed return on equity that is competitive, and an allowance for the real cost of debt that is based on a conservative/realistic central case allowance for long-term CPIH inflation.

2 Base costs

We welcome the CMA's recognition in the PD that our efficient base cost requirements are higher than allowed for in Ofwat's PR24 FD, and there are several areas where the PD approach represents an improvement over Ofwat's. However, we consider that further work is needed in relation to "what base buys" and base cost modelling. Overall, our analysis building on the PD supports the efficiency of the £1,300m base cost funding request we made in our SoC, and we request that the CMA ensure our base costs are funded at this level in the Final Report.

Introduction

2.1 We welcome the steps forward that the CMA has taken in its investigation into our base expenditure requirements. In the PD, the CMA has recognised some of the challenges we face as a company operating in the South East of England. The CMA has also corrected material flaws in Ofwat's assessment of our base expenditure requirements, including in relation to:

(a) **The PR19 under-delivery adjustment** – the CMA has correctly recognised that the PR19 determination gave companies flexibility to respond to a changing operating environment, that ex-post adjustments based on perception would weaken efficiency incentives, and that there is no evidence of companies gaming the settlement, given the underperformance penalties incurred during AMP7. The CMA has rightly removed the under-delivery penalty as a consequence.

(b) **The implicit allowance for network reinforcement** – the CMA has recognised that the models implicitly fund companies for an average growth in new connections and has therefore determined the implicit allowance based on industry-wide cost shares.

(c) **The allowed unit cost for mains and meter replacement** – the CMA has recognised that SEW faces higher unit costs for maintenance activity due to the high wages in the South East of England and has made adjustments accordingly.

2.2 We agree with the CMA's movement in these areas and consider it important that the principles the PD rests upon in these areas continue to be reflected in the CMA's final analysis of our efficient base expenditure requirements.

2.3 In this Section, we focus on three specific areas where we consider that the CMA needs to do further work ahead of its Final Report.

2.4 We start with very targeted representations on the question of 'what base buys' (or, specifically, the CMA's starting implicit allowances for mains renewal and meter replacement). We explain that there is a clear error of logic in the CMA's provisional decision to use a 13-year reference period when assessing how much physical work its benchmark-based cost allowance funds.

2.5 We then consider the steps that the CMA can take to develop and reinforce its PD modelling of base costs (including its allowances for real price effects (**RPEs**)).

Sector-wide cost adjustments – what base buys

2.6 The PD contains only a short, two-paragraph explanation[17] of the CMA's provisional decision to assess 'what base buys' by reference to the average volumes of work that companies delivered over the period 2011/12 to 2023/24.

2.7 We ask the CMA to reconsider this important issue before it issues its Final Report. Ofwat's original decision to calculate implicit allowances by reference to work carried out over an extended period, rather than over the five-year period that Ofwat used to calculate its PR24 cost benchmarks (i.e. 2019/20 to 2023/24), was an outright error. It follows that the CMA's provisional decision to adopt the same overall approach[18] as Ofwat in the PD means that the CMA has carried over the same error into its calculations.

2.8 The nature of the error can best be seen by stepping back and thinking about what it is that Ofwat and the CMA are fundamentally trying to accomplish by setting PR24 base cost allowances in line with a benchmark level of expenditure. In the simplest terms, Ofwat and the CMA are consciously saying that all companies in the sector should be capable of spending in line with the lowest quartile of observed costs in the sector during the years immediately preceding the reset of price controls. Ofwat and the CMA therefore use a 2019/20 to 2023/24 'actual spend' benchmark as the starting point for the base allowances for each and every company, and make adjustments up or down from the quartile benchmark only in respect of cost drivers that are outside of a firm's control (e.g. due to their scale, as revealed by the cost models).[19]

2.9 One important consequence that comes from the roll forward of lower quartile costs is that future cost allowances are implicitly sized according to the physical volumes of work that companies undertake in the benchmark period. If it happens that companies undertook an unconstrained, sustainable amount of asset replacement between 2019/20 and 2023/24, the roll forward of lower quartile costs will ensure that companies can continue with the same level of activity during the period 2025/26 to 2029/30. If, however, for whatever reason – e.g. more pressing customer priorities elsewhere – companies cut back on work volumes during the most recent five-year period, the roll forward of costs will fund only the same low level of activity again over the next five years, holding all other things equal.

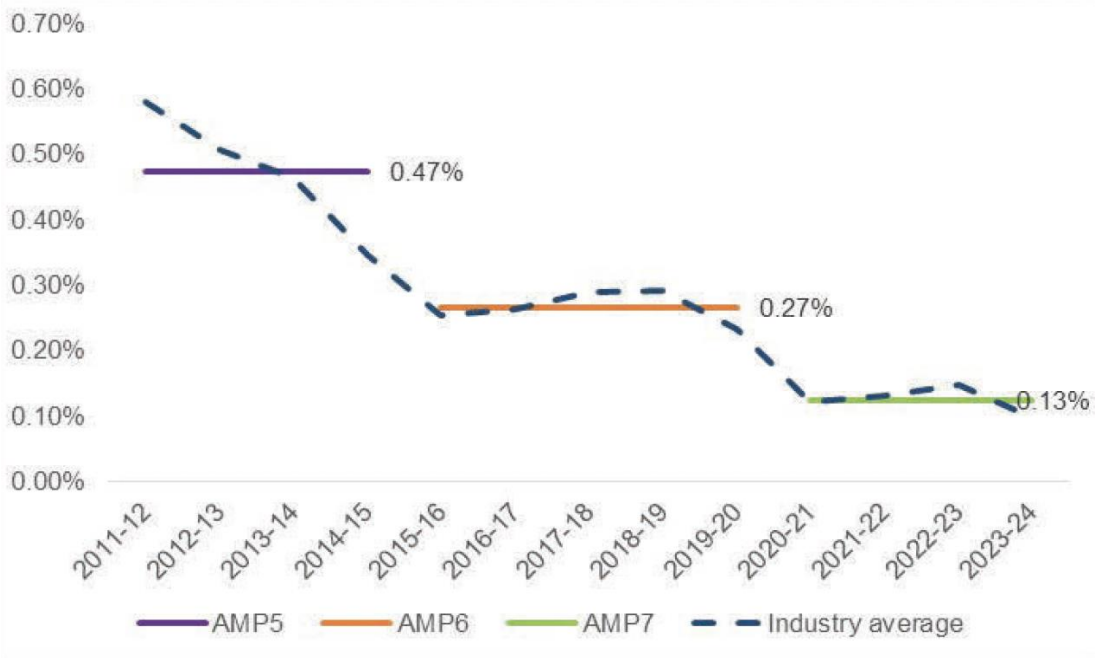
2.10 The CMA identifies in Figure 4.9 of its PD that mains renewal volumes, in particular, have fallen across the sector over a period of more than 15 years, as shown in Figure 2.1 below.

[17] After the CMA completes its factual observations, the CMA's reasons for its position on time period are laid out in a very short section of text at paragraphs 4.333 and 4.334 of the Provisional Determination.

[18] We note and agree with the CMA's decision to extend Ofwat's reference period by one year to 2023/24. The CMA also determined what base buys using the median activity given its relative robustness to extreme values.

[19] The allowances for factors outside of companies' control are based on econometric modelling of the relationship between scale/other drivers and costs over a 12- or 13-year period. The pre-2019 data serves only to improve the calibration of the coefficients in the econometric model; it does not materially impact the amount of funding that Ofwat and the CMA go on to provide at an industry level.

Figure 2.1: Historical industry average water mains renewal rates[20]



2.11 To further underscore the error made in this area, we enclose with this Response two reports by Economic Insight and Oxera that explain in a more technically rigorous way why the CMA's cost benchmarks give no weight to *levels* of spending prior to 2019/20 and, hence, why the volumes of activity that companies were recording as far back as 2011 are irrelevant:

(a) An expert report by Economic Insight, "Time inconsistency error in 'what base buys'"; and

(b) An expert report by Oxera, "Error in the CMA's assessment of 'what base buys'".

2.12 Our reading of the PD is that the CMA's main objections to calculating 'what base buys' by reference to volumes of work carried out between 2019/20 and 2023/24 come from its sense that the low replacement during this five-year period might not have been optimal or efficient in the long run. We agree with this sentiment (there were rising cost pressures in AMP7 that were not reflected in our PR19 base allowances (including higher input prices and stringent service targets), such that the optimal response for our customers was to temporarily reduce some maintenance activity, reinvest in other areas, and absorb a significant proportion of the cost pressures through overspend penalties). For the avoidance of doubt, the out-turn volume of replacement work in AMP7 is *not* sustainable in the long run and there is unanimity across the sector that the pattern shown in Figure 2.1 cannot continue.

2.13 A consensus that there should be a reversion to pre-AMP6 rates of replacement does not, however, mean that companies are funded for the required work. For the reasons explained above, following a period in which expenditures have reduced,[21] the roll forward of observed lower quartile spend mechanistically locks the level of funding for the next five years at the previous run rate and not at the efficient level of spend.

2.14 We therefore request that the CMA steps in and ensures that we are fully funded for the optimal level of replacement activity. This can be achieved by:

[20] CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, Figure 4.9.

[21] While expenditure has increased in real terms during AMP7, the outturn expenditure is lower than it otherwise would have been if companies had delivered more asset replacement activity.

(a) recognising, as an overarching point of principle, that the use of a 2019/20 to 2023/24 cost benchmark rolls forward spending and activity levels from 2019/20 to 2023/24 for another five years;

(b) calculating the implicit allowance for mains renewal and meter replacement by reference to the average volume of work delivered between 2019/20 and 2023/24; and

(c) providing in its sector-wide uplift for funding for the difference between the 2019/20-23/24 replacement volumes and the agreed optimal level of work going forward (e.g. in SEW's case, a mains renewal rate of 0.43%).

Base cost models

2.15 The CMA's allowance for modelled costs is based on a different set of econometric models than the ones used by Ofwat in its FD.

2.16 We welcome aspects of the CMA's new thinking in this area, including the CMA's:

(a) Recognition that Ofwat's models omitted some of the factors that drive costs in our region;

(b) Inclusion of an allowance for differences in regional wage levels;

(c) Better modelling of the effect that topography has on costs;

(d) Willingness to account for economies of scale at WTWs;

(e) Overarching concern that the spread of efficiency scores in Ofwat's PR24 FD was too wide;

(f) Appreciation that the question of whether to use an UQ benchmark, or some alternative benchmark level of spend, has to be looked at in the context of the comfort or discomfort that the CMA feels with the overall shape of its allowances and its confidence in the base cost models; and

(g) Ultimate conviction that the level of funding provided by Ofwat in its PR24 FD materially understated our efficient cost requirements.

2.17 Table 2.1 shows that the combination of the above considerations result in an allowance for modelled costs that is £13m higher than Ofwat provided for in its PR24 FD.

Table 2.1: CMA PD Modelled allowances vs Ofwat FD (£ m's 2022-2023 prices)[22]

	Ofwat PR24 FD model	CMA PD model	Percentage difference
Modelled allowances including real price effects, CACs for WTW and catch-up efficiency, but before frontier shift	854	867	+1.5

2.18 Notwithstanding these important steps forward, it is clear from our technical review of the CMA's working files, and from the queries raised by other companies following the PD publication, that more work will be needed over the coming weeks to build on the CMA's provisional findings and

[22] CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, Table 4.4; SEW analysis. Note that the CMA's table originally incorrectly cited Ofwat FD modelled allowances of £844m.

bring the CMA's technical modelling work up to the requisite standards. We set out a proposed way forward below.

Approach to input prices

2.19 It has been standard practice in the UK up until now for a regulator to make allowance for real input price inflation via an overlay to modelled costs. It was a surprise to us, therefore, to see the CMA attempt to allow for wage growth and changes in energy prices within some (but not all) of its econometric models.

2.20 We have identified several limitations to this approach:

(a) First, as has been noted throughout the PR24 process, the inclusion of input prices and particularly energy prices within the models risks conflating the genuine economic impact of recent increases in input prices with broader recent upward pressures on companies' annual expenditures;

(b) Second, the particular design of the CMA's "wages interacted with scale" and "energy interacted with scale" variables do not accord with any normal operational understanding of the underlying relationship between input prices and water company costs. Specifically, the CMA's chosen log-log variables require one to believe that larger companies are relatively more labour and energy intensive than smaller companies and that a given percentage change in wages or a given percentage change in energy prices has differing percentage impacts on companies depending on their size. Neither of these assumptions accord with operational reality; and

(c) Finally, one of the CMA's measures of "scale" – length of mains – is not, in reality, an operationally relevant driver of abstraction and water treatment costs, as may be seen from the non-inclusion of such a variable in the CMA's modelling of WRP expenditure.

2.21 Our adviser, Oxera, expands on each of these points at Section 3.3.2 of a technical report that we are submitting alongside this Response ("Assessment of the CMA's base cost modelling in the provisional determination", the **Oxera Modelling Report**). Taking all the above points together, our conclusion is that the CMA's attempt to control and allow for input price inflation within its models has not been a success.

2.22 We note the CMA's interest in the impact of wages and energy prices was prompted by two company-specific cost adjustment claims submitted by Southern Water. These claims relate to the scale of Southern Water's labour and energy costs relative to other companies, not to the general trends in costs over time. As such, it was/is not strictly speaking necessary for the CMA to alter an established part of the Ofwat modelling framework – i.e. the separation of the benchmarking of relative efficiency from allowances for annual real input price inflation – in order to assess the reasonableness of Southern's requests.

2.23 Given the problems that we have identified with the CMA's work, our strong preference would be for the CMA to revert in its Final Report to a separate, stand-alone allowance for RPEs. Insofar as the CMA wishes to test for the impact of differences in regional wages, the appropriate explanatory variable for the CMA to include in its long list of candidate cost drivers would be of the form:

$$\textit{Wage index}_{it} = \textit{wage rate}_{it} / \textit{wage rate}_{t}$$

where
wage *index* $_{it}$ is the wage index of company i in year t
wage rate $_{it}$ is the regional wage rate for company i in year t, according to Office for National Statistics (**ONS**) data
wage rate $_{t}$ is the national wage rate in year t, according to ONS data

2.24 The average value of this variable is equal to 1 in each year by construction, such that there is no conflation with general trend effects or the separate RPE allowance.

Selection of explanatory variables

2.25 The CMA has in the PD applied the LASSO technique in order to identify the cost drivers that exhibit the strongest statistical relationship with costs, and then to determine which explanatory variables should ultimately be included and excluded from its chosen models.

2.26 In very general terms, we consider that it is right that the CMA should start in its modelling work with the fullest set of explanatory variables that, from an engineering and economic perspective, appear to have a meaningful impact on companies' expenditures. We also agree that a data-driven approach like LASSO can initially be helpful in narrowing down to a smaller, more manageable set of key cost drivers, when considered alongside other relevant modelling principles.

2.27 Crucially, however, we think that the CMA must add a layer of expert judgment when assessing the reasonableness of both the models that LASSO selects and the £m allowances that the models generate. Viewed from the outside, it is difficult for us to discern how far the CMA was able to apply such an assessment prior to publishing the PD. The impression that the PD gives is that the modelling workstream was mainly algorithm-led and the CMA had only very limited time to validate the modelling results or to sense check that the published models provide a logically intuitive explanation of the factors that drive water industry costs. If this is correct, we would suggest that it has contributed significantly to the criticisms and challenge that the CMA will be receiving from multiple parties in their responses to the PD.

2.28 As the CMA moves to making its Final Report, we encourage it to show more explicitly that it has combined best practices in statistical modelling with a genuine expert eye for the chosen, final model specifications. The Oxera Modelling Report outlines a five-step process that Oxera would expect a decision-maker to work through, as follows:

(a) Step One – identify a long list of operationally relevant cost drivers that have sufficiently high-quality data to be included in a cost assessment model;

(b) Step Two – select cost drivers that are strongly associated with costs in statistical terms (where LASSO could feature as one tool among many);

(c) Step Three – determine whether the resulting models are aligned with operational expectations;

[iterate as necessary back through steps two and three]

(d) Step Four – test the robustness of the selected model, and assess the volatility of the model to minor changes in the data and underlying assumptions;

[iterate as necessary back through steps two, three and four]

(e) Step Five – where no single model is clearly superior to all others, consider aggregating the results of multiple models into a composite predictor of efficient costs.

2.29 We think this proposed approach strikes the right balance between objective statistical interrogation of the data set that the CMA proposed in its *Approach and Prioritisation* document,[23] on the one hand, and the appropriate application of expert judgment, on the other. Accordingly, we strongly encourage the CMA to show on the face of the Final Report how it has worked through each of the steps in the above process, focusing especially on the measures that it has applied to ensure that its statistical work is meaningful and relevant.

[23] CMA, May 2025, Water PR24 redetermination references – approach and prioritisation, paragraph 43.

Required expert interventions

2.30 Our expectation is that when the CMA revisits its PD modelling work in light of the representations received from companies and other stakeholders, the models that emerge from step two of the analysis may be different from the models that were selected for the PD. This makes it difficult for us to comment more precisely on how the CMA might wish to approach the remaining steps in its work. However, we can make the following general observations.

2.31 A first key area of focus should be treatment of economies of scale at WTWs.

2.32 The CMA recognised that economies of scale is a relevant driver of costs, and its long list of candidate cost drivers includes average volume per WTW as a possible explanatory variable for WRP costs. The LASSO technique, as applied at PD, then goes on to select the average volume per WTW as one of the variables in its preferred model. However, the estimated sign on the variable turns out to be positive, meaning that as the typical size of a company's WTWs get bigger (or smaller) total costs supposedly increase (or reduce), which is the opposite to general operational understanding of the relationship between treatment work size and cost.

2.33 The correct response at this point is for the CMA to intervene and remove the average volume per WTW variable from the model. A model specification that does not align with operational realities is not a good or defensible model, and the efficiency scores and allowances it produces are not reliable. WTW economies of scale are operationally intuitive because a water treatment works is a classic example of a plant with a linear process that processes one input (raw water) into a finished product (treated water). It is subject to all the economies of scale that would be expected in such a plant, and this is well understood throughout the industry.

2.34 We remain of the view that our inability to benefit from the same economies of scale as the rest of the industry should be recognised via a company-specific cost adjustment claim. As outlined in our DDR and SoC—and as agreed by Ofwat in the PR24 FD – a variable capturing economies of scale may not perform well in the econometric modelling due to its correlation with other cost drivers, specifically density (where it is assumed that companies with small treatment works operate in sparsely populated regions). However, SEW operates in a region that is only marginally sparser than average, yet we have some of the smallest treatment works in the industry i.e. the density variable does not capture the costs we face as a company operating small treatment works.

2.35 Ofwat assessed the appropriate size of the required cost adjustment to be £14.3m. We set out in our SoC why the correct adjustment is £25.1m.[24] We ask the CMA to provide a detailed assessment of this difference of opinion.

2.36 If, however, the CMA wishes to make another within-model attempt to control for economies of scale, our suggestion would be that the CMA bring weighted average treatment size (**WATS**) into its long list of candidate cost drivers. This measure better captures the sources of diseconomies/economies of scale from an operational perspective. It also aligns with the economies of scale measure used in Ofwat's/the CMA's wastewater network plus model and with the lens that Ofwat used when assessing SEW's PR24 cost adjustment claim.

2.37 A second key area of focus concerns the CMA's approach to controlling for density.

2.38 The CMA's long list of candidate cost drivers includes six possible density variables. The LASSO technique, as applied at PD, selects four of these variables in both the WRP and the TWD model. As Oxera explains in Section 3.4.1 of the Oxera Modelling Report, this patchwork of cost drivers leads to the relationships between density and costs in both the TWD and WRP models taking on an unusual and unintuitive shape, such that the overall effect that the density variables have within the models becomes difficult to explain or defend.

2.39 We think that the appropriate response to this problem could be for the CMA to segregate the selected density variables into a series of different models. This would help to ensure that the

[24] South East Water, March 2025, Statement of Case, paragraph 4.33(a).

CMA can pick up the full set of factors that may be driving water industry costs but in a way that is intuitively and statistically robust.

2.40 The main consequence this has is that the CMA need not necessarily present a single preferred model in its Final Report, but can instead aggregate a predicted level of efficient cost for each company from multiple defensible models (see Step Five in paragraph 2.28(e) above). Oxera explains in more detail how this can be accomplished in Section 5 of the Oxera Modelling Report.

2.41 Finally, we note that it is not possible to include three of the scale-related explanatory variables in the CMA's long list – connected properties, length of mains and properties over mains – within the same TWD model as they are perfectly colinear (i.e. since the cost drivers are modelled in logarithms, properties over mains is a perfect linear combination of connected properties and length of mains). We therefore propose that the CMA should run the LASSO algorithm twice in TWD for each density run, once with connected properties as a scale variable and once with length of mains as a scale variable.

Revised approach

2.42 In Section 5 of the Oxera Modelling Report, Oxera shows how the CMA's PD models could potentially be respecified in a way that remains true to the principles and intent that the CMA lays out in the PD but without encountering the technical problems that the CMA has run into in its initial analysis. This would entail:

(a) **Initial cost driver selection** – following the CMA's approach, Oxera includes cost drivers that reflect the substantive arguments raised by Disputing Companies in their SoCs in the initial long-list of candidate cost drivers. However, it: (i) removes the input price indices); (ii) introduces the 'de-trended' regional wage index outlined in paragraph 2.23;[25] (iii) replaces the CMA's WTW size variable with WATS.

(b) **Refining the long list** – in the first instance, Oxera runs the LASSO procedure three times for WRP and six times for TWD, reflecting the three different density variables that Ofwat and the CMA use in their models and the distinction between the scale variables in TWD. This approach ensures that multiple density measures are not introduced in an inconsistent or misaligned manner.

(c) **Operational assessment** – Oxera assesses whether the estimated relationships between costs and cost drivers are directionally aligned with operational expectations. If a cost driver has an operationally unintuitive relationship with costs, the LASSO procedure is re-run with that cost driver removed or replaced.

(d) **Model validation** – Oxera tests the quality of the models using standard statistical tests (such as whether coefficients are statistically significant) and validation techniques (such as testing alternative estimation approaches and the sensitivity of the models to changes in the underlying data).

(e) **Model aggregation** – rather than selecting a single model based on model fit, Oxera considers a triangulation approach aligned with Ofwat's approach at the PR24 FD (i.e. a simple average across reasonable models). The CMA has previously recognised that 'model quality' is much broader than just model fit[26] and, in the absence of clear metrics that can be used to weight different models, we consider that a simple average across competing models is appropriate in this context.

2.43 This improved approach to using LASSO for model development results in six WRP models and six TWD models being selected, as set out in Tables A2.1 and A3.1 in the Oxera Modelling Report.

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25 As the variable is 'de-trended', there is no overlap between the base cost models and the RPE true-up mechanism, nor is there a risk that the variable captures general increases in costs over time.

26 For example, see CMA, March 2015, Bristol Water plc: A reference under section 12(3)(a) of the Water Industry Act 1991 Appendices 1.1 – 4.3, appendix 4.2, paragraph 46.

2.44 In both cases, the resulting models show a good alignment with those presented in our SoC, with the following exceptions: in WRP, all models control for WTW-level economies of scale, and in TWD a regional wage variable is selected in all models.

Conclusions on base cost modelling

2.45 The results that the different modelling approaches produce are summarised in the table below.

Table 2.2 – SEW modelled base allowances

	SEW SoC models[1]	CMA PD	Improved application
Baseline efficient cost, pre ongoing efficiency (£m)	885[2]	867	926[2]

Note: [1]These models do not control for WTW-level economies of scale or regional wage pressures, such that a CAC is required to fund SEW for its unique operating environment. [2] To ensure direct comparison to the CMA PF, we include the corrected application of the labour RPE, and a £29m uplift for the energy adjustment as per Ofwat's FD.

2.46 We consider that our SoC models continue to be robustly evidenced and aligned with operational reality. We have demonstrated that relative to Ofwat's FD models, our SoC models represent a clear improvement in statistical quality and robustness, along the dimensions confirmed by the CMA's analysis (e.g. model fit), while also reducing bias, improving precision, and maintaining simplicity and operational relevance.

2.47 Relative to the CMA's models, we think our SoC models are: (i) simpler, in that the relationships between cost and cost drivers can be readily inferred; (ii) aligned with operational expectations; (iii) estimated using different cost drivers and different levels of aggregation to mitigate the bias associated with using only one model; (iv) robust to small changes in the data; and (v) predict costs with a lower degree of uncertainty.

2.48 Accordingly, we maintain that the appropriate approach to base cost modelling is for the CMA to implement the improvements to Ofwat's suite of models identified in our SoC. Simply retaining Ofwat's models unadjusted would fail to fund our efficient costs, for the reasons set out in our SoC.

2.49 However, should the CMA be minded to continue using the LASSO approach, it should incorporate the adjustments identified in paragraph 2.42 to ensure that the resulting models are robust and aligned with operational expectations.

2024/25 cost data

2.50 One further potential source of change to the allowances that the CMA has proposed in its PD comes from the opportunity that the CMA has to incorporate out-turn 2024/25 cost data into its cost modelling.

2.51 As a general observation, we would support the inclusion of the latest available data within the CMA's work, provided that the CMA is content that it has the capacity and the time to make the necessary updates to its numbers. The point of principle here is one that applies as much to the base cost models as to the post-modelling adjustments, the setting of outcomes and the calibration of the allowed return: the CMA will reach a better determination if it is able to process all the data that is available to it at the point where it must make its decision.

2.52 It is important, however, that the update for 2024/25 data involves more than a mechanistic 'turning of the handle' on the models. One of the positive aspects of the CMA's PD was the way in which the CMA considered in paragraphs 4.63 to 4.72 of the base costs chapter whether the

use of an UQ benchmark generated allowances for the Disputing Companies and for the industry as a whole that appear sensible in the round.[27]

2.53 A key consideration at Final Report stage will continue to be the scale of the cost challenge that the CMA can credibly apply at sector level. The CMA will have noted that Ofwat's PR24 FD contained a noticeably more stringent challenge to base costs than was deemed appropriate in PR19 (-4% at PR24 vs -0.4% at PR19).[28] The subsequent experience of overspending and under-delivery of outcomes/outputs over a five-year period sends a strong directional signal that it would be inappropriate for the CMA to tighten allowances further in its determination.

2.54 Accordingly, in the event that the inclusion of 2024/25 costs results in a lowering of industry or company allowances, we would expect the CMA to revisit the question of whether an UQ remains appropriate.

RPEs

2.55 We explained above that we think that the CMA should revert to a stand-alone overlay for RPEs (specifically, in the case of base costs, wage growth and changes in energy prices). Irrespective of the approach that the CMA takes in its Final Report, we have the following additional comments on the sizing of the CMA's eventual allowances for future input price inflation:

(a) Wage forecast – we disagree with the CMA's straight-line extrapolation from historical rates of wage growth and see no reason to depart from the consensus forecasts for wage increases that the CMA is using when sizing its bioresources, enhancement and retail totex allowances;

(b) Non-modelled costs – by switching RPEs to zero in the 'Controls' tab in its 'Base costs aggregator model', the CMA has inadvertently allowed for zero RPEs for all non-modelled water and wastewater costs. The RPE allowance should be switched back on in the CMA's Final Report;

(c) End-of-period true-up – the PD is silent on the CMA's thinking as regards the need for and form of an ex post adjustment for the differences between allowed and actual input price changes. We are clear that an end-of-period true-up is needed for the reasons that Ofwat gave in its PR24 FD. We think that the calculation for SEW should:

(i) look at the difference between the allowances that the CMA provides for in its Final Report and the out-turn values of the indices that Ofwat specified in December 2024 decision document; and

(ii) use the industry-wide shares for labour and energy that Ofwat identified in its FD.

Next steps

2.56 The base costs workstream stands out from the other parts of the CMA's PD as the area where there is the greatest potential for fundamental changes.

2.57 Along with the other Disputing Companies, we wrote to the CMA on 30 October 2025 and indicated that we would like for there to be an open dialogue with the CMA as it brings its work on the base cost models, and associated issues like RPEs, to a conclusion. It is for the CMA to determine what form further discussions might take – e.g. a small working group and/or a targeted working paper. However, we consider that some form of further consultation will be essential if the CMA is to avoid the technical difficulties that afflict its PD.

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27 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraphs 4.61 to 4.72.

28 Ofwat, December 2024, PR24 final determinations: Expenditure allowances, page 362; Ofwat, December 2019, PR19 final determinations: Securing cost efficiency technical appendix, page 167. Note these figures are industry-wide and include wastewater and retail businesses.

3 Enhancement costs

We welcome the CMA's provisional decision to increase our overall enhancement funding by £60.6m. However, we are concerned by the significant cost gap of £166.8m that remains in our enhancement programme and the CMA's limited engagement with many of our enhancement requests. This poses a significant challenge to our ability to deliver the service improvements our customers want and need.

There is still more for the CMA to do to address these real-world challenges and remove the unacceptable water security risks that our customers otherwise face in the short and longer term. It is critical that the CMA should complete its redetermination by engaging fully with the evidence which we have provided to support these schemes and by providing the funding required to secure delivery for our customers.

Introduction

3.1 Our SoC explained how our enhancement programme was developed by bringing together all statutory and customer drivers into a single, optimised and prioritised programme capable of improving water security and addressing the resilience challenges faced by our network, and was strongly supported by our customers.

3.2 We set out our key concerns with Ofwat's assessment of our enhancement programme, namely that:

(a) Ofwat's shallow dive cost efficiency challenge was flawed because it failed to take into account relevant evidence on the efficiency of costs proposed for the specific scheme;

(b) Ofwat had wrongly disallowed funding based on misunderstanding the evidence on needs case;

(c) Ofwat's assessment of cost efficiency failed to take into account compelling evidence; and

(d) Ofwat wrongly disallowed funding for overlap with PR19 or base funding when no such overlap exists.

3.3 Since submitting our SoC, Ofwat has indicated that it would allow additional funding compared to its FD. This includes: one **resilience interconnector scheme** (Poverty Bottom); additional allowance for our **service reservoirs** scheme costs; increased funding for **leakage** to reflect an update to our 2024/25 PCL baseline; new funding for **leakage smart technology** and **funding for PFAS investigations**. The CMA has agreed with Ofwat in these areas. It is clear to us that Ofwat's more detailed engagement with some elements of our proposed investment programme through the Redetermination process has given it a better understanding of our investment needs.

3.4 This means that the only areas where the CMA has come to a different view than Ofwat are the CMA's partial acceptance of our case on **other leakage costs** and partial acceptance of our **water efficiency (demand) costs**.

