



## Report on Portsmouth Water's PR14 Business Plan

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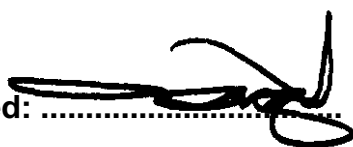
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David Guest

CCG Independent Chairman

# CCG Members

Following a widespread invitation exercise of potential stakeholder groups, the following representatives agreed that they would be part of the Portsmouth Water Customer Challenge Group. Except where noted, these members attended one or more of the CCG meetings. All members have been provided with the opportunity to provide input to, and feedback on, the contents of this report.

Charles Burns, Federation of Small Businesses	Karen Gibbs, Consumer Council for Water
Chris Manning, South Downs Group	Keith Evans, Fareham Borough Council
Colin Buckle, Environment Agency	Kirk Phillips, Winchester City Council
Daire Casey, West Sussex County Council	Leslie Keeble, Fareham Borough Council
David Collins, Havant Borough Council (did not attend)	Louise Bardsley, Natural England
David Fisher, East Hampshire District Council	Marge Harvey, East Hampshire District Council
David Guest, Independent CCG Chairman	Milo Purcell, Drinking Water Inspectorate
David Howarth, Environment Agency	Paul Dendle, Arun District Council
Derek Kimber, Gosport Borough Council	Rachel Crabbe, Natural England
Douglas Kite, Natural England	Richard Harris, West Sussex Hospital Trust
Elinor Cordiner, Drinking Water Inspectorate	Rob Wood, Portsmouth City Council (did not attend)
Hugh Caley, Carillion Plc	Simon Oakley, Chichester District Council
Ian Rawson, Kelda Water	Stephen Philpott, Gosport Borough Council
Jim Barker, Environment Agency	Tim Richings, South Downs Group
John Conner, Chichester District Council	Traci Baker, Hampshire Chamber of Commerce (did not attend)
John Havenhand, Consumer Council for Water	Victoria Weston, Winchester City Council
Jon Stuart, Havant Citizens Advice Bureau	

# Table of Contents

Executive Summary.....	4
1. Introduction .....	8
1.1. Role of the CCG and Scope of this Report.....	8
1.2. Review of the CCG Engagement process .....	9
1.3. Evidence Base for this Report.....	10
2. Customer Consultation .....	11
2.1. Overview .....	11
2.2. Nature and Scope of the Customer Engagement Process.....	11
2.3. Adequacy of the Methods Used.....	12
2.4. Company Interpretation of Findings.....	14
2.4.1. Drinking Water Quality .....	14
2.4.2. Affordability.....	15
2.4.3. Other Service Measures .....	16
2.4.4. Customer Acceptability and Vulnerable Customers.....	18
2.5. Summary Opinion on the Customer Engagement Process .....	19
3. Outcomes and Incentives .....	20
3.1. Development of Outcomes.....	20
3.2. Compatibility of Outcomes with Customer and Stakeholder Preferences .....	20
3.3. Outcome Delivery Incentives .....	22
3.4. Summary Views on the Outcomes and Incentives .....	22
4. Business Plan Costs, Risks and Rewards.....	23
4.1. Delivery Incentives and Explanatory Variables.....	23
4.2. Expenditure Proposals .....	23
4.2.1. Compatibility with Stated Outcomes .....	23
4.2.2. Statutory Requirements .....	24
4.2.3. Affordability and Value for Money .....	26
4.3. Balancing Risks in the Longer Term .....	27
5. Conclusions .....	28
5.1. Comments on the Quality of the Company's Customer Engagement .....	28
5.2. Comments on the Extent to which the Business Plan Reflects Customer and Stakeholder views .....	28
5.3. Comments Relating to Statutory Obligations .....	28

Appendix A: Technical Assurance and Peer Review Summaries

Appendix B: Correspondence from the Environment Agency

Appendix C: Correspondence from the Drinking Water Inspectorate

Appendix D: Minutes of CCG Meetings

# Executive Summary

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1. This Report provides a summary of the opinions and challenge that the independent Portsmouth Water Customer Challenge Group (CCG) brought to the process of customer engagement and the resulting Business Plan that Portsmouth Water ('the Company') has produced for the PR14 Price Review.
2. The requirement and process for an independent CCG was set up by Ofwat as a new entity for the PR14 water industry price review process. Ofwat describes the CCG as being 'a new and powerful forum' who's views will be 'will be crucial in [Ofwat's] risk-based review'. Ofwat's main description of the CCG's remit, and the key items is that it is expected to comment on:
  - the quality of the Company's customer engagement; and
  - how well their proposed outcomes, associated commitments and delivery incentives reflect their customer engagement, and wider consumers' views and priorities.
3. Ofwat also requested, through information notice 13/20, that comments from the Drinking Water Inspectorate (DWI) and environmental regulators about the fulfilment of statutory obligations within the Company's Business Plan are also provided within the CCG report.
4. The intention of the PR14 process is that the CCG provides meaningful comment on the Company's customer engagement and the development of its Business Plan as a result of that engagement. This required the CCG to be meaningfully engaged and informed during the development of the customer engagement process and production of the Business Plan.
5. The CCG's considers that the Company invested the time necessary to provide for this engagement, and the Company was very open in its approach and dealings with the CCG. There was a genuine process of challenge and modification of both the Company's customer engagement and formulation of the Outcomes contained within its Business Plan as a result of that challenge.
6. The nature of the PR14 price review process and truncated programme resulted in time pressures. It has not therefore been possible to consider all points in detail and hence reach a full consensus conclusion on every issue that has been raised for discussion and challenge. These have been identified where appropriate within this Report; however, overall, the CCG considers that it has had sufficient information and time to gain an adequate understanding and reach a considered opinion for the purposes of reporting to Ofwat.

## *Comments on the Quality of the Company's Customer Engagement*

7. In terms of the process and strategy used by the Company for its PR14 customer engagement, the CCG is satisfied that this was consistent with the consultation needs, considering the Company's current low level of bills and relatively small AMP6 capital programme. A more extensive process is unlikely to have resulted in different Outcomes that could have improved customer acceptability of the Business Plan by any significant amount, so in turn was unlikely to have provided value for money for the Company.
8. The Company's approach to customer engagement was in line with the United Kingdom Water Industry Research (UKWIR) Code of Practice principles and individual survey methods used for customer research. This was confirmed as being acceptably designed and implemented by Peer Review. The derivation and interpretation of the Outcomes was an uncertain process, and the CCG did have a number of queries and concerns about the mapping of customer research to the identified customer preferences. However, the Company carried out a number of modifications and provided clarifications in response to the CCG challenges and was able to demonstrate support for its interpretation for most of the Outcomes. The initial evaluation of customer preferences through qualitative research was open and unbiased, and there was a

reasonable link between this and the subsequent quantitative research. The Company accounted for the inherent limitations of the industry standard approaches for quantitative customer research that are generally available by using Willingness to Pay (WTP) to rank and inform the interpretation process; rather than using the WTP values directly.

### **Comments on the Extent to which the Business Plan Reflects Customer and Stakeholder views**

9. The key to demonstrating a link between customer views and the Business Plan lay in the way in which the Company interpreted customer preferences based on the qualitative and quantitative research that it carried out.

Some members of the CCG did highlight the fact that there was an inherent tension between customer preferences for affordable bills, and the WTP for service improvements that was expressed in the quantitative research for areas such as leakage control. Although this was not agreed by all CCG members, this did raise some concerns that the Company's interpretation that customers would prefer leakage to be reduced to a level that was just below the Economic Level of Leakage (ELL), was not ambitious enough. In response, the CCG notes that the Company has indicated that it will endeavour to adopt new technologies for leakage control that become available to reduce leakage, if this can be achieved without placing additional pressure on customer bills.

Concerns were also raised about water efficiency and metering, although these were largely addressed by the Company's adoption of a Per Capita Consumption (PCC) target as one of the measures of success for the Business Plan. Other than this, the CCG considers that the Company's interpretation of customer research into customer preferences was reasonable, and reflected the customer priorities expressed in the surveys.

The CCG particularly notes that the acceptability testing carried out by the Company for its Business Plan demonstrated overwhelming customer support for the proposed level of bills and the Outcomes. Any uncertainties in the process did not seem to affect the overall validity of the Company's interpretation of customer priorities.

10. The CCG considers that the Company adopted a very open and responsive approach to the derivation and definition of the Outcomes, and significantly adapted both its approach and the nature of its stated Outcomes as a result of CCG challenge. Following this refinement process, the CCG considers that there is a reasonable link between the Company's interpretation of customer priorities, the Outcomes and the associated measures of success that have been detailed within the Business Plan.
11. Some of the stakeholder members of the CCG were concerned that there were no specific commitments to vulnerable customers within the Outcomes, given the recent high profile of affordability and social tariffs within political and media circles.

The CCG therefore challenged the Company to include commentary and commitment on affordable tariffs within the Business Plan. This is now included within the 'debt and affordability' section of the Retail Business Plan.

Due to the separate service supply and billing for water supply and waste water collection and treatment in the Company's area of operation, the Company says that it *'would like to offer a Social Tariff and that they have been closely watching Southern Water's development of such a tariff'*. At this stage the CCG understands that Southern Water has agreed in principle to allow the Company to mirror its proposals, and hence provide a combined affordable tariff for water supply and waste water services. However, the provision of the tariff is still dependent on Southern Water's adoption of the scheme and the Company has indicated that it will need to 'gain customer approval' before the tariff is adopted.

12. The CCG notes that the issue of affordability was the focus of considerable regulatory and political pressure during the development of the Business Plan. During qualitative research,

customers also indicated that water supply charges 'remaining affordable' are of significant concern.

'Affordability' of the Business Plan proposals was therefore a key element of the discussions between the CCG and the Company, and the Company's assertion that water supply charges that increase in line with nationally reported Retail Price Index (RPI) inflation is acceptable to its customers was subjected to considerable challenge by the CCG.

Overall, the Company provided strong evidence that the customer priority for affordable bills can be expressed as a preference for the lowest reasonable bill levels that are able to support the Outcomes proposed in its Business Plan. Based on the evidence provided, the CCG also considers that the Company demonstrated that customers would clearly prefer a Business Plan that maintains current service levels, rather than a Business Plan that proposes a reduction in service levels in order to reduce customer water supply charges. Because customer preferences were relatively clear on this matter, the CCG challenged the Company to demonstrate the following two points:

1. Whether the Business Plan adequately reflects the appropriate level of operational, maintenance and investment activities that will be necessary to deliver the proposed Outcomes;
  2. Whether the expenditure associated with those activities is reasonably based and efficient so that the Business Plan can be shown to be consistent with the affordability priority.
13. In relation to the first point, the information and independent assurance provided meant that the Company was able to demonstrate consistency between the activity proposals contained in the Business Plan and the Outcomes associated with drinking water quality, interruptions to supply, leakage, and the performance of assets. Other measures of success were reviewed, and it was noted that they either form part of the statutory obligations, or can be delivered within current organisational structures and hence levels of operational expenditure. Metering will remain at optant-only levels, in line with the stated Outcomes.
14. The Company was also able to demonstrate that the Business Plan activities were in line with longer-term expenditure requirements, and that variations from historic maintenance expenditure generally related to exceptional items and new obligations such as the need to replace membrane filters.
15. In relation to the second point, it is noted that it is not necessarily within the CCG's remit to provide comment on whether Business Plan cost proposals have been reasonably and efficiently derived. However, in response to the challenges that were made, the CCG considers that the Company was able to demonstrate the relative efficiency of its operational expenditure, and provided technical assurance that it was adopting a reasonably efficient approach to its capital investment proposals.

The CCG notes that the Company has committed within its Business Plan to sharing AMP6 outperformance with its customers, such that in the interests of affordability, it will pass on efficiencies that it does achieve in excess of the Business Plan assumptions.

This indicates that opportunities for efficiency are therefore limited; given that, and because the Business Plan already includes a commitment for an early return of AMP5 out-performance to customers, the Company explained that the only remaining options for reducing bill levels below RPI would be to cut the scope of its capital maintenance expenditure, or save money through its financing options.

The Company has demonstrated to the CCG that opportunities for savings through financing are limited, but this constraint is considered to be outside of the CCG technical remit to challenge further.

16. Based on the above, the CCG therefore considered it apparent that the Company has sought to balance the priority for affordability with the other stated Outcomes, and that this has formed the cornerstone of its Business Plan.
17. The CCG notes that there is an expectation from Ofwat that quantified Outcome Delivery Incentives (ODIs) will be proposed by companies in PR14. The Company has linked its ODIs directly to customer priorities, and includes a financial reward only where there is some evidence of customer support for further improvement.

The CCG expressed reservations about the appropriateness of the methods that are needed to quantify customer preferences into ODIs, but notes that the financial rewards and penalties that the Company has proposed are comparatively small, and only relate to three outcomes. Their potential impact on future bills is therefore considered to be correspondingly small.

#### ***Comments Relating to Statutory Obligations***

18. In the Environment Agency's view, from the information provided, it understands that the Company is planning to meet its statutory environmental requirements set out in Defra's Statement of Obligations, and it welcomes the Company's commitment to meeting them. Within its correspondence to the Company it also states that *'in so far as the comments herein relate to the natural environment, they also reflect the advice of Natural England'*.
19. The DWI has provided feedback on all of the submissions made by the Company relating to drinking water quality schemes. Of these, the DWI has formally supported three of the Company's proposals and they will put legal instruments in place to make the proposals legally binding programmes of work. In addition, they have commended for support three proposals. All of the schemes that were included within the Company submission for these six proposals have been included as appropriate within the Business Plan.



# Report on Portsmouth Water's PR14 Business Plan

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## 1. Introduction

### 1.1. Role of the CCG and Scope of this Report

20. This report provides a summary of the opinions and challenge that the independent Portsmouth Water Customer Challenge Group (CCG) has brought to the process of customer engagement and resulting Business Plan that the Company produced for the PR14 Price Review.
21. The requirement and process for an independent CCG was set up by Ofwat as a new entity for the PR14 water industry price review process. Ofwat describes the CCG as being 'a new and powerful forum' who's views will be 'will be crucial in [Ofwat's] risk-based review'. Ofwat's main description of the CCG's remit is that it is expected to comment on:
- the quality of the Company's customer engagement; and
  - how well their proposed Outcomes, associated commitments and delivery incentives reflect their customer engagement, and wider consumers' views and priorities.
22. In terms of the CCG report itself, Ofwat has provided the following guidance through its consultation process and final price control methodology:
- Ofwat's risk based review of the Business Plan will begin with an assessment of a company's customer engagement process. The representations contained within the CCG Report will therefore help Ofwat to determine the status of the Company's submission ('enhanced', 'standard' or 'resubmission') and be used to inform the draft determination if the submission is classified into the 'standard' category. A short form additional CCG report will be required if the Company is required to resubmit the Business Plan.
  - Ofwat expects the CCG Report to provide information about the quality of companies' customer engagement, and how well the companies' business plans reflect customer views and priorities. This includes challenges on the Outcomes and the ODIs.
  - Ofwat has indicated that they would expect that the CCG report to highlight both consumer and environmental concerns. Within information notice IN13/20 Ofwat stated that they would expect comment from the environmental and DWI quality regulators within each CCG's report to confirm whether or not a company has provided adequate assurance that it will meet its future statutory obligations.
23. The remit to comment upon the customer engagement process and the associated outcomes is therefore clear, and is addressed accordingly within this Report. The remit to provide comment on how well customer's views and priorities have been reflected within the Business Plan is less straightforward, and has been interpreted by the CCG according to the following criteria:
- The clarity and logic that the Company has applied when interpreting customer priorities from the surveys and studies that it has undertaken as part of the engagement process, and the evidence that it has gathered on the acceptability to customers of the overall Business Plan;
  - The clarity of the link between the customer priorities and the ODIs that have been produced, and the degree of commitment offered by the incentives in terms of both measurability; and where appropriate, links to customers' willingness to pay;

- The extent to which the expenditure proposals and balance of risks presented within the Company's Business Plan reflect customer views and priorities.
24. Based on the remits described above, this Report has therefore been structured into the following sections:
- **Section 2** provides comment on the **Customer Consultation** carried out by the Company, and the methods that it adopted to identify customer priorities based on that consultation;
  - **Section 3** provides comment on the **Outcomes** proposed by the Company, and the degree to which the Outcomes **and Long Term Strategy** reflect customer priorities;
  - **Section 4** provides comment on the degree to which the five year **Business Plan Costs, Risks and Rewards** reflect customer priorities and the longer term strategy. Comments from the statutory regulators are also provided within this Section.

## 1.2. Review of the CCG Engagement process

25. The Company engaged with the CCG and provided them with evidence of their customer engagement and Business Plan process through the following methods:
- **Presentations and discussion at CCG meetings.** These started on 25/05/2012 and a total of 14 meetings were hosted by the Company prior to the submission of the Business Plan. The Company has presented information on customer consultation, outcomes, statutory requirements, expenditure proposals, efficiency and financing considerations during these meetings. It has also facilitated exclusive sessions where the CCG was free to discuss its opinions in the absence of the Company representatives;
  - **Technical sub-groups** that were formed to review and challenge the customer consultation and development of outcomes. Representatives of the customer consultation sub-group attended customer consultation sessions relating to both the design and interpretation of the quantitative customer surveys;
  - **Independent Peer Review** carried out by Accent consulting. The Company sought CCG inputs on both the selection of the Peer Review and the scope of the review exercise, which was broadly based and was not constrained by the remit that they were given;
  - **Independent assurance** of the adequacy and reasonableness of certain technical aspects of the Business Plan and associated presentations that were made to the CCG, generally relating to the adequacy of capital investment needs and operational cost forecasts.
26. The general consensus of the CCG is that the Company invested the time necessary to provide meaningful engagement with the CCG, and provided independent validation of the information that it presented where this was required. The CCG notes that the Company's openness in its engagement, and the provision of information on matters such as financial risks and costs of capital to enable the CCG to have a more rounded view of the Business Plan proposals.
27. The nature of the PR14 price review process and the truncated programme resulted in time pressures. It has not therefore been possible to consider all points in detail to reach a full consensus conclusion on every issue raised for discussion and challenge. These are identified as appropriate within the body of this Report. Overall, the CCG considers that it has had sufficient information and time to gain an adequate understanding and reach a considered opinion for the purposes of reporting to Ofwat; although, some of the more direct CCG involvement in customer surveys has had to be curtailed due to the time pressures that have been placed by Ofwat on the PR14 process.

### 1.3. Evidence Base for this Report

28. The comments contained within this Report are based primarily on the CCG, its sub-technical group meetings and the information presented by the Company at those meetings. The minutes of those meetings therefore provide the primary evidence of the process of challenge carried out by the CCG, and are provided within Appendix D of this Report.

The customer consultation Peer Review and the technical assurance reporting has also been used to demonstrate evidence of the process of challenge. The summary conclusions of the relevant reports and presentations are provided within Appendix A of this Report.

## **2. Customer Consultation**

### **2.1. Overview**

29. This section contains the CCGs opinion and findings in relation to the customer engagement process that was undertaken by the Company for its PR14 Business Plan, and comments on the way in which the outputs from customer engagement are interpreted by the Company.
30. A summary of the engagement process carried out by the Company is provided within its Business Plan. In reviewing the adequacy of this customer engagement process, the CCG sought to address the following questions:
1. Is the nature and scope of the customer consultation proportionate to a water company with the Company's level of charges and proposed future expenditure?
  2. Were the engagement activities carried out appropriately with adequate methods and sample sizes?
  3. Is the interpretation of the process findings; as presented within the Business Plan, appropriate and reflective of customer wishes?
31. The CCG challenged the customer consultation process from a very early stage, and there have been significant changes to many of the activities that were undertaken as a result. The three questions posed above were distilled from the various challenges and issues raised during meetings with the Company, and used to form the basis of the CCG's overall conclusions about the customer consultation process. The following sections therefore address each question in turn and highlight the challenges and alterations that have resulted, before drawing a general conclusion about the adequacy of the customer engagement process.
32. A key part of the CCG's considerations in this area have come from the Peer Review report commissioned by the Company in consultation with the CCG. This was used to inform the opinions expressed where appropriate within the following text.

### **2.2. Nature and Scope of the Customer Engagement Process**

33. The nature and scope of the engagement process forms the first key element in providing confidence that customers' views were considered appropriately as the basis of informing the Business Plan preparation. This section provides the CCG's views on the strategy used to identify which methods should be used within the customer engagement process. Views of the CCG and challenge of the methods used within individual stages of the process are provided in Section 2.3.
34. The customer engagement process adopted by the Company for PR14 is significantly larger and broader in scope than any such process it has undertaken in the past, and included:
- Qualitative research to understand initial customer opinions based on focus groups;
  - Face to face interviews, including customer satisfaction (value for money) questions and stated preference approaches to evaluate willingness to pay and customer priorities on a quantitative basis;
  - Web-based consultation on the draft Business Plan;
  - Acceptability testing of the proposed Business Plan;
  - Development of incentives for the Business Plan.

35. The Company also carried out further deliberative research into customer's opinions about leakage. This was challenged by the CCG as it was considered that there were inherent risks in obtaining feedback on single issues without the wider context. The Company acknowledged these concerns and only used the deliberative research to inform its interpretations of the findings of the other research.
36. The Company presented the CCG with the proposed customer engagement strategy at an early stage. Initially this was provided to inform the CCG rather than as a proposal for review. However, following development of working relationships between the Company and the CCG, a specific sub-group was established to amend and develop the proposed customer engagement strategy. The CCG strongly challenged the initial proposals, as they seemed to be limited and very much in line with the previous (PR09) Business Plan activities. This resulted in more extensive customer engagement proposals. The CCG considers that the Company addressed this challenge appropriately.
37. The CCG confirms the strong response to the initial qualitative research, discussed by the CCG sub-group and used to inform the subsequent qualitative research. The CCG sub-group met with the consultants involved and provided direct input to both the qualitative focus groups and the design of the quantitative surveys. The overall process has therefore been reasonably based on an initial 'open' questioning of customer views, which have followed through to the qualitative research and hence the Company interpretation of customer priorities. The potential for influence by the Company over the nature of the questions and the interpretation of outcomes is discussed in the following section, but it is clear that the basis of the process itself was customer led and did not reflect a pre-conceived agenda prescribed by the Company.
38. In terms of the scope and range of customers involved, the CCG provided consistent challenge and is confident that the Company has engaged across an appropriate and proportionate range of demographics for household customers (including socio-economic groups, rural/urban location, income types, ages etc). It has also engaged adequately across a range of both smaller and larger non-household customers. This is supported by the findings of the Peer Review, as discussed below.
39. Although the adequacy of the range of customers engaged through the PR14 process was generally supported by both the Peer Review and the CCG, the inclusion of vulnerable customers was challenged, as there was very limited engagement with such groups within the qualitative research; they were not specifically targeted during the acceptability testing. The Company responded that the selection for the acceptability testing was random and did not necessarily include all socio-economic groups. This was broadly accepted by the CCG, but the representation and interpretation of needs for vulnerable customers was specifically scrutinised as part of the Company interpretation of customer priorities, as detailed in Section 2.4.3 of this Report.

### **2.3. Adequacy of the Methods Used**

40. The methods and nature of customer engagement that were used in the individual studies and surveys that were undertaken for PR14, form the second key element of the CCG challenge and views on the adequacy of the customer engagement process. These are described within this section.
41. The CCG confirms that it was adequately consulted on individual methodologies (through its customer consultation technical sub-group), and timely opportunity was provided for challenge at all stages. As a result, the Company carried out significant revisions to all of the individual studies that it carried out within the customer engagement process, which included:
  - During the initial qualitative research, the Company increased the number of Focus Groups from 2 to 4;
  - For the quantitative research (and associated stated preference surveys), web based approaches were dropped and all 500 domestic customer interviews were carried out face

to face. The locations of surveys were widened to include locations such as shopping centres;

- The deliberative research on leakage was only used to inform interpretation, as discussed previously;
  - The format and wording of the Business Plan commitments published for consultation, was strongly influenced by the changes to the Outcomes and associated service commitments resulting from the CCG challenge process described in Section 3.1;
  - For the acceptability testing, the Consumer Council for Water (CCW) representatives on the CCG were invited to present on good practice principles and thresholds for customer acceptance. The Company took account of these recommendations when designing its acceptability testing.
42. The initial qualitative research was generally well run and attended by representatives from the CCG customer consultation sub-group, who reviewed the materials that were used and were able to sit in on some of the sessions. The CCG considers that the opinions that were expressed were not unduly influenced and were reasonably used to inform the quantitative research questions.
43. For the quantitative research, the CCG notes that there are uncertainties with the methodology and potential for biased responses within stated preference studies, even though they are used as standard water industry practice.

As noted in the following section, the CCG consistently challenged to Company to consider this point when it was interpreting and using the outcomes of the quantitative research to inform the Business Plan preparation.

The Peer Review document and presentations and reports by the consultants involved demonstrated that socio-economic and demographic factors were accounted for in accordance with good practice.

The Company also sought to engage a range of household customers, SMEs, institutional non-households and larger business users as part of the quantitative surveys.

44. The CCG noted that the figures used in relation to the degree of changes in service measures within the stated preference surveys, were not necessarily realistic or designed to align with Business Plan estimates of the service improvements that might be achieved. Rather, they were intended to be sufficiently large to elicit meaningful WTP from the customers involved. This is an accepted feature of standard stated preference approaches.

Based on CCG discussions and the feedback provided within the Peer Review report, the CCG is confident that accepted good practice was followed for the quantitative surveys, but would highlight the limitations of these methods and the need for caution when results are being interpreted. This has created some uncertainty in the interpretation of results, as discussed in Section 2.4 below.

45. The CCG also note that the stated preference surveys only explored WTP, and did not investigate the possibility of reduced service levels in return for lower charges. This represented a policy assumption by the Company that a reduction in service levels is not acceptable to customers or stakeholders.

The question was asked in the qualitative research and there was some indication that this might be acceptable in relation to telephone and complaint handling, but the Company generally considered that the regulatory risk from this would not be acceptable. However, because this issue had been raised by customers and challenged by the CCG, the Company commissioned further consultation as part of the acceptability testing process, as discussed below.

46. Questions on value for money were asked as part of both the quantitative research stage and the acceptability testing stage. The CCG did note that the preamble to these studies highlighted the Company's position as having the lowest overall charges within the water industry, which could have affected responses, The technical sub-group concluded that it is difficult to decide whether the presentation of a relative cost position counts as undue influence when the Company is seeking opinion on value for money, which will always be a relative concept.

The Peer Review document did not comment on the value for money surveys, as they did not form a major part of the Business Plan development.

47. The materials used for the acceptability testing of the Business Plan showed that key cost proposals and the Outcomes were clearly and simply expressed to customers at the start of the testing exercise. Given the Peer Review comments, the CCG was satisfied that testing had been carried out in a reasonable manner.

It was noted that only 'informed' opinions (i.e. opinions once customers had been shown a single page summary of the Business Plan) were sought for the acceptability testing, but after discussion and challenge. The CCG accepted the Company response that 'uninformed' opinions would not have added value to the exercise. Challenge was also raised in relation to the way that the impact of RPI on actual bills was represented within the acceptability testing. This is discussed within Section 2.4.4.

48. The testing of an alternative to the preferred Business Plan whereby customers were asked to express their relative acceptability of lower cost, lower service option was clearly and simply carried out without obviously biased questioning.

49. The methodology adopted for the development of incentives was based on a bespoke approach developed by the Company's consultants in response to the need for quantified, monetised incentives for the PR14 Business Plan. The CCG considered that this additional effort and attempt at innovation should be commended, and accept that alternative approaches to quantifying incentives based directly on customer opinion are not generally available. However, many aspects of the methodology were challenged by both the CCG and the peer reviewers, and the CCG considers that the results and innovative methodology need to be viewed with a degree of caution. This is reflected in our comments on the monetary incentives, as described in Section 3.2.

## **2.4. Company Interpretation of Findings**

50. The final key element of the customer consultation process related to the approach and assumptions that were adopted by the Company when it was interpreting the results of the surveys into customer preferences and hence the proposed Outcomes, This was one of the more uncertain aspects of the engagement process and has resulted in some areas where it is not possible to be entirely clear about the link between customer preferences and the Outcomes KPIs (Key Performance Indicators) developed for the Business Plan. The CCG's views as to the clarity of the interpretations and some of the areas of uncertainty that have resulted is provided below. These have grouped according to subject area below.

### **2.4.1. Drinking Water Quality**

51. Whilst most of the customer preferences were identified and interpreted based on the results of the quantitative surveys, the customer priority for a safe, clean supply of water was taken from the initial qualitative focus groups. There was a strong and consistent message from these focus groups that water should be safe and palatable to drink.

Customers were generally satisfied with the current high rate of regulatory compliance. The relatively low number of customer complaints indicates that customers are generally satisfied with current service levels. The Company therefore concluded that drinking water quality is a priority, but interpreted that customer preferences in this area were to maintain existing service levels. This view is considered to be compatible with the views expressed by customers and



the CCG. The CCG did not challenge the exclusion of drinking water quality as a consideration from the subsequent quantitative surveys.

#### 2.4.2. Affordability

52. The identification of affordability and value for money as a key customer priority was based on the findings of the qualitative focus groups, and as a result of the relatively low WTP values expressed in the quantitative surveys. This appears to be an appropriate interpretation of customer priorities, particularly given current economic conditions and regulatory views expressed during the price review process.

As discussed in Section 3.2, the most challenging interpretation that the Company has made in relation to the 'affordability' priority is that bills should increase at a rate that is no higher than the RPI measure of inflation during AMP6. The CCG exerted considerable challenge on this point, and specifically asked why charge increases that were lower than inflation had not been proposed to represent the 'affordability' priority. The main response to this challenge is that the Company does not consider that it can maintain asset serviceability (and the related Outcomes), meet its statutory obligations and remain financeable with acceptable levels of gearing without increasing charges in line with inflation. The Company was very transparent about its assumptions on this point and noted the following to the CCG when it was making its case about potential bill impacts from the Business Plan proposals:

- The initial calculations of expenditure required to meet statutory obligations and other customer priorities initially resulted in bill increases above RPI. As a result, the Company actively took the decision not to claim the outperformance that it will achieve in AMP5 as part of the legacy adjustment allowance. Effectively it has decided to return this outperformance to customers earlier than it has to, in order to meet the 'affordability' priority;
  - Some financing/debt issues mean that the Company has less flexibility in relation to borrowing costs and hence Weighted Average Cost of Capital (WACC), which makes it difficult to adjust financial aspects to reduce charges in the short term. Specifically, the financial modelling used by the Company indicates that there is a risk that interest covers will drop below 1.6 if WACC assumptions are changed.
53. The CCG considers that it is beyond its remit to technically comment on either of these points, but it is apparent that the Company has examined the financial side of the Business Plan and attempted to reduce cost inflation as far as it considers that it can reasonably do. In light of the below RPI inflation that has been historically experienced by the Company's customers, and the fact that the Company is willing to return outperformance to customers, the CCG considers that the Company has adopted a reasonable approach when interpreting the affordability priority.

Effectively, the RPI increase represents the lowest limit that the Company considers it can place on customer bills without compromising the other customer priorities, and hence provides a good balance between the customer desire for 'affordability' and the Outcomes relating to maintenance/improvements in other service measures. The main caveat to this view is that it only holds true if the Company can demonstrate that its expenditure proposals to meet other Outcomes has been efficiently derived, and represents a reasonable least-cost approach to delivering the Outcomes in AMP6 and beyond. The CCG views on this matter are provided within Section 4.2.3 of this Report.

54. As noted previously, following the CCG challenge that a lower cost, lower service option had not been tested with customers, the Company included some specific questioning within its acceptability testing to evaluate customer preferences on this issue. The following specific question asked was as follows:
- *'do you agree or disagree with the Company's proposal to maintain bill levels and increase maintenance, compared with an alternative option of marginally reducing bills and maintaining current services in the short term but risk increased interruptions in supply?'*



55. The Business Plan proposals for maintaining service measures whilst maintaining flat bills in real terms was overwhelmingly supported by customers in preference to the lower cost, reduced service alternative. Because the Company's proposed Outcomes are essentially aimed at maintaining service and asset serviceability in the long term, the CCG considers that this question was relevant and its challenge was adequately addressed. It therefore appears that the Company has reasonably interpreted that the customer priority for affordable bills can be expressed as a preference for the lowest reasonable bill levels that are able to support the Outcomes proposed in its Business Plan.

#### 2.4.3. Other Service Measures

56. For areas where service measures improvements were considered, the Company interpretation of customer's priorities was based on the results of the quantitative research, with some secondary influence from the deliberative research into customers' views on leakage. The 'core' of the Company's interpretation was essentially based on a ranking of customer priorities according to their relative WTP for the potential service improvements that were identified through the qualitative focus groups. This resulted in the identification of the following priorities for household customers, based on the relative WTP values of these service measures in comparison to the other service measures that were tested:

- Improved wildlife habitat in streams and rivers (biodiversity);
- Water softening;
- Reduced carbon footprint;
- Reduced leakage;
- Public amenities and community support.

57. The CCG notes that given customer preferences for affordable bills, and the focus that politicians and Ofwat have placed on affordability during the PR14 process, the Company did not interpret that stated WTP values should represent a reason to increase customer's bills; but rather, took a policy decision that they should just be used to prioritise customer preferences than actually be used as a reason to increase customer's bills in return for service enhancements.

58. There was discussion within the CCG that this may imply that the Company has not proposed a Business Plan that is in line with customer preferences, as greater improvements could have been proposed in areas such as leakage whilst maintaining bill increases to within the amounts that were allowed for in the aggregate WTP. However, it is clear from the evidence that the Company presented to the CCG, that the need to ensure asset stewardship (in the form of some increases in non-infrastructure capital maintenance costs) and meet statutory obligations, meant that only modest service measures improvements could be considered without rises in charges beyond RPI measured inflation. This meant that there was an inherent conflict between the aggregate results of the WTP studies and the Company's interpretation of the affordability priority. The CCG therefore has some differing views on this point, which are highlighted below in relation to the interpretation of leakage and water efficiency preferences.

59. As well as the conflict between affordability and WTP, the CCG noted that some of the service measure improvements quoted in the stated preference surveys used for the quantitative research would have been significantly more expensive to deliver than others. Because the WTP was then used to rank priorities without considering the relative cost of the improvements that were stated, this introduced additional uncertainty into the interpretation process. However, whilst the peer reviewers also noted this issue, it was not considered to be significant enough to invalidate the findings of the quantitative research. The large differences in costs between the service measures improvements that were tested, were therefore taken into account as an uncertainty by the CCG during its assessment of the Company's interpretation of customer priorities, rather than a source of significant bias or flaws within the research.

60. Taking account of the two issues described above, the CCGs' main comments on the interpretation of priorities from the quantitative customer research are as follows:
- The customer preference for leakage reduction has been interpreted by the Company as reflecting a desire to return to the ELL. This is a much smaller change than that proposed in the stated preference survey, which related to a halving current leakage levels. However, the WTP for such a step-change in the service measure was well below the costs that would be involved, and the deliberative research demonstrated a general support for the ELL approach once customers were informed of leakage management practice. Overall the CCG was not able to agree whether this was a clear interpretation of customer preferences, as some members considered that the Company could have adopted more ambitious targets for leakage, with a small concurrent increase in bills;
  - The customer preference for water softening has also been interpreted into a limited target, in this case to the provision of greater information rather than any commitment to treatment. Again, this was largely due to the fact that the WTP was well short of the expenditure that would be required to provide full softening at the Company's treatment works. The CCG accepted that this interpretation is reasonable, as, unlike leakage, it is not meaningful to partly introduce this improvement and customers were clearly not willing to pay for the full costs involved;
  - There was an expressed preference by customers for some provision of water efficiency devices alongside water efficiency information, beyond existing activities. Given the relatively low WTP on the household side, and the lack of water resources pressure that the Company faces, this service enhancement was not taken forward as a specific household customer preference. However, it was noted that the proposed service improvement was only just lower than the identified priorities in terms of WTP, and would be significantly less costly than the measures associated with leakage or water softening; so, it may be more of a customer priority than was suggested by a simple ranking of WTP values. It was also identified as a priority to non-household customers, as noted below. Some members of the CCG therefore considered that specific commitments to enhance water efficiency measures could have been included within the Business Plan;
  - The interpretation of customer preferences in relation to metering was difficult to review, as the fact that metering will generally save money for an optant means that both customers and stakeholders had the impression that meters save, rather than cost money to the Company and its customers as a whole. The main CCG challenge was therefore that metering should be better promoted to those customers that would save the most from metering, and the Company responded to this by including provisions for enhanced metering information within its Business Plan. Customer preferences relating to the social equity of metering were not investigated, mainly because the analyses that the Company carried out for its Water Resources Management Plan (WRMP) clearly demonstrated that enhanced metering programmes are not cost-beneficial given the current water resource position.
61. Potential service measures improvements relating to customer contacts, hosepipe bans, interruptions to supply and enhanced cross-subsidies to vulnerable customers were found to be of a lower priority within the stated preference surveys, so enhancements to these service measures were not considered to be a customer preference. Because the potential for reducing service levels in return for cost savings was not investigated during the quantitative surveys, the Company's interpretation of customer preferences in these areas was that service measures should be maintained at current levels.
62. For business (non-household) customers, their preferences were similar to domestic customers but improvements in water efficiency and longer term interruptions were stated as a higher priority. Community support was also relatively important to business customers. The CCG challenged the Company's initial interpretation of customer preferences as they did not well reflect business customers' priorities, so a priority relating to support for the community and local economy was added, as described in Section 3.2. Because customer's views on the importance of improvements in long term interruptions varied between domestic and business

users, the Company interpreted that this should not form a priority within its Business Plan. This seems reasonable given the already high inter-connectivity and resilience of the supply system and the very low level of interruptions that the Company has in comparison to the rest of the water industry.

63. With respect to the interpretation of water efficiency and metering preferences, the CCG noted that, following feedback from the CCG Outcomes technical sub-group, the Company has included an Outcome committing it to a continuous reduction in PCC as part of its commitments on biodiversity. Whilst some CCG members considered that a more direct interpretation of customer preferences could have been included, it is acknowledged that customer preferences on these issues were not clear. The general PCC commitment does acknowledge the effects that should result from metering and customer water efficiency, whilst supporting the customer preference to enhance biodiversity, which was clearly stated.

#### 2.4.4. Customer Acceptability and Vulnerable Customers

64. Although the evaluation of customer priorities is inherently uncertain because of the methods that are available, the CCG notes that the response from the customer acceptability testing was overwhelmingly positive (99% acceptability for domestic customers and 94% acceptability for Business Customers). If the acceptability testing can be considered to be valid, then it would appear that the Company's interpretation of customer priorities must also be valid given the response rate.
65. As noted previously, the CCG considers that the key Business Plan cost proposals and Outcomes were clearly and simply expressed to customers as part of the acceptability testing, and the peer reviewers were satisfied with the approach that had been taken. The only significant challenge related to the affordability issue and the way that the proposal to increase bills in line with the RPI measure of inflation was phrased within the presentation.

The Company responded that, although further clarification could have been provided about inflation increases in bills, this had to be balanced against the risk that it might have confused the issue and hence the research. The CCG noted that dissatisfaction was slightly higher within the A/B socio-economic groups, which may have been linked to a greater understanding of the impact of the RPI measure of inflation on bills. However, this affect was very marginal (2%), so it was considered very unlikely that a greater understanding of RPI implications amongst other socio-economic groups would have affected acceptability to the point where it would have undermined the overall interpretation of the results. The CCG is therefore satisfied that the Company addressed its concerns over RPI increases and perceived affordability within its research.

66. Although they did not form a key part of the development of the Business Plan, the CCG noted that the two satisfaction surveys that were carried out produced consistent results, which confirmed the adequacy of the sample size and selection process that was used for the associated quantitative and acceptability testing exercises. The CCG noted that satisfaction amongst domestic customers was much higher than for business customers (98% v 66%-68%) and challenged the Company to understand and respond to this within the Business Plan.

The Company confirmed that measures were already being implemented in relation to free water audits, relationship management and consolidated billing and indicated that this would be reflected within the narrative for the non-household retail Business Plan.

67. As noted previously, stakeholders within the CCG were concerned that vulnerable customers had not been specifically targeted for engagement, so interpretations of their priorities and acceptance of the Business Plan was questioned. The Company responded by including an affordability section within its Retail Business Plan, and is proposing measures for vulnerable customer tariffs that are designed to link in with Southern Water's proposals for wastewater. In terms of engagement with vulnerable customers, the selection of respondents to the quantitative and acceptability testing research had been random and did represent all SEGs (as confirmed by the peer review). The CCG also noted that the lower income socio economic groups demonstrated 100% acceptability of the Plan, so there was no trend of reducing

acceptability with lower incomes. Therefore, although specific testing had not been carried out, the CCG was satisfied that 'vulnerable customers' had been consulted through the research.

## 2.5. Summary Opinion on the Customer Engagement Process

68. The CCG was provided with sufficient opportunity to challenge the Company throughout the customer engagement process, and significant changes were made to both the methods and the interpretation of the results as a result of those challenges.
69. In terms of the overall PR14 engagement process, the CCG considers that the Company has derived and implemented a reasonably proportionate strategy with individual methods that were confirmed as being acceptably designed and implemented by the peer review process. The CCG considers that the strategy adopted by the Company is consistent with the consultation needs of the Company given its current low level of charges and relatively small AMP6 capital programme. The CCG notes that a more detailed process would not necessarily have been required or represent value for money in the Company's position.
70. The issue of affordability and the Company's interpretation that bills increasing in line with RPI inflation are acceptable to its customers was subjected to considerable challenge by the CCG in light of the current economic climate and comments made by Ofwat. Overall, the Company provided strong evidence that it has reasonably interpreted that the customer priority for affordable bills can be expressed as a preference for the lowest reasonable bill levels that are able to support the Outcomes proposed in its Business Plan.
71. The derivation and interpretation of Outcomes is an uncertain process, and the CCG did have a number of queries and concerns about the mapping of customer research to the identified customer preferences. However, the Company carried out a number of modifications and provided clarifications in response to the CCG challenge, and was able to demonstrate support for its interpretation for most of the Outcomes. The acceptability testing also demonstrated overwhelming customer support for the final Business Plan proposals. Other than an inherent tension between affordability and the expressed WTP for some service measures improvements, and associated concerns about leakage commitments, the CCG therefore considers that the Company's interpretation of customer research into customer preferences is reasonable. The Company has accounted for the inherent limitations of the industry standard approaches for quantitative customer research that are generally available by using WTP to rank and inform the interpretation process.
72. The CCG commends the attempt to develop an approach that seeks to elicit cost incentives for under and over-performance of stated outcomes, but notes the limitations and uncertainties of the method used. This is reflected in the CCG comments on the Outcome Delivery Incentives within Section 3.3 of this Report.

### **3. Outcomes and Incentives**

#### **3.1. Development of Outcomes**

73. The development of the Outcomes was subject to considerable challenge by the CCG, which included a specific meeting of a sub-group to discuss and finalise the Outcomes. The Company was very receptive to those challenges and significantly modified both its general approach to the development of the Outcomes and the specific commitments as a result of its engagement with the CCG. Each Outcome, along with details of proposed activities and measures of success is now detailed in accordance with CCG recommendations within the 'Our Commitments' section of the Business Plan.
74. The Outcomes themselves are defined on a high level basis by the key outcome statements produced by the Company. The main changes that occurred to these outcome statements as a result of CCG challenge are as follows:
- A long term focus was placed on drinking water quality and an outcome reflecting the Company's community role was added to reflect customer priorities;
  - The wording was generally changed to reflect commitments rather than aspirations, and most became 'true' outcomes in the sense that they describe end results in the past tense;
  - Carbon reduction was added as this represents a key priority for customers.
75. There was also sustained challenge from the CCG with respect to the measures of success associated with the Outcomes; adapted from initial statements that concentrated on activities, to commitments for delivery with associated KPIs where appropriate. Measures of success and associated KPIs were reduced in number and complexity as a result of the CCG challenge and the CCG is now confident that both the measures of success and KPIs that underpin the Business Plan present a clear, quantifiable commitment to customers. The measures of success were used as the main description of the commitments that the Company used in its customer consultation and acceptability testing for the Business Plan.
76. The CCG also challenged the Company to use KPIs that were, where appropriate, aspirational rather than 'business as usual', even in those areas where specific customer preferences for enhanced service measures had not been identified. This included commitments to share financial out-performance benefits with customers. Comments on the KPIs that resulted from this challenge process are provided in the next section.
77. The final area of challenge with respect to the development of Outcomes and consultation on measures of success was to enable both the CCG and customers to view these in the context of the Company's current commitments and achievements during AMP5. Again, the Company responded appropriately to this challenge and provided clear information about AMP5 achievements to the CCG and as part of its customer consultation on the Business Plan. The 'Current Record' is clearly shown within the 'Our Commitments' section of the Business Plan.

#### **3.2. Compatibility of Outcomes with Customer and Stakeholder Preferences**

78. The CCG's view on the identification of customer priorities and the interpretation of these priorities into broad level commitments is detailed within Section 2.4 of this Report. This section concentrates on the specifics of the Outcomes that have been derived from those broad commitments, and their compatibility with the customer research evidence that the Company collected.
79. As noted previously, the initial proposals were not very clearly linked and hence subject to challenge from the CCG Outcomes technical sub-group. Following this refinement process, the CCG now considers that there is a reasonably clear link between the measures of success for

the Outcomes, and the interpretation of the customer preferences as described in Section 2.4. Specifically the CCG notes that:

- There are commitments to maintain drinking water quality and asset serviceability to ensure safe, reliable long term water supplies. These are supported by KPIs that either seek to maintain current service measures, or deliver minor improvements as demonstrated by the KPI for customer complaints. There is a commitment to provide better information on hard water and lead (Pb), which reflects the interpretation of customer preferences as discussed in Section 2.4;
  - There is a commitment to a reduction in leakage, although this is only down to just below the Company assessed ELL. As noted in Section 2.4, some members of the CCG consider that this is not entirely reflective of customer preferences and the Company could adopt a more ambitious target for this KPI. Technical assurance on the derivation of the ELL is discussed within Section 4.2.1;
  - In terms of customer preferences for service and 'value for money', the commitments are clear and specific. As well as the commitment to bill increases that are no more than RPI (as discussed in Section 2.4.2), there is a longer term, absolute commitment to maintain bills at less than 0.5% of average earnings. The Company responded to the CCG challenge for aspirational KPIs by including commitments for improving customer experience (through the Service Incentive Mechanism (SIM) regulatory reporting score) and an improvement in first time resolution of issues (to 90%). For the SIM score, there is a commitment to maintain the Company's position in relation to the rest of the water industry. This has been done to provide an incentive to adopt innovations that might become available to the industry in the future;
  - For the protection of the environment, there are quantified KPIs that commit to reductions in the Company carbon footprint and early delivery of National Environment Programme schemes, which have been included to reflect customer preferences for improved service measures in those areas. Although an increased provision of water efficient devices or enhanced metering activities has not been included within the measures of success, there is a commitment to enable reductions in personal consumption. As noted in Section 2.4, the inclusion of this measure of success within the environment Outcome statement reflects the clear customer preference to enhance biodiversity, which has been interpreted as being best met through a general reduction in demand and hence abstraction pressures;
  - There is a commitment to support the community and local economy. The measures of success associated with this were increased following CCG challenge to include the stated commitments to developers, school education, local procurement and support for water efficiency to business customers. The Company has also included a quantitative commitment within this Outcome, based on procurement from local suppliers and Developer satisfaction.
80. There are a number of measures of success and associated KPIs that reflect the Company's interpretation of customer's preferences to maintain, rather than improve, customer service in certain areas. This includes commitments on hosepipe bans and interruptions to supplies. Again, these are quantifiable through existing reporting systems.
81. The Company has stated a number of commitments that relate to financeability. These are largely outside the CCG's remit, but the CCG has provided challenge in relation to the long term finance strategy and the implications that assumptions about historic out-performance and constraints relating to debt servicing have had on the flexibility that the Company might have in using financing options to reduce customer bills. These are discussed in Section 2.4.2.
82. The CCG notes that there is no Outcome commitment within the Business Plan in relation to vulnerable customers. The CCG understands that this is partly because joint proposals are being considered with Southern Water. The CCG challenged the Company to include some

form of commitment within the Business Plan text, and commentary on affordable tariffs has been included within the 'debt and affordability' section of the Retail Business Plan.

Due to the separate service supply and billing for water supply and waste water collection and treatment in the Company's area of operation, the Company says that it *'would like to offer a Social Tariff and that they have been closely watching Southern Water's development of such a tariff'*.

At this stage the CCG understands that Southern Water has agreed in principle to allow the Company to mirror its proposals, and hence provide a combined affordable tariff for water supply and waste water services. However, the provision of the tariff is still dependent on Southern Water's adoption of the scheme and the Company has indicated that it will need to 'gain customer approval' before the tariff is adopted.

### 3.3. Outcome Delivery Incentives

83. The majority of the incentives proposed are either reputational, or relate to regulatory incentives (SIM) or statutory penalties (drinking water quality). The three measures of success where it has chosen financial penalties (and rewards in two cases) have been chosen for understandable reasons, which primarily relate to the fact that they are largely controllable by the Company and can be accurately reported through existing systems.
84. The CCG provided substantial challenge to the development of the ODIs where financial penalties or rewards are being proposed, as it considers there are significant uncertainties with any methodology that seeks to quantify customer opinion on this issue. The specific academic concerns that the peer reviewer had in relation to the method that was adopted, and the Company response on this, can be found in the relevant reports and are not detailed here. Nevertheless, the Company has sought to do this directly based on customer's views through its methodology, and the actual likely potential effects of the rewards and penalties that are involved are very small, which reflects the relatively low WTP values that were elicited from customers during the surveys.
85. The CCG understands that the inclusion of a financial reward for leakage is intended to incentivise the Company to use any efficiency improvements in leakage control to achieve lower leakage levels, rather than increase leakage expenditure. This appears to be in line with customer priorities.

### 3.4. Summary Views on the Outcomes and Incentives

86. The CCG considers that the Company adopted a very open and responsive approach to the derivation of its Outcomes, and significantly adapted both its approach and the nature of the outcomes as a result of CCG challenge. The adoption of clear commitments for delivery with associated KPIs, which match to customer priorities and are set within the context of current achievements, has resulted from an ongoing process of challenge and engagement between the Company and the CCG. Following this refinement process, the CCG considers that there is a reasonably clear link between the measures of success for the Outcomes, and the interpretation of the customer preferences as described in Section 2.4.
87. The issues and general conclusions made in relation to the interpretation of customer preferences within Section 2.4 are generally reflected within the Outcomes and measures of success. Other than some reservations amongst some members of the CCG in relation to commitments on leakage, the CCG considers that the proposed Outcomes can be generally mapped through to customer preferences. Whilst there are inevitable uncertainties in this process, the CCG notes that the proposed Outcomes and measures of success formed the summary of the Business Plan that was used in the customer acceptability testing, and customer acceptance of those proposals was very high.



88. In terms of the proposed financial incentives and penalties for the ODIs, the CCG notes that the Company has attempted to link these directly to customer surveys, but has reservations about the accuracy of any such approach. The CCG acknowledges that there is an expectation from Ofwat that quantified ODIs will be proposed, and the actual rewards and penalties that are involved are very small, so are unlikely to significantly influence Company behaviour or customer bills. This is generally reflective of the low WTP values that were elicited from customers.

## 4. Business Plan Costs, Risks and Rewards

89. This Section comprises two components, namely; a review of how well the delivery incentives and explanatory variables within the Business Plan comply with the Outcomes and ODIs discussed in Section 3, and a review of how well the expenditure proposals meet the Outcomes, statutory obligations and longer term Company objectives.

### 4.1. Delivery Incentives and Explanatory Variables

90. Because the Company has stated its KPIs in terms of measureable outcome values, the compatibility between the Outcomes - as described in Section 3 and the Business Plan tables - is clear and straightforward.
91. For the incentives described in Table W2, the CCG has been provided with independent technical assurance and can confirm that the evaluation of ODIs is compatible with the results and analysis of the customer research that was presented to the CCG during the sub-group meetings.

### 4.2. Expenditure Proposals

92. The CCG challenge into the compatibility between the proposed expenditure contained within the Business Plan and the customer priorities described in Section 2.4. comprises three elements:
1. A challenge of how well the proposed programme of capital expenditure, as presented to the CCG, will actually meet customer priorities;
  2. Opinion from the Environment Agency and the DWI on whether or not the proposed Capital Programme delivers statutory obligations;
  3. Challenge about the affordability and value for money that is contained within the expenditure proposals.
93. The outcomes of these three areas of challenge are provided in the following sections.

#### 4.2.1. Compatibility with Stated Outcomes

94. Significant challenge was applied in relation to proposals for investment in asset maintenance, and assurance was sought from the Company to demonstrate that their proposed activities would maintain existing service levels in relation to drinking water quality and supply interruptions. The Company was able to demonstrate that the Business Plan activities were in line with longer term expenditure requirements, and that variations from historic maintenance expenditure generally related to exceptional items and new obligations such as the need to replace membrane filters. The independent technical assurer provided the following statements in relation to capital maintenance expenditure:
1. For distribution mains, the Company amended its forecasts as a result of the assurance challenge. Following those changes, it was noted that *'overall we consider that the model forecasts [of activities required to maintain burst rates] are reasonable and supportable'*.



For trunk mains it was confirmed that *'it does not appear that the Company is taking excessive risk in not allocating expenditure to trunk mains in AMP6'*;

2. For non-infrastructure assets, again following challenge and amendments, it was confirmed that *'the proposals for the maintenance of sources, treatment works, pumping stations and reservoirs therefore appear to be a realistic reflection of the costs required to maintain the Company's assets in both the short and medium term'*.
95. The CCG further challenged the Company in relation to drinking water quality to confirm that the approaches to mains renewals and non-infrastructure asset maintenance would maintain drinking water quality. This was confirmed through discussion and input from both the DWI and technical assurer. It was also confirmed that cost items to improve disinfection, as noted in the Company Business Plan, are included within the AMP6 maintenance proposals.
96. For the large expenditure associated with the Farlington wash-water scheme, the Company provided the CCG with detailed explanation of the need and risks associated with the current situation. Whilst it is apparent that there is considerable uncertainty over the required solution, assurance was provided over the current level of operational cost risk and the risk to Company finances if a robust solution is not implemented.
97. Comments relating to the needs and proposed schemes to address deteriorating raw drinking water quality, meet the requirements of the WRMP and meet statutory environmental obligations are provided in Section 4.2.2 below.
98. For leakage, it was confirmed by the independent technical assurer that the proposed expenditure relates to a level of leakage that is slightly below the most realistic assessment of the ELL.
99. Based on the above, it is apparent to the CCG that the Company has demonstrated consistency between the activity proposals contained in the Business Plan and the Outcomes associated with drinking water quality, interruptions to supply, leakage, and the performance of assets. Other measures of success were reviewed and either form part of the statutory obligations, as discussed below, or can be delivered within current organisational structures and hence levels of operational expenditure. Metering will remain at optant only levels, in line with the stated Outcomes.

#### **4.2.2. Statutory Requirements**

100. Environment Agency representatives have regularly attended the CCG. Included in Appendix B of this report are copies of the relevant correspondence between the Environment Agency and the Company (dated 1st and 21st November). The comments in this correspondence were made following dialogue with the Company throughout the business planning process and WRMP process including the Statement of Response up to the date on the relevant correspondence. These comments were made without having seen the final Business Plan. The Environment Agency expects to continue to work with the company on some of the details of proposals however it does not anticipate any material changes in its overall response. In terms of meeting statutory environmental obligations, the Environment Agency has summarised that the Company has:
  1. *'worked well with us to remove uncertainty from the National Environment Programme (NEP), are positive about catchment management and have a biodiversity strategy for your own sites where you plan to implement 90% of the actions by 2020'*;
  2. *'presented sufficient information... to demonstrate how the Business Plan will allow the Company to meet the statutory environmental requirements set out in Defra's Statement of Obligations.'*

3. *[agreed] to include all of the measures set out in the NEP within the Company's final Business Plan. We believe that the programme will allow the Company to deliver what is best for both the environment and the Company's customers.'*

101. The Environment Agency has also received assurance from the Company's Board that it has included the confirmed and/or likely sustainability changes set out in NEP phase three in the water resources supply-demand component of its Business Plan, considered whether planned increases in abstraction may cause deterioration in WFD water body status and considered which abstractions would fall within Ofwat's Abstraction Incentive Mechanism.
102. In the Environment Agency's view, from the information provided, it understands that the company is planning to meet its statutory environmental requirements set out in Defra's Statement of Obligations, and it welcomes the company's commitment to meeting them. Within its correspondence to the Company it also states that *'in so far as the comments herein relate to the natural environment, they also reflect the advice of Natural England'*.
103. As well as comments relating to the detail of the WRMP, reservoir safety and resilience, the Environment Agency has made two recommendations within its response. The first of these relates to change mechanisms for AMP6. This is a regulatory matter between the Company and Ofwat and is not within the remit of the CCG to comment upon. The Environment Agency has also commented on the interpretation of customer preferences in relation to the leakage target. This has been reflected within the discussions contained in Section 2.4.3 of this report.
104. A full copy of the DWI's letter of representation to the CCG is provided in Appendix C. In summary, the Company submitted seven formal proposals for drinking water quality to the Inspectorate. They commended the Company on the quality of the submissions to the Inspectorate, which were received in part by the published deadline of 31st July 2013, and which complied with the DWI PR14 guidance. The DWI has formally supported three of the Company's proposals and will put legal instruments in place to make the proposals legally binding programmes of work. In addition, they commended three proposals for support.
105. The letter confirms that:
  - the package of measures included in the Company's lead (Pb) strategy will improve compliance with the new standard for lead (Pb) and reduce consumers' exposure to lead from drinking water;
  - the proposed scheme for increasing the resilience of water supplies is consistent with the requirements of Defra's Statement of Obligations published in October 2012, and the Inspectorate's guidance on principles for the assessment of drinking water quality provisions within the PR14 process, as set out in DWI Information Letter 01/2013, published on 1st February 2013;
  - the proposals for Distribution System Operational Maintenance (DOMs), and improvements to disinfection arrangements are consistent with the requirements of Defra's Statement of Obligations, and the DWI's guidance on principles for the assessment of drinking water quality provisions within the PR14 process, as set out in DWI Information Letter 01/2013;
  - The DWI supports the need for *cryptosporidium* controls at two sites and intends to issue a Notice under Regulation 28(4) of the Water Supply (Water Quality) Regulations 2000;
  - The DWI supports the Company proposals for the control of nitrates at groundwater sources as an appropriate means of contributing to delivering wholesome water in the longer term, and will include the proposal in a regulation 28(4) Notice;
  - In addition, the letter noted that these improvement schemes will make only a small, if significant, contribution to enabling the Company to meet its legal obligations in respect of drinking water quality. These obligations are met overwhelmingly by the Company making

sufficient provision for operational and maintenance requirements in its business plan, and by its use of those resources. These are matters for the Company to determine and deliver. For its part, the Inspectorate will continue to keep under review, and report on, the performance of the Company in meeting its legal obligations. Statutory powers are available to secure or facilitate compliance, if necessary.

106. The Company has demonstrated to the CCG that all of the schemes that were contained in the proposals and that were either formally supported or commended have been included within the PR14 Business Plan proposals. This includes the requirement for turbidity control associated with the *cryptosporidium* schemes.

#### 4.2.3. Affordability and Value for Money

107. Based on the interpretation of customer preferences and the associated outcomes, and the high level of customer acceptability of the proposed Business Plan, the CCG considers that the Company has demonstrated that customers would prefer a plan that at least maintains current service levels. The Company also provided evidence that the investment activities that are proposed within the AMP6 Business Plan are reflective of these preferences.
108. As noted in Section 2.4.2, in terms of affordability, it is apparent that customers are willing to accept bill increases that are in line with RPI inflation in order to pay for these investments. However, the CCG exerted challenge on a number of points to determine whether bill increases that are in line with inflation are actually necessary to deliver the proposed Business Plan Outcomes and statutory obligations. The key responses to those challenges are discussed below.
109. The operational efficiency of the Company and its expenditure proposals were challenged in relation to staff costs, energy expenditure and past efficiency achievements. Whilst the Company did not consider that issues such as potential wage increases were within the remit of the CCG to challenge, it did provide evidence of its comparative efficiency against other water companies in England and Wales. On an aggregate level the Company provided evidence that shows it clearly at the forefront of comparative operational efficiency within the water industry. It is also proposing an additional 0.25% per annum efficiency over AMP6, has identified some additional IT savings, and is prepared to share its outperformance within AMP5 with its customers in order to keep bill increases down.
110. In terms of the efficiency of the proposed capital investments, the main challenge was provided through the independent technical assurance. This relied on a combination of Ofwat's past assessments of comparative efficiency, benchmarking exercises carried out by the Company and efficiency achievements that have been made through tendering and capital management in AMP6. Detailed comments from this challenge are provided within the technical assurance document in Appendix A, but in summary it was found that the Company's PR14 costs are at or around the 'benchmark' level of efficiency. Some potential improvements were identified, but these were generally small (less than 5%), only covered part of the capital programme and the Company indicated that it may increase the risk that it has to cut the scope of its capital programme, and hence its ability to maintain service levels in the longer term, if they are included 'up front' within the Business Plan allowances.
111. Because the Business Plan already allows for a return of out-performance to customers, and opportunities for efficiency are limited, the Company explained that the only remaining options for reducing bill levels below RPI would therefore be to cut the scope of its capital maintenance expenditure, or save money through its financing options. Based on the evidence provided, cutting investment may increase risks to serviceability of the Company's assets in the longer term, which does not seem to be aligned with customer preferences. Options for savings through financing were considered to be beyond the technical scope of the CCG, although the Company did share with the CCG the difficulties and financing risks that it considers it would face if it tried to reduce the WACC below the levels proposed within the PR14 Business Plan.
112. Finally, the CCG notes that the Company has committed within its Business Plan to sharing AMP6 outperformance, so in the interests of affordability, it will pass on efficiencies that it does

achieve in excess of the Business Plan assumptions to its customers. The CCG did express a preference for more specific proposals about the proportions and mechanisms that would be adopted, but time constraints meant that this could not be fully explored prior to reporting. However this does show that, if there are efficiency gains that can be made beyond those assumed in the Business Plan, then the customers will benefit either through reduced bills or increased expenditure on asset maintenance.

### **4.3. Balancing Risks in the Longer Term**

113. Within its Business Plan, the Company has committed to a key message that the plan should be 'financeable and sustainable for the long term'. Therefore the CCG requested that assurance be provided that the expenditure proposals were consistent with a sustainable, long term maintenance strategy that was intended to both maintain assets in the long term, and meet the Company objectives in relation to longer term affordability.
114. The independent assurer confirmed that the levels of capital maintenance that are proposed for both infrastructure and non-infrastructure are clearly aligned with the Company's current best estimate of the longer term expenditure that will be required to maintain asset serviceability. The Company has been open and transparent on this point, and the CCG notes that it adjusted its forecasts and AMP6 spend on infrastructure as a result of the assurance challenge process. Therefore, although there is inevitable uncertainty in the forecasts, the evidence that is available suggests that the maintenance expenditure proposals do form part of a longer term sustainable plan.
115. In terms of other risks, the CCG notes that investigations to resilience are being undertaken within AMP6, and the Environment Agency has been generally positive to the Company's approach to identifying and managing potential environmental requirements beyond AMP6. The Environment Agency has noted that a greater commitment to enhancing metering activity and leakage control could help to improve resilience in the longer term, but accepts that this would put pressure on customer bills and hence affordability in the shorter term.
116. The DWI has indicated to the CCG that it is supportive to the Company's approach to managing and monitoring for drinking water quality risks, and does not have any specific concerns about the potential longer term maintenance of drinking water quality.
117. The sustainability of the Company's financing position is beyond the CCG's technical remit, but information was provided that confirmed it had considered implications of movements in WACC and interest covers beyond AMP6.

## 5. Conclusions

118. The intention of the PR14 process was that the CCG should be able to provide meaningful comment on the Company's customer engagement and the development of its Business Plan as a result of that engagement. This meant that the CCG itself had to be meaningfully engaged and informed during the development of the customer engagement process and the Business Plan.

The CCG's considered opinion is that the Company has invested the time necessary to provide for this engagement, has provided information as required and been very open in its approach and dealings with the CCG. There has been a genuine process of challenge and modification of both the Company's customer engagement and the Outcomes within its Business Plan as a result of that challenge.

119. The nature of the PR14 price review process means that there have been time pressures, and it has not been possible to consider all points in detail and hence reach a full consensus conclusion on every issue that has been raised for discussion and challenge. These have been identified where appropriate within this report, however, overall the CCG considers that it has had sufficient information and time to gain an adequate understanding and reach a considered opinion for the purposes of reporting to Ofwat.

### 5.1. Comments on the Quality of the Company's Customer Engagement

120. In terms of the process and strategy used by the Company for its PR14 customer engagement, the CCG is satisfied that this was consistent with the consultation needs, considering the Company's current low level of bills and relatively small AMP6 capital programme. A more extensive process is unlikely to have resulted in different Outcomes that could have improved customer acceptability of the Business Plan by any significant amount, so is unlikely to have provided value for money for the Company.
121. The Company's approach to customer engagement was in line with the UKWIR Code of Practice principles and individual survey methods used for customer research. This was confirmed as being acceptably designed and implemented by Peer Review.

The derivation and interpretation of the Outcomes was an uncertain process, and the CCG did have a number of queries and concerns about the mapping of customer research to the identified customer preferences. However, the Company carried out a number of modifications and provided clarifications in response to the CCG challenges and was able to demonstrate support for its interpretation for most of the Outcomes.

The initial evaluation of customer preferences through qualitative research was open and unbiased, and there was a reasonable link between this and the subsequent quantitative research. The Company accounted for the inherent limitations of the industry standard approaches for quantitative customer research that are generally available by using WTP to rank and inform the interpretation process, rather than using the WTP values directly.

### 5.2. Comments on the Extent to which the Business Plan Reflects Customer and Stakeholder views

122. The key to demonstrating a link between customer views and the Business Plan lay in the way in which the Company interpreted customer preferences based on the qualitative and quantitative research that it had carried out.

Some members of the CCG did highlight the fact that there was an inherent tension between customer preferences for affordable bills, and the WTP for service improvements that was expressed in the quantitative research for areas such as leakage control. Although this was not agreed by all CCG members, this did raise some concerns that the Company's interpretation

that customers would prefer leakage to be reduced to a level that was just below the ELL, was not ambitious enough. In response, the CCG notes that the Company has indicated that it will endeavour to adopt new technologies for leakage control that become available to reduce leakage, if this can be achieved without placing additional pressure on customer bills.

Concerns were also raised about water efficiency and metering, although these were largely addressed by the Company's adoption of a PCC target as one of the measures of success for the Business Plan. Other than this, the CCG considers that the Company's interpretation of customer research into customer preferences was reasonable, and reflected the customer priorities expressed in the surveys.

The CCG particularly notes that the acceptability testing carried out by the Company for its Business Plan demonstrated overwhelming customer support for the proposed level of bills and the Outcomes. Any uncertainties in the process did not seem to affect the overall validity of the Company's interpretation of customer priorities.

123. The CCG considers that the Company adopted a very open and responsive approach to the derivation and definition of the Outcomes, and significantly adapted both its approach and the nature of its stated Outcomes as a result of CCG challenge. Following this refinement process, the CCG considers that there is a reasonable link between the Company's interpretation of customer priorities, the Outcomes and the associated measures of success that have been detailed within the Business Plan.
124. Some of the stakeholder members of the CCG were concerned that there were no specific commitments to vulnerable customers within the Outcomes, given the recent high profile of affordability and social tariffs within political and media circles.

The CCG therefore challenged the Company to include commentary and commitment on affordable tariffs within the Business Plan. This is now included within the 'debt and affordability' section of the Retail Business Plan.

125. The CCG notes that the issue of affordability was the focus of considerable regulatory and political pressure during the development of the Business Plan. During qualitative research, customers also indicated that water supply charges 'remaining affordable' is of significant concern.

'Affordability' of the Business Plan proposals was therefore a key element of the discussions between the CCG and the Company, and the Company's assertion that water supply charges that increase in line with nationally reported Retail Price Index (RPI) inflation is acceptable to its customers was subjected to considerable challenge by the CCG.

Overall, the Company provided strong evidence that the customer priority for affordable bills can be expressed as a preference for the lowest reasonable bill levels that are able to support the Outcomes proposed in its Business Plan. Based on the evidence provided, the CCG also considers that the Company demonstrated that customers would clearly prefer a Business Plan that maintains current service levels, rather than a Business Plan that proposes a reduction in service levels in order to reduce customer water supply charges. Because customer preferences were relatively clear on this matter, the CCG challenged the Company to demonstrate the following two points:

1. Whether the Business Plan adequately reflects the appropriate level of operational, maintenance and investment activities that will be necessary to deliver the proposed Outcomes;
  2. Whether the expenditure associated with those activities is reasonably based and efficient so that the Business Plan can be shown to be consistent with the affordability priority.
126. In relation to the first point, the information and independent assurance provided meant that the Company was able to demonstrate consistency between the activity proposals contained in the Business Plan and the Outcomes associated with drinking water quality, interruptions to supply,

leakage, and the performance of assets. Other measures of success were reviewed, and it was noted that they either form part of the statutory obligations, as discussed below, or can be delivered within current organisational structures and hence levels of operational expenditure. Metering will remain at optant only levels, in line with the stated Outcomes.

127. The Company was also able to demonstrate that the Business Plan activities were in line with longer term expenditure requirements, and that variations from historic maintenance expenditure generally related to exceptional items and new obligations such as the need to replace membrane filters.
128. In relation to the second point, it is noted that it is not necessarily within the CCG's remit to provide comment on whether Business Plan cost proposals have been reasonably and efficiently derived. However, in response to the challenges that were made, the CCG considers that the Company was able to demonstrate the relative efficiency of its operational expenditure, and provided technical assurance that it was adopting a reasonably efficient approach to its capital investment proposals.

The CCG notes that the Company has committed within its Business Plan to sharing AMP6 outperformance with its customers, such that in the interests of affordability, it will pass on efficiencies that it does achieve in excess of the Business Plan assumptions. This indicates that opportunities for efficiency are therefore limited; given that, and because the Business Plan already includes a commitment for an early return of AMP5 out-performance to customers, the Company explained that the only remaining options for reducing bill levels below RPI would be to cut the scope of its capital maintenance expenditure, or save money through its financing options.

The Company has demonstrated to the CCG that opportunities for savings through financing are limited, but this constraint is considered to be outside of the CCG technical remit to challenge further.

129. Based on the above, it is therefore apparent that the Company has sought to balance the priority for affordability with the other stated Outcomes, and that this has formed the cornerstone of its Business Plan.
130. The CCG notes that there is an expectation from Ofwat that quantified ODIs will be proposed by companies in PR14. The Company has linked its ODIs directly to customer priorities, and includes a financial reward only where there is some evidence of customer support for further improvement. The CCG expressed reservations about the appropriateness of the methods that are needed to quantify customer preferences into ODIs, but notes that the financial rewards and penalties that the Company has proposed are comparatively small, and only relate to three outcomes. Their potential impact on future bills is therefore considered to be correspondingly small.

### 5.3. Comments Relating to Statutory Obligations

131. In the Environment Agency's view from the information provided, it understands that the company is planning to meet its statutory environmental requirements set out in Defra's Statement of Obligations, and it welcomes the company's commitment to meeting them. Within its correspondence to the Company it also states that *'in so far as the comments herein relate to the natural environment, they also reflect the advice of Natural England'*.
132. The DWI has provided feedback on all of the Company submissions it has made relating to drinking water quality schemes. Of these, the DWI has formally supported three of the Company's proposals and we will put legal instruments in place to make the proposals legally binding programmes of work. In addition, they have commented for support three proposals. All of the schemes that were included within the Company submission for these six proposals have been included as appropriate within the Business Plan.

# Appendix A: Technical Assurance and Peer Review Summaries

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# Technical note

<b>Project:</b>	Portsmouth Water Reporter	<b>To:</b>	CCG Members
<b>Subject:</b>	Update on Assurance Findings Version 2	<b>From:</b>	Doug Hunt
<b>Date:</b>	7 Nov 2013	<b>cc:</b>	

## Introduction and Objectives

This technical note provides a summary of the current findings of the assurance process that Atkins has undertaken for Portsmouth Water's PR14 Business Plan submission. It includes both the original assurance items that were discussed with Portsmouth Water at the start of the process and additional items requested by the CCG. The findings contained within this note have been based on the following sources of information:

- Face to face audit meetings and document & data review for the infrastructure and non-infrastructure capital maintenance costs, and capital efficiencies associated with those costs.
- A face to face audit review of the August submission to Ofwat and subsequent discussions at the CCG meetings in relating to base operational costs
- Document review for the Economic Level of Leakage assessment and the cost/benefit evaluation of metering
- Document review for catchment management costs
- General discussion relating to the approaches to trunk main and non-infrastructure asset management processes
- Document review and subsequent discussions at the CCG meetings in relating to quantitative customer research

The key findings relating to each of these items are provided below.

It should be noted that all of the costs that we have reviewed to date either reflect the capital costs that Portsmouth Water currently experiences (e.g. distribution mains), or contractor/consultant estimates. Whilst we have therefore reviewed the appropriateness of the proposed schemes and activities included in the capital programme, we have not yet been provided with any estimates of potential procurement/capital delivery efficiencies.

## Key Findings by Area

### ***Infrastructure Capital Maintenance (incl. distribution mains, trunk mains & communication pipes)***

The average annual renewals rates for distribution mains (i.e. the length of poor condition mains replaced each year) that are required to maintain burst rates and hence average customer interruptions in the network have been calculated based on modelling by a well respected consultancy (WRc). Whilst there are uncertainties in the analysis, overall we consider that the model forecasts are reasonable and supportable. The model also included potential forecast trends in leakage caused by mains renewals activities, but our investigations concluded that these calculations were too uncertain to base strategic decisions upon. The Company therefore took a pragmatic approach and focused its strategy on maintaining burst rates. We do not consider that there is a significant risk that leakage will be significantly impacted by this decision and the overall strategy is designed to maintain the serviceability of distribution mains.

In terms of unit costs and cost efficiency, Portsmouth Water's open cut mains laying rates at least match the industry 'benchmark' (as it stood at PR09), and may be 1% to 2% more efficient than the industry standard. The approach to delivery was decided upon following market testing after the FD09 had been received, and it appears that this has been successful as the Company is able to achieve good rates using local contractors and 'conventional' forms of contract. There is some evidence to suggest that the 'no-dig' techniques are less efficient, however even if 25% of mains renewals become 'no-dig', for AMP6, a potential efficiency improvement of 10%-20% in open cut techniques would only improve overall costs by around 2.5% - 5%. Given the probable efficiency of the open cut renewals, the overall net potential for efficiency in the aggregated mains renewals rate is likely to be less than 3%.

Because Ofwat's new approach to efficiencies will be based on the average cost per metre 'all in', we do have some concerns about the lack of detailed information that the Company currently has about the costs

# Technical note

associated with mains laying in different surface types. This means that cost/benefit ratios are not currently a formal part of the identification of renewals schemes in a way that links through to the longer term maintenance strategy. We are aware of a number of companies that are introducing methods for reducing aggregate mains renewals costs by looking to deliver the lowest cost mix of schemes that will maintain network serviceability (i.e. when ranking schemes for renewal, the likely cost is taken into account, as well as the burst and customer risk benefits). This can yield significant efficiencies (10%+) under some circumstances, but it takes a long time to implement these approaches, and the realisation of significant benefits within the AMP6 period may be difficult.

For trunk mains there is no expenditure proposed for either investigation or renewals in AMP6. This is mainly because the current trunk main investigation programme is showing that condition related risks are generally in line with expectations and there are no significant concerns over trunk main failures in the AMP6 period. The approach that was explained to us is reasonable and it does not appear that the Company is taking excessive risk in not allocating expenditure to trunk mains in AMP6.

## ***Non-Infrastructure Capital Maintenance and Water Quality Schemes***

Our most recent assurance audit confirmed that the Company has addressed issues associated with 'double counting' of maintenance needs generated by the three different approaches that they have used, and the revised programme is generally a realistic reflection of AMP6 maintenance needs. As a result of our challenges, and following internal review, the Company has also identified opportunities for reducing expenditure below the costs provided at the September CCG, which includes the following notable items:

- For control panels and air contact breakers, the Company has been able to identify replacements that can be extended beyond AMP6 as a result of 'scavenging' of components to avoid obsolescence.
- For dechlorination of run to waste facilities, a greater acceptance of risk has been adopted, and work on lower risk discharge facilities has been deferred to AMP7. This is a minor environmental risk that does not affect customer's water quality.
- For the membrane plants at Farlington, we challenged whether costs could be avoided if a UV plant is used instead. This has been reviewed and a similar 'scavenging' approach has been adopted, along with a move to UV as part of the washwater recovery scheme described below.

This removed approximately £3.1m from the capital programme, and costs for 'core' capital maintenance are now very similar to historic levels of expenditure. They also reconcile well with the longer term maintenance models that the Company has produced in accordance with reasonable industry practice. The proposals for the maintenance of sources, treatment works, pumping stations and reservoirs therefore appear to be a realistic reflection of the costs required to maintain the Company's assets in both the short and medium term.

In terms of the cost efficiency of these 'core' non-infrastructure works, the key comparison that we used to benchmark PR14 cost efficiency was to compare the costing methods against the scheme costs that are currently being achieved for AMP5. As with infrastructure works, the choice to continue delivering in AMP5 using a small in-house team and preferred contractors on an individual contract basis was made following market testing after the FD09 had been received. This has been largely successful and the Capital Programme is mainly on track to deliver the circa 10% efficiency challenge set by Ofwat, which should now place the Company within the accepted industry 'benchmark' efficiency range. It appears that a proportion of the efficiency that has been achieved in AMP5 has been included in the costs that have been developed for the PR14 business plan. However, we did note that some of the approaches, such as scheme bundling and 'smart solutions' that have been used in AMP5 do not appear to have been reflected in the PR14 Capital Programme costing. A proportion (probably less than half) of the 10% efficiency approaches that have been applied in AMP5 may therefore still be available to apply to the costs that have been developed for PR14.

In terms of 'exceptional' schemes, we note that the costs for the washwater recycling plant Farlington, and the cryptosporidium & turbidity treatment at Eastergate and Westergate have escalated since the September CCG. This is due to a simple misunderstanding from the contractor that was providing the costs for these schemes, who had initially provided costs for construction only, and did not include allowances for contractor risks, profits, insurances etc. These have added up to 60% onto the scheme costs (£3.15m). This is fairly typical of the uplifts that we would normally see for such schemes, and is comparable to our recent reviews at other Water Only Companies.

# Technical note

Although we have been provided with relatively high level costings for the schemes, it is clear that they have been put together by an experienced Design & Build contracting partnership, the reports have included adequate optioneering and we did not have any major concerns with the unit costs involved. Some of the unit costs (e.g. for buildings) are at the upper end of the realistic range, but this was not found to be significant in relation to the overall scheme cost. We note that Portsmouth has added a 10% client cost contingency (in addition to identified management costs). This is a nominal allowance that is difficult to assure, as Portsmouth has relatively little historic evidence of client risks for large design & build schemes of this type. It was not possible to reasonably comment on the overall cost efficiency of the exceptional items and enhancement schemes on an absolute basis, however, we can confirm that we did not encounter anything within the costing exercise that leads us to consider that the costs were either inefficient or over-inflated.

In terms of need, we have been informed that the cryptosporidium treatment at the Eastergate and Westergate schemes has been supported by the DWI. Although there is a turbidity issue, this is currently being reviewed and discussed with the DWI. For the cryptosporidium treatment itself, the use of UV plant seems to be the lowest cost solution to the risk that has been identified.

The Farlington washwater recycling scheme has been proposed for two reasons:

- We have seen evidence that Southern Water are now seeking to charge for the discharge into their sewer, in accordance with the industry standard Mogden formula. This could cost up to £400,000 per annum. This level of charge could be disputed, but there will be a cost and the risk is considerable.
- The Environment Agency may require a discharge consent, which could be problematic as this is an untreated discharge directly to the Solent. If a discharge consent is not provided, then disposal costs would escalate, possibly up to £800k per annum, and a new connection to a foul sewer would also be required.

The need for some form of works at Farlington is therefore clear. Following our queries at audit, Portsmouth have indicated that they will be seeking to remove the membranes and replace the treatment with ultraviolet (UV), which will save on membrane replacement and hence costs in the long term. We have reviewed the report that has been produced to support the preferred scheme, and note the following:

- The solution that has been adopted is the most expensive of the feasible options, and represents a low risk position. However, whilst it is apparent that there are options that could be further investigated for cost reduction (possibly up to £1.7m of the scheme cost), these would all need time to investigate, either through monitoring for water quality, or investigations and negotiations over discharge consents. Unfortunately the Southern Water charges mean that significant costs could be accrued during optioneering, so risks to final outturn costs are significant if time is taken to investigate lower cost options.
- The proposed solution incorporates a 'staged' position that is approximately £350k more expensive than an immediate implementation of the full solution. This has been adopted to avoid having to incur costs until the AMP6 period.
- There are still some significant financial risks associated with the accrual (and possible back-payment) of discharge costs before the staged scheme is implemented. It is not yet been decided how these operational costs will be managed through the Business Plan process.

## ***Catchment Management and Other NEP/Biodiversity Schemes***

We have reviewed the basis of the catchment management proposals and note the following:

- There is a reasonably well identified need to address rising trends in nitrates caused by pollution in the catchment, but there are uncertainties over the age of the nitrates involved and hence the likely long term risk and effectiveness of catchment management. Around half of the proposed expenditure (£600k) therefore relates to investigation and modelling activities that have been costed in detail by consultants with specific experience in this area.
- The remaining £600k costs relate to initial catchment management activities. The scope of this is uncertain, but seem to reflect a realistic programme. It could be argued that these activities might be delayed until the above investigations are complete, but there is a real risk that this could reduce the

# Technical note

ability of catchment management to address the issue and hence result in higher total costs if nitrate removal plants become necessary.

Other costs in this category are small and have been reasonably costed based on investigation needs and staff time requirements.

## ***Economic Level of Leakage and Metering***

The economic level of leakage calculations have been carried out in accordance with industry standard practice and we do not have any significant concerns with the general approach that has been adopted. We raised two challenges on key technical inputs (the 'policy minimum leakage' calculation and the derivation of the marginal economic cost of water), which the Company reviewed and analysed for sensitivity. If the current high marginal cost of water is maintained, then the sensitivity on policy minimum indicated that the 'mid-point' SELL is likely to be in the range 29.3 – 31.4 Ml/d. However, the marginal cost of water is at the upper end of the range that could have been adopted, and any lower assumption would cause a resultant increase in SELL. The 30Ml/d proposed by the Business Plan Outcomes therefore represents a pragmatic 'lower bound' target, which allows for the uncertainties that arise from the historic leakage reporting difficulties that the Company has identified and addressed.

The analysis of metering options clearly demonstrates that metering is not cost effective for the Company, and hence the customer base, as a whole. Whilst there are uncertainties with such an analysis, these are not sufficient to change this conclusion, which is usually for water companies that do not need to build new water resource schemes to maintain a supply/demand balance. This includes allowances for environmental and social costs. This means that any deliberate acceleration of the metering programme beyond the basic meter optant approach will result in higher average bills to customers and would cost more than the economic benefits that could reasonably be assigned to metering.

Costs for metering are currently running around 30% higher than those allowed for in the Final Determination. This appears to have been caused by very optimistic assumptions that were used for the PR09 Business Plan. The current metering contract is part of the mains renewals contract, so current unit rates are only at a high level and cannot realistically be used for business planning purposes. The Company has therefore estimated unit rates using 'bottom up' cost estimating calculations, which appear reasonable and well benchmarked, although there are two minor areas where they could be reduced (with an impact of up to £10/meter on the overall cost). However, because rates have not been based on existing contract costs it is difficult to determine whether this is a reasonable conclusion to draw at this stage

## ***Operational Cost Forecasts***

Our assurance of operational costs to date has been based on the August submission to Ofwat, which forecast costs to the end of AMP5. Based on this information we conclude that forecasts are reasonable, although we have not audited adjustments associated with pensions or business rates in any detail. We have previously noted that the only forecast changes beyond 2015 relate to assumptions over energy costs, which are based on Ofwat figures, and costs of competition, which are a Company interpretation of the figures that have been produced by the 'High Level Group' that Ofwat has brought together to facilitate competition in the water sector. We have not yet reviewed Portsmouth's interpretation of these costs.

## ***Quantitative Customer Research***

The main assurance process for the quantitative customer research will be provided through the peer review that is being proposed by the Company. However, as requested by the CCG, Atkins has carried out a preliminary review based on its statistical knowledge of surveys and stated preference approaches. Overall we concluded that the number of customers that were interviewed through the customer consultation process was statistically significant, and MVA had used reasonable demographic factors to obtain a sample population that is reflective of the customer base as a whole. The stated preference approach that was adopted used standard methods and seemed appropriate. Our only point of concern relates to the relative cost of some of the service improvements that were offered in the stated preference surveys, as some options would clearly cost significantly more than others. This has implications when the results are being used to rank preferences according to 'willingness to pay', as the cost and hence relative benefit of an item could affect WTP. This issue has been highlighted within the CCG report, but generally we consider that it does not invalidate the interpretation of customer preferences that the Company has adopted as a result of the surveys.

**Portsmouth Water  
PR14 Customer  
Engagement  
Peer Review of Research  
Draft Report  
October 2013**

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## Executive Summary

Portsmouth Water has recently conducted a series of research activities to provide a body of evidence to support its PR14 review submission to Ofwat.

Accent has been commissioned by Portsmouth Water to conduct a peer review of the following elements of research:

- Peer review of all PR14 research including:
  - Qualitative research
  - Quantitative research (WTP)
  - Deliberative research
  - Combined acceptability testing/outcomes research.

The peer review consists of a review the findings of each element of research and critiques, as appropriate, the design, methodology, analysis and reporting of the research.

Each strand of research is assessed in detail and rated against a number of criteria using a five point scale. In addition to the qualitative review of each element, this quantitative rating provides a framework, against which, a systematic review can be structured. Below is a table which outlines the rating for each element of research.

**Table 1 Ratings for each element of research**

	Willingness to Pay- Qualitative Research	Willingness to Pay- Quantitative Research	Deliberative Research	Combined Acceptability / Outcomes Research
The aims and objectives of the study should be clear, logical and well considered	4	4	4	4
There should be a clear understanding of the background and context of the research with related studies	4	3	4	3
The methodology should be thoroughly considered and executed well	3	3	3	2
Techniques, data and information should be the best in field	4	4	4	4
The interpretation of the data and resultant findings should be clear, explicit and justified	3	4	3	4
The resulting research document should be accurate and well written and structured	3	3	3	4
The research should meet its objectives and be relevant to stakeholders	3	4	3	3
The research overall should be objective and independent	4	4	4	4

The research programme has been well considered and appropriately designed for the size of operation of Portsmouth Water. This is in keeping with the guidance set out by UKWIR<sup>1</sup>.

There are some concerns over the 'Outcomes' research (part of phase 4) as we consider the way that the results from these questions are applied is invalid. In our view, the results here are not suitable for the use to which they are being put, and should not be used in this way unless accompanied by a strong caveat.

However, overall, the research elements have been generally well considered, designed and implemented. There are a number of areas where the research could possibly be challenged. This includes, for example, the sample sizes concerning businesses, analysis of and reporting on sub-groups such as 'vulnerable' and business customers, and some deviations from regulatory guidelines and/or best practice but, in the main, these comprise shortcomings in the reporting which can easily be resolved.

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<sup>1</sup> UKWIR (2011) Carrying Out Willingness to Pay Surveys, UKWIR Report Ref No. 11/RG/07/22

# Appendix B: Correspondence from the Environment Agency

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creating a better place



Neville Smith  
Portsmouth Water  
PO Box 8  
West Street  
Havant  
Hampshire  
PO9 1LG

Date: 1 November 2013

Dear Neville

**Portsmouth Water Business Plan Evaluation Response**

I would like to thank Portsmouth Water for providing the Environment Agency with material from your draft business plan.

In the attached report, we have used this information to assess the extent to which your business plan will meet your statutory requirements, and the environmental obligations set out in Defra's Statement of Obligations.

When making our assessment, we have reviewed how quickly you are planning to deliver your obligations, together with your overall level of performance. For your river basin management plan obligations in particular, Ministers are looking for assurance of early delivery wherever possible.

My team would be happy to discuss the report with you. We would be pleased to include any clarifications before we contribute to the Customer Challenge Group report and prior to our submission to Defra in mid November.

We look forward to continuing to work with Portsmouth Water to help ensure that your investment protects and improves the water environment, for the benefit of your customers and the economy.

Yours sincerely

A handwritten signature in black ink that reads "Davidson".

**Howard Davidson**  
**Director South East Region**

Cc: Dr Paul Leinster CBE, Chief Executive, Environment Agency  
Ian Barker Head of Land and Water, Environment Agency  
David Guest, Portsmouth Water CCG Chair  
Sonia Brown, Ofwat  
Tim Collins, Natural England  
Milo Purcell, Drinking Water Inspectorate

Kings Meadow House, Kings Meadow Road, Reading, RG1 8DQ.  
Customer services line: 08708 506 506  
Email: [enquiries@environment-agency.gov.uk](mailto:enquiries@environment-agency.gov.uk)  
Website: [www.environment-agency.gov.uk](http://www.environment-agency.gov.uk)





## Response to Portsmouth Water

### Introduction

The final price review methodology confirms that Ofwat expect the Environment Agency to highlight in the Customer Challenge Group (CCG) report whether your business plan will meet your statutory obligations (section 4.2.1 Setting Price Controls for 2015-2020, Ofwat, July 2013). As part of our engagement with your CCG, we have been working with you to be assured that your business plan is in accordance with these requirements.

The following report summarises our views of the draft plan, CCG papers and additional evidence provided. These views are based on a high-level review of the processes as described in the letter explaining our expectations sent to you in August 2013.

### Overview

We have had good ongoing dialogue with you during development of the business plan.

We note that the willingness to pay (WTP) surveys carried out by the company appear to show that customers are satisfied with the current level of service and are willing to pay for only small improvements, but you are planning modest improvements funded largely from efficiency gains.

You have worked well with us to remove uncertainty from the National Environment Programme (NEP), are positive about catchment management and have a biodiversity strategy for your own sites where you plan to implement 90% of the actions by 2020.

On the issue of inter-water company transfers it is essential that your final Water Resources Management Plan is consistent with Southern Water's plan.

### We welcome:

- Your environmental outcomes and associated delivery measures.
- The way you have worked with us to remove uncertainty from the NEP.
- Your commitment to meeting your environmental obligations.
- Your commitment to catchment management and the implementation of 90% of your biodiversity strategy during AMP6.

### We are pleased to note that:

- Despite low willingness to pay values you propose to deliver some modest level of service improvements, paid for by efficiencies (protecting wildlife, reducing your carbon footprint and water efficiency).

- Adopting a target for per capita consumption (pcc)
- You are maintaining your commitment of 100% compliance with discharge consents and abstraction licences.

**We need to see:**

- More ambition on leakage reduction. Your customers have given you a clear message (backed up by WTP) that they expect you to do more on leakage reduction than achieving the economic level.
- Putting more emphasis on the role you are going to play to influence the downward projection of pcc.
- Taking more opportunities to meter your customers, e.g. at change of occupancy, users of high water using devices etc. – will help you achieve your pcc reduction target.

**We have made more specific comment on the following areas:**

These are our observations on the replies you have made to the questions posed in response to the expectations letter.

**1. Delivery of statutory and environmental requirements**

We welcome the commitment you have made to meet your environmental obligations. We believe that you have presented sufficient information in your response and in your 27 September letter to Howard Davidson, to demonstrate how your business plan will allow Portsmouth Water to meet the statutory environmental requirements set out in Defra’s Statement of Obligations.

**2. Measures identified within the National Environment Programme (NEP)**

We are encouraged by your agreement to include all of the measures set out in the NEP within your final business plan. We believe that the programme will allow you to deliver what is best for both the environment and your customers.

**2.1 Transition investment programme**

You told us you were considering the possibility of catchment management and NEP water resources schemes being brought forward. We encourage you to do so.

**3. Provision for the outcome of second cycle river basin management plans and their ambition for Water Framework Directive (WFD) obligations.**

Early delivery of Water Framework Directive measures is essential if England is to make progress towards the necessary environmental improvements by 2027. We are pleased that your water company has made provision within its business plans for achieving outcomes from the second cycle river basin management plan. It is important that you translate this into a balanced programme of delivery to ensure your Water Framework Directive (WFD) obligations can all be achieved by 2027. We recognise that you have worked with us closely to minimise uncertainty, such that you have no uncertain water resources schemes in your plan. For those schemes that have a WFD measure there is a possibility that due to cost-benefit and affordability considerations it might not appear in the final river basin management plan, or it could appear in the plan with an alternative objective.

#### **4. Evidence of options and proposals for reducing the impact of a company's abstractions from the most seriously affected sites**

We are pleased to see that your company is putting forward options and proposals within your business plan to reduce the impact of its abstraction from the most seriously affected sites. We note that you have:

- included the confirmed and/or likely sustainability changes set out in NEP phase three in the water resources supply-demand component of its business plan.
- considered whether planned increases in abstraction may cause deterioration in WFD water body status (but we would like to see a more comprehensive assessment as requested in our representation).
- considered which abstractions would fall within Ofwat's Abstraction Incentive Mechanism.

#### **5. Alignment of the Water Resource Management Plan options and business plans**

We expect Water Resource Management Plan (WRMP) options to form the supply-demand component of the business plan, and ask that any material differences between the two plans should be justified. We note that you have made some changes to your water resources demand forecasts and that you don't anticipate that there will be any differences between your final business plan and your final WRMP. We would also expect consistency between your final WRMP and that of Southern Water (the plans were inconsistent on the matter of inter-company transfers in the draft WRMPs).

#### **6. Reservoir safety**

We note your intentions to maintain reservoir safety although you have provided limited information on the programme of work. This is an important duty given the potential high impact your reservoirs pose to public safety. Your continued maintenance and capital investment is essential for public safety.

You have not referenced the recent changes in reservoir legislation. Please confirm how you will implement these changes during the next AMP.

Defra set out its expectation in the Statement of Obligations that companies will prepare reservoir plans. We would expect you to continue to develop and maintain on-site plans. You do not refer to incident planning and working with partners to reduce impacts to downstream communities, should an incident occur. We encourage you to co-operate with relevant authorities and partners on the development and maintenance of site plans and on incident planning.

#### **7. Mitigation measures adopted to manage future risks**

You have provided some evidence that you plan to take appropriate measures to manage risks from natural hazards and climate change. However, we expected to see more details about your approach, and how you have used relevant guidance from Ofwat and others. At our business plan meeting with you, you confirmed that you no longer had any critical infrastructure in flood risk zones and that you had no properties dependent on a single source of supply. We understand that your plan will propose further investigations which may identify investment requirements for AMP7. This seems appropriate given the situation you outlined.

## **8. Environmental outcomes**

We welcome the outcomes, performance measures and targets included in your business plan which accurately reflect the important role that your company plays in protecting the environment.

### **8.1 Delivery and incentives.**

We are encouraged by your approach to setting delivery levels and designing incentives around your environmental outcomes and obligations, to ensure these are achieved. There appears to be a good mix of reputational, reward and penalty incentives but at this stage we cannot comment on the degree of ambition because we haven't seen the targets associated with the rewards and penalties. Demonstrating the tightest links between quantitative evidence of customer preferences and your ambition and incentives is essential. We expect all companies to explore using financial and reputational incentives in tandem, to go further and faster than statutory environmental obligations wherever justified by consumer research.

## **9. Change mechanism**

At previous price reviews, Ofwat has used the change protocol for managing in-period changes to the risks and costs. This time you are being asked to put forward proposals for dealing with such changes. It is imperative that new statutory requirements, for example schemes arising from the 2<sup>nd</sup> River Basin Management Plan can be delivered whilst maintaining levels of ambition around customer priorities. We would like to see a clear process for dealing with predictable but, nonetheless uncertain new commitment you could face during AMP6.

To be assured that important "discretionary" outcomes are not prejudiced by additional legislative requirements, we believe you do require an explicit change mechanism for dealing with such changes. We acknowledge your assurance that you are developing one.

## **10. Eel Regulations**

The Eel Regulations apply to one of your sites and you have told us that you are planning an investigation in AMP6, and if full screening is required you will implement this early in AMP7 and before 2021, the end date for compliance. We are happy with such an approach but at the same time remind you that after 1 January 2015, it will become an offence not to screen intakes or outfalls for eels, unless we have specifically issued an exemption notice.

## **11. Natural England**

In so far as the comments herein relate to the natural environment, they also reflect the advice of Natural England.

## **Concluding remarks and recommendations**

Overall we are satisfied that your plan will meet statutory requirements and environmental obligations. We have the following recommendations for improvement. We would like you to consider:

- Further development of your approach to Managing Uncertainty including the proposal of a change mechanism
- Taking more account of your customers' expectations in setting your leakage target

We look forward to working closely with you over the next few weeks to finalise your business plan. Our aim is to help you produce a plan that delivers its statutory obligations and facilitates the continuing achievement of better environmental performance.

**David Howarth**  
**1 November 2013**



creating a better place



Neville Smith  
Managing Director  
Portsmouth Water Ltd  
PO Box 8  
Havant  
Hampshire  
PO9 1LG

**Date:** 21 November 2013

Dear Neville

**Portsmouth Water Business Plan Evaluation Response**

Thank you for your letter dated 7<sup>th</sup> November 2013 providing further information on your Business Plan.

From the information you have provided, we understand that you are planning to meet your statutory environmental requirements set out in Defra's Statement of Obligations. We welcome the commitment you have made to meeting them.

I have attached an annex which includes our comments on your responses, which you can include as an addendum to our original report.

I hope that you find this additional response useful. If you have any further queries please do not hesitate to contact us again.

Yours sincerely

A handwritten signature in black ink that reads "Davidson".

**Howard Davidson**  
**Director, South East**

Cc: Dr Paul Leinster CBE, Chief Executive, Environment Agency  
Ian Barker, Head of Land and Water, Environment Agency  
David Guest, Portsmouth Water CCG Chair  
Sonia Brown, Ofwat  
Tim Collins, Natural England  
Milo Purcell, Drinking Water Inspectorate

## Response to Portsmouth Water

### 21 November 2013- Update following further communication with the company

Following receipt of our evaluation report on 1 November 2013, we have been involved in further discussions with you regarding our recommendations in the report. This note provides an update to our response based on those discussions.

The following table summarises the company's response to Environment Agency recommendations:

<b>Environment Agency statement/recommendation</b>	<b>Company response (letter 7<sup>th</sup> November 2013)</b>	<b>Environment Agency comment 21<sup>st</sup> November 2013</b>
<p>At previous price reviews, Ofwat has used the change protocol for managing in-period changes to the risks and costs. This time you are being asked to put forward proposals for dealing with such changes. It is imperative that new statutory requirements, for example schemes arising from the 2nd River Basin Management Plan can be delivered whilst maintaining levels of ambition around customer priorities. We would like to see a clear process for dealing with predictable but, nonetheless uncertain new commitment you could face during AMP6. To be assured that important "discretionary" outcomes are not prejudiced by additional legislative requirements, we believe you do require an explicit change mechanism for dealing with such changes. We acknowledge your assurance that you are developing one.</p>	<p>We will ensure that our Plan includes a change protocol mechanism.</p>	<p>Thank you for providing assurance.</p>



<p>We would like you to take more account of your customers' expectations in setting your leakage target.</p>	<p>We have undertaken four different stages of customer research to inform our Business Plan. The quantitative research revealed that customers would be willing to pay more to see a reduction in leakage though overall they would not like to see an increase in their bill. We undertook a further stage of deliberative research to enable us to understand how customers' perceptions on leakage changed when they become for informed. The results were mixed with some customers' attitudes changing but other customers remained of the same view.</p> <p>We believe that our plan does reflect our customers' views by firstly continuing to set a leakage target that is below our sustainable economic level of leakage. Secondly, we are including an outcome delivery incentive that encourages the Company to reduce leakage further below the target level.</p>	<p>Thank you for providing clarification of your customers' expectations. We note your inclusion of an outcome delivery incentive for leakage.</p>
<p>We would also expect consistency between your final WRMP and that of Southern Water (the plans were inconsistent on the matter of inter-company transfers in the draft WRMPs).</p>	<p>We will work with Southern Water to ensure that this is achieved.</p>	<p>Noted</p>
<p>We need to see more emphasis put on the role you are going to play to influence the downward projection of pcc.</p>	<p>We recognise that we have a duty to work with our customers to reduce PCC. We have outlined in our Draft Final Water Resources Management Plan our intention of working with local stakeholders to further promote optional metering and water efficiency. We have also included an outcome delivering incentive that is financial which we believe reflects our commitment to lower PCC.</p>	<p>We welcome your proposals. We note the inclusion of an outcome delivery incentive for pcc.</p>
<p>We need to see you taking more opportunities to meter your customers, e.g. at change of occupancy, users of high water using devices etc. – this will help you achieve your pcc reduction target</p>	<p>We undertook a cost benefit analysis of potential metering programmes to inform our Water Resources Management Plan. This considered various metering programmes including compulsory metering, change of occupier and optional metering.</p>	<p>Thank you for providing additional details of your metering programme.</p>

	<p>The analysis showed that our current form of optional metering is the most cost effective. However, we believe that we can do more to promote optional metering and our Business Plan will note this commitment. Our recent customer engagement indicated that our customers were in favour of us promoting more water meters but the message was that this should only be for customers who would save money. Our plan commits us to targeting these customers more effectively. We will continue to review change of occupier metering as part of our overall strategy but it is likely we will only employ this tactic if we are falling short of the target level of meter optants outlined in our Water Resources Management Plan.</p>	
<p>You told us you were considering the possibility of catchment management and NEP water resources schemes being brought forward. We encourage you to do so.</p>	<p>We can confirm that we will be making provision in our Business Plan for early start schemes for catchment management water resources NEP schemes and the Farlington washwater recovery scheme to reduce discharge to the harbour.</p>	<p>Thank you for the additional details.</p>
<p>You have not referenced the recent changes in reservoir legislation. Please confirm how you will implement these changes during the next AMP.</p>	<p>The principal impact of the new reservoir legislation is to change the risk categorisation of reservoirs. The changes will have the affect of reducing the number of sites requiring an elevated level of assessment. However, irrespective of the less onerous requirement the Company will continue to inspect reservoirs to existing standards. Our capital maintenance expenditure reflects this position.</p>	<p>Thank you for providing assurance.</p>
<p>There appears to be a good mix of reputational, reward and penalty [Outcome Delivery] incentives but at this stage we cannot comment on the degree of ambition because we haven't seen the targets associated with the rewards and penalties.</p>	<p>These will be presented at the CCG meeting on the 12th November.</p>	<p>We had the opportunity to comment on your proposals at the CCG on 12<sup>th</sup> November.</p>

# Appendix C: Correspondence from the Drinking Water Inspectorate

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## Drinking Water Inspectorate Statement for Portsmouth Water's Customer Challenge Group Report to Ofwat

### 1. Introduction

- 1.1 The Drinking Water Inspectorate (DWI) is the independent regulator of drinking water quality in England and Wales. We protect public health and maintain confidence in public water supplies by ensuring water companies supply safe clean drinking water that is wholesome, and that they meet all related statutory requirements. Where standards or other requirements are not met, we have statutory powers to require water supply arrangements to be improved.
- 1.2 We publish information about drinking water quality and provide technical advice to the Secretary of State for the Environment, Food & Rural Affairs, and to Welsh Ministers.
- 1.3 For PR14, water companies are expected to ensure that their business plans make provision to meet all their statutory obligations, including the need for public water supplies to be safe, clean and wholesome, and that provision is made for a sustainable level of asset maintenance to maintain public confidence in drinking water quality. Ministers summarised these requirements in Defra's Statement of Obligations<sup>1</sup>, and in their further guidance on PR14 matters to Ofwat. In addition, the Inspectorate set out in **DWI Information Letter 01/2013 – The 2014 Periodic review of Prices – Guidance for water companies**, published on 1<sup>st</sup> February 2013 supplementary guidance to companies on the regulatory framework for drinking water quality, statutory requirements, the Inspectorate's role in the Price Review process and our requirements for companies seeking technical support. The Inspectorate also published separate PR14 guidance on a range of specific issues. All of the Inspectorate's published PR14 guidance is available on the DWI website.
- 1.4 It is worth noting the particular emphasis that Ministers placed in their Guidance on the resilience of supply systems, and that the Inspectorate placed on existing duties to manage the introduction of new sources and to plan supply arrangements to protect consumers and ensure no deterioration in the quality of their supplies.

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<sup>1</sup> <http://www.defra.gov.uk/publications/files/pb13829-statement-obligations.pdf>

1.5 The Inspectorate has a position on all of the water companies' customer challenge groups in England and Wales. The Inspectorate's representative on Portsmouth Water's Customer Challenge Group has supported the process by acting as an independent member with the overall remit of ensuring that the Company business plan proposals reflect the views of consumers and place drinking water quality at the forefront of such plans.

## 2. Formal Drinking Water Proposals Requiring DWI Technical Support

2.1 As with previous periodic reviews, water companies seeking technical support from the Inspectorate must demonstrate the need for each proposal. The case for justification must be accompanied by evidence of the company's options appraisal process to identify the most robust, sustainable and cost-effective solution, with evidence that the preferred solution will adequately address the risk and deliver the required outcome within an appropriate timescale.

2.2 Portsmouth Water submitted seven formal proposals for drinking water quality to the Inspectorate, listed in the table below:

PR14 DWI Ref.	Scheme Name	Quality Parameter(s)	Scheme Type	Preferred Option	DWI Final Decision
PRT113	Lead Strategy	Lead	Company lead strategy	Package of measures	Regulation 28 Notice
PRT114	DOMS	Iron, Manganese, consumer acceptability	Distribution	Mains renewal/replacement/flushing etc	Commend for Support
PRT115	Resilience	Extreme weather, Power outages, sabotage	Various	Various	Commend for Support
PRT116	Disinfection improvements at 11 WTW	Regulation 26	Treatment	Various	Commend for support
PRT117	Eastergate WTW Westergate WTW	<i>Cryptosporidium</i>	Treatment	UV	Regulation 28 Notice
PRT118	Eastergate WTW Westergate WTW	Turbidity	Treatment	Cartridge filtration Automated run to waste	Declined to support
PRT119	Catchment Management	Nitrates	Catchment	Various monitoring and catchment activities	Regulation 28 Notice

2.3 The Company is to be commended on the quality of the submissions to the Inspectorate, which were received in part by our published deadline of 31<sup>st</sup> July 2013, and which complied with our PR14 guidance. The Inspectorate discussed requirements with the Company on a number of occasions, and, in addition, discussions had taken place at the CCG. Therefore, we were broadly aware of the Company's plans for drinking water quality and we are generally supportive of the Company's approach.

- 2.4 The Inspectorate has formally supported three of the Company's proposals and we will put legal instruments in place to make the proposals legally binding programmes of work. In addition, we comment for support three proposals. Our final decision letters were sent to the Company on 18<sup>th</sup> October 2013 and 22<sup>nd</sup> November 2013.
- 2.5 We support the Company's proposal to update its lead strategy to enable it to secure or facilitate compliance with the lead standard, and we will include the proposal in a regulation 28(4) Notice. The standard for lead will reduce from 25µg/l to 10µg/l in December 2013, and the package of measures included in the Company's proposal will improve compliance with the new standard and reduce consumers' exposure to lead from drinking water.
- 2.6 The Inspectorate was invited to review the proposals by Portsmouth Water to increase the resilience of its water supply system, to reduce the risks to consumers from quality and sufficiency problems associated with serious unplanned events such as extreme weather, power outages and acts of deliberate sabotage. The Inspectorate commends for support the proposals to improve the resilience of the Company's water supply systems to mitigate these residual risks to consumers, and we agree that the proposals should be included by the Company in its Final Business Plan. We confirm that the proposed scheme is consistent with the requirements of Defra's Statement of Obligations published in October 2012, and the Inspectorate's guidance on principles for the assessment of drinking water quality provisions within the PR14 process, as set out in DWI Information Letter 01/2013, published on 1<sup>st</sup> February 2013.
- 2.7 The Company also invited us to review its proposals for its Distribution Operation and Maintenance Strategy (DOMS). All companies should have DOMS in place as part of their drinking water safety plans, which identify zones in the network that are at high risk, based on customer contacts and water quality data, and we are happy to commend this AMP6 strategy for support. We confirm that the proposed scheme is consistent with the requirements of Defra's Statement of Obligations, and the Inspectorate's guidance on principles for the assessment of drinking water quality provisions within the PR14 process, as set out in DWI Information Letter 01/2013.
- 2.8 The Inspectorate also commends for support the proposals to deliver improvements to the disinfection arrangements at 11 water treatment works to mitigate residual risks to the wholesomeness of water supplied to consumers, and we agree that the proposals should be included by the Company in its Final Business Plan. We confirm that the proposed scheme is consistent with the requirements of Defra's Statement of Obligations, and the Inspectorate's guidance on principles for the assessment of drinking water quality provisions within the PR14 process, as set out in DWI Information Letter 01/2013.
- 2.9 The Company identified the need to mitigate the risk of *Cryptosporidium* as a potential danger to human health from the water supplied from Eastergate Water

Treatment Works and Westergate Water Treatment Works. The Inspectorate supports the need for these controls and intends to issue a Notice under Regulation 28(4) of the Water Supply (Water Quality) Regulations 2000, as amended, requiring the Company to complete this work. It is expected that the design of the improvements required will take account of all matters that may impact the effectiveness of the proposed solution, including turbidity.

- 2.10 The Company submitted a proposal to address increasing levels of nitrate in groundwater sources by means of various site-specific catchment management activities. We are happy to support these proposals as an appropriate means of contributing to delivering wholesome water in the longer term, and we will include the proposal in a regulation 28(4) Notice.
- 2.11 It should be noted that these improvement schemes will make only a small, if significant, contribution to enabling the Company to meet its legal obligations in respect of drinking water quality. These obligations are met overwhelmingly by the Company making sufficient provision for operational and maintenance requirements in its business plan, and by its use of those resources. These are matters for the Company to determine and deliver. For its part, the Inspectorate will continue to keep under review, and report on, the performance of the Company in meeting its legal obligations. Statutory powers are available to secure or facilitate compliance, if necessary.
- 2.12 The summary of improvement schemes above reflects the position at the time of writing this statement. Further discussions are needed with the Company to finalise details. We will advise the CSG and Ofwat of any material changes.
- 2.13 This statement will be copied to Rod Porteous of Portsmouth Water. Any queries arising should be directed to Jacqueline Atkinson, Inspector, Drinking water Inspectorate, telephone number: 03000686402; email [dwipricereview@defra.gsi.gov.uk](mailto:dwipricereview@defra.gsi.gov.uk).



**Milo Purcell**  
**Deputy Chief Inspector (Regulations)**

**Drinking Water Inspectorate**

Area 7e, 9 Millbank  
c/o Nobel House  
17 Smith Square  
London SW1P 3JR

**22<sup>nd</sup> November 2013**

# Appendix D: Minutes of CCG Meetings

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## CUSTOMER CHALLENGE GROUP CALENDAR OF MEETINGS

	<b>2012</b>
May	Friday 25
July	Tuesday 3
October	Tuesday 2
	<b>2013</b>
January	Thursday 10
March	Tuesday 26
June	Tuesday 25
August	Thursday 15
September	Tuesday 24
October	Tuesday 22
November	Tuesday 12

**CUSTOMER CHALLENGE GROUP  
SUB GROUP  
CALENDAR OF MEETINGS**

	<b>2012</b>
<b>Market / Customer Research</b>	Wednesday 27 June
<b>Market / Customer Research</b>	Wednesday 2 August
<b>Market / Customer Research</b>	Tuesday 18 December
	<b>2013</b>
<b>Market / Customer Research</b>	Thursday 7 February
<b>Market / Customer Research</b>	Thursday 21 March
<b>Outcomes</b>	Thursday 1 August
<b>Market / Customer Research</b>	Friday 8 November

# PORTSMOUTH WATER Ltd

## CUSTOMER FORUM

### MEETING HELD ON FRIDAY 25 MAY 2012

**PRESENT:** Amy Atkins (Secretary), Jim Barker (Environment Agency), Rachel Crabbe (Natural England), Cllr Paul Dendle (Arun District Council), Karen Gibbs (Consumer Council for Water), David Guest (Independent Chair), Mark Hann (Consultant), Simon Oakley (Chichester District Council), R Porteous (Portsmouth Water), Milo Purcel (Drinking Water Inspectorate), Nick Sheeran (Portsmouth Water), G Simmonds (Portsmouth Water), Neville Smith (Portsmouth Water), Jon Stuart (Havant & District Citizens Advice Bureau), Cllr Victoria Weston (Winchester City Council), Stuart Wedgbury (East Hampshire District Council & Havant Borough Council), David Fisher (East Hampshire District Council & Havant Borough Council)

**APOLOGIES:** Stuart Wedgbury (East Hampshire District Council & Havant Borough Council) In Part  
Cllr Stephen Philpott (Gosport Borough Council)  
Traci Baker (Hampshire Chamber of Commerce)

#### 1. Welcome and Introductions

David Guest informed the Members that Ofwat's Customer Engagement Policy requires the formation of Customer Challenge Groups as a Regulatory Forum. He advised that the Forum will be expected to scrutinise Portsmouth Water's 5-year Business Plan prior to its submission and to be satisfied that the Company has effectively engaged with its customers. They will be considering the following:

- Customer concerns
- Business planning and benchmarking
- Security of Supply – safeguarding continuity
- Quality and quantity of supply
- Cost certainty
- Value for money
- Asset risk management and mitigation planning
- Measure of success

The Forum will prepare and submit a Report on their findings and recommendations to Ofwat and include a review of the Company's evidence based assessment of key issues and outcomes.

David Guest confirmed that he envisaged the Forum meeting at least three times a year with the addition of periodic Sub-Group meetings.

#### Action

## 2. Setting the Scene

Neville Smith, Managing Director of Portsmouth Water, gave the Forum an Introduction to Portsmouth Water, providing them with a background to the Company and the Business Strategy.

## 3. Purpose of the Forum

Mark Hann, an Independent Consultant, gave an overview of Ofwats expectations of the Forum and outlined the process and timetable of the price review. Mark Hann advised the Forum to read Ofwats 'Future Price Limits – Statement of Principles'. It was agreed that the Secretary would email this document to the Members of the Forum.

AA

David Guest suggested Members of the Forum should attend regular Ofwat Workshops to have an 'Experience Exchange' learning what other Companies are doing in the Forum Process.

## 4. Governance of the Forum

Neville Smith advised the Forum that he hoped to have the Customer Research completed this year with the results prepared ready for discussion at the Forum in October. Taking into account the Market Research a Strategy document will need to be produced by the Company in early 2013. The Company will also need to produce its Water Resources Management Plan which will inform the Strategy.

Neville Smith suggested setting up working panels of volunteers within the Forum to discuss issues as they arise and report back to the Forum. The members agreed to this in principal.

David Guest recommended that the Forum needed better Representation from Portsmouth Water's 'large user' customers e.g. Hospitals and the Naval Base. Neville Smith suggested we contact Kelda to represent the Naval Base. Other recommendations from the Forum included representations for;

- Horticulture and Agriculture e.g. West Sussex Growers Association
- Vulnerable Customers – Age Concern
- Portsmouth City Council
- Single Issue Groups
- Individual representatives from Industry
- Federation of Small Businesses
- Southern Water
- South Downs National Park

David Guest requested a list of all those initially invited to join the Forum and he will write again enforcing the need for them to be represented. It was agreed that the Secretary would provide this list.

AA/DG

David Guest informed the Members that he will ask a Havant Borough Council Environmental Portfolio Holder to attend.

DG

Neville Smith commented that as part of the evidence we need to demonstrate that Portsmouth Water tried to obtain the best representation.

Cllr Victoria Weston, of Winchester City Council, recommended that there be a two tier Forum. The first tier being those that need to be represented at the Forums meetings, and the second tier of those we need to engage with and should be included in all correspondence for them to be able to respond / contribute should they wish.

David Guest commented on the Ofwat Workshop he attended with the other Customer Forum Chairs. He was impressed with how well informed Anna Bradley, the Chair of the Southern Water's Customer Forum was and how it would be beneficial for all the Chair's to meet. It was agreed that the Secretary and Chair would try and arrange this. David Guest provided the Secretary with a list of the Chairs that attended the Ofwat Workshop as a starting point.

AA/DG

#### 4. Governance of the Forum Cont'd

Nick Sheeran, Finance and Regulation Director of Portsmouth Water, suggested submitting an Interim Report to Ofwat to ensure we have understood their guidance ahead of the final submission. Mark Hann commented that Ofwat did not want to specifically be involved in the Customer Challenge Groups. Neville Smith recommended that Ofwat be invited to all future Customer Forum meetings, in particular the one which will discuss Strategy to allow them to monitor the Forums progress and to avoid surprises. It was agreed that Ofwat should be invited in the hope they may attend one or two. The Secretary is to ensure they are included.

AA

Milo Purcel, the Deputy Chief Inspector of the Drinking Water Inspectorate, advised that an Independent Engineering Auditor may be beneficial to invite when technical issues arise and the Forum needs an independent view. Neville Smith recommended an Engineering auditor that had previously been used by the Company.

NS

Milo Purcel raised concern that ultimately the Competition Commission may require a copy of the Forums final Report to Ofwat and therefore the report will need to be well evidenced. If that was the case by having an Independent Auditor the Forum could demonstrate that it had taken the best advice and the Auditor would also be able to give evidence if required at any subsequent hearing.

*Stuart Wedgbury, Environmental Health Joint Service Manager of East Hampshire District Council & Havant Borough Council left The Meeting*

#### 5. Outcomes

Gareth Simmonds, Regulation Manager of Portsmouth Water, presented on the Company's suggested outcomes for their Business Plan which the Forum will ultimately have to agree.

GS

The presentation covered the influences on the outcomes, the strategy to achieve the outcomes and the outputs that need to be achieved in order to deliver the outcomes.

The Forum is required to agree the outcomes and then decide how they are to be monitored and delivered. Gareth Simmonds advised that the Forum will need to appoint Team Leaders to form Sub Groups owning each of the outcomes.

The draft outcomes were discussed by the Forum with the following initial suggestions:

Dr Rachel Crabbe, Senior Adviser at Natural England, commented that the Environmental outcome is worded more like a strategy and suggested words like; high quality environment that supports biodiversity, public amenities and recreation;

Cllr Victoria Weston advised that the outcome 'Safe secure and reliable supply of drinking water' should include the wording 'Over the longer term' to reassure customers during population growth;

Milo Purcel noted that there should be an outcome demonstrating the Company's role within the Community, support of future growth, development and intergeneration;

Karen Gibbs of the Consumer Council for Water, requested the outcome 'delighted customers' be expanded upon e.g. 'Customers delighted with the service, quality and value for money';

David Fisher, of East Hampshire District Council & Havant Borough Council, envisaged energy costs being a big factor for Portsmouth Water and a key output should be to drive energy costs down to achieve the businesses outcomes. Neville Smith agreed and commented that the Company has a Carbon Reduction Strategy.

## 5. Outcomes Cont'd

Gareth Simmonds asked if there were any influences to the outcomes that had been missed and the following suggestions were made:

Simon Oakley of Chichester District Council commented on the supply demands of surrounding water companies and it was agreed that Water Resources in the South East (WRSE) should be included as an influence;

Milo Purcel suggested Climate Change and reduced rainfall could impact largely on the Company's outcomes. David Guest noted that this would be included in a Risk Register to be agreed by the Forum;

David Guest suggested the Company provide more detail on their outcomes, taking into account the comments raised and circulate ahead of the next meeting.

GS/AA

## 6. Customer Research

Nick Sheeran presented to the Forum on the objectives of the Customer Research and how it will be conducted. He informed the Forum that MVA Consultancy was the Company's preferred supplier to conduct the Customer Research. However, MVA would not be appointed until the Forum was satisfied with their approach. The Research would be completed using both online surveys and face to face methods.

Milo Purcel asked if the Company's previous Customer Research could be used as part of the process. Nick Sheeran considered the information may be out of date as there have been a number of factors that could influence the customers answers; e.g. recession and drought.

Milo Purcel commented that he was disappointed with the lack of innovation on the part of the consultants. He was expecting them to suggest research methods using Twitter, social media, utilising the visitors we have to our site and school children. The Customer Research needs to be more in depth than in previous price reviews, better evidence is needed that the Company has engaged customers. Neville Smith noted this and confirmed the Company would consider his suggestions although has slight reservations about the Company using social media due to the way the Company has to deal with customer contacts / complaints.

Karen Gibbs was concerned that an online survey would rule out a large number of customers. Nick Sheeran noted concern and confirmed that supplementary surveys would be carried out to cover this concern.

Victoria Weston raised the issue that sampling only 500 customers would not be sufficient. Gareth Simmonds reassured the Forum that in previous price reviews Ofwat only required a sample of 250 and that 500 would be statistically significant.

Nick Sheeran asked for volunteers to form the Sub Group to deal with the Customer Research. It was agreed that an email would be sent to all Members of the Forum with a list of each of the Sub Groups for Members to volunteer for the Group where their expertises will be best utilised.

NJS/AA

Karen Gibbs volunteered for the Customer Research Sub Group commenting that the Forum needs to ask the right questions to get quality results. Paul Dendle also volunteered to be part of this sub group.

## 7. Any Other Business

David Fisher advised that the Customer Research should include geographic information which could prove useful.

Jim Barker, Water Planning Manager at the Environment Agency, commented that the Water Resources Management Plan includes a lot of Risk issues that should be discussed at the Forum and put on their Risk Register.

Milo Purcel raised the issue of confidentiality when discussing Company sensitive

information. It was agreed that Neville Smith would decide how he would want the Company's information managed, include it on the Terms of Reference and circulate ahead of the next meeting to be adopted.

**Action**

NS/AA

**8. Date of Next Meeting**

3 July 2012 9.30 am To Be Held at Portsmouth Water's Head Office, Havant

**9. Date of Future Meeting**

25 October 2012

NS

# PORTSMOUTH WATER Ltd

## CUSTOMER FORUM

### MEETING HELD ON TUESDAY 3 JULY 2012

**PRESENT:** Amy Atkins (Secretary), Louise Bardsley (Natural England), Jim Barker (Environment Agency), Hugh Caley (Carillion Plc), Cllr Paul Dendle (Arun District Council), Karen Gibbs (Consumer Council for Water) In Part, David Guest (Independent Chair), Richard Harris (NHS), John Havenhand (Consumer Council for Water), Simon Oakley (Chichester District Council), R Porteous (Portsmouth Water), Milo Purcell (Drinking Water Inspectorate), Ian Rawson (KWS Defence), Nick Sheeran (Portsmouth Water), G Simmonds (Portsmouth Water), Neville Smith (Portsmouth Water), Jon Stuart (Havant & District Citizens Advice Bureau) In Part, Cllr Victoria Weston (Winchester City Council)

#### Action

#### 1. Apologies

Apologies were received from David Bland (Consumer Council for Water), David Collins (Havant Borough Council), Rachel Crabbe (Natural England), Andrew Day (Ofwat), Mark Hann (Consultant), Cllr Stephen Philpott (Gosport Borough Council), Stuart Wedgbury (East Hampshire District Council & Havant Borough Council)

#### 2. Minutes & Actions of Meeting Held on 25 May 2012

The minutes were approved.

Gareth Simmonds advised that new members had been invited and subsequently joined the Group following an action from last times meeting as follows;

- Hugh Caley (Carillion)
- Richard Harris (West Sussex Hospitals)
- Ian Rawson (KW Defence)

These Members represent the Company's Large Commercial Customers, Hospitals and the Naval Base.

Jon Stuart confirmed that as well as representing the CAB he could also represent Charities and Vulnerable Customers.

Louise Bardsley requested the National Farmworkers Union be invited to the Forum and Neville Smith confirmed we could find a contact from our work on Catchment Management.

GS

Gareth Simmonds confirmed that other Groups had been contacted and we are waiting for a response.

#### 3. Outcomes

Gareth Simmonds outlined the updated proposed Outcomes to reflect the suggestions made by Members of the Customer Forum at their meeting held on 25 May 2012.

The revised outcomes are set out below;

- A safe secure and reliable supply of drinking water over the long term.
- Customers that are delighted with service, water quality and value for money they receive from Portsmouth Water.
- To provide value for money by continuing to strive for efficiencies, a goal being to deliver a stable bill profile.



- To promote a high quality environment that supports biodiversity, public amenities and recreation.
- Portsmouth water will support the community they serve by taking opportunities to support growth and development.
- Portsmouth Water will continue to be attractive to investors and provide a long term financially sustainable business.
- To promote a culture of health and safety through all our activities.

Gareth Simmonds confirmed that these would not be the final outcomes as they would be influenced by the Customer Research.

The Forum discussed the Outcomes and proposed that the first outcome should include a sustainable supply of water.

#### 4. Customer Research

Nick Sheeran updated the Members on the progress of the Customer Research.

Portsmouth Water had requested volunteers from the Forum to join a Market Research Sub-Group and Nick Sheeran confirmed the Members as follows;

- Amy Atkins (Secretary)
- Rachel Crabbe (Natural England)
- Cllr Paul Dendle (Arun District Council)
- Karen Gibbs (Consumer Council for Water)
- John Havenhand (Consumer Council for Water)
- Nick Sheeran (Portsmouth Water)
- Victoria Weston (Winchester City Council)

The Market Research Sub-Group held their first meeting on 27 June 2012 and discussed the following;

- Objectives of the Research
- Discussion on MVA's Proposal
- Consideration of Previous Research
- Innovation in the Research

Portsmouth Water held a meeting with MVA on 29 June 2012 regarding their proposal and discussed the points raised at the meeting of the Sub-Group.

MVA are preparing a revised proposal by 6 July 2012 for the Company to consider. Once this has been received another meeting of the Sub-Group will be arranged.

Jon Stuart of the Citizens Advice Bureau also expressed that he would like to join the Sub-Group to represent Vulnerable Customers.

Nick Sheeran agreed to the two new Members and confirmed that the invitation remains open to anyone who would still like to join.

Milo Purcell advised that stated preference techniques are extremely valuable and should be included. The Forum also needs assurance that;

- there is sufficient expertise in the Sub-Group to carry out the Qualitative Research;
- that there will be language testing in the Quantitative Research;
- and that the Willingness to Pay work being carried out is technically sound, this may require the expertise of an Independent Reviewer

David Guest asked when would be the appropriate time to involve an Independent Reviewer.

Milo Purcell felt that the Forum needed to flesh out the details of the willingness to

pay before involving an Independent Reviewer.

John Havenhand agreed it would be beneficial to have guidance on reliability of technical issues, presumed questions and interviewer bias by an Independent Reviewer.

John Havenhand also commented that willingness and preference are two different things and can produce different results.

Ian Rawson suggested the qualitative research tease out customer issues and which are then dealt with in the quantitative research.

Paul Dendle raised concern over the introduction of Social Tariffs within the Willingness to Pay work and whether the majority of customers will want to subsidise the undeserving poor.

Milo Purcell recommended MVA be asked to analyse and present a comparison of customers priorities in qualitative work to be included in the quantitative work.

Nick Sheeran confirmed that this research is critical to the Business Plan and the points raised will be discussed at the next Sub-Group meeting and put to MVA.

## 5. Updated Terms of Reference

Neville Smith circulated an updated Terms of Reference prior to the meeting to include wording on confidentiality. Neville Smith asked the Forum that by agreeing to the minutes they will also be agreeing to the confidentiality and Terms of Reference.

Neville Smith also advised that since the circulation of the revised Terms of Reference Ofwat had confirmed that they would like to be removed from the Membership within the Terms of Reference and that a final revision will be sent with the minutes.

NS/AA

## 6. Water Resources Management Plan

Gareth Simmonds gave an overview of the Water Resources Management Plan outlining key issues of the statutory process and the progress made to date in preparing the next Plan. A copy of the presentation is attached to these minutes.

Simon Oakley questioned how Portsmouth Water were forecasting the population and housing growth and Gareth Simmonds advised that a joint project between all the water companies in the South East is being conducted to develop a consistent property population forecast. This is being undertaken by Experian and will be inline with the best practice guidance published by the Environment Agency.

Gareth Simmonds confirmed that through the Water Resources in the South East Project Portsmouth Water are exploring options to share supplies with neighboring companies.

There was a discussion on the current environmental studies being undertaken to determine the impact of Portsmouth Waters abstraction on the environment.

Gareth Simmonds noted that there was a Stakeholder Group for Water Resources Management Planning and it was agreed that this Group would continue running parallel to the Customer Forum with outcomes of the Group being brought and discussed at the Customer Forum.

As Water Resources Management Planning will be a key issue for Portsmouth Water this will be a standing agenda item.

## 7. Capital Maintenance Planning

Rod Porteous presented an overview of how Portsmouth Water manage their

assets and decide when replacement is appropriate.

Rod Porteous noted that the Company is proposing to engage a Consulting Engineer to provide an independent view on the detailed technical aspects of Capital Maintenance Planning. It is hoped that this report can give confidence to the Forum on the appropriateness of Portsmouth Waters approach.

The Company highlighted the challenges it faced in justifying an appropriate level of expenditure to maintain assets in a stable condition. The challenges included the cyclical nature of capital maintenance expenditure and limited historical asset performance data.

Milo Purcell noted that with water supply assets, failure must be prevented and it was the responsibility of the Board to decide how risk averse it needs to be to achieve this.

Milo Purcell again noted Ofwat place a lot emphasis on providing evidence to support Business Plans. The Forum will need to come to a view if the Company's approach to risk is appropriate. It is important that the Company uses the Strategic Direction Statement to illustrate the long term view of managing the Company's assets, so the 5 year plan can be seen in this context.

Louise Bardsley noted that the Customer Research should seek to clarify the cost risk balance Customers are willing to accept.

Paul Dendle raised a concern that Portsmouth Water were trying to satisfy Ofwat rather than the Customer.

Neville Smith noted that Ofwat have a duty to protect the customer ensuring that the Company maintained a good service but at a price that is not more than it needs to be. To achieve this they need evidence, but agreed the Company should seek to establish and deliver what customers wanted.

The Forum discussed the potential impact on bills of changing levels of investments and the benefits and practicalities of smoothing bills in the longer term.

Rod Porteous gave a summary of the planned studies the Company's undertaking to determine the required capital maintenance.

A copy of the presentation is attached to these minutes.

**8. Any Other Business**

**9. Date of Next Meeting**

Tuesday 2 October 2012 at 10.00 am

# PORTSMOUTH WATER Ltd

## CUSTOMER CHALLENGE GROUP (CCG)

### MEETING HELD ON TUESDAY 2 OCTOBER 2012

**PRESENT:** Amy Atkins (Secretary), Colin Buckle (Environment Agency), Hugh Caley (Carillion Plc), John Colley (Portsmouth Water), Cllr Evans (Fareham Borough Council), Karen Gibbs (Consumer Council for Water), David Guest (Independent Chair), R Porteous (Portsmouth Water), Milo Purcell (Drinking Water Inspectorate), Nick Sheeran (Portsmouth Water), G Simmonds (Portsmouth Water), Neville Smith (Portsmouth Water), Jon Stuart (Havant & District Citizens Advice Bureau), Cllr Victoria Weston (Winchester City Council)

#### Action

#### Apologies

Apologies were received from Louise Bardsley (Natural England), Jim Barker (Environment Agency), David Bland (Consumer Council for Water), Cllr David Collins (Havant Borough Council), Andrew Day (Ofwat), Cllr Paul Dendle (Arun District Council), Mark Hann (Consultant), Richard Harris (NHS), John Havenhand (Consumer Council for Water), Cllr Simon Oakley (Chichester District Council), Chris Manning (South Downs), Cllr Stephen Philpott (Gosport Borough Council), Ian Rawson (KWS Defence), Tim Richings (South Downs), Stuart Wedgbury (East Hampshire District Council & Havant Borough Council), Cllr Rob Wood (Portsmouth City Council)

#### 1. Minutes & Actions of Meeting Held on 3 July 2012

The minutes were approved.

At the last meeting Louise Bardsley requested the National Farmworkers Union be invited to join the CCG. Gareth Simmonds confirmed that John Archer, the Company's Catchment Management contact has been invited.

Neville Smith confirmed that the revised Terms of Reference was circulated to the CCG on 30 July 2012.

#### 2. Outcomes Update

Gareth Simmonds informed the meeting on the proposed Outcomes Assurance Statement and Process.

When explaining the Method of Delivery for the proposed Outcomes Gareth Simmonds recommended that an Independent Engineering Consultant is appointed to review the technical details behind the options of delivery to provide the CCG with assurance. Neville Smith confirmed that the Company would seek to engage an appropriate individual or firm.

There was a discussion on the Incentive Mechanism being developed by Ofwat. Gareth Simmonds confirmed that the incentives were both penalties and rewards and Ofwat will publish a Methodology Statement in December providing guidance on these.

Milo Purcell commented that the DWI were in discussion with Ofwat regarding these Incentive Mechanisms as they believe companies shouldn't gain benefits for delivering what is expected of them. Gareth Simmonds confirmed that the rewards may not be financial but reputational.

Gareth Simmonds suggested that Ofwat's Methodology for the Incentive Mechanism be put on a CCG agenda following its publication in December.

GS

Milo Purcell commented that the Company needs to be able to measure

	Action
<p>performance not only by demonstrating that the activity has been done but that the desired outcome has been delivered. Gareth Simmonds confirmed that the Company will discuss how to measure performance and then share the ideas with the CCG to decide the best way forward.</p>	GS
<p>Gareth Simmonds advised that at the next meeting the Owner/Sponsor of each Outcome - which will be a Director and a Manager, will present to the CCG on their Outcome Assurance Statement and Performance measures. Karen Gibbs requested that these presentations be circulated ahead of the next meeting.</p>	
<p><b>3. Customer Research Update</b></p>	
<p>Nick Sheeran updated the meeting on the progress of the Customer Research following the Sub Group's meeting on 2 August 2012.</p>	
<p>The Sub Group recommended the following changes to MVA Consultants proposals:</p>	
<ul style="list-style-type: none"> <li>• Qualitative Research – Increased the number of Focus Groups from 2 to 4</li> <li>• Quantitative Research – All 500 customer interviews will now be carried out face to face.</li> </ul>	
<p>MVA Consultants are currently organising the Focus Groups and design material. The design material will be circulated to the Sub Group for approval and then MVA Consultants can proceed with the Focus Groups with completion by end of October 2012.</p>	NJS
<p>Quantitative Research can then be developed with completion in January 2013.</p>	
<p>Nick Sheeran confirmed that the approved design material will be circulated to the CCG for information and the results of the Focus Groups will be reported back at the next meeting.</p>	
<p>David Guest requested a copy of this report ahead of his meeting with the other CCG Chairs on 6 November 2012.</p>	NJS
<p>Karen Gibbs requested that the CCG be notified of the dates and times of the Focus Groups for any members to attend and observe.</p>	NJS
<p>Milo Purcell suggested getting assistance from the CBI or Chambers of Commerce to contact Businesses. Nick Sheeran agreed to discuss this with MVA Consultants. Karen Gibbs commented that Consultants such as MVA would have a large Business Customer Database to utilise.</p>	NJS
<p><b>4. Water Resources Management Plan Progress</b></p>	
<p>Gareth Simmonds presented on the progress of the Water Resources Management Plan.</p>	
<p>He highlighted the most significant change in this years plan is that the Company is no longer in a deficit position; therefore, certain projects such as Havant Thicket and Compulsory Metering will not be necessary in the current plan.</p>	
<p>Cllr Evans questioned whether the Company would be in a deficit position should the planning forecast change or the affects of climate change have an impact. Gareth Simmonds confirmed that the level of risk associated with these is included for in the headroom.</p>	
<p>David Guest requested that all future graphs be enlarged to ensure the information is clearly displayed.</p>	GS
<p>Colin Buckle commented on lessons learnt during previous plans and advised that customer engagement tends to increase as the process goes along but wanted to remind the CCG that the most important stage to engage our customers is now at the draft stage.</p>	

David Guest informed the meeting that the lack of new housing development is causing a national crisis in under provision. The Company needs to consider the need and supply of new housing. Gareth Simmonds will raise this with Experian.

GS

Jon Stuart questioned the reason the Company was measuring by Per Capita Consumption. Gareth Simmonds confirmed that Ofwat's guidance requires Per Capita Consumption forecasts.

David Guest suggested encouraging household re-use. Gareth Simmonds commented that the Company has enough water to meet the demand and it is cheaper for the customer to have the Company supply water than for them to carry out rain water harvesting. Milo Purcell added that grey water has a high water quality risk with pollution problems.

**5. Catchment Management Presentation**

Alastair Stewart was invited to present on the Catchment Management Project. A copy of the presentation is attached to these minutes for information.

Rod Porteous advised the meeting that the Project costs the Company £50,000 a year which is minimal compared to a Nitrate Membrane Plant costing £4M. Proposals for AMP6 will be bought forward at a future meeting.

**6. Any Other Business**

**7. Date of Next Meeting**

**10 January 2013**

**8. Further Meeting Dates**

**Tuesday 26 March 2013**

**Tuesday 25 June 2013**

**Tuesday 24 September 2013**

**Tuesday 7 January 2014**

**PORTSMOUTH WATER Ltd**  
**CUSTOMER CHALLENGE GROUP (CCG)**  
**MEETING HELD ON THURSDSAY 10 JANUARY 2013**

**PRESENT:** Jane Day (Secretary), Jim Barker (Environment Agency), John Colley (Investment Manager), Cllr Paul Dendle, Arun District Council, Karen Gibbs (Consumer Council for Water), David Guest (Independent Chair), Richard Harris (West Sussex Hospitals Trust), John Havenhand (Consumer Council for Water), Chris Manning (South Downs), Rod Porteous (Engineering Director), Elinor Cordiner (Drinking Water Inspectorate), Ian Rawson (KWS (Defence)), Nick Sheeran (Portsmouth Water), Gareth Simmonds (Portsmouth Water), Neville Smith (Portsmouth Water), Andrew Day (Ofwat Observer), Cllr John Conner (Chichester District Council).

**Action**

**Apologies**

Apologies were received from Louise Bardsley (Natural England), Hugh Caley (Carillion), Simon Oakley (Chichester District Council), Cllr Victoria Western (Winchester City Council), Jon Stuart (Havant & District Council Review), Amy Atkins (Portsmouth Water), Cllr Evans (Fareham Borough Council)

**1. Minutes & Actions of Meeting Held on 2 October 2012**

The minutes were approved and taken as a correct record.

The following actions were reported on:

At the last meeting Gareth Simmonds agreed to include Ofwat's methodology for the incentive mechanism to put on a CCG agenda following its publication in December.

Gareth Simmonds confirmed that the methodology would be published early 2013. It will also be included on the next agenda.

Portsmouth Water confirmed they would discuss how to measure the Company's performance in achieving their outcomes and then share ideas with the CCG to decide the best way forward.

Gareth Simmonds reported that this is ongoing and will be discussed further in Item 4.

It was agreed at the last meeting to circulate the Customer Research design material to the sub group for approval.

Nick Sheeran reported that this is now complete.

It was agreed at the last meeting that Nick Sheeran would send a copy of the design report to David Guest and other CCG chairs ahead of the meeting.

Nick Sheeran reported that this had been completed.

At the last meeting Karen Gibbs requested that CCG be notified of the dates and times of the focus group for any members to attend and observe.

Nick Sheeran reported that this has now been completed.

At the last meeting it was recorded that Milo Purcell suggested getting assistance from the CBI and Chambers of Commerce to contact businesses. Nick Sheeran agreed to discuss this with MVA Consultants.

Nick Sheeran replied that this is an ongoing action.



David Guest requested that all future graphs be enlarged to ensure the information is clearly displayed.

It was agreed that this had been done.

At the last meeting David Guest noted that the lack of new housing development is causing a national crisis in under provision. The Company needs to consider the need and supply of new housing. Gareth Simmonds will raise this with Experian.

Gareth Simmonds reported that he has been in contact with Experian and they had contacted local councils and parish councils and the property forecast took account of this research.

## 2. Overview of process & draft itinerary

Nick Sheeran informed the meeting of the Overview of Process & Draft Itinerary, highlighting major milestones through to 2014. It ties into each meeting the ideas/requirements that need to be addressed to ensure that the CCG forums are informed of progress and how to challenge us.

Jim Barker stated that it is important that relevant reports are produced and actions are included.

Nick Sheeran commented that Portsmouth Water are currently in the process of appointing an External Reporter to ensure that everyone is completely informed and kept up to date with progress.

It was agreed to review the timetable and reissue it.

NJS

## 3. Governance Procedures

David Guest presented the meeting with the Governance Procedures and the Governance Procedures were accepted by the group.

It was agreed that the draft outcomes would be published on the website to encourage comments/thoughts from customers that will evolve over time.

NJS

## 4. Outcome Assurance Statements

Gareth Simmonds presented the Outcome Assurance Statements to the CCG and explained that the reasons for the statements are to allow the CCG to challenge them. Gareth stressed that this is a live document and that it will evolve over time.

Karen Gibbs questioned the content but suggested this be discussed in more detail outside the meeting. Members of the CCG to provide comments on the documents to Portsmouth Water.

All

Several alterations were made to the Outcome Assurance Statements. It was agreed that Gareth Simmonds would update and circulate.

GS

## 5. Leakage

Rod Porteous updated the CCG on the current leakage situation. Portsmouth Water are currently in discussion with Ofwat after an error in the calculation of our reported leakage figure. We are now reviewing our methodology of leakage and how we calculate leakage. In July 2012 we appointed an Independent Consultant who identified a number of issues. We informed Ofwat early October 2012 of our missed leakage target. Rod Porteous stressed that this was a genuine mistake and Portsmouth Water were open and honest with Ofwat and adhering to the recovery process.

The Company has put in place a recovery plan we are working to the cost of which is not borne by our customers but funded by reduced dividends for shareholders, there was no deterioration in their level of service.

Neville Smith commented that this was a serious error. Portsmouth Water are now on target for delivering their leakage action plan and reaching our goals. There is a requirement to spend more money on leakage to rectify the situation.

John Havenhand questioned whether this level of leakage is historic?

Rod Porteous replied that under reporting dates back to a number of years, but Portsmouth Water are currently challenging leakage internally.

## 6. Customer Research: Results & Update

Nick Sheeran presented to the meeting an overview of the Draft Engagement Strategy highlighting the main points from the qualitative research carried out by MVA consultants, which was presented to the Customer Research Sub Group on 18 December 2012.

It was agreed that Nick Sheeran would update the Draft Engagement Strategy with timelines and reports to reflect the input of work Portsmouth Water are carrying out to the Water Resources Management Plan.

It was agreed that Nick Sheeran would redraft and reissue.

A discussion took place on whether Portsmouth Water's approach to customer research was innovative enough and should additional approaches be considered. The group discussed the importance of maintaining the balance between the approach to research and impact on customer bills.

Nick Sheeran stated that we are now at the quantitative stage and this is very critical. Early feedback from the Customer Research Sub-group is essential.

Nick Sheeran stated that Phase 3 of the research would provide an opportunity to carry out further research.

Karen Gibbs said that Portsmouth Water needed to do more to raise awareness of who we are and what we do (and to distinguish ourselves from Southern Water). Paul Dendle said that we should do more to communicate with and read out to younger people i.e. via Social Media.

Karen Gibbs questioned whether Portsmouth Water could contact other companies, schools, local parties of the Water Resources Management Plan for additional feedback.

Nick Sheeran talked through the next steps of the customer research and stressed that Portsmouth Water are on an extremely tight schedule over the next few months. MVA Consultants are concerned about the tight timescale.

## 7. Water Resources Management Plan

Gareth Simmonds presented the progress of the Water Resources Management Plan. It was highlighted that Portsmouth Water is forecasting a surplus over the planning period. However Portsmouth Water has the potential to offer bulk supplies to neighbouring Companies as a result of the WRSE work.

Jim Barker noted the engagement the Company has undertaken and welcomed the sharing of the work on plan with the EA. WRMP shareholder group should seek to engage a wider group.

It was also noted that the per capita consumption forecast was falling over the planning period and this met the aspiration set out on the Government Water White Paper.

The group discussed the implications of Portsmouth Water providing a bulk supply and how this may impact customers.

It was commented that Portsmouth Water needed to ensure that all the WRMP Stakeholders gave their views before the document went to consultation. We may have to 'coerce' them.

#### **8. External Reporter**

Nick Sheeran reported to the meeting that the Company is currently in the process of tendering for an External Reporter. When appointed, the Auditor will also, independently, assist the Customer Challenge Group in their analysis of information provided by Portsmouth Water in its preparation of a Business Plan.

This should be in place by the end of February 2013.

#### **9. Base Level of Operating Expenditure (OPEX) & Impact on Bills**

Nick Sheeran presented the Company's base level of Operating Expenditure and the impact on bills.

John Connor noted that the figures consistently fall under the final determination, could Ofwat reduce the final determination?

Neville Smith agreed that this is a possibility but Ofwat normally base it on operating numbers.

David Guest questioned when was the last time Portsmouth Water had an increase?

Neville Smith replied that it has been some years since there has been an increase, prices are reducing each year. It is important to note that bills won't be stable.

Paul Dendle questioned whether it is because of lower economic activity that bills have not increased.

Nick Sheeran reported that businesses are more focused on water efficiency

David Guest replied that this is a product of marketing – to save water and waste less.

David Guest stated that on the subject of "Financeability" that the CCG should refer to this in their final report to show that it had been considered and discussed.

#### **10. Portsmouth Water's Relative Efficiency**

Neville Smith presented the CCG with a report on Portsmouth Water's Relative Efficiency. He explained that Ofwat set water companies an efficiency challenge for both Operating and Capital Expenditure. Incentives to improve are agreed by the CCG.

Neville Smith indicated that Portsmouth Water were at the high end of the league table. Portsmouth Water has to provide evidence that this is still the case.

#### **11. Presentation from the Angling Trust**

Mark Owen was invited to present on the Angling Trust – Blueprint for Water.

**Action**

**12. Any Other Business**

Nothing to report.

**13. Date of Next Meeting**

Tuesday 26 March 2013.

**PORTSMOUTH WATER Ltd**  
**CUSTOMER CHALLENGE GROUP (CCG)**  
**MEETING HELD ON TUESDAY 26 MARCH 2013**

**PRESENT:** Colin Buckle (Environment Agency), Charles Burns (Federation of Small Businesses) Cllr Paul Dendle (Arun District Council), Amy Denford (Secretary), Karen Gibbs (Consumer Council for Water), David Guest (Independent Chairman), John Havenhand (Consumer Council for Water), Douglas Hunt (Atkins Independent Reporter), Simon Oakley (Chichester District 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)

**Action**

**Apologies**

Apologies were received from Traci Baker (Hampshire Chambers of Commerce), Hugh Caley (Carillion), John Colley (Portsmouth Water), David Collins (Havant Borough Council), Elinor Cordiner (Drinking Water Inspectorate), Andrew Day (Ofwat), Cllr Evans (Fareham Borough Council), Richard Harris (West Sussex Hospitals Trust), Douglas Kite (Natural England), Chris Manning (South Downs), Cllr Stephen Philpott (Gosport Borough Council), Ian Rawson (KWS Defence), Tim Richings (South Downs), Stuart Wedgbury (East Hampshire District Council & Havant Borough Council), Cllr Victoria Weston (Winchester City Council) and Cllr Rod Wood (Portsmouth City Council)

David Guest expressed concern over the number of apologies being received. It was agreed that when apologies are received in the future they will be asked to send a representative.

AD

**1. Minutes & Actions of Meeting Held on 10 January 2013**

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

The following actions were reported on:

**Overview of process & draft itinerary**

Nick Sheeran confirmed that a revised timetable had been agreed and circulated.

**Governance Procedures**

Nick Sheeran confirmed that the revised Outcomes were included in the Draft Outline Business Plan which will be published on the website shortly.

**Outcome Assurance Statements**

Gareth Simmonds confirmed as above that the Outcome Assurance Statements had been updated and circulated to the CCG as part of the Draft Outline Business Plan.

**Customer Research: Results & Update**

Nick Sheeran confirmed that a revised Engagement Strategy had been drafted and sent to the CCG with the Agenda for this meeting to be discussed in AOB.

**2. Ofwat Methodology**

Gareth Simmonds presented to the CCG giving an overview of the Ofwat framework, highlighting the different approach from the last Price Review.

Gareth Simmonds raised concern over timescales if Ofwat decide to bring forward the deadline for the Final Business Plan submission from January 2014 to the beginning of December 2013. This would require the Final Business Plan to be

completed by November 2013 to submit to the Board for approval.

Neville Smith confirmed that work is underway on the Final Business Plan on the basis of Ofwat's previous Methodology as the Methodology for this Price Review is not anticipated to be available until the end of Summer 2013. The Company is concerned that this will not give the Company sufficient time to complete the Plan taking into account any changes to Ofwat's Methodology and will not give the CCG adequate time to give due consideration to the Plan to prepare their Report to Ofwat.

David Guest suggested writing to Ofwat expressing concerns over both the Company's inability to complete the Final Plan in a timely manner and the CCG's inability to prepare and submit their report on the Final Plan in the given timescales. The CCG were in agreement and it was decided that David Guest would write to Ofwat on behalf of the CCG and copy the other CCG Chairs into his letter, also writing to the CCG Chairs separately asking if they share the same concerns and what measures they are putting in place.

**DG/AD**

Gareth Simmonds highlighted that the Company and CCG need to work and co-operate with Ofwat in order to deliver a Business Plan for our Customers.

Neville Smith raised concern that there needs to be sufficient time for technical issues to be resolved and to look at the various options to approach Customers with which the new timetable is not allowing time for.

David Guest requested the Company draft a revised timetable that is workable with Ofwat's new deadline including possible rescheduling meetings, and that the Company circulates this to the CCG.

**GS**

Gareth Simmonds confirmed that Ofwat will be publishing their Information Requirements in April which will give some guidance. He also stressed that collectively all Companies had expressed their concerns to Ofwat at a recent Meeting.

Colin Buckle asked if the Water Resources Management Plan that informs the Business Plan is aligning with the new timescales. Gareth Simmonds confirmed that it was, however, the Water Resources Management Plan is not proposing any investment and therefore any further changes should not fundamentally change the Business Plan.

David Guest asked Karen Gibbs to update the CCG on a recent Ofwat Workshop.

Karen Gibbs informed the CCG that the Ofwat Workshop outlined the key aspects of the Methodology and its impact on the CCG's. She confirmed that Ofwat's thinking still hadn't got into the detail of what the CCG's Report should cover. Ofwat's new Team did not want to prepare a template as they feel this would stifle innovation. The point was raised to Ofwat that for the CCG's to be able to provide a Report that is fit for purpose more clarity is needed. Ofwat agreed to provide more information to CCG Chairmen and it was suggested that after the release of their Information Requirements at Easter another Workshop should be held to discuss reporting requirements.

Karen Gibbs advised that Regina Finn of Ofwat confirmed that the new approach is to move Companies away from being lead by Regulation and rather be informed by Customers.

Neville Smith confirmed that he thought the new approach was working and that Companies are taking genuine ownership of their Plan.

Karen Gibbs confirmed that Ofwat will provide comparative information to inform the CCG and is setting up a webpage for CCG Members to refer to.

### 3. Customer Quantitative Research

Nick Sheeran presented on the Final Results of the Customer Quantitative Research.

John Havenhand raised his concern over contextualising willingness to pay (WtP). The Company did ask Customers if they would be WtP if Southern Water increased their bill but did not then put it into context e.g. reminding them that their salary would remain the same and everything else they pay for will also be going up. Therefore, he stressed the need for the results to be looked at with care and not taken literally.

John Havenhand highlighted a good point made by MVA at the Customer Research Sub Group Meeting that Customers don't like to see increases in their bills, however, during the Research when asked how much their bill currently was they had no idea, so technically may not notice an increase.

Nick Sheeran highlighted that the WtP figures actually needed to be factored down, as at the end of the survey Customer's were asked "what is the maximum they would be WtP?" This was only £7.00.

Karen Gibbs commented that the Company would not have to spend the maximum WtP to address the improvements: e.g. in respect of water softening. The Company does not have to carry out full water softening but provide more information and advice to Customers on the issue of water hardness.

Nick Sheeran commented that would mean that the WtP for these aspects would therefore be reduced.

Karen Gibbs highlighted that the findings showing the Customers top six improvements is not a literal budget but customers' priorities.

Jon Stuart informed the CCG that the maximum WtP figure should not be taken literally as 25% of Customers didn't want any increase but were excluded from the Results. Douglas Hunt expressed concern over this; however, the Customer Research Sub Group reassured the CCG that MVA confirmed it was standard practice and they were happy with their explanation.

John Havenhand made the point that Customers may already be satisfied and therefore not willing to pay for any improvements. However, if they were dissatisfied Customers may be willing to pay.

John Havenhand spoke on behalf of the Customer Research Sub Group and confirmed that they were satisfied that MVA had done the job well but the methodology was open to interpretation and therefore care needed to be exercised when reviewing the Results.

David Guest confirmed that he would like Douglas Hunt to review the Customer Research and Results to give the CCG a level of confidence.

DH

Colin Buckle noted from the Results that it suggests 75% of Customers may be happy with metering.

Neville Smith agreed that the Company needs to get the message across to Customers that they could save money by going on a meter.

Paul Dendle suggested Portsmouth Water liaise with Local Councils to obtain Single Occupier Information and then they can target Customers that would benefit from switching to a water meter.

### 4. External Assurance Reporter

Nick Sheeran advised the CCG that the Company had undertaken a Tender

Process to select a new Independent Reporter. He introduced Douglas Hunt from Atkins as the newly appointed Reporter who would also be working for the CCG.

Douglas Hunt gave the CCG assurance regarding his experience, capability, independence and his involvement in the Engagement Process.

Neville Smith confirmed that he will circulate a schedule of work that Douglas Hunt is carrying out for the Company ahead of next times meeting so the CCG can decide what additional work they would like him to complete on their behalf.

NS

The CCG accepted the appointment of Atkins as their provider of assurance. It is essential however, that Douglas Hunt is regarded as independent of the Company when dealing with issues on behalf of the CCG.

## 5. Outline Business Plan

Nick Sheeran circulated the Draft Outline Business Plan that has been informed by the Customer Research and recently agreed by the Board.

Nick Sheeran confirmed that it was being put on the website and going out to Stakeholders for Consultation at the end of March. The Plan includes a Feedback Questionnaire. A summary will be included in Portsmouth Waters Customer Newsletter in May with a free prize draw as an incentive to encourage a good response from Customers.

NJS

Nick Sheeran welcomed comments on the Draft. Colin Buckle commented that the EA had seen five other Companies Outline Business Plans and that Portsmouth Water had the best suite of Outcomes. However, he noted that throughout the Leakage Section of the Plan the Company repeatedly says 'we will continue to...' when the Research shows that this is a priority for Customers and they want this to be heightened. Nick Sheeran confirmed that this wording was chosen following the Research as the Company did not want Customers to think it was a new approach as these things are already being done. However, the point was taken and the wording will be reconsidered.

Colin Buckle also commented that the Environmental Outcome is worded 'We aim to promote...' which is very subjective terminology and suggested it be replaced with more objective phraseology.

Karen Gibbs suggested within the Customer Priorities changing Water Softening to Water Hardness and re-wording the statement to be more positive as to what the Company intends to do.

The CCG's comments were noted and Nick Sheeran encouraged the Members to make any further representations during the Consultation period.

## 6. WRMP – Draft Plan and Consultation Process

Gareth Simmonds presented to the CCG on the Water Resources in the South East (WRSE) and Portsmouth Water's Water Resources Management Plan (WRMP).

Gareth Simmonds encouraged CCG members to make representations during the Consultation period. He noted that the CCG would comment on the Plan as it would form part of the business plan.

Neville Smith informed the CCG the WRMP will be submitted on the Base Plan.

David Guest questioned whether Climate Change is considered in the Plan.

Gareth Simmonds confirmed that Climate Change is taken into account in the Company's Drought Plan. The WRMP is based on a dry year / critical period average whereas the Drought Plan is based on a historical worst case event that



has already taken place to inform how to meet the demand. The WRMP plans up to a drought but does not include them.

John Havenhand commented that there is a logical problem with drought planning based on a historical worst case event as there still could be a more significant drought in the future. He noted that Havant Thicket was not required in the Base Plan and the Supply Demand Balance Graph looks quite tight towards the end.

Gareth Simmonds commented that this is the problem with Schemes that need a long lead time. By the time they are required you don't have time to put them in place. The WRSE is clear that Havant Thicket has an important part to play in sustaining supplies in the future for bulk supplies.

David Guest suggested that Havant Thicket would reduce the environmental impact of bulk supplies.

Colin Buckle agreed that Havant Thicket did have a regional benefit.

John Havenhand asked what needed to happen for the Alternative Plan to get some traction.

Gareth Simmonds confirmed that it was dependant on other Companies requiring bulk supplies.

Gareth Simmonds referred the CCG to the WRSE Scenarios in his presentation and commented that Scenario C3 would trigger the Alternative Plan.

Karen Gibbs asked what the current rate of meter optants were and Gareth Simmonds confirmed that it was 5,000 and would stay the same.

Karen Gibbs raised the point that Research shows Customers want meters and neighbouring Companies are bringing in metering.

Douglas Hunt commented that metering may be cheaper for individual Customers but metering the Customer base as a whole will increase bills for everyone.

## **7. Efficiency**

Neville Smith informed the CCG that Ofwat have historically set price limits based on RPI plus or minus K: an efficiency index for Companies. He raised the question of what the Company needs to provide in the way of evidence to the CCG to satisfy them of the Company's efficiency. Historically Portsmouth Water has always been regarded as the most efficient Company.

Neville Smith suggested not completing any further work but to rely on historical data and industry benchmarks that Ofwat may produce and commented that it would not be in anyone's interest to spend money on something already being carried out at industry level.

Karen Gibbs agreed that Ofwat's data published will be enough to satisfy the CCG.

Neville Smith confirmed that Ofwat will give Company a baseline of opex/capex and the CCG can challenge then, rather than doing a specific piece of work now.

Karen Gibbs commented that the CCG will need to compare Company's assumptions with those of Ofwat.

Douglas Hunt confirmed that Ofwat have historically published a paper that shows the relative efficiencies of companies and the CCG could compare this paper with the Company's assumptions. The paper assesses how much more efficient a Company should get: Comparative Benchmarking.

Neville Smith noted that if the end results are increased prices you could question a Company's efficiency. He commented that Ofwat published a paper stating that if there was pressure on prices because of competition Companies would find ways of being more efficient.

John Havenhand commented that efficiencies relate to input / output and therefore wanted to make sure that efficiencies are not delivered by reducing activity.

Neville Smith summarised confirming that the Company would not be doing a specific piece of work but will rely on Ofwat to inform the CCG of the Company's efficiency.

## 8. Base Opex

Nick Sheeran presented to the CCG on the Company's Base Opex, comparing the budget to Ofwat Determination and current projection.

Nick Sheeran confirmed that the actual operating costs came in lower than the Ofwat Determination and last years budget.

Jon Stuart questioned where the Company had spent less and Nick Sheeran confirmed that savings had been made on electricity usage and the Environment Agency decided not to impose abstraction charges.

Nick Sheeran commented that the prices given in his presentation were indicative as awaiting Ofwat's Methodology and still need to factor in Totex.

John Havenhand questioned if the figures were not subject to inflation then the retail element is not indexed resulting in RPI being less than actual RPI.

Neville Smith confirmed that Retail is 10% therefore can only increase 90% by RPI.

Jon Stuart asked what the commercial overspend related to, resulting in Capex being more than expected. Nick Sheeran confirmed that this was due to additional IT costs and a new Billing System.

Neville Smith confirmed that before the September meeting the Company will ask Douglas Hunt to look at the Base Opex to be able to reassure the CCG.

NJS/DH

## 9. Indicative Capital Maintenance – Infrastructure

Rod Porteous presented the Company's Infrastructure Indicative Capital Maintenance to the CCG.

He outlined the six types of Capital Maintenance Expenditure;

- Quality
- Security / Emergency Measures
- Enhanced Service
- Supply and Demand
- Management and General
- Capital Maintenance

Capital Maintenance is further split between infrastructure and non-infrastructure, below and above ground assets.

Rod Porteous highlighted that the Company has approximately 300,000 stopcocks and their repair / replacement accounts for 50% of the Company's Opex Expenditure. In recent years the Company made the decision to stop installing stopcocks on the Customers boundary but instead to mount them on Customers properties, known as wall-mounted meter boxes. This has dramatically reduced the Company's costs and referring back to John Havenhand's early comment regarding the difficulty in cutting the fat from something that's already lean. The

Company would find it difficult to find further efficiencies in this area.

Rod Porteous picked up on a term used by Milo Purcel at a previous CCG meeting; 'Stewardship'. As Portsmouth Water is a small Company there is a good understanding and knowledge of its Network and reassured the CCG of continual monitoring and investigation undertaken.

Rod Porteous confirmed that Douglas Hunt would be asked to look at the Deterioration Modelling completed by the Water Research Centre (WRC) on behalf of Portsmouth Water to give confidence to the CCG.

**RCP/DH**

Rod Porteous outlined the deterioration modelling that the Water Research Centre (WRC) was undertaking on infrastructure, work follows a similar approach to that taken for AMP4 & AMP5. He outlined an incremental increase in lengths of main lost with associated benefits such as leakage. The outcomes from WRC draft report are undergoing internal challenge, once the Company is satisfied upon the technical robustness they will arrange for the Reporter to review the work and report to the CCG.

Karen Gibbs raised concern over the Company's decision to undertake deliberative research on leakage in isolation as it could produce biased results.

Neville Smith commented that the Company's approach to leakage is one of the single biggest areas the CCG will need to challenge, as a reduction below the economic level is likely to increase the Customers bill. Customers will not necessarily see the results, as the Company already has a surplus of water.

**10. Any Other Business****Revised Draft Engagement Strategy**

Nick Sheeran confirmed that he had revised the Draft Engagement Strategy incorporating the feedback from the CCG at their last meeting.

**11. Date of Next Meeting**

Tuesday 25 June 2013

**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.

**PORTSMOUTH WATER Ltd**  
**CUSTOMER CHALLENGE GROUP (CCG)**  
**MEETING HELD ON THURSDAY 15 AUGUST 2013**

**PRESENT:** Charles Burns (FSB), Daire Casey (West Sussex County Council), John Colley (Portsmouth Water) In Part, Amy Denford (Secretary), Keith Evans (Fareham Borough Council), Karen Gibbs (Consumer Council for Water), David Guest (Independent Chairman), Marge Harvey (East Hampshire District Council), John Havenhand (Consumer Council for Water), Douglas Hunt (Atkins Independent Reporter), Mike Kirk (Portsmouth Water) In Part, Douglas Kite (Natural England), Terry Lazenby (Portsmouth Water), Simon Oakley (Chichester District Council), Milo Purcell (Drinking Water Inspectorate), Nick Sheeran (Portsmouth Water), Gareth Simmonds (Portsmouth Water) and Neville Smith (Portsmouth Water)

**Action**

**Apologies**

Apologies were received from Traci Baker (Hampshire Chambers of Commerce), Jim Barker (Environment Agency), Andrew Day (Ofwat), Cllr Paul Dendle (Arun District Council), Hugh Caley (Carillion), David Collins (Havant Borough Council), Richard Harris (West Sussex Hospitals Trust), Cllr Derek Kimber (Gosport Borough Council), Chris Manning (South Downs) Cllr Kirk Phillips (Winchester City Council), Rod Porteous (Portsmouth Water), Ian Rawson (KWS (Defence), Tim Richings (South Downs), Jon Stuart (Havant & District Citizens Advice Bureau) and Cllr Rod Wood (Portsmouth City Council)

**Minutes & Actions of Meeting Held on 25 June 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 advised that he still had to send Doug Hunt MVA Consultants explanation of why they include one obviously more favourable option in the Customer Research to break down the correlation in the results.

**Base Opex**

Doug Hunt advised that his actions arising out of this item from the last meeting were going to be covered in this agenda.

**Mains Renewals**

Doug Hunt advised that his actions arising out of this item from the last meeting were going to be covered in this agenda.

**Outcomes**

Neville Smith advised that a Sub Group had been formed to look at the Outcomes in more detail and they met on 1 August 2013. Feedback from this meeting will be provided later in this agenda.

**Company's External Assurance Process / Timetable**

Karen Gibbs advised that she still had to provide the Company with the name of a recommended Customer Research Expert to provide a Report giving further assurance.

Karen Gibbs advised that she will inform the CCG of the CCWater Acceptability Threshold Research that had been completed later in this agenda.

**NJS**

**KG**

Nick Sheeran advised that he still had to reconvene the Customer Research Sub Group to challenge the deliberative research. MVA have started preparing the Research and the Sub-Group will be reconvened shortly.

### **Approach to CCG Assurance and CCG Report**

Neville Smith advised that a paper on the Company's Past Performance was enclosed with the agenda for the CCG's information.

### **Base Opex and Cost of Capital**

Doug Hunt advised that his actions arising out of this item from the last meeting were going to be covered in this agenda.

Nick Sheeran advised that his actions arising out of this item from the last meeting were going to be covered in this agenda.

Nick Sheeran confirmed that Ofwat were not going to provide any information on the Cost of Competition. They referred the Company to the High Level Group.

### **Timetable and CCG Meeting Dates**

Amy Denford confirmed that meeting dates had been scheduled up until the submission of the Business Plan and the dates were enclosed with the agenda.

### **Water Quality Schemes - Boreholes Turbidity**

Neville Smith informed the CCG that this Scheme would no longer be included in the Business Plan as the risk will be dealt with in different way.

Milo Purcell advised that the DWI can write a letter of recommendation for these Schemes if Company wanted to include them in their Business Plan.

## **1. Consumer Council for Water Research – Acceptability Threshold**

Karen Gibbs circulated a presentation on the Customer Acceptability Threshold Research recently carried out by CCWater. She advised the CCG that CCWater have placed a great deal of importance on the Company carrying out acceptability testing on their Business Plan to sense whether the Company correctly interpreted the results of the Customer Research.

The Research was conducted via Focus Groups across the country. The Research showed on average 70-80% of Customers found Company's Business Plans acceptable with a range of 64-95%. Research also gave an indication of how customers felt engaged in the process.

Nick Sheeran questioned that as the Research had been based on Focus Groups it is not statistically robust and therefore can it be relied upon? Karen Gibbs confirmed that it was not statistically significant it was to inform Company's and give an indication of what Customers would find acceptable.

Douglas Kite questioned how the Company chooses between something with high public acceptability or high cost effectiveness e.g. leakage v metering.

Karen Gibbs advised that whatever choice is made, the reasons why need to be explained to Customers.

Terry Lazenby commented that Douglas Kite made a good point and that choices shouldn't be looked at individually but put in a package.

Gareth Simmonds advised that the Company's Acceptability Testing will look at Options, Packages and Priorities.

Marge Harvey asked if demographics were used in Customer Research. As different Options Packages would appeal to different demographics.

Nick Sheeran confirmed that the samples were representative of demographics.

Neville Smith confirmed that the point raised by Douglas Kite in respect of high public acceptability v high cost effectiveness e.g. leakage v metering would be addressed at the next meeting with a cost benefit analysis on metering being presented for Doug Hunt to review.

Neville Smith questioned what would happen if a Company does not achieve 70% acceptability would that be a problem? Karen Gibbs confirmed that this was not a Regulatory benchmark the Research was carried out just for information to help companies strive to achieve a Customer acceptability level of 70-80%. Whatever level companies achieve the testing will tease out why, which would then be for each Company to address.

Doug Hunt questioned if a national benchmark comes out of this Research, is someone going to look at who is marketing this Acceptability Testing. Karen Gibb's confirmed that there were high level principles set for Acceptability Testing that have been published to assist and Companies are using Consultants that are well experienced in this area for national consistency.

## 2. Summary of Responses to WRMP Consultation

Gareth Simmonds updated the CCG confirming that consultation has led to the receipt of 15 representations mainly from Stakeholders and Regulators, not any direct Customers.

The representations received commented on the following areas;

- Stakeholder Engagement
- Demand Forecast
- Optional Meters
- Bulk Supplies
- Leakage

John Havenhand commented that there was no financial incentive for Customers to reduce their consumption as water bills are so low. However, there would be a saving for them on their sewerage bills if they had a meter installed and this message needs to be communicated effectively to Customers.

Gareth Simmonds confirmed that the Company works proactively with Local Authorities to align the WRMP with Local Authority Plans.

## 3. Outcomes and Measures of Success

Neville Smith advised that the appointed Sub-Group met on 1 August 2013 to discuss in more detail the Company's Outcomes. Revised Outcomes were enclosed with the agenda for the CCG's comments. Neville Smith explained that the next step would be to agree incentive rewards for success, and penalties for failure against each Outcome. He confirmed that a draft proposal would be brought to the next meeting for comment.

Neville Smith advised that the Outcomes would continue to be refined and wording refined throughout the process, and highlighted several suggested amendments since issuing the agenda.

Douglas Kite advised that there needed to be a connection between the Customer priorities established through Customer Research and the Outcomes. He noted that Carbon was not included in the Outcomes. Neville Smith agreed to look at this.

Douglas Kite advised that some of the Outcomes would be difficult to measure e.g. biodiversity. Gareth Simmonds confirmed that measurement methods are being considered.

Neville Smith confirmed that other than biodiversity, the Company chose Outcomes that were measurable and had statistics for them.

David Guest questioned how the Company could measure the Outcome 'value for money'. Neville Smith advised that Customer Satisfaction Surveys; although not statistically robust, gave the Company a good steer.

Simon Oakley reiterated his concern from an earlier meeting regarding highway impact from leakage and how was it measured. Neville Smith confirmed that interruptions to supply statistics are available, measured by the number of properties affected over 3 and 6 hour periods.

Gareth Simmonds added that when the Company sets leakage targets it takes into account traffic disruption and a cost appraisal for that is included.

Milo Purcell advised that other Companies have employed specialist risk assessments for impact on business, especially financial, when setting incentives. Neville Smith confirmed that the Company will carry this out internally as one of the Company's sensitivities.

Gareth Simmonds advised that the incentives would also include Ofwat's Service Incentive Mechanisms (SIM's).

#### **4. Cost of Capital – Current Assumptions**

The Company presented its current view on the weighted cost of capital. The potential impact of Havant Thicket on gearing was raised, as this would require significant capital. The CCG challenged whether this risk should be paid for by Portsmouth customers if the scheme is primarily intended to supply Southern Water.

It was also requested that the potential impact of the Ofwat gearing assumption on bills should be provided at the next CCG.

***Mike Kirk joined the meeting***

#### **5. Base Operating Cost – Final Position**

Nick Sheeran circulated a paper on the Company's proposed Base Operating Costs to be included in the Plan and on Competition Costs.

A discussion followed which covered electricity, pensions, competition and reduction of leakage.

Key challenges were made in relation to electricity, where Nick Sheeran noted that the central assumptions used by Ofwat in the methodology paper were used, the pension assumptions were based on an initial valuation of the pension scheme, and competition costs, were based on Industry estimates.

***John Colley joined the meeting***

#### **6. Legacy Items**

Nick Sheeran informed the CCG that at the end of the planning period Ofwat complete a review of the initial assumptions used and make any necessary adjustments for the next planning period: these are referred to as legacy items. He advised that Ofwat have issued guidance on how to calculate these and therefore

the Company has confidence that they will find this acceptable.

Neville Smith highlighted that legacy items impact on bills by an increase of 4%.

Nick Sheeran advised that they take into account the Cost of Capital, Base Operating Costs as well as legacy Items to get the overall implications on bills which will be addressed later on the agenda.

Simon Oakley requested a breakdown on the revenue correction mechanism. It was agreed that this would be provided at the next meeting.

Nick Sheeran added that commercial consumption had unexpectedly decreased which had an affect.

## 7. Capital Expenditure

In the absence of Rod Porteous, Neville Smith updated the CCG on deteriorating water quality and mains renewals. He welcomed John Colley, Investment Manager to field any technical questions.

### Water Quality

Neville Smith advised that a scheme was required to reduce the risk of Cryptosporidium at two sites. He confirmed that a proposal would be submitted to DWI for the installation of UV Plants at both sites.

Douglas Kite questioned whether the problem could be tackled at source as a cheaper option.

Milo Purcell agreed, and advised that the DWI would recommend Catchment Management which would have to be part of the solution to help the end of pipe solution. However, he confirmed that it would depend on whether that would deliver a quick enough solution to the Cryptosporidium threat and if not, then it would look at interim solutions e.g. UV Plants.

Terry Lazenby raised concern that the Company would not want to risk water contamination. He advised that levels of incidents were increasing and there was a conclusive Geological Survey Report on the matter. He stressed the need for these schemes to be implemented.

Milo Purcell suggested the Company expand on the information they have received at the next CCG.

Terry Lazenby highlighted that relying solely on Catchment Management as a solution leaves the Company and therefore the Customer at risk.

Simon Oakley asked what has changed since the last risk assessments.

John Colley confirmed that the Company had addressed Catchment Management to discover why it has happened, but this is not yet identifiable. He explained that the Company was taking a multi-barrier approach; not just plant, but will also minimise risk through Catchment Management. He emphasized the need for the Company to protect public health.

Simon Oakley stressed the need to identify the source of the problem. John Colley confirmed that there are continuous risk assessments being carried out to identify problem and a better quality well-lining had been installed. The query was made as to whether the 'new' risk was being caused by raw water deterioration and, if so, were alternative options available for mitigation. Milo Purcell indicated that the main reason for the re-appraisal was due to the detection of crypto in samples, and that this may have been associated with recent weather patterns. In terms of alternative options for control, both the DWI and the Reporter team will be challenging to determine if this is feasible, but at this time a catchment

management may be too late.

### **Mains Renewals**

Neville Smith advised that the Board had decided to restrict distribution mains renewals to 22km, which would allow burst levels to remain at current levels and not increase prices for Customers.

John Colley advised that trunk mains were being reviewed by a physical condition assessment. Excavating in areas with high corrosive ground, testing for corrosion and estimating likelihood of future failure.

Doug Hunt confirmed that mains renewals had been challenged thoroughly and advised that the risk involved was reasonable.

Milo Purcell queried whether trunk mains had been subject to sufficient analysis. John Colley noted that historically they had not been a problem and so minimal expenditure was proposed, but this had not been checked by Doug Hunt for assurance purposes.

### ***Marge Harvey left the meeting***

Milo Purcell suggested that the Company make a statement in their Plan re the resilience in distribution mains and likelihood of bursts. The Company has an interconnecting network and burst-impact on Customers is low. He also commented that high cost work can it be spread over 2 AMP periods to reduce impact on customer's bills.

Doug Hunt confirmed that his report dealt with balancing current and future bills.

### **8. CCG Confidential Discussion**

The Portsmouth Water Representatives left the Room for the CCG Members to have confidential discussions. This part of the Meeting was minuted separately.

### **9. Feedback to Company following Customer Challenge Group Confidential discussion**

David Guest requested the Company allow a one hour time slot on the agenda at future meetings for deliberation and decisions.

AD

Doug Hunt fed back to the Company some issues raised at the confidential discussion as follows;

Concern over Company's reputation in respect of promoting water efficiency.

Company had not included water quality failures in mains renewals evaluation. Gareth Simmonds confirmed this was addressed through DOM's Strategy and will discuss this strategy with the CCG at a later date.

RCP

For opex, the CCG challenged and wished to see greater visibility of the potential for efficiency in staff/manpower costs.

The CCG questioned how financial risks are managed. The CCG were not challenging the technical details – e.g. Cost of Capital analysis, but the process, was it balanced, has what is in the best interest for the Customer been considered?

Water quality risks were discussed, and Milo Purcell indicated that he will cover them at the next meeting.

MP

David Guest advised that the CCG will start to engage in the reporting process and will give continuous feedback to the Company.



**10. Outstanding Issues for Review**

Neville Smith advised that the following issues were outstanding for review;

- Incentives
- Catchment Management
- Costing for Capital Schemes
- Capital Maintenance – Non-infrastructure

He confirmed that the above would be discussed at the next meeting, where they relate to bills and what the Company are proposing for efficiencies.

NS

Milo Purcell asked for one additional item to be included on the next meeting agenda, to draw comparisons between Strategic Direction Statement and the Business Plan. How Company will deliver objectives. CCG can see Company is not just looking at 5 years but long term. Focus on expenditure profile through AMP Period and traditional dip at the end. Ofwat have provided in methodology that expenditure in AMP6 can be brought forward to AMP5. Could this be done?

NJS

Nick Sheeran confirmed that due to impact on gearing he did not think it would be a good idea to bring capital expenditure into this period.

Milo Purcell also requested that the Company demonstrates how ownership of the Business Plan has changed.

**11. Implications for Prices**

Nick Sheeran presented to the CCG on the current view of the assumptions being included in the Business Plan having implications for prices. He circulated a paper showing the real changes excluding inflation. He confirmed that the Board's aspiration would be to have no increase before inflation.

Following challenge by Milo Purcell, he confirmed that the Company does not yet know what impact the assumptions will have on business financeability as that part of the Model is not yet available; however, this will be presented at the next meeting.

NJS

Terry Lazenby advised that this needs to be presented with Customer preferences and the Company's Outcomes for CCG to challenge.

NJS

**12. Update on Next Stage of Customer Research**

Nick Sheeran advised that the Company had completed its Customer Research and have decided to carry out Deliberative Research in two areas; Leakage and Resilience. This will consist of Customers in small Focus Groups, to understand Customers views on leakage and resilience.

**13. Update on External Technical Assurance Reviews**

Doug Hunt gave the CCG assurance that his Technical Review on Distribution Mains Renewal is now complete and that he will now review Trunk Mains. He confirmed that the methodology approach was put together well. There were uncertainties on leakage risks and future spend profile, but the Company have amended their proposals to allow for this and hence proposals are now in line with the Assurance Review. He confirmed that what the Company have included in Business Plan is therefore reasonable for infrastructure maintenance. In respect of above ground maintenance it is too early to tell. Further refining/challenge being done to programme. Approach is reasonable and as you would expect.

Quality Schemes Review will be looked at in more detail. He advised that the decision whether each scheme is needed is down to DWI, therefore the CCG will

just challenge the proposed solution.

In respect of Operational Costs there is not much to assure on. He confirmed that he is awaiting the Actuarial Valuation Results to review. Electricity is taken out of the Company's hands as Ofwat are benchmarking. He will provide a further update at the next meeting.

DH

**14. August Data Submission and Report from External Assurance**

Doug Hunt circulated his Report on the August Data Submission. He confirmed this was a standard submission with no significant matters that CCG need to challenge. He gave the CCG assurance that the submission was accurate, reliable and complete.

Milo Purcell asked if there is anything the CCG need to know about regarding efficiencies. Neville Smith advised that efficiencies have been made relative to the Final Determination in 2009 and the Board need to decide if they are passing those benefits to Customers.

Milo Purcell asked if Company are demonstrating innovation in Business Plan. Doug Hunt advised that the process is moving more in line with business best practice.

**15. Calendar of Meetings**

Tuesday 24 September 2013  
Tuesday 22 October 2013  
Tuesday 12 November 2013

**16. Any Other Business**

There was no other business.

**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.

**PORTSMOUTH WATER Ltd**  
**CUSTOMER CHALLENGE GROUP (CCG)**  
**MEETING HELD ON TUESDAY 22 OCTOBER 2013**

**PRESENT:** Paul Barfoot (Portsmouth Water), Hugh Caley (Carillion), 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), Derek Kimber (Gosport Borough Council), Douglas Kite (Natural England), Mike Kirk (Portsmouth Water) In Part, Terry Lazenby (Portsmouth Water) In Part, Kirk Phillips (Winchester City Council), Rod Porteous (Portsmouth Water), Milo Purcell (Drinking Water Inspectorate), Nick Sheeran (Portsmouth Water), Gareth Simmonds (Portsmouth Water) and Neville Smith (Portsmouth Water)

**IN ATTENDANCE:** Paul Le Masurier MVA Consultants

**Action**

1. **Apologies:** Traci Baker (Hampshire Chambers of Commerce), Jim Barker (Environment Agency), Charles Burns (FSB), Daire Casey (West Sussex County Council), David Collins (Havant Borough Council), Cllr Paul Dendle (Arun District Council), Keith Evans (Fareham Borough Council), Marge Harvey (East Hampshire District Council), Chris Manning (South Downs), Simon Oakley (Chichester District Council) Ian Rawson (KWS -Defence) Tim Richings, Jon Stuart (Havant & District Citizens Advice Bureau) and Rob Wood (Portsmouth City Council)

2. **Minutes & Actions of Meeting Held on 24 September 2013**

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

The following actions were reported on:

**Implications for Prices**

Nick Sheeran confirmed that following Terry Lazenby's suggestion he would provide the CCG with the Implications for Prices with Customer Preferences and the Company's Outcomes to the CCG later in the meeting for them to challenge.

**Update on Customer Research**

Nick Sheeran confirmed that he had emailed the research proposal and materials to the Sub Group and confirmed that they would be meeting on 8 November 2013.

He also confirmed that Accent had been commissioned to complete the Peer Review on behalf of the CCG.

**Feedback from CCG**

David Guest confirmed that the draft CCG Report had been circulated for comments.

**Water Quality Risks**

Milo Pucrell advised that the DWI had completed their assessment and have written to the Company with their decision on their Submissions. He confirmed that this would be covered later in the meeting for the CCG to challenge.

Neville Smith confirmed that the Company would justify the Capex figure proposed for the Business Plan later in the meeting.

**Update on Assurance**

Doug Hunt advised that he was in a position to provide the CCG with a full update on his Assurance to date and will circulate a paper later in the meeting.

### 3. Update on Assurance

Doug Hunt circulated a Technical Note providing a summary of the current findings of the assurance process that Atkins has undertaken. It included both the original assurance items that were discussed with the Company at the start of the process and additional items requested by the CCG.

The CCG discussed aspects of the assurance received to date with the Company before they left the meeting.

***Portsmouth Water Representatives left the meeting***

### 4. CCG Discussions on the Draft Business Plan and CCG Report

There was a consensus from the CCG to share the minutes of their discussions with the Company.

Doug Hunt circulated the latest draft of the CCG Report. He advised that he had received further comments from David Howarth.

Doug Hunt advised that the report had been structured according to four key components;

- Role of the CCG and Scope of this Report
- Customer Consultation
- Outcomes and Long Term Strategy
- Business Plan Costs, Risks and Rewards

He asked if the CCG were comfortable with the scope of what the report was trying to achieve;

The remit to comment upon the customer engagement process and the associated outcomes is therefore clear and is addressed accordingly within this report. The remit to provide comment on how well customer's views and priorities have been reflected within the Business Plan is less straightforward, and has been interpreted by the CCG according to the following criteria:

- The appropriateness of the Company's interpretation of customer priorities based on the engagement process and associated survey results.
- The clarity of the link between the customer priorities and the outcomes and ODIs that have been produced, and the degree of commitment offered by the incentives in terms of both measurability and, where appropriate, links to customers' willingness to pay.
- The extent to which the expenditure proposals and balance of risks presented within the Company's Business Plan reflect customer views and priorities.

Milo Purcell suggested including reference to the Acceptability Testing that will have been completed.

***Karen Gibbs joined the meeting***

Karen Gibbs commented that the Introduction read as if Ofwat had established the Group rather than Company. Doug Hunt agreed and will reword.

Doug Hunt suggested that In reviewing the adequacy of the customer engagement process, the CCG sought to address the following questions:

1. Is the nature and scope of the customer consultation appropriate to a company of Portsmouth Water's size and current favourable position in terms of bills, cost efficiency and the size of the statutory challenges that it is facing?
2. Have the engagement activities been carried out appropriately with adequate methods and sample sizes?
3. Is the interpretation of the process findings, as presented within the Business Plan, appropriate and reflective of customer wishes?

He asked if these were the questions the CCG were hoping to see.

Karen Gibbs commented that they should link customer research to the CCG report.

David Howarth suggested there being a 'golden thread' from Customer Preferences through to Company's Outcomes.

Karen Gibbs advised that there had been a lot of challenge in the Customer Research Sub Group which should be referred to as evidence.

Milo Purcell suggested including bullet points of the Company's initial customer priorities, summarising the work completed to date and then listing the final Outcomes explaining why some priorities were being included and some not. He further commended the Company for providing a lot of information very quickly.

Doug Hunt agreed that section 2 of the CCG report does need to include the early stages and clearly demonstrate how the Company reached the decisions they have made to date.

John Havenhand suggested rewording the paragraph 'The CCG provided challenge and input to each stage of the engagement process, as described below. Whilst the CCG was also presented with the proposed engagement strategy at an early stage, we note that there was less opportunity to challenge the strategy as a whole, as it was presented as a proposal rather than as options for consideration. This occurred largely as a result of the untried nature of the PR14 price review process rather than any failing on Portsmouth Water's part, but this point has been taken into consideration when presenting our final opinion on the adequacy of the customer engagement.' He feels that the wording suggests the challenge was inadequate which is not the case.

Doug Hunt commented that he felt the minutes of the Customer Research Sub Group suggested that there was not much challenge in the early stages but grew through the process, however, he agreed to rephrase.

Doug Hunt asked if the CCG was happy with how the Qualitative Research informed the Quantitative.

Karen Gibbs confirmed that she was comfortable as the Sub Group had the opportunity to meet MVA Consultants to review and challenge all the research proposals and materials.

Milo Purcell commented that he had early concerns as the process seemed to have a slow start, however, as the CCG and Company has grown in trust and confidence the engagement has developed. He also suggested changing the wording 'reasonable minimum' to 'proportionate' in the following paragraph within the CCG report 'In terms of the overall process, the CCG considers that Portsmouth Water has derived and implemented an adequate strategy, although

the approach taken represents a reasonable minimum given the expectations of the PR14 price review process’.

John Havenhand commented that the Qualitative Research should have had more involvement from the CCG Sub Group.

Milo Purcell suggested that this was as a result of Ofwat reducing the timescale.

David Guest commented that had the CCG not lost that month then they would have had more time to challenge to inform Qualitative Research.

David Howarth commented that the report needs to refer to the size of the Company.

Milo Purcell commented that the Company needs to demonstrate that it has reached the widest range of Customers. Confirmation that all demographic has been reached.

Doug Hunt advised that should be assured in the Peer Review. He noted that Nick Sheeran had circulated the Scope of the Peer Review to the CCG Sub Group for comments. Amy Denford circulated a hard copy of the Scope of the Peer Review for further consideration.

Karen Gibbs requested the Chair ask the Company for a copy of the Qualitative Research Final Report.

John Havenhand advised that from memory he thought Customers were asked if they would accept a reduction in service for a reduced bill and they said yes.

Doug Hunt commented that the CCG would need sight of the Final Report to determine. He also noted that the CCG had previously expressed concern over using WtP Surveys to rank preferences.

John Havenhand confirmed that was correct but need to refresh memory on how the process was carried out, e.g. when they introduced money into the ranking of preferences. Need to establish that first and then query.

Milo Purcell suggested the report say that the CCG had diverse opinions on WtP but as a whole had confidence that the Company used best practice, implemented it well and drew reasonable conclusions.

Doug Hunt advised the CCG that they need to address what has the Company has done to address affordability in the plan. He also reminded the CCG that at the beginning of process the Company was talking of positive bill increases but through research have been influenced by economic pressures and messages from Ofwat.

David Guest questioned where a bill increased by RPI comes from, is RPI for increase in staff costs?

John Havenhand commented that other factors impacting on the business will be increasing in cost e.g. energy costs, electricity will go up by more than RPI.

Milo Purcell advised that the Company cannot solely make decisions on customer's views; they have a responsibility to take a long term view, stewardship of their assets.

Derek Kimber advised that other Water Company's were looking at the future, driving metering and reducing leakage to reduce energy costs. Have the Customers been asked to think about the future. If electricity prices double the Company will only be able to absorb so much and will have to pass some on to Customers in the future.

Doug Hunt advised that the Company's energy costs are less than other Water Company's due to natural filtration and reduced treatment.

Doug Hunt feels comfortable that there has been sufficient challenge made on the Company's Outcomes. However, the CCG have not yet been presented with the final ODI's and will need to request these.

Doug Hunt confirmed that he would feedback to the Company those questions and with those answers as well as the comments made during the discussion would revise the CCG Report ahead of the next meeting.

DH

## 5. Feedback and Questions to Company following CCG Discussion

Following the CCG's Company exclusive discussion Doug Hunt posed the following questions to the Company on behalf of the CCG;

How does the Acceptability Testing fit in with the timing of the CCG Report?

Nick Sheeran advised that the Acceptability Testing is due for completion by the end of October and Results circulated to the Sub Group ahead of their meeting on 8 November 2013. These will then be discussed at the next full CCG Meeting on 12 November 2013. The Peer Review will also adhere to the same timetable.

Is the Company's decision that Customers do not want a reduction in service/bill's one that can be evidenced?

Nick Sheeran confirmed that the most recent research had covered this issue and would be reported on in MVA's forthcoming report.

Paul Barfoot advised that this question was specifically being asked as part of current further research that is being undertaken.

John Havenhand commented that he thought it was asked in the initial stages of the Research and Customers said they would be willing to accept a reduction in service and in turn their bill. Nick Sheeran confirmed that it was asked specifically in relation to the call centre not the business as a whole.

How did the Company decided that Customers Preference of Affordability is a bill increased within RPI? Why is that a fair interpretation of affordability?

Paul Barfoot confirmed that this was also being covered in the current further research.

Neville Smith advised that the Portsmouth Water bill was less than 0.5% of average household income. Added to that the level of deprivation in the Company's area is lower than the national average, therefore this bill shouldn't cause the Customer's affordability issues. However, this is being tested in current further research.

In respect of Leakage does the Company intend to have an incentive to award/penalise, linked to WtP?

Gareth Simmonds advised that the current further research is determining an up/downside for each Outcome. This will enable the Company to calibrate its Outcomes. The current further research is testing that the Company's Incentives reflect Customer's values and this will be presented on 8 November 2013 at the Sub Group Meeting.

David Howarth commented that there was a penalty for Per Capita Consumption (PCC).

Gareth Simmonds advised that the difficulty was in measuring it. Neville Smith added that there was so much variability it would be fairer to penalise.

Milo Purcell suggested approaching Incentives in a different way e.g. what percentage of turnover is at risk.

Gareth Simmonds confirmed that essentially that is what the Company's Outcomes/Incentives were.

Neville Smith confirmed that the Company will produce a variation – up/downside.

NS

When are the Company's Final ODI's & KPI's going to be presented to the CCG and be aligned with the Business Plan?

Gareth Simmonds confirmed that the ODI's had to follow the current further research and the KPI's would be available at the next CCG. The strength of the ODI's will also go to next meeting but the Company does not propose them to change.

GS

When will the narrative to accompany the Business Plan be given to CCG?

Gareth Simmonds confirmed that the key parts of the narrative can be extracted and provided to the CCG at the next meeting.

GS

Neville Smith advised that the Draft High Level Business Plan was almost complete and the Company would make available to the CCG as soon as possible.

NS

The CCG would like clarification on the Financeability Outcome and would like to understand the assumptions made. Neville Smith suggested providing CCG with a paper on assumptions & efficiencies and what the Company thinks the ratios will be and circulate as soon as possible.

NS

David Guest acknowledged that the Financeability of the Company was not within the CCG's remit; however, should there be a Determination not in line with Business Plan the CCG want to know what the impact on Customers might be at high level.

## 6. Red Flags for Business Plan/Ten Key Messages for Business Plan

Nick Sheeran detailed a number of issues which may attract a 'Red Flag' from Ofwat when they review the Company's Business Plan, and therefore impact whether the Plan is classed as 'Enhanced', 'Standard' or 'Resubmit', along with other key decisions to be made. He explained the reasons why the following items may attract 'Red Flags'

- Increased level of Capital Expenditure
- Inclusion of Farlington washwater recovery
- Leakage
- Non renegotiation of bank loan
- Cost of capital
- Retail uplift on prices
- SIM score – recent performance

Nick Sheeran circulated a paper highlighting the ten key messages which the Company will want to put across in their Business Plan. It should be noted that these are the initial drafts and may be subject to change.

The proposed "Ten Key Messages" are as follows:

- We will improve services but our prices will not increase by any more than inflation. We will achieve this through further improvements in efficiency

and innovation. This follows below inflation price increases every year from 2010.

- As a proportion of household income Portsmouth Water customers pay less for their water than they did 15 years ago. We are the cheapest supplier, by some margin, and one of the most efficient in the industry and we intend to maintain this.
- Customer engagement – we have listened to our customers and our stakeholders and have created our Plan to reflect their priorities and challenges. Engagement has been more detailed than ever before.
- The Board has shown it is committed to keeping bills down by giving up the benefit of rolling over the Opex efficiency achieved from 2010. This amounts to over £2m which we could have charged to customers in the first three years of AMP 6.
- Board Assurance – The Board, including the non-execs, has been involved in every aspect of the development of the Plan and has challenged the content of the plan, in detail, at every stage. The Board fully supports the proposed Plan.
- After very careful consideration the Board believes it is in the long term interest of customers to increase capital expenditure from that allowed at the last determination. This is partly due to new obligations and replacement of short term assets constructed in AMPs 3 & 4, but also reflects the cyclical nature of our maintenance.
- Leakage – recovery plan in place. Being paid for by shareholders, not customers.
- We are different from most other companies in the sector due to our ownership structure (EBT). This allows us to take the long term view.
- Portsmouth Water customers have benefitted from our reliable and resilient assets. We have not had a hosepipe ban since 1976.
- SIM performance – our performance in the Qualitative SIM score has consistently been in the top quartile. We have the lowest level of written complaints in the industry.

Douglas Kite questioned why environment was not amongst the ten key messages. Nick Sheeran agreed that it needed to be included.

NJS

## 7. Capex Update

Rod Porteous informed the CCG that Capital Expenditure may be a 'red flag' to Ofwat as proposing a large increase from £47m to £63m over the AMP period.

He advised that if the cost of new obligations and requirements were removed from Capex the increase would not then be material.

He confirmed that the Company had employed an Independent Cost Consultant and that the proposals had been subject to robust Board challenges.

He advised that the Consultant had identified Crypto and Farlington Schemes had excluded £3m worth of costs so Capex needed to be reviewed. Schemes submitted for DWI for following reasons;

- Deteriorating Water Quality



- Capital Maintenance Spend to Maintain Water Quality & Serviceability
- Capital Maintenance Nitrates/Oil Pollution

## 8. **DWI View on Company's Water Quality Risks**

Milo Purcell advised the CCG that the DWI had now written to the Company with decisions on their Submissions.

The Company put forward six submissions;

Lead Submission Supported

DOMs Strategy Commended

Resilience Commended – Consistent with guidance, however, DWI would like more attention to be given for telemetry failures.

Disinfection Strategy at 11 Water Treatment Work's Commended. Insufficient weighted evidence to give it a Legal Instrument, scheme commenced.

Eastergate and Westergate Schemes Both Declined to Support – DWI want to see robust validation of proposals, demonstrate benefit of each solution. (Subsequent to meeting support confirmed).

Feedback for next meeting.

**MP**

Doug Hunt asked for formal wording on this for inclusion in the CCG Report.

Milo Purcell advised that conclusions, challenges, would be available at the beginning of November and can provide CCG with draft report. The formal DWI letter can be appended to the CCG Report.

**MP**

David Howarth advised that the Environment Agency are preparing a report on the Company's Business Plan which will be sent to the Company this month for comments, this could also be appended to the CCG Report.

**DH**

## 9. **Customer Preferences**

Nick Sheeran circulated a paper detailing Customer Preferences and how they have informed the Company's Outcomes.

He explained that the table within the paper mapped out the key messages which have been forthcoming from the Company's Customer and Stakeholder engagement and how these have been translated into the Outcomes or 'Commitments' set out in our Draft Business Plan.

As there was quite a lot of detail for the CCG to digest it was agreed that the paper would be circulated with the minutes of the meeting for the CCG to consider and challenge at a later stage.

**AD/CCG**

## 10. **Any Other Business**

### **Update on Customer Research & Peer Review**

Nick Sheeran advised that both results were due by 31 October 2013 and confirmed that good progress was being made. The meeting of the Sub Group would be held on 8 November 2013 and Doug Hunt and David Guest had been invited.

**Annual Corporate Water Risk Conference**

Richard Harris advised the CCG of an Annual Corporate Water Risk Conference being held next year that may be of interest. Amy Denford agreed to circulate the details to the CCG.

**Other**

Jon Stuart emailed the Secretary ahead of the meeting to ask for the Company's 'take' on Ofwat plans to block the proposed Thames Water price rise. Neville Smith confirmed that Company had no comment to make.

He also asked for the Company's view on the possible impact of the failing of Smartsorce Water. Paul Barfoot advised the CCG that Smartsorce Water were a Company who administered water bills on behalf of Customers who had recently gone into liquidation. He confirmed that the Company only had 11 Smartsorce Water Customer's, none of which owed any money to the Company. Paul Barfoot confirmed he would formally reply to Jon Stuart.

**PAB**

**PORTSMOUTH WATER Ltd  
CUSTOMER CHALLENGE GROUP (CCG)  
MEETING HELD ON TUESDAY 12 NOVEMBER 2013**

**PRESENT:** Paul Barfoot (Portsmouth Water) In Part, Heather Benjamin (Portsmouth Water) In Part, Charles Burns (FSB), Amy Denford (Secretary), David Guest (Independent Chairman), John Havenhand (Consumer Council for Water), David Howarth (Environment Agency), Douglas Hunt (Atkins Independent Reporter), Derek Kimber (Gosport Borough Council), Mike Kirk (Portsmouth Water) In Part, Terry Lazenby (Portsmouth Water) In Part, Chris Manning (South Downs), Simon Oakley (Chichester District Council), Kirk Phillips (Winchester City Council), Rod Porteous (Portsmouth Water) In Part, Milo Purcell (Drinking Water Inspectorate) In Part, Nick Sheeran (Portsmouth Water) In Part, Gareth Simmonds (Portsmouth Water) In Part and Neville Smith (Portsmouth Water) In Part.

**Action**

**1. Apologies:**

Traci Baker (Hampshire Chambers of Commerce), Hugh Caley (Carillion), Daire Casey (West Sussex County Council), David Collins (Havant Borough Council), Cllr Paul Dendle (Arun District Council), Keith Evans (Fareham Borough Council), Karen Gibbs (Consumer Council for Water), Richard Harris (West Sussex Hospitals Trust), Marge Harvey (East Hampshire District Council), Douglas Kite (Natural England), Ian Rawson (KWS -Defence) Tim Richings, Jon Stuart (Havant & District Citizens Advice Bureau) and Rob Wood (Portsmouth City Council)

**2. Minutes & Actions of Meeting Held on 22 October 2013**

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

The following actions were reported on:

**CCG Discussions on the Draft Business Plan and CCG Report**

Doug Hunt confirmed that he had issued a revised version of the CCG Report following the points raised at the last meeting.

**Feedback and Questions to Company following CCG Discussion**

Neville Smith confirmed that the Company have produced a variation – up/downside on Outcomes and Incentives that will be discussed later in the meeting.

Gareth Simmonds confirmed that the ODI's and KPI's would be provided later in the meeting.

Gareth Simmonds confirmed that the key parts of the narrative had been extracted and will be provided to the CCG later in the meeting.

Neville Smith advised that the Draft High Level Business Plan had been issued to the CCG ahead of the meeting and a copy was also included for information in with their papers for the meeting.

Neville Smith confirmed that there would be an update on financeability later in the meeting.

**Red Flags for Business Plan/Ten Key Messages for Business Plan**

It was noted that there was an inaccuracy in the minutes of the meeting held on 22 October 2013 and it was Douglas Kite not Derek Kimber who questioned

why environment was not amongst the ten key messages. The Secretary agreed to amend this.

Nick Sheeran confirmed that environment had been included in the ten key messages.

### **DWI View on Company's Water Quality Risks**

At the last meeting Milo Purcell advised that the DWI declined to support both the Eastergate and Westergate Schemes requesting sight of robust validation of proposals and for the Company to demonstrate the benefit of each solution. Neville Smith advised that since that meeting the DWI has confirmed their support of these Schemes.

David Howarth advised that the Environment Agency had sent their report on the Company's Business Plan. Neville Smith confirmed that the Company had also responded to the Environment Agency.

### **Customer Preferences**

Nick Sheeran confirmed that his paper detailing Customer Preferences and how they have informed the Company's Outcomes was circulated with the minutes of the last meeting for the CCG to consider.

Paul Barfoot confirmed that he had formally replied to Jon Stuart regarding his question regarding the failure of Smartsources.

## **3. Technical Assurance**

Doug Hunt circulated an updated Technical Note providing a summary of the current findings of the assurance process that Atkins has undertaken for Portsmouth Water's PR14 Business Plan submission.

Doug Hunt provided the CCG with technical assurance on the Company's Cost Efficiency.

Simon Oakley asked if staff costs were included.

Doug Hunt confirmed that staff costs were included in Operational Cost Efficiency, however, he clarified that the technical assurance he was currently providing was in respect of Capital Cost Efficiency. He added that in terms of challenge the Company's Operating Cost Efficiency was 'bullet proof'. In PR09 Ofwat classed them as the most efficient in the Industry, they have outperformed during that period and are using that outperformance to keep bills down by 7% and passing those efficiencies onto their Customers which they don't have to.

Kirk Phillips questioned if the CCG are expected to take a view on the Company's Capital Cost Efficiency within their Report to Ofwat.

Doug Hunt advised that he was unsure if it was within their remit. However, the challenge to make is on whether the Company's proposals on Capital Cost Efficiency sufficient or could they cut costs.

John Havenhand commented that from Doug Hunts Technical Note he concluded that there did not seem to be a lot of scope to cut costs.

Doug Hunt confirmed that was right, if the Plan is refused the Company would need to refinance or cut Capital Maintenance.

John Havenhand commented that to cut costs now would build problems for the future.

David Howarth commented that the Customer Research highlighted Customers were happy for bills to increase. Ofwat instigated this Engagement Process and advised Company's to listen to their Customers and therefore Ofwat intervening and not allowing Company's to increase their bills could make a mockery of the whole process.

Simon Oakley asked if during the research Customers were informed that they could expect a continual improvement / maintenance of assets in return for a bill increasing by RPI?

Doug Hunt confirmed that yes; bills will be inline with inflation and will finance capital expenditure.

John Havenhand asked for the word 'assumed' to be removed from the following sentence within the Technical Note; 'This has implications when the results are being used to rank preferences according to 'willingness to pay', as higher cost items with a larger benefit can usually be *assumed* to tend to attract a higher WTP.' He commented that any views / reports should be based on facts not assumptions. Doug Hunt agreed he would reword this.

DH

Doug Hunt advised that his Technical Assurance Notes will form part of the CCG Report.

Milo Purcell commented that Ofwat had changed their methodology on how it measures Opex and Capex. The new model is trying to bring the two together to alter the balance and the way the Company allocates work to Opex/Capex. He asked Doug if this change has resulted in the Company changing their approach to activities. He advised that he doesn't believe it has but thinks totex has introduced uncertainty.

Doug Hunt advised that the only change made was in respect of Metering. The Company now included this within Capital Costs and agreed that Totex has introduced a big uncertainty. He explained that Totex has exceptional items to strip out which can cause problems because if they are not accepted by Ofwat this could drastically change the Company's position.

David Guest agreed but advised that it was outside the remit of the CCG and would be up to Ofwat to decide

Doug Hunt suggested commenting on this within the CCG Report.

Milo Purcell asked if the Company's Technical Programme is aligned with that of the long term.

Doug Hunt confirmed that yes; their proposal is inline with the long-term modeling and will include a clear statement to that effect in the Report.

#### ***NJS and PAB joined the Meeting***

#### **4. Customer Research Sub-Group Feedback**

Doug Hunt circulated a Technical Note following the Sub-Group meeting held on the 8 November 2013.

#### **Peer Review**

Doug Hunt advised that the Peer Review Report by Accent was discussed at the Sub-Group meeting and it was generally agreed that it supported the

approach and methods that have been adopted by MVA. He explained that this was expected as the Company had generally used methodologies that are currently used as standard within the Water Industry.

John Havenhand commented that inaccuracy comes in when research is used to inform incentives, rewards/penalties.

Nick Sheeran confirmed that Ofwat expects the Company to do just that. John Havenhand advised that if that was what Ofwat wanted he didn't have a problem with it.

Kirk Phillips commented that he did not feel it necessary to include the Accent Report as an appendix in CCG Report. He thought it would be sufficient to just note in the Report that it had been completed.

Nick Sheeran advised that it would be included within the Business Plan Appendices for the CCG to refer to. Also included in the Appendices will be MVA's response to Accents Peer Review.

John Havenhand advised that he was reassured that Accent found the same uncertainties with MVA's Research as the Sub-Group.

Doug Hunt advised that he disagreed with Accents' Conclusion, although it may be academically correct, in terms of finding out customers' views the research was acceptable.

John Havenhand agreed that you Shouldn't always follow the science but use judgement.

### **Acceptability Testing**

Doug Hunt advised that the Acceptability Testing results were overwhelmingly high and highlighted that almost all Domestic Customers consider the Company's Draft Business Plan to be acceptable in its entirety, as do the vast majority of Business Customers.

Milo Purcell commented that the results of the Acceptability Testing make it difficult for Ofwat to challenge.

### **Outcomes**

Doug Hunt advised that the Sub-group challenged MVA's Methodology on Outcomes and asked the Company to provide further information in relation to the following two questions:

1. Does the research provide support for the inclusion of the monetary outcome delivery incentives (ODIs) that are being proposed?
2. Can the Company justify the level of financial rewards that are being proposed based on this research?

Nick Sheeran advised that MVA had responded and he will circulate later in the meeting.

John Havenhand requested wording be put in the CCG Report that the Methodology was agreed and results needed to be taken with caution.

Kirk Phillips thought the word caution was too heavy and asked for 'a degree' of caution to be included along with a statement commending the Company's effort and innovation.

Doug Hunt suggested including a statement that confirms that whatever

proposals there were to come up with methodology it has been acceptability tested to a high standard and therefore the only challenge left is how it is translated into Incentives.

Nick Sheeran advised that the research highlighted that Customers do believe the Company should have penalties/rewards for under/over performance.

Milo Purcell expressed that he was anxious bringing together the testing of Outcomes and developing Incentives. Does not want the CCG's confidence in the Company's Outcomes to be undermined. CCG Report needs a strong statement to say there is evidence that Customers support Outcomes but its just the matter of the Company's performance in delivering Outcomes.

Paul Barfoot advised that there will be an item on Incentives later in the meeting for them to challenge.

### ***NJS and PAB left the Meeting***

## **5 - 6 CCG Draft Report & Discussions on the Draft Business Plan**

Doug Hunt issued the latest version of the Draft CCG Report for comments. He took the CCG through the Report section by section and highlighted key items.

He advised that he would add development of incentives to the bullet points within Section 2.2.

Kirk Phillips questioned if Customers were asked to comment on Incentives.

Doug Hunt was unsure and confirmed that it was something Ofwat asked for. He advised that there was an item on Incentives later in the meeting and it may come to light then.

Doug Hunt was of the opinion that the CCG didn't seem confident in WtP and asked if this should be commented on within Section 2.3 of the Report?

David Howarth expressed that he didn't feel qualified to make such a criticism.

John Havenhand commented that although not qualified they could recognise that the Company followed good practice nevertheless judgement needs to be made.

Chris Manning advised that the Accent Report highlighted WtP was difficult and didn't have any better ideas. Therefore the research MVA completed is as good as we can expect.

David Howarth commented that the Peer Review has therefore done the job that CCG are not qualified to do.

Doug Hunt advised that he will include in the Report that the Peer Review didn't have any better ideas.

Doug Hunt raised an issue that came out of the Sub-Group about the Acceptability Testing including leading questions. He informed the CCG that the Company first informed Customers that they had the lowest bills in England and Wales before asking if they found a bill only increasing by inflation acceptable.

John Havenhand confirmed that the Sub-Group did challenge this but were satisfied with the Company's response that Customers need to be informed to be able to answer.

Simon Oakley asked what the RPI increase was going to be spent on.

Doug Hunt advised that the Business Plan is put together in real cost terms. Therefore, RPI is to allow for future cost increases on what they have to pay for e.g. wages, construction, power.

Kirk Phillips commented that RPI can also be negative so should it say the bill will be plus or minus RPI.

Doug Hunt advised that Customers will effectively be getting a bill with a hedge against inflation input costs.

Doug Hunt confirmed that he would add some more to Section 2.4.2 on the challenge made on RPI.

David Howarth expressed concern that the Research seems to disconnect from the Company's proposals. He commented that the Research highlighted Customers were willing to have an increase in bills for improvement. However, the affordability priority is that the Company only increasing bills at a rate no higher than RPI. Where's the link, 'golden thread'?

Doug Hunt advised that there is inherent tension between WtP/Preferences and has commented on this within Section 2.4.2 of the Report as follows;

'On the face of it this would appear to indicate the Portsmouth has not proposed a Business Plan that is in line with customer preferences, as greater improvements could have been proposed in areas such as leakage whilst maintaining bill increases to within the amounts that were allowed for in the aggregate WTP. However, it is clear from the evidence that the Company presented to the CCG that the need to ensure asset stewardship (in the form of some increases in non-infrastructure capital maintenance costs) and meet statutory obligations meant that only modest service measures improvements could be considered without rises in bills beyond RPI inflation. This meant that there was an inherent conflict between the aggregate results of the WTP studies and the interpretation of the affordability priority. The CCG therefore has some differing opinions on this point, which are highlighted below in relation to the interpretation of leakage and water efficiency preferences.'

David Howarth reiterated his concern and commented that he felt the Company were listening to Ofwat rather than what the Customer wants.

John Havenhand agrees but commends the Company in using their judgement not to increase Customer bills. He confirmed that the Acceptability Testing shows that Company got it right.

Doug Hunt summarised that the Company made a judgement call and has come up with a Plan that is acceptable to their Customers.

Charles Burns asked if the CCG should include in their Report that they accept a bill with an increase no greater than RPI but hope it to be less.

Doug Hunt advised that if the Company outperform they will give this back to their Customer.

Simon Oakley asked if there should be a comment in their Report regarding the use of RPI and noting that it is an unstable measure of income.

Doug Hunt advised that it was not within the CCG's remit to challenge Ofwat's measuring mechanism. However, challenge can be made on efficiencies and he will make that clear in their Report.



Doug Hunt enquired if the CCG were satisfied with the leakage preference.

David Howarth commented that they can't blame the Company for position/decision made.

John Havenhand suggested adding the wording 'Company's judgement' as it was the research informing the decision as opposed to direct link.

Doug Hunt asked if the CCG were happy with the Company's interpretation of Customer priorities

- Leakage
- Water Softening
- Water Efficiency
- Metering

Potential service measures improvements relating to customer contacts, hosepipe bans, interruptions to supply and enhanced cross-subsidies to vulnerable customers were found to be of a lower priority within the stated preference surveys, so enhancements to these service measures were not considered to be a customer preference.

David Guest asked for clarification on where social tariffs for vulnerable Customers were included in the Business Plan. Doug Hunt noted to ask the Company.

Doug Hunt advised that he didn't think there were any areas of concern outstanding in Section 3 and asked for the CCG's consensus that it would be closed off as agreed. The CCG were in agreement.

Doug Hunt commented that the only outstanding item is for the Company to provide final KPI's and ODI's and he would ask the Company for those later in the meeting.

David Howarth commented that the two Outcomes on being attractive to Investors and Health and Safety were not generated from Customer Engagement. They were driven by Stakeholders and the Company. He noted that they were both valid and good but suggested it would be worth noting in the Report that the CCG are supportive of these even though they had not arisen from Customers, in case Ofwat challenge them.

Doug Hunt advised that the CCG had broadly agreed the scope for Section 4 and it would include high level Assurance taken from Atkins Technical Assurance Notes.

Doug Hunt asked David Howarth and Milo Purcell if the EA and DWI Letters could be summarised in Section 4.2.2 and appended to the Report. They both confirmed that this would be acceptable.

Doug Hunt advised that the Capital Programme proposed is essentially to maintain service levels as they are for AMP6 inline with Incentives. He asked the CCG if he could confirm they are happy with this and he would comment on in Section 4.2.1, the CCG confirmed they found this acceptable.

David Howarth raised concern over Section 4.2.3 on Affordability and Value for money commenting that he felt uncomfortable and that it was outside the remit of the CCG. He advised that the CCG can confirm from the Research and evidence provided by the Company that Customers view it as value for money.

Doug Hunt noted that he needed to include in Section 4.3.1 Milo Purcell's earlier statement that the five year Plan aligns to the long term view.

Doug Hunt asked if the CCG felt they had received enough information to complete Section 4.3.2 on Balancing Risk.

David Guest commented that the Company advise they do have a Risk Register in place.

Kirk Phillips suggested asking the Company for a copy.

Milo Purcell advised that the Company have discussed Risks with the CCG indirectly in respects of water quality, water resources and operational issues. He feels the CCG have sufficient evidence to say they have interacted with the Company on Risk during the Engagement Process. He suggested a comment be made in the Report that the CCG explored and challenged risks throughout the process.

Simon Oakley suggested noting in the Report that RPI is a risk.

Doug Hunt advised that if the Company start to encounter risks as a result of RPI they could approach Ofwat to change mechanism. He also commented that the Business Plan itself is a risk process.

***Milo Purcell left the meeting.***

***Portsmouth Water Representatives joined the meeting: Paul Barfoot, Heather Benjamin, Mike Kirk, Terry Lazenby, Nick Sheeran, Gareth Simmonds and Neville Smith***

## 7. Update on Financeability

Nick Sheeran circulated a paper updating the CCG on financeability and providing clarification on the assumptions made.

Doug Hunt questioned the efficiency being 1.85% in year two. Nick Sheeran explained that was coming off the Company's computer mainframe currently costing £400k per annum. He advised that they only put some of the saving through due to potential risks and cost of new systems.

John Havenhand asked what the implication of the Cost of Capital being higher than Ofwat expected.

Nick Sheeran confirmed that as previously advised it could be potential red flag with Ofwat but the Company feels they are telling Ofwat a good story regarding Cost of Capital, e.g. possible refinancing and not taking legacy efficiencies from previous AMP.

John Havenhand asked what if Ofwat don't agree, what's the Plan B?

Neville Smith confirmed it would result in a reduced service and Nick Sheeran added the Company would have to cut Capex.

## 8. Incentives / Penalties / Values

Gareth Simmonds circulated a paper on the Company's Financial Incentives. He advised that the Company decided the following Outcomes would have incentives;

Leakage  
Water Efficiency  
WFD

David Howarth raised concern that expressing leakage as a percentage was unfair as influenced by other components of water balance e.g. large

Customers.

Gareth Simmonds confirmed the Company can translate the percentage to an absolute target as the percentage was just used as part of the WtP exercise.

John Havenhand asked if these financial rewards / penalties were really an incentive.

Gareth Simmonds agreed they were relatively small amounts, however, Ofwat outline what should be financial or reputational incentives. These financial areas are those customers have prioritised.

Neville Smith advised that the penalty doesn't necessarily drive the Company but the reputational the same as SIM.

David Howarth highlighted the water efficiency incentive had no reward.

Gareth Simmonds commented that it was difficult to measure accurately and therefore the Company didn't feel comfortable having a reward on that basis. The incentive again is reputational.

Simon Oakley asked who will be measuring these.

Gareth Simmonds confirmed that the Company Self Report and External Assurance is provided to the Board.

## **9. Outstanding Actions for Company and CCG**

Doug Hunt raised the following outstanding questions that CCG had for the Company to enable them to complete their Report.

How are social tariffs for vulnerable Customers included in the Business Plan?

Paul Barfoot advised that the Company are currently looking at and plan to follow Southern Water's model being piloted from 1 October. The Company feels it's important that Customers can save on both bills through one application.

David Guest asked if the Company can give the CCG comfort that risks have been evaluated.

Neville Smith advised that it doesn't expect anything to arise, however, should a new obligation arise the Company can get approval to get an increase. If Ofwat want to reduce Cost of Capital because of embedded debt the Company may be at risk. However, there is a Sustainable effect clause in licence that could be exercised.

David Guest commented that the CCG had not been privy to mitigation plans.

Neville Smith reassured the CCG that the Company does have Risk Registers, Risk Assessments and Emergency Plans.

David Guest advised that CCG had discussed this but decided how the Company mitigates risk was not within their remit.

Simon Oakley commented that RPI poses a risk.

Neville Smith agreed that if RPI became negative it would cause problems if it continued.

Nick Sheeran circulated MVA's response to the Sub-Groups challenge as promised earlier in the meeting.

**Timetable**

Doug Hunt informed the CCG that he planned to send the Final Draft CCG Report to Members by Monday 18 November 2013. He would allow one week for Members to make comments/representations and an additional week to finalise the Report and add the relevant appendices ready for submission to Ofwat on 2 December along with the Company's Business Plan.

Terry Lazenby on behalf of Board thanked the CCG for their input and felt the Company had a better Business Plan for it.

David Guest also thanked the Company for cooperation and information aiding the CCG throughout the process.

Neville Smith advised the CCG that a revised version of the High Level Business Plan was included with their papers for information.

**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), Chris Manning (South Downs), Simon Oakley (Chichester District Council), Milo Purcel (Drinking Water Inspectorate) and Ian Rawson (KWS Defence)

**In Part for Portsmouth Water:** Terry Lazenby, Rod Porteous, Nick Sheeran and Neville Smith

**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), Jon Stuart (Havant & District Citizens Advice Bureau), Stuart Wedgbury (East Hampshire District Council & Havant Borough Council) and Cllr Rod Wood (Portsmouth City Council)

**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.

Doug Hunt then reminded the CCG that their purpose was to report to Ofwat on how customer engagement had informed preparation of the Business Plan. He commented that the CCG needs to consider the evidence based content of the Business Plan and what further research evidence they would seek other than pure technical issues.

Doug Hunt confirmed that he would write a Report Structure that reflects question and challenge at high and low level.

Karen Gibbs commented that this was a valuable session for the CCG to take stock of where the Company and CCG have got in the process, the quality of the Customer engagement and how well the output has been used. Now the WRMP has been published the CCG have a better idea of what the Company will include in their Plan. The CCG needs to consider whether they can confidently say that the Customer Research follows through to the Business Plan.

David Guest commented that the CCG needs to decide if they feel the outcomes truly reflect what the Customer wants. John Havenhand agreed that Ofwat have put more emphasis on Companies producing Business Plans based on what customers want.

Richard Harris suggested that the Report should indicate what the CCG had challenged. He recommended that the Business Plan sections be reviewed by sub-groups and challenge any particular issues of concern.

Simon Oakley reiterated his earlier concern about pay increases and commented how the Company seemed uncomfortable to discuss the topic. Doug Hunt restated Neville Smith's earlier comment that pay forms part of the Company's operational costs and therefore to challenge pay the CCG would need to challenge the

Company's efficiencies.

David Howarth raised concern that CCG Members should be expressing the views of the Customer who they are representing not the Industry they work in.

Ian Rawson suggested framing this forthcoming AMP with some history on how the Company delivered on promises from previous AMP period and what their long term view is beyond the next 5 year period. An unpredictable 5 year plan makes things difficult for Business Customers.

Karen Gibbs commented that it is the Company's responsibility to produce a high quality Business Plan. The CCG are in an informed position to challenge the Business Plan. Report should demonstrate the challenges made and how they had changed the Company's Plan.

Milo Purcel highlighted that the CCG needs to understand how the Report will be used by Ofwat. The report only forms one part of Ofwat's risk based assessment and it will be used relatively early in the process to inform the level of scrutiny and acceptance that they apply. The CCG cannot do Ofwat's job for them, they can only comment on principles of customer engagement at a very high level. The CCG needs to record every challenge made and the differences it has made in an evidence-based Report.

John Havenhand commented that the CCG has challenged the process all the way through not just the Final Plan. The CCG have also witnessed that the Company has been engaging with its Customers. He further added that the CCG should be challenging all operational costs not singling out one area.

Leslie Keeble suggested there be a section in the Report on metering.

Ian Rawson recommended a section on innovation and how the Company has bought that to the Business Plan. Has the Company given a lot of thought on how to improve?

Doug Hunt confirmed that based on the above discussions, he would provide a note on the proposed structure of the Report and circulate it to the CCG for comment.

**DH**

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**

**PORTSMOUTH WATER Ltd**  
**CUSTOMER CHALLENGE GROUP (CCG)**  
**MEETING HELD ON THURSDAY 15 AUGUST 2013**

**PRESENT:** Charles Burns (FSB), Daire Casey (West Sussex County Council), Amy Denford (Secretary), Keith Evans (Fareham Borough Council), Karen Gibbs (Consumer Council for Water), David Guest (Independent Chairman), John Havenhand (Consumer Council for Water), Douglas Hunt (Atkins Independent Reporter), Douglas Kite (Natural England), Simon Oakley (Chichester District Council) and Milo Purcell (Drinking Water Inspectorate)

**Action**

**Apologies**

Apologies were received from Traci Baker (Hampshire Chambers of Commerce), Jim Barker (Environment Agency), Andrew Day (Ofwat), Cllr Paul Dendle (Arun District Council), Hugh Caley (Carillion), David Collins (Havant Borough Council), Richard Harris (West Sussex Hospitals Trust), Cllr Derek Kimber (Gosport Borough Council), Chris Manning (South Downs) Cllr Kirk Phillips (Winchester City Council), Ian Rawson (KWS (Defence), Tim Richings (South Downs), Jon Stuart (Havant & District Citizens Advice Bureau) and Cllr Rod Wood (Portsmouth City Council)

**1. Customer Challenge Group Confidential Discussion**

David Guest opened the discussion. He expressed surprise with the amount of financial information offered by the Company. He noted that other companies are not being interrogated as much. He felt that the CCG were not qualified to challenge figures just the process.

Douglas Kite commented that it was good to have the costs so the CCG can provide a more forceful challenge. He raised concern that some costs were not provided e.g. Company state they will manage leakage but don't include a cost.

Doug Hunt explained that the infrastructure model is uncertain about the impacts of mains renewals on leakage and in reality the CCG shouldn't be concerned as there is relatively little evidence that it will rise as a result of the mains renewals that are proposed. The proposed renewal programme appears reasonable given the existing burst rates, indicating a manageable level of risk. As a general comment, the impact of mains renewal on leakage is nearly always marginal for any water company.

Simon Oakley asked if the balance between minimising burst and leakage is reflected in costs. The Company's view is that it's manageable but is it the Customer's view that it is reasonable?

Doug Hunt confirmed that the Company's approach and level of investment are reasonable, and are unlikely to result in unacceptable risks to consumer supply in the longer term. Current improvements in targeting renewal activities may even continue to slightly decrease mains bursts in the shorter term, being designed to prevent adverse impacts from leakage and mains renewal activities.

Douglas Kite commented that water is relatively cheap to provide, with energy being the biggest cost involved is supply. He was therefore surprised that the Company did not mention that per-capita consumption, water efficiency would reduce costs. Reducing water consumption reduces risk.

David Guest advised that the CCG should challenge whether enough is being done on this.

Doug Hunt explained the main reason why the Company is behind in this area is that unlike some other companies in the South East, Portsmouth Water has ample water supply sources.

Douglas Kite questioned on that basis whether the Company cares about its reputation in promoting water efficiency.

Milo Purcell agreed that this would be a good point on which to challenge the Company, by questioning what the Company can do to proactively reduce leakage and promote water efficiency. He added that the Company not incentivised as the Regulator enforces an economic level of leakage; rather than one that is specifically based on reputation or perception. He noted that water quality elements had not been reflected in the mains renewals proposals and that this should also be challenged.

Milo Purcell noted that the UV Plants that the Company is proposing due to cryptosporidium risks at two of its boreholes are relatively low-cost compared to amount of money that was spent on water quality in PR09.

Simon Oakley raised concerns about the proportion of 'base opex' that will be spent on internal manpower cost. He considered that Pension and Salary costs, as well as wages need to be challenged; they should reflect what is happening in the rest of society e.g. not simply linked to RPI.

David Guest agreed that the CCG should challenge these issues further.

Milo Purcell commented that important decisions have been made by the company in respect of Gearing - the Debt element risk to Customer and Equity risk to Shareholder. This may be outside the CCG's remit; however, it was agreed that the CCG did need to better understand the general impacts of decisions on customers and the risks that this might place on customer future bills.

The challenge would be that the CCG recognises the significance of these elements, asking the Company to explain/justify the impact on Customers bills and future risks. The intention would not to challenge the financial aspects, but to obtain comfort that these decisions are taken in the best interests of both the Company and its customers.

Doug Hunt advised that Gearing may change following Ofwat's decisions on acceptable financial performance, and this could add to bills. This could have implications on affordability acceptance testing before Ofwat makes those decisions. Karen Gibbs noted that this was to be expected, but CCW also anticipated that further acceptability testing would be carried out if bill impacts change as a result of Ofwat's review of the Company Business Plan.



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

**PRESENT:** 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), Chris Manning (South Downs), Milo Purcell (Drinking Water Inspectorate), Kirk Phillips (Winchester City Council) and Jon Stuart (Havant & District Citizens Advice Bureau)

**Action**

**Apologies**

Apologies were received from Traci Baker (Hampshire Chambers of Commerce), Jim Barker (Environment Agency), Hugh Caley (Carillion), Daire Casey (West Sussex County Council), David Collins (Havant Borough Council), 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)

**1. Customer Challenge Group Confidential Discussion**

Doug Hunt drew the Groups attention to the outline report he had prepared and circulated ahead of the meeting.

David Guest advised that he had discussed the outline report with the other CCG Chairs and was satisfied with the proposed content and structure and that it was inline with other Water Companies. He asked the CCG Members to agree the outline report.

David Howarth commented that it was a good aim for all the CCG members to agree the report however, expressed concern that all members are from different backgrounds and therefore full agreement may not be achievable and a degree of compromise may be required.

Kirk Phillips questioned whether each Member of the CCG needed to have the report approved by the Customer they were representing e.g. Councils.

David Guest confirmed that each member as a representative of that Customer Group had the individual responsibility to approve the report.

Doug Hunt advised that the outline report included questions to get the CCG thinking and wanted their feedback on whether certain aspects were considered within their remit and what they wanted to include. Overall were the CCG happy with structure of the report?

Doug Hunt then took the CCG through the outline section by section requesting feedback as the meeting progressed.

Doug Hunt questioned if the CCG were comfortable that a clear picture of customer preferences can be drawn from the work that has been carried out to date? If not, then what else is required?

David Howarth commented that the CCG will be in a better position to answer once the Peer Review had been completed.

Karen Gibbs agreed and that the Acceptability Testing will also aid the CCG in answering this.

Jon Stuart raised concerns that earlier in the process vulnerable customers were

discussed; however, he doesn't think they are included in the draft Business Plan and feels the Company's approach in this regard needs to be stated in the Plan.

David Guest clarified that the Company need to detail their approach to Social Tariffs in their Business Plan.

Derek Kimber commented that following MVA Consultants earlier presentation he felt the Customer Research was aimed at justifying a price increase. Unsure why the Company were asking Customers if they were willing to pay (WtP) for improvements, felt the Company should have been asking would Customers be satisfied with their approach/improvement.

David Guest reminded the CCG that the Company were not looking to increase bills and that their draft Business Plan was for bills to remain the same and only increase by inflation.

Keith Evans commented that the Company seemed to be embarrassed to spend money on investment and increase bills.

Doug Hunt advised that the reason bills were low was due to the advantageous set up of the Springs and the South Downs, which inherently reduces operational and maintenance costs. This, along with the flexible, low cost structure of the Company's operations allows it to be more efficient than other water companies. He confirmed that it was not as a result of the Company's approach to Capital Maintenance being worse than other Water Companies.

David Howarth would like to find out from the Company if during the Research Customers were asked if they would like a reduction in bills for a reduction in service? He also questioned what the Customer viewed as affordable bills? Does the Company's proposal of bills increased by inflation reflect Customers views?

Karen Gibbs advised that the CCG would have the opportunity to challenge later in the full meeting during the item on Efficiency.

Milo Purcell informed the CCG that Ofwat made comment on windfall gains, and can expect to see something returned to Consumers. The Company need to demonstrate that it hasn't made windfalls gains or that it has made returns to consumers.

David Howarth questioned whether the Company has shown Customers the impact of inflation on bills during the WtP Research.

Karen Gibbs advised that would be included as part of the Acceptability Testing.

Doug Hunt clarified that the costs used in the WtP were fairly nominal, and in some cases actually showed that customers are not willing to support the actual costs that would be required for some of the improvements that were being surveyed (e.g. leakage and softening improvements would cost significantly more than the WtP that customers demonstrated).

Chris Manning questioned whether the CCG has confidence in the Company correctly assessing the Customers priorities or does it have confidence in the Company coming up with cost/WtP? If confidence is in the priorities, then the actual values elicited from the WtP are irrelevant.

John Havenhand advised that the Peer Review will help asses if the Customer Research Results were interpreted correctly and the priorities accurately reflect the Customers views.

Chris Manning questioned if there could be a further test to go back to Customers?

Karen Gibbs commented that there needs to be a balance as some Customers want certain improvements and others do not.

David Guest commented that the Company has to make the ultimate decision on Customer priorities and the CCG need to review the Company's proposals and question why.

Milo Purcell commented that he feels that the draft Business Plan is pitched about right and is consistent with evidence from Consumers. He suggested taking the Company's Outcomes/Commitments and putting them into context. Removing them as Customer preferences by putting them in context and justifying why the Company has proposed such.

Doug Hunt highlighted three areas where the CCG needed to be comfortable with the Company position, as the Company decisions have involved quite a lot of interpretation of customer preferences. These were; leakage, which had been interpreted as meaning that the ELL will be met, water softening, which was only going to be on a customer information approach, and affordability which assumed that RPI bill increases would be acceptable.

Milo Purcell felt that the area of bills was covered quite well in research. Leakage and water softening needed specific arguments and options to go forward. He felt there was a general consensus from the CCG on the Company's position. However, advice and support on water efficiency was not really covered.

John Havenhand recommended removing the wording WtP from the Business Plan and replace with stated preference.

#### ***Keith Evans left the Meeting***

Doug Hunt asked if the CCG felt the Engagement process had been effective.

Jon Stuart commented that during the early stage of the process the CCG members were invited to observe at Customer Research sessions. He suggested they should also have the opportunity to be present during the proposed further research.

#### ***Kirk Phillips left the Meeting***

Doug Hunt asked what the CCG would like to include in the report under Customer Consultation. Are the CCG just stating that it is satisfied or does evidence need to be provided?

David Howarth commented that the CCG needs to question if the Company has adequately consulted with its Customers and have they taken their views into account?

Milo Purcell commented that there needs to be an external technical review as the CCG can only be satisfied that issues such as sample size are adequate via Peer Review and they need to ensure engagement has reached all Customer spectrums. Essentially the report would need to identify whether the CCG considered that the Company had done enough to be consistent with reasonable expectations of a water company of their size.

Doug Hunt asked whether the CCG felt the Consultation was comprehensive.

Derek Kimber advised that the CCG need to set the parameters for the Peer Review. He suggested that Company are asked to involve the CCG when writing the brief / structure.

Chris Manning suggested that the results of the research from specific Focus Groups could be cross checked by doing a wider consultation.

Karen Gibbs commented that the draft Business Plan that was tabled at the meeting earlier was going out for Consultation in October. The issue of wider

consultation was one area where she considered that the Company were playing 'catch up' with others in the industry, and that this process would be a key verification of their strategy.

Doug Hunt asked if the CCG were comfortable with the Outcomes and challenge process to date.

David Howarth commented that when looking at the Outcomes/Commitments he felt that numbers 5 - 7 wouldn't be important to Customers and are therefore not reflective of customers' views even if they are important.

Doug Hunt feels there had been a fair amount of challenge on the Company's Outcomes, including a specific Sub Group, and asked whether the CCG are satisfied with process.

David Guest confirmed he felt there had been sufficient challenge made, especially with the thought process behind them changing them from a 'wish list' to actual outcome objectives.

David Howarth commented that during the process the Company were very receptive and made changes to their Outcomes following challenge. He confirmed that the Outcomes Sub Group meeting was beneficial.

Doug Hunt commented that the CCG had mentioned water efficiency, are they happy with that outcome?

Milo Purcell commented that there was not enough information provided by Company on what they propose to do in regard to water efficiency.

Doug Hunt recommended that in respect of the Water Resources Management Plan and similar documents the CCG Report just comments that these are statutory processes.

David Howarth indicated that the Environment Agency would be writing to the CCG with comments that they would like to see passed on to Ofwat. This could therefore form the main basis of the section of statutory requirements, along with any comments that the DWI wish to see reflected.

Doug Hunt confirmed that following the discussion he would flesh out sections 1 -3 of the report and advised that there was not enough information yet for section 4 onwards. Need to consider if the Business Plan is in line with long-term strategy with customers and shareholders preferences? Is that what CCG consider is in their remit?

**DH**

Karen Gibbs suggested the CCG should encourage the Company to demonstrate this.

David Howarth suggested the main areas of challenge made by the CCG should be listed.

David Guest advised that the Company have done this and will ask for it at the next meeting.

**DG**

## PORTSMOUTH WATER Ltd

### CUSTOMER FORUM – MARKET RESEARCH SUB-GROUP

#### MEETING HELD ON THURSDAY 7 FEBRUARY 2013

**PRESENT:** Paul Barfoot (Portsmouth Water), Amy Denford (Portsmouth Water - Secretary), Paul Le Masurier (MVA Consultancy), Jon Stuart (CAB), Nick Sheeran (Portsmouth Water), Victoria Weston (Winchester City Council)

**APOLOGIES:** Louise Bardsley (Environment Agency), Cllr David Collins (Havant Borough Council), Cllr Paul Dendle (Arun District Council), Karen Gibbs (Consumer Council for Water) and John Havenhand (Consumer Council for Water)

#### 1. **Minutes of the Meeting held 18 December 2012**

The minutes, which had previously been circulated, were approved.

#### 2. **MVA Pilot Feedback - Revised Questionnaire and Materials**

Paul Le Masurier of MVA advised the Sub Group that the Pilot was informed by the Qualitative Phase and the design of previous PR09 Research. The Pilot consisted of 20 Domestic Customers being interviewed on what improvements they would be willing to pay for. The actual research will consist of 500 Domestic and 100 Business Customers. The Pilot only targeted Domestic Customers. The Business Customer Interviews will be on the same basis with the addition of some specific Business issues e.g. Onsite Leak Detection, Direct Account Managers and Water Audits.

Paul Le Masurier outlined the aims of the pilot survey was to test;

- the recruitment process of respondents;
- fieldwork logistics, and whether the questions, and show material, were understood by respondents;
- the range of values presented in the SP exercises; and
- the length of the questionnaire

Nick Sheeran asked what the recruitment process was. Paul Le Masurier explained that MVA hold Portsmouth Waters region electronically and can overlay a census, it is separated into Catchments of 200 Households. MVA randomly select 50 Catchments and Interview 10 Households in each Catchment according to quota to achieve the 500 Interviews of Domestic Customers.

Victoria Weston questioned whether it had to be the homeowner / bill payer that could take part in the Interviews. Paul Le Masurier confirmed that currently that is what Ofwat require, however, there is an argument that younger participants are the bill payers of the future and their views on improvements and willingness to pay would be valuable.

Nick Sheeran confirmed that additional areas of research have been identified to engage Customers e.g. shopping centres, local community groups etc, so we should be able to get the opinions of the younger demographic. Also the Engagement Strategy is currently being redrafting to include additional aspects of research to assist our Customer Research.

Victoria Weston suggested approaching Local Colleges and Universities to interview the younger demographic. Jon Stuart recommended South Downs College as they run a Personal Finance Course and the interview could form part of their coursework.

Nick Sheeran advised that the Quantitative Research will be completed in March 2013 and then Phase Three will commence when the other aspects of the Customer Research can be addressed.

The interviews for the pilot were conducted using the Questionnaire and Show Materials previously agreed by the Sub Group.

Paul Le Masurier made the following observations to improve the flow of the survey:

- interviewers to be given a Letter of Authority that explains the bona fide nature of the survey from Portsmouth Water;
- some of the showcard shading needs to be lightened to make easier to read;
- the term 'biodiversity' needs to be better explained;
- the format of Showcards A, B & C should be made easier on the eye, using bullet points;
- a showcard for the income question would be useful (to decrease the number of refusals);
- re-consider showcard labelling (all currently denoted A, B, C etc)

Paul Le Masurier commented that the success of the Interviews were dependant on the goodwill of the participant and is therefore considering a cash prize draw as an incentive.

Paul Le Masurier explained in detail the Pilot Results to the Sub Group.

Jon Stuart asked if Portsmouth Water had released their charges increase yet as that may affect the results of the Research. Nick Sheeran confirmed that the Company had announced a 2.3% increase for Domestic Customers and an average of 1.5% overall, a below inflation increase. He also confirmed that Southern Water has announced a 5.5% Increase on their sewerage charges which may also impact on the results of the Research.

Nick Sheeran raised a question on behalf of Karen Gibbs who was unable to attend the meeting as to whether MVA feel the presentation of the different packages, as grouped, impacts the level of willingness to pay and whether they are confident that customers understood the implications of their choices in terms of their water bill and service. Jon Stuart agreed with this and as a representative of the Citizen Advice Bureau thought those Customers may find the Questionnaire and Materials challenging to follow. