



# Price Control for Water and Sewerage Services 2021-2027

## Mid-Term Review Draft Determination

May 2024



## About the Utility Regulator

The Utility Regulator is the economic regulator for electricity, gas and water in Northern Ireland. We are the only multi-sectoral economic regulator in the UK covering both energy and water.

We are an independent non-ministerial Government Department and our main duty is to promote and protect the short- and long-term interests of consumers.

Our role is to make sure that the energy and water utility industries in Northern Ireland are regulated, and developed within ministerial policy, as set out in our statutory duties.

We are governed by a Board of Directors and are accountable to the Northern Ireland Assembly.

We are based at Queens House in Belfast. The Chief Executive and two Executive Directors lead teams in each of the main functional areas in the organisation: CEO Office; Price Controls, Networks and Energy Futures; and Markets and Consumer Protection.



### Our mission

To protect the short- and long-term interests of consumers of electricity, gas and water.



### Our vision

To ensure value and sustainability in energy and water.



### Our values

- Be a best practice regulator: transparent, consistent, proportionate, accountable and targeted.
- Be professional – listening, explaining and acting with integrity.
- Be a collaborative, co-operative and learning team.
- Be motivated and empowered to make a difference.



## Abstract

The Utility Regulator (UR) is the independent economic regulator for water and sewerage services in Northern Ireland (NI). Our primary role within the water industry is to protect the interests of consumers, both today and in the future.

PC21 is our current NI Water price control. It runs for the period 2021 to 2027. PC21 ensures the monopoly company - NI Water - who deliver our water and sewerage services, has enough revenue to operate an efficient business that delivers what Northern Ireland consumers need. We take account of the Department for Infrastructure's (DfI) Social and Environmental Guidance (S&EG) in coming to our PC21 decisions.

As part of PC21, we allowed NI Water an opportunity to clarify expenditure requirements for the price control period for costs which were uncertain when we set our PC21 Final Determination in 2021. This is called the Mid-Term Review (MTR). The purpose of today's draft determination is to set out our MTR provisional findings, following our assessment of NI Water's MTR submission.

We propose an increase in tariffs for non-domestic consumers, equivalent to 4.6% in each of the last two years of the price control period for an increase in power costs. We also propose a capital allowance equivalent to c£2.39bn in 'money of the day' prices (i.e. nominal) for the full price control. Some limited adjustments to output targets are also proposed.

We welcome responses to our consultation by noon on Thursday 27 June 2024.

## Audience

Principal stakeholders (i.e. Department for Infrastructure, Northern Ireland Water, Northern Ireland Environment Agency, Consumer Council for Northern Ireland, Drinking Water Inspectorate), consumers and their representatives.

## Consumer impact

This document sets out our PC21 Mid-Term Review Draft Determination findings. It explains the changes that we propose making to charges, our revised assessment of the capital funding required to deliver the established needs and the impact that the process has had on the outputs and delivery targets for PC21.



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# Foreword

The Utility Regulator (UR) is the independent economic regulator for water and sewerage services in Northern Ireland (NI). Our primary role within the water industry is to protect the interests of consumers, both today and in the future.

PC21 is our current NI Water price control. It ensures the monopoly company – NI Water - who deliver our water and wastewater services, has enough revenue to operate an efficient business that delivers what Northern Ireland consumers need.

Our PC21 Final Determination was published in May 2021 and covers the six-year period from 2021 to 2027. As part of this process, NI Water submitted a business plan to us detailing how it was going to meet the priorities set out in the Department for Infrastructure's (DfI) Social and Environmental Guidance (S&EG). This guidance recognised that continuing investment at previous levels would have a significant detrimental impact on the economy, the environment and the wellbeing of citizens.

In line with the S&EG, our PC21 Final Determination ensured value for money by allowing NI Water revenue to support a deliverable investment plan which was efficient and affordable from a tariff perspective. This was a positive development which the Utility Regulator continues to support.

PC21 also provided NI Water with a single opportunity to deal with material changes during the period 2021 to 2027, to address any uncertainty that existed at the time of the PC21 Final Determination. This is called the Mid-Term Review (MTR).

The purpose of this draft determination is to set out our MTR provisional findings for consultation, following our assessment of NI Water's MTR submission.

Our MTR proposes:

- Limited adjustments to output targets.
- An average tariff increase of 4.6% for non-domestic consumers in each of the last two years of the PC21 period to mitigate against an unprecedented increase in NI Water's power costs.
- A capital allowance of c£2.4bn in 'money of the day' prices (nominal) for the full price control period to maintain existing services and deliver the upgrades required to meet its quality, environmental and service level obligations.

Our MTR proposals remain consistent with the S&EG principles.

Whilst ongoing Government public expenditure constraints may affect the budget available to NI Water, the MTR does not take account of the potential impact, as we consider this to be a matter for NI Water and its shareholder, DfI.

We welcome all responses to our consultation by noon on Thursday 27 June 2024.

# Key Findings

## Operating Costs

We propose that NI Water should be allowed some additional revenue due to the significant increase in its power costs. We have allowed an increase of £54m compared to the PC21 Final Determination to cover the estimated variance in power costs for the final 3 years of the price control period. This adjustment results in an average tariff increase for non-domestic consumers (we call this a weighted annual average charge increase) which is equivalent to 4.6% for each of the final two years of PC21.

We found that all other types of revenues in NI Water's MTR submission largely balanced out. We therefore did not consider them in our MTR Draft Determination due to the immateriality of the net impact. This approach aligns with the established principle that the PC21 MTR should only reopen material issues and retain the integrity of the PC21 Final Determination as far as possible.

## Capital Investment

We propose a capital allowance of c£2.4bn in 'money of the day' prices (i.e. nominal prices) for the full price control period to maintain existing services and deliver the upgrades required to meet its quality, environmental and service level obligations. In terms of how we have arrived at this figure, we note that:

- The proposed capital allowance for the full price control period is £1.75bn in 2018-19 prices (i.e. the real terms price base for PC21 which allows costs to be compared on a consistent basis). This reflects the outcome of our assessment of the company's updated capital submission for wastewater and sewerage schemes and the inclusion of three 'change control'<sup>1</sup> projects required to meet water quality or supply resilience needs.
- However, inflation in PC21 has been much higher than assumed at the time of the PC21 Final Determination. We estimate that the nominal requirement for the period as a whole has increased from £2.1bn at the PC21 Final Determination to £2.4bn.
- NI Water requested an additional £0.28bn of Real Price Effects (i.e. cost pressures above inflation) as part of its MTR submission. However, we have not seen sufficient evidence to justify its claim, as our analysis indicates that inflation should provide sufficient cover for water sector cost rises. So, we have excluded NI Water's Real Price Effect. This represents the majority of

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<sup>1</sup> The Change Control Protocol allows for new projects to be added to a price control after the final determination if a critical need arises and stakeholders agree that it is necessary. Further details can be found in [Annex M](#) of the PC21 Final Determination.

the difference between our proposal of £2.4bn nominal and the nominal figure of £2.75bn submitted by NI Water.

## **Outputs**

The changes made to outputs within the Mid-Term Review are limited. The targets for four wastewater and sewerage nominated outputs have been adjusted to account for NI Water's wholesale review of the solutions and costs for wastewater and sewerage schemes. This exercise has identified that costs have increased materially in general which is putting pressure on the delivery programme, that some schemes are no longer required and that further time is needed to investigate lower cost solutions in cases where costs have increased disproportionately. Targets for two consumer measures have been updated to reflect the outcome of a planned review by the Consumer Measure Satisfaction (CM/SAT) stakeholder group. Five development outputs have been closed following their completion and low pressure targets have been rebased to account for a comprehensive reassessment of low pressure issues undertaken by NI Water. Targets for a further two measures have been changed based on queries we originally raised in the PC21 determination process.

# 1. Introduction

## Regulatory Context

- 1.1 The Utility Regulator's (UR) primary role within the Northern Ireland water industry is to promote and protect the interests of the consumer, both today and in the future.
- 1.2 NI Water is a Government-owned company which is responsible for providing water and sewerage services to consumers in Northern Ireland. Since it is the sole provider of these services, the UR regulates the amount of revenue the company receives.
- 1.3 Our determination of the company's revenue requirement is undertaken through periodic price controls. These:
- Establish the funding required by NI Water to meet Departmental priorities for the price control period contained within its Social and Environmental Guidance;
  - Require NI Water to deliver enhanced regulatory outputs, continued investment, improvements in service and efficiencies; and,
  - Aim to ensure value for money for consumers and determine how much the company is allowed to charge.
- 1.4 The domestic consumer charge and the domestic allowance for commercial consumers is met by Government subsidy through public expenditure (PE) mechanisms. The remainder of the charge for non-domestic consumers is recovered through bills.
- 1.5 NI Water's reliance on Government funding for the majority of its revenues, means it is also classified as a non-departmental public body for public expenditure (PE) purposes. As a result, it is subject to the rules that govern PE and is required to operate within PE limits set by the NI Executive. Our regulatory processes and determinations are set within this context.

## Overview of NI Water Price Controls

- 1.6 NI Water's first three price controls, known as PC10, PC13 and PC15, covered the three year period (2010-13), the two year period (2013-15) and the six year period (2015-21) respectively. NI Water is currently in its fourth regulatory price control period, known as PC21, which began on 1 April 2021 and runs for six years until 31 March 2027.



- 1.7 Longer timescales were introduced for PC15 and PC21. This was to provide a more stable and predictable framework to support DfI's long-term water strategy. Longer price control periods can also promote better planning and efficient delivery.
- 1.8 A period of six years was chosen to provide an appropriate balance between allowing sufficient time for efficient planning/delivery and the potential uncertainty of outcome associated with planning over the long term.
- 1.9 Our approach to PC21 was developed within the context of DfI's long-term water strategy (LTWS) for Northern Ireland. This covers a 24-year horizon and aims to deliver a more strategic, holistic and integrated approach to the management of all aspects of the water and sewerage industry.
- 1.10 DfI's LTWS helped inform the content of the Department's Social and Environmental Guidance (S&EG) for the PC21 period. The S&EG was subsequently reflected in NI Water's business plan proposals and the outcome of our PC21 Final Determination.
- 1.11 The next price control period (referred to as PC27) will commence on 1 April 2027. The development of our approach to PC27 has commenced through initial engagement with principal stakeholders.

### **Provision for a PC21 Mid-Term Review**

- 1.12 As in PC15, our PC21 Approach recognised the uncertainty that might be associated with longer investment planning periods and that work undertaken in the early part of the price control period might help inform delivery proposals for the remainder of the PC21 period.
- 1.13 We therefore provided NI Water with a single opportunity to deal with material changes to address any uncertainty that existed at the time of the PC21 Final Determination. We call this the Mid-Term Review.
- 1.14 In Section 6 of our [PC21 Final Determination](#), we explained the potential remit of the Mid-Term Review and listed the elements of the price control that we were not minded to re-open as part of the process.
- 1.15 Our approach to the Mid-Term Review built upon the outline proposals included in our PC21 Final Determination and has been informed by the outcome of engagement undertaken with our principal stakeholders:
- Department for Infrastructure (DfI);
  - Northern Ireland Water (NI Water);

- Consumer Council for Northern Ireland (CCNI);
- Drinking Water Inspectorate (DWI); and,
- Northern Ireland Environment Agency (NIEA).

## **2. The Mid-Term Review Process**

### **Our approach**

- 2.1 When we introduced the concept of a Mid-Term Review, it was our intention that it should be limited to those areas where it would provide benefit, or was necessary. This is to ensure the opportunities and incentives of a 6-year plan are maintained as far as possible.
- 2.2 Our PC21 Mid-Term Review has been undertaken in this context and we have taken this into account when undertaking our assessments and coming to our conclusions.
- 2.3 The approach also recognises that established processes already exist for accounting for change, such as the logging up and down process that will be applied in the next price control.
- 2.4 In addition, we have considered opportunities for the Mid-Term Review to feed off existing regulatory processes and sources of information, such as the annual information return and the planned PC21 scope certainty submissions.

### **Engagement and consultation**

- 2.5 Our intention was that the Mid-Term Review process should be as open, transparent and collaborative as possible. We have therefore engaged with NI Water and principal stakeholders during the process. We acknowledge and appreciate the input provided to date.
- 2.6 In advance of the publication of the draft determination we provided updates on the emerging findings of the process so that some initial feedback could be provided and considered. However, it is acknowledged that further time will be required for others to fully consider the Mid-Term Review findings and for responses on specific issues to be prepared.
- 2.7 The publication and consultation on this draft determination will therefore provide the opportunity for NI Water, stakeholders and consumers to comment on our draft findings. It will also allow us to consider the feedback as we work towards our MTR Final Determination and the publication of our final Mid-Term Review report. We look forward to the positive engagement to date continuing as part of this process.

## **Our approach to specific elements of the Mid-Term Review**

2.8 Section 3, 4 and 5 of this draft determination document detail how we have undertaken our Mid-Term Review assessment for the key areas of the price control as follows:

- Section 3 - Outputs;
- Section 4 - Operating Expenditure; and,
- Section 5 - Capital Investment.

2.9 These sections outline the key issues considered, the approach taken and the conclusions reached.

## 3. Outputs

### Background

- 3.1 During a price control period, water and sewerage companies deliver a series of outputs which aim to secure the outcomes consumers want.
- 3.2 For PC21 we assessed NI Water's proposed outputs in line with the anticipated level of investment and the priorities set out in DfI's Social and Environmental Guidance. The outputs included in the PC21 Final Determination formed part of an overall package which the company is expected to deliver.
- 3.3 Tables 3.1 and 3.2 of our PC21 Final Determination detailed the targets we had set for the 45 consumer service, water service and sewerage service key performance measures established for NI Water for the period. The specific named schemes that the company was expected to deliver were listed in Annex G. In addition, we set 25 development objectives<sup>2</sup> for NI Water, which were listed in Table 3.3 and Annex T of our PC21 Final Determination.
- 3.4 In the Mid-Term Review we have tried to maintain the integrity of the PC21 Final Determination as far as possible. We have therefore only amended output targets where:
- a) the PC21 Final Determination noted that this would be required, for example:
    - (i) as a consequence of planned refinement of the newly established consumer measures by the consumer measure stakeholder group;
    - (ii) to account for the impact of the scope certainty exercise that we had asked NI Water to complete to clarify and the needs and costs for the wastewater and sewerage investment sub-programme schemes; and,
    - (iii) to account for the outcome of a development objective we had asked NI Water to complete, in order to confirm the number of properties affected by low water pressure issues.