3.5 The PD overall engagement with our enhancement case is limited, and its provisional conclusions on our funding requests in a number of areas are flawed because:

(a) Under-delivery adjustments are maintained without properly considering the evidence we have provided to show that these disallowances are not justified.

(b) Like Ofwat, the CMA has failed to engage with and take into account relevant evidence on the efficiency of costs and the need for proposed schemes.

(c) Blunt 10% or 20% cost reductions are applied for efficiency, without adequately justifying the need for, or size of, such reductions based on the evidence.

(d) Certain schemes are relegated to processes outside the Redetermination, without any assurance that those processes can deliver the required funding, and without recognising evidence which justifies why funding them now furthers the consumer objective.

(e) The approach to RPEs applicable to enhancement costs should take into account relevant points highlighted in paragraph 2.55 above.

3.6 Overall, the PD has increased our enhancement funding by £60.6m compared to Ofwat's FD. This leaves a £166.8m cost gap in our enhancement programme, which poses significant challenges to our ability to deliver the service improvements customers want and need. The improvements that are under threat include:

(a) a water supply that is resilient to extreme weather events;

(b) ensuring long-term water security in all our resource zones; and

(c) complying with the DWI guidance and legal undertakings.

We request that the CMA reconsider the evidence that we have provided throughout the Redetermination process and close the cost gaps relative to the proposed expenditure in our plan.

Resilience interconnectors

3.7 The CMA has assessed the case for resilience interconnectors and allowed £0.1m in additional funding. This is equivalent to a 29.6% challenge on the programme request.

Table 3.1: Resilience interconnectors funding requested compared with the Ofwat FD and CMA PD allowance

Ofwat FD funding	SoC requested funding	CMA PD funding
£90.6m	£128.8m	£90.7m

Summary of the CMA's approach

3.8 The CMA has provisionally:

(a) Accepted the enhancement case for Poverty Bottom following evidence we have provided on sites that are facing abstraction reductions. Ofwat had agreed to additional funding for Poverty Bottom in its response to our SoC.[29] We welcome this change.

(b) Retained the PR19 under-delivery adjustments applied to Surrey Hills to Fleet and Ashford. The CMA has stated that its considerations on base under-delivery adjustments do not apply to these cases and that the under-delivery adjustment is appropriate as follows: "*[…] we find clear evidence that funding was given in PR19 for the specific named scheme in question and there is clear evidence of under-delivery. South East has not delivered the scheme and has not demonstrated that it has secured equivalent or better outcomes through alternative schemes that would not otherwise have been delivered.*"[30]

[29] Ofwat, April 2025, PR24 Redeterminations: Response to South East Water's Statement of Case, paragraph 4.122.
[30] CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.509.

(c) Retained the 20% cost challenge for Groombridge and Row Dow to Kemsing on the basis of base overlap. The CMA has agreed with Ofwat's reasoning that these schemes address hazards caused by extreme weather events, and other companies address these through base.

(d) Retained the disallowance of 100% for Bloodshots to Darnley and Oakhanger to Alton. The CMA has stated that Bloodshots to Darnley should be covered by base expenditure as it addresses increase in growth, and there is not sufficient evidence of cost efficiency and optioneering for the Oakhanger to Alton scheme.

Our response

Surrey Hills to Fleet and Ashford

3.9 We disagree with the CMA's reasoning that the under-delivery adjustments for Surrey Hills to Fleet and Ashford are justified and discuss each of the following arguments in turn:

(a) Why the PR24 Ashford and Surrey Hills to Fleet schemes are different from the PR19 schemes.

(b) Inconsistency with the CMA's assessment of the under-delivery adjustments in base.

(c) PR19 overspending.

(d) Equivalent benefits provided to customers in response to new and emerging risks.

3.10 The table below shows the funding gaps remaining for the PR24 Ashford and Surrey Hills to Fleet schemes.

Table 3.2: Funding requested for Ashford and Surrey Hills to Fleet compared with the Ofwat FD and CMA PD allowance

Scheme	SoC requested funding	Ofwat FD/CMA PD funding	Funding gap
Ashford	£20.6m	£4.5m	£16.1m
Surrey Hills to Fleet	£43.7m	£26.6m	£17.0m

Why the PR24 Ashford and Surrey Hills to Fleet schemes are different from the PR19 schemes

3.11 It is important to note that even though the original PR19 schemes and the updated PR24 schemes have similar names and are clearly aimed to address issues in similar geographic areas, the specific solutions we have submitted are significantly different from each other.

3.12 The PR24 Surrey Hills to Fleet scheme comprises a [redacted], and the PR24 scheme will be able to protect water supply system pressures [redacted].

3.13 The PR24 Ashford scheme will take water [redacted] as proposed at PR19 and comprise a [redacted]. The scheme will protect water supplies [redacted] and provide a range of additional secondary benefits including resilience in the wider areas and protecting abstraction licenses in

different systems.[31] Ofwat has agreed with the need for these schemes, and it is not the case that Ofwat has previously funded these specific improvements.[32]

Inconsistency with the CMA's assessment of the under-delivery adjustments in base

3.14 As part of its assessment of base expenditure, the CMA considers both the relevant economic considerations related to under-delivery, and whether it is feasible to identify under-delivery in the context of companies' PR19 investments (including areas such as meter replacement and mains renewal).[33] In doing so, the CMA reaches a view on whether it is appropriate to apply PR19 under-delivery adjustments to base costs for PR24. Ultimately, the CMA concludes that it is not appropriate to do so.

3.15 Despite this conclusion for base expenditure, the CMA considers it remains appropriate to apply a PR19 under-delivery adjustment to our Surrey Hills to Fleet and Ashford schemes. We note that these schemes were part of base expenditure (CACs) at PR19, and we consider that the logic applied by the CMA in its assessment of base expenditure should also apply to these schemes.

3.16 However, we understand that the key logic behind the CMA's decision to retain an under-delivery adjustment here is that the scheme in question was 'named' at PR19, and that this makes the identification of under-delivery possible.

3.17 Our view is that the **CMA's logic and reasoning for base expenditure are applicable regardless of whether the PR19 expenditure was part of a named scheme** and that the CMA's retention of an under-delivery adjustment here is therefore inconsistent with its decision in its assessment of base costs. To demonstrate this, we consider the elements of the CMA's reasoning and approach to base expenditure in turn below.

The economic considerations related to under-delivery

3.18 In assessing base expenditure, the CMA first sets out its view of the relevant economic considerations related to under-delivery adjustments. We agree with the CMA's position on these economic considerations. Specifically, we agree with the CMA that:

(a) There are both 'fairness' (for customers) and 'efficiency' arguments which could in-theory justify retrospective adjustments in cases of under-delivery. However, before any adjustments apply, it is first necessary to establish clear and compelling evidence that a company's expenditure decisions represent 'gaming' of the regulatory settlement and are not a result of the company using "*the flexibility afforded to [companies] by the outcome-based regime for legitimate purposes*".[34] In addition, fairness also needs to be considered from the company's point of view. Without a scheme-specific ODI and with the flexibility of the totex and outcomes regime as designed by Ofwat, we operated in good faith by re-prioritising our investment programme. At the time of making these decisions, we could not have foreseen that Ofwat would retrospectively make adjustments at PR24 as none of the price control mechanisms at PR19 were set up in this way. If we had known that Ofwat would disregard the PR19 totex regime they designed and effectively apply a retrospective scheme-specific ODI, we might have taken a different course of action. Importantly this would also have affected our in-the-round assessment of the PR19 Final Determinations, and whether to request a referral to the CMA for Redetermination at that time.

(b) There may be negative unintended long-term consequences if such adjustments are applied in cases that are unjustified. If companies expect the regulator to claw back genuine efficiency savings, they may avoid making them, leading to higher long-term costs for customers and reduced investor confidence due to greater regulatory uncertainty.

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31 See SEW, July 2025, Response to CMA RFI05, Table RFI5.4 for a more detailed description of the key differences between the PR19 and PR24 schemes.
32 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.494.
33 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.423.
34 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.427.

(c) Given this, under-delivery adjustments should be reserved for cases where *"gaming can be established based on convincing evidence",*[35] and there should be a 'high evidence bar' for doing so in the case of a company that was overspending its totex allowance.

3.19 When a scheme is named, evidence of 'gaming' would involve the company not delivering a scheme that is technically feasible and would still deliver the identified benefits for customers. In this situation, the company would have justified a higher allowance on the basis of the need for the schemes but then decided not to deliver the schemes despite technical feasibility and no change in the costs and benefits to customers. However, if the scheme is no longer technically feasible or the benefits to customers are now expected to be much lower than emerging alternatives, this is not evidence of 'gaming' but instead part of managing ongoing changes in circumstances and new risks to customers. In these instances, the company needs to re-prioritise its investment schemes using *"the flexibility afforded to [companies] by the outcome-based regime for legitimate purposes"*. As discussed at length in our response to SEW RFI05,[36] the PR19 Ashford scheme would not have delivered any benefits to customers and the PR19 Surrey Hills to Fleet scheme became technically infeasible. Therefore, the CMA's conclusion that the regulator should 'tread carefully' when making retrospective adjustments should also apply in the case of the PR19 Surrey Hills to Fleet and Ashford schemes.

Identification of under-delivery

3.20 Having concluded that the same economic considerations are relevant, the key question then is whether certain components of PR19 base expenditure being part of 'defined' or 'named' schemes have different implications for the identification of under-delivery.

3.21 On identifying under-delivery, the CMA notes that, in principle, deciding whether companies have under-delivered would require assessing their investment decisions after the period in question and determining whether these were consistent with good management, given the information available at the time. The CMA notes that *"to understand whether a company has under-delivered requires consideration of activity levels across its asset base 'in the round' and the reasons behind the investment decisions they have taken"*.[37]

3.22 Again, we see no reason for this logic not to apply in the case of named schemes. The naming of schemes simply allows us to establish that a scheme has 'not been implemented', but this is different from 'under-delivery'. There is a clear distinction.

3.23 There is a further point on the schemes being 'named' and whether the non-delivery of these schemes constitutes an under-delivery. At PR19, Ofwat had the ability to attach ODIs to specific outputs to ringfence funding for schemes that had to be implemented within the period. Even though Ashford and Surrey Hills to Fleet were both named schemes, there was no separate funding allocated to them in the form of bespoke ODIs (as was the case for Wellwood to Potter's Corner, for example). The lack of a bespoke ODI associated with these schemes means that Ofwat's funding was not contingent on the delivery of these precise schemes. If Ofwat wanted to ensure at PR19 that the PR19 Ashford and Surrey Hills to Fleet schemes were delivered, it could and should have used a bespoke ODI. The lack of a bespoke ODI demonstrates that the funding was part of a base cost adjustment intended to deal with a range of issues but without an expectation of delivering each named scheme.

3.24 The key question, as acknowledged by the CMA in its assessment, is whether we have *"secured equivalent or better outcomes through alternative schemes that would not otherwise have been delivered"*.[38]

3.25 Using the CMA's own principles, an assessment of *under-delivery* would require a full understanding of the counterfactual, and an *'in the round'* assessment of past delivery across the asset base, even for named schemes. The CMA has concluded that it has not been possible to carry out such an assessment for base costs due to the limited availability of activity-level data.

[35] CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.429.
[36] SEW, July 2025, Response to CMA RFI05, paragraphs 29(a) and 39.
[37] CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.4.
[38] CMA, October 2025, Provisional Determinations, Volume 1, Chapter 5, paragraph 5.497.

We agree with the CMA's conclusion and note that, for the reasons set out above, there is no reason to believe that the same data limitations are not applicable to named schemes.

3.26 The CMA also acknowledges that, even if such data were available, this assessment would *"require complex judgements about how trade-offs between investment in asset categories were made to understand whether the investment was prudent."*[39] Despite these difficulties, in our response to SEW RFI05 we have provided evidence that our schemes represent better value for customers.[40] We cover this in more detail below.

3.27 Given the CMA concludes that an 'in the round' assessment is not possible, the following factors influence its decision to remove the PR19 under-delivery adjustment for base expenditure:

(a) The CMA notes that *"in its PR19 FD Ofwat did not set out any specific targets for levels of expenditure or maintenance activities other than high-level top-down totex allowances and outcomes targets"*.[41] This is true and is applicable here. While the allowance for the PR19 Surrey Hills to Fleet and Ashford schemes was estimated in advance in determining the CAC, this did not constitute a 'target'. As stated above, Ofwat did not apply a bespoke ODI.

(b) The CMA considers the fact that there was substantial overspend across many companies and the industry as a whole during AMP7 *"does not clearly support a conclusion that companies have under-delivered"*.[42] As we note below, this is also a relevant consideration for determining under-delivery here, given the need for 'in the round' assessment across past activity.

(c) The CMA uses examples from companies that had to re-prioritise their programmes. This includes the sinkhole that appeared under one of the service reservoirs in Maidstone, an example we provided as a reason for the reprioritisation we undertook at PR19.[43] It is unclear how the CMA can use this example to justify the removal of an under-delivery adjustment in base, but not consider it relevant to its decision to retain the adjustment here.

(d) The CMA considers the risk of potential unintended consequences, such as those described above, as a result of unjustified adjustments suggests caution is necessary. As above, there is no reason this does not apply to named schemes.

3.28 Therefore, having considered the CMA's rationale for removing Ofwat's under-delivery adjustments on base expenditure, we see no reason the same rationale should not directly apply to the PR19 Surrey Hills to Fleet and Ashford schemes. The CMA's provisional decision to retain the under-delivery adjustment here is inconsistent.

PR19 overspending

3.29 Another key point of context is our overall overspend in PR19. The CMA has acknowledged the importance of this point in its discussion of base costs, stating that *"whilst [the overspend] may have been driven to a substantial extent by unforeseen events, overall this does not clearly support a conclusion that companies have under-delivered"*.[44]

3.30 Over PR19, we have overspent our totex allowance by £153m.[45] This means that we used more resources than anticipated to deliver customer benefits and manage emerging risks, and we demonstrate below that we delivered more benefits than our original programme estimated.

3.31 Our overall programme overspend alone might not be sufficient to justify the case for these schemes, but it provides important context for the activities that were undertaken to deliver outcomes customers paid for, and the requirement to reassess and reprioritise our activities

39 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.433.
40 SEW, July 2025, Response to CMA RFI05, section 'Customer benefit' under answer to Question 1.
41 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.437(a).
42 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.436.
43 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraphs 4.435(c).
44 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.437.
45 Ofwat, October 2025, Water Company Performance Report 2024-25.

against a significant cost challenge to our resilience and growth, and network development totex programmes.

Equivalent benefits provided to customers in response to new and emerging risks

3.32 In addition to under-funding, we were faced with significant new and emerging risks during AMP7 which we discussed in detail in our response to SEW RFI05, including water quality and resilience risks.[46]

3.33 We agree with the CMA (and Ofwat) that the test following non-delivery should be whether customers have received the benefits they have funded, even if this has not been via specific named schemes. This is to ensure that customers receive at least the benefit that was agreed at the time of price setting for the given bill level. **The first question is therefore: What level of benefit were customers expecting from the PR19 interconnectors?**

3.34 The table below shows the expected Benefit Cost ratios from the submitted PR19 interconnector schemes, as submitted in our PR19 business plan. To reiterate, this is not ex-post analysis, but the ex-ante benefits we were expecting to realise when the PR19 schemes were first proposed. The below table means that for every £1 spend on Surrey Hills to Fleet and Ashford, we were expecting to realise £3.27 and £2.50 of benefits for customers respectively.

Table 3.3: PR19 interconnector schemes – expected Benefit Cost ratios at PR19

Scheme	Expected BCR[47]
PR19 Surrey Hills to Fleet	3.27
PR19 Ashford scheme	2.50

3.35 **The second question is whether the alternative schemes delivered higher or lower net benefits to customers.** We have demonstrated that customers have received greater net benefits from our re-prioritised programme in our response to RFI05.

3.36 The table below lists the Benefit Cost ratios that we estimated for the additional schemes delivered during AMP7.[48]

Table 3.4: SEW RFI05 Benefit Cost ratio for additional schemes at PR19

Category	Scheme	Benefit to customers	Benefit Cost Ratio (BCR)
External factors	Resilience Action Plan in response to supply interruption incidents	Avoided risk of more frequent supply interruptions	5.81
Water Quality	Disinfection to improve water quality in Kent, Sussex and Hampshire	Avoided risk of more frequent supply interruptions and drinking water notices	13.00
Water Quality	Address saline intrusion in our boreholes at [redacted]	Avoided risk of more frequent supply interruptions	2.57

46 SEW, July 2025, Response to CMA RFI05, paragraph 10.
47 SEW, July 2025, Response to CMA RFI05, Table RFI5.3.
48 SEW, July 2025, Response to CMA RFI05, Table RFI5.7.

Category	Scheme	Benefit to customers	Benefit Cost Ratio (BCR)
Water Quality	Containerised ultraviolet treatment plan to enable a quick and agile response to crypto or disinfection risks following an increase in turbidity in the raw water	Avoided drinking water notices	31.22
Water Quality	Reservoir maintenance in response to DWI notice	Avoided risk of more frequent supply interruptions	26.77[49]
Unexpected event	Sinkhole under a service reservoir in Maidstone	Avoided drinking water notices	26.71
Unexpected event	Unexpected repair of a strategic water tank at [redacted]	Avoided risk of more frequent supply interruptions	8.04
Network reinforcement	Additional network reinforcement expenditure to enable housing developments and protect the resilience for existing customers	Avoided incidents of low pressure	3.85

3.37 The Benefit Cost ratios were estimated based on actual scheme costs and the estimated benefits of avoiding the identified risks for each scheme.

3.38 These risks comprised low pressure, water supply interruptions, and water quality notices. To quantify the benefits, we estimated the likely duration of any disruptions, the number of properties that would likely be impacted by each disruption and monetised the benefits using GSS payments. This is because GSS payments provide compensation for the minimum level of service and therefore should represent at least the amount customers value avoiding an interruption. GSS payments also provide a consistent valuation source as water quality notices are generally not covered in WTP surveys. This is a conservative approach as willingness-to-pay values for supply interruptions would lead to higher Benefit Cost ratios.

3.39 The alternative activities that we delivered consisted of a mix of reactive schemes that responded to emerging issues that posed immediate risks to customers, and proactive schemes that were aimed to address emerging future risks. We found these Benefit Cost ratios to be larger than those submitted for the Ashford and Surrey Hills to Fleet schemes at PR19.

3.40 The impact on customer benefits from our re-prioritisation is that customers received between £2.57 and £26.77 for every £1 spent on alternative schemes (in contrast to £3.27 in benefits for every £1 spent on the PR19 Surrey Hills to Fleet schemes and £2.50 in benefits for every £1 spent on the PR19 Ashford scheme). Customers are clearly better off with the prioritisation.

3.41 **The third question is whether customers would have received the benefits that were expected if we had continued to deliver the PR19 schemes as proposed at PR19**.

3.42 Table 3.5 below shows that customers would have received no benefits from the PR19 Ashford scheme. This is because the spare water that was expected to be connected to Ashford was no longer available due to increased local demand requiring all the available water up to the abstraction license total.[50] For the PR19 Surrey Hills to Fleet scheme, customers would have received fewer benefits than costs as the technical constraints would have meant that the costs would have exceeded benefits. Note that the 'Customer benefit' section in our response to

[49] This is a conservative estimate based on a 1-week interruption as a 4-week interruption is plausible.
[50] SEW, July 2025, Response to CMA RFI05, paragraph 29(a).

Question 1 in RFI05, as well as Annex RFI5.1, discuss these points in extensive detail. It is clearly not in customers' interests to pursue schemes that do not provide net benefits, particularly when other highly cost beneficial schemes have emerged.

Table 3.5: PR19 interconnector schemes outturn Benefit Cost ratios

Scheme	Outturn BCR[51]
PR19 Surrey Hills to Fleet	Technically not feasible – working around the environmental constraints would have increased costs to reduce BCR below 1
PR19 Ashford scheme	0

3.43 Even with the schemes in question being named and explicitly funded, not delivering the schemes should not mean that we lose the allowance, as we have demonstrated that customers have received equivalent or better outcomes through alternative schemes.

3.44 **The fourth question is what other actions were available to us at PR19.** This is also linked with how the CMA defines "equivalent outcomes" or "schemes that would not have otherwise been delivered". We discuss this further by defining different counterfactuals below.

3.45 We cannot demonstrate equivalent benefits for the same customers as PR19 Ashford and Surrey Hills to Fleet schemes, as these schemes were designed to address future growth and risks, without any available alternatives. However, we can demonstrate better outcomes for other customers, who were faced with more immediate risks.

3.46 In the face of the PR19 Ashford and Surrey Hills to Fleet schemes becoming infeasible, there were different hypothetical options that we could have pursued:

(a) **Option 1: Deliver Ashford and Surrey Hills to Fleet and not deliver schemes to address emerging risks**. This would have ultimately led to some treatment works being non-compliant and not being able to be used. It would also mean that we would have deliberately spent money on schemes that are not delivering net benefits to customers. This is clearly not acceptable.

(b) **Option 2: Not deliver Ashford and Surrey Hills to Fleet, deliver alternative schemes that would benefit customers in the same geographical areas with equivalent or better outcomes**. This was not an option that was available to us. If delivering alternative schemes to deliver equivalent or better outcomes was possible in the first place, these schemes would have been submitted in place of our PR19 schemes. When it became apparent that the Surrey Hills to Fleet and Ashford schemes could not be delivered in their original form, we started planning for alternative schemes. This is what led to the development of the PR24 schemes. It has taken time to develop these schemes so we could not have pivoted towards these schemes early in AMP7 and by the time the schemes were ready we had to submit our PR24 business plan.

(c) **Option 3: Not deliver Ashford and Surrey Hills to Fleet, progress other strategic projects where possible and take a more proactive approach to emerging risks**, ultimately leaving customers better off, notwithstanding that these customers were not in the same geographical area and did not receive the same kinds of benefits as the Ashford and Surrey Hills to Fleet schemes. This is the approach we took while also working on alternative strategic plans to overcome the issues with the PR19 schemes.

3.47 It seems that the CMA and Ofwat are suggesting that we should have undertaken Options 1 or 2 at PR19, where these were not in customers' interests and infeasible respectively. Option 2 was

[51] SEW, July 2025, Response to CMA RFI05, Table RFI5.3.

not available immediately as it took time to develop and investigate alternative schemes to the PR19 interconnectors. Option 1 would imply that we should deliver agreed schemes without applying any sense checks, which is clearly not in customers' interests.

3.48 Retaining Ofwat's decision on the under-delivery adjustments would therefore introduce clear incentives to the water sector to deliver named schemes regardless of the outturn benefit of these schemes. This is shown in our example of hypothetical options, where the Ofwat decision (and the CMA's provisional decision) would mean that Option 1 would likely have been the most financially advantageous action for us to have taken. This leads to higher bills without additional benefits and is not in the interest of customers. This is a point that the CMA has cautioned against in its discussion of under-delivery adjustments: *"[..] unjustified adjustments could undermine incentives to make savings, leading to higher bills"*.[52] It means water companies should be more concerned with the requirements of regulators at fixed five-yearly price control review points, rather than evolving customer needs in the face of changing circumstances.

3.49 We disagree with the CMA's provisional decision position and have demonstrated that our actions do not constitute under-delivery. Our actions also reflect the flexibility that was part of the regulatory framework at PR19, which allowed us to change our delivered activities to respond to new information on feasibility of schemes and emerging risks. The CMA's characterisation of the outcomes of alternative schemes *as "different benefits which were not subject to the same regulatory scrutiny"*[53] overlooks the circumstances under which these benefits were delivered, with the non-delivered schemes no longer having the benefits that had been identified at the 'point in time' of regulatory scrutiny.

3.50 We maintain that any other action at PR19, upon discovering the infeasibility of the relevant schemes, would have led to no realised benefits for customers than the actions we have taken, and request that the CMA award us the full allowance for our Ashford and Surrey Hills to Fleet schemes.

Groombridge/Row Dow to Kemsing

3.51 We disagree with the CMA's provisional decisions on Groombridge and Row Dow to Kemsing. It is not correct that other companies have been addressing climate change adaptation activities via base. Various enhancement schemes have been allowed by Ofwat to address the impacts of climate change (including the climate resilience scheme submitted by Northumbrian, and the sector-wide climate change uplift).[54] We did not accept the climate change uplift as our resilience programme has provided a more company and region-specific assessment of the required expenditure, rather than a wholesale 0.7% uplift.[55]

3.52 The CMA's proposal to maintain Ofwat's 20% base overlap costs challenge for our climate change related enhancement schemes puts us at a risk of not delivering the required upgrades to address anticipated extreme weather events in the near future. We have previously discussed the increasing climate change risks applying to our region in detail.[56]

Bloodshots to Darnley/Oakhanger to Alton

3.53 We disagree with the CMA's provisional decisions on Bloodshots to Darnley and Oakhanger to Alton. Bloodshots to Darnley does not just address growth in demand, but also addresses a resilience need.[57] On Oakhanger to Alton, the CMA has mischaracterised the evidence provided – we were unable to provide quantification of [redacted] as this scheme was selected through the WRMP process. This is an example of how the re-categorisation of our

52 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.429.
53 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.501.
54 Ofwat, December 2024, Water resilience enhancement expenditure model.
55 See response to query OFW-REP-SEW-069.
56 AtkinsRéalis, April 2025, Adaptive Planning Scenarios.
57 SEW, March 2025, Statement of Case, Annex G, paragraph 88.

supply interconnector schemes as resilience interconnectors has put our schemes at a disadvantage, through a change in required evidence.[58]

3.54 Further, the cost efficiency of resilience interconnectors was checked by Ofwat in the supply interconnector model.[59] Our supply and resilience interconnector schemes were found to be cost efficient (in fact among the most cost efficient schemes considered across all companies), and there were no cost efficiency challenges applied by Ofwat. It is therefore unclear why the CMA is requesting evidence on cost efficiency at this stage, when Ofwat has only challenged the "need" for our schemes.[60]

Conclusion

3.55 We welcome the CMA's provisional decision to allow the Poverty Bottom scheme in full.

3.56 We disagree with the CMA's provisional decision on Ashford and Surrey Hills to Fleet, Groombridge and Row Dow to Kemsing, and Darnley to Bloodshots and Oakhanger to Alton. The PR19 under-delivery adjustments should be removed so as not to impose a retrospective adjustment to the PR19 regulatory regime, and the drivers for enhancement funding for our schemes should be reconsidered. Consequently, these investments should be allowed in full.

Bewl WTW

3.57 The CMA has assessed the case for Bewl WTW and provisionally awarded no funding. This is equivalent to a 100% challenge on the programme request and constitutes no change from Ofwat's FD.

Table 3.6: Total funding requested for Bewl vs Ofwat FD and CMA PD funding

Ofwat FD funding	SoC requested funding	CMA PD funding
-	£26.7m	-

Summary of the CMA's approach

3.58 The CMA has pointed at the lack of a *"clear and complete explanation at a network level"*[61] of the need for [redacted] at Bewl WTW following ongoing investments and those planned for AMP8.

3.59 The CMA has also stated that our SoC has not explained why the AMP7 upgrades have not translated to additional headroom at Bewl WTW, and the capacity requirement to meet peak demand has only been evidenced by reference to the Summer 2022 peak demand event with no additional comment on the circumstances around this event and the likelihood of similar events occurring in the future.

3.60 The CMA has also indicated that SEW could seek funding for Bewl WTW through the contingent allowance.

Our response

3.61 Throughout our Response, we have aimed to bring together information supplied in various submissions to Ofwat and the CMA to bring a wider network view of the needs case for Bewl WTW.

58 SEW, March 2025, Statement of Case, Annex G, paragraphs 80 to 85 for further discussion of this reallocation.
59 Ofwat, February 2025, PR24 Final Determinations: CA92 Water supply interconnectors enhancement expenditure model.
60 Ofwat, February 2025, PR24 Final Determinations: CA94 Water Resilience interconnectors enhancement expenditure model, tabs "SEW_1" and "SEW_2".
61 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.553.

3.62 We have also provided additional network-level exhibits to provide a comprehensive view of the need for the Bewl WTW case. We would welcome the opportunity of a workshop with the CMA to explain the technical details surrounding the network-level case and our wider network strategy, including interrelationships between various schemes.

3.63 We note that the resilience benefits from the Bewl WTW upgrade can [redacted], while the 15,000 figure the CMA has quoted[62] refers to the [redacted]. The additional resilience benefits are due to the [redacted] of Bewl WTW [redacted] in cases of local outages at other water treatment works.

Bewl WTW needs case and its interaction with other schemes

3.64 We reiterate that the needs case for upgrading Bewl WTW from [redacted] Ml/day to [redacted] Ml/day in AMP8 has been driven by the need to strengthen regional resilience and reduce water supply interruptions. We need to ensure that we have sufficient water supplies, not just at the water resource zone and not just on an average day, but in all supply areas and during peak demand times.

3.65 It is important to have a whole network explanation of how various schemes interact with each other, which we aim to do below. As covered in detail in previous submissions[63] and during the hearings,[64] the SEW network has been made up of the combination of smaller, separate water networks. This makes it particularly important for us to implement the right resilience schemes in the right locations.

3.66 The links between Bewl WTW, Burham WTW and Butler WTW have been questioned by Ofwat and the CMA throughout the Redetermination process. The table below shows the links at a high level, and we detail the improvements in each WTW and how they interact in the below.

Table 3.7: links between AMP8 upgrades at Butler WTW, Burham WTW and Bewl WTW

	AMP7 configuration	AMP8 configuration	Reason for change	Overlap with other WTWs
Butler WTW	[redacted]			
Burham WTW (bulk supply from Southern Water)				
Bewl WTW				

62 CMA, October 2025 Provisional Determinations, Volume 2, Chapter 5, paragraph 5.541.
63 SEW, March 2025, Statement of Case, "Our history and regions".
64 Outcomes Hearing Transcript, 30 June 2025, page 12.

	AMP7 configuration	AMP8 configuration	Reason for change	Overlap with other WTWs
	[redacted]			

3.67 The diagram below shows a simplified map of our network configuration at AMP7 (before the AMP7 improvements at Bewl WTW were implemented). We have developed this to assist the CMA in understanding the needs case for Bewl WTW, including details where relevant and simplifying our network to make it easier to understand.

