

PORTSMOUTH WATER Ltd
CUSTOMER CHALLENGE GROUP (CCG)
MEETING HELD ON TUESDAY 25 JUNE 2013

PRESENT: Amy Denford (Secretary), 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), Cllr Leslie Keeble (Fareham Borough Council), Terry Lazenby (Portsmouth Water), Chris Manning (South Downs), Simon Oakley (Chichester District Council), Rod Porteous (Portsmouth Water), Milo Purcel (Drinking Water Inspectorate), Ian Rawson (KWS Defence) (In Part), Nick Sheeran (Portsmouth Water) and Neville Smith (Portsmouth Water)

Action

Apologies

Apologies were received from Traci Baker (Hampshire Chambers of Commerce), Charles Burns (Federation of Small Businesses), Hugh Caley (Carillion), John Colley (Portsmouth Water), David Collins (Havant Borough Council), Andrew Day (Ofwat), Cllr Paul Dendle (Arun District Council), Cllr Derek Kimber (Gosport Borough Council), Douglas Kite (Natural England), Cllr Kirk Phillips (Winchester City Council), Tim Richings (South Downs), Gareth Simmonds (Portsmouth Water), Jon Stuart (Havant & District Citizens Advice Bureau), Stuart Wedgbury (East Hampshire District Council & Havant Borough Council) and Cllr Rod Wood (Portsmouth City Council)

The Chairman reinforced the importance of Members sending a representative to future meetings if they are unable to attend personally.

1. Minutes & Actions of Meeting Held on 26 March 2013

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

The following actions were reported on:

Ofwat Methodology

The Chairman confirmed that the decision to write to Ofwat and the other CCG Chairs expressing concern over the shortened timetable was no longer necessary.

Nick Sheeran confirmed that a revised Timetable is included in this meeting.

Customer Quantitative Research

Doug Hunt confirmed that he had reviewed the Customer Research Results and was able to assure the CCG Members that it was statistically robust. He commented on one of the Research Options to be obviously more favourable and Nick Sheeran confirmed that it was deliberate to make one option appear stronger to provide a logic check and to break down the correlation in the results. Nick Sheeran confirmed that he would send Doug MVA Consultants explanation of this.

NJS

External Assurance Reporter

Neville Smith confirmed that a schedule of works being carried out by the Reporter Doug Hunt for the Company is included in this meeting.

Outline Business Plan

Nick Sheeran confirmed that the Outline Business Plan had been published on the Website for Consultation and included a Questionnaire and Prize Draw to encourage a good response from Customers.

Base Opex

Simon Oakley raised concern that at the meeting in March he questioned how employees' salaries were going to be taken into consideration in this process and it was omitted from the minutes. Nick Sheeran advised that this concern was formally responded to and suggested the response be circulated to the rest of the CCG. Simon Oakley felt that the issue still warranted further discussion at the meeting. Neville Smith explained how employees' salaries were covered in the Company's Operating Costs and therefore wrapped up in inflation increases and therefore not specifically dealt with; however, he welcomed the CCG's views on this. Karen Gibbs stressed the importance that the Final Business Plan needed to clearly show where Customers money is going. The Chairman requested that Doug Hunt check the Final Business Plan includes this.

DH

Mains Renewals

Rod Porteous confirmed that Doug Hunt was currently reviewing the Deterioration Modelling completed by the WRc to provide confidence to the CCG.

DH

2. Outcomes

Neville Smith circulated the Outcomes Assurance Statements with the Key Measures of Success and Incentives for discussion by the CCG.

A number of points were raised as follows:

Outcomes

Generally accepted, except that the Company should think about the use of "will" and "aim". For example instead of "Portsmouth Water will provide a safe..." it should say "Portsmouth Water provides a safe..."

Metric and Targets

There was some disquiet about the measures of success and several could not see the metrics as a driver for the business and, thought they were passive and even inappropriate. The measures should show the vision and the objectives of the Board clearly stated and showed what the Company would deliver and the resources would be available. The Company should not use DWSP or Water Resource Management Plans as they are statutory requirements and are the minimum. David Howarth thought that the Company should tell the story from research to what we will deliver.