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<sup>2</sup> Objectives which are aimed at developing NI Water's capability to identify and balance investment priorities and maximise the benefits delivered to consumers over the longer term. Refer to [PC21 Final Determination Main Report](#), commencing paragraph 3.82, for further details.

- b) delivery of an output has carried over from PC15 to ensure that this is not seen as outperformance against PC21 investment.
- c) change controls have been agreed by stakeholders and the associated allowances have been included in our determination.
- d) it is necessary to address errors and concerns we had in relation to the original targets submitted by NI Water for the price control period.
- e) planned development work has been completed and the associated development objective can therefore be closed.

3.5 The sections below identify the changes that we propose making in the Mid-Term Review within this context.

### **Consumer measures**

3.6 Section 3 of our PC21 Final Determination explained the work that had been undertaken by the CM/SAT Working Group (NI Water, CCNI, DfI and chaired by the Utility Regulator) on the development of alternative and more meaningful consumer measures and satisfaction surveys.

3.7 This resulted in the following changes to the metrics and targets that were adopted for the PC21 price control period:

- Unwanted Contacts - a new target measure which was introduced for PC21;
- First Point of Contact Resolution (FPOCR) - a new target measure which was introduced for PC21;
- Net Promotor Score (NPS) - a new target measure which was introduced for PC21;
- Overall Performance Assessment (OPA) - a previous target which was re-categorised as a 'semi-retired' measure and only to be monitored during PC21.
- Re-categorisation of the following customer contact measures as 'semi-retired' measures which were only to be monitored during PC21:

- ◆ DG6 (% of billing contacts dealt with within 10 working days),
- ◆ DG7 (% of written complaints dealt with within 10 working days); and
- ◆ DG9 (% of calls not abandoned).

3.8 Section 3 of our PC21 Final Determination also explained the proposals for the continued review of the PC21 measures by CM/SAT as well as its consideration of the development of new measures.

3.9 CM/SAT has continued this work as planned in order to identify further amendments which could be introduced at the Mid-Term Review. This is to make the PC21 consumer measures more relevant to NI Water and its customers. The Mid-Term Review changes that have been agreed by the group are set out below.

***Unwanted Contacts***

3.10 Minor changes have been introduced to align the definition of the Unwanted Contacts Measure with Ofwat guidance. Private issues, third party issues, developer services, Dfl and managed processes will be excluded. Reporting unwanted telephone contacts for both domestic and non-domestic consumers will continue. There is also a correction to the reporting of ‘run of water’ and ‘leak line’ contacts. This will ensure the methodologies are consistent, with the first call reported as ‘wanted’ and subsequent calls reported as ‘unwanted’. This also aligns with established guidance and good practice in England and Wales and will make sure the measure only reflects service failures for which NI Water is responsible.

3.11 CM/SAT has agreed revised targets which take account of these changes. These are presented alongside the original targets in Table 3.1 below.

Consumer Measure	2024-25	2025-26	2026-27
FD – Unwanted Contacts	64,300	63,400	62,500
MTR – Unwanted Contacts	56,000	55,100	54,200

**Table 3.1: Revised Unwanted Contact measure targets compared to original FD measure targets.**

***First Point of Contact Resolution (FPoCR)***

3.12 CM/SAT has agreed to retain the FPoCR measure in its current format and to leave the target of 84% unchanged for the PC21 period.

### **Net Promotor Score (NPS)**

- 3.13 NPS is calculated from information gathered through Voice of the Customer surveys conducted by an independent Customer Experience and Insight specialist. It captures the views of customers who have had dealings with the company through the main contact centre and other parts of the business.
- 3.14 For the Mid-Term Review, NPS has been changed from a measure which applies to both domestic and non-domestic customers, to a measure which only applies to domestic customers. It will be weighted equally between water and wastewater contacts. To account for this change, non-domestic consumer satisfaction will be measured separately through new measures, which will be developed through CM/SAT and introduced in PC27. This approach will help ensure the right outcomes for customers, by providing better visibility on performance for the different services that NI Water provides to domestic and non-domestic customers. It will also facilitate better comparisons with other UK water companies.
- 3.15 Targets for the new 'domestic only' measure have been agreed by CM/SAT and these are presented alongside the original targets for the combined measure in Table 3.2 below.

Consumer Measure	2024-25	2025-26	2026-27
FD – Net Promotor Score (NPS) (Domestic Non-domestic)	+42	+42	+42
MTR – Net Promotor Score (NPS) (Domestic)	+40	+41	+42

**Table 3.2: Revised NPS measure targets compared to original FD measure targets.**

### **Overall Performance Assessment**

- 3.16 An Overall Performance Assessment (OPA) score has historically been used to assess NI Water's overall delivery of service to customers. This is a composite score which includes a broad range of measures covering service delivery in the areas of water supply, sewerage service, customer service and environmental performance.
- 3.17 CM/SAT has decided it is content for the Overall Performance Assessment (OPA) score used in previous price controls to be fully retired at the Mid-Term Review. This is because it is now considered to have limited use as:
- comparisons with English and Welsh water companies are not possible because OPA has not been reported by those companies since 2009-10;



- a number of individual OPA components have been superseded; and,
- many others are already consistently achieving the maximum possible OPA score.

3.18 In taking this decision, CM/SAT recognised that the majority of the components of the OPA measure already form part of the Annual Information Return. It has also been agreed that the UR will make the minor adjustments necessary to ensure that all critical OPA component data is captured. This will ensure that a comparative year on year score can be calculated in the future if this is ever deemed necessary.

### ***Semi-Retired Director General (DG<sup>3</sup>) Measures***

3.19 CM/SAT has decided that there is no longer a need to report NI Water's performance for the semi-retired customer contact measures (i.e. billing contacts dealt, response to written complaints and telephone calls not abandoned) after the Mid-Term Review.

3.20 NI Water will however continue to capture this data for the remainder of the PC21 period to allow it to be referenced if necessary.

### ***Development of new Consumer Measures for PC27***

3.21 CM/SAT has agreed to commence data collection and planning for the potential introduction of a number of new measures for the PC27 period. The consideration and development of these measures, which are detailed below, will continue over the remainder of PC21.

- a) Internal Developer Services Bespoke Consumer Measure: CM/SAT has agreed that NI Water should aim to introduce a new metric at the start of PC27 to measure and report on customer experience of engaging with Developer Services. This will bring NI Water in line with companies in England, Scotland and Wales who have already introduced specific measures which have a clear and tangible impact on the delivery of improvements.

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<sup>3</sup> This term dates back to the original privatisation of water in England and Wales (E&W) and regulation by the original Director General or 'DG'.

- b) Non-Domestic Net Promotor Score (NPS): There are concerns over the potential volatility of a Non-Domestic NPS measure due to the relatively low numbers of survey responses from business customer. CM/SAT has therefore decided to continue to monitor the Non-Domestic NPS throughout the remainder of PC21 to determine whether it is suitable for introducing as a target measure in PC27. Several potential options will be considered, including changing to a “range target” or a hybrid approach through the survey of non-domestic silent customers.
- c) Consumer Vulnerability: CM/SAT discussed setting targets linked to increasing awareness of NI Water’s Customer Care Register and for measuring the level of satisfaction of the support provided to consumers in vulnerable circumstances. However, due to concerns regarding availability of historical data, budget and the nature of services, it was agreed that the remaining PC21 period should be used to plan and set meaningful targets for PC27. This process will allow future outputs from the UR Best Practice Framework Programme to be taken into account. A high-level plan for Customer Care Register (CCR) targets was agreed. In the interim, NI Water will continue to track awareness of the CCR through the annual Omnibus Survey.
- d) Consumer Engagement: The PC21 Consumer Engagement development objective noted the potential to “undertake a consumer research and engagement review/appraisal at the mid-point of PC21”. CM/SAT considered this to be addressed through its discussions and agreed there was no requirement for further research work at the mid-point of PC21. This will be considered further as part of the PC27 price control process.

3.22 CCNI has also highlighted a concern in terms of the visibility of NI Water's performance against the aims/promises set out in the company's Codes of Practice. We anticipate that consideration of this, including how monitoring and reporting of NI Water’s performance might be implemented, will also form part of the CM/SAT discussions for PC27.

## **Nominated Outputs**

3.23 Nominated outputs are specific items, often identified by the quality regulators (NIEA and DWI), such as improvements to treatment works so that discharge standards meet mandatory legislative requirements. They also include a number of specific improvements that NI Water has identified

as nominated outputs in its business plan, such as trunk main schemes and the provision of additional water storage capacity.

3.24 The PC21 Final Determination included a list of named priority outputs which NI Water was expected to deliver through its capital investment programme. In its Mid-Term Review submission, NI Water proposed that the following changes be made to the PC21 nominated output targets.

	NIW adjusted PC21 FD	Not needed	Deferral	New / Additional	NIW proposed revision
Trunk main schemes	14		3	1	12
Service reservoirs / Clear water tanks	4		1	1	4
Water treatment works schemes	20		1	15	34
Improvements to UIDs	136	14	33	13	102
Wastewater treatment work schemes	46	4			42
Economic constrained areas eased	12		2		10
Serious development restrictions eased	37		1		36

**Table 3.3: NI Water's proposed changes to nominated output targets.**

3.25 However, changes in planned capital investment occur in every price control. This may be a consequence of:

- the clarification of need as investigations and studies into required solutions progress;
- the impact of material cost variances; or,
- the inability to deliver particular projects as a result of issues associated with other processes, such as achieving planning approval or purchasing land.

3.26 We have therefore decided to apply two different approaches for dealing with the nominated output changes set out in table 3.3 above. We have accounted for some within this MTR process and will account for others through our established price control logging process at the end of PC21.

***Nominated outputs dealt with through established Logging process***

3.27 When material changes in planned delivery occur, we normally use a logging up/logging down process to apply the necessary financial corrections retrospectively. This means that consumers and NI Water are not disadvantaged by any change that has occurred.

- 3.28 This logging process either ‘benefits’ the company through a positive Regulatory Capital Value (RCV) adjustments for outperformance, or ‘penalises’ it through a negative RCV adjustment for underperformance.
- 3.29 On the basis of this and our MTR Draft Determination conclusion in relation to the evidence for Real Price Effects, we believe that the targets for any nominated outputs which are not linked to NI Water's scope certainty exercise should remain as they were in the PC21 Final Determination.
- 3.30 As a result, any variance in delivery for these measures will be accounted for using the standard logging up/logging down process.
- 3.31 The PC21 targets for trunk mains, service reservoir/clear water tanks and water treatment works have therefore not been amended, apart from accounting for any change control and any PC15 carry over, as detailed in Table 3.4 and Table 3.5 below.

	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	PC Total
FD – Trunk main schemes	0	2	1	5	2	4	14
MTR – Trunk main schemes	0	2	1	5	2	5 <sup>1</sup>	15

Note 1 One output added in 2026-27 to account for Unagh/Beltoy Pumping Station Change Control (CCP003).

**Table 3.4: Utility Regulator’s proposed adjustment of Trunk Main nominated output targets.**

	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	PC Total
FD – Water treatment works schemes	1	0	5	4	1	8	19
MTR – Water treatment works schemes	1	2 <sup>1</sup>	5	4	1	8	21

Note 1 Two outputs added in 2022-23 to account for Dorisland WTW PC15 carryover and Derg WTW MCP Change Control (CCP001).

**Table 3.5: Utility Regulator’s proposed adjustment of WTW nominated output targets.**

***Nominated outputs adjusted in MTR***

- 3.32 However, it is recognised that the provision for NI Water to make scope certainty submissions for significant elements of the wastewater and sewerage sub-programmes, as a consequence of them being insufficiently developed at the time of the PC21 Final Determination, was unusual.
- 3.33 It was clear at the outset that this process had the potential to affect the solutions/costs and therefore the associated outputs. The remit of the associated development objective included in the PC21 Final Determination therefore acknowledged and reflected this.

- 3.34 The outputs associated with the scope/certainty exercise have therefore been treated as sitting outside the standard logging up/logging down process and instead have been dealt with as part of this Mid-Term Review.
- 3.35 As a result, we have reviewed, and if necessary, revised them so that they are more reflective of the figures that would have been in the PC21 Final Determination if the relevant information had been available at that time.
- 3.36 For large wastewater treatment works and unsatisfactory intermittent discharges, we have reviewed and accepted the revised targets proposed by NI Water. The revisions reflect the following approach adopted by the company in its Mid-Term Review submission:
- a) It removed a number of projects as a consequence of being able to prove that the environmental need does not exist.
  - b) In cases where cost increases were overly disproportionate and no longer considered cost beneficial, it deferred schemes to PC27 to allow further modelling to be undertaken and lower cost solutions to be investigated in conjunction with NIEA.
  - c) It deferred projects considered undeliverable for engineering reasons.
  - d) Where possible, it included other projects to help offset the deferrals. However, the scale of the cost increases in the sub-programmes meant that bringing in 'substitute' schemes in all circumstances was unachievable.
- 3.37 Taking this approach for the draft determination ensures that the wastewater treatment works and unsatisfactory intermittent discharge outputs align with our Mid-Term Review determination of the capital allowance required for the wastewater and sewerage sub-programmes.
- 3.38 Whilst this approach results in the number of outputs being slightly lower than in the PC21 Final Determination, we believe it remains consistent with DfI's PC21 Social and Environmental Guidance objective of establishing a deliverable investment plan which meets established needs and is affordable from a tariff perspective.
- 3.39 The minor changes to the targets for economic constrained areas and serious development restrictions proposed by NI Water have also been accepted. This is on the basis that they are associated with the changes to the number of wastewater treatment works and unsatisfactory intermittent discharge upgrades being delivered.