Figure 3.1: Simplified network configuration at AMP7 (before the AMP7 improvements at Bewl WTW were implemented), including demand recorded during the 2022 peak demand event [Confidential Figure - including text box below]

Table 3.8: Average flows in and out and sub zonal transfers in RZ7 during peak demand 2022 (AMP7 configuration)

	In to Bewl WIS (Ml/d) [1]	Out of Bewl WIS (Ml/d) [2]	Demand (Ml/d) [3]
[redacted]			

Interaction with Butler WTW and Burham WTW

3.68 The CMA has stated that we have *"not previously mentioned [the] works in the Butler WTW area in [our] submissions on the need for further investment in Bewl, and did not, therefore, address any implications these works might have for the Bewl investment"*.[65] We addressed the impact of works at Butler WTW in our DDR detailing the Bewl WTW upgrade.[66]

3.69 The Butler WTW is a newly commissioned [redacted]Ml/d treatment works with a completion date of September 2025. It serves around [redacted] both in the [redacted] and in [redacted].

[65] CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.560.
[66] SEW, 2024, SEWDD2b - Response on cost assessment - Resilience and Security - Resubmission 200924, page 46.

The Ashford scheme is of [redacted] and is discussed in further detail in paragraph 3.9 onwards). The population served by Butler WTW and Burham WTW [redacted], [redacted].

3.70 [redacted]

Figure 3.2: Overview of River Medway Scheme [Confidential Figure]

[redacted]

Why do we need to [redacted] at Bewl WTW if we now effectively have spare capacity at Burham WTW?

3.71 Bewl WTW and Burham WTW are 28 km apart and serve different population areas. Treated water can only be minimally moved between these areas [redacted] – see diagram above. This means the treated water available at

67 SEW, March 2025, Statement of Case, Annex G, paragraphs 19 and 20.

68 Currently, 1.7-2.1 Ml/d can be transferred through this main. A large reinforcement scheme has previously been considered to move more water from RZ6 to RZ7, see alternative option KRN003d submitted as part of SEW10 Combined Dossiers. This would require a new main from Linton Park SR to Curtisden Green SR, installation of a new main and booster between Cranbrook SR to Bedgebury SR, and increase the storage capacity at Bedgebury SR. This option was

[redacted]. In addition, Burham WTW is at the northern edge of our supply area and therefore only reaches [redacted] In contrast, Bewl WTW sits in the [redacted]. The diagram below illustrates this by showing the areas that can be reached by Bewl WTW at [redacted]Ml/d.

How does this interact with the AMP8 upgrades at Burham WTW?

3.72 Burham WTW is operated by Southern Water and there are plans to upgrade the treatment works to be compliant with DWI requirements and for resilience. The upgrades will return the site to its original design capacity of [redacted] Ml/d. The site is currently operating at [redacted]Ml/d due to restrictions including water quality. As such, current planned upgrade works will not increase the [redacted] at Burham WTW but rather enable [redacted].

Why does the AMP7 upgrade not lead to sufficient headroom?

3.73 The CMA has also questioned why the Bewl WTW upgrades at AMP7 have not provided additional headroom at Bewl WTW. It has referred to the evidence we provided on supply during the 2022 peak demand event to argue that there should be [redacted]Ml/d additional headroom at Bewl WTW following the AMP7 upgrades.[69] To be clear, Bewl WTW does not have spare headroom going into AMP8, as the AMP7 upgrade has been a direct replacement of the loss of Darwell reservoir.

3.74 To understand why Bewl WTW with [redacted] Ml/d does not have spare headroom, it is important to consider not only the supply side but also the demand side. The evidence we provided on Bewl WTW flows during the 2022 peak demand event shows that the full [redacted] Ml/d capacity at Bewl WTW was required. Importantly, this was not sufficient to meet demand in the region and, at that time, [redacted]. Significant supply interruptions occurred at this time, with around[redacted] affected and 19.8 interruption minutes per property,[70] even though Bewl WTW was operating at full capacity. This means that in a similar extreme weather event in the future and due to the inclusion of [redacted], the AMP7 upgrades will not provide any additional headroom against these levels of peak demand.

Why do the AMP7 upgrades not translate into additional headroom if we expected to supply [redacted]and now only need to send [redacted] Ml/d from Bewl WTW?

3.75 Hazards Green WTW is a surface works [redacted].

3.76 In our SoC, we described how in the summer of 2022 [redacted]transferred [redacted] Ml/d to Hazards Green[71] and, as stated above, the demand around Bewl WTW exceeded the capacity.

3.77 In addition, and to further support the need for redundancy, there have been instances where Hazards Green WTW has required the full [redacted]Ml/d from Darwell bulk supply due to low river levels (which usually coincides with extreme weather events linked to peak demand) or poor river water quality. [redacted].[72]

discounted given the complexity of work (installing new mains in rural area) compared to to increasing the WTW capacity on an existing site.

69 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraphs 5.556 to 5.557.

70 SEW, March 2025, Statement of Case, Annex F, Table ANF10.

71 After the AMP7 upgrades, Bewl WTW does not directly supply Hazards Green WTW but supports the WTW by supplying RZ3 via Bedgebury flows and supporting Barcombe via Cottage Hill SR (which supports Arlington WTW in turn). These flows allow Hazards Green WTW to supply RZ3 and reduce support to other WTWs.

72 See “Darwell Volume Output to SEW”, provided together with this Response.

3.78 This means that, effectively, the increase in peak demand and the requirement to [redacted] erodes any additional supply-side headroom from our AMP7 upgrades.

Overview of interactions between [redacted]

3.79 The diagrams below show the links between the WTWs in question and the supply-demand balances in areas that are served from each WTW, comparing the PR19 configuration against the proposed PR24 configuration. We use WRMP 2028 peak demand to calculate the surplus/deficit in RZ7 under each configuration.

Figure 3.3: Simplified network configuration including all AMP7 and AMP8 investments except for Bewl WTW, under 2028 peak demand [Confidential Figure - including text box below]

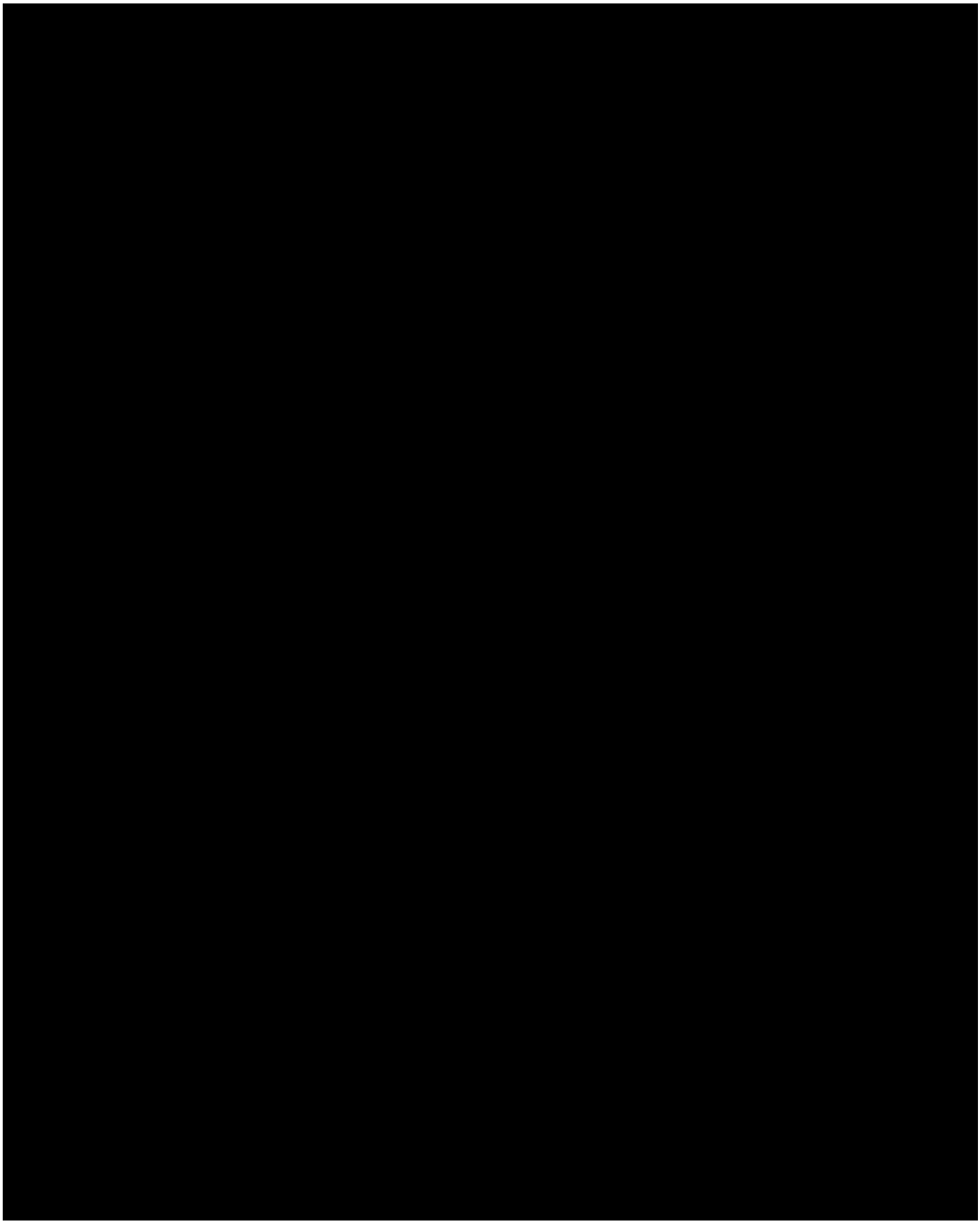


Table 3.9: Average flows in and out and sub zonal transfers in RZ7 under 2028 peak demand with Bewl WTW at [redacted]Ml/d

	In to Bewl WIS (Ml/d) [1]	Out of Bewl WIS (Ml/d) [2]	Demand (Ml/d) [3]
[redacted]			

Figure 3.4: Simplified network configuration including all AMP7 and AMP8 investments including Bewl WTW upgrade to 30 Ml/d, under 2028 peak demand [Confidential Figure including text box below]

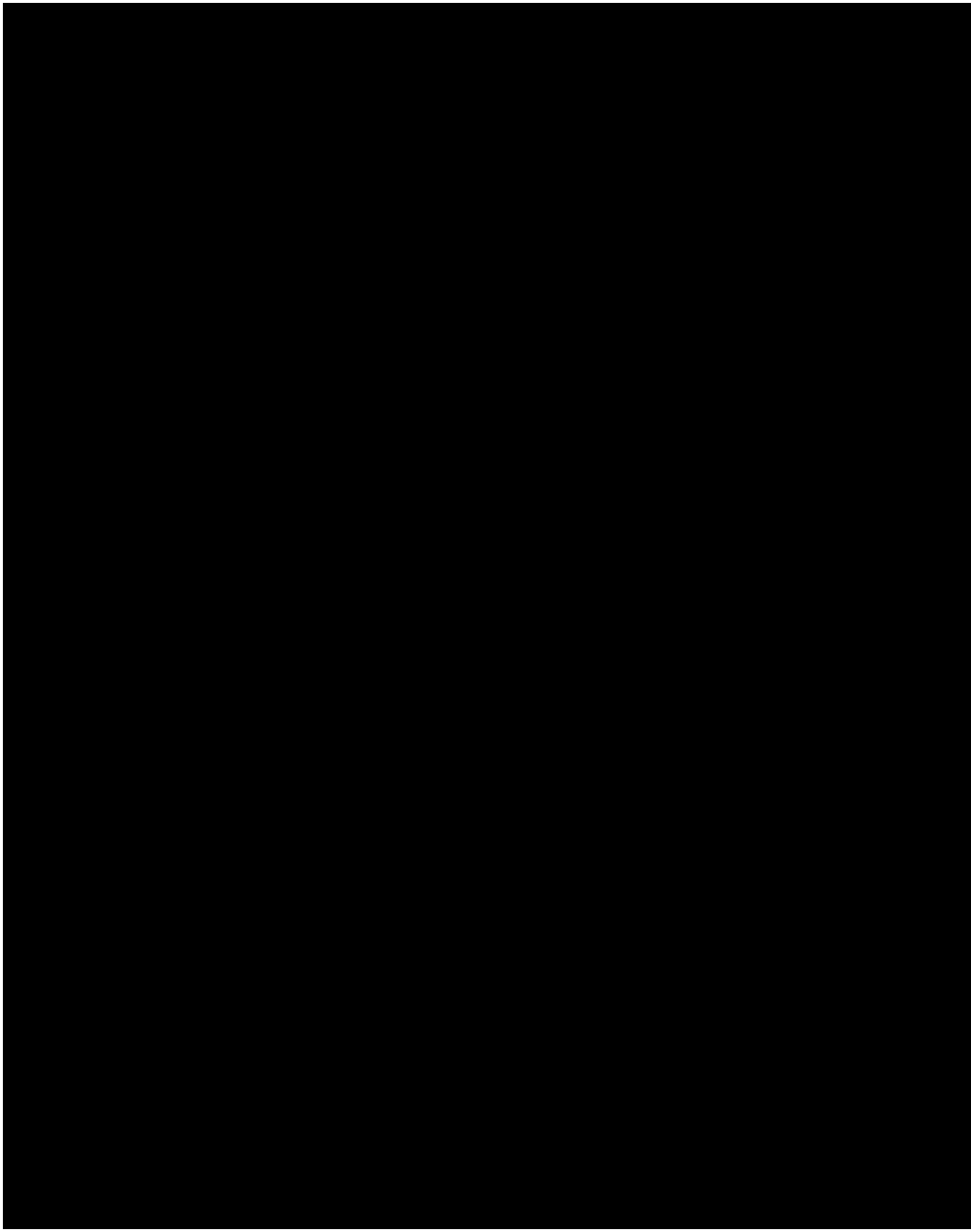


Table 3.10: Average flows in and out and sub zonal transfers in RZ7 under 2028 peak demand[73] with Bewl WTW at ■Ml/d

	In to Bewl WIS (Ml/d) [1]	Out of Bewl WIS (Ml/d) [2]	Demand (Ml/d) [3]
[redacted]			

[73] The Dry Year Critical Period used in WRMP provides a design headroom of around 8%, or 2.3 Ml/d. All Bewl deficits and surpluses calculated are based on this DYCP estimate that includes the design headroom. Headroom assessment is a key component of our baseline supply-demand balance calculations and is aimed to address uncertainties in our forecasts. For WRMP24, we anticipate a headroom allowance of 7.2% - 8.3%. Our headroom assessment is in line with the latest version of the Water Resources Planning Guideline. See SEW, October 2024, Water Resources Management Plan 2025 to 2075, pages 67-68, and SEW, October 2024, Headroom assessment: WRMP24 Technical Report, page 9. Our surplus calculation also assumes that leakage is reduced and customers engage with our water efficiency initiatives and reduce their water consumption. Temporary leakage breakouts can occur during extreme weather events (from movements in the ground due to it drying out), and we currently have no proof that reducing overall PCC will have an equal impact on peak demand during extreme weather events. A customer may reduce their consumption all year but may change behaviour as a result of hot weather. These factors mean that it is not clear how much of the surplus we have estimated will translate into a genuine surplus during an extreme weather event.

Summary of interaction with Butler WTW, Burham WTW and Hazards Green WTW

3.80 In summary, the upgrade at Bewl WTW is:

(a) Required to avoid further supply interruptions as a result of extreme weather events as we have observed 4 times in the last 5 years;

(b) Not negated by extra capacity at Burham WTW as the populations served do not overlap extensively and there is minimal interconnection (the expansion of the interconnection between [redacted] has previously been considered as an alternative option but discounted due to project complexity);[74]

(c) Needed on top of the AMP7 upgrade even if Hazards Green WTW at times only requires 4 Ml/d – because there have been [redacted] and the increase in peak demand in the population served by Bewl WTW is higher than any headroom delivered by the [redacted] Ml/d scheme;

(d) Enabled by [redacted], which enables us to take more water from [redacted].

Interaction with other PR24 upgrades

3.81 In our SoC, we quantified the resilience benefits associated with various enhancement schemes in isolation. We estimated Bewl WTW upgrades to bring 00:04:19 (4.31 minutes) of WSI improvements over AMP8 over and above other resilience schemes. The CMA has raised concerns with our quantification of water supply interruption benefits – see Section 5, paragraph 5.34 of this Response for further discussion. More widely, we have estimated Bewl WTW upgrades to contribute 11% of the water supply interruption benefits expected to be achieved by our investments at AMP8.[75]

3.82 The table below further demonstrates the number of customers impacted from recent major extreme weather events in areas served by Bewl WTW, and how allowed PR24 investments and Bewl WTW AMP8 upgrades would have changed these impacts. To demonstrate these impacts, we have conducted analysis which shows how the Bewl WTW upgrade and our wider enhancement schemes interact with the set of four severe weather events we experienced in AMP7.

3.83 First, we have identified the areas and properties that experienced supply interruptions during the Summer Demand events in 2020, 2022 and 2023, and the Freeze Thaw event in 2022. Using network schematics, we have then identified whether these areas would be supported by the PR24 schemes, by matching the relevant schemes to each impacted District Meter Area (**DMA**).

3.84 Using water balance data from each year, we have used data from the 'critical period' (the highest demand for the company during the reporting year) to calculate how many properties a megalitre of water can supply during the highest demand in the relevant year in each water resource zone. To be clear, the critical period demand does not necessarily correspond to the individual weather event stated, but instead with the highest demand in that given year. With this value, we can create an estimation of the amount of additional water needed to supply each of the properties interrupted in the relevant weather event.

3.85 Against this, we have assessed the amount of additional supply that our AMP8 schemes provide to the impacted areas. If this additional supply is greater than the estimated shortfall, then the schemes are deemed to be sufficient to have prevented the interruptions.

3.86 The results of this analysis are shown in the table below. As can be seen, while an estimate, our analysis suggests that the number of properties without supply in areas that can be supplied by

[74] SEW, March 2025, Statement of Case, Annex G, paragraph 88.
[75] Ofwat, PR24 Outbound Query, OFW-OBQ-SEW-116 company response to question 1.

Bewl WTW would have been reduced to zero in each of the four events analysed. This analysis demonstrates that our enhancement schemes are designed to address current risks and therefore should be taken into account when setting out company specific PCL.

Table 3.11: Number of customers impacted from recent major extreme weather events[76]

	How many properties were without water at the time that could be reached by Bewl WTW?	Estimate of customers impacted if allowed PR24 schemes were in place – without Bewl upgrade	Estimate of customers impacted if allowed PR24 schemes were in place – with Bewl upgrade
Summer Demand 2020 (Met office confirms >34degrees Celsius, 7th – 12th Aug 2020)	[redacted]	[redacted]	0
Summer Demand 2022 (Met Office red warning, and level 4 alert in July 2022)	[redacted]	[redacted]	0
Freeze Thaw Dec 2022 (12 nights sub-zero then rapid thaw on 18th/19th Dec to 14 degrees Celsius)	[redacted]	[redacted]	0
Summer Demand 2023 (Met office confirms hottest June on record)	[redacted]	[redacted]	0

2022 peak demand/return period – how frequently should we expect these extreme weather events to occur?

3.87 The CMA has agreed with Ofwat's position that there is no further information about resilience needs at Bewl WTW beyond the 2022 peak demand event.[77] At a minimum, the Dry Year Critical Period values we have used in WRMP (and for the design demand in the above diagrams) include a design headroom of around 8%, or [redacted] Ml/d. This headroom is currently not available at Bewl WTW.

3.88 The Bewl region experienced four separate extreme events over the last AMP (specifically over three years) that had significant impacts:[78]

(a) Summer Demand 2020 (Met office confirms >34degrees Celsius 7th – 12th Aug 2020).

(b) Summer Demand 2022 (Met Office red warning, and level 4 alert in July 2022).

(c) Freeze Thaw Dec 2022 (12 nights sub-zero then rapid thaw on 18th/19th Dec to 14 degrees Celsius).

[76] Note, property numbers from our modelling have been rounded to the nearest 50.
[77] CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.558.
[78] SEW, 2024, SEWDD2b - Response on cost assessment - Resilience and Security - Resubmission 200924, pages 46 to 51.

(d) Summer Demand 2023 (Met office confirms hottest June on record).

3.89 As part of our DDR, we also provided supporting evidence showing the future near-term need (AMP8) to address the continuing and worsening impacts of climate change (including the AtkinsRéalis Climate Scenario report SEWDD2b28).

3.90 The new Atkins analysis on the extreme heat and "hot spells" in our water resource zones, submitted to the CMA and main parties by email on 7 May 2025, has shown the increasing frequency of extreme weather events: *"Projected 1-in-100-year high temperatures (Probabilistic Extremes RCP8.5 median) have been observed with a 1-in-8-year return period since 2001"*.[79] This shows the extent of the challenge of climate change adaptation in our region.

3.91 Overall, we conclude that the frequency of such events at AMP7 and projected increases in extreme weather events indicate that 2022 peak demand was not a one-off event, and such extreme weather events should be anticipated with increasing frequency.

3.92 This will mean increased risk of supply interruptions in the Bewl region unless the Bewl WTW AMP8 upgrades are implemented. Our supply interruptions performance is clearly an area that customers want to see improvements in, and further investment is required to implement lasting solutions.

3.93 In this context, it is also important to consider the balance of risk from implementing Bewl WTW upgrades at this stage against the risks of the upgrades being unfunded. Any extreme weather events will lead to continued supply disruptions in the Bewl region in the near future without the implementation of the Bewl WTW upgrades, while the risk of funding Bewl WTW at this stage is that there might be no extreme weather events in the next two years and we will have increased the resilience of our network early.

Funding for Bewl WTW upgrades – why is the contingent allowance not the appropriate mechanism?

3.94 For the reasons outlined above, we consider that the Bewl WTW upgrades should be fully funded now to increase our network resilience and deliver the reduction in supply interruptions that our customers expect. It is not consistent with the consumer objective or the resilience objective for the CMA to assume that a further delay of up to 15 months to a clear funding decision enabling the commencement of upgrade works at Bewl is immaterial. There is a very real risk of extreme weather events occurring in that period which will pose continued water supply interruption risks to customers, and the CMA has the evidence to enable timely intervention to address and manage those risks.

3.95 A delay to the upgrade programme would also prevent us from maintaining the efficiencies planned using the existing design and construction team currently on site at Bewl as part of the AMP7 programme. This team could continue to deliver the AMP8 upgrade target, providing continuity and efficiency. However, if the programme is delayed in line with the CMA's provisional decision, SEW would need to demobilise the current team and later remobilise a new one, which would be inefficient and likely lead to higher cost, while prolonging the period during which customers in an area already affected at AMP7 remain at risk of further supply interruptions.[80]

3.96 As stated in our previous submissions,[81] the contingent allowance is not a suitable mechanism for funding Bewl WTW. This is because the contingent allowance, as specified by Ofwat, was designed to address future risks, whereas the Bewl WTW upgrade targets a clear and immediate need. Furthermore, allocating Bewl WTW to the contingent allowance would use over 50% of the total allowance (leaving £23.3m from the overall £50m fund) significantly limiting SEW's ability to manage actual future risks that emerge.

[79] AtkinsRéalis, April 2025, Adaptive Planning Scenarios, page 5.
[80] SEW, June 2025, Response to CMA RFI02, Question 4b.
[81] SEW, March 2025, Statement of Case, paragraphs 4.47 to 4.55.

3.97 If, in spite of the comprehensive additional evidence set out in this Response, the CMA is not minded to fully fund Bewl WTW in its Final Report, we propose that – as a fallback option – funding be provided through a gated allowance, rather than the existing contingent allowance, given the clear limitations to the latter described above.

3.98 We believe a gated allowance would be more appropriate for Bewl WTW, particularly given the significant complexities around its interactions with other schemes. This complexity around scope aligns with the criteria Ofwat applies to schemes funded via the gated allowance process.[82]

3.99 Since the upgrade of Bewl WTW is already at an advanced stage of development, the two-stage submission process that Ofwat envisages for large, gated schemes could be streamlined in this case. Alternatively, if the CMA does not support this, the Bewl WTW upgrades could be included in an "accelerated" gated allowance process, which would allow for quicker implementation and more effective delivery.

3.100 Under this approach, we request that the CMA sets a clear target date for approving the Bewl WTW upgrades. We suggest that within one month of the CMA's Final Report, Ofwat must outline a process and scope of work it would like us to complete with a final decision no later than 1 July 2026. This would ensure a timely, accelerated gated allowance process.

Conclusion

3.101 We do not agree with the CMA's provisional decision on Bewl WTW. We have demonstrated that there is a joined-up, network-level needs case for Bewl WTW that has considered other PR19 and PR24 investments. We have provided a more detailed network explanation, including a set of network configurations that include the benefits and supply/demand headroom from the AMP7 and AMP8 schemes. We have also shown that the 2022 peak demand event was not a one-off event, and similar events should be expected and planned for with increasing frequency.

3.102 The CMA should accept the need for the Bewl WTW upgrades and allow full funding, which will significantly improve the resilience of our network to future extreme weather events. We would welcome the opportunity of a workshop with the CMA to explain the technical details surrounding the network-level case and our wider network strategy.

Smart Network

3.103 The CMA has assessed the case for delivering a Smart Network and awarded £8m in funding across the Smart Network line and the relevant Leakage line ('new funding for investment in smart technology'). This is equivalent to an 83% challenge on the programme request and an increase of £8m relative to Ofwat's FD.

3.104 As outlined in our SoC[83], the total cost of our proposed smart network programme is £58.9 million. In our PR24 plan we separated out the proposed funding by allocating £48.1 million in the 'Smart Networks' line, and the remaining £10.8 million which we allocated to 'Other Leakage Activity'. Ofwat in its Final Determinations reallocated a further £11.3m from SEW's proposed Smart Network programme to leakage. We disagreed with the reallocation in our SoC.[84]

3.105 The table below provides a breakdown of the funding request included in 'Smart Networks' and allowances.

Table 3.12: Total funding requested compared with the Ofwat Final Determination and CMA Provisional Determinations allowance for Smart Networks

82 Ofwat, August 2025, PR24 large scheme processes guidance, page 4.
83 SEW, March 2025, Statement of Case, Annex G, paragraph 383.
84 SEW, March 2025, Statement of Case, Annex G, paragraph 397.

	Ofwat FD allowance	SoC requested funding	CMA PD
Smart network – additional funding for investment in smart technology	£0m	£36.8m	£0m
Leakage – new funding for investment in smart technology	£0m	£11.3m	£8m
Total	**£0m**	**£48.1m**	**£8m**

Summary of the CMA's approach

3.106 The CMA retains Ofwat's disallowance of £36.8m for the **smart network programme** for the following reasons:

(a) Considering engineering expertise provided by its independent engineering advisers WRc, the CMA acknowledges that the concept of a smart network could constitute a step change, particularly given the extensive deployment of sensors and relatively novel application of certain types of sensors.

(b) Despite this, WRc argues that we should have provided further explanation on how additional sensors would lead to improved outcomes for customer complaints, minutes lost as well as reductions in bursts and leaks.

(c) The CMA contends that "*South East has not provided sufficient and convincing evidence required to demonstrate that the planned investment […] goes beyond that which it could have been expected to deliver in this or previous price control periods funded through base allowances*".[85] To support this, the CMA refers to Ofwat's evidence on our performance relative to other companies, and investments made by other companies in smart technology.

3.107 For **leakage – new funding for investment in smart technology**, the CMA provisionally allows £8m, following Ofwat's view that an allowance should be included for trunk main meters following changes to leakage regulatory reporting.[86] This is based on allowing electromagnetic meters (£9.753m) with a 20% cost efficiency challenge (£7.802m) and four years of opex (£0.04m per annum), for the following reasons:

(a) Ofwat recommended that the CMA includes an allowance of £2.098 million based on ultrasonic meters for trunk mains (rather than electromagnetic meters).

(b) Based on WRc advice, the CMA considers that our preference for electromagnetic meters as discussed in RFI02 is justified.[87]

(c) However, the CMA applies a 20% reduction to estimated costs, as it questions the absence of *"detailed and externally verified costings"*,[88] and of a more detailed comparison of costs of electromagnetic meters and ultrasonic meters over an *"appropriate period"*.[89]

85 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.597.
86 Ofwat, April 2025, PR24 Redeterminations: Response to South East Water's Statement of Case, paragraph 4.42.
87 SEW, June 2025, Response to CMA RFI02, Question 2.
88 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.663.
89 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.663.

Our response

Is the smart network a step change that should be considered as enhancement expenditure?

3.108 First, the CMA has concluded that the smart network should be funded from base. We agree that small incremental changes to the number of sensors without software or integration across different technologies have been funded from base to date. However, we are now proposing to implement a full smart network where the investment delivers a step change greater than the sum of its parts. The Smart Network plan involves adding around 24,000 sensors, including 4,750 pressure sensors, and 19,000 acoustic sensors. This compares to approximately 5,000 pressure sensors and 600 permanent acoustic sensors today (constituting a 95% increase in pressure sensors, and more than 3,000% in acoustic sensors in our network). This is clearly a step change in terms of quantity. The CMA's technical advisors WRc said *"the smart network concept could be considered as a step change, in the sense that many more sensors are installed, and the use of some types of sensors is relatively new in water networks"*.[90] We agree with this assessment as it demonstrates that there is a difference in the scale and scope of the investment we are proposing and the activities covered by base expenditure in the past.

3.109 Second, the CMA appears to suggest that the smart network could have been funded from base in previous price control periods. As stated in the SoC, smart networks have only been available relatively recently.[91]

Do other companies fund smart networks from base?

3.110 The CMA mentions Ofwat's evidence on investment *"made by other companies in smart technology"* in its decision. Specifically, Ofwat states that *"Other companies delivered **smart network improvements** from base",* and that *"[…] other companies have successfully delivered **smart networks** through the maintenance and replacement of existing assets".*[92] It goes on to list a number of examples, reaffirming that *"[a]ll the above examples of smart networks have been achieved through these companies' base expenditure".*[93] We note that there is a difference between "smart network improvements" and "smart networks". Additionally, as far as we can tell from publicly available information, these investments are not comparable to our proposal because:

(a) they are generally small in scale and often relate to trials where companies have tested the benefits of potentially smart networks;

(b) many of the investments do not appear to include software;

(c) the funding routes do not only include base expenditure but also innovation funding and use of enforcement penalty funds.

3.111 We have run our own Smart Network trial. Based on a Veolia trial for a Smart Network in Lyon in 2011,[94] we commissioned a report from Veolia in 2018 to understand the likely scale of different benefits from our own smart network. This then resulted in a pilot in New Barn and Longfield (Kent),[95] costing £740k and covering approximately 2,100 properties. The trial involved deploying 1,785 digital customer meters, 159 network sensors and loggers (pressure, noise, water quality), two communications networks, and analytics software. The difference between this number and the 24,000 sensors proposed for our PR24 Smart Network plan shows a different order of magnitude. Results included a significant reduction in the time to find a leak, less water lost per burst, and the ability for the high consumption team to use live consumption data to proactively

90 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.595.
91 SEW, March 2025, Statement of Case, Annex G, paragraph 400.
92 Ofwat, April 2025, PR24 Redeterminations: Response to South East Water's Statement of Case, paragraph 4.52.
93 Ofwat, April 2025, PR24 Redeterminations: Response to South East Water's Statement of Case, paragraphs 4.52 to 4.58.
94 Link to Veolia site here.
95 Vodafone, 15 July 2019, Press release - Vodafone and South East Water trial narrowband IoT solution to help reduce water leaks.

contact customers before they knew they had an issue. It was also discovered that flow data and pressure data should be combined with acoustic data, supporting our argument that the Smart Network relies on a mix of sensors to function.

3.112 While this trial was funded from base, it is far from constituting a full Smart Network roll-out, which requires bespoke enhancement funding.

3.113 Below we set out investments mentioned by Ofwat, as well as further relevant investments, which are either smaller in size or scope than our proposed programme, and/or trials, similar to the trial we already ran and/or not funded from base expenditure.

Table 3.13: Comparison of other companies' smart network funded schemes

Company	Activity	Difference to SEW smart network
Affinity Water[96]	Automated meter readings combined with logging and network hydraulic models, AI tool	• This programme seems to have been discontinued, as these activities were not mentioned in their 2024 WRMP[97] • The programme does not seem to involve the installation of any additional sensors
Southern Water[98]	22,000 sewer level monitors	• This is a sewerage example, so it is not comparable • Given the length of the sewer network, this implies a significantly lower density of sensors than our Smart Network programme[99]
South West Water (via innovation fund project led by Anglian Water)[100]	"Safe Smart Systems" Software and algorithms	• This was funded via Ofwat Innovation Fund (£7.5m awarded)[101] • It is a trial only and does not involve hardware
Portsmouth Water[102]	500 "leak bugs": smart pressure sensors, machine learning	• This was described as a trial only, involving significantly fewer sensors than our Smart Network programme • It was most likely discontinued (in the business plan 2025 – 2030, the sensors were assessed as less cost-effective than other options)[103]

3.114 In addition, Northumbrian Water has been allowed to use £8.3m in funding as a result of an enforcement penalty for sewer smart network investment.[104] If all smart network investment could be funded by base, there would be no benefit to customers to allowing enforcement penalties to be used as investment in smart networks.

96 We matched this to a 2021 Affinity statement that they are using Automated Meter Readings with data from logging and network hydraulic models (Affinity Water Strategic Direction Statement 2021-2025).

97 Based on there being no relevant mention of artificial intelligence or hydraulic modelling in their 2024 WRMP, Affinity Water - Water Resources Management Plan 2024.

98 Southern Water, link to press release here and Higham Paris Council article here.

99 Southern Water's sewerage network is over 40,000km long (link to Southern website: here), whereas SEW's water network is 9,000 miles, or 14,500km long (link to SEW website: here). That means that Southern Water's 24,000 new sewer level monitors cover 2.76 times as much distance each on average than the 24,000 sensors proposed as part of the Smart Networks programme (not considering existing sensors).

100 Still in progress, with an estimated completion date of May 2026 (link to Ofwat Innovation Fund: here).

101 See link to Ofwat Innovation Fund: here.

102 Portsmouth Water, October 2024, Water Resource Management Plan.

103 Portsmouth Water, Business Plan Delivering Outcomes For Our Customers, Table 22.

104 Ofwat, link to press release here.

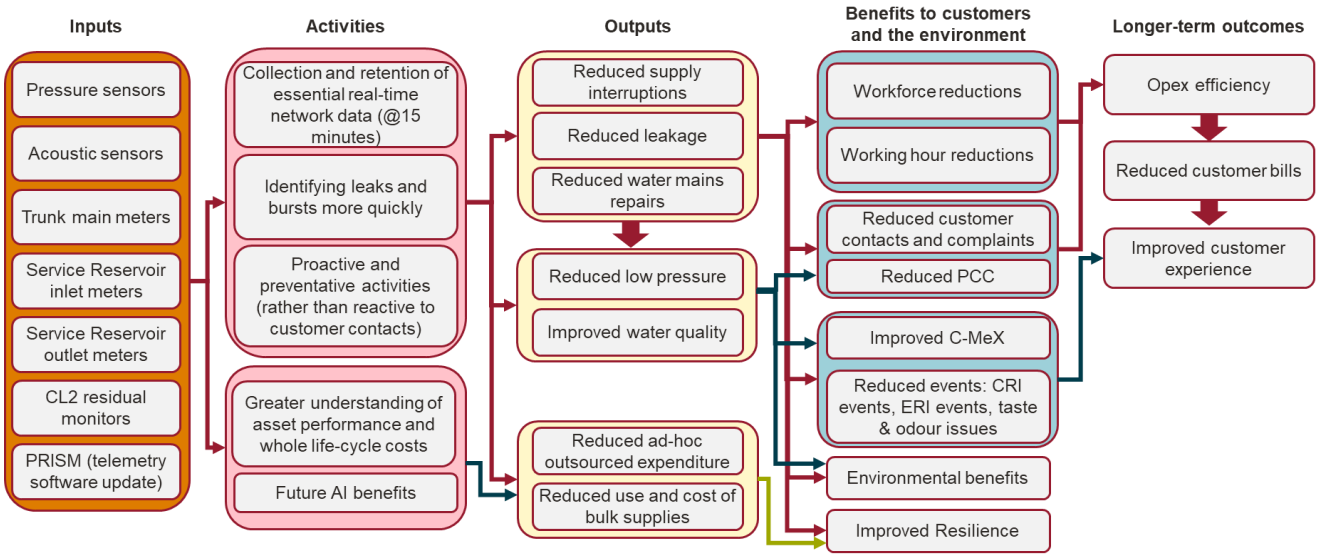
3.115 Overall, this demonstrates that the investments in smart networks made by other companies are not comparable to our proposal. It is unreasonable to expect us to fully fund the smart network from base when there is no evidence that other companies have done so.

What are the benefits to customers from the smart network?

3.116 We welcome WRc's invitation to explain the link between sensors and improved customer outcomes.[105] Below we set out (a) the link between these, and (b) the expected improvements.

3.117 The logic map below demonstrates how the inputs translate into short-term and long-term outcomes:

Figure 3.5: Logic model on the links between sensors and improved customer outcomes, and expected improvements



(a) First, it should be noted that specific benefits cannot be uniquely traced to specific sensors, as the benefits from the smart network are greater than the sum of its parts. Having sensors across the network allows an integrated detection and response – having half the sensors would provide less than half the benefits.[106]

(b) As explained in the SoC,[107] the smart network will help monitor **water quality** issues, specifically chlorine (215 chlorine residual meters) and turbidity. 19,000 **acoustic sensors** detect the noise from water leaking from pipes. 4,750 **pressure sensors** monitor pressure, assisting with near real-time data and information. **Service Reservoir meters** will help with ongoing monitoring of leakage and/or flow, and **strategic Trunk Mains meters** will further assist with identifying burst main locations.

(c) Using these and other elements of the smart network programme (for example, the telemetry software update), SEW will be able to collect and retain essential real-time network data (at a frequency of 15 minutes). This allows for both proactive and/or preventative activities (rather than waiting for customer contacts), and quicker identification and location of bursts and depressurisation events. For example, more sensors per kilometre of mains pipe mean that bursts can be pinpointed to a smaller section of the network, meaning that repair teams can be dispatched to a more precise location and with

105 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.596. To note that where WRc referred to "*how extra pressure would detect potential incidents in the network",* we assumed this referred to pressure sensors rather than pressure itself.

106 To be precise, with a lower density of sensors, issues would be detected less accurately, and it would take longer to pinpoint specific issues. Alternatively, if sensors were installed at the correct density in only some of South East Water's areas, this would lead to a "two-tier network", causing operational inefficiencies and be unfair for customers.

107 SEW, March 2025, Statement of Case, Annex G, paragraphs 390 and 391.

a higher certainty as to the repair equipment required, allowing them to find and fix the burst more quickly.

(d) These activities in turn lead to reduced supply interruptions, reduced leakage, and reduced water mains repairs. Low pressure is reduced, and water quality can be improved (as chlorine residual meters alert us to issues more quickly).

(e) In turn, this reduces customer contacts and complaints, as issues are prevented, and/or detected and repaired before they affect customers. This improves the customer experience.

3.118 In the table below we set out the quantified benefits from the Smart Network programme on various outcomes, for example a reduction of 6.1 minutes (per property) in supply interruptions. These benefits are expected in addition to longer-term efficiency gains in opex as a result of better prioritisation and targeting of resources. Note that this assessment includes the sensors that Ofwat has re-allocated to leakage.

Table 3.14: Quantified benefits of the proposed Smart Network programme

Measure	Benefit
Water Supply Interruptions	6.1 minutes[108]
Leakage	5% reduction in overall leakage levels
Water Mains Repairs	14% reduction in burst mains
Compliance Risk Index	30% reduction in CRI score
Appearance	20% reduction in customer contacts
Taste and Odour	20% reduction in T&O contacts
Customer Measure of Experience	1% improvement in C-MeX result per year for five years
Low pressure	10% reduction in properties receiving low pressure (not monetised in our benefit-cost ratio)

3.119 We have undertaken a high-level cost-benefit analysis that compares the benefits in the table above against the costs. This shows that the smart network is cost-beneficial with a cost-benefit ratio of 1.15. It is therefore clear that it is in the interests of customers to fully fund the smart network now.

How does our performance relative to other companies affect the case for smart network investment?

3.120 The CMA also refers to "*South East Water's performance relative to other companies*"[109] in supply interruptions in its reasoning for retaining Ofwat's allowance. It is not entirely clear how this has fed into the decision making. While we acknowledge that our performance on WSI is poor relative to other companies, on other related PCLs such as leakage, this is not the case. In any case, it is not clear how our relative performance supports the decision to retain Ofwat's assessment. Poor relative performance may strengthen the case for the smart network, as it is an efficient way to improve performance. At the same time, for those measures where we already

[108] We have stated in Table ANF11 of the South East Water Statement of Case, as well as our RFI07 response, Annex RFI7.5, that the benefit of increased operational resilience (Smart Water Networks) is 3 minutes (Year 2) – the 6.1 minutes refer to the long-term benefit.

[109] CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.597.

perform well, the smart network can be seen to demonstrate how innovation can drive further improvements.

3.121 Overall, we disagree with the CMA's provisional decision to disallow our smart network. We have demonstrated that our smart network would constitute a step change and have discussed in detail how the programme would lead to improved outcomes for customers. We therefore request that the CMA awards the full allowance for our smart network programme.

Leakage - new funding for investment in smart technology to support reporting

3.122 On **Leakage - new funding for investment in smart technology**, we welcome the CMA's confirmation that our choice of electromagnetic meters over ultrasonic meters is justified on the basis of its technical advisor's assessment.

3.123 However, the CMA has applied a 20% cost reduction as it questions the absence of "*detailed and externally verified costings"*,[110] and of a more detailed comparison of costs of electromagnetic and ultrasonic meters over an "*appropriate period*".[111] We disagree with this provisional decision and address each of these points in turn.

(a) In terms of externally verified costings for electromagnetic meters, the costing was generated as follows.

(i) For CAPEX, costs of £9.753m were derived from a combination of:

(A) Supply and installation of the flow sensors (which make up 0.7% of the costs): two quotes from Technology.[112]

(B) Magnetic flow meter at service reservoir with bypass (which make up 99.3% of the costs): unit cost database, with rates from the 2017 framework uplifted to 2022/23. The unit cost database assumes that 120 trunk meters are installed with a diameter of 500mm. Cost models were built using framework contractor rates. [113]

(ii) A similar approach was taken to derive OPEX estimates.

(b) We have also compared the costs of electromagnetic meters and ultrasonic meters over the asset life of electromagnetic meters. Our present value assessment includes capex and opex for both types of meters over a 33-year period (the asset life of electromagnetic meters). The analysis shows that the present value of costs is broadly similar.

(c) WRc agrees that the accuracy and reliability of electromagnetic meters is higher, stating that "*full-bore electromagnetic types* […] *tend to offer the best accuracy and are generally reliable over a long period with an expected life of 20+ years without requiring maintenance*".[114] While it is difficult to monetise this value, the relatively small cost difference shows that the net benefits of electromagnetic meters are likely to be much higher than those of ultrasonic meters.

(d) WRc, as part of our WRMP24 leakage modelling, evaluated some of our Smart Network costs, stating that "*WRc independently reviewed the overall costs and estimated yield, and compared the unit cost for sensors such as permanent acoustic loggers and hydrophones and compared with quotes we had obtained independently from the supply chain. We recognised that smart networks may evolve as a solution, but undertook independent cross checks and felt that the overall costs were reasonable*".[115]

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110 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.663.
111 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.663.
112 SEW, 11 May 2023, Smart Water Network Report - Rev 03, tabs 'Service Reservoir Outlet Meters' and 'Supplier Quotes.
113 See SR023b Flow Meter v3.10.xlsx, tab '2022'.
114 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.661.
115 WRC, November 2025, Memorandum – SEW PR24 leakage.

Leakage – Other Leakage Activity

3.124 The CMA has assessed the case for Other Leakage Activity and allowed £34.5m in funding. This is equivalent to a 20% challenge on the programme request and an increase of £15.7m relative to Ofwat's FD. This funding relates to the reduction from 81.0 to 70.5 megalitres per day (Ml/d) and is not impacted by the updated PCL baseline discussed in the next section.

Table 3.15: Total funding requested compared with the Ofwat FD and CMA PD allowance for other leakage activity

Ofwat FD funding	SoC requested funding	CMA PD funding
£18.8m	£43.1m	£34.5m

3.125 We requested £43.1m to deliver 8.14 Ml/d reduction in leakage through Other Leakage Activity over AMP8. Ofwat in its FD used a unit cost benchmark based on SES's forecast unit costs to calculate an allowance of £18.8m The CMA has provisionally found that Ofwat's unit cost benchmark is *"not a robust and reliable basis for setting South East's allowance for 'other leakage'".*[116] The CMA therefore evaluates our programme costs separately and has applied a 20% cost challenge to our total programme costs. In its PD, the CMA states that we have not provided *"sufficient and convincing evidence"*[117] to show our proposed costs are efficient. Specifically, it raises the absence of *"detailed cost breakdowns and external assurances"*[118] on the costs.

Our response

3.126 The CMA's assessment of Ofwat's unit cost benchmark focuses on both the suitability of the high-performing companies' forecast data and the choice of SES as the benchmark unit cost:

(a) The unit cost forecasts used by Ofwat for high-performing companies are considered unsuitable for determining a unit cost benchmark for efficient costs without further investigation. This is because of the high variability within the sample and the limited sample size.[119]

(b) The CMA also raises concerns around selecting SES as the unit cost benchmark, stating that selecting SES's unit costs as indicative of the efficient costs in such a small sample without further investigation around the cost difference is inappropriate. Further, the CMA states that Ofwat has failed to set out in its FD why it considers SES's unit costs to be indicative of a good performer.

3.127 As discussed in our SoC,[120] we agree with the concerns raised by the CMA, as SES's other leakage activity is not comparable to the programme we are proposing, and its costs are therefore not a robust benchmark for our costs. SES's other leakage programme over AMP8 includes activities such as Pressure Management and Calm Networks, activities which are markedly different in terms of cost from our programme of Find and Fix, as shown for pressure management in table ANG13 in our SoC.[121] We therefore support the decision to not simply use SES's costs to determine our allowance and evaluate our programme costs separately. However, we disagree with the 20% cost challenge applied to our programme costs. We can address the CMA's challenge in the following way:

(a) An explanation of how our costs were developed, including external assurance from WRc on those costs and our approach; and

116 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.642.
117 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.646.
118 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.646.
119 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.643 and 5.644.
120 SEW, March 2025, Statement of Case, paragraph 172 to 182.
121 SEW, March 2025, Statement of Case, paragraph 181 and Figure ANG13.

(b) A comparison of our historical costs based on Ofwat data.

3.128 We provide detailed information on each of these two areas below.

How were our costs developed? What external assurance can WRc provide on this?

3.129 As per our SoC,[122] our leakage strategy has been externally assured as it is informed by independent external expert consultants WRc (who have also been engaged by the CMA for the purpose of the PR24 Redeterminations). The main inputs to our cost estimates are based on modelled outputs provided by WRc. The modelled outputs, presented in our AMP8 demand management strategy, show Active Leakage Control (**ALC**) alongside an appropriately funded Smart Network as the most cost-effective way to achieving 8.14 Ml/d reduction over AMP8.

3.130 We summarise WRc's findings below and more detail is included in the note submitted with this Response.[123]

3.131 Our total cost estimates are based on:

(a) A cost of £55 per hour per person for ALC. This price includes all costs for a leakage technician including training, transport and all relevant equipment for ALC. WRc have said the "*unit cost of £55 per hour (in 2022/23 prices) for a leakage technician including all equipment and on-costs. This is efficient and reasonable*." The ALC cost of £55 per hour (in 2022/23 prices) was used in WRc's WRMP24 modelling to inform our Other Leakage Activity programme. WRc have said that overall our "*leakage management costs used at the time of producing the WRMP24 options appeared to be reasonable and do not appear to be industry outliers*".

(b) An industry standard time taken for both detecting and fixing leaks. We provided WRc with an average time taken for both detecting and fixing leaks of 16.2 hours based on our historical performance. WRc have used this in their modelling accounting for the expected improvement provided by investment in Smart Network technology. WRc overall found the average time taken for detecting and fixing leaks as "*reasonable for a high performing company*".

(c) Smart Network investment which is both efficient and reasonable. This investment is required to bring down the time taken to locate leaks. It is particularly important for us as our historical high performance on leakage means we are faced with fixing a high number of small leaks over AMP8, which is more time consuming to do without the data from smart sensors. At the time of the WRMP24 modelling, WRc evaluated the Smart Network costs we provided. WRc have said that they undertook independent cross checks on the overall costs and felt that they were reasonable, as stated in paragraph 3.121.

A comparison of our locate and mend costs to other companies' costs

3.132 The efficiency of our unit costs is also demonstrated by Ofwat's historical cost comparisons in their leakage enhancement model. In our SoC, we showed that we are relatively efficient in terms of total cost per repair when using the most recent outturn data in Ofwat's leakage enhancement model.[124] For the purposes of this Response, WRc has analysed the 'Locate' and 'Mend' cost per detected leak over the most recent data in Ofwat's leakage enhancement model. The charts below show that SEW are relatively efficient when compared to the rest of the industry.

122 SEW, March 2025, Statement of Case, paragraph 156.
123 WRC, November 2025, Memorandum – SEW PR24 leakage.
124 SEW, March 2025, Statement of Case, paragraph 160 and figure ANG10.

Figure 3.6: Locate cost per detected leak (Average, 2021/22 to 2023/24)[125]

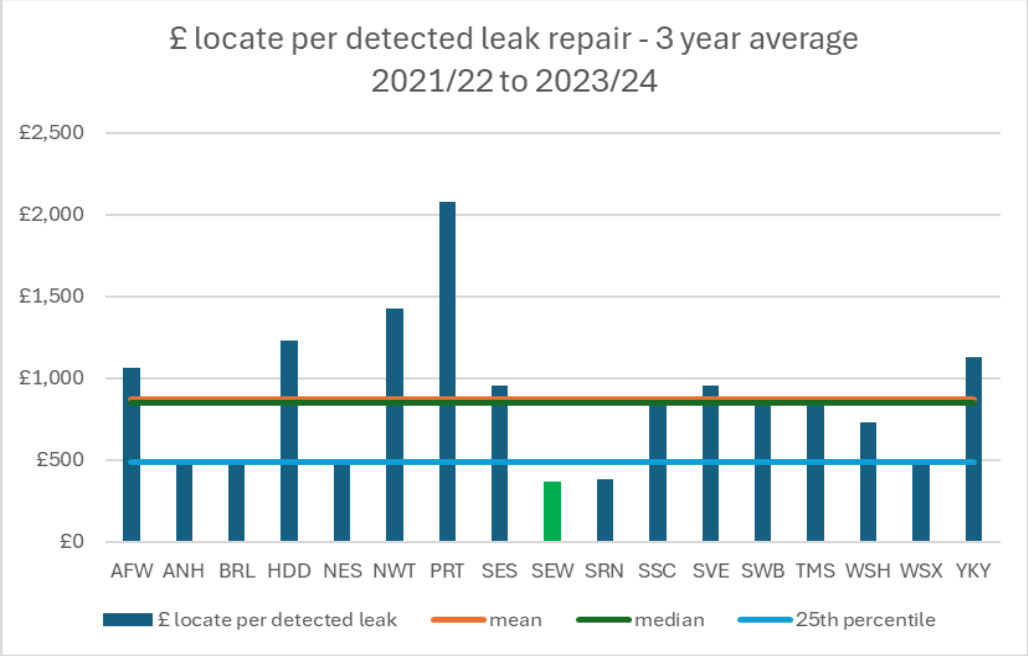
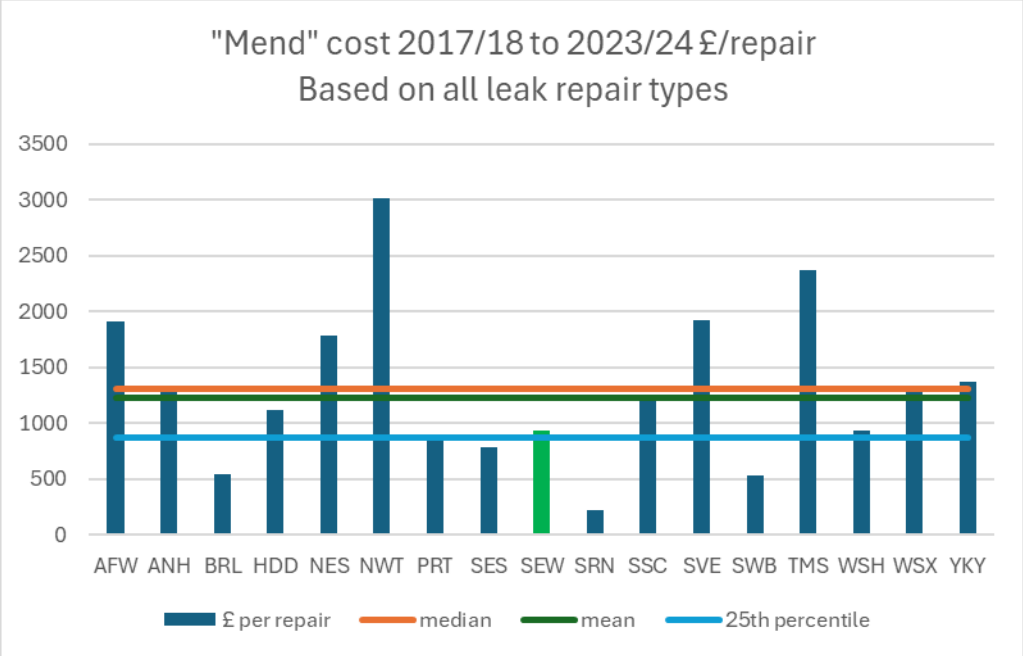


Figure 3.7: Mend cost per detected leak (Average, 2021/22 – 2023/24)



Conclusion

3.133 The efficient bottom-up costs highlighted above which were used in WRc's modelling result in a top-down unit cost of £5.29m per Ml/d reduction. We are a high-performing company in terms of leakage reduction, this means that we are operating at higher points of the leakage cost curves, modelled by WRc as part of the WRMP24, relative to the standard company.

125 When analysing the locate cost per detected leak WRc state they have only used three years to prevent reducing the sample size as a result of gaps in the earlier years of the dataset.

3.134 To achieve our desired reduction over AMP8, we need to fix a large number of small leaks. WRc have recognised this in their WRMP24 modelling, stating that "*The transitional cost to move from a current level of leakage to a lower position is also going to require fixing a high number of very small leaks, due to SEWs higher level of historical leakage performance*".[126] The underlying costs associated with detecting and fixing these leaks is comparable to those of fixing large leaks, however, the benefit in terms of Ml/d reduction is smaller. This results in a higher unit cost as the amount of water saved by each repair is lower.

3.135 The external assurance provided by WRc addresses the CMA's concerns and shows that our proposed costs for Other Leakage Activity are efficient. On this basis, we request that the CMA reconsider and remove the 20% cost challenge so that our Other Leakage Activity programme is fully funded.

Leakage – PCL baseline change

3.136 The CMA's PD accepts our updated PCL baseline and applies a unit rate of £1.406m per Ml/d, awarding a £19m allowance for reducing leakage from 94.5 Ml/d to 81.0 Ml/d. We support the CMA's decision and agree with both the baseline and unit cost used.

Table 3.16: Total funding requested compared with the Ofwat Final Determination and CMA Provisional Determinations allowance for Leakage – PCL baseline change

Ofwat FD funding	SEW requested funding[127]	CMA PD funding
-	19.3m	£19m

3.137 We recognise that the CMA, Ofwat and SEW are aligned on the use of 94.5 Ml/d as an updated PCL baseline for leakage on the basis of the following RFI responses:

(a) Ofwat in its response to RFI04 recommended the CMA considers amending our leakage allowance to align the leakage PCL baseline with the 2024/25 expected leakage outturn, taking into account that we had a PR19 clawback mechanism.[128] This is to ensure that Disputing Companies are treated consistently as Ofwat in response to Anglian's SoC recommended that if the CMA were to intervene then it should use the actual 2024/25 outturn position to update the baseline and profile for leakage.[129]

(b) In our response to RFI04 to SEW, we provided both the most recent outturn level of 104.8 Ml/d and a proposed updated baseline of 94.5 Ml/d. [130] We suggested the use of 94.5 Ml/d as this is the point where the PR19 leakage clawback mechanism activated to recover enhancement expenditure. Therefore, the reduction from our forecast outturn of 104.8 Ml/d to 94.5 Ml/d should be covered through base allowances as required at PR19.

(c) Ofwat, in response to RFI12 question 4(a), agrees that SEW's updated allowance should be calculated using a baseline of 94.5 Ml/d and use a unit cost of £1.406m Ml/d.[131] We acknowledge that this is the correct unit cost for calculating the reduction from 94.5 to 81.0 Ml/d, as is used by the CMA in its provisional allowance.

126 WRC, November 2025, Memorandum – SEW PR24 leakage.
127 The request for an update to the Leakage PCL baseline was submitted following our Statement of Case as explained in paragraphs 3.137(a) to (c).
128 Ofwat, May 2025, Response to CMA RFI04, Question 5e.
129 Ofwat, April 2025, PR24 Redeterminations – Expenditure allowance – common issues, paragraph 4.58.
130 SEW, July 2025, Response to CMA RFI04, Question 1.
131 Ofwat, July 2025, Response to CMA RFI12, Question 4a.

Water efficiency initiatives

3.138 The CMA has assessed the case for water efficiency initiatives and allowed £30.1m in funding. This is equivalent to a 20% challenge on the programme request and an increase of £8m relative to Ofwat's FD.

Table 3.17: Total funding requested compared with the Ofwat FD and CMA PD allowance for water efficiency

Ofwat FD funding	SoC requested funding	CMA PD funding
£24.1m	£40.2m	£32.1m

Summary of the CMA's approach

3.139 The CMA has agreed with WRc's support for our water efficiency initiatives.

(a) We shared detailed cost breakdowns of our proposed water efficiency initiatives, and WRc viewed these as industry leading. WRc said that *"the comparative review shows that South East was effectively out in front of the industry in the scope and intensity of demand-side measures, and that it was tackling customer-side leakage and water waste head-on"*.[132]

(b) We shared unit cost benchmarking that shows our two main initiatives are efficient compared to Ofwat's own benchmarks.[133] WRc agreed that *"South East's costs are indeed efficient in light of its high performance."*[134]

(c) WRc agreed that alternative supply-side interventions would be more expensive, and that we could not deliver target water savings of 12Ml/d with lower allowances. *"WRc stated that alternative options … would cost far more per Ml/day, and that if South East spent only the allowed £24 million, it could deliver cheaper [savings] … but not the full 12Ml/d target."*[135]

3.140 Despite this, the CMA has proposed a 20% reduction to our requested allowances, because:

(a) *"South East's water efficiency programme does not involve investments into physical capacity or capability of the network but rather the hiring of people to identify and address opportunities to reduce water demand*";[136] and

(b) SEW's programme will be delayed as there will only be four years left of the AMP8 cycle rather than five, and so only four years of opex are required.

Our response

3.141 The CMA agrees with our choice and unit cost of water efficiency initiatives. However, by not allowing the full request, the CMA effectively disagrees with the volume of our initiatives.

3.142 The volume of water demand reduction we must deliver is based on our Water Resources Management Plan (**WRMP**). WRMPs are used to plan water resources for public water supplies in England and Wales. This is a well-established process where each water company prepares a 25-year plan every 5 years and this is signed off by the Secretary of State. These plans set out how companies intend to achieve security of supply and protect the environment. Companies are

132 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5.
133 Ofwat estimates least-cost unit costs for household audits as £3.11m/Ml/day and for leaky loos as £8.06m/Ml/day. Given the volume of activity that we intend to carry out, Ofwat's own benchmarks would suggest an efficient cost of £42.68m for these programmes whereas we are requesting allowances of £28.62m for these programmes.
134 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5.
135 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.669.
136 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.671.

required to plan to a '1 in 500 years' level of resilience to exceptional demand restrictions associated with emergency drought orders.