Outputs

Milo Purcell felt that they were comprehensive, but thought the Company were open to risk with such a large number and he was uncomfortable with that. The risk is that we have one sided penalties. The Company should have one or two key metrics. He also thought that the Company needed to show opportunities for innovation. His points were again generally agreed.

Doug Hunt thought that the Company should show trends rather than point numbers.

Following extensive discussion it was decided that a Sub Group be formed to look at in more detail ahead of the next formal meeting of the CCG.

NS/AD

3. Company's External Assurance Process / Timetable

Doug Hunt circulated a Schedule of the Audits he will be conducting to provide assurance to the CCG and ensure they have a technical understanding of the models forming the Business Plan.

Action

Milo Purcel advised that this Timetable captures in one document the assurance the CCG has received which will be helpful to use as evidence.

Karen Gibbs suggested the CCG appoint a Customer Research Expert to provide a Report giving further assurance. She advised that she could provide names of experts that other Water Companies have used. The CCG were in agreement.

KG

Leslie Keeble stressed that communication to the Customer needs to be addressed.

David Howarth commented that the Company are faced with the challenge that Customers have expressed they would be WtP more to have reduced leakage, therefore the Company need to look at the current economic level of leakage.

Doug Hunt confirmed that the Company is doing this.

Chris Manning advised that it's not what the economic level of leakage is that needs to be communicated to the Customer, just as a number, but what it represents.

Doug Hunt confirmed that he can assure the technical side but the challenge would be communicating this to the Customer.

Neville Smith advised that in the 2009 Business Plan money was allocated to reduce leakage. However, this was rejected on the basis that the Company did not fully explain leakage in its WRMP, therefore the Customers were not able to make an informed decision on whether they would be WtP more. He recommended doing further Deliberative Research on Leakage.

Karen Gibbs highlighted that the problem with singling out one specific item is it can distort peoples views on WtP. For example in respect of leakage it may not be to do with how much the Company is spending to reduce leaks, but the time taken to repair them, the Customer Service aspect.

Neville Smith noted these comments and agreed that although the deliberative research may not be statistically robust it would give the Company a feel for Customers views and would therefore still have this extra research completed.

John Havenhand expressed the need for the Company to exercise caution when tying up numbers to preference.

Karen Gibbs informed the CCG that CCWater have prepared a Report advising all Water Companies not to put too much onus on one topic taking it out of context. Karen Gibbs would send this to the Company once published in July.

KG

Milo Purcel commented that he could see the difficulties in addressing issues out of context. All factors need to be looked at together, for example, is the Company up to date with good practice, consistent with other Companies, what is its 'USP' and how much risk is it willing to take? All these aspects need to be taken into account when setting the economic level of leakage

Nick Sheeran suggested reconvening the Customer Research Sub Group with either existing or new members to review the format of the deliberative research. The CCG were in agreement.

NJS

Simon Oakley suggested that when calculating the impact of leaks the Company needs to take into account the impact of the highways and Customer perception of leakage.

Doug Hunt confirmed that disruption to traffic is taken into account in the calculation of the economic level of leakage.

4. Approach to CCG Assurance and CCG Report

The Chairman informed the CCG that at recent meetings with the other Chairs there was concern that CCG's are not showing their independence and impartiality. CCG Members need to be mindful that they are not being influenced or led by the Company. In view of this, the Chairman asked if the Company's Representatives could leave the meeting to give the CCG an opportunity to have an open discussion. This portion of the meeting has been minuted separately.

The Company representatives re-joined the meeting and Doug Hunt outlined the draft structure of the CCG Report:

- How good was the Consultation;
- How well is it reflected in objectives set;
- How it demonstrated challenge;
- How the CCG reflected on the previous AMP outcomes and ongoing prospects of customer engagement.

Neville Smith advised that the Business Plan will include past performance as well as long term. He will endeavour to draft the history and circulate it to the CCG.

NS

5. Base Opex and Cost of Capital

Nick Sheeran presented on the Company's Base Opex and Cost of Capital, the main building blocks of Revenue allowed by Ofwat.

Nick Sheeran outlined the Operating Costs Risks and highlighted that Ofwat require the Company to provide evidence of electricity costs. The Company is therefore looking at entering a fixed term deal as well as reducing usage which commenced last year. The CCG Members requested evidence of these savings. Neville Smith advised that an Industry Group is looking at this and will present it in the Business Plan. He also advised that the Company is considering increasing its Solar Panels.