3.40 Table 3.6, Table 3.7 and Table 3.8 below show the nominated outputs changes that we intend making in the Mid-Term Review as a consequence of the outcome of the scope certainty exercise completed by NI Water and any PC15 carry over. The annual targets incorporate some re-profiling of the revised totals.

	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	PC Total
FD – Improvements to UIDs	7	21	21	13	25	49	136
MTR – Improvements to UIDs	4	3	4	29	23	39	102 <sup>1</sup>

Note 1 14 UIDs have been identified as not needed, 33 UIDs have been deferred for further investigation, 13 new UIDs have been added. The revised PC21 total has been re-profiled across the price control period.

**Table 3.6: Utility Regulator’s proposed adjustment of Unsatisfactory Intermittent Discharge (UID) nominated output targets.**

	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	PC Total
FD – Wastewater treatment work schemes	0	5	16	3	7	14	45
MTR – Wastewater treatment work schemes	1	6	4	2	10	19	42 <sup>1</sup>

Note 1 One output added in 2021-22 to account for Ballykelly WwTW PC15 carryover; one output identified as not needed in 2023-24 (Kilkeel WwTW), three outputs identified as not needed in 2026-27 (Culmore WwTW, Larne, Kilkeel WwTW, Carrickfergus WwTW). The revised PC21 total has been re-profiled across the price control period.

**Table 3.7: Utility Regulator’s proposed adjustment of WwTW nominated output targets.**

	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	PC Total
FD – Economic constrained areas eased	0	0	0	2	1	9	12
MTR – Economic constrained areas eased	0	0	0	1 <sup>1</sup>	0 <sup>2</sup>	9	10
FD – Serious development restrictions eased	4	0	0	8	9	16	37
MTR – Serious develop restrictions eased	4	0	0	8	8 <sup>3</sup>	16	36

Note 1 One output (Enniskillen) removed from 2024-25

Note 2 One output (Newry) removed from 2025-26.

Note 3 One output (Maghera) removed from 2025-26.

**Table 3.8: Utility Regulator’s proposed adjustment of Economic Constrained Area and Serious Development Restriction nominated output targets.**

3.41 NI Water also asked for the definition of the targets for economic constrained areas and serious development restrictions to be changed from 'removed' to 'eased'.

3.42 This is because 'removal' would require all unsatisfactory intermittent discharges in a catchment to be addressed and it is recognised that it will take a number of price controls before this is achieved.

- 3.43 We have therefore accepted this change in definition as we believe it more accurately reflects the original intention of the target and removes the potential for any misinterpretation in relation to what is being delivered by the investment in PC21.
- 3.44 We note that NI Water has not proposed any adjustments to its wastewater treatment percentage compliance targets as a consequence of the change in the number of nominated outputs. We will therefore engage with NI Water between the MTR Draft and Final Determinations to check that this approach is appropriate.

### **Other PC21 MTR output adjustments**

- 3.45 We plan to amend a limited number of other output targets at the Mid-Term Review as a consequence of the rebasing of company data/plans and to correct for errors in the original business plan submission. Further details, including the rationale for making the changes, are provided below.

#### ***Properties at risk of low pressure (DG2)***

- 3.46 NI Water maintains a DG2 register of properties that are at risk of low pressure, which helps it to target investment to deliver the maximum benefit for consumers.
- 3.47 In its PC21 business plan submission NI Water highlighted concerns that the information on its DG2 register might be underrepresenting the number of properties experiencing low pressure.
- 3.48 As a consequence, we included a development objective in our PC21 Final Determination requiring the company to
- 3.49 undertake the necessary modelling and investigations to confirm the number of properties affected.
- 3.50 This development objective was aimed at improving the quality and confidence of NI Water's data to provide a more robust basis for setting targets and delivering improvements for customers moving forward.
- 3.51 Our PC21 Final Determination noted that the PC21 low pressure targets would potentially need to be revised at the Mid-Term Review as a consequence of the completion of this work.
- 3.52 The company completed its DG2 register update in August 2022. This resulted in the number of recorded low pressure properties increasing from c600 to c1,900.



- 3.53 In its PC21 Mid-Term Review submission the company proposed changes to its low pressure targets based on the revised number of properties registered.
- 3.54 As part of our Mid-Term Review assessment we asked the Reporter to check if NI Water's approach to the 'refresh' of the register had been undertaken in accordance with the reporting guidance and industry best practice. The Reporter was also asked to confirm if the revised numbers represented a reasonable basis for setting targets moving forward and to propose revised targets for the remainder of the PC21 period if this was found to be the case.
- 3.55 Following engagement with company, the Reporter advised that NI Water were broadly compliant with the relevant guidance. He found that the associated business as usual processes were being conducted by a dedicated team that had good technical knowledge of the subject area, the geography of the water supply area and the delivery of operations/schemes related to the DG2 performance metric.
- 3.56 However, the Reporter also noted some concerns in relation to NI Water's data and methodology. Most notably, the need to employ technology and systems which are more aligned to industry best practice, and in particular, the need to establish ongoing logging and analysis to monitor pressures across the network. He suggested that these could have negated the need for the register 'refresh' in the first place and would provide much greater granularity of data, in terms of the location and timing of issues.
- 3.57 The Reporter's review of the revised targets submitted by NI Water for 'removals by company action', concluded that they were lower than might have been expected based on the outcome of the register 'refresh'. NI Water has since agreed to increase its annual targets accordingly.

The revised Mid-Term Review targets for the number of low pressure properties removed by company action and the total number of low pressure properties on the register, are presented in Table 3.9 and Note 1 Actual delivered by NI Water to date.

3.58 Table 3.10 below alongside the original PC21 targets.

	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
FD – DG2 Properties at risk of low pressure removed from the risk register by company action	147	145	143	139	137	135
MTR – DG2 Properties at risk of low pressure removed from the risk register by company action	176 <sup>1</sup>	143 <sup>1</sup>	200 <sup>1</sup>	158	188	263

Note 1 Actual delivered by NI Water to date.

**Table 3.9: Revised targets for the number of low pressure (DG2) properties removed by company action.**



	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
FD – DG2 Properties receiving pressure below the reference level at end of year	492	427	365	306	250	195
MTR – DG2 Properties receiving pressure below the reference level at end of year	1,715 <sup>1</sup>	1,780 <sup>1</sup>	1,642	1,534	1,396	1,183

Note 1 Actual delivered by NI Water to date.

**Table 3.10: Revised targets for total number of low pressure (DG2) properties.**

***Impermeable surface water area***

- 3.59 Targets for the impermeable surface water area removed from the combined sewerage network have been adjusted to account for an incorrect conversion factor applied by NI Water in its PC21 business plan submission. This was in error by a factor of 10.
- 3.60 This amendment addresses a concern we originally raised with the company during the PC21 determination process. It has no implications for funding as the allowance requested by NI Water in its business plan submission was based on the delivery of the lower ‘corrected’ impermeable surface area that is now reflected in the Mid-Term Review targets.
- 3.61 Details of the original and revised targets are shown in Table 3.11 below.

	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
FD – Impermeable surface water area (m2)	364,540	364,540	364,540	364,540	364,540	364,540
MTR – Impermeable surface water area (m2)	-	-	-	36,450	36,450	36,450

**Table 3.11: Impermeable surface water area removed.**

***Power derived from renewable sources***

- 3.62 Targets for the percentage of NI Water's power usage derived from renewable sources have been re-profiled to align with NI Water's Climate Strategy.
- 3.63 NI Water's Climate Strategy was developed after the company submitted its PC21 business plan to take account of the aims of the Department for the Economy's (DfE) Energy Strategy, which wasn't finalised until after the PC21 Final Determination.
- 3.64 The amendment of the targets addresses concerns we expressed in our PC21 Final Determination in relation to NI Water setting a closing target of 100% in advance of the publication of the Energy Strategy and the implications this might have in terms of power purchase costs.

- 3.65 This change has no adverse implications. It does not affect PC21 funding or the PC21 proposals relating to self-generation as almost all of the company's renewable energy is purchased from others. It will however help ensure that NI Water can continue to purchase its renewable energy at an efficient cost to the benefit of consumers by avoiding this self-imposed target becoming a driver for increased costs as a consequence of the significant increase in the cost of Renewable Energy Guarantees of Origin (REGO).
- 3.66 Details of the original and revised targets are shown in Table 3.12 below.

	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
FD – percentage of NI Water's power usage derived from renewable sources (%)	45	45	50	50	75	100
MTR – percentage of NI Water's power usage derived from renewable sources (%)	-	-	-	50	50	50

Note 1 95% of power usage derived from renewable sources is purchased and 5% is self-generated.

**Table 3.12: Percentage of power usage derived from renewable sources.**

### Development outputs

- 3.67 The Final Determination for PC21 included 25 key development objectives which cover areas of improvement that cannot necessarily be monitored using numerical targets. They are intended to help ensure NI Water develops its planning capability and introduces new techniques to improve this and the service delivered to consumers over the longer term.
- 3.68 The development objective list for PC21 included areas where we considered development to be necessary to justify the need for investment in the second half of the price control period and to support NI Water's preparation of its PC27 business plan submission.
- 3.69 For the Mid-Term Review we have:
- Assessed business cases submitted by NI Water for those objectives where approval for continued investment for the remainder of the period was dependent on proof of benefit; and,
  - Assessed NI Water's progress in delivering all the PC21 development outputs using the annual progress updates submitted as part of NI Water's annual information return. In doing so, we considered the extent to which specific milestones had been met. We also considered whether sufficient progress is being made to deliver the objective in PC21 and, where appropriate, support the company's PC27 submission; and,

- Decided whether any development outputs are substantially complete, and can therefore be closed at the Mid-Term Review.

3.70 Further information on our assessments and conclusion are provided below.

### ***Smart Metering***

3.71 As part of their PC21 Business Plan submission, NI Water proposed embarking on a smart metering programme for non-domestic customers.

3.72 The company's initial PC21 proposal for a 'big bang' strategy, whereby all dumb meters were replaced by smart meters over an 18-month period, was not accepted by us due to a range of concerns in relation to the justification presented by the company.

3.73 It was instead agreed that NI Water could implement a business as usual (BAU) proposal. This proposal was that non-domestic dumb meters would be replaced by either a drive-by (AMR)<sup>4</sup> meter or fully smart (AMI)<sup>5</sup> meter when they reached end of life or failed. Continued investment over the whole price control period was dependent on this being proven to be an appropriate and cost beneficial programme of work.

3.74 We therefore introduced a PC21 development objective, which required NI Water to:

- use the information gathered from its installation programme in the first half of PC21 to prove its smart metering concept,
- identify the most suitable technology, and
- develop a cost benefit analysis (CBA) for consideration at the Mid-Term Review.

3.75 The purpose was for NI Water to prove that the move away from dumb meters was beneficial from an operational and cost perspective.

3.76 The CBA submitted by NI Water in the Mid-Term Review proposed that 90% of the replacements should be AMR drive-by meters. This was primarily for areas where installation of the technology to support fully smart AMI meters would not be cost beneficial. It also proposed that 10% should be AMI meters, primarily in urban areas where the installation of the support technology would make more sense from a cost benefit perspective.

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<sup>4</sup> AMR – Automatic Meter Reading (drive by or walk by requiring a meter reader using Bluetooth to capture readings) considered an upgrade rather than fully smart.

<sup>5</sup> AMI – Advanced Metering Infrastructure a 'fully smart' option which allows for usage and more detailed information to be transferred to a receiver rather than in-situ personnel to obtain a reading.

- 3.77 NI Water's CBA identified savings in the region of £1m over the 17-year period considered, when other benefits of smart metering such as leakage reduction, consumption reduction and revenue protection<sup>6</sup>, were taken into account.
- 3.78 As part of our assessment of NI Water's PC21 submission we asked our engineering consultants to review the company's CBA. This included the methodology employed, the assumptions made, the choice of technology proposed and the submitted costs.
- 3.79 The consultants concluded that, despite a number of shortcomings in the CBA approach/methodology applied by the company, the switch from dumb meters to drive-by meters (as a minimum), represented a positive operational development.
- 3.80 The consultants also concluded that '...the continuation of smart metering (and meter upgrades) as currently proposed would be considered cost beneficial', noting that the company had been conservative in its consideration of the broader benefits that might be delivered.
- 3.81 The PC21 Final Determination allowance has therefore not been adjusted in this Mid-Term Review.
- 3.82 We however plan to engage further with the company on its approach to assessing the costs and benefits of smart metering for PC27, taking account of our engineering consultant's comments and recommendations.

### ***Leakage***

- 3.83 In its PC21 business plan submission, the company proposed a leakage reduction profile which would deliver the sustainable economic level of leakage (SELL) of 149.98Mld by the end of the price control period. We accepted the PC21 targets submitted by the company on the basis of this assessment which had been undertaken in 2019.
- 3.84 The PC21 Final Determination included allowances for innovative technology trials intended to help NI Water reduce leakage and meet its targets. However, because of the innovative nature of the proposals, a development objective was included for the company to report on the outcome of the trials as part of its annual information return, so that we could consider if continued funding beyond the Mid-Term Review made economic sense.
- 3.85 The leakage innovation technologies trialled by the company include:

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<sup>6</sup> Detection & prevention of misuse of Domestic supply for non-domestic purposes e.g., Dom/Agri supplies via AMR logging data.