3.143 As part of these plans, water companies must forecast demand and supply over at least 25 years and appraise a range of interventions to reduce any deficit. Demand-side interventions consist of either reducing leakage or reducing consumption, and supply-side interventions relate to new water sources and storages. Within Ofwat's own definitions, water efficiency – also known as demand – *"typically covers customer-side options to reduce water consumption and wastage within household and non-household properties. This excludes costs and benefits identified for leakage and metering activities."*[137]

3.144 By definition therefore, demand-side water efficiency measures cannot include "*investments into physical capacity or capability of the network*" as the CMA suggests.[138] In fact, within the bounds of water efficiency initiatives, we are doing more physical installation than any other water company by actively fixing leaks and fitting water-saving devices, rather than *"focusing on easier wins like metering and education"* (as stated WRc).[139]

3.145 Our WRMP, approved by the Secretary of State, has identified the level of demand reduction required in PR24 to prevent a deficit (where we have insufficient water to maintain supply to customers in severe drought conditions) given the supply we expect to have available. We therefore need to undertake these water efficiency activities – regardless of the length of time remaining in the price control – to ensure we have enough water to supply our customers. Moreover, the reductions outlined in the WRMP are required to meet Government policy targets and the basis upon which our per capita consumption (**PCC**) performance commitment level (**PCL**) was set by Ofwat.[140] These targets come with associated penalties (£280,000/l/p/d) and have not been adjusted to reflect the reduced length of PR24.

3.146 We estimated the initiatives required to meet our WRMP and corresponding PCL – for example, carrying out 125,000 household audits – and the corresponding cost of £40.2m. We have previously assumed that these initiatives would be carried out evenly across the five years of PR24 – i.e. 25,000 household audits per year – meaning an annual cost of £8.0m. If we only have four years remaining in AMP8 to carry out our initiatives, then we will need to undertake a higher level of activity each year – i.e. 31,250 household audits per year – at a higher cost of £10.1m.

3.147 However, the CMA has assumed that the same annual workload (£8.0m) would be required across the remaining four years of AMP8, meaning that we only require £32.1m in PR24. This logic is flawed. WRc states that we would not be able to deliver the full 12Ml/d target with lower allowances.[141] By only providing us with 80% of our requested allowances, the CMA is limiting us to undertaking 80% of our water efficiency activities and achieving a maximum of 80% of our water savings. At a minimum, this would incur a £2m penalty on our PCC target but, more importantly, it would reduce our ability to maintain supply to our customers.

Lead

3.148 The CMA has assessed the case for lead and awarded funding of £6.9m. This is equivalent to a 71% challenge on the programme request and retains Ofwat's FD allowance.

Table 3.18: Total funding requested compared with the Ofwat FD and CMA PD allowance for lead

Ofwat FD funding	SoC requested funding	CMA PD funding
£6.9m	£24.3m	£6.9m

137 Ofwat, July 2024, PR24 Draft Determinations Expenditure Allowances.
138 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.671.
139 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.669.
140 Ofwat, February 2023, SEW – draft water resources management plan 2024 consultation response.
141 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5.

3.149 In our SoC, we included a requested full funding of our legal undertaking with the DWI.[142] The CMA has retained Ofwat's cost allowances for lead but also stated that it encourages "*South East, Ofwat and the DWI to engage promptly to develop an agreed alternative lead reduction strategy for South East to adopt in AMP8."* and will *"consider how best to reflect any agreed alternative approach in our final determination and we may adjust allowances down or up to reflect this."*[143]

3.150 In its approach, the CMA has consulted with the DWI regarding our undertaking and notes the DWI's position as:

(a) The DWI accepted our undertaking as it felt it was beneficial to achieving our target to be lead free by 2050.

(b) Our programme is *"under-ambitious"* as there is not enough lead pipe replacement scheduled for AMP8. The DWI *"did not necessarily agree that surveying all properties was necessary nor the best use of resources"*.[144]

(c) The DWI would only consider changing an existing undertaking if we are able to provide an acceptable plan which explains the revised lead strategy we wish to adopt.

3.151 We agree with the DWI's view that conducting these surveys will help us become lead free by 2050 through facilitation of effective targeted lead replacement. However, we disagree that our programme is under-ambitious. Based on our conversations with the DWI, we understand they consider all companies' proposed lead programmes over AMP8 as unambitious except for one. The proposed surveys are industry leading, and the DWI has previously acknowledged that *"No company holds a complete dataset of pipe material"* and that these surveys would *"provide a wealth of information which can be used for future targeted work on replacements".*[145] We agree with the DWI that these surveys would produce a complete dataset of pipe material that would facilitate effective lead replacement in future AMPs. This would provide our customers with cost effective and targeted lead replacement.

3.152 Based on both Ofwat and the DWI's views, the CMA concludes that we are now required to deliver a scheme that is not fully supported by Ofwat or the DWI. The CMA first encourages Ofwat and the DWI to work together to resolve this situation in the best interests of SEW's customers. Further, the CMA encourages SEW, Ofwat and the DWI to engage promptly to develop an agreed alternative lead reduction strategy for SEW to adopt in AMP8. In its Final Report, the CMA will then consider how to best adjust allowances to reflect a new approach.

3.153 The CMA's provisional approach, combined with our remaining legal obligation, places us in an uncertain position regarding our lead programme. We agree with the view expressed by the CMA that this is a clear example of the concerns highlighted by the IWC.[146] The misalignment between Ofwat and the DWI has led to inefficiencies which threaten to negatively affect customers. We have invested considerable time and resources designing the AMP8 lead strategy to develop our undertaking that was accepted by the DWI. Re-scoping our programme now would create a situation where our customers are at risk of paying twice.

3.154 We welcome the opportunity to engage with Ofwat and the DWI to find a solution. Following publication of the PD, we contacted the DWI and Ofwat promptly to facilitate early engagement. The DWI has indicated that it is willing to engage in discussions regarding a change to the undertaking but has not provided any indication on what it would accept at this stage, stating it would only consider an ambitious alternative. Based on these discussions, we understand the DWI is writing a response to the CMA on our lead strategy and we request the opportunity to

142 DWI, April 2024, South East Water Limited – AMP8 Lead Strategy SEW-2023-00016. The undertaking requires us to: *d) Conduct a survey of all company and service pipes to determine the composition of lead in AMP8.*
143 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.688.
144 CMA October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.683.
145 DWI, 2022, Drinking Water 2022: Public supplies in England, page 18.
146 Independent Water Commission, July 2025, Final Report, paragraph 330.

provide input following this and prior to the CMA's Final Report. We have consulted with external expert advisors to support the development of an alternative lead strategy as a matter of urgency.

3.155 Following our request to meet the DWI to discuss the undertaking, we understand the DWI met with Ofwat on 5 November 2025, and a further tripartite meeting that we organised between the DWI, Ofwat and South East Water took place on 7 November 2025.[147] We plan to continue to engage with both regulators to agree a revised strategy, undertaking and allowance for inclusion in the CMA's Final Report. This is reliant on both regulators' continued engagement and timely input. We ask that the CMA keeps this issue open following the deadline for response to its PD and provides a date by which a revised undertaking needs to be agreed in order to be included in the Final Report. If we can agree an alternative strategy with the DWI, we agree in principle that the CMA should reflect this alternative strategy in an updated allowance in its Final Report.

3.156 If an acceptable revised undertaking cannot be agreed with the DWI prior to the CMA's Final Report, we request that the CMA includes our lead programme in an 'in-period adjustment'. Funding under this adjustment would be determined by Ofwat during the PR24 price control period. Such a mechanism would protect our customers from any risk of under-delivery and the company from being subject to an unfunded obligation. We request the following framework be applied to the in-period adjustment:

(a) Remove the obligations we currently have that are unfunded;

(b) Set a reasonable deadline for an alternative lead strategy to be agreed with the DWI and Ofwat;

(c) Outline a cost assessment mechanism and timeline (which Ofwat would carry out) once work scope is proposed.

WINEP investigations

3.157 The CMA has assessed the case for WINEP investigations and retained Ofwat's FD allowance of £47.2m in funding. This is equivalent to a 20% challenge on the programme request.

Table 3.19: Total funding requested compared with the Ofwat FD and CMA PD allowance for WINEP investigations

Ofwat FD funding	SoC requested funding	CMA PD funding
£47.2m	£58.9m	£47.2m

Summary of the CMA's approach

3.158 The CMA's approach has mainly focused on the latest evidence that was provided as part of RFI02 and has not considered Ofwat's modelling approach. Overall, the CMA states that we have not presented *"sufficient and convincing evidence that [our] costs for WINEP investigations are efficient",*[148] noting:

(a) The EA considers we are comparable to other water companies in the scale of our investigations;

(b) We have not provided detailed cost breakdowns either to the CMA or to Ofwat; and

(c) We have not provided an explanation for why we have not needed to develop groundwater models before.

147 DWI, November 2025, Letter to the CMA: Water PR24 Price Redeterminations – Update from the Drinking Water Inspectorate.

148 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5.

3.159 The CMA therefore chose to retain Ofwat's FD allowance.

Our response

3.160 We address the following issues:

(a) Detailed cost breakdown and issues with Ofwat's benchmarking;

(b) Response to EA's assessment of our investigation programme.

Detailed cost breakdown and issues with Ofwat's benchmarking

3.161 As outlined in our response to RFI02, the apparent cost gap between us and other companies is driven by a lack of comparability. In its FD, Ofwat itself states that it is "*not feasible to benchmark the associated costs accurately against other investigations or provide an indicative benchmarked allowance*".[149] This is not only because we have efficiently aggregated our schemes where other companies have not, but also because we have included important monitoring and evaluation components into our investigations (which other companies have not). While the EA may feel that the scale of our investigations is comparable to other companies, it is the structure and components within them that mean it is not possible to use top-down benchmarks to assess the efficiency of our investigations. The CMA has not commented on the benchmarking but instead questioned the difference in costs between us and other companies. As this is based on a flawed comparison of units (as discussed in our SoC and RFI02), we ask the CMA to re-consider its starting point – to one that is based on a bottom-up assessment of these costs.

3.162 We agree with Ofwat that it is not feasible to benchmark our costs with simplistic top-down benchmarking. We therefore contend that the CMA should review bottom-up costs as a more suitable approach to assessing the efficiency of our investigations. The CMA's PD states that we have not provided detailed cost breakdowns of our programmes, but this is not correct. In October 2024, we provided Ofwat with detailed cost breakdowns of each of our 36 investigations for query OFW-REP-SEW-060 as part of the price control process. We have previously referred to this information in our SoC,[150] but the CMA has not to date sought to obtain and review the underlying evidence. We are therefore providing it now in this Response.

3.163 These breakdowns demonstrate annual spend at a granular level for each of our activities (e.g. rainfall gauging) across each year of PR24. These costs have been developed by third-party experts – AtkinsRéalis – with minimal updates since (for example, updates relating to adjusting base years and reprofiling spend to reduce 'peakiness'). Having been developed by external consultants, we believe that these breakdowns represent sufficient evidence of our efficient activities and costs.

3.164 Given Ofwat's acceptance of the challenges with top-down benchmarking for our investigations and the bottom-up costs that we have provided, we do not consider an arbitrary 20% cost challenge to be appropriate. Ofwat has provided no evidence supporting the level of challenge, which is an outlier when considering the challenge placed on other deep dived companies for water investigations (10%) and on wastewater investigations (0%). While we accept that our costs have increased from PR19 levels, this is irrelevant in light of the changing requirements of the EA and Ofwat's introduction of strict PCDs for WINEP investigations. Both of these mean that new investigations activities are required for PR24, including the development of complex groundwater models that have not previously been needed for our WINEP investigations.

149 Ofwat, December 2024, PR24 Final Determinations: CA40 Water Investigations – enhancement expenditure model, SEW tab.

150 SEW, March 2025, Statement of Case, paragraph 375.

Response to the EA's assessment of our programme

3.165 In our SoC and RFI02, we outlined the complexity of our WINEP investigations including the need to build groundwater models that already exist for other water companies. In its response to EARFI01, the Environment Agency (**EA**) stated that our WINEP investigation programme:

(a) Is comparable to other water companies;

(b) Does not require groundwater modelling that is particularly complex; and

(c) Can be undertaken with existing models that are not less well developed than for other water companies; and

(d) Does not require us to build new models.

3.166 In preparing our response to the EA's RFI01, we have consulted with expert third-party consultants AtkinsRéalis, Groundwater Science and WSP**.**

3.167 We do not agree with the response from the EA's Deputy Director of Water Quality and Investment, and it does not reflect the discussions we have had with the EA, Local Operations, South East and East region (**Local EA**). The response to RFI01 highlights a disconnect between the national EA and Local EA. This is a further example of regulatory misalignment consistent with the concerns raised by the IWC in its recent review of the water sector. The Local EA has been engaged throughout the preparation of our WINEP Investigations programme and approved the proposed project scope of our investigations. Our approach for the specific actions which require groundwater model updates has been discussed with the EA over a period of several years. Our intention to update the EA's models in order to meet our needs is therefore well known to the EA and has not been challenged until this point.

3.168 It is standard practice throughout England that companies carry out additional refinements to groundwater models informed by better local data collected under WINEP drivers. This is both encouraged and scrutinised by the local EA team model owners. Refinements are then returned to the EA at the end of each investigations round to feed into the next update of models. This process is essential to be able to test potential solutions more confidently and ensure that bill-payers money is not wasted on measures which will not deliver the anticipated solution.

3.169 We do not agree with the national EA's assessment that our WINEP investigation programme is of a similar nature to other companies' and can easily be undertaken with existing models because:

(a) As highlighted in our SoC, we are highly dependent on groundwater abstraction. Of our total water resources, 86% is sourced from groundwater abstraction. This is the second highest proportion in the industry and 45% above the average based on 2024/25 Annual Performance Review (**APR**) data. This means that a large number of our investigations are aimed at maintaining the sustainability of groundwater abstraction, the results of which can lead to closure of sustainable sources putting pressure on our supply-demand balance. We are relatively more reliant on groundwater models in this case and the models, where they exist, require complex refinement to suit our purposes. Given our limited headroom, the results of our investigations must be both accurate and robust to prevent incorrect closure of sustainable sources. This shows the focus of our investigations and in particular, the complexity of our groundwater modelling is not comparable to the average company.

(b) Where EA groundwater models exist, we will make use of these in our investigations. We are not proposing to build a new groundwater model where one already exists. We agree with the EA in that it would be unhelpful to develop competing water company models and this is not our intention. The majority of our requested investment relates to development of existing models. Table 3.20 below shows a breakdown of the groundwater modelling activities and associated costs for each relevant WINEP Investigation action. Our investigations cannot be undertaken using the EA's existing models without development

either because i) there is a gap in the data required and/or ii) they are not fit for the purpose of our investigation.

(i) Investigations can be complex and depend on the availability of data on protected sites and baseline modelling. Our experience is that in the majority of investigations baseline environmental data is not available and this has to be generated to understand the health of the environment, potential factors driving environmental degradation and to support an understanding of the reasons for water quality deterioration or potential impact of water abstraction. Further, geological data is often not available for parts of our service area. For example, we have commissioned the British Geology Society (**BGS**) to revisit all geological mapping and remap the chalk stratigraphic units in a 3D model for the Seaford and Eastbourne area. This will allow us to determine the number of layers which we need to build into the proposed groundwater model, the geology of the area and what impact this could have on hydrogeology.

(ii) EA models consider flow only and, taken “as is”, are not fit for our purposes. For our purposes, we must also understand ecological conditions, potential contamination and the impact of climate change, etc. ('conceptualisation of the catchment'). This is so that we can understand the likely outcomes from the schemes informed by the investigations output before investing heavily in restructuring our water network. The EA does not have this information, and this is why the Local EA supported inclusion of groundwater modelling in our WINEP. It is important to highlight that we use the most up-to-date modelling software that is appropriate to the local area to deal with the 'environmental risk in the catchment' whether this be contamination, chemical, ecology or WFD. A governance group and peer review is part of the process, both Groundwater Science and WSP are utilised for this work (the same consultants used for EA modelling), thus ensuring that work is embedded to update regional water resource planning.

(iii) Alongside groundwater modelling, our studies also include hydro-ecological modelling, WINEP action 08SE100037 for example, and water quality modelling to understand the ecosystem and biodiversity consequences. This holistic approach is essential to ensure the investment delivers tangible benefits as clearly set out in the UKWIR Environmental Destination Framework.

(c) Where we have proposed to develop new groundwater models, these are required as EA modelling is not available for a sizeable proportion of our water supply area. This is why during AMP7 we have developed the North Kent model in conjunction with Southern Water. A key example for our AMP8 programme is WINEP action ‘08SE100070’. As part of this investigation, we plan to develop a groundwater model for the Seaford and Eastbourne chalk block as one currently does not exist. This is a very important scheme as the [redacted]. Given the large chalk block, understanding the geology of this area is key as chalk is highly porous and stores vast amounts of water within its fissures. Any changes to land use through developments can disturb this and impact our [redacted] greatly, putting our water supply at risk. The need is further exacerbated by our limited headroom which makes the decision to turn off abstractions highly consequential. We have requested £0.4m relating to model development costs, a detailed breakdown of these costs can be seen in the cost sheets submitted in response to query OFW-REP-SEW-060.[151]

(d) In summary, while some modelling may be available, this is not always fit for purpose for the WINEP investigations and therefore we need to undertake additional work to assess the emerging environmental risks in line with the EA’s WINEP requirements. We take a holistic approach to these investigations considering broader impacts. Often the outputs

[151] We note that the outputs from groundwater modelling often feed into other investigations. In the submitted cost sheets, we have flagged where this occurs. These costs are included across investigations but are only included once in the final Totex estimate, such that no double counting has taken place.

of these models feed into local development planning, ecology reports and Raw Water quality monitoring.

Table 3.20: Breakdown of Groundwater Modelling cost by WINEP Action

WINEP Action	Cost (£m)	New/Existing Model?	Description of model development or refinement
08SE100042	2.379	New - Friston	• Gap analysis and gap filling (e.g. measuring spring discharge to understand groundwater body water balance). • Conceptualisation (including data collection, geological mapping, geophys, CCTV) and reporting of. • Conductivity logging • Grid and regional groundwater model build • Surface water accounting modelling (SWAC) or 4R (recharge) modelling • Identification of groundwater dependant terrestrial ecosystems (GWDTEs), monitoring of GWDTEs and build of hydro-ecology model • Model build report • Model output runs for Options Appraisal
08SE100068	0.453	EA's East Kent GW model	• Gap analysis • Update to conceptual model and some data collection around our abstractions • Identification of GWDTEs, monitoring of GWDTEs and build of hydro-ecology model • Model build report • Model output runs for Options Appraisal
08SE100070	0.527	New – Seaford and Eastbourne	• Gap analysis and gap filling (e.g. measuring spring discharge to understand groundwater body water balance) • Conceptualisation (including data collection, geological mapping, geophys, CCTV) and reporting of. • Grid and regional groundwater model build • Surface water accounting modelling (SWAC) or 4R (recharge) modelling • Identification of GWDTEs, monitoring of GWDTEs and build of hydro-ecology model • Model build report • Model output runs for Options Appraisal

WINEP Action	Cost (£m)	New/Existing Model?	Description of model development or refinement
08SE100071	0.738	EA's Wey and Mole GW model	• Gap analysis • Update to conceptual model and some data collection around our abstractions • Identification of GWDTEs, monitoring of GWDTEs and build of hydro-ecology model • Model build report • Model output runs for Options Appraisal
08SE100038	0.179	EA's Kent Lower Greensand GW model (Hothfield)	• Gap analysis • Update to conceptual model and some data collection around our abstractions and the Hothfield SSSI • Monitoring of groundwater GWTDES and build of hydro-ecology model • Model output runs for Options Appraisal

Service Reservoirs

3.170 The CMA has assessed our case for service reservoir upgrades and awarded funding of £30.6m. This is equivalent to a 10% challenge on the programme request and is consistent with Ofwat's revised allowance proposal. In its FD, Ofwat applied a 27% cost challenge but recommended this be revised to 10% after being provided with further evidence.[152]

Table 3.21: Total funding requested compared with the Ofwat FD and CMA PD allowance for service reservoirs

Ofwat FD funding	SoC requested funding	CMA PD funding
£25m	£34m	£30.6m

3.171 We requested £34m for capacity upgrades at service reservoirs in Sussex and Kent over AMP8. In its FD, Ofwat applied a 27% cost challenge and allowed £25m. In our SoC,[153] we highlighted that Ofwat had ignored independent quantitative cost benchmarking evidence from ChandlerKBS which justifies our programme costs. Ofwat, in its response to our SoC, stated "*this additional evidence increases Ofwat's confidence in the company's costs compared to the supporting evidence available at the time of FD24. In particular, had this information been available at the time of FD24, Ofwat would likely have applied a 10% cost efficiency challenge.*"[154] Ofwat base the 10% cost efficiency challenge on the assertion that increasing capacity at existing sites is less costly than building a new service reservoir. In response to RFI05,[155] Ofwat stated the revised enhancement allowance should be set at £30.6m.

3.172 The CMA has provisionally retained Ofwat's revised allowance proposal of £30.6m, stating that *"sufficient and convincing evidence"* on our costs has not been provided. In particular, the CMA states that *"the evidence provided in ChandlerKBS' report is qualitative"* and we have not

152 Ofwat, April 2025, PR24 Redeterminations: Response to South East Water's Statement of Case, paragraph 4.89.
153 SEW, March 2025, Statement of Case, paragraph 248.
154 Ofwat, April 2025, PR24 Redeterminations: Response to South East Water's Statement of Case, paragraph 4.89.
155 Ofwat, May 2025, Response to RFI05, Question 3b.

provided an "*externally assured assessment that the design and cost of the planned works are efficient*".[156]

3.173 In our response to RFI02, we submitted additional qualitative evidence from ChandlerKBS which addresses Ofwat's assertion in its Response to our SoC that expanding current reservoirs is less costly than building new ones. Within this submission, ChandlerKBS analysed the areas of cost saving proposed by Ofwat in its Response to our SoC and did not find *"sufficient evidence for any cost savings of adding storage capacity over constructing a new Service Reservoir."*

3.174 In its evaluation, the CMA asked its independent engineering advisors WRc to advise on whether it is likely to be less costly to expand existing service reservoirs rather than build new ones. WRc stated that it is *"largely supportive of South East's position that expanding existing sites was as costly, if not more so, than building new service reservoirs".*[157] The PD accepts this evidence and agrees with our position that expanding existing sites is not cheaper than building new reservoirs. We support both WRc's findings and the CMA's provisional decision to accept this evidence. However, we disagree with the 10% cost challenge provisionally applied to our programme costs as we can address the CMA's challenges on externally assured assessment of our costs, having already submitted quantitative benchmarking by ChandlerKBS alongside our SoC. Data used by ChandlerKBS for the service reservoir cost comparisons included 22 projects to construct service reservoirs from 7 water companies.[158] The report considered project level benchmarks and found that:

(a) *"The SEW service reservoir costs are consistently low which could be interpreted as an indicator that similar project estimates in the capital programme would also have similar variances of -36% to -46% compared with benchmark costs."*

(b) *"There were 19 SEW cost curves benchmarked in total. There were no SEW cost curves that presented a significantly high cost in our comparison with benchmark data"*.

3.175 As this benchmarking became available to us ahead of the Business Plan submission but with insufficient time to amend our cost estimates, we used the evidence to update our costs in the DDR. The ChandlerKBS report found an overall variance of -42% comparing our business plan costs with their benchmark costs.[159] Based on this, we increased our programme request by 36%, applying a 6% efficiency challenge to ChandlerKBS' benchmarked costs. We retained this request in our SoC. This means that our requested costs are 6% more efficient than the external, quantitative benchmarking provided by ChandlerKBS.

3.176 We encourage the CMA to engage with the findings of this detailed, independent bottom-up evidence which we detailed in our SoC. We also highlight that Ofwat has accepted the quantitative evidence but questioned the difference in costs between new and existing sites. As WRc and ChandlerKBS have both advised that existing sites are not expected to be less costly than new sites, this addresses Ofwat's final concern around our cost estimate. On this basis, we request the 10% cost challenge is removed and the service reservoir programme is fully funded.

Raw Water Deterioration

3.177 There are two items of our PFAS enhancement expenditure that we included in our SoC as summarised below:

(a) A further five catchment investigations (£4.2m), which were in addition to what had been allowed in the PR24 Final Determination.

(b) PFAS schemes at Beenhams Heath WTW (£3.4m) and Forstal WTW (£4.8m).

156 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.571.
157 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.570.
158 The 22 Service Reservoir data points are for newly constructed water storage assets and contains a mixture of construction on both new and existing sites. The data does not distinguish between new and existing sites.
159 ChandlerKBS, 15 August 2024, PR24 Benchmarking report – South East Water, page 10.

3.178 On (a), we welcome the CMA's decision to fund our requested allowance for these additional investigations in full. This is consistent with Ofwat's view, where it has stated that "*if the company had submitted investigation costs in its business plan or in its representations we would have funded them in full*."[160]

3.179 On (b), the CMA has chosen to deprioritise this request. At the time of our reply to the CMA's Approach and Prioritisation document,[161] we accepted that these costs of circa. £8.2m could be deprioritised by the CMA on the understanding that they would be eligible for the "PFAS reopener". Since then, Ofwat has published further details on how it proposes to run the cost change process (which includes the PFAS reopener) and introduced a triviality threshold for PFAS costs of 0.5% of totex. Ofwat, in its reply to RFI16, estimated that this threshold for SEW would be around £9m, and that "*based on the information we have, it is possible that Beenhams Heath WTW and Forstal WTW schemes together may not meet the triviality threshold*".

3.180 The decision in the CMA PD, combined with Ofwat's approach on the cost change process, means that our PFAS costs of circa. £8.2m are unfunded. There is also now a new perverse incentive to artificially inflate cost forecasts to increase the chance that schemes pass the triviality threshold in order to be considered for funding through Ofwat's cost change process.

3.181 As these schemes are required to comply with DWI guidance, our costs should not be unfunded.[162] It is also not clear why the CMA cannot deal with this issue, as it can be resolved simply – either through ex-ante funding of the schemes or by directing Ofwat to amend the triviality threshold for the PFAS element of the cost change process. We ask the CMA to reconsider its position in this regard.

Deprioritised areas

3.182 In respect of the following areas, we are providing a short response to aid with the prioritisation of key issues, consistent with the overriding objective. However, this should not be taken to mean that we support the CMA's provisional position and we would welcome the opportunity to engage further with the CMA on these areas.

Net Zero

Table 3.22: Total funding requested for net zero schemes

Ofwat FD funding	SoC requested funding	CMA PD funding
-	£12.6m	-

3.183 The CMA has provisionally retained Ofwat's decision not to provide any funding for our net zero programme on the basis we have not demonstrated that the schemes would support sector innovation and learning. We disagree with this position and reiterate that the purpose of our proposed enhancement schemes is to reduce emissions and they cannot be funded through base cost allowances for the reasons outlined in our SoC. Further, we believe that our proposed schemes satisfy the criteria outlined in Ofwat's three phase deep dive applied by the CMA.

River Medway Scheme

3.184 The CMA has assessed the case for River Medway Scheme in line with Southern Water's corresponding case and moved the scheme to the large scheme gated process. We welcome this change and the opportunity to be involved in further discussions with Southern Water and Ofwat on the need for investment and efficient costs.

160 Ofwat, July 2025, Response to CMA RFI16, Question 2.
161 CMA, May 2025, Water PR24 redetermination references – approach and prioritisation
162 Specifically, the DWI issued a consolidated guidance document in August 2024 (days before the DDR was due), see para 143-145 of our SoC, Annex G.

3.185 We request that the CMA clarify and direct that the cost risk we bear in the allowances set by the gated allowance must be commensurate with the influence we have over the costs as part of the gated allowance process. This should also cover any contribution SEW may be required to make towards Southern Water's project development costs incurred in the early stages, before the scheme progresses through the formal approval gates, or any reallocation of Southern Water's capital expenditure to base expenditure.

Cyber, SEMD, Drinking Water Protected Areas

3.186 The CMA has deprioritised four of our enhancement claims, allowing no additional funding. These are Drinking Water Protected Areas, Cyber, SEMD, and a portion of our Raw Water Deterioration claim (which is discussed separately in the dedicated section). We disagree with the CMA's position and reiterate that these enhancement lines should be considered and allowed in full, in line with the points made in our SoC. This is because they are important areas of security and water quality that matter to our customers and the lack of funding increases the risk of delays in delivery and customer impacts.

Table 3.23: Total funding requested for Cyber, SEMD, Drinking Water Protected Areas

Ofwat FD funding	SoC requested funding	CMA PD funding
£55.8m	£60.3m	£55.8m

Contingent Allowance

3.187 The CMA has assessed the contingent allowance and provisionally decided not to amend the arrangements in Ofwat's FD.

Table 3.24: Total funding requested compared with the Ofwat FD and CMA PD contingent allowance funding

Ofwat FD funding	SoC requested funding	CMA PD funding
£50m	£166.4m (Resilience programme)	£50m

Summary of the CMA's approach

3.188 In its FD, Ofwat included a £50 million contingent allowance to enable us to manage new resilience risks that may require additional enhancement expenditure in AMP8. Ofwat specifically states that:

(a) *"Investment under the resilience contingent allowance is to manage increasing risks from hazards that are beyond their control and not covered by other enhancement areas or base allowance areas"*; [163] and

(b) the funding can only be used *for "new and increasing risks identified after November 2026, ensuring alignment with Ofwat's Final Determination objective."*[164]

3.189 The CMA has provisionally decided not to amend Ofwat's FD approach to the contingent allowance, retaining the level of funding and the conditions for accessing it.

[163] Ofwat, February 2025, PR24 Final Determinations: Expenditure allowances, page 226.
[164] Ofwat, February 2025, PR24 Final Determination Inbound Query, OFW-FD-SEW-002 Ofwat Response.

3.190 The CMA considers the requirements for accessing the contingent allowance, as set out by Ofwat,[165] reasonable and in the interests of customers.[166] The CMA's assessment of the contingent allowance is outlined below:

(a) *"We also consider that the potential for South East to access additional funding that has already been factored into customer bills is an appropriate mechanism for balancing remaining concerns around the need for investment proposed by South East, and the risk identified by Ofwat that South East may need to access funding for additional investment for resilience schemes during 2025-30. In particular, we consider the mechanism sends a signal to South East that funding will be made available if it can make the case for the investment, and demonstrate its ability to deliver."*[167]

(b) *"We consider that the contingent allowance mechanism provides an opportunity for South East to address concerns that remain about the need for the investment, but we would also encourage Ofwat to take all reasonable steps to minimise any associated delays."*[168]

(c) *"South East has not provided detailed submissions with supporting evidence on what it considered the size of the fund should be. In particular, South East has not provided an assessment of the schemes it considered might be appropriate for funding through a contingent allowance, including the costs of these schemes."*[169]

Our response

3.191 At the time of drafting our SoC, we asked for our resilience programme to be fully funded at £166.4m, on an ex-ante basis. We stated that if we received this funding, we would not have a need for the contingent allowance. However, based on the PD, we will not be fully funded for our resilience programme. As such, we support the retention of the £50m contingent allowance in principle. However, we maintain the concerns outlined in our SoC, specifically that the conditions to access the resilience contingent allowance are too restrictive and inconsistent with the consumer objective.[170]

3.192 We request the following changes be made to the contingent allowance:

(a) **Scope** - While we accept the £50 million value of the contingent allowance set by Ofwat, we think that this allowance should be used to address *"new and increasing risks*" as outlined in Ofwat's response to query 'OFW-FD-SEW-002'.[171] As set out above, we do not support Ofwat's suggestion to use the contingent allowance for existing schemes such as Bewl. Ofwat has stated in its response to query 'OFW-FD-SEW-002' that Bewl could be considered for funding under the existing £50m contingent allowance. However, Bewl is designed to address known risks rather than new ones. Including it within the £50m contingent allowance would use up more than 50% of the potential funding. This would leave inadequate funding to address emerging resilience risks in AMP8. We consider that our Bewl WTW investment should be funded in full in the CMA's Final Report.