Richard Harris commented that fixed costs are 60% of St Richards Hospitals bills and therefore questioned whether a fixed tariff would be of benefit to the Customer or just to satisfy Ofwat. He advised that as the Company would be paying as part of an Industry Group variable costs may be more competitive. Neville Smith confirmed that the Company was looking at all the options.

Simon Oakley asked if the Company had sufficient space to increase the number of solar panels and if this would impact on the electricity contract. Neville Smith commented that it would not be significant enough.

Richard Harris suggested having an electricity audit carried out on the offices to assist with reducing usage. Rod Porteous advised that electricity costs mainly arise from pumping. Therefore, capital consideration includes energy costs for example, replacing pumps, usage of pumps i.e. times. The Company conducts 'Pump Scheduling' and balances Risk v Cost; this has proved successful with savings of £200k just by changing the triads usage.

Doug Hunt advised that this was more of an engineering problem not standard energy.

Doug Hunt to provide the CCG with assurance on the Base Opex.

DH

Nick Sheeran advised that a Consultant was completing work on the cost of Competition and would provide a copy to the CCG for them to challenge.

NJS

Karen Gibbs asked whether Ofwat were going to provide any information on the Cost of Competition. Nick Sheeran confirmed he would enquire.

NJS

Nick Sheeran confirmed that a Consultant was providing a forecast on Business Rates to be built into the Plan and the CCG will be able to review and challenge.

Nick Sheeran advised that the current cost of the IT Mainframe was £400k per annum and the Company invested £2m of its own money, not supported by Ofwat, to replace the Mainframe and over a 18-24 month period save the annual cost. Neville Smith commented that the £2m invested from the Company should be recovered from Ofwat.

Milo Purcel questioned whether the Company's 80% level of gearing was sustainable. Nick Sheeran confirmed that the Company aimed to reduce its gearing over the long term if feasible. Neville Smith advised that compared to other Companies, Portsmouth Water does not have a large Capital Programme and therefore the current level of gearing should be sustainable.

Milo Purcel asked whether Ofwat are likely to introduce a windfall tax on gains from higher inflation. Neville Smith explained that Commercial Revenue has fallen well short of what was determined and therefore gains do not apply to Portsmouth Water.

Milo Purcel asked whether the Board feels the Company has some distinguishing feature that the CCG should take into account. Neville Smith commented that Portsmouth Water is the only Water Company that is owned by its employees and this unique structure may offer something to its Customers and the Local Community, something to consider. Milo Purcel added that this would enable the Company to be very transparent in the Business Plan process.

Terry Lazenby commented that there are no Investors on the Portsmouth Water Board and can therefore remain independent.

6. Timetable and CCG Meeting Dates

Nick Sheeran provided a high level timetable for discussion by the CCG. He stressed the need for additional meetings to be arranged so that monthly meetings are held between now and submitting the Final Business Plan and CCG Report to Ofwat in November. This would provide the CCG with sufficient opportunity to challenge every aspect of the Plan. The CCG agreed and decided additional meetings would be decided upon and circulated to the Members following the meeting.

Ian Rawson left the meeting.

7. Consultation on the Future Management of Private Water Supply Pipes

Rod Porteous circulated a Defra Consultation Paper on the Future Management of Private Water Supply Pipes for information. He explained that it sets out a proposal to enable the ownership of private water supply pipes to be transferred to water supply companies. Defra believe that the benefits would include a reduction in leakage and protect water quality, ensuring water supplies remain resilient and sustainable for the future. He advised that the Company were overall supportive of this proposal, however, it is unlikely to impact on this Business Plan.

Rod Porteous further commented that this proposal may address some issues of lead pipes. Currently the Company offers a subsidised private supply pipe replacement during mains renewals, which there may be approximately 5 taken up each year. This may have a significant cost implication if the Company adopts the private supply pipes.

Richard Harris asked how much longer will it be before the Company adopts the whole network up to a certain point within the Property and what will be level of surface repair for example reinstating ornate gardens. Rod Porteous advised that the Company was already starting domestic progress to other premises of a certain size. With regard to the level of surface repair, there was the same debate when the private sewer pipes were adopted in 2011; however, it turned out to be less problematic than they thought.

Rod Porteous reiterated that this proposal will not impact on this Business Plan it is

AD

just a note of interest for the CCG. He also confirmed that the Lead Strategy for this Plan is to increase awareness and therefore if this proposal is accepted it could mean an increase in lead pipe replacements.

Simon Oakley asked if the proposal was accepted would it be an added cost to the Company or would it go to the Customer. Rod Porteous assumed that it would be averaged out to all Customers but that will all be considered in the Consultation process in July.

Chris Manning commented that the business implications of this proposal for Farmers would be of great interest.

Milo Purcel confirmed that the DWI would be in support of the proposal, but Ofwat would be against it as they would not want to see assets being added to the Company's Asset Value.

8. Consumer Council for Water - Expectations on water companies testing of customer views on acceptability of their business plan for 2014 Price Review

Karen Gibbs circulated the CCWater paper on its Expectations on water companies testing of customer views on acceptability of their business plan for 2014 Price Review. She explained that the paper sets out good practice for the way Company's approach their acceptability testing. The reviewer should be able to trace the Customers engagement throughout the process and test the results reflect the outcome of the Customer Research. This will give the CCG another level of assurance that the Company Business Plan reflects what the Customer wants.

Nick Sheeran advised that he discussed the paper with MVA Consultants who are completing the Company's acceptability testing in September and they have no problems with the expectations outlined.

Neville Smith advised that when completing the acceptability testing the Company will have to reflect what is happening on the Southern Water Bill as well.

Karen Gibbs explained that waste and water would need to be differentiated. Milo Purcel confirmed that the Company would find that a challenge to do.

9. Approach to Capital Maintenance Planning for Above Ground Assets

Rod Porteous presented to the CCG on the Company's approach to Capital Maintenance Planning for Above Ground Assets.

Richard Harris asked whether the model used could be developed, for example is there the facility for feedback from live maintenance to be input e.g. failures. Rod Porteous advised that the model uses industry best practice for failures. There is not much data on technology available as it is always being superseded. The Company does condition based monitoring but the cost of inspecting exceeds running plant to destruction.

Richard Harris asked if the way the Company maintains plant is included in the Plan. Rod Porteous explained that the impact on Customers is very minimal as plant failure is quickly switched, as the Company's network is all interconnected. He confirmed that no Customer has lost supply through Capital failure.

Doug Hunt confirmed that it was common practice in the Water Industry to run plant to failure.

10. Water Quality Schemes

Nitrates

Tracey Viney presented to the CCG on the Company's Catchment Management work highlighting the problems encountered in particular by nitrates and oil pollution. She outlined the nitrates analysis and modeling that is currently being

carried out and informed the CCG that this information would be used to provide a robust business case to the DWI, EA and Ofwat to support further Catchment Management work.

Tracey Viney also advised that data is currently being gathered from the EA to establish if a robust case can be made in the Business Plan for additional resources, to provide a more proactive approach to assessing and addressing the risk of fuel storage in Portsmouth Water's Catchments.

Boreholes Turbidity

Rod Porteous advised the CCG that this has a £4.5-£5m impact on the Business Plan maintaining standards and he would report findings at the next meeting.

RCP

11. Proposal for Biodiversity

Tracey Viney presented to the CCG the proposal for Biodiversity. She highlighted that the Company's Customer Research has indicated that Customers are WtP for some enhanced biodiversity activities, in conjunction with Community investment.

Tracey Viney outlined three proposals to enhance biodiversity at low, medium and high cost. She confirmed that the Board had agreed to the high cost proposal totaling £75,000 per annum which would increase Customers bills by 25 pence per annum.

David Howarth commented that the Company could have been accused of not listening to their Customers had they not chosen the high cost proposal.

Richard Harris questioned whether the Company could be enhancing biodiversity with any cost neutral solutions. Tracey Viney confirmed that Company was already doing this through staff awareness, operators and volunteers.

12. Date of Next Meeting

Thursday 15 August 2013

13. Any Other Business

Nick Sheeran advised the CCG that Ofwat had launched their Customer Challenge Groups Webpage which included comparative KPI data, along with other background briefing material relevant to Customer Challenge Groups. He circulated a copy of the Comparative KPI Data for information.