

# SRN-DDR-022 Business Rates Cost Evidence Case

28<sup>th</sup> August 2024



from  
**Southern  
Water** 

## 1. Introduction

In our February 2024 submission, we re-stated our business rates liability. The revision reflected revaluations due to be performed by the Valuation Office Agency (VOA) in 2026 and 2029 using the methodology applied by the VOA for previous revaluations. For the purposes of this estimation, we adopted the transitional relief methodology adopted for the most recent (2023) revaluation.

Our view is that estimating future business rates liability is the most prudent approach reflecting past revaluations and adjustments made by the VOA.

## 2. Issue

In the Draft Determination (DD) Ofwat set allowances on the basis of the rateable values set at the 2023 revaluation and the 2023-24 multiplier set by the Central Government. Ofwat did not reflected the revaluations due in 2026 and 2029 in our allowances. Ofwat also failed to reflect in our DD allowances the increases in business rates due to changes in wastewater asset stock in the period 2025-30.

Ofwat recognises that companies have limited control over business rates and goes on to advise that given the high degree of uncertainty around revaluations over the 2025-30 period, it proposes to increase cost sharing rates, so that companies recover 90% of any costs in excess of its PR24 cost allowance, and customers recover 90% of the amount by which their costs are lower than PR24 allowances.

Ofwat claims that this approach provides companies with protection from changes in business rates and retains some incentive for companies to try and minimise any future increases to business rates, while protecting customers by ensuring they share the benefits where the Valuation Office Agency reduces business rates.

## 3. Our response

Ofwat acknowledges that further revaluations are expected in 2026 and 2029. The Central List revaluation is based on a generic formula adopted by the VOA across the water industry. The VOA have advised that this formula is to be used in the 2026 revaluation.

The Central Government's standard multiplier increased in April 2024 from 51.2 to 54.6 (an increase of 6.6%). Historically, pre COVID, the Central Government increased the multiplier year on year and there is no reason for the Central Government not to resume such annual increase. Water companies cannot influence the setting of the multiplier. Though it is anticipated that increases will be in line with inflation and therefore accounted for in the inflationary provisions of the PR24 framework, this is not guaranteed, and the Central Government could see this as an opportunity to raise money by increasing the rate above inflation.

As per our response in our February 2024 submission, our assessment of the revaluation using the Central List formula, the figures submitted under PR24 amounts to an increase in business rates charge of £28.962m in 2026/27 (216%). Applying the transitional arrangements, this still amounts to an overall

increase in rates charged up to 2029 of £39.339m. Based on the same VOA formula there is a further increase in business rates charge of £9.305m in 2029, which due to the transitional arrangements for the 2026 revaluation amounts to an actual increase of £11.35m in 2029. We will provide evidence of our expected business rate liability at later date.

Ofwat recognises that companies have limited control over business rates, yet it expects companies to try to minimise any future increases to business rates. Business rates are governed by statute and the VOA, meaning that the ability of companies to minimise any future increases is extremely limited. With the significant increases in the cumulo being understood from using the VOA formula and the PR24 figures, we consider it is unreasonable for water companies to carry the cost of this increase through the AMP period and to only be able to reclaim 90% of the overall increase. This would have a huge impact on cash flow for businesses carrying the cost of significant increases during the AMP, thereby amplifying our financeability constraints. Ofwat's approach exposes companies to undue risk outside management control without providing value to customers.

To the extent that Ofwat is concerned that our proposal would disincentivise Southern Water from exercising the limited opportunity it does have to challenge the rates set by the VOA, this concern is misplaced. We already have a duty to our customers, driven through the regulatory framework, to reduce costs where possible. The significant impact of business rate increases, e.g., on cash flows is disproportionate to the minor increase in Southern's incentive to argue business rates with the VOA.

All of these provide a significant incentive to challenge the rates chargeable. This is reflected by the fact that we already proactively pursue rate savings through the VOAs Check Challenge and Appeal process and can evidence significant savings gained to date.

Any savings however need to be offset against the cost of pursuing those savings and the increase in the rates liability as a result of the building of new assets or the VOA undertaking their own re-assessment of a site. It is also anticipated that when self-assessment is introduced, this will result in a one-off increase in rates liability

## 4. Summary

In summary, we are challenging Ofwat's Draft Determination on the AMP8 allowances for business rates.

Our proposal to rectify this is as follows:

- Full account is taken within the determination of revaluations in 2023 and 2026 and we are allowed the amount as requested. This is in line with the previous valuations.
- The cost sharing mechanism is removed and a 100% pass through is provided.
- An in-period truing up of actual rates costs is undertaken following the 2026 and 2029 revaluations, instead of Ofwat's proposal for an end of AMP8 true-up.