(b) **Timing** – while we agree that a submission date of November 2026 is appropriate for new and emerging risks, we request greater flexibility around emerging schemes that are urgent and can be delivered more efficiently and deliver customer benefits sooner. It is not in our customers' interest to delay urgent issues due to regulatory process and we therefore request that:

(i) We have an open dialogue with Ofwat about emerging investment needs and how they fit within the contingent allowance.

165 Ofwat, February 2025, PR24 Final Determinations: Expenditure allowances, page 226.
166 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, page 172.
167 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.705.
168 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.706.
169 CMA, October 2025, Provisional Determinations: Volume 2, Chapter 5, paragraph 5.707.
170 SEW, March 2025, PR24 Redetermination Statement of Case, page 7.
171 Ofwat, February 2025, PR24 Final Determination Inbound Query, OFW-FD-SEW-002 Ofwat Response.

(ii) We can submit urgent schemes as and when they arise rather than having to wait until November 2026.

(c) **Delivery requirement** - In the PR24 FD, Ofwat provided a set of criteria to be met before accessing the £50 million contingent allowance. These include demonstrating that we have spent our enhancement allowances and that our resilience programmes are on target.[172] In its response to our SoC, Ofwat stated that our enhancement programme needs to be "on track" to access funding.[173] We understand Ofwat's rationale for linking our access to the contingent allowance to progress across our wider resilience programme. However, Ofwat's requirement that our resilience programme must be "on target" or "on track" before we can access the contingent allowance is unnecessary and disproportionate. As addressed further below, the CMA is not proposing to alter PCDs, meaning that we are already strongly incentivised to deliver our resilience programme on time. Adding an additional condition that ties access to the contingent fund to the delivery status of each and every scheme is unreasonable and risks customer detriment. We ask the CMA to remove this requirement to allow us access to the contingent allowance while maintaining existing delivery incentives.

PCDs

3.193 In its PD, the CMA retains Ofwat's approach to the PCDs framework and does not accept any changes.

Summary of the CMA's approach

3.194 The CMA considered submissions from both the Disputing Companies and Third Parties[174] regarding Ofwat's PR24 FD approach to PCDs.

3.195 For the purposes of the Redeterminations, the CMA's approach has been to address issues "*at source*".[175] This means it focuses on resolving problems by targeting specific features of the PCD framework only where they are shown to cause broader negative effects.[176]

3.196 The PCD-related concerns reviewed by the CMA fall into the following categories:

(a) Amendments to specific PCDs related to enhancement or base expenditure allowances.

(b) Non-delivery PCDs that could result in negative expected returns.

(c) Requests for changes to time incentives.

(d) Flexibility to adjust PCDs during the AMP period.

(e) Potential overlapping penalties resulting from PCDs.

(f) Administrative and regulatory burdens associated with PCDs.

3.197 In all these areas, the CMA retains Ofwat's PR24 FD approach. It also expresses support for Ofwat's PCDs draft consultation[177] proposing the development of a narrowly defined change control process for PCDs.[178] Additionally, the CMA retains Ofwat's approach to non-delivery

172 "*This allowance is available to South East Water, subject to proving 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"* - Ofwat, February 2025, PR24 Final Determinations: Expenditure allowances, page 226.
173 Ofwat, April 2025, PR24 Redeterminations: Response to South East Water's Statement of Case, paragraph 4.133.
174 Third parties included Blueprint for Water, Citizens Advice, CCW, The Global Infrastructure Investor Association, The Thames Investor Group, Thames Water and Water UK.
175 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.18 and 6.20.
176 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, footnote 47.
177 Ofwat, September 2025, Consultation on changes to PR24 price control deliverables.
178 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.100.

PCDs, provided that, through the PCD consultation process, Ofwat gives sufficient clarity on the implementation of clawback.[179]

Our response

3.198 Whilst the CMA claims to apply an "at source" approach, it has not engaged with any of the PCD-related arguments we have put forward.

3.199 Our current mains renewals PCD establishes three separate targets (for base, asset enhancement, and leakage driven). In practice, however, renewal programmes inevitably comprise a mix of all three categories within any given area. Managing delivery to meet an exact balance between these categories would be inefficient and impractical. Moreover, while the non-delivery penalty is the same across categories – which should, in theory, make reallocation between them neutral in delivery incentive terms – our analysis indicates otherwise. Scenario testing[180] shows that even a modest 10% shift between two categories would result in a delivery penalty of £7.6m by 2030. This demonstrates that, in effect, there is no genuine flexibility within the current framework.

3.200 During the hearings, [redacted]. We proposed that delivery should be measured at the programme level (i.e., based on total km of mains renewals rather than specific categories) and the timing of the PCD set at the end of the AMP period. This would allow substitution between different types of mains replacement within the programme. Such an approach strikes the right balance between affording customers protection while also allowing us some flexibility within the period to respond as effectively as possible to changes and innovations that occur. If the CMA is not minded to change the definition to a programme level, we request that the CMA make two straightforward changes:

(a) remove the annual targets and instead set a total PCD for the end of the AMP for mains renewal; and

(b) allow a reasonable degree of movement between categories, which we suggest being set at 25%.

3.201 This would allow us to optimise our programme over time while ensuring that the full programme is delivered. This approach would be in the best interest of customers, as greater flexibility would enable us to plan and deliver the programme more efficiently, ultimately reducing overall costs.

3.202 In addition, we support the introduction of broader flexibility into the PCD framework, consistent with the proposals outlined in Ofwat's draft consultation. Our full position is set out in our response to the PCD consultation.[182]

179 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.74.
180 SEW, 2025, Response to Ofwat's consultation on Changes to PCDs consultation, page 5.
181 SEW Hearing Transcript, 4 July 2025, page 14, lines 10 to 16.
182 SEW, 2025, Response to Ofwat's consultation on Changes to PCDs consultation.

4 Frontier shift

We welcome the CMA's recognition that Ofwat's FD illogically presumed that the water sector should have been able to outperform UK productivity growth by a factor of 10 at AMP8, and that a lower frontier shift estimate is justified. However, we note additional factors supporting a frontier shift estimate below 0.7% and submit that, consistent with the evidence we have previously submitted, the final figure should be 0.5%.

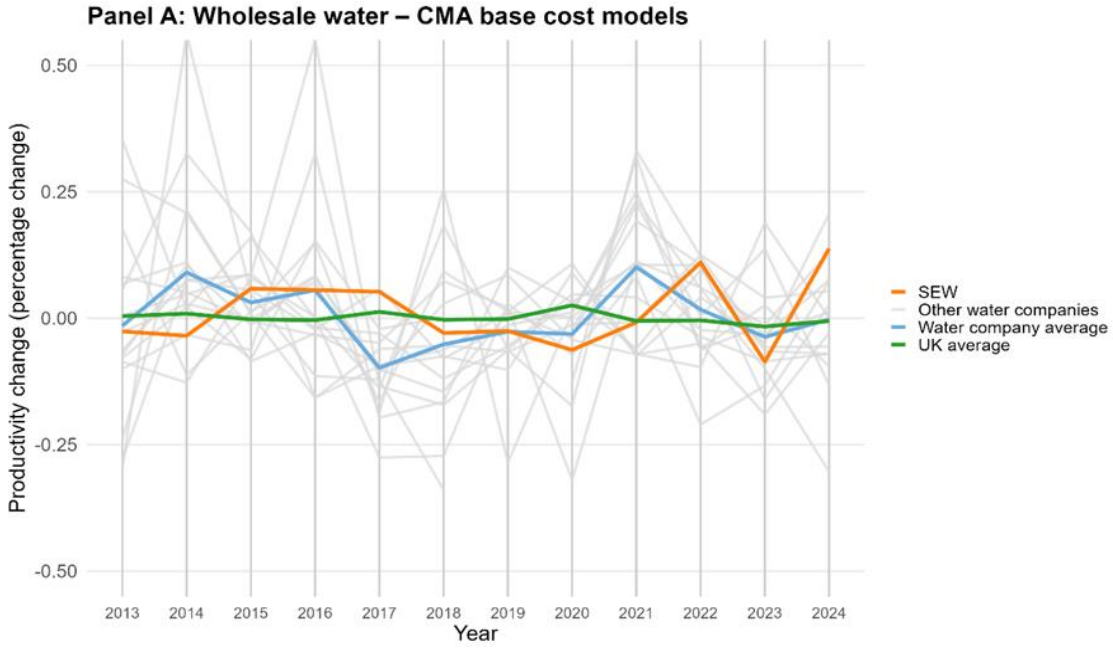
4.1 We welcome the CMA's provisional decision to set a frontier shift target of 0.7% per year, being materially lower than the target of 1.0% per year set by Ofwat in its PR24 FD.

4.2 We also welcome, and agree with, the reasoning that the CMA has relied on in reaching the above view. In particular, we agree that the CMA is right to focus on the question of whether, and to what extent, the productivity performance of the water sector should be expected to be similar to that of the wider UK economy (which has seen near-zero productivity growth in the post financial crisis era). We further agree that the evidence the CMA has considered in answering this question is highly relevant. This includes analysis showing that: (i) the historical productivity growth of the water sector has been similar to that of the UK economy; and (ii) most sectors of the economy have experienced a slow-down in productivity growth, following the financial crisis.

4.3 We have replicated the CMA's analysis of water company productivity changes and compared the resulting estimates to UK productivity growth, as shown in the chart below. We have sourced the estimates of UK productivity growth from the ONS multifactor productivity (**MFP**) dataset,[183] which extends up to 2024 and, therefore, allows comparison over the same period for which the CMA estimated water company productivity growth (2013 to 2024). Similar to the CMA's provisional conclusions, we find that the average[184] productivity growth of the water industry (as calculated by the CMA) is similar to the UK as a whole, being slightly above in some years and slightly below in others. This conclusion also holds specifically for SEW's estimated productivity growth.

[183] See ONS link here. Data relates to total UK market economy.
[184] The 'water company average' shown on the chart in a given year is the mean productivity growth across all water companies that year.

Figure 4.1: Productivity changes of water companies compared to the UK average



4.4 Following from the above (and also consistent with our previously submitted evidence), we welcome the conclusions the CMA logically draws from said evidence; namely, that: (i) *"the causal factors of the slowdown [are] mainly economy-wide [and] have affected most sectors to some degree, including the water sector;"*[185] and (ii) there are no strong reasons to expect the productivity growth of the water sector to *"diverge substantially"*[186] from that of the UK economy[187] (where the CMA primarily considers whether previous investment levels, and the scope to benefit from innovation and technology, might imply materially different productivity growth for the water sector, relative to the wider economy).

4.5 We disagree with just two aspects of the CMA's provisional decision.

4.6 Firstly, having reached a view that the water sector is likely to have productivity growth similar to that of the UK as a whole, to set the frontier shift target, the CMA next asks itself the question: "*what are the forecasts for productivity growth in the economy as a whole and for the water sector?*"[188] The CMA then reviews forecasts from the OBR and Bank of England, placing some weight on each, to arrive at its proposed target of 0.7% per year. If the CMA is seeking to set a frontier shift target that best reflects overall UK productivity growth over AMP8, it should place at least some weight on actual recent UK productivity growth data and not rely solely on forecasts. This is because all forecasts are subject to error, and forecasts of UK productivity growth specifically have proven to be systematically (and materially) optimistic, relative to outturn productivity growth, as the CMA itself recognises.[189] In this context, the CMA's proposed target of 0.7% per year appears high, relative to the UK's current productivity growth. For example, the ONS MFP dataset shows total UK productivity growth averaged just 0.3% per year over 2024.[190] The CMA's current proposed target therefore implies – in our view implausibly – that the water industry will deliver productivity growth of more than double that currently being achieved by the UK.[191] Moreover, when commenting on the implications of its decision for other sectoral regulators, the CMA itself states that data on actual productivity performance (in addition to

185 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.159.
186 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.173.
187 Whilst (like the CMA) we do not expect the water sector's productivity growth to *substantially* differ from that of the UK's, we remain of the view that the evidence is most consistent with a central expectation that it would have somewhat lower productivity growth than the UK average.
188 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.155(b).
189 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.162.
190 See ONS link here. Data relates to total UK market economy, average of quarterly % growth over 2024.
191 Or, put another way, it presumes that, if the water sector performs in-line with the UK economy, then the UK's productivity growth performance will more than double over this period.

forecasts) should be taken into account when setting frontier shift: *"frontier shift decisions should reflect recent evidence and if productivity growth data or forecasts were to change then other regulators may reach different conclusions"* [emphasis added].[192] Finally, the OBR is currently due to publish its latest forecasts on 26 November 2025[193] and so (to the extent the CMA attaches weight to forecasts in its Final Report), we would encourage it to reflect any changes made by the OBR at that time.

4.7 Secondly, in relation to the issue of whether there is a potential overlap between frontier shift and outcomes targets, the CMA states: *"water companies are expected to deliver improvements in outcomes* from *their base expenditure in AMP8. It is likely that other industries also improve the quality of their products. Our provisional view is that this is not a convincing reason to expect productivity growth in the water sector to diverge substantially from the wider economy."*[194] We agree with the CMA's statement that water companies being required to make quality improvements is not a reason to expect their overall productivity growth to differ from that of the UK. However, the pertinent issue is not the total achievable productivity growth, but rather what is being measured in the productivity data being used to set the frontier shift target. Specifically, the UK TFP data will measure productivity gains made by the UK as a whole, through either cost reductions and/or quality improvements. Therefore, if the CMA's assessment is that the UK will achieve productivity growth of 0.7% per year over AMP8 (and therefore, so can water companies), the conclusion that logically follows is that the frontier shift target, as applied to company costs, must be somewhat below 0.7% per year, in order to avoid a double count with the stretching improvements required under the PR24 outcomes package. Put differently, we agree with the CMA's framework and analysis, but not with the final inference it then draws in the setting of the frontier shift target (as is applied to company costs).

4.8 In conclusion on this topic, we strongly welcome the CMA's position to recognise the illogical presumption under Ofwat's FDs that the water sector should have been able to outperform UK productivity growth by a factor of 10 at AMP 8, and over recent decades. We also agree with the CMA's reasoning. However, due to the two matters set out above, we consider that the CMA's reasoning in fact implies that the frontier shift target (set on costs) should be below 0.7% per year; and should be set at 0.5% per year, consistent with our business plan and the evidence submitted with our SoC.

192 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.174.
193 OBR press release here.
194 CMA, October 2025, Provisional Determinations, Volume 1, Chapter 4, paragraph 4.166.

5 Outcomes

We welcome the CMA's recognition that: (i) there is no merit in setting the WSI collar at -2% of RoRE; (ii) the WSI PCL should reflect SEW's company-specific circumstances; and (iii) the PD outcomes package is negatively skewed by c. 20bps, consistent with the risk analysis submitted.

We ask that the CMA reconsider the level of our company specific PCL for WSI as the DDR WSI PCL represents a target that is too stretching as it included an extreme weather exclusion (which has not been reflected in the CMA PD) and therefore exposes us to a significant level of downside risk.

Introduction

5.1 This section sets out our response to the CMA's decision in the following areas:

(a) WSI – Collar;

(b) WSI – PCL for SEW; and

(c) Other (C-MeX, NHH Voids, Leakage).

Water Supply Interruptions - Collar

5.2 In the PR24 FD, Ofwat set our collar on WSI to -2% of RoRE compared to -1% of RoRE for the rest of the industry. In our SoC, we made the case for a collar at -0.5% of RoRE. The CMA's provisional determination is that our WSI collar should be set at -1% of RoRE, consistent with the rest of the industry.

5.3 We provide below a summary of the reasons why we should have a tighter collar than -2% of RoRE.

(a) One of the reasons that Ofwat set a collar of -2% was that it felt we needed sufficient incentives to improve our performance on WSI. The CMA also cited incentive considerations to justify retaining the sector collar at -1%, noting that a "*requested 0.5% RoRE collar could significantly weaken incentives to avoid poor performance*".[195] This is a flawed argument. With a tighter collar and the same ODI rate, we face the same marginal incentives to improve. To the extent that Ofwat or the CMA may be concerned about the lack of incentives we face if we hit the collar, this concern should be mitigated by the number of other mechanisms that would continue to incentivise us and protect customers. These other mechanisms include reputational incentives, the overlap with other ODIs such as C-MeX, as well as substantial costs such as the operational cost of fixing service disruptions, and GSS payments.[196]

(b) Ofwat allowed United Utilities a company-specific PCL for internal sewer flooding, due to United Utilities' historical performance issues in this service area. Ofwat did not however set United Utilities a company specific collar for internal sewer flooding. It would therefore be inconsistent to set a company specific collar for us on WSI.[197]

(c) As noted in Section 7 below, the CMA has adopted an approach of fixing risk at source, rather than aiming up in setting the cost of capital, which we support. It is therefore

195 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.495.
196 SEW, March 2025, Statement of Case, Annex F, paragraph 57.
197 SEW, March 2025, Statement of Case, Annex F, paragraph 52(d).

necessary for us to face a tighter collar to ensure that we are not faced with an unreasonable level of downside risk on WSI.

5.4 Overall, there is a strong case for us to have a tighter collar than -2% of RoRE, and we welcome the CMA's provisional decision in this regard. However, we consider that there remains a strong case for our WSI collar to be set at -0.5% of RoRE to ensure an overall balanced package of incentives when considered alongside all of the other ODIs. As indicated in paragraphs 7.7 to 7.9 below, the CMA's proposed WSI PCL causes significant concern as it creates excessive risk exposure for our company given that we are very likely to hit the -1% RoRE collar level during AMP8. This in turn can impact our investment grade rating under plausible downside scenarios.

Water Supply Interruptions - PCL

The CMA's approach

5.5 The CMA has provisionally set a company-specific PCL for WSI, at the level set out in Table 5.1 below.

Table 5.1: Provisional Determinations – WSI PCL for SEW

25/26	26/27	27/28	28/29	29/30
00:12:22	00:11:26	00:10:30	00:09:35	00:05:00

5.6 To determine this PCL, the CMA took the starting point as our DDR PCL of 12 minutes and 22 seconds,[198] which was originally proposed alongside an extreme weather exclusion. The CMA then calculated the uplift this implied above the common PCL in the first year of AMP8. This results in an uplift of 3 minutes and 39 seconds. The CMA then adds this uplift to the common PCL for the first four years of AMP8. In year five, the CMA sets our PCL at 5 minutes, in line with the common PCL.

5.7 In reaching its provisional decision, the CMA asked itself the following three questions:[199]

(a) Should a company-specific PCL be applied to SEW for water supply interruptions?

(b) What factors should inform the level at which the company-specific PCL is set?

(c) At what level should a company-specific PCL be set?

5.8 We consider the CMA's approach to each of these questions below.

5.9 The CMA has set a reward deadband between the company-specific PCL and the common PCL. We agree with this approach. It also remains acceptable to us that our WSI PCL be strictly penalty-only, as we had originally proposed, thereby eliminating any possibility of outperformance payments. However, the CMA's approach is reasonable in principle.

Our response to the CMA's approach

Should a company-specific PCL be applied to SEW for water supply interruptions?

5.10 The CMA's view is that there should be a high-bar for implementing a company-specific PCL, and that it is appropriate to "*only move away from a PCL that has been set at a common level, and set a company-specific PCL, where there is compelling evidence that a company-specific*

198 We note that since the publication of the Provisional Determinations, our Draft Determination Response position has been clarified. At that point in time, the proposed starting PCL was intended to be 12 minutes and 22 seconds, as set out at page 18 of SEWDD3, though our PCL trajectory was erroneously calculated and presented in Table 3.1 of SEWDD3 starting from 12.22 minutes (12 minutes and 13 seconds). The CMA's Provisional Determination is consistent with the intention of our Draft Determination Response, and therefore we use this as the starting point for our response.

199 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.258.

approach would be justified".[200] While we hope that the regulatory approach may change as recommended by the IWC's report on the water sector, such that there is greater consideration of company-specific circumstances, we understand why the CMA has set a high-bar for a company-specific PCL in the context of a Redetermination of PR24.

5.11 Through our submissions to Ofwat, in our SoC, in responses to the CMA's requests for information and during the PR24 main party hearings, we have provided comprehensive evidence on the need for a company-specific PCL. This has covered our WSI performance, the factors that drive our performance, and the steps we have taken and will take in future to improve our performance. As set out in Table ANF4 of our SoC and Table 5.2 below, we have provided an equivalent level of justification and evidence in support of a company-specific PCL to that provided by United Utilities, for whom Ofwat applied a company-specific PCL for internal sewer flooding.

Table 5.2: Comparison of UU and SEW evidence

	Evidence provided by United Utilities as referenced by Ofwat	Evidence provided by SEW
Asset configuration and external factors	Interaction between high urban rainfall and proportion of combined sewers	Interaction between network configuration, change in customer behaviour and demand post Covid and extreme weather.[201]
Overspend and effort to fix the issue	Significant effort to tackle performance during 2020-25 and overspending of PR19 allowance	As evidenced in Query Ref – OFW-OBQ-SEW-124, we have overspent[202] in the areas of growth and resilience and have revised our operational approach to WSI significantly.
Good performance in related area	Frontier level of sewer blockage performance	Our western region has a low level of supply interruption which demonstrates this is a network configuration issue, not an operational issue.[203]

5.12 We have provided a compelling case for a company-specific adjustment and we welcome the CMA's provisional decision to make such an adjustment.

What factors should inform the level at which the company-specific PCL is set?

5.13 In the PD, the CMA considers how the following factors may have relevance for the level at which a company-specific PCL is set:

(a) our PR24 enhancement schemes;

(b) the scope for operational improvements;

(c) our submissions on the challenges we face in relation to water supply interruptions, including on the impact of extreme weather; and

(d) our proposed PCL in response to Ofwat's DD.

200 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.262.
201 SEW, March 2025, Statement of Case, Annex F.
202 Ofwat has disputed this in the resilience interconnector deep dive but it has failed to account for developer services being regulated as a hybrid till. See Section 3, 'resilience interconnectors' of this Response for a more detailed description.
203 SEW, March 2025, Statement of Case, Annex F.

5.14 In general, we agree with the CMA's approach to determining the relevance of these factors, and we set out our views related to each of these below. We note, as does the CMA,[204] that once the relevant factors have been considered, the methodology we employ to estimate the appropriate level of the PCL differs from that taken by the CMA. We discuss this in more detail in paragraphs 5.29 to 5.40 below.

5.15 In relation to **enhancement schemes**, we agree with the CMA that our PR24 enhancement schemes should be considered a relevant factor in determining the appropriate level of the company-specific PCL.[205] We also agree that enhancement schemes accounting for region-specific risk are the relevant ones to take into account. However, the CMA notes that it only considers schemes which address current risks as relevant and does not consider that schemes which address future risks are relevant considerations.[206] It is not clear to us how the CMA defines current risks and future risks in this context.

5.16 There are two interpretations of the CMA's approach:

(a) A future risk could potentially be a risk that we will face in the future, but which is currently unknown to us. None of our enhancement schemes have been designed to reduce such risks.

(b) Another possible interpretation is something which is currently known to us, based on historical experiences we have faced and which we expect to continue to be a risk in future (though in many cases, an increased risk). This reflects the sorts of risks we are typically attempting to reduce through our enhancement spend.

5.17 To demonstrate the fact that all our enhancement schemes are designed to address current risks of the type described under (b) above, we have conducted an analysis which shows how these schemes interact with a set of four severe weather events we experienced in AMP7.

5.18 As explained in paragraphs 3.82 to 3.85, we have identified the areas and properties that experienced supply interruptions during the Summer Demand events in 2020, 2022 and 2023, and the Freeze Thaw event in 2022. Using network schematics, we have then identified whether these areas would be supported by the PR24 schemes, by matching the relevant schemes to each impacted DMA. We provide further detail in paragraphs 3.82 to 3.85 on the modelling we have carried out, and the results of this analysis are shown in the table below.

5.19 As can be seen, while an estimate, our analysis suggests that the number of properties without supply would have been reduced to zero in each of the four events analysed. This analysis demonstrates that our enhancement schemes are designed to address current risks and therefore should be considered when setting our company specific PCL.

Table 5.3: AMP8 enhancement schemes and AMP7 weather events

AMP8 enhancement schemes		Summer Demand 2020	Summer Demand 2022	Freeze Thaw 2022	Summer Demand 2023
[redacted]	Customers impacted during AMP7 high demand events	0	1,716	12,105	508
	Estimate of customers impacted if PR24 schemes were in place	0	0	0	0

204 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.279.
205 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.266.
206 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.287.

AMP8 enhancement schemes		Summer Demand 2020	Summer Demand 2022	Freeze Thaw 2022	Summer Demand 2023
[redacted]	Customers impacted during AMP7 high demand events	3,596	454	21,693	7,507
	Estimate of customers impacted if PR24 schemes were in place	0	0	0	0
	Customers impacted during AMP7 high demand events	2,465	1,182	0	146
	Estimate of customers impacted if PR24 schemes were in place	0	0	0	0
	Customers impacted during AMP7 high demand events	0	7,630	77	3,494
	Estimate of customers impacted if PR24 schemes were in place	0	0	0	0
	Customers impacted during AMP7 high demand events	0	1,988	5,703	1,681
	Estimate of customers impacted if PR24 schemes were in place	0	0	0	0
	Customers impacted during AMP7 high demand events	0	1,610	72	690
	Estimate of customers impacted if PR24 schemes were in place	0	0	0	0

5.20 In relation to the contribution of **operational responses**, we agree with the CMA that the scope for such responses should be a relevant factor in informing the company-specific PCL.[207] We have reviewed and learned lessons from each supply interruption incident – focusing on prevention, mitigation and response – and listened carefully to our customers. We have developed and implemented an action plan comprising a set of schemes which have already improved our supply resilience. These are addressed in more detail in Annex D of our SoC. We have also made public our reviews of our performance. For example, following the significant 2018 freeze-thaw event (the "Beast from the East") we published a detailed report on the lessons we learned.[208]

5.21 We generally use tankers in the following three ways. We have used them to effectively improve the customer experience and reduce our interruptions, but they do not have a significant impact on our WSI performance.

207 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.271.
208 SEW, September 2018, 'Beast from the East' Incident Response – South East Water Action Plan.

(a) One of the main uses of tankers is to supply water to vulnerable sites such as hospitals, schools and care homes in a big event. This improves our customers' experience but does not have a significant impact on our WSI performance in a big event.

(b) We also use tankers in the build up to a big event, supplying up to a [redacted] a day. This could extend the amount of time before an interruption occurs, reducing the overall impact to a small extent.

(c) Tankers can also be used during more frequent, but lower impact events such as burst mains to help reduce the impact.

5.22 We maintain, however, that operational improvements alone will not be sufficient to improve our performance to a level that our customers need. We also note that the CMA appears to recognise this, as it concludes that operational improvements do not negate the need to consider enhancement schemes as a relevant factor.[209] While operational responses are of course important, potential responses such as the deployment of additional tankers alone cannot replicate the benefits of capital enhancement schemes, which deliver permanent increases in system capacity and interconnectivity.

5.23 In considering the relevance of operational improvements further, the PD cites the examples presented by Ofwat of Severn Trent and Affinity Water, both of whom reportedly achieved substantial improvements in performance. In general, it is not appropriate to use the experience of other companies to gain an indication of the extent of the 'minutes' improvement possible through operational responses for us in our region. This is because the scope for improvements varies by company and is driven by regional and network characteristics.

5.24 The submissions from Ofwat are anecdotal, rather than analytical, and neither Ofwat nor the CMA have conducted a full assessment of the viability of operational responses between companies. Additionally, we note that there are equivalent examples from other companies demonstrating the importance of network characteristics. For example, Portsmouth Water, in 'Managing our Resilience in the Long Term' states:

> *"The interconnectivity of the network built up over many years leaves the business in an extremely strong position with regards to supply interruptions. We can easily move water around our entire area of supply and can swiftly recover from major burst mains or outages at treatment works by diverting water from other areas within the network"*[210]

5.25 We do not have a detailed view of the configuration of other companies' networks or the relative challenges they face but we note, as discussed in the hearings, that Severn Trent has had significant resilience funding previously. For example, the Birmingham Resilience Project (**BRP**) which was completed in 2020 at the cost of approximately £300m. This project was aimed at providing backup supply for Birmingham in case of failure. This included a 26km pipeline from the River Severn to Frankley WTW, new pumping stations and treatment upgrades, and underground tunnels and mains forming a ring around Birmingham.

5.26 This is also true of other top performers on supply interruptions, such as Portsmouth and Wessex.[211] Portsmouth's network was heavily reinforced in WW2 to protect the naval shipyard. Wessex built a resilience grid between 2010 and 2020, which involved funding for 200km of trunk main, 24 new and refurbished pumping stations, and 12 new storage tanks. During the main party hearings, Wessex [redacted]

209 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.266.
210 Portsmouth Water, Managing our Resilience in the Long Term, page 6.
211 For example, Portsmouth and Wessex. Portsmouth's network was heavily reinforced in WW2 to protect the naval shipyard. Wessex built a resilience grid between 2010 and 2020, which involved funding for 200km of trunk main, 24 new and refurbished pumping stations, and 12 new storage tanks. Both are top four performers on WSI and have delivered under five minutes on average 2020-24.

[redacted][212]

Our customers have not paid for equivalent enhancement schemes in the past.

