

PORTSMOUTH WATER Ltd
CUSTOMER CHALLENGE GROUP (CCG)
MEETING HELD ON TUESDAY 24 SEPTEMBER 2013

PRESENT: Paul Barfoot (Portsmouth Water), Charles Burns (FSB), Amy Denford (Secretary), Keith Evans (Fareham Borough Council), Karen Gibbs (Consumer Council for Water), David Guest (Independent Chairman), Richard Harris (West Sussex Hospitals Trust), John Havenhand (Consumer Council for Water), David Howarth (Environment Agency), Douglas Hunt (Atkins Independent Reporter), Derek Kimber (Gosport Borough Council), Terry Lazenby (Portsmouth Water), Chris Manning (South Downs), Milo Purcell (Drinking Water Inspectorate), Kirk Phillips (Winchester City Council), Rod Porteous (Portsmouth Water), Nick Sheeran (Portsmouth Water), Gareth Simmonds (Portsmouth Water), Neville Smith (Portsmouth Water), and Jon Stuart (Havant & District Citizens Advice Bureau)

IN ATTENDANCE: Paul Le Masurier MVA Consultants

Action

Apologies: Traci Baker (Hampshire Chambers of Commerce), Jim Barker (Environment Agency), Hugh Caley (Carillion), Daire Casey (West Sussex County Council), David Collins (Havant Borough Council), Cllr Paul Dendle (Arun District Council), Marge Harvey (East Hampshire District Council), Douglas Kite (Natural England), Simon Oakley (Chichester District Council) Ian Rawson (KWS -Defence) Tim Richings and Rob Wood (Portsmouth City Council)

Minutes & Actions of Meeting Held on 15 August 2013

The minutes were taken as a correct record and approved by the CCG.

The following actions were reported on:

Customer Quantitative Research

Nick Sheeran confirmed that he had provided Doug Hunt with MVA Consultants explanation of why they included one obviously more favourable option in their Customer Research.

Company's External Assurance Process / Timetable

Nick Sheeran advised that he had received a recommendation from Doug Hunt for a Customer Research Expert to provide further assurance to the CCG.

Nick Sheeran confirmed that the proposal for further Customer Research would be reviewed at this meeting and the Sub Group would be reconvened thereafter.

Outcome and Measures of Success

Neville Smith confirmed that Carbon had now been included in the Environmental Outcome in the Business Plan.

Water Quality

Milo Purcell confirmed that he would be discussing this later in the meeting under the Water Quality item on the agenda.

Feedback to Company following Customer Challenge Group Confidential discussion

David Guest confirmed that the Company had allocated the CCG one hour on the agenda for their confidential discussion.

Rod Porteous advised that the DOM's Strategy would be covered later in the agenda.

Milo Purcell confirmed that he would discuss Water Quality risks later in the agenda.

Outstanding Issues for Review

Neville Smith advised that the following outstanding issues; Incentives, Catchment Management, Costing of Capital Schemes and Capital Maintenance, and how they relate to bills and what the Company is proposing for efficiencies would be discussed later in the agenda.

Nick Sheeran confirmed that Milo Purcell's question regarding the possibility of AMP6 expenditure being brought forward to AMP5 would be addressed later in the meeting.

Implications for Prices

Nick Sheeran confirmed that the part of the model showing the impact the assumptions have on the businesses financability was now available.

Nick Sheeran advised that Terry Lazenby's suggestions to present the Implications for Prices with Customer preferences and the Company's Outcomes for the CCG to challenge was still outstanding.

NJS

Update on External Technical Assurance Reviews

Doug Hunt advised that he will be providing the CCG with an update on assurance later in the meeting.

1. Update on Outcomes/KPI's

Nick Sheeran advised that the draft Business Plan includes the Company's final outcomes, the customer's priorities as established through research, environment, leakage, carbon footprint, water efficiency. He confirmed that this can all be achieved without increasing bills by more than inflation.

Neville Smith presented a graph highlighting that the Company's bill increases have historically been less than household income increases.

Gareth Simmonds presented to the CCG on the revised wording of the agreed Outcomes and an additional Outcome included in the draft Business Plan.

2. Draft Business Plan and Impact on Bills

Nick Sheeran circulated three versions of the draft Business Plan to the CCG, a single page summary, a 15 page summary and the full document. He advised that it was draft, subject to Board approval and therefore remains confidential until published. The documents are aimed at Customers to inform them of the highlights of the Company's proposals and ask for their feedback. He advised that it would be published on the Company's website with a Prize Draw to win £500 to encourage feedback, as this approach proved very successful in response to the Outline Business Plan 'Looking Ahead'. He confirmed that the full document will form the basis of the report being submitted to Ofwat in December.

Nick Sheeran took the CCG through the documents and requested comments by 27 September 2013.

John Havenhand recommended that under 'Our Performance' on page 4 of the summary document the tenth bullet regarding leakage needs more detail.

Derek Kimber further commented that the leakage reference has been included in

a list of positives... 'What we have done' may need to be rethought.

David Howarth commented that the Environment Agency have made it an internal rule not to use the word 'deliver'. Suggested the Company replace with the term 'What we will do', would still be consistent with the rest of the document. Nick Sheeran agreed to consider.

David Howarth suggested revising the wording of the fourth Outcome, currently states that the Company will encourage the efficient use of water by our customers, thinks it should state 'without affecting Customers lifestyle'.

Richard Harris advised that all three documents should be consistent.

David Guest commented that the What will you pay? Chart within the 15 page summary document should clearly cross reference to Outcomes.

David Howarth commented on the same chart and suggested combining Environment and Safe Secure Water as 7% for Environment doesn't look like a lot.

David Guest agreed and suggested breaking down in more detail within the full document.

Charles Burns commented on the same page and suggested including Portsmouth Water in the 'What does this mean for you?' ...without increasing your 'Portsmouth Water' bill... so Customers are clear which supplier won't be increasing their bills.

Milo Purcell asked if the Company was intending to include any notified items that may result in an interim determination in the next price review.

Neville Smith advised that there were no notified items that may result in an interim determination in the next price review.

Milo Purcell was satisfied that the Company was making the Plan in good faith and did not anticipate anything that would cause the Company to re-apply for a revision to the Plan within the 5 year period.

Doug Hunt questioned if the proposal for the adoption of customer supply pipes was a concern for the Company.

Rod Porteous confirmed that it was a concern as it imposes a capital maintenance burden. However, he advised that it was a long way from implementation and it was highly unlikely to see change within this Business Plan period.

Milo Purcell was able to confirm that this was the case.

Neville Smith advised that these Business Plan documents were going to consultation as drafts and will have further feedback from customers and CCG by the end of October.

3. Issues for Review

Incentives

Gareth Simmonds circulated a paper providing an update on the development of the incentive framework being considered for the Business Plan. He advised that, as allowed by Ofwat, the Company have proposed its own incentives in addition to those included in the Ofwat methodology.

He informed the CCG that the Company was undertaking further customer research to gather information on how customers value the outcomes and this will inform the calibration of the incentives. He circulated a table setting out the current position on incentives which will be updated by the results of the further customer research.

He advised that incentives are in place to drive behaviour and are both Rewards and Penalties. Neville Smith commented that any rewards/gains for outperformance beyond a certain level would be given back to the Customer at the end of the period, but advised that how or when these gains would be passed on was yet to be decided.

John Havenhand commented that the description of the leakage incentive states that customer research has indicated that customers value a reduction in leakage and suggested this should change to 'some' customers.

Paul Le Masurier confirmed that during the first stage of customer research, the conclusion was that overall customers were keen for improved levels of leakage. However, further deliberate research revealed that when more informed customers were happy that the Company just maintained the current economic level of leakage. This new incentive will maintain SELL and will be innovative and look for ways to reduce leakage without cost.

Milo Purcell questioned the company's degree of confidence was on water efficiency to influence outcome.