- Acoustic logging
- Satellite imagery
- New equipment – Ground Penetrating Radar/Gas/Drones

3.86 The company has reported that certain technologies are proving more successful than others. For example, satellite imagery is delivering a higher success rate than FIDO acoustic loggers. The trials involving this new technology and equipment are still ongoing and we have decided to retain the associated allowances for the remainder of the PC21 period to allow a full range of options and opportunities to be explored. This will allow NI Water to fully assess the benefits of each technology and to develop an evidence-based investment proposal for PC27.

3.87 The PC21 Final Determination also included a requirement for NI Water to update its SELL assessment so that the amendment of leakage reduction targets could be considered at the Mid-Term Review if there was a material change. The revised SELL figure of 149.28MI/d that NI Water derived through this reassessment was almost identical to the figure that the PC21 targets were based on and so it has not been necessary to make any changes at the Mid-Term Review.

***Closure of completed Development Outputs***

3.88 NI Water's Mid-Term submission proposed that seven of the 25 PC21 development objectives should be closed at the Mid-Term Review, because the company considered them to be complete. These are listed in Table 3.13 below.

Development output	Description
1	Consumer engagement
2	Consumer Protection/ Care Register
5	Refresh of DG2 Register
9	WwPS / CSO Quality (UID) and WwPS (Capacity increase)
11	Cranfield Catchment, Kilkeel Storm Separation
24	Smart Meters
25	Addressing scope uncertainty for the Mid-Term Review

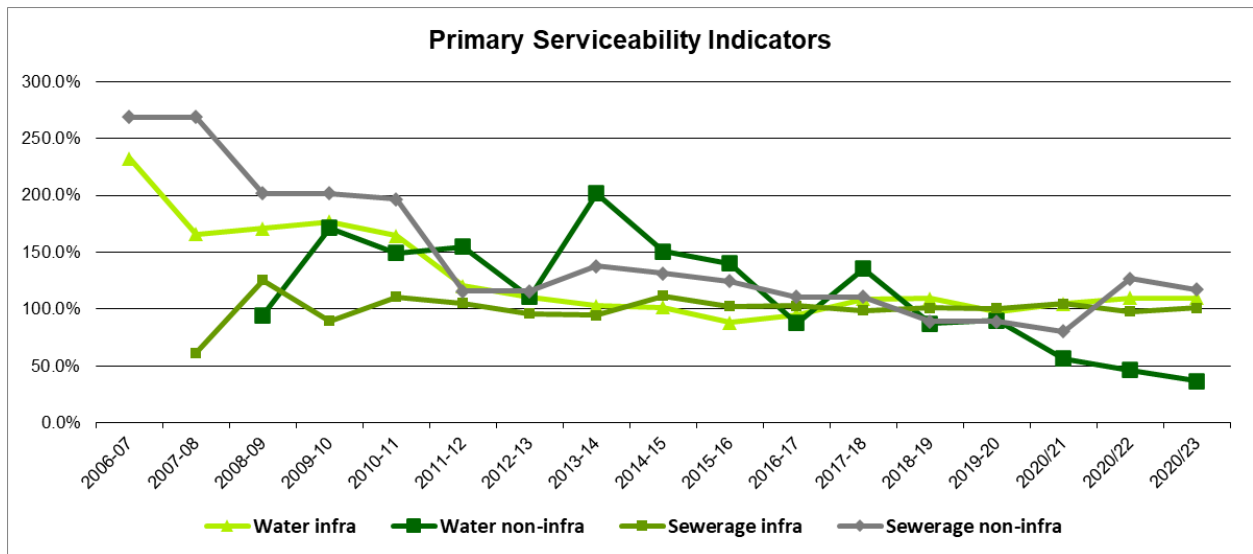
**Table 3.13: Development Outputs proposed for closure by NI Water.**

3.89 We agree with the company's assessment for the majority of these objectives and plan to close all of them apart from two, as detailed below.

- Objective 1 relates to the development of consumer measures and consumer engagement. In this case, we think that there would merit in retaining an oversight of developments for the remainder of the PC21 period as a consequence of the need to undertake consumer engagement for the PC27 price control and establish targets for any new consumer measures that are due to be introduced.
- Objective 2 relates to activities linked to consumer protection and the consumer care register. In this case, we think that there would merit in retaining an oversight of developments during the remainder of the PC21 period as a consequence of the recent publication of the Utility Regulator's Consumer Protection Programme decision paper and the need for companies to implement requirements associated with this.

## **Serviceability**

- 3.90 Our primary mechanism for assessing the sufficiency of the company's base maintenance allocation, and whether it is maintaining its assets effectively, is our serviceability assessment. This considers trends for a range of primary and secondary performance indicators for above and below ground water and wastewater assets.
- 3.91 Annex F of our PC21 Final Determination explained the assessment process, the outcome of our assessment and the performance bands chosen for monitoring performance during the price control period.
- 3.92 We assess actual performance against the serviceability performance bands each year for our annual cost and performance report. This assessment considers whether the performance for individual indicators is stable, improving, deteriorating or marginal across the four different service areas and allows us to conclude whether serviceability is being maintained overall.
- 3.93 We have updated our serviceability assessment for the Mid-Term Review using the updated information and longer data trends received in the company's 2022-23 annual information return. Our assessment shows that serviceability has remained stable in all service areas as demonstrated by the selected trends for the primary indicators below.



**Figure 3.1: Primary Serviceability Indicators.**

- 3.94 The updated data trends have remained within the control limits set for each indicator in the PC21 Final Determination and the reference levels remain broadly reflective of performance. We have therefore concluded that there is no need to change these at the Mid-Term Review and they will be 'refreshed' in the PC27 determination process using the additional data captured during PC21.
- 3.95 This serviceability assessment also provides an indication that the capital maintenance allowance included in the PC21 Final Determination is sufficient, which supports our decision not to adjust this at the Mid-Term Review.

### **Delivery of Social and Environmental Priorities**

- 3.96 Our price control determinations are intended to establish the funding required by NI Water to meet the priorities contained within DfI's Social and Environmental Guidance (S&EG).
- 3.97 However, at the time of the PC21 Final Determination there were large elements of the wastewater treatment and sewerage programmes which could not be determined as solutions were insufficiently developed.
- 3.98 A 'holding' allowance for these schemes was therefore included and plans were put in place for the finalised solutions to be submitted by NI Water at a later date for determination at the Mid-Term Review. It was understood at the time that this 'scope certainty' exercise would likely change the PC21 capital funding requirement and associated outputs.

- 3.99 This exercise has now been completed and we have adjusted the PC21 investment plan, allowances and associated outputs accordingly. We consider that the overall outcome of the Mid-Term Review process, including the 'scope certainty' exercise, remains aligned with the aim of the Social and Environmental of formulating a deliverable investment plan which meets established needs and is affordable from a tariff perspective.
- 3.100 NI Water made good progress in the delivery of its PC21 requirements in the first two years of the price control, when fully funded. We consider that fully funding the plan continues to represent the best outcome for consumers and the environment. It would help avoid delays in the planned delivery of environmental compliance, the release of development constraints and the delivery of a more sustainable and efficient service. It would also avoid the transfer of responsibility and risk away from the company to others, including DfI and consumers.
- 3.101 We will report on NI Water's delivery against the aims of the Social and Environmental Guidance at the end of the PC21 period, reflecting on the impact that any funding allocations might have had, as part of that process.

### **PC21 Mid-Term Review output summary**

- 3.102 Table 3.14 and Table 3.15 below provide a complete summary of the updated list of PC21 key output targets. These tables take account of the proposed changes described above.



Line description		Units	PC15	PC21					
A Consumer Service			2019-20	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
1	DG2 Properties at risk of low pressure removed from the risk register by company action	nr	115	147	145	143	158	188	263
2	DG2 Properties receiving pressure below the reference level at end of year	nr	626	492	427	365	1534	1396	1183
3	DG3 Supply interruptions > 12hrs (unplanned and unwarned)	%	0.088	0.091	0.087	0.084	0.080	0.077	0.073
4	DG3 Supply interruptions (overall performance score)	nr	0.79	0.81	0.79	0.77	0.75	0.72	0.70
5	DG8 % metered customers received bill based on a meter reading	%	99.5	99.0	99.0	99.0	99.0	99.0	99.0
6	Unwanted contacts	nr	67,013	67,000	66,100	65,200	56,000	55,100	54,200
7	First Point of Contact Resolved (FPOCR)	%	90	84	84	84	84	84	84
8	Net Promoter Score	nr	42	42	42	42	40	41	42
9	Total Leakage	MI/d	161	157	156	154	153	151	150
10	Security of supply index	nr	100	100	100	100	100	100	100
11	Percentage of NI Water's power usage derived from renewable sources	%	44	45	45	50	50	50	50
B Quality Water									
12	% overall compliance with drinking water regulations	%	99.90	99.83	99.83	99.83	99.83	99.83	99.83
13	% compliance at consumers tap	%	99.84	99.74	99.74	99.74	99.74	99.74	99.74
14	% iron compliance at consumers tap	%	98.89	98.62	98.62	98.62	98.62	98.62	98.62
15	% Service Reservoirs with coliforms in >5% samples	%	0.00	0.00	0.00	0.00	0.00	0.00	0.00
C Water Outputs									
16	Water mains activity - Length of new, renewed or relined mains	km	149	139.7	139.7	139.7	139.7	139.7	139.7
17	Completion of nominated trunk main schemes	nr	0	0	2	1	5	2	5
18	Completion of nominated water treatment works schemes	nr	1	1	2	5	4	1	8
19	Completion of nominated improvements to increase the capacity of service reservoirs and clear water tank	nr	1	1	0	0	0	3	0
D Serviceability									
20	Water infrastructure serviceability	Text	Stable	Stable	Stable	Stable	Stable	Stable	Stable
21	Water non-infrastructure serviceability	Text	Stable	Stable	Stable	Stable	Stable	Stable	Stable
E PC15 Additional Output Measures									
22	Number of lead communication pipes replaced	nr	1,781	1,844	1,844	1,844	1,844	1,844	1,844
23	Number of school visits	nr	229	176	176	176	176	176	176
24	Number of events	nr	143	57	57	57	57	57	57
F PC21 Additional Output Measures									
25	Number of catchments where management plan recommendations have been delivered	nr	n/c	0	3	4	5	5	3
26	Number of treatability studies completed	nr	n/c	0	0	0	12	0	0

**Table 3.14: Water Provision and Service Output Targets - MTR.**

Line description		Units	PC15	PC21					
			2019-20	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
<b>A Consumer Service Sewerage</b>									
1	DG5 Properties at risk of flooding - number removed from the 2 in 10, 1 in 10 and 1 in 20 risk register by company action	nr	1	0	0	20	6	10	21
2	DG5 Properties on the 2 in 10, 1 in 10 and 1 in 20 risk register at the end of the year	nr	119	120	123	106	103	96	78
<b>B Quality Sewerage</b>									
3	% of WwTWs discharges compliant with numeric consents	%	94.90	92.05	91.63	92.33	93.26	93.72	94.14
4	% of total p.e. served by WwTWs compliant with numeric consents	%	99.50	99.18	94.65	94.65	95.71	95.72	95.77
5	Small WwTW compliance (works greater than or equal to 20p.e. but less than 250p.e.)	%	89.29	90.76	91.09	93.07	95.05	97.03	99.01
6	Number of high and medium pollution incidents attributable to NI Water	nr	13	12	11	10	9	8	7
<b>C Sewerage Outputs</b>									
7	Sewerage activity - Length of sewers replaced or renovated	km	18.5	10.1	10.1	10.1	10.1	10.1	10.1
8	Delivery of improvements to nominated UIDs as part of a defined programme of work	nr	3	4	3	4	29	23	39
9	Delivery of improvements to nominated WwTWs as part of a defined programme of work	nr	2	1	6	4	2	10	19
10	Small wastewater treatment works delivered as part of the rural wastewater investment programme	nr	9	6	6	6	6	6	6
<b>D Serviceability</b>									
11	Sewerage infrastructure serviceability	Text	Stable	Stable	Stable	Stable	Stable	Stable	Stable
12	Sewerage non-infrastructure serviceability	Text	Stable	Stable	Stable	Stable	Stable	Stable	Stable
<b>E PC15 Additional Output Measures</b>									
13	Number of CSO and EO discharges at which event and duration monitoring equipment is installed/fully optimised, and meet NIEA requirements	nr	37	66	67	117	166	166	162
14	Number of qualifying Wastewater Treatment Works delivered as part of the defined programme of improvements to comply with PPC Regulations	nr	7	0	0	4	3	4	4
15	Impermeable surface water collection area removed from the combined sewerage network (such as roads and pavements, roofs and hardstandings)	m2	59,586	36,454	36,454	36,454	36,454	36,454	36,454
16	Number of 'sustainable solution' WWTW serving a PE ≥ 250 delivered as part of the defined programme of work for improvements to nominated WWTWs	nr	0	0	0	0	1	1	2
17	Number of 'sustainable solution' WWTW serving a PE < 250	nr	0	0	0	0	1	1	1
<b>F PC21 Additional Sewerage Output Measures</b>									
18	Number of Economic Constraint Areas Eased	nr	n/c	0	0	1	2	1	6
19	Number of Serious Development Restrictions Eased	nr	n/c	0	6	2	6	8	14

**Table 3.15: Sewerage Provision and Service Output Targets - MTR.**

## 4. Operating Expenditure

### NI Water's Revenue Claim

- 4.1 Our PC21 Final Determination outlined our proposals for the PC21 Mid-Term Review, including the extent and scope of the work that we anticipated undertaking. For operating expenditure, we indicated that we were not minded to reopen the financial determination to reconsider operational cost efficiency or general changes in operational expenditure, such as unit rates for power or changes in labour or contractor costs.
- 4.2 This is based on the principle that the risks associated with these issues should remain with the company to manage over the duration of a six-year price control. This approach helps ensure that the timing of a Mid-Term Review does not have an impact on how the company plans and delivers efficiency. It also ensures that the Mid-Term Review is not driven by short term changes in key unit rates which might be reversed during the remainder of the price control.
- 4.3 In our Mid-Term Review Approach, we advised that our minded to position in relation to operational cost efficiency had not changed. However, we acknowledged that the company's power costs had increased significantly since the PC21 Final Determination and that we would consider how these additional costs should be dealt with for the remainder of the PC21 period, including the impact they might have on tariffs. We also said that we would consider other material cost pressures, such as increased chemical costs on the basis of any evidence submitted by the company.
- 4.4 In May 2023 the company notified the UR of its intention to seek a review of K-Factors as a consequence of the financial pressures currently being faced, such as the significant increase in power costs.
- 4.5 In its PC21 Mid-Term Review submission, NI Water included the Revenue adjustment claim shown in Table 4.1 below, which it estimated equated to an overall annual Weighted Average Charge Increase (WACI) of 4.3% in real terms. This means that, on average, customer tariffs would increase by a maximum of 4.3% in real terms over the remainder of the PC21 period.

