

MD173

**TO ALL MANAGING DIRECTORS OF
WATER AND SEWERAGE COMPANIES
AND WATER ONLY COMPANIES**

17 December 2001

**FORMAT AND TIMETABLE FOR PUBLISHING FUTURE REGULATORY
CAPITAL VALUES**

The regulatory capital value (RCV) is one of the critical parameters underlying price limits. Currently only historical RCVs are disclosed each year in our annual report 'Financial performance and expenditure of the water companies in England and Wales'. The investment community have indicated that they would like future RCVs to be published. They believe that this would increase not only the transparency of regulatory decisions but also their consistency and predictability. Two water and sewerage companies have already chosen to publish future RCVs provided by Ofwat as part of the supplementary information to the final determination.

In September 2001 I wrote to you to consult on the proposal to publish future RCVs. MD172 – Publishing Future Regulatory Capital Values sought views on whether future RCVs should be published, and if so, the degree of detail which should be provided and the supporting commentary and explanation needed. We received 17 responses to this consultation; copies of which are available from the Ofwat library. A list of respondents is attached at Annex 2.

All respondents to the consultation agree that future RCVs should be published. The majority of respondents favour a rolling reconciliation of the opening and closing RCV for each year at the company level. The most favoured is option 4 of the alternatives suggested in MD172. This requires a simple explanation of the role of RCVs in price setting and the economic principles of the RCVs together with a brief description of the method of calculation and a description of the adjustments that might be made at periodic reviews.

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I therefore intend to publish, in February next year, the future RCVs for the water and sewerage and water only companies. I anticipate that this will take the form of an RD letter and will consist of:

- A reconciliation of the opening and closing RCV for each of the years from 2001-02 to 2004-05 for each company. The table in Annex 1 sets out the proposed format for this.
- A simple explanation of and commentary on the role of RCVs and their calculation. This will include a description of the adjustments to be made at periodic reviews.

A number of companies have said that they should see the information for their company prior to publication. I agree. A copy of the relevant information to be disclosed will therefore be sent to each company in January 2002. This will give companies time to consider the data fully before publication in February 2002.

I will also write to you in January 2002 on the review of the regulatory accounting guidelines and proposed changes to the regulatory accounts (following consultation earlier this year). This letter will propose that RCVs are also disclosed annually in the regulatory accounts in the same format as set out in Annex 1.

If you have any questions about this letter please contact:-

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Philip Fletcher

Format for Publishing Future Regulatory Capital Values

XXX Company Limited

(Numbers are for illustration only)

	2001-02	2002-03	2003-04	2004-05
Opening RCV	2,000	2,150	2,315	2,505
Capital Expenditure	440	480	500	515
Infrastructure Renewals Expenditure	50	60	70	80
Grants & Contributions	(20)	(20)	(25)	(25)
Depreciation	(200)	(225)	(225)	(250)
Infrastructure Renewal Charge	(70)	(70)	(70)	(70)
Outperformance of Regulatory Assumptions (5 years in arrears)	(50)	(60)	(60)	(50)
Closing RCV	2,150	2,315	2,505	2,705
Average Year RCV	2,075	2,232	2,410	2,605

All amounts are in £m and in 2000-01 prices

List of respondents to MD172

Anglian Water Services Ltd

Bristol Water plc

Bournemouth & West Hampshire Water plc

Cambridge Water plc

Mid Kent Water plc

Northumbrian Water Ltd

Portsmouth Water plc

Severn Trent Water plc

South East Water plc

South Staffordshire Water plc

Southern Water Services Ltd

Sutton and East Surrey Water plc

Thames Water Utilities Ltd

United Utilities plc

Welsh Water (Dŵr Cymru)

Wessex Water Services Ltd

Yorkshire Water Services Ltd