

Economy and Key Performance

We need a variety of physical assets to meet our statutory duty to provide water and wastewater services to the public and to protect the environment. Assets are the infrastructure and plant needed to run our business operations. These assets deteriorate with age and use and can require maintenance, repair, refurbishment or replacement. Sometimes alternative or additional assets may be needed to meet new demands for quality or capacity of services.

Key Performance

- **During 2000-2005 we delivered high quality water and wastewater services, with customers benefiting from price reductions. Average bills fell from £278 to £247**
- **We lead the industry in our record of reducing leakage from our water distribution system**

Past Performance and Future Plans

The annual price movement in the water and wastewater industry in the UK is set by the Office of Water Services (Ofwat) in a five-yearly review of what each company needs to charge to finance services. Part of this assessment considers our performance over the previous period (2000-2005).

Ofwat's assessment of our water service performance is currently ranked as stable and our future plans for investment aim to preserve this position. We plan to maintain current levels of service to customers and comply with standards set by the Drinking Water Inspectorate and the Environment Agency.

Ofwat assessed our wastewater treatment performance (for above-ground assets such as treatment plants) to be marginal. This can be considered as below average. Our current performance is marred by quality failures relating to the concentration of metals in the effluent. Typically, these metals are from unlicensed industrial sources. A lack of capital maintenance funding to invest over the 2000-2005 period contributed to a decline in the performance of our wastewater treatment works. We invested significantly more than determined by Ofwat in its last review.

The Office of Water Services (Ofwat) is the key regulator for the water industry (Known as the Water Services Regulation Authority from 1 April 2006)

Ofwat has a method for assessing overall service to customers so that it can compare different water companies across the UK

Ofwat takes company performance into account in setting price limits for each company

Case Study

Water Charges 2005 to 2010

Annual price movement is set by Ofwat. At the five-yearly industry review, Ofwat assesses, for each year, the amount we need to charge to finance the provision of our services and to meet our obligations. We apply the price limit according to an agreed formula laid down in our operating licence and price increases cannot, on average, exceed these amounts.

A number of factors are significant in setting price limits, including:

- Operating costs and expected annual growth in these over the five-year period

- Revenue and expected annual growth in this over the period
- Financing investment required to meet quality obligations
- Taxation

The influence of these factors has resulted in the following price profile for 2005-2010.

Economic factors apparent in 2004-2005 prevent us from being able to smooth the first year price increase.

Price profile for 2005-2010

2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	Average %
%	%	%	%	%	
12.6	3.9	3.5	5.8	2.6	5.6

Links: www.ofwat.gov.uk | www.watervoice.org.uk | www.environment-agency.gov.uk | www.water.org.uk

We also gradually increased our investment maintaining these works over the last ten years. Despite this increased expenditure, monitoring demonstrates that the overall performance of our wastewater treatment works is not yet stable.

The necessary improvement can only be achieved through an increase in the level of replacement and refurbishment of our assets. This requires capital maintenance investment over 2005-2010. Ofwat consider our below-ground wastewater assets, such as our sewerage network, to be stable and our investment in 2005-2010 will maintain this position.



The control room at Eastbourne Wastewater Treatment Works

Key Outputs Monitored by Ofwat

Service Indicator	1997-1998	2001-2002	2002-2003	2003-2004	2004-2005
Water Pressure: % properties receiving low water pressure	0.08	0.06	0.05	0.05	0.05
Supply interruptions (aiming for low score)	0.40	0.67	0.30	0.38	0.35
Restrictions on water use	0	0	0	0	0
Billing contacts (% dealt with in five working days)	95.7	98.4	98.3	99.3	100
Response to written complaints (% dealt with in ten days)	99.2	99.8	99.9	100	100
Bills for metered customers (% with reading)	99.7	99.8	99.7	99.9	99.9
Telephone contact (% calls answered in 30 secs)	88.4	91.6	92.6	95.31	95.0
Properties flooded due to overloaded sewers (number of incidents)	N/A*	42	40	28	15
Properties flooded due to other causes (number)	300	233	299	202	277

* Not Applicable; indicator not used by Ofwat in 1997-1998.
130 properties flooded due to overloaded sewers in 1997-1998

Capital maintenance is the total cost of the work required to preserve replace, our infrastructure to ensure continued customer service

Links: www.environment-agency.gov.uk

In this section we present the principal strategies for investment in a variety of areas of our operations with environmental and social impact. For further details on investment planning for 2005-2010 please see our Monitoring Plan at www.southernwater.co.uk.

Key Performance

- **Ofwat determined that our total investment for 2005-2010 should be £1,563 million**
- **Regulatory Capital Value for 2004-2005 was £2,389 million**
- **Interest Cover for 2004-2005 was 1.8**

Funding, Investment and Planning for the Future

Our 2005-2010 financing needs are shaped by upward pressure on operating costs and our investment needs. Our total proposed investment for 2005-2010 is £1,563 million. Included in our targets for the period are some challenging efficiency targets. Customer prices need to rise by 5.6% on average each year over 2005-2010. This increase is required, in part, due to the 13% price reductions that customers benefited from in 2000-2001. In real terms, 2005-2006 customer prices will still be lower than in 1999-2000.