MTR Revenue Claim (2018-19 £m)	2024-25	2025-26	2026-27	PC21
Power	+24.01	+20.51	+18.32	+62.84
Chemicals	+2.63	+2.63	+2.63	+7.89
Cloud Implementation	+8.77	+2.99	+0.57	+12.33
Rates	(7.42)	(7.42)	(7.42)	(22.26)
PPP	(2.64)	(2.25)	(2.59)	(7.48)
Insurance	+1.08	+1.10	+1.10	+3.16
Efficiency Adjustment	(0.54)	(0.75)	(0.72)	(2.02)
Tax	(1.84)	(0.01)	-	(1.85)
Sub Total – adjusted building blocks	+24.01	+16.75	+11.84	+52.60
Revenue Over recovery (from years 1-3) <sup>2</sup>	(4.41)	(4.41)	(4.41)	(13.23)
Opex under recovery (from years 1-3 pressures) <sup>2</sup>	+21.92	+21.92	+21.92	+65.75
Tax (from years 1-3) <sup>2</sup>	(1.28)	(1.28)	(1.28)	(3.83)
Reduction in Alpha credit	+3.71	+3.71	+3.71	+11.13 <sup>3</sup>
Sub Total – Other Revenue Adjustments	+19.94	+19.94	+19.94	+59.82
Net Revenue Adjustment	+43.95	+36.69	+31.78	+112.42

Note 1. Figures may not sum due to rounding.

Note 2. Smoothed for year 4-6 adjustment.

Note 3. Six year figure smoothed for year 4-6 adjustment.

#### Table 4.1: MTR revenue claim.

- 4.6 This claim included a range of cost items covering the full six-year price control period. Power was the most significant element representing over 100% of the overall revenue claim, as a consequence of the other elements (positives and negatives) broadly balancing out.
- 4.7 NI Water has advised that it had to use its 'loan note' facility to cover £66m of extra operating costs in years 1 to 3, as DfI only provided budget cover for the cost increase rather than any additional 'cash' budget. The fact that the power cost increase in years 1 to 3 was in excess of the 'loan note' draw down indicates that considering power in isolation would represent a conservative approach to assessing the net negative revenue impact being experienced by NI Water. Based on the information submitted this also appears to be the case for the final three years of PC21.
- 4.8 As a result of this, and in line with the established principle that the Mid-Term Review should only re-open material issues and retain the integrity of the PC21 Final Determination as far as possible, the decision was taken that the draft determination assessment would only consider NI Water's power claim. As indicated above this simplified approach is marginally beneficial to NI Water for the period considered.

- 4.9 Whilst NI Water used its 'loan note' for meeting power costs in years 1 to 3, it has made the case that this is not sustainable moving forward. Its reasoning is that the additional borrowing has eroded any headroom remaining within the current 'loan note' facility and that it needs to repay this. It also highlighted the ongoing interest associated with the debt, the risk of the 'loan note' being breached before the end of PC21 if it is not replenished and that tariffs had become 'unreflective' as they do not account for the impact of the additional power costs. This remains the company's position.
- 4.10 Our intention was that the Mid-Term Review operating cost considerations should be forward looking rather than retrospective. For the draft determination we have therefore only considered the impact of the increase in power costs for the final three years of PC21.
- 4.11 NI Water based its power costs for the final 3 years of PC21 on the following assumptions:
- Volume of c293GW as per Budget 2023-24;
  - NI Water's new contracting arrangement from 1 October 2023 which moved to a SMP Day Ahead Electricity Product; and
  - Regulated Charges increasing by 6% in each of the years.
- 4.12 This resulted in cost projections of £54.4m, £50.9m and £48.7m for 2024-25, 2025-26 and 2026-27.
- 4.13 For our PC21 Mid-Term Review assessment we firstly considered whether NI Water was taking reasonable steps to minimise cost increases, within the constraints of the local market and its governance/purchasing arrangements. Through information requests and engagement we concluded that NI Water's electricity procurement processes were robust, that it had established contracts which were very keenly priced and that it was actively trying to reduce demand, all of which was helping to limit cost increases and expenditure.
- 4.14 Having established that NI Water was taking reasonable steps to minimise cost increases, we undertook an independent assessment of projected power costs. Our analysis used data from the UR's Retail Market Monitoring function, alongside publicly available information on the historical prices in the SEM Day-Ahead Market (DAM) and formulae published by the SEM Committee, to develop an independent estimate of the expenditure the company is likely to face in the final three years of PC21.
- 4.15 Our analysis resulted in forecast expenditure estimates which were £2.9m per annum (in 2018-19 prices) lower than the figures submitted by NI Water.

The variance was primarily a result of downward movements in forward commodity prices which would not have been visible to NI Water at the time of their submission.

- 4.16 We have therefore deducted this figure from NI Water’s submitted power costs to establish revised revenue adjustment figures for our Mid-Term Review Draft Determination. Table 4.2 below shows the annual uplift that needs to be applied to the PC21 Final Determination allowances based on the outcome of our assessment.

Power (2018-19 £m)	2024-25	2025-26	2026-27	PC21
FD – Allowance	30.34	30.34	30.34	91.02
NI Water MTR submission	54.35	50.85	48.66	153.86
MTR – Assessment	51.45	47.95	45.76	145.17
MTR – Revenue Uplift from FD Allowance	+21.11	+17.61	+15.42	+54.15

Note 1. Figures may not sum due to rounding.

**Table 4.2: Power variance uplift applied in Mid-Term Review.**

- 4.17 NI Water also proposed implementing a true-up mechanism to account for any further Revenue changes in the second half of PC21. This has not been adopted in the Mid-Term Review on the basis as we consider that introducing a new mechanism at this point of the PC21 process would not be proportionate.
- 4.18 We will review how we treat power as part of PC27 price control process, including how it is treated within our Real Price Effect (RPE) assessment methodology.

### **Tariff adjustment**

- 4.19 The PC21 Mid-Term Review allowed for a review of tariffs if this was considered necessary. We have accepted NI Water's request to do so as a consequence of the scale of the increase in power costs experienced by the company and have used the revised financial model submitted by NI Water to re-assess K-Factors.
- 4.20 Through this re-modelling, we have derived annual charge caps for each of the 7 revenue groups as shown in Table 4.3 below. The price limits are shown in real terms (i.e. excluding inflation).
- 4.21 The overall revenue requirement has been allocated to revenue groups on the basis of volumes of water consumed or sewage returned using the same assumption used in the PC21 Final Determination.

PC Stage	Revenue Group	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
PC21 FD (Table 2.6)	Domestic unmeasured water	-1.7%	1.0%	0.9%	0.9%	0.9%	0.9%
	Domestic unmeasured sewerage	-1.7%	-0.4%	-0.4%	-0.4%	-0.4%	-0.4%
	Non-domestic measured water	-1.8%	-1.8%	-1.8%	-1.8%	-1.8%	-1.8%
	Non-domestic measured sewerage	-1.7%	-0.9%	-0.9%	-0.9%	-0.9%	-0.9%
	Non-domestic unmeasured water	-1.5%	0.2%	-0.3%	-0.2%	-0.1%	0.0%
	Non-domestic unmeasured sewerage	-1.5%	0.2%	-0.3%	-0.2%	-0.1%	0.0%
	Trade effluent	-1.7%	1.5%	1.5%	1.5%	1.5%	1.5%
	<b>Overall K factor (or WACI)</b>	<b>-1.7%</b>	<b>0.0%</b>	<b>0.0%</b>	<b>0.0%</b>	<b>0.0%</b>	<b>0.0%</b>
MTR Submission (Table 6.14)	Domestic unmeasured water	As per annual tariffs			5.4%	5.4%	5.4%
	Domestic unmeasured sewerage	As per annual tariffs			3.6%	3.6%	3.6%
	Non-domestic measured water	As per annual tariffs			3.0%	3.0%	3.0%
	Non-domestic measured sewerage	As per annual tariffs			3.8%	3.8%	3.8%
	Non-domestic unmeasured water	As per annual tariffs			4.6%	4.7%	4.8%
	Non-domestic unmeasured sewerage	As per annual tariffs			5.2%	5.3%	5.4%
	Trade effluent	As per annual tariffs			6.1%	6.1%	6.1%
	<b>Overall K factor (or WACI)</b>	As per annual tariffs			<b>4.3%</b>	<b>4.3%</b>	<b>4.3%</b>
MTR DD	Domestic unmeasured water	As per annual tariffs			5.4%	5.4%	
	Domestic unmeasured sewerage	As per annual tariffs			4.3%	4.3%	
	Non-domestic measured water	As per annual tariffs			3.0%	3.0%	
	Non-domestic measured sewerage	As per annual tariffs			3.9%	3.9%	
	Non-domestic unmeasured water	As per annual tariffs			4.7%	4.8%	
	Non-domestic unmeasured sewerage	As per annual tariffs			5.4%	5.5%	
	Trade effluent	As per annual tariffs			6.1%	6.1%	
	<b>Overall K factor (or WACI)</b>	As per annual tariffs			<b>4.6%</b>	<b>4.6%</b>	

**Table 4.3: K factors by Revenue Group.**

4.22 It can be seen that NI Water’s Mid-Term Review submission had an overall annual Weighted Average Charge Increase (WACI) of 4.3% for each of the last three years of the price control. In the intervening period, the 2024-25 tariffs have been set using the PC21 Final Determination price limits and it was agreed that any adjustments from the Mid-Term Review determination would be applied to the final two years’ tariffs.

4.23 In our draft determination we adjusted the company's revenue claim to allow only Power costs based on our forecast estimates for the final three years of the price control period. This reduced the mid-term revenue uplift from £112m, as requested by NI Water, to £54m (in 2018-19 prices).

- 4.24 This £54m uplift and the Net Present Value was applied to the final two years of the price control period in the model. In addition, we adjusted the 2024-25 tariffs to actuals and adjusted inflation to November 2023 OBR annual figures.
- 4.25 The outcome of these adjustments is an overall WACI of 4.6% in real terms which is to be applied in 2025-26 and 2026-27 as can be seen in Table 4.3 above.



## 5. Capital Investment

- 5.1 NI Water invests capital expenditure to maintain its existing assets, meet more demanding quality obligations, provide extra capacity for growth and improve the service that it currently provides to consumers.
- 5.2 Our PC21 Final Determination included allowances which we had assessed as being required to meet the established needs for the price control period based on the information available at the time. This aligned with the aims and priorities set out in the Department's Social and Environmental Guidance, including the formulation of a deliverable and affordable plan.
- 5.3 Our PC21 Final Determination however also included the provision for a PC21 Mid-Term Review due to uncertainty over certain elements of the investment programme and set out our proposals for the review, including the extent and scope of the work that we anticipated undertaking.
- 5.4 For capital expenditure we indicated that we were not minded to reopen our PC21 final assessment of capex cost efficiencies or to undertake a wholesale review of the investment proposals. We have followed this principle when undertaking our Mid-Term Review and have limited our considerations to the areas detailed below.

### Scope Uncertainty in the capital programme

- 5.5 In our PC21 Final Determination we noted that the majority of the schemes in NI Water's wastewater treatment (SP16) and sewerage (SP12) sub-programmes were insufficiently developed from a scope/cost perspective to allow them to be determined at that time.
- 5.6 For the PC21 Final Determination we therefore made provision for NI Water to undertake the work needed to establish an efficient scope and cost for these schemes, so that a determination could be undertaken as part of the Mid-Term Review. This included:
- The company's Drainage Area Plans and integrated environmental studies needed to identify solutions to major drainage issues; and,
  - The future consents and catchment studies needed to identify appropriate solutions for wastewater treatment and sewerage system upgrades.
- 5.7 In the interim, our PC21 Final Determination included a 'holding' allowance for these schemes. This ensured that price limits and capital budgets made

some provision for the necessary work while the efficient solutions were being developed.

5.8 At the time, NI Water provided a list of the wastewater treatment and sewerage projects where further development work was necessary to allow an efficient scope and cost to be established. It also submitted a programme which would allow the cost of these schemes to be determined at the PC21 Mid-Term Review.

5.9 The 'cost certain' information for these schemes was submitted by the company in four batches between September 2021 and March 2023. This is summarised in Table 5.1 below. This shows that the overall cost increased significantly compared to the estimate included in the PC21 Final Determination.

	No. SP12	No. SP16	Orig SP12 IPAC cost £m	Orig SP16 IPAC cost £m	Subm SP12 cost £m	Subm SP16 cost £m	Total cost change £m
Batch 1 submission total	9	0	16.177	0.000	17.926	0.000	1.749
Batch 2 submission total	14	8	19.150	46.035	44.827	68.916	48.558
Batch 3 submission total	25	4	39.386	18.560	52.153	30.299	24.506
Batch 4 NIAMP5 submission total	24	16	46.820	88.760	19.379	124.806	8.605
Batch 4 LWWP submission total <sup>2</sup>	55	12	180.252	305.513	130.222	555.741	200.198
Batch 1-4 total <sup>2</sup>	127	40	301.785	458.867	264.507	779.762	283.616
Total	165 <sup>2</sup>		760.652		1044.269		283.616

Note 1. Figures may not sum due to rounding. All costs are in 2018-19 prices (pre efficiency) unless stated otherwise.