Gareth Simmonds advised that it was driven by optional metering.

Doug Hunt asked if there was a reward.

Gareth Simmonds confirmed that there wasn't but would accept that as a challenge.

Neville Smith confirmed that the customer research had not shown it to be an area customer values so don't think it can be a reward.

National Environment Programme (NEP) and Catchment Management

Gareth Simmonds advised the CCG of the National Environment Programme (NEP) which details the Environment Agency's view of the issues companies have to address as a result of environmental legislation. He confirmed that the Company has also reviewed its existing Catchment Management activity against the future water quality risks and the water safeguard zones set out in the NEP and informed the CCG of the Company's proposals to address these issues.

Gareth Simmonds advised that the National Environment Programme requires the Company to address the risk of entrapment of eels at one of its abstraction points.

Doug Hunt questioned if the cost of the study is included in the Business Plan.

Gareth Simmonds advised that the cost of feasibility studies and planning is included in this Business Plan. However, compliance with the Eels Directive is not required until 2021. If the studies indicate engineering work is required, funds could be included in next AMP period and the Company would still be compliant with Water Framework Directive.

John Havenhand asked for clarification on the proposal to reduce nitrates through Catchment Management long term would increase bills by 67 pence from 2015.

Gareth Simmonds clarified that bills would be 67 pence lower if the work was not completed.

Capital Expenditure

Rod Porteous reminded the CCG that at the August meeting the Company presented its proposals for mains renewals and its water quality schemes for addressing deteriorating water quality. He circulated a paper detailing the remaining elements of the Company's capital programme for challenge by the

CCG.

He advised that the overall cost of the current programme is £63.5m compared with the AMP5 Determination of £47.9m and that a number of scheme costs are still being finalised, however the scheme cost charges are unlikely to impact significantly upon the final £63.5m proposed expenditure. He continued to outline the key elements of the Plan.

He circulated a further paper comparing the Business Plan and the 2009 Financial Determination.

John Havenhand questioned who benefits from meter deterioration, the customer or the Company.

Rod Porteous confirmed that a faulty meter tends to under read and therefore the Customer benefits.

Rod Porteous highlighted the big variances in the comparison. He went on to explain the basis of the Company's resilience proposals and confirmed a key element was a resilience study. He commented that the Company needs to demonstrate that its doing everything it can to be pro-active and to undertake the best capital approach to address problems.

Kirk Phillips asked if the Company can identify the oil potential contaminants.

Rod Porteous confirmed that they can identify potential Commercial oil contaminants through Environment Agency known spill records. He advised that Domestic is more challenging, however, there was expenditure in proposals to address challenges in catchment management.

Kirk Phillips questioned the Company's approach to running equipment to destruction and what its lifespan is.

Rod Porteous confirmed that the Company's telemetry has a relatively short lifespan and is continually being upgraded or replaced. He further commented that redundancy was built into network.

Doug Hunt reassured the CCG that running equipment to destruction was a Standard water industry approach.

Richard Harris asked if the demand for metering has increased. What percentage were unmetered are now metered?

Gareth Simmonds advised that approximately 25% of customers are metered and about 5,000 added each year.

Richard Harris commented that demand may increase through education.

4. Update on Customer Research

Paul Le Masurier of MVA Consultants presented to the CCG an update on the research completed to date; Stages 1 and 2 Qualitative / Quantitative Research, Stage 3 Deliberative Research and the proposed future research; Stage 4 Commitments, Willingness to Pay and Acceptability Testing.

He informed the CCG in detail the results of the deliberative research completed on leakage and resilience.

Nick Sheeran requested the original Customer Research Sub Group reconvene to challenge the further research on Commitments (Outcomes) and Acceptability Testing. He suggested meeting in early November to review the results and report back to the full CCG at the November meeting. The CCG were in agreement.

He confirmed he would email the research proposal and materials to the Sub Group following this meeting and advise of a date for the November meeting.