Drinking Water Quality

Our record of compliance with water quality standards is among the highest of the water service companies. This has been achieved with sustained investment of capital maintenance.

We have agreed programmes of work with the Drinking Water Inspectorate (DWI) for the following principal areas:

- Environmental investigations into the effect of water abstractions on the environment (six studies)
- Reduction of cloudiness (turbidity) in water from a number of groundwater sources
- Reduction of nitrate concentrations in water at a number of groundwater sources

2005-2010 Capital Investment (£ million)	Water Service	Sewerage Service
Above-ground asset maintenance	102	449
Below-ground asset maintenance	97	73
Drinking water and environmental quality improvements	14	629
Growth – resources and new development	55	57
Flooding and Levels of Service		86

Environmental Quality

The Environment Agency (EA) requires us to carry out environmental quality improvements which will cost £629 million over 2005-2010. Much of this investment will deliver the requirements of the European Union Urban Waste Water Treatment Directive:

- Completion of major schemes delayed by planning and permissions from the previous investment period of 2000-2005
- Nutrient removal schemes and schemes specific to sensitive areas

The Habitats Directive will require wastewater treatment improvements at ten sites in our region. It also requires investigative studies at 19 wastewater treatment works. In addition, we will also need to invest in asset improvements to reduce the risk of negative impacts to the environment from intermittent storm discharges.

At five year intervals, Ofwat consult with other regulators such as the Environment Agency and the Drinking Water Inspectorate, to determine the future quality obligations that should be funded by water and sewerage customer charges. This is determined this with the Secretary of State for the Environment, Food and Rural Affairs

Our current five-year investment period is April 2005 - March 2010

We estimated the costs of delivering schemes and improvements necessary to achieve our future quality obligations in our Business Plan. Ofwat have now considered our Business Plan and made their final determination of customer charges. More details on our investment programme for 2005-2010 are available from our Monitoring Plan at www.southernwater.co.uk



Investment during 2005-2010 will ensure drinking water quality remains high

Growth

Major new development and growth is planned throughout our region. Implementation of Government housing policy is forecast to increase the current rate of house building by some 50 per cent.

Growth is a key issue in the already densely populated region of the South East. Existing water resources here are fully utilised. Combined with the dry conditions in our region, growth puts an additional strain on these resources. Water companies, the Environment Agency (EA) and Ofwat continue to work together on the water strategy for the South East. Excessive abstractions from aquifers (groundwater resources) can have an adverse effect on local habitats.

We continue to work with the EA to achieve a sensible balance between the environment and our customer needs. As this is a key issue in our region we promote demand management options in our water resources strategy before the promotion of new water abstraction schemes.

Our water strategy for 2005-2010 includes:

- Enhancements to works to secure increased capacities to meet future peak demands
- Enhancements to pipelines to secure supplies to water deficient areas in times of peak demand and to reduce leakage
- Manage demand by installing meters where there is a change of occupier in our supply areas in Sussex
- Two strategic water resource investigations to refine the medium to long-term strategy for our region. Supporting investigations will look at the supply/demand balance according to industry best practice
- A series of major studies to investigate the possible adverse effects of abstractions

We assessed the location, size and timing of new development to forecast investment for 14 locations. These were locations where we identified the capacity of strategic sewerage infrastructure as a constraint to the delivery of this development. Our policy is to require contributions from developers to pay the cost of serving new development. However, where a developer can connect to an existing sewer on their site we are not in a position to recover all costs associated with servicing the new development. Ofwat has allowed £57 million for sewerage growth through our 2005-2010 investment plan. This is the first step towards the total expenditure of around £180 million to cater for likely growth over 2005-2015.

The main points of our wastewater strategy in relation to growth for 2005-2010 are:

- Providing sewerage infrastructure to the major growth areas
- Providing capacity for the longer term
- Promoting the use of wastewater requisitions for new connections through early negotiations with developers

Flooding

Investment to reduce sewer flooding over 2005-2010 forms a principal part of the £86 million Ofwat allowed us to improve service provision. This is a substantial increase from the £1 million allocated in the 1999 price determination.

Our proposed programme of work includes 125 individual schemes that will remove 259 properties from our register of properties that are at frequent risk of internal flooding. The schemes will also prevent a further 400 external areas from flooding. The majority of these areas are gardens.

We identified schemes to be addressed using our prioritisation system. WaterVoice Southern Customer Committee approved this methodology. We devised the methodology to consider the frequency, severity and persistency of flooding against cost resolution of different schemes. This prioritisation method ensures the greatest number of customers benefit from our expenditure.

Odour

We have a number of treatment works situated in close proximity to residential areas. We reviewed the frequency and effect of odour at these sites in order to prioritise those for investment. Ofwat allocated funding for investment in odour abatement over 2005-2010 for seven of these sites.