5.27 As is clear from the above, we therefore disagree with the CMA that our submissions on demand and headroom do not introduce additional factors that should be taken into account when determining the PCL.[213] Our view is that these submissions demonstrate both the current risks that we face, and how they are expected to evolve over AMP8, which is relevant for considering the impact of our enhancement schemes on the appropriate level of PCL. These submissions also provide evidence on characteristics of our network which limit the scope for improvements through operational responses alone.

5.28 Finally, the CMA considers our DDR proposed PCL to be a relevant factor, though it notes that it does not "*inform the appropriateness of a company-specific adjustment to reflect South East's relevant enhancement schemes in AMP8*".[214]

5.29 We understand the logic for considering this proposal, however we wish to make two observations, which explain why we consider that this proposed PCL is of limited relevance. Firstly, we agree with the CMA that this PCL does not accurately reflect the impact of our enhancement schemes. Additionally, as set out in our response to RFI06, this PCL was developed in the context of the incentives provided by the Quality and Ambition Assessment (**QAA**) QAA, and presented based on the assumption that Ofwat would exclude extreme weather incidents when assessing companies' WSI performance for the purposes of the WSI ODI. We made this explicit in our DDR submission at various points:

(a) *"We believe a more appropriate approach would be to exclude severe weather events as these are outside of our control and we are not funded to be resilient to all possible weather events."*[215]

(b) *"Exception for severe weather on water supply interruptions: whilst we invest through AMP8 to significantly improve the network's resilience, we are requesting an exemption for severe weather events."*[216]

5.30 At the time of Ofwat's Draft Determination, we were faced with a QAA penalty of £6m (calculated as 15 basis points of RoRE). In its justification for this penalty, Ofwat directly referenced our proposals on supply interruptions.[217] We therefore faced significant regulatory and financial pressure to propose a PCL which would be acceptable to Ofwat. We note that these perverse incentives generated by the QAA have been recognised by the IWC, which has made a recommendation that the QAA should be removed in future.[218] In its review, the IWC found "*the QAA also appears to have introduced perverse incentives, with companies responding by proposing expenditure plans with lower costs to attempt to align with Ofwat's 'ambition' criteria on outcomes, costs and affordability – rather than (potentially) what they actually need".*[219]

212 PR24 Outcomes Hearing, Transcript, page 115 lines 2 to 9.
213 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.277.
214 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.282.
215 SEWDD3, August 2024, Performance Commitments and Outcome Delivery Incentives, page 19.
216 SEWDD4, August 2024, Financials Response, page 16
217 Ofwat, 2024, South East Water Quality and Ambition Assessment Appendix.
218 Independent Water Commission, 21 July 2025, Final Report, Recommendation 21.
219 Independent Water Commission, 21 July 2025 Final Report, paragraph 466.

5.31 In contrast, the PCL proposed in our SoC was based on improved modelling which explicitly took account of our enhancement schemes. It was also developed under the assumption that extreme weather would *not* be excluded, and that we would not be penalised (through the QAA) for presenting a realistic view of our performance. While we understand that the CMA considers the DDR PCL a useful reference point, we consider the PCL proposed in our SoC a more robust data point in determining the appropriate level for our company-specific PCL.

At what level should the company-specific PCL be set?

5.32 We recognise that in determining the appropriate level for a company specific PCL in our SoC, we followed a different approach and logic to that set out by the CMA in the PD.

5.33 While the CMA's provisional choice of PCL does not reflect the impact of our enhancement schemes, the CMA does set out a logical theoretical approach taking into account the impact of relevant schemes in setting the PCL. Our understanding of the CMA's proposed approach is that it involves adding on the expected benefit (in minutes) of the funded enhancement schemes which it considers relevant to the common PCL, to reflect the impact of company-specific challenges that we currently face on our performance. In our SoC, we followed a different approach. Instead of adding expected benefits to the common PCL, we calculated a stretching but achievable trajectory by considering our current performance and assuming improvements in line with the benefits of our enhancement schemes as and when they are delivered.

5.34 The CMA ultimately concludes that, given concerns over whether estimated benefits of our enhancement schemes are a reliable basis for setting the PCL, our DDR position of 12 minutes and 22 seconds is an appropriate starting point. However, this represents a target that is too stretching, is not a PCL that we can reasonably be expected to achieve, and exposes us to a significant level of downside risk. At the very least, this approach fails to take account of the impact of severe weather. We maintain that our SoC below sets out our best estimate of our company specific PCL:

Table 5.4: SEW SoC PCL for WSI

	25/26	26/27	27/28	28/29	29/30
SEW SoC PCL for WSI	00:33:00	00:30:00	00:29:00	00:24:00	00:08:00

5.35 We have provided extensive evidence and justification for this PCL, through our SoC and RFI Responses. Notwithstanding that, we have looked to provide an alternative estimate of our company specific WSI PCL, taking into account the CMA's considerations in the PD. We have developed the following two approaches and one cross-check to consider how our company specific PCL should be set.

(i) Approach 1: We have adopted the CMA's method for setting a company-specific PCL, i.e. uplifting the common PCL to reflect our region-specific issues, using more conservative assumptions on the impact of our enhancement schemes.

(ii) Approach 2: We have amended our DDR proposal to reflect the impact of severe weather.

(iii) Cross-check: Our year-to-date WSI performance for 2025/26.

5.36 In the remainder of this section, we set out the steps we have taken for each of these three approaches and show the company specific PCLs we estimate with each.

Approach 1: Uplifting the common PCL to reflect our region-specific issues

5.37 The CMA provisionally concluded that it cannot explicitly take into account the impact of our enhancement schemes as it has concerns over the reliability of the data, and in particular considers that the estimated benefits in terms of minutes of interruptions are overstated. We do

not share the CMA's concerns with the data, and refute the assertion in the PD that our estimated benefits fail to reflect operational improvements and so constitute an overestimate.[220] We set out in detail the approach that we took to estimate the impact of our enhancement schemes on our WSI performance in our response to RFI07. However, we understand that it is challenging for the CMA to be confident in its assessment of this data, given a lack of common approach adopted by companies and the time available to carry out the PR24 Redeterminations.

5.38 We have therefore worked within the CMA's approach of uplifting the common PCL but using a much more conservative estimate of the impact of our enhancement schemes. To do this, we have taken the following steps, reflecting the CMA's view in the PD.

(a) First, we have identified the relevant PR24 enhancement schemes. For this, we have considered schemes which have been either fully or partially funded by Ofwat in its FD or by the CMA in the PD. For the avoidance of doubt, there is still a need for the schemes which have not been fully funded, or partially funded, however we are working within the CMA's approach to calculating a company specific PCL. As discussed above, all our enhancement schemes are to reduce current risks, and so we have not removed any schemes from the list to reflect this point. The schemes we have included and excluded are shown in Table 5.5 below.

(b) Noting the CMA's concerns about the scale of the impact we have estimated our enhancement schemes will have, we have tested two sensitivities, one being 100% of the impact we estimated and another being only 50% of our estimated impact.

(c) Our estimated impacts show the point at which the enhancement schemes will have an impact on our performance. Under the CMA's logic, for the included schemes, this means that we will face region-specific issues until the scheme has an impact on our performance, and we need to add an uplift in minutes to the common PCL only until the impact of the scheme kicks in. For almost all currently funded schemes, as set out in Table 5.5, the expected benefits materialise from the start of Y5. However, for [redacted] we expect that we will see 00:00:55 benefits from the start of Y3 and for *Interconnectivity* [redacted] we estimate that we will see 00:01:03 benefits from the start of 28/29. This means that while the CMA's current approach applies a uniform uplift for the first four years of AMP8, the uplift we apply reduces in Y3 and Y4 to take into account the delivery of these schemes. Consistent with the CMA's approach, we do not apply an uplift to the common PCL in Y5.

Table 5.5: SEW view of included enhancement schemes under the CMA's approach

Scheme	Expected benefit (minutes)	Expected benefit (HH:MM:SS)	First year benefits realised	Included/Excluded in PCL calculation
[redacted]	0.91	00:00:55	Y3	Included
	1.05	00:01:03	Y4	Included
	2.92	00:02:55	Y5	Included
	2.54	00:02:32	Y5	Included
	1.25	00:01:15	Y5	Included
	0.69	00:00:41	Y5	Included
	2.06	00:02:04	Y5	Included

220 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.292.

Scheme	Expected benefit (minutes)	Expected benefit (HH:MM:SS)	First year benefits realised	Included/Excluded in PCL calculation
[redacted]	1.39	00:01:23	Y5	Included
	5.2	00:05:12	Y5	Excluded
Additional tankers	0.5	00:00:30	Y1	Excluded
Smart water networks	3	00:03:00	Y2	Excluded
[redacted]	4.31	00:04:19	Y4	Excluded

5.39 Based on this view of the relevant schemes and their intended benefit, the table below shows the implied company-specific PCLs assuming 100% of the estimated minutes benefit, and 50% of the estimated minutes benefit.

Table 5.6: Implied PCLs assuming different benefit estimates[221]

	25/26	26/27	27/28	28/29	29/30
Common PCL	00:08:43	00:07:47	00:06:51	00:05:56	00:05:00
Updated PCL - total impact	00:26:43	00:25:47	00:23:56	00:21:58	00:05:00
Updated PCL - 50% of impact	00:17:43	00:16:47	00:15:23	00:13:57	00:05:00

5.40 Our view is that only including 50% of the impact of the funded schemes represents a highly conservative approach. However, we recognise that while we disagree with these concerns, the CMA has reservations over the extent to which our data represents a reliable basis for calculating the PCL. We therefore consider this figure in establishing our range of possible PCLs.

Approach 2: Our DDR PCL with extreme weather

5.41 As noted above, we do not believe our DDR PCL provides a reasonable basis for determining the appropriate level of company-specific PCL. Our SoC is based on improved modelling and was developed outside of the context of the QAA – and therefore represents a more realistic view of performance. Crucially, our proposed DDR PCL excluded extreme weather events, firstly because it was based on the best three years of our performance, and secondly because it was presented alongside the request that Ofwat would exclude extreme weather from the definition of supply interruptions, which has not been the case.

5.42 Therefore, the DDR PCL must be adjusted to take into account the impact of extreme weather if it is to be considered a reasonable basis for setting the company-specific PCL. In our SoC, we estimated the impact of extreme weather to be 9.47 minutes (00:09:28). To establish a PCL based on the DDR, but accounting for the impact of extreme weather, we add 00:09:28 to the uplift above the common PCL that the CMA has provisionally determined of 00:03:39. This implies a total uplift of 00:13:07, and a PCL in line with Table 5.7 below:

Table 5.7: SEW DDR PCL including extreme weather impact

	25/26	26/27	27/28	28/29	29/30
SEW DDR PCL plus extreme weather	00:21:50	00:20:54	00:19:58	00:19:03	00:05:00

221 Including Bewl and Smart Water Networks in this calculation would increase the starting PCL to 00:34:02 under the 100% impact scenario or 00:21:22 under the 50% impact scenario. Our view is that these schemes should be funded and taken into account under the CMA's outlined logic.

5.43 However, we note that the table above represents a conservative position. This is because our SoC estimate of extreme weather impact was predicated on an expected annual frequency of one to two events over AMP8, whereas we could likely be exposed to a higher number of events under current climate conditions. The Met Office (2024) report concludes that, *"the UK is seeing, on average, more frequent periods of hot weather"*.[222] These studies suggest that climate-related volatility is now a persistent, structural feature of our operating environment, not a transient anomaly, and directly affects our performance on WSI.

Cross-Check: Our year-to-date performance

5.44 As a cross-check for a reasonable level at which to set our company specific PCL, we have also looked at our year-to-date performance for WSI for 2025-26. We are not proposing that our PCL should be set based on our actual performance but believe that this does provide helpful contextual information on what we reasonably might be expected to achieve this year.

5.45 For the first half of the year, to the end of September 2025 (latest available), we have incurred 18 minutes of WSI. This includes the impact of extreme weather during the 2025 heatwave, which accounts for approximately a third of the minutes. Our operational response in the summer of 2025 included the deployment of tankers, but as explained above, there are limitations to the impact that tankers can have on our WSI performance in big events.

5.46 Due to the way that the performance measure is calculated, it is not possible for us to have a lower number than this by the end of the year. Therefore, our actual performance will be at least 18 minutes. Our internal reporting estimate of our end of year performance is 33 minutes, in line with our SoC. This shows that analysis submitted in our SoC is realistic and credible, which reaffirms that we will be exposed to significant downside risk even if CMA adopts our proposals under Approach 1 and/or 2.

Conclusion: our estimate of our company specific PCL

5.47 We maintain that the PCL set out in our SoC is based on the most appropriate position, as it is based on comprehensive evidence and takes into account all our relevant enhancement schemes. We continue to believe that the CMA should use this as the basis for setting our PCL for water supply interruptions.

5.48 However, in responding to the PD, we have looked to explore different approaches that could be used to determine the PCL, drawing directly upon the logic, data and conclusions set out in the PD. The differing approaches are summarised in Table 5.8 below.

Table 5.8: Summary of alternative PCL approaches

	25/26	26/27	27/28	28/29	29/30
SoC - SEW	00:33:00	00:30:00	00:29:00	00:24:00	00:08:00
Approach 1: Uplifting the common PCL to reflect our region specific issues - total impact	00:26:43	00:25:47	00:23:56	00:21:58	00:05:00
Approach 1: Uplifting the common PCL to reflect our region specific issues - 50% of impact	00:17:43	00:16:47	00:15:23	00:13:57	00:05:00
Approach 2: Our DDR PCL with extreme weather	00:21:50	00:20:54	00:19:58	00:19:03	00:05:00
Cross-Check: Year-to-date performance	00:18:00 *(only includes H1 FY26)*				

222 Met Office, 25 July 2024, Temperature extremes and records most affected by UK's changing climate.

5.49 This further analysis suggests a minimum range for our starting PCL of between 18 minutes (based on an optimistic view of our current performance in which we incur no more interruptions this year) and 33 minutes, consistent with our SoC. This suggests that the company specific PCL included in the CMA PDs is unachievable and too stretching, and we urge the CMA to reconsider where to set our company specific PCL in light of this evidence.

Other - C-MeX, NHH Voids and Leakage

C-MeX and NHH voids

5.50 We disagree with the CMA's decision not to adjust our C-MeX PCL and PR19 NHH Voids penalty, and maintain the reasoning set out in our SoC.[223]

5.51 On C-MeX, we welcome the CMA's recognition in the PD that there is statistically significant evidence of differences in scores between the South East and the rest of England.[224] However, we disagree with the CMA's conclusion that the fact that the difference identified is small means no adjustment should be made. As the C-MeX PCL is updated through AMP8, the true materiality of the difference cannot be estimated at this stage. Ultimately, continuing to benchmark our performance against national UKSCI scores means we face an unfair disadvantage which is straightforward to correct. As set out in our SoC, the CMA should amend the C-MeX methodology such that we are benchmarked against the all-sector average for the South East, and not the all-sector overall average.

5.52 On PR19 NHH voids, the CMA's provisional position is that no adjustment should be made because we accepted our PR19 price control settlement in the round, and our SoC seeks a retrospective adjustment in this area. As this is a PR24 reconciliation, in our view, it is relevant for the PR24 determination. In addition, in focusing on the alleged retrospective nature of the adjustment, the CMA has not engaged with the substance of our argument, which is that: (i) our performance in this area has been significantly impacted by factors outside our control which could not have been anticipated at the time of the PR19 FD, namely the effects of the COVID-19 pandemic on NHH voids and the consequences of Ofwat's flawed retail market design; and that (ii) Ofwat has introduced a PR19 adjustment to reflect the impact of COVID-19 on PCC PCL performance, but has refused to make equivalent adjustments for NHH Voids. This inconsistent approach is not in keeping with the principles of best regulatory practice, and the CMA's PD does not engage with the evidence we have submitted on this issue.

Leakage

5.53 We support the CMA's provisional decision to adjust our leakage PCL to account for current performance and endorse the approach summarised at Table 9.4 of the CMA's PD to adjust SEW's baseline leakage PCL to reflect its 2024/25 outturn performance and introduce a glidepath to the 2029/30 PCL. We note that all parties, including Ofwat, agree that this represents the correct approach.

223 See SEW, March 2025, Statement of Case, Annex F, paragraphs 64 to 90 and SEW, March 2025, Statement of Case, Annex I.

224 CMA, October 2025, Provisional Determinations, Volume 3, Chapter 6, paragraph 6.340.

6 Allowed return

We welcome the CMA's willingness to take a fresh look at the Cost of Capital calculation, resulting in an increase in the Cost of Equity from 5.10% to 5.90%.

However, in the Final Report we encourage the CMA to: (i) revisit the CAPM assessment, and base the RFR estimate solely on index-linked gilts, use a measure of the ERP which is consistent with the chosen RFR estimate, and select a beta estimate which reflects the increase in investor perceptions of sector-specific risk since PR19; (ii) revise its estimate of the future CPIH inflation to 2.1% to be consistent with the OBR's latest five-year economic forecasts; (iii) reconsider the approaches to calculating the cost of debt, which include technical flaws and risk understating the allowance; and (iv) take into account the financial loss to our shareholders resulting from not allowing a CSA to our cost of embedded debt, when considering the overall balance of the price control.

Overview

6.1 The return on capital is an important component of the CMA's determination. Our ability to deliver such a large investment programme – and the improvements that our customers demand – requires us to maintain ongoing access to investor capital at a cost that reflects the risk of the investment. The allowed return is not the only factor that determines whether investors will make finance available to us, but it does play a crucial role in shaping investors' view of the attractiveness of our business in the short, medium and long term.

6.2 We appreciate the new analysis that the CMA has provided in the PD. The scope that there is within the Redetermination process for the CMA to bring a 'fresh pair of eyes' to the calculation of the cost of capital has long been an important safety net of the water industry's redetermination regime and we look forward to the CMA's final assessment in the forthcoming Final Report. Our overall assessment of Chapter 7 of the PD is that the CMA has taken a number of positive steps towards meeting investors' requirements. However, we think that there are two important areas in which the CMA needs to make adjustments to its calculations if it is to make good on its stated intention of ensuring that *"debt and equity investors are appropriately remunerated for the risks of providing capital to the regulated businesses"*.[225] They concern:

(a) the precise calibration of the allowed return on equity; and

(b) the allowance within the cost of debt calculation for inflation of the RCV.

Allowed return on equity – top-down assessment

6.3 We support the way in which the PD looks at the required return on equity primarily through a 'top-down' lens. Investors ultimately have a choice about which companies and which industries they invest in. They look at the returns on offer, and they channel capital to investments that offer the best balance of risk and reward. It follows that, if investors are to positively choose to put money into our industry rather than alternative investment opportunities, the CMA's Final Report must put companies in a position where returns in the water industry are competitive next to risk adjusted returns that can currently be obtained elsewhere.

[225] CMA, October 2025, Provisional Determinations, Volume 4, Chapter 7, paragraph 7.2.

6.4 In our SoC, we looked at Ofwat's PR24 FD return on equity next to the observable rates of return that an investor can obtain from other assets and showed that the return allowed by Ofwat was inadequate.[226] Table 6.1 provides the same kind of benchmarking for the CMA's proposed return.

Table 6.1: Comparison of the CMA's proposed return on equity with observable returns on government and corporate bonds

	Yield/return[227]
20-year UK gilts	5.6%
10+ year A rated corporate bonds	6.0%
10+ year BBB rated corporate bonds	6.4%
Yields on Anglian Water, Northumbrian Water, Wessex Water 20-year bonds	6.7%
CMA PD return on equity	CPIH + 5.9%[228]

6.5 The table shows that, as of September 2025 (i.e. the CMA's proposed reference month for its Final Report), the PD offers a return that is approximately 2.5 percentage points above the yield on government bonds and around 1.5 percentage points above the yields on high quality corporate bonds.

6.6 As stated in our SoC,[229] by far the most useful way for the CMA to frame the question it has to answer in this part of the price review is to self-assess: is this level of reward sufficient to cause me to choose to put my money into water company shares given the level of risk-adjusted return available elsewhere?

6.7 Our view is that, while the PD rate of return is more attractive than Ofwat's manifestly inadequate FD rate of return, the offered return remains very tight against the kind of rewards that investors can currently obtain elsewhere, while taking on significantly less risk. In saying this, we accept that there is no single right way of establishing what the appropriate premium over gilt rates or the necessary gap between the cost of debt and the CoE ought to be. However, our strong sense, based on the extensive discussions that we have had with investors over the last 24 to 36 months, is that a return of CPIH + 5.9% offers an inadequately thin layer of reward for the cost, performance, capital delivery, political, regulatory, and reputational risks that investors are being asked to take on when putting money as equity into water companies. This is particularly true at a time when such a significant amount of capital is being sought to deliver customer outcomes across the sector.

6.8 We welcome in this regard the CMA's analysis of the cost of debt compared to the unlevered cost of equity. The cost of equity in the PD is within a handful of basis points of the cost of debt on an unlevered basis, with the lower end of the PD range *below* the cost of debt. This corroborates our view that the gap between cost of debt and cost of equity is too tight based on the PD.

6.9 In this context, we consider that the CMA has been too quick in its PD to dismiss points of reference or cross-checks that offer assistance when attempting to triangulate the required 'risk premium' into a logical place. We consider that it is possible for the CMA to take a useful directional signal from the evidence in the round. In particular, our reading is that:

226 SEW, March 2025, Statement of Case, Table 6.1.
227 See Bank of England UK Gilt Data: here and S&P Global IHS Markit: here.
228 Equivalent to an all-in return worth a little over 8% in nominal terms.
229 SEW, March 2025, Statement of Case, paragraph 6.8.

(a) Frontier Economics' work on hybrid bonds provides a helpful 'ready reckoner' indication of the extra return that investors require when asked to take on additional equity-like risks; and

(b) there is unambiguous informational value in evidence that investors can currently obtain returns of >10% from listed infrastructure funds.[230]

6.10 We ask the CMA to keep this evidence 'front of mind' as it prepares its Final Report.

6.11 The CMA can also take a strong directional signal by examining the sentiment currently facing the sector. We highlighted in our SoC multiple reports that documented a heightened risk arising from the scale of the industry's investment programme and a loss of confidence in the regulatory regime, in particular. This body of evidence has grown still further since March 2025. We draw the CMA's attention, in particular, to:

(a) Moody's[231] and S&P's[232] decisions to downgrade the predictability and stability of the regulatory regime;

(b) the large swing towards "unfavourable" ratings for the UK water industry in the Global Infrastructure Investor Association's quarterly surveys of investor sentiment;[233]

(c) Oxera's 2024 finding from a survey of investors that perceptions of the overall risk level in the water sector are markedly higher than in previous periods;[234]

(d) Barclays' 2025 finding from a survey of investors that UK water is now regarded as the riskiest utility sector in Europe;[235]

(e) the National Audit Office's (**NAO**) report on water industry regulation, which noted that "*the regulatory framework has contributed to worsening investor perception of the sector*";[236]

(f) the IWC, which highlighted in its final report that: "*The Commission has heard that Ofwat's approach in recent years has had a significant adverse impact on investor returns and investors' assessment of the risks they bear in the water sector*";[237] and

(g) the clear widening of credit spreads in the sector and the CMA's provisional decision to set the water industry's allowed cost of debt 30 basis points above iBoxx benchmarks.[238]

6.12 Stepping back and looking at this evidence alongside the benchmarking in Table 6.1, our view is that a return of CPIH + 5.9% per annum, equivalent to an all-in return worth a little over 8% in nominal terms, is too low. One of our main requests of the CMA ahead of its Final Report, therefore, is that the CMA provide for a further upward adjustment to the allowed return as part of a deliberate effort to ensure that the flow of capital into the sector is not impeded.

Allowed return on equity – CAPM analysis

6.13 The CMA's calculation of the allowed return is ultimately presented in terms of values for the risk-free rate (**RFR**), the Total Market Return (**TMR**) and beta. A key question we ask the CMA to reflect on as it assembles its Final Report is: why is it that the mid-point CoE estimate that emerges from analysis of the CAPM parameters is out of line with the top-down view of the required return?

230 Ofgem, July 2025, RIIO-3 Draft Determinations - Finance Annex, page 65, paragraph 3.97.
231 Moody's, November 2024, Reduced predictability of regulatory environment pressures credit quality
232 S&P, February 2025, U.K. Water Regulatory Framework Support, Low Financial Flexibility In Coming Regulatory Period Drive Rating Actions.
233 Global Infrastructure Investment Association, December 2024, Infrastructure Pulse Survey
234 Oxera, October 2024, PR24 Investor Engagement Report.
235 Barclays, November 2024, Rating agencies and investor survey: All about contagion.
236 NAO, April 2025, Regulating for Investment and Outcomes in the Water Sector, page 11, paragraph 24.
237 Independent Water Commission, July 2025, Final Report.
238 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 7, Figures 7.16 and 7.17,

6.14 Our assessment is that the CMA has given too much weight in its PD to low-end values of each of the RFR, the TMR and beta, skewing its CAPM range unnaturally downwards.

Risk-free rate

6.15 In the case of the RFR, we note that the CMA in its PR19 Redeterminations was careful to allow for the 'specialness' of index-linked gilts (**ILGs**). The CMA noted, in particular, that "*analysis of the current and historic yields associated with [ILGs] demonstrates that the government can borrow at rates significantly lower than would be accessible by even the highest-rated private investor*".[239] This led the PR19 CMA panel to take reference from a basket of proxies for the riskless asset rather than place sole reliance on readings of ILG yields.

6.16 We are surprised that the PD signals a different conclusion in this area and points to an ILG-only proxy for the riskless asset. In part, this change of position looks to be because the CMA has erroneously concluded that the different proxies for the riskless asset are all currently pointing to the same sort of RFR numbers (see paragraphs 6.31 to 6.35 for a discussion of the worth of CPIH inflation). More fundamentally, it is because the CMA has departed from the important point of principle it established in the PR19 Redeterminations when it said that: "*ILGs do not completely meet our requirement of the RFR as applied in CAPM*".[240]

TMR

6.17 In the case of TMR, we are pleased that the CMA responded to the request that we made in our SoC when we asked it to consider the consequences of using only an average TMR at a point in time when interest rates are expected to be 'higher-for-longer'. We do have concerns, however, that both the lower bound (6.7%) and the upper bound (7.3%) in the PD TMR range have been under-estimated.

6.18 At the lower bound, the PD states that historical ex-ante expectations of UK stock market returns looking over a 124-year period have averaged 6.7% in CPIH real terms. This estimate is lower than the figures that we have seen other regulators and experts quote, as set out in table 6.2 below.

Table 6.2: Estimate of the historical ex-ante TMR

Report	Return
Ofwat, PR24 FD (December 2024)	6.68% to 6.91%
Ofgem RIIO-3 DD (July 2025)	6.79%
KPMG, PR24 (March 2025)	6.68% to 6.82%
Kairos, PR24 (March 2025)	6.85% to 6.92%

6.19 At the upper bound, we are concerned that the CMA may have inadvertently made a 'pick'n'mix' error when combining its estimate of the historical equity-risk premium (**ERP**) with the current, forward-looking RFR.

6.20 There are a range of possible proxies for the riskless asset which can give either lower or higher readings of the RFR. Putting to one side for a moment the concerns that we raise above about the CMA's choice of reference instrument, there must, as a matter of fundamental principle, be an internal consistency between (i) the measure of risk-free return that the CMA wishes to add its calculated ERP to, and (ii) the measure of risk-free return that the CMA uses when computing the historical ERP.

6.21 This is not the case in the PD:

239 CMA, 17 March 2021, PR19 Final Report, paragraph 9.92.
240 CMA, 17 March 2021, PR19 Final Report, paragraph 9.104.

(a) The PD forward-looking RFR, as mentioned above, is the current yield on 20-year ILGs.

(b) The PD ERP calculation measures the premium that stock market investors have typically enjoyed relative to a bond index compiled by Dimson, Marsh and Staunton (**DMS**). The DMS index measures the returns on –

(i) UK government consols/perpetual bonds (1900 to 1954); and

(ii) high-coupon, long-dated conventional government bonds with a mean maturity of 20 years (1955 onwards).

6.22 The mismatch between (a) and (b) here matters because index-linked and conventional gilts of the same maturity have for many years offered markedly different expected returns.[241] The consequence this has is that:

(a) when the CMA computes TMR in the PD, it adds current ILG yields of 2.5% and its historical ERP of 4.8% to give an expected market return of 7.3% per annum; whereas

(b) had the CMA started with the current yield on 20-year conventional gilts of 5.3% (as at June 2025) and added its ERP of 4.8%, it would have obtained a TMR of 10.1% in nominal terms, equivalent to ~8% per annum in real CPIH-stripped terms.

6.23 In this case, the second of these calculations would be more appropriate. If the CMA wishes to measure the ERP versus 20-year conventional gilt yields, it is incumbent on the CMA to add its ERP looking forward to current 20-year conventional gilt yields. Any other approach creates a 'pick'n'mix' error and results in a misstatement of the prevailing TMR.

Beta

6.24 Finally, in the case of beta, we support the CMA's decision to bring Pennon into its comparator set and agree that Ofwat's refusal to take any information from Pennon's beta was an error. We also support the CMA's use of a 3-year spot beta as a pragmatic way of using the available data in the particular circumstances of this review.

6.25 We do not, however, agree with the lower bound of the CMA's beta range. An unlevered beta of 0.28 compares to the CMA's PR19 unlevered beta of 0.29. The CMA is therefore saying in its PD that it gives 50% weight to a view that investors' perceptions of the relative riskiness of water companies have changed in a favourable way during the last five years. The CMA will be able to see for itself that this is not credible. By any reading of the body of evidence that we cite in paragraph 6.11 above, risks to investor capital have increased since PR19 and the PR24 beta must logically be higher than the PR19 beta.

6.26 Inherently, the CMA's reliance on 10-year betas at the lower end of the range places less weight on forward-looking risk, which is better captured in more recent data. Its inclusion without adjustment to capture changes in risk facing the sector introduces a systematic downwards bias to the PD beta range.

Allowed return on equity – CAPM conclusions

6.27 Taking all of the preceding points made in paragraphs 6.13 to 6.26 together, we do not think that the lower bound of the CMA's CAPM CoE calculation is a plausible estimate of required return. This, in turn, means that the CMA's mid-point CAPM CoE calculation is not, as intended, a true central case cost of capital figure.

6.28 We appreciate the pragmatism that the CMA has shown in the PD 'aiming up' from the mid-point of its range. However, we ask that the CMA reflects ahead of its Final Report on the discussion in paragraphs 7.547 to 7.552 of the PD. The CMA is clear that "*a modest degree of aiming up on*

[241] Competition Commission, 2014, Northern Ireland Electricity Limited Final Price Determination, paragraph 13.117, Figures 13.3 and 13.4.

the cost of equity may overall be beneficial to customers".[242] This is because aiming up will "*reduce the risk of the sector being unable to attract new capital to finance the large-scale capital programme needed to deliver improvements in service and resilience*" which is "*ultimately in customer interests*".[243]

6.29 We submit to the CMA that it has not, in fact, protected customers in the way that it considers it has. The 'aiming up' in the PD serves only to neutralise the positioning of the lower bounds in each of the RFR, TMR and beta ranges and, hence, to paper over the consequent miscalibration of the calculated mid-point of the CAPM range. In order to build in a genuine safeguard against inadvertent under-estimation of the required return, the 'aiming up' in the FD needs to be an 'aim up' relative to a properly balanced cost of equity calculation.

6.30 In our assessment, this means aiming up from 5.9% and providing for an allowed return on equity that begins with a 6.

Allowed cost of debt

6.31 The CMA's provisional calculation of the allowed cost of debt contains only a small number of modifications to Ofwat's calculation of water companies' current and forecast interest costs. However, the CMA does make a significant change to the established consensus approach that the CMA and regulators have hitherto used when converting nominal, all-in interest rates into a real cost of debt allowance.

6.32 Along with the other Disputing Companies, we asked John Earwaker at First Economics for his views on this matter, as someone who has written extensively over a period of many years about regulators' treatment of inflation. In a short paper which we are submitting together with this Response,[244] he advises that:

(a) it is right for the CMA to consider afresh as part of this Redetermination the value that investors will place on the worth of the H in CPIH inflation indexation;

(b) there is reason to think that the housing costs will escalate more quickly than other prices in the economy, principally because of the feed-through that one would expect there to be over the long term between (above-inflation) wage growth and nationwide house prices;

(c) expectations as regards future earnings growth and future house price increases are, however, inextricably linked to expectations around economy-wide productivity growth;

(d) as the CMA itself notes in chapter 4 of the PD, the OBR has a track record of being over-optimistic about the speed with which the UK will overcome the factors that have been weighing down on productivity growth since the global financial crisis.[245] In this context, the high likelihood is that investors will currently place only very limited weight on the OBR's long-term "assumptions" about a return to strong productivity growth in the 2030s and 2040s;

(e) the CMA should, as a result, show similar caution when looking at the OBR's illustrative October 2024 "long run" CPIH inflation "estimate" of 2.4%; and, as such

(f) the best available anchor for the current outlook for productivity, earnings, house prices, and the resulting conversion that there will be from 2% CPI inflation into an equivalent rate of CPIH inflation, is the OBR's latest five-year CPIH inflation forecast, and particularly the 'exit rate' for CPIH inflation as at the final year (i.e. year 5) in the OBR's published outlook.

242 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 7, paragraph 7.577.
243 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 7, paragraph 7.577.
244 First Economics, October 2025, CPIH Inflation.
245 CMA, October 2025, Provisional Determinations, Volume 4, Chapter, 1, paragraph 4.173.

6.33 We agree with this assessment. The OBR's latest five-year forecast, published in March 2025, *before* the mooted downgrade in the OBR's assessment of the UK economy's productivity potential, contains the following forecasts of CPI and CPIH inflation.

Table 6.3: OBR forecasts of inflation

	CPI	CPIH
2027/28	2.0%	2.1%
2028/29	2.0%	2.0%
2029/30	2.0%	2.1%

6.34 These forecasts corroborate the view that it might be necessary to forecast inflation of RCV indexation in excess of 2.0% per annum. However, they fall well short of justifying a switch to a 2.4% CPIH inflation forecast.

6.35 In this context, our recommendation to the CMA, in line with the conclusions in John Earwaker's paper, is that the maximum admissible CPIH inflation at the current point in time is 2.1% per annum.

6.36 When the CMA comes to update its PD cost of debt calculation, we ask it to consider the following additional issues.

6.37 On the cost of embedded debt, we welcome detailed engagement with company debt books and expected costs across AMP8. However, we are concerned that the CMA places weight on the actual notional approach, which overlays the notional debt mix to the sector-wide debt book. While the CMA justifies this approach on the basis that it makes the allowance more reflective of the costs of a notionally efficient company, it introduces distortions and excludes floating rate debt which is a standard part of financing across the sector.[246]

6.38 SEW's costs based on the actual notional approach are implausibly different to SEW's all-in costs.[247] This is reflected in the results for other companies, such as United Utilities.[248] For us, this is clearly driven by the actual-notional approach not capturing that a significant proportion of our index-linked debt was issued before the global financial crisis, when rates were higher. As the actual-notional approach does not control for when debt was issued but simply superimposes the notional debt mix, it can lead to significant distortions that have nothing to do with efficiency. We strongly encourage the CMA to attach no weight to this imperfect cross check.

6.39 We welcome the movement that the CMA has made on the liquidity allowance provided for as part of the additional borrowing costs allowance. However, the CMA appears to have departed from its view in other parts of the PD that the most recent data is the most reflective of future rates. In particular, the PD has adopted a three year averaging period in setting the cost of holding cash.[249] Applying a 1-month averaging approach – consistent with RFR and the cost of new debt – and updating the benchmark adjustment to 45bps (as above), drives an 8bps uplift on the liquidity allowance.[250] We urge the CMA to consider this targeted amendment to the cost of holding cash assumption in light of current market data.

246 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 7, paragraph 7.609.
247 CMA, Supporting workbook for the cost of embedded debt: "PR24 CMA PD – CoD – embedded debt, share", <Notionalised analysis>.
248 CMA, Supporting workbook for the cost of embedded debt: "PR24 CMA PD – CoD – embedded debt, share", <Notionalised analysis>.
249 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 7, paragraph 7.727 (b).
250 KPMG, November 2025, Analysis of WACC in the PR24 Provisional Determinations, paragraph 7.1.10.

Company-specific adjustment to the cost of debt

6.40 Our SoC requested that the CMA provide a company-specific adjustment (**CSA**) to our cost of debt to reflect the greater point in time risk that we have historically faced as a relatively infrequent issuer of debt. We welcome the CMA's acknowledgement of our different circumstances and the CMA's finding that "*South East has faced greater point-in-time risk at the times that it has needed to raise debt finance*".[251] However, we are disappointed that the CMA has not translated this into any form of allowance for our higher interest costs.

6.41 We have a number of concerns with the CMA's reasoning for not doing so in the PD. We note in particular, that:

(a) The CMA treats Ofwat's one-size-fits-all approach to setting companies' cost of debt allowances as fixed[252] and opts not to consider the inherent drawbacks that there are in a methodology that exposes infrequent issuers like us to greater risk of cost of debt out- and under-performance.

(b) The CMA considers that there is no need for a CSA as we did not receive one at PR19, and the cost of embedded debt allowance takes into account our costs.[253] However, we have consistently submitted evidence supporting a CSA since PR99. We received an uplift to the cost of equity in PR99 and PR04[254] to reflect SEW's position as a small company and a CSA on cost of debt in PR09.[255] We also requested a CSA to reflect our smaller company characteristics in PR14,[256] PR19,[257] and PR24.[258]

(c) The CMA finds a median issuance size in the sector of around £60 million, and a mean issuance size of around £130 million based on post 2011 debt issuance.[259] However, it is unclear why the CMA's analysis omits debt issuances before 2011. The CMA's analysis on an instrument level is distorted by the inclusion of lease instruments, and its analysis of the average issuance size does not accurately account for (i) cases where one issuance is split into multiple tranches; and (ii) tap issuances.[260]

(d) There is no basis for the CMA to dismiss the higher point in time risk that we have faced as diversifiable in nature, given that the underlying source of the risk is the uncertain profile of the interest rate cycle – i.e. a key part of the systematic risks faced by all global equity investors. It is not clear whether it is possible in practice to construct a portfolio to fully diversify the risk associated with the issuance profile of an infrequent issuer.[261] Even if the CMA considers that some proportion of our higher risk can be diversified, it is not plausible to assume that our higher risk profile has no systematic component.

6.42 In light of the above, and our previous submissions on this issue, we ask the CMA to be cognisant, when evaluating the 'in the round' balance in our price control, of the financial loss to our shareholders resulting from not allowing a CSA to our cost of embedded debt.

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251 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 7, paragraph 7.776.
252 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 7, paragraph 7.775.
253 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 7, paragraph 7.771
254 Ofwat, 1999, Future water and sewerage charges 2000-05 Final Determinations, Section 10.3.5 and Ofwat, 2004, Ofwat - Future water and sewerage charges 2005-10 Final Determinations, page 59.
255 Ofwat, 2009, Ofwat - Future water and sewerage charges 2010-15 Final Determinations, page 132.
256 Ofwat, 2014, Setting price controls for 2015-20 Final price control determination notice: company-specific appendix – South East Water, Table A2.7.
257 SEW, 2020, PR19 CMA Submission, page 25, and SEW, 2021, CMA Cost of Capital Consultation Response, Section 3.2.
258 SEW, 2024, PR24 Draft Determinations Response, page 28.
259 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 7, paragraph 7.774 (a).
260 Adjusting bond data for these factors results in a mean bond issuance size of £140m in the period from 2006 to 2011 (median of £100m), and a mean bond issuance size of £345m in the period from 2011 to 2025 (median of £250m). These metrics are broadly in line with the time varying iBoxx benchmark size thresholds used in the KPMG analysis.
261 We explained this further in our written response to hearings, see: South East Water – Written Response to PR24 Hearings, paragraph 16.

7 Risk and financeability

The CMA has rightly recognised that the sector faces higher risk in AMP8 but the PD does not take sufficient steps to ensure that its cost allowances, outcome targets and allowed return result in a 'fair bet'. Indeed, the CMA's risk and financeability analysis includes errors which lead to understating a significant downside risk for a notional company operating in our region, which is inconsistent with maintaining financial resilience.

The CMA should seek to remedy these risks by correcting the clear error in the CMA's assessment of 'what base buys', providing base and enhancement costs allowances and an outcomes package in line with our SoC, and providing an allowed return on equity that is competitive and an allowance for the real cost of debt that is based on a conservative/realistic central case allowance for long-term CPIH inflation.

7.1 We welcome the CMA's recognition that the sector faces higher risk in AMP8 and that this has informed its approach to returns, risk allocation, and financeability at both the sector and company level.

7.2 A key failing of Ofwat's PR24 FD was the precarious overall position that Ofwat put us in – resulting in a need for everything to 'go right' in AMP8 for us to deliver for our customers.

7.3 The preceding chapters of this Response have highlighted that the CMA has taken meaningful steps in its PD to create a more balanced price control package. However, there remains work to do:

(a) we still see an expected return for the next five years that falls short of the regulated allowed return. This is due in part to the shortfalls identified in Sections 2, 3 and 6, but also due to the structural asymmetry that the CMA has acknowledged there is in the ODI package;

(b) projected credit metrics are either extremely tight against or below the thresholds that rating agencies have said are required for a Baa1/BBB+ credit rating, giving us very little capacity to absorb downside risks;

(c) we are concerned that the CMA has not modelled downside scenarios which are consistent with the heightened risk environment in which we are operating. We urge the CMA to consider more severe downside scenarios in line with operational downsides companies test in their Long Term Viability Statements, which are typically equivalent to at least 3% RoRE; and, as a consequence

(d) the CMA has not yet got to a position where it can safely say that its determination would be 'investable', in the sense that any rational investor would positively choose to provide the equity that we require in order to finance the programme of work that we have been tasked with.

7.4 We elaborate on these points below.

Assessment of risk implied by the PD for SEW

7.5 We welcome the CMA's recognition that the sector faces higher risk in AMP8 and that this has informed its approach to returns, risk allocation, and financeability at both the sector and company level. We nevertheless have several concerns with the CMA's overall risk assessment, as set out in Chapter 9 of the PD. In particular, in contrast with the CMA's assessment, our

analysis indicates that the PD does not constitute a 'fair bet'. Specifically, we consider that there remains a negative skew across the price control package and an excessive amount of downside risk.

Negative skew

7.6 The CMA concludes that the overall PD package is broadly balanced on the basis that a negative skew in the Ofwat outcomes package is offset by positive skew in potential future financing performance. In particular, the CMA concludes there is a small positive skew on inflation based on the modelling approaches applied by Ofwat.[262] However, our analysis indicates that based on the regulatory mechanism prescribed in the PDs, we remain exposed to negative skew across both outcomes and financing performance.

Outcomes

7.7 On outcomes, the CMA's conclusion that the outcomes package is negatively skewed is consistent with the risk analysis submitted by both Ofwat and the Disputing Companies to the CMA at SoC stage, which estimated a negative skew on ODIs of c.20bps. However, we have significant concerns with the CMA's approach at PDs to the risk implications of ODIs and the provisional conclusions it draws.

7.8 In particular, we are concerned that the PD proposed WSI PCL does not fully reflect our network characteristics and limited operational headroom across AMP8, which will have a material impact on our ability to manage WSI until we have implemented our enhancement programme. Using the DDR WSI PCL in the PD represents a target that is too stretching and exposes us to a significant level of downside risk.

7.9 The CMA recognises our company-specific characteristics – including limited operational headroom and network interconnectivity – as factors outside of our control which are driving WSI performance, and that these structural constraints need to be addressed through enhancement investment to support convergence with the common PCL over AMP8. We need time to implement the enhancement investments that our business needs, and we won't see benefits until year five in many cases. By setting a PCL that anticipates benefit realisation ahead of physical completion, the PD sets the WSI PCL at a level that is unachievable. Additionally, extreme weather is a key driver of negative skew on ODIs more broadly. We welcome the CMA's recognition that different geographical regions are likely to be impacted differently by climate change with reference to Met Office data.[263] However, we are concerned that the CMA implicitly assumes that the extreme weather events observed in AMP7 were stochastic outliers and that weather pattern will revert to long-term historical mean. As set out in Section 5 of this Response, this assumption is not supported by empirical evidence.

Financing

7.10 The CMA concludes that the overall PD package is broadly balanced on the basis that the negative skew on ODIs is offset by positive skew on financing performance. In particular, the PD concludes there is a small positive skew on inflation based on the modelling approaches applied by Ofwat.[264]

7.11 We do not agree that there is this natural offset. The CMA's analysis of inflation risk is based on the distribution of possible out-turn inflation outcomes that Ofwat identified around a 2.0% long-term CPIH inflation assumption.[265] The CMA finds in its PD that it is appropriate to make a small upward adjustment to this 2.0% allowance (we discuss the precise scale of this adjustment in Section 6 above). It should be straight-forward to see at this point that it is not tenable for the CMA to assume that Ofwat's upside-downside distribution of inflation risk can be placed unchanged around its new, higher central case inflation forecast.

262 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 8, paragraph 8.95.
263 CMA, October 2025, Provisional Determinations, Volume 2, Chapter 5, paragraph 5.223 to 5.224.
264 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 8, paragraph 8.120.
265 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 8, paragraph 8.107.

7.12 This is particularly the case given that, whilst the midpoint implied by Ofwat's analysis is positive, the P50 is negative. The median is a more appropriate measure of central tendency for inflation as the midpoint does not capture the impact of skew, which is present in the inflation dataset. We refer the CMA to the detailed discussion of this point in the KPMG Industry Risk Report, submitted with our SoC.[266]

7.13 The table below updates Ofwat's analysis of financing risk to reflect the CMA's specific treatment of inflation. The result demonstrates that the financing package exhibits a material negative skew when either the CMA's 2.4% long-term CPIH assumption or our preferred 2.1% inflation assumption is applied.

Table 7.1: RoRE impact of inflation calibration[267]

	P50	Mid-point
2.4% long-term inflation	-55 bps	-20 bps
2.1% long-term inflation	-25 bps	+10 bps
2.0% long-term inflation	-15 bps	+20 bps

7.14 The CMA cannot therefore assume that the PD package is broadly balanced, because expected structural under-performance on ODIs is not balanced by an equal and offsetting likelihood of inflation out-performance.

Excessive downside risk

7.15 One of the stand-out features of Ofwat's PR24 methodology is the sheer amount of downside risk to which Ofwat has sought to expose companies and their shareholders.

7.16 The CMA will have noted that this was one of the key themes in Sir John Cunliffe's IWC report. The IWC noted that "*long-term investors have been clear that, at current risk levels, the sector is not attractive and will struggle to attract the finance needed from such investor*s".[268] This led the IWC to make the following recommendation: "*to support the attractiveness of the sector as a whole to long-term, low-risk, low-return investors, it has to present a lower risk profile than has been the case in recent years*".[269]

7.17 We had expected that the CMA would give consideration to the available remedies for this problem as part of the redetermination process. Ofwat's own analysis at FD showed that a P10:P90 range for the RoRE for an efficient company is -5.4% to + 5.5% and the CMA's PD interventions in costs and outcomes bring only a very marginal change to the width of this range (specifically due to the lowering of the ODI rate on pollution incidents). Contrary to our expectations, however, the CMA pays this matter almost no attention, with the CMA focusing its analysis of risk almost exclusively on the question of whether potential upsides and potential for downside are balanced and neglecting to ask whether the scale of the risks that companies are exposed to is excessive.

7.18 We hope that the CMA will be able to give this matter proper scrutiny ahead of its Final Report and reflect, in particular, on the consequences that our very high-risk exposure has for the calibration of each of the cost, outcome and financial building blocks in the final price control package.

266 KPMG, March 2025, PR24 Final Determinations – Risk Analysis for a Notional Company, page 20.
267 Source: KPMG, November 2025, Analysis of and commentary on risk and financeability in PR24 Provisional Determinations.
268 Independent Water Commission, July 2025, Final Report, paragraph 753.
269 Independent Water Commission, July 2025, Final Report, paragraph 753.

Financeability and financial resilience

7.19 A financeability assessment provides a holistic cross-check that an efficient water company can reasonably expect to finance itself at the allowed cost of capital, by achieving a Baa1/BBB+ target credit rating at the notional financing structure, and to maintain investment grade credit rating under plausible downside scenarios.

7.20 We note that the CMA's PR24 PD contains a noticeable down-weighting of the financeability testing in comparison to the prominence that the CMA's PR19 panel gave to this part of the decision-making process five-years ago. The PR19 Redetermination considered financeability analysis as a *"valuable cross-check on the point estimate for the cost of equity"* and a tool to assess the impact on credit ratings of companies' ability to achieve cost and outcome targets, including companies' financial resilience to a "*reasonable downside in operational performance*".[270] The CMA highlighted the importance of considering financeability in the context of ensuring "*that a company is able to finance the proper carrying out of its functions (in particular, by ensuring reasonable returns on its capital)*".[271]

7.21 We welcome that the PD does still contain assessment of financeability and financial resilience. However, we would like to see this work play a more central role during the formulation of the CMA's Final Report as strong credit ratings are fundamental to attracting the finance to deliver the large investment programme that our customers demand.

7.22 In this context, we have two particular concerns about the specification of the CMA analysis.

The CMA assessment of financeability rests on rating thresholds which would not apply to the notional company

7.23 We note, first of all, that the CMA has applied the wrong rating thresholds in its financeability assessment. In particular, it has:

(a) specified incorrect credit rating thresholds for the S&P FFO/net debt ratio;

(b) specified incorrect credit rating thresholds for the Fitch cash PMICR; and

(c) failed to include in the assessment the Fitch cash PMICR.

7.24 Specifically, the CMA has relied on thresholds that would be applicable only to senior secured debt issued by companies with Whole Business Securitisation (**WBS**) structures. This is inconsistent with Ofwat's positioning on the notional company and the concerns that it has raised with regard to the use of highly covenanted arrangements – for example, as set out in its 2021 discussion paper on financial resilience in the water sector.[272]

7.25 On the S&P FFO/net debt ratio, the PD cites a target of 10% but notes that even 8-9% "*is likely to be consistent with a rating of Baa1/BBB+.*"[273] The CMA thus finds that its PD would be financeable despite all of the Disputing Companies except Southern Water having FFO/debt below 10%, indicating that it ultimately uses a threshold in the range of 8-9%. However, in reality, this level of FFO/net debt would be consistent with BBB+ only for the highest-rated, senior secured tranche of debt at Affinity Water, Welsh Water and Yorkshire Water, which receive a one-notch uplift for their WBS structures (from 11% down to 8%).

7.26 We would not expect the notional company to be classified in the same way – i.e. having senior secured debt issued under a WBS structure – and so it is not appropriate to determine the price control as financeable at a Baa1/BBB+ rating on this basis. Instead, a higher rate of FFO/net debt of 11-13% would be required to achieve a BBB+ rating.

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270 CMA, 17 March 2021, PR19 Final Report, paragraph 10.73(d).
271 CMA, 17 March 2021, PR19 Final Report, paragraph 10.1.
272 Ofwat, 7 December 2021, Financial resilience in the water sector: a discussion paper.
273 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 8, paragraph 8.254.

7.27 Further, we find it difficult to reconcile the 8% FFO/net debt threshold used by CMA being looser than the 9% used by Ofwat in its FD. This is implausible, given that Ofwat's thresholds did not incorporate S&P's subsequent downgrade of the regulatory framework and resulting tightening of rating thresholds.[274]

7.28 On the Fitch cash PMICR assessment, the PD considered that 1.4-1.5x cash PMICR would be consistent with a BBB+ rating. Again, this threshold is applicable only to the senior secured debt of a WBS issuer, whereas the senior unsecured debt of a corporate-like water company with a cash PMICR in this range would be rated BBB and its Issuer Default Rating (**IDR**) would be BBB-. It is notable that Ofwat has consistently maintained that the relevant Fitch rating for assessing financial resilience is the IDR.[275]

7.29 While the PD discusses the appropriate threshold for the Fitch cash PMICR ratio,[276] it omits the threshold assessment from its financeability results, and it is not clear why it has chosen to do so. We find consideration of this threshold to be an important part of the financeability assessment. Fitch is one of the three main agencies rating water companies, with wider coverage of WaSCs and large WoCs (rating ten of twelve companies) than S&P (eight of twelve). As a result, its rating is directly relevant to assess water companies' compliance with the financial resilience licence provisions, and it is important for financeability to be tested with regard to its required outcomes.[277]

7.30 A comparison between Ofwat's FD, the CMA's PD and appropriate credit metrics thresholds is provided in the table below:

Table 7.2: Target thresholds assumed to be consistent with a Baa1/BBB+ rating

	Ofwat FD threshold	CMA PD threshold	Correct range for unsecured structure
Moody's AICR	1.6x	1.7x	1.6-1.8x (midpoint 1.7x)
S&P FFO/debt	9%	10% target, but 8-9% "still consistent" with BBB+	11-13% (midpoint 12%)
Fitch cash PMICR	n.a.	1.4x	1.7x-2.0x (midpoint 1.85x)

7.31 The CMA outcome for the financeability assessment rests on the assumption that the notional company can meet the cost and outcome targets and achieve neutral performance in the median-expected case. We have shown above that the risk implied by the PD is not balanced, and have aligned our approach to the commentary set out in the PD.[278] Our PD aligned risk analysis indicates the following risk ranges for a notional company operating in our regions:

Table 7.3: SEW notional risk ranges (PD aligned)[279]

Notional SEW	P10	P50	P90
Totex	-1.95%	-0.00%	1.94%
Retail	-0.30%	-0.00%	0.30%
Outcomes (incl. MeXes)	-2.18%	-0.67%	0.68%

274 S&P, February 2025, U.K. Water Regulatory Framework Support, Low Financial Flexibility In Coming Regulatory Period Drive Rating Actions.

275 Ofwat, July 2019, Conclusions on strengthening the regulatory ring-fencing framework, paragraph 2.6; Ofwat, July 2020, Conclusions on section 13 of the WIA91 on proposed modification to ring-fencing provisions, page 5.

276 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 8, paragraph 8.250 to 8.251.

277 South East Water consolidated instrument of appointment, updated to August 2025, page 30. Available at: South East Water Licence.

278 Further discussion of the updates to the approach to risk analysis is set out in: KPMG (November 2025), Analysis of and commentary on risk and financeability in PR24 Provisional Determinations.

279 Source: KPMG analysis.

Notional SEW	P10	P50	P90
Financing	-1.83%	-0.44%	0.91%
Revenue & other	-0.05%	-0.00%	0.01%
RoRE (simulated)	-4.04%	-1.19%	1.69%

7.32 Our updated risk analysis shows that a notional company operating in our region can expect underperformance of 1.19% RoRE from outcomes and financing based on the PD.

7.33 This translates into a Moody's AICR at Baa2, S&P FFO/net debt and Fitch PMICR marginally above or at BBB- rating. The risk imbalance in the PD exerts significant pressure on credit metrics for the notional company which are already extremely tight.

The downside scenario testing applied by the CMA is mis-specified and does not capture realistic downside exposure for SEW

7.34 The CMA has tested whether the notional company can maintain an investment grade credit rating by applying:

(a) **Scenario 1:** a downside scenario with underperformance equivalent to 1% RoRE in each year of the price control;

(b) **Scenario 2:** a downside scenario with underperformance equivalent to 1% RoRE in 3 years of the price control and 2% in the other 2 years, equating to approximately 1.4% on average.

7.35 We are surprised that the PD assumes that these sensitivities represent a severe but plausible downside. These scenarios fall well short of the risks which we consider could occur based on the PD, and are very modest when compared both to all sources of risk analysis submitted to the CMA as part of this process or average operational under-performance observed in the sector across AMP7 (4.2% RoRE). [280]

7.36 These scenarios are also not consistent with the approach used by companies in setting their long-term viability statements (**LTVS**). Companies are obliged by regulatory requirements to assess long-term viability and demonstrate they are financially resilient through stress testing, aligned with principles set by the Financial Reporting Council more broadly. In its guidance to companies,[281] Ofwat sets out that stress tests should cover "*…severe, plausible and reasonable scenarios for key variables, covering the principal risks facing the business in the short and longer term*". For the purpose of the financeability assessment, downside scenarios assessed by companies to support their long-term viability statements represent plausible, robust stress tests linked directly to principal risk exposure. Companies typically test downside scenarios equivalent to at least 3% RoRE as part of their LTVS.

Realistic downside scenarios show that downside risk exposure implied by the PD is excessive and that the notional company is not financially resilient

7.37 As shown in Table 7.4 below, the notional company may lose investment grade rating with one of the rating agencies in case of persistent underperformance at only -2% RoRE, a relatively conservative downside scenario if compared against companies' assessment of potential risks in their LTVS (where most water companies stress test viability against totex and ODI downsides at least 3% RoRE).

280 This could be arrived at through a combined ODI and totex scenario based on Table 7.3.
281 Ofwat, March 2018, Information Notice.

Table 7.4: Downside stress tests[282]

	Economic RoRE	Cash flow RoRE	AICR (Moody's)	FFO/Net debt (S&P)	Cash PMICR (Fitch)
AMP8 average metrics					
1% RoRE	-1.00%	-1.00%	1.57x	8.2%	1.57x
1% + 2% yr 2-3	-1.40%	-1.40%	1.49x	7.8%	1.49x
2% RoRE	-2.00%	-2.00%	1.37x	7.2%	1.37x
3% RoRE	-3.00%	-3.00%	1.18x	6.3%	1.18x
Severe downside	-4.04%	-5.20%	1.03x	5.4%	1.03x
Credit rating minimum thresholds					
Baa1/BBB+	NA		1.60x	11.0%	1.70x
Baa2/BBB	NA		1.40x	8.0%	1.50x
Baa3/BBB-	NA		1.20x	6.0%	1.40x

7.38 This picture has very significant implications on the notional company operating in our region's ability to secure financing at a cost compatible with the target credit rating. In a severe downside scenario, a notional company operating in our region would fall below investment grade thresholds with all three rating agencies. We find a very similar outcomes for a 3% RoRE scenario, which is an operational downside typically modelled in companies' LTVS assessments. Such outcomes mean that the notional company will likely face increasing financing costs on new debt issuances, at a level above the allowed cost of debt, with deteriorating performance on cost of financing as a result. This supports the conclusion that the notional company is not financially resilient based on the PD and that downside risk exposure under the PD is excessive and not in the interests of our customers.

Recent equity issuances do not provide evidence that the sector is investable

7.39 While there have been equity raises in the sector in recent years, many recent equity injections have been for the purpose of rescue capital and are not 'fresh' equity injections. We and Southern described, during the Risk and Return hearings, the significant challenges we faced in securing equity capital from existing shareholders. Our shareholders wrote to the CMA to clarify the difference between protecting an existing investment and injecting new equity into a new investable proposition and underlined that they would not have provided this capital if they did not already have an existing investment in the sector.

7.40 Recent equity injections should not be interpreted as evidence of investability for PR24 as these were largely aimed at capital restructuring or improving financial resilience. The PD has recognised that recent equity raises from SEW, Anglian and Southern relate to debt restructuring or financial resilience improvements. However, the PD has considered these as "*further evidence that investors are willing to commit new equity into the sector*".[283] Whilst these equity raises show commitment of existing shareholders, they do not constitute evidence that new investors are likely to commit capital based on an investment appraisal of the PD.

7.41 The delivery of the AMP8 programme requires that companies have continued access to financing from current, as well as new investors. A financial framework that is not sufficiently attractive for new capital may result in companies deprioritising capital investment to the detriment of the service improvements that our customers demand.

Our request to the CMA

7.42 In our SoC, we requested that the CMA should address the shortcomings in Ofwat's FD by making specific targeted amendments to the calculation of our allowed revenues, adjusting certain of our PCLs and ODIs, and amending the calibration of Ofwat's OAM and ASM. The CMA indicates in its PD that it is not necessary or appropriate for the CMA to make changes to

282 Source: KPMG analysis.
283 CMA, October 2025, Provisional Determinations, Volume 4, Chapter 8, paragraph 8.310.

established industry architecture, meaning that the OAM and ASM will be left as a low-probability safety net for extreme scenarios only. This makes it even more important that the CMA's Final Report takes the steps that are needed to centre its cost allowances, outcome targets and allowed return into a genuinely 'fair bet'.

7.43 To attain this position, it is essential that the CMA's Final Report provides for:

(a) a correction of the clear error in the CMA's assessment of 'what base buys';

(b) a base costs allowance in line with our SoC;

(c) an enhancement costs allowance in line with our SoC;

(d) an outcomes package in line with our SoC;

(e) an allowed return on equity that is competitive next to the returns that investors will be able to obtain from competing investments and alternative asset classes on a risk adjusted basis; and

(f) an allowance for the real cost of debt that is based on a conservative/realistic central case allowance for long-term CPIH inflation.

south east water