Note 2. There are 2 projects allocated to both SP12 and SP16, costs have been split equally across both SP's.

**Table 5.1: Scope certainty submissions Batch 1-4 summary.**

5.10 As part of the Mid-Term Review process, the selections of projects and the associated costs were refined further by NI Water. This resulted in the company resubmitting a consolidated list containing updated cost data in Annex E of its Mid-Term Review submission.

5.11 During our assessment of the company's submissions, we found that NI Water had included 19 additional projects in both its scope certainty and Annex E submissions. These were not in its original list of scope uncertain schemes and so we consider them to have been subject to determination as part of the original PC21 process. As a result, we have excluded them from our Mid-Term Review assessment and intend to deal with any cost variances through the standard logging up/logging down process at the end of the PC21 period.

5.12 Table 5.2 shows the Annex E submission figures following our exclusion of the 19 projects and compares this to the original Annex E submission, the total collated cost of NI Water's scope certainty submissions and our original PC21 'holding' allowance.

	No. SP12	No. SP16	SP12 cost £m	SP16 cost £m	Total cost £m
FD – SC projects	123	23	275.1	370.2	645.4
Scope certainty submissions <sup>2</sup>	127	40	264.5	779.8	1044.3
Annex E SC lines as submitted	125	40	330.8	660.2	991.0
Annex E SC lines excl 19 projects	123	23	319.4	514.6	833.9

Note 1. Figures may not sum due to rounding. All costs are in 2018-19 prices (pre efficiency) unless stated otherwise.

Note 2. There are 2 projects allocated to both SP12 and SP16, costs have been split equally across both SP's.

**Table 5.2: Scope certainty projects cost change by submission.**

5.13 As part of our assessment process, we asked the Reporter to carry out an independent review of the proposed solutions and costs for a sample of the company's Annex E schemes.

5.14 The aim was to check if the solution chosen was reflective of need and represented the least cost option, whether value engineering had been undertaken to help minimise costs and if any scope risk applied was reflective of the improved confidence in the solutions.

5.15 A summary of the Reporter's audit and the resulting cost challenges, based on the original list of scope certainty projects, is shown in Table 5.3.

	LWWP	NIAMP5	CCP	Total
Number of sample projects	6	15	3	24
Sample projects cost	371.0	118.7	22.6	512.3
Challenge validity of specific cost lines	33.3	1.4	0.0	34.7 (6.8%)
Challenge other miscellaneous costs	9.9	7.8	0.0	17.8 (3.5%)
Total Reporter cost challenge	43.2	9.3	0.0	54.4 (10.2%)

Note 1. All costs are in 2018-19 prices (pre efficiency) unless stated otherwise. Figures may not sum due to rounding.

Note 2. Living with Water Programme (LWWP); NI Water Asset Management Plan 5 (NIAMP5); Change Control Protocol (CCP).

**Table 5.3: Reporter's scope certainty cost challenge.**

5.16 It can be seen that the Reporter's overall cost challenge was c£54m (10.2%) for 24 sample projects which had a total PC21 value of c£512m. This comprised of c£35m (6.8%) for cost lines/curves not supported by sufficient evidence and c£18m (3.5%) for other miscellaneous challenges, including

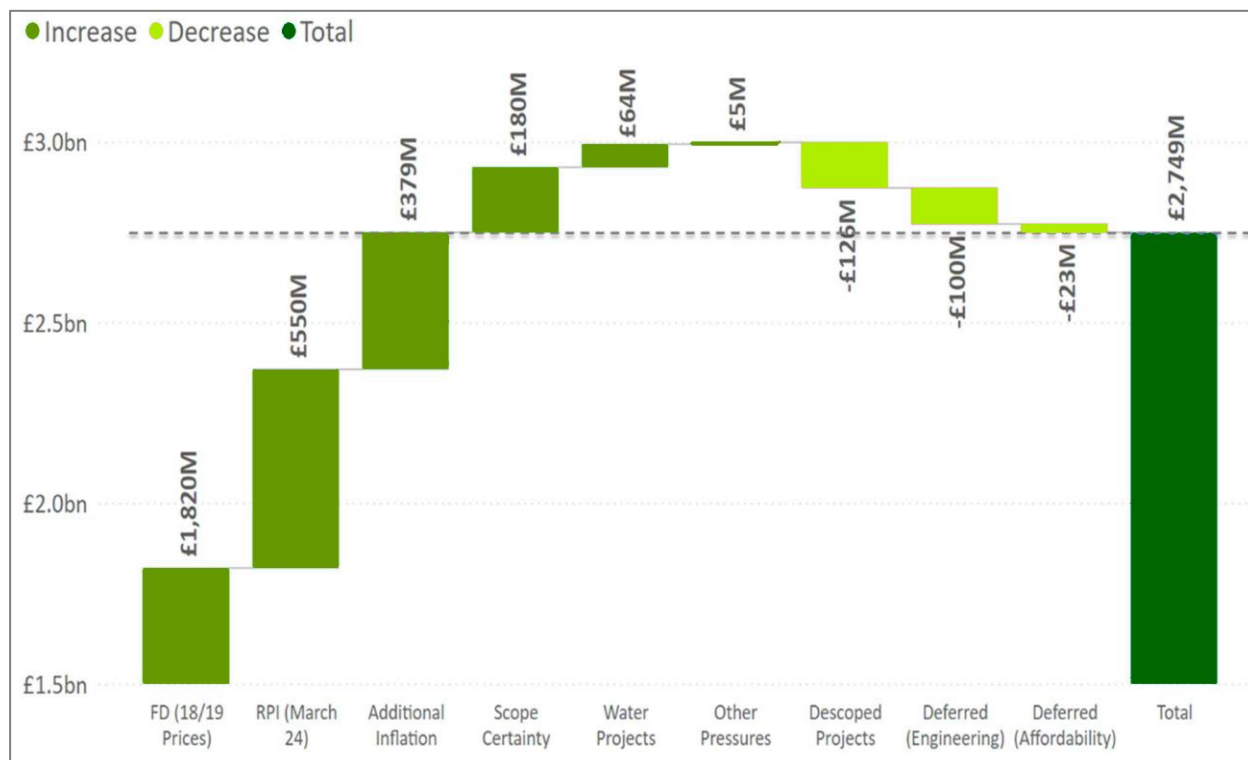
those associated with the scope risk which NI Water had applied to individual projects.

- 5.17 The Reporter's findings have been shared with NI Water and it accepts that c£6m (1.2%) of the miscellaneous cost challenge is justified. It however believes it can provide additional information to justify the inclusion of the majority of the remaining costs, including all those associated with the cost lines/curves.
- 5.18 The Reporter has advised that he is not necessarily disputing the need for the activities associated with the c£35m cost lines/curves challenge, it is just that NI Water has not provided information to justify the submitted cost. NI Water is confident it can do so and on the assumption that this is the case, we have excluded this amount from our Mid-Term Review scope certainty adjustment.
- 5.19 We have therefore only applied a reduction of 3.5% to the scope certainty projects, equivalent to the miscellaneous cost challenge identified through the Reporter's sample audit.
- 5.20 We believe that this represents a reasonable and balanced approach for the draft determination, pending NI Water's provision of further justification in advance of the MTR Final Determination. It takes account of the fact that NI Water believes it can provide justification for c£12m of the c£18m 'miscellaneous' cost challenge and that any success in doing so has the potential to balance any of the c£35m 'cost line/curve' deduction that NI Water is not able to fully justify.
- 5.21 We would however highlight that we will reinstate any Reporter cost challenges in the MTR Final Determination if the company is unable to provide sufficient evidence to refute them. On this basis, the MTR Final Determination scope certainty challenge could lie anywhere in the range between 1.2% (based on the challenge currently accepted by NI Water) and 10.2% (based on the full Reporter challenge if NI Water cannot provide justification for the costs).

### **Capital Cost Pressures above Inflation (Real Price Effects)**

- 5.22 In its Mid-Term Review submission, NI Water advised it had experienced significant construction cost pressures above inflation as a result of unprecedented economic instability since the PC21 Final Determination. It indicated that this had been driven by external factors such as Brexit, Covid19 and energy/resource inflation. It requested that these real price effects (RPEs) be allowed as part of the Mid-Term Review.

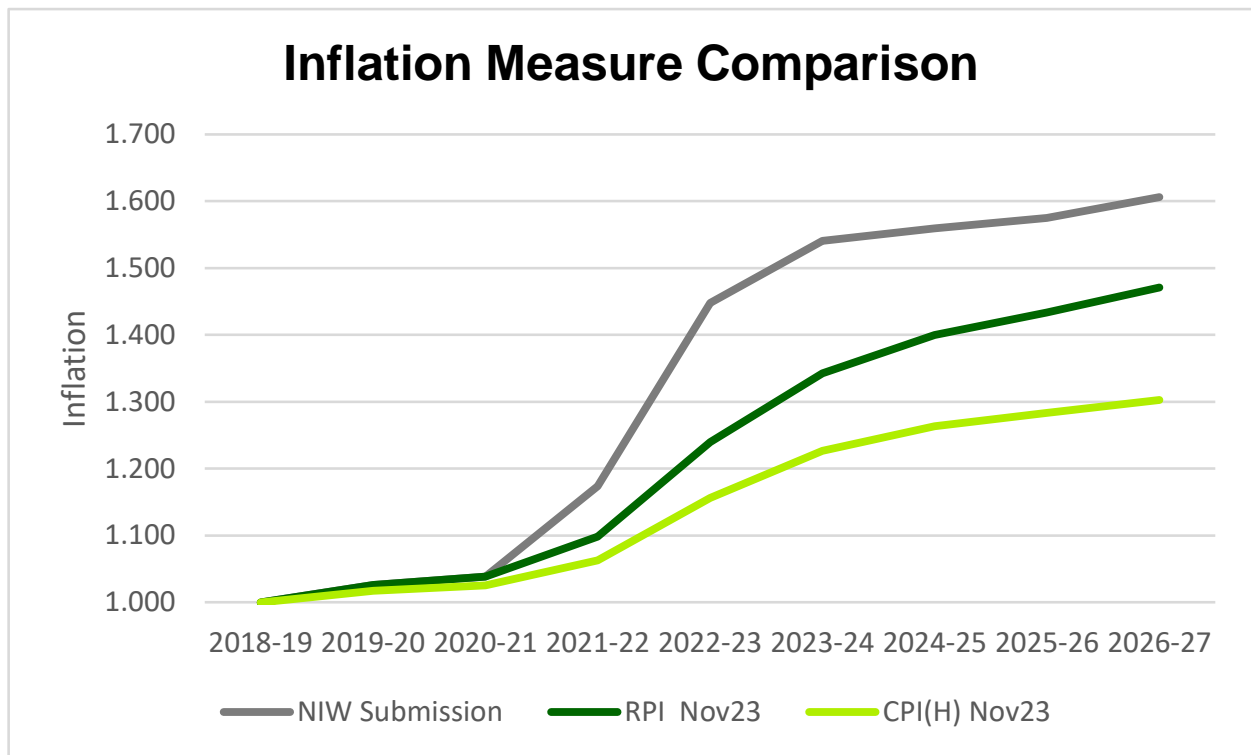
5.23 NI Water's submission included a waterfall diagram which can be seen in Figure 5.1. This separated out the various components of the company's capital funding request, which totalled £2,749m in nominal terms. It can be seen that the company's additional inflation request for RPEs was £379m above RPI, based on March 2023 Office of Budget Responsibility (OBR) RPI forecasts.



**Figure 5.1: NIW Mid-Term Review submission waterfall diagram.**

- 5.24 NI Water had estimated this Real Price Effect using a new detailed 'bottom up' approach, which was materially different to that used by ourselves and the company in the PC21 determination process.
- 5.25 This new NI Water analysis resulted in estimates of inflation of 13.0% and 23.4% for 2021-22 and 2022-23, which were around 7% and 11% higher than RPI respectively. For the remaining years of the PC21 period, NI Water assumed inflation levels would revert to the forward projection of RPI based on March 2023 OBR data.
- 5.26 The effect of this analysis and the extent to which NI Water's assessed figures exceed the RPI and CPI(H) figures published by OBR (based on November 2023 OBR data) can be seen in Figure 5.2.
- 5.27 Based on an approximation, we estimate that OBR's CPI(H) figures would need to be increased by c25% to match NI Water's. This conclusion is surprising, considering the fact that the published inflation figures (including

the construction PAFI indices that NI Water has materially adjusted in its assessment) are intended to capture and allow for inflationary impacts.



**Figure 5.2: Comparison of NIW measured inflation to RPI and CPI(H).**

5.28 NI Water provided the analysis used to determine its inflation figures as part of its Mid-Term Review submission. Our initial observations were that the adopted approach was complex, involved extensive data manipulation and adjustment of published inflation data, had the potential to be selective and was based on a small number of projects. This raised concerns in relation to the confidence that could be placed on the conclusions and the extrapolation of the findings to the entire investment programme.

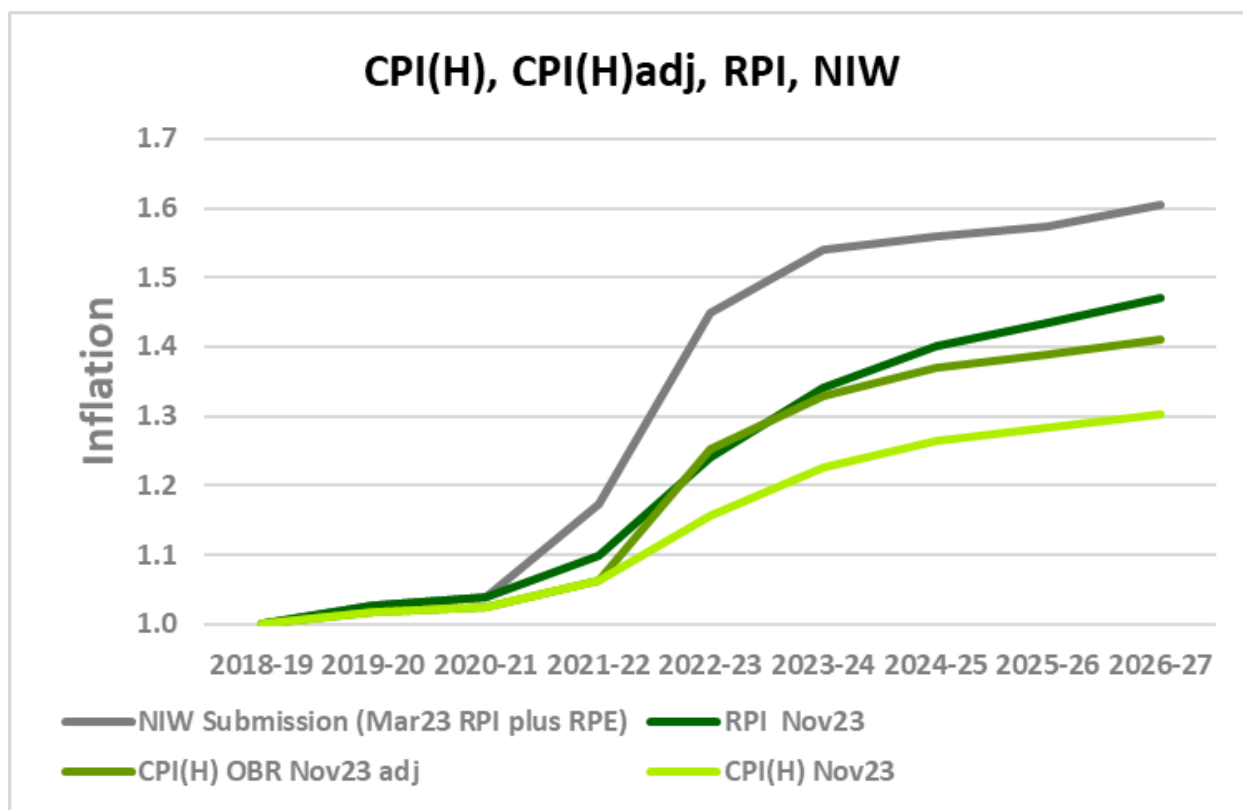
5.29 As a result, we decided to consider NI Water’s request from a range of different perspectives as described below.

5.30 We 'refreshed' the original PC21 RPE calculations using updated inflation figures and input price indices and tested various combinations. These included:

- Repeating the PC21 UR approach for frontier shift.
- Repeating the PC21 NIW approach for frontier shift.

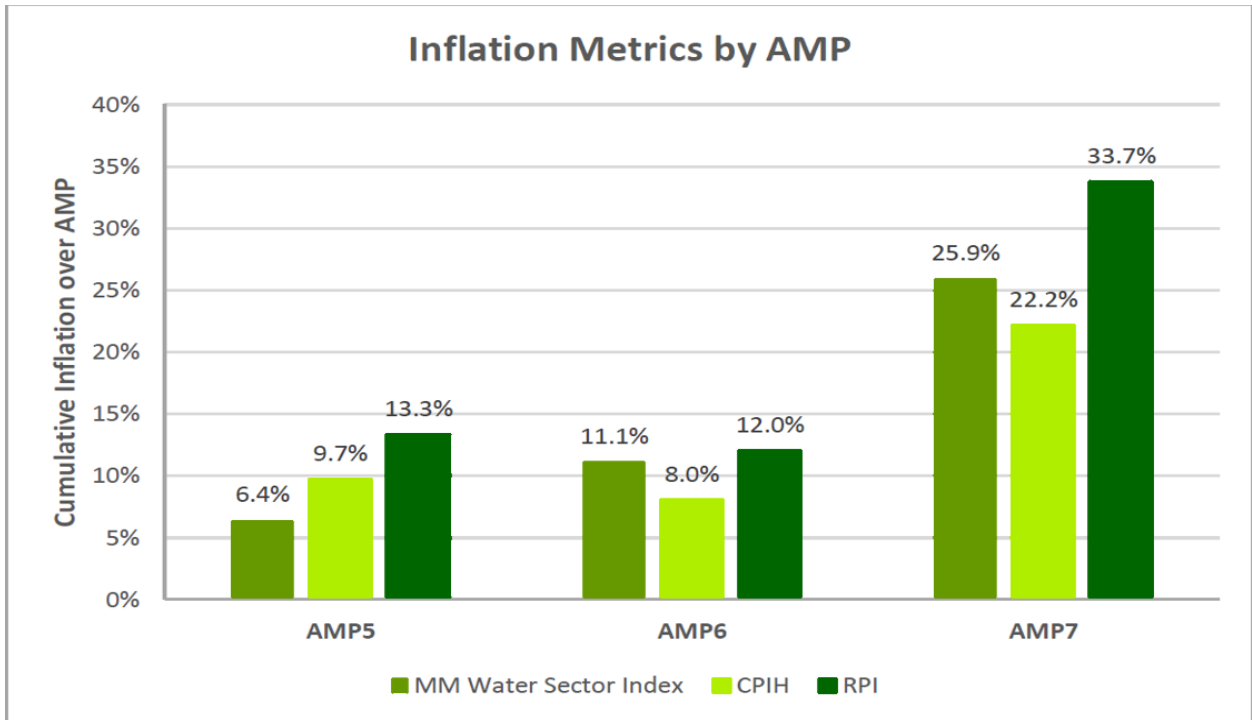
5.31 These analyses estimated RPEs which were below RPI.

5.32 We sense checked NI Water's figures against the CPI(H) adjustments allowed in our GD23 determination. We did so by approximating the effect on the November 2023 OBR CPI(H) trend line. This can be seen in Figure 5.3 below.



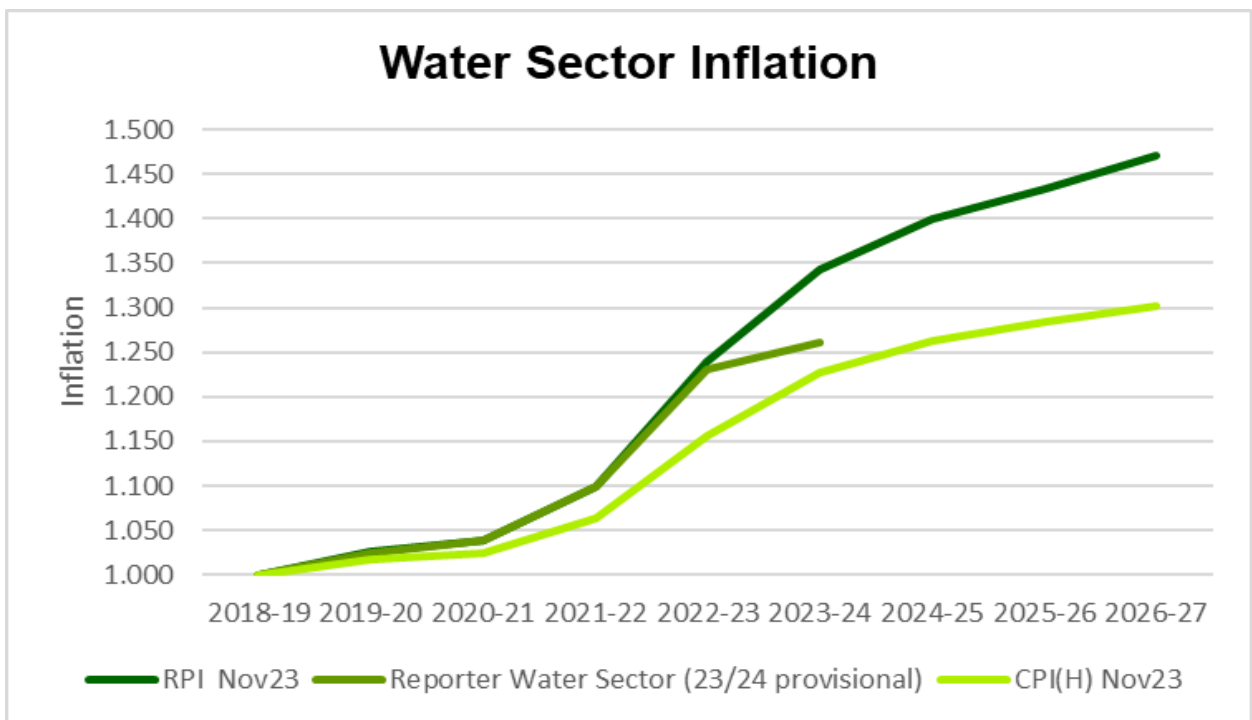
**Figure 5.3: Comparison of water sector inflation to adjusted CPI(H).**

- 5.33 This analysis only resulted in the adjusted CPI(H) figures marginally exceeding RPI in one year rather than exceeding it materially on a consistent basis.
- 5.34 We commissioned an independent review by the Reporter which provided access to cost estimation expertise, direct knowledge of company requests being made as part of the Ofwat PR24 process and an extensive database (c£800m) of water sector specific cost data from England and Wales (E&W).
- 5.35 The Reporter provided an analysis of inflation in the water sector in E&W over the long term for the Asset Management Periods AMP4-AMP7 covering the years 2005-25, as shown in Figure 5.4. This illustrates that RPI has consistently exceeded cost increases in the E&W water sector.



**Figure 5.4: Long term water sector inflation - Reporter (Mott McDonald).**

5.36 The Reporter also provided a shorter term analysis which can be seen in Figure 5.5 below. This indicates that the E&W water sector cost data did not materially exceed RPI at any point within the period and that it is not reflective of NI Water’s inflation data.



**Figure 5.5: Comparison of water sector inflation to RPI and CPI(H).**



- 5.37 While the Reporter data included in the figures above applies to E&W, we have consistently found in our price control determinations that construction costs in Northern Ireland are lower than the overall United Kingdom average.
- 5.38 NI Water suggested this might have changed due to the localised impact of Brexit. We therefore undertook a regional construction price sense check by considering more recent data sourced from two public websites<sup>7</sup>. These quoted figures of 75% and 82% for Northern Ireland, which compares to the PC21 Final Determination range of 87%-94%. This exercise therefore did not support any change to our previous conclusions.
- 5.39 We also sense checked the scale of increase proposed by NI Water against the uplift that would be provided by RPI. We found that November 2023 OBR RPI figures would already allow a £650m (36%) increase against the PC21 Final Determination real price figure of £1.82bn and that NI Water's figures would equate to a 50% increase.
- 5.40 NI Water's request suggests that the extra £650m that the November 2023 OBR RPI figures already allow, would need to be uplifted by a further 43% to match NI Water's figures. We are not aware of any other independent sources of information which would support this assertion.
- 5.41 Based on the outcome of the above tests/checks we have concluded that RPI continues to provide sufficient headroom for water sector inflation. We have therefore excluded NI Water's Real Price Effect claim (equating to £279m based on November 2023 OBR data) as we have not found any independent sources of information which support it.
- 5.42 NI Water is aware of our MTR Draft Determination conclusion and has indicated it will be seeking to provide further evidence prior to the MTR Final Determination to support its position.

### **Base maintenance investment**

- 5.43 A major component of NI Water's capital programme is the investment needed to maintain its existing assets and the service they deliver. This equates to approximately 40% of the company's total capital budget and is referred to as base maintenance.
- 5.44 In line with consumer expectations and the requirements of the S&EG, the established policy is that base maintenance allowances should be maintained as a priority when faced with any budgetary pressures.

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<sup>7</sup> <https://costmodelling.com/regional-variations>  
<https://constructioncosts.eu/cost-index/united-kingdom/>

- 5.45 This principle is intended to ensure that there is no overall deterioration in the asset base and the associated level of service provided to existing consumers. We have continued to apply this principle in the Mid-Term Review.
- 5.46 The company has made the case that its base maintenance costs have increased in PC21 due to the impact of RPE cost pressures above inflation. However, as indicated above, our draft determination conclusion is that the general measure of inflation (i.e. RPI) should provide sufficient headroom for water sector cost rises and so we do not believe that any adjustment to base maintenance is required at the Mid-Term Review.
- 5.47 The extension of this conclusion is that we do not consider the company's proposal to use the PC21 Regulatory Depreciation allowance to meet this cost pressure to be necessary. We therefore expect this allowance to be used for its original purpose.

### **Enhancement investment**

- 5.48 The remainder of the capital budget is allocated for enhancing NI Water's assets to deliver improvements for consumers. This includes meeting enhanced quality obligations, providing extra capacity to accommodate growth/development and improving the service provided to consumers (for example by reducing incidents of low pressure or flooding).
- 5.49 The established principle of prioritising base maintenance expenditure means that any budgetary pressures primarily impact the enhancement element of the budget and the associated improvements that this was intended to deliver for consumers. Furthermore, in line with the established principles of prioritising drinking water investment within the enhancement budget, any impacts would be expected to mainly affect wastewater investment and more specifically the Unsatisfactory Intermittent Discharge (UID) programme.
- 5.50 In the Mid-Term Review we have evaluated various aspects of the enhancement programme. Our conclusions are summarised in Table 5.4 below and these have been taken into account in coming to our final assessment for the Mid-Term Review.

Enhancement programme investment aspect	Conclusion on potential impact
The work undertaken to review and revise the prioritised list of wastewater outputs because of the scope certainty submissions	We have accepted NI Waters prioritised list as the best available. We recognise that NI Water continues to work with NIEA to confirm the list.
Any change controls that have been submitted/approved	The Reporter assessed the solution and associated costs included in CCP1-3 and we have updated the enhancement element of the costs as part of the Mid-Term Review.
The impact of cost pressures above inflation	Our assessment concludes that general inflation (RPI) provides sufficient headroom and that costs above inflation (RPEs) are not present when measured against RPI.
Additional outputs that can be delivered as a consequence of any cost challenges applied	We have updated the list of outputs as a result of the scope certainty submissions
The outcome of our assessment of the business cases submitted by NI Water for expenditure areas where approval for continued investment for the remainder of period is dependent on proof of benefit	NI Water have successfully demonstrated the need for continued investment in the remainder of the price control.

**Table 5.4: Enhancement programme investment aspect consideration.**

## Change control projects

- 5.51 It is recognised that there can be a need to make changes to the planned delivery programme during a price control, for example as a result of changing regulatory standards or quality regulator enforcement.
- 5.52 Our established regulatory processes already include a formal Change Control Protocol which allows these changes to be accommodated and managed. This sets out the procedures and steps that key stakeholders have to follow to control changes to outputs. It provides a structured framework for managing changes and ensuring they have been agreed by stakeholders.
- 5.53 NI Water submitted three change controls in the first half of PC21. These were accepted by all key stakeholders (subject to Utility Regulator cost assessment) on the basis that they were needed to meet either key water quality or supply resilience drivers.
- 5.54 The additional enhancement budget allowances requested for these change controls in the mid-term submission are detailed in Table 5.5 below. The table also includes some 'balancing' budget reductions, which result from some of the original PC21 Final Determination allocations having been replaced by the change control proposal or no longer being required due to project delays. The figures included in the table only relate to the enhancement element of the budget because the base maintenance allocation for all capital investment is set as a single allowance for the price control and is therefore already covered. As a consequence, we only need to adjust the enhancement budget in the Mid-Term Review.

Enhancement costs variance for change control projects	Project ref	PC21 enhan £m	Mid-Term Review enhan £m	Variance £m
CCP001 Derg				
Derg Treatability Improvements	1927, JN562	2.8	7.2	4.5
Derg WTW MCPA PEO Undertakings	JN538	4.9	3.7	-1.2
CCP002 Ballinrees				
Ballinrees WTW, MCPA treatment investigations	JL795, JA341	4.3	14.8	10.5
Pilot Plant Studies 2022/23	JI280		0.9	0.9
CCP003 Beltoy - Unagh				
Beltoy / Unagh WPS	JI212		1.6	1.6
Caugh Hill, Carmoney to Strabane Strategic Link Watermain	JL715	17.8	12.2	-5.6
CCP001, CCP002 and CCP003				
Total		29.7	40.4	10.6

Note 1. All costs are in 2018-19 prices (pre efficiency) unless stated otherwise. Figures may not sum due to rounding.

#### Table 5.5: Change control protocol projects.

- 5.55 The Reporter reviewed the business cases for these change control projects as part of his wider Mid-Term Review audit and has confirmed that NI Water's proposed solutions are appropriate. We have therefore included the enhancement element of the costs in our Mid-Term Review capex allowance and deducted any balancing budgets linked to the original PC21 investment proposals accordingly.
- 5.56 The outcome is a net increase of £10.6m in the required capex allowance when expressed in 2018-19 prices.

#### Mid-Term Review Capex conclusion

- 5.57 Our reassessment of the overall PC21 Capex requirement for the PC21 period is £1.75bn in 2018-19 prices. This accounts for the removal of the RPE claim, the deduction of 3.5% from the scope certain scheme costs and the inclusion of the change controls driven by in-period quality and resilience requirements. This 'real price' requirement is £65m less than the PC21 Final Determination figure of £1.820bn.
- 5.58 This reduction is primarily a result of the removal of projects that are no longer required, are undeliverable or have been deferred due to delivery costs being prohibitive.

- 5.59 The most significant impact in relation to funding requirements results from RPI being much higher than anticipated at the time of the PC21 Final Determination. This has increased the nominal budget requirement from the PC21 Final Determination estimate of £2.086bn (based on March 2021 OBR forecast) to an estimated £2.389bn (based on November 2023 OBR figures/forecast). This represents an increase of £303m (c15%) compared to the PC21 Final Determination nominal budget estimate but represents a c13% reduction when compared to the figure of £2.749bn submitted by NI Water.
- 5.60 We note that OBR has published a further RPI inflation dataset (i.e. March 2024) since we completed our Mid-Term Review analysis. We therefore plan to update our inflation assumptions using this updated data for the MTR Final Determination to ensure our projections are as accurate as possible.
- 5.61 Table 5.6 below summarises the outcome of our financial assessment in real and nominal terms and includes the PC21 Final Determination figures for comparison.

	Real 2018/19 price			Nominal			OBR RPI Inflation source
	Base	Enhan	Total	Base	Enhan	Total	
FD – Gross capex	715.040	1104.558	1819.598	816.238	1270.120	2086.358	Mar 21
Scope certainty projects	715.040	1028.474	1743.513	965.950	1410.781	2376.731	Nov 23
CCP1-3 adjustment	0.000	10.636	10.636	0.000	12.677	12.677	Nov 23
MTR – Gross capex	715.040	1039.109	1754.149	965.950	1423.458	2389.408	Nov 23
Variance from PC21 FD			-65.449			303.050	

Note 1. Figures may not sum due to rounding.

**Table 5.6: Mid-Term Review gross capex requirement.**

## 6. Implications for Public Expenditure

- 6.1 This section sets out how our allowances translate into the mechanisms which Government use for allocating public expenditure (PE).
- 6.2 NI Water does not charge domestic customers directly for the services they receive. The domestic consumer charge and the domestic allowance for commercial consumers is therefore met by Government subsidy through PE mechanisms. This subsidy is provided annually in nominal, or cash, terms and represents about 80% of the funding that the company receives.
- 6.3 NI Water is classified as a Non-Department Public Body (NDPB) as a consequence of receiving this level of subsidy and is required to operate within PE limits as a result. PE limits, also known as Departmental Expenditure Limits (DEL), are subdivided into operating costs (Resource DEL) and capital costs (Capital DEL).
- 6.4 Inflation has an impact on the money that NI Water needs to spend in nominal, or cash, terms in each year to operate its business and deliver its planned investment. As future levels of inflation are not known at the time of our price control determinations, we use costs expressed in the price base for a particular year to ensure all our financial assessments are undertaken on a consistent, like for like, basis. For our PC21 determination we used a price base of 2018-19.
- 6.5 We then use the most recent published inflation projections to estimate what this might represent in annual nominal budgets for the price control as a whole. The nominal budget requirements stated in our determinations can therefore only be considered as indicative until actual annual levels of inflation are known. This is why we allow our annual revenue allowances to be uplifted by the latest RPI figures annually through the scheme of charges process.
- 6.6 In simple terms, if inflation has been higher than assumed in the PC21 Final Determination, NI Water will require more money in each year than originally estimated to deliver the same level of service and the same number of outputs.
- 6.7 This is of particular importance to Dfl, as the impact of inflationary movements not only has implications for non-domestic charges, but also the public expenditure budget that the Department provides on an annual basis in lieu of domestic charges.
- 6.8 Our PC21 determination used the latest Retail Price Index inflation forecasts published by the Office of Budget Responsibility (OBR) available at that time

(i.e. March 2021). For the Mid-Term Review assessment we have used the latest RPI forecast figures that were available when we were undertaking our analysis (i.e. November 2023). This has allowed us to provide a more up to date assessment of the ongoing nominal budget requirements.

- 6.9 The following sections explore the implications of our Mid-Term Review assessment in terms of Resource DEL and Capital DEL budgetary requirements (i.e. the elements subsidised by Dfl).

## Resource DEL

- 6.10 The Resource DEL nominal budget estimates included in the PC21 Final Determination were based on March 2021 OBR inflation projections. The Resource DEL total was c£732m as shown in Table 6.1 below.

PE Resource DEL	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	PC21 Total
FD – Nominal OBR Mar21	122.0	120.8	119.7	119.9	122.9	126.8	732.1

Note 1. Figures may not sum due to rounding.

**Table 6.1: PC21 Final Determination Resource DEL.**

- 6.11 These PC21 Final Determination figures form the basis of our MTR Resource DEL estimates. Additional revenue has been added to the final three years of PC21 to account for the £54m power costs uplift and the additional non-domestic income arising from the MTR tariff uplift.
- 6.12 When we account for the impact of inflation (based on November 2023 OBR inflation projections) and our Mid-Term Review revenue assessment, we estimate that the public expenditure Resource DEL provision for the final three years of PC21 would need to be c£511m, as shown in Table 6.2 below. This is c£142m higher than would have been expected, based on PC21 Final Determination estimates.

PE Resource DEL	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	PC21 yrs4-6 Total
FD – Nominal OBR Mar21	-	-	-	119.9	122.9	126.8	369.6
FD – Received/forecast nominal	148.6	171.6	171.9 <sup>2</sup>	-	-	-	-
MTR – Nominal OBR Nov23	-	-	-	178.3	168.8	164.1	511.3
Variation from FD (OBR Mar21) to MTR (OBR Nov23)	-	-	-	58.4	45.9	37.3	141.6

Note 1. Figures may not sum due to rounding.

Note 2. Provisional figure, unaudited.

**Table 6.2: MTR Public Expenditure Resource DEL Requirements.**

## Capital DEL

6.13 The Capital DEL nominal budget estimates included in the PC21 Final Determination were based on March 2021 OBR inflation projections. The Capital DEL total was c£2,050m as shown in Table 6.1 below.

PE Capital DEL	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	PC21 Total
FD – Nominal OBR Mar21	178.6	251.2	327.3	438.2	449.4	405.7	2050.5

Note 1. Figures may not sum due to rounding.

**Table 6.3: PC21 Final Determination Capital DEL.**

- 6.14 For the purposes of MTR Capital DEL budget requirement calculation, we have assumed that capital grants and contributions, residual interest and alpha PPP maintenance all remain unchanged from the PC21 Final Determination in real terms.
- 6.15 In addition we have used actual figures for the first two years of PC21 and a provisional figure for 2023-24 to calculate the balance required for the final three years of the price control period.
- 6.16 When we account for the impact of inflation (based on November 2023 OBR inflation projections), our Mid-Term Review assessment and the budget received to date, we estimate that the public expenditure Capital DEL provision for the final three years of PC21 would need to be c£1,481m to deliver the planned investment and outputs. As can be seen in Table 6.4 below, this is c£188m higher than would have been expected, based on PC21 Final Determination estimates.

PE Capital DEL	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	PC21 yrs4-6 Total
FD – Nominal OBR Mar21	-	-	-	438.2	449.4	405.7	1293.3
FD – Received/forecast nominal	222.1	290.1	337.3 <sup>2</sup>	-	-	-	-
MTR – Nominal OBR Nov23	-	-	-	464.7	556.8	459.8	1481.2
Variation from FD (OBR Mar21) to MTR (OBR Nov23)	-	-	-	26.5	107.4	54.1	187.9

Note 1. Figures may not sum due to rounding.

Note 2. Provisional figure, unaudited.

**Table 6.4: MTR Public Expenditure Capital DEL Requirements.**



## 7. Next Steps

### Consultation process

- 7.1 This PC21 Mid-Term Review Draft Determination is published as an open document for consultation. We have not posed any specific questions and instead invite consumers and stakeholders to express views on any particular aspect of the determination that they wish to.
- 7.2 The consultation period is eight weeks and so written responses should be received no later than noon on Thursday 27 June 2024. These should be addressed to:
- Paul Stewart  
Price Control Manager (NI Water Lead)  
Utility Regulator  
Queen's House  
14 Queen Street  
BELFAST  
BT1 6ER
- Tel: 028 9031 1575
- Email: [Paul.Stewart@uregni.gov.uk](mailto:Paul.Stewart@uregni.gov.uk) and  
[UREGNI\\_Water\\_Responses@uregni.gov.uk](mailto:UREGNI_Water_Responses@uregni.gov.uk)
- 7.3 Our preference is for responses to be submitted by e-mail.
- 7.4 We will publish submissions received in response to the consultation to provide a public summary of the responses received. If respondents do not wish their response or name made public, this should be stated clearly by marking the response as confidential. Any confidentiality disclaimer that is automatically produced by an organisation's IT system or is included as a general statement in its fax or coversheet will be taken to apply only to information in the response for which confidentiality has been specifically requested. Individual respondents may ask for their responses not to be published in whole or in part, or that their identity should be withheld from public disclosure. Where either of these is the case, we will ask respondents to also supply us with the redacted version of the response that can be published.
- 7.5 As a public body and non-ministerial Government Department, we are bound by the Freedom of Information Act (FOIA) which came into full force and effect on 1 January 2005. According to the remit of FOIA, it is possible that

certain recorded information contained in responses can be put into the public domain. Hence, it is now possible that all responses made will be discoverable under FOIA – even if respondents ask the Utility Regulator to treat responses as confidential. It is therefore important that respondents note these developments and in particular, when marking responses as confidential or asking the Utility Regulator to treat responses as confidential, should specify why they consider the information in question to be confidential.

- 7.6 In view of this, it would be helpful if respondents could explain to us why they regard the information they have provided as confidential in relation to the Freedom of Information Act. If we receive a request for disclosure of the information we will take full account of the explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances.

### **Timeline to completion**

- 7.7 The timetable for the completion of the Mid-Term Review is shown in Table 7.1 below. This timeline includes an 8-week consultation period on the Mid-Term Review Draft Determination. Publication of the MTR Final Determination report is scheduled for the end of August.

<b>Phase 3: Completion - publication of Mid-Term Review report and Tariff Approval</b>	<b>Date</b>
UR publishes consultation version of draft report	2 May 2024
Consultation on draft report closes	27 June 2024
UR considers feedback and produces final report	July 2024
UR Board approves final report	22 Aug 2024
UR publishes final report taking account of feedback	w/c 26 Aug 2024
NI Water submits final tariff submission for 2025-26	End Jan 2025
UR review and approval of Scheme of Charges for 2025-26	Mid Feb 2025

**Table 7.1: Mid-Term Review - timeline to completion.**