NJS

John Havenhand commented that the research had been carried out in a way that was as best as could be given the normal limitations of such research methodology. The Willingness to Pay values were open to interpretation and should therefore not be regarded as a licence to increase bills by this amount. He was pleased that the Company had accepted this interpretation and used in our Draft Business Plan.

Nick Sheeran reminded the CCG that earlier in the process they requested a Peer Review be completed. He has therefore obtained a quote from Accent, to carry out the Review. Accent were recommended by Atkins and he asked the CCG if they would still like a Peer Review to be completed.

John Havenhand asked for clarification on what the Review would be of.

Nick Sheeran confirmed that they would review MVA Consultants research, the approach, methodology, reports, conclusions and whether best practice was adopted. The CCG were in agreement and requested Nick Sheeran to instruct Accent to carry out the Peer Review.

NJS

Paul Le Masurier and Terry Lazenby left the Meeting

5. CCG Confidential Discussion

The Portsmouth Water representatives left the meeting and the CCG Members held a confidential discussion which was minuted separately.

6. Feedback from CCG

Doug Hunt informed the Company of the key actions arising from the confidential discussion;

- Vulnerable Customers / Social Tariffs need to be reflected in Business Plan
- CCG would like to be involved in the brief for Peer Review
- CCG want to be invited to observe further research
- CCG wanted clarification on windfall gains and would this be shared with Customers
- CCG confirmed that draft text of their report would be available shortly

DG

The Company noted the above and Nick Sheeran advised that the Company had received less revenue and achieved lower returns than allowed for in the Determination in the current AMP. Therefore there were no financial outperformance gains to be passed onto customers.

7. Efficiency

Neville Smith reminded the CCG that at the last meeting they requested greater visibility of the potential for efficiency in 'staff and manpower costs'.

He had understood that costs and efficiency were not considered within the remit of the CCG. However, he circulated a paper addressing efficiency in general, which reviewed cost efficiency relative to the Industry, savings made since the last determination and the likely assumption for the future.

He advised the CCG that Portsmouth Water have long been considered the most efficient Water Company in the Industry and this would be reflected in the efficiency levels shown in the Plan. The report also contained evidence that salaries were competitive, but within the range of salaries paid in the area.

Doug Hunt asked what impact salary levels have on Customers.

Neville Smith advised that salaries constitute about 20% of bills which is not expected to change over the next five years.

8. Water Quality Risks

Milo Purcel informed the CCG that the Environment Agency identify water quality risks through their National Environment Programme (NEP), take Ministers views on social/environmental guidance and then confirm to companies in greater detail what is required of them. The onus is then on the Company to identify a work programme. The Company is expected to carry out risk assessments of sites in four areas; catchment, treatment, distribution and customer.

He reminded the CCG of two submissions the Company have made to the DWI to reduce the risk of Cryptosporidium and turbidity at their sites in Westergate and Eastergate to which the DWI will respond by the end of October.

He advised that if the DWI decide not to support these proposals and the Board still believe the water quality risk to be high they may consider funding through Capital Maintenance Schemes.

Milo Purcell confirmed that he will bring DWI's conclusion to next meeting for CCG to challenge.

MP

He advised the CCG to ensure they are comfortable with what is included in the Capital Expenditure Report. He felt these were reasonable proposal and satisfied that the Schemes are well funded. However, as it is such a large increase he would expect the CCG to comment / challenge.

Neville Smith commented that the Capital Expenditure of £63m could be a red flag to Ofwat. The Company propose to justify at the next meeting and the Board will be discussing this week.

NS

Richard Harris left the meeting.

9. Update on Assurance

Doug Hunt summarised his assurance to date.

- Infrastructure has been assured.
- Challenge on Non-infrastructure is starting this week. Also including Cryptosporidium cost efficiency.
- Should receive SELL Report shortly for comment.

Doug Hunt advised that he will be in a position to provide a summary paper with a full update at the next meeting in October.

DH

10. Calendar of Meetings

Tuesday 22 October 2013
Tuesday 12 November 2013

11. Any Other Business

There was no any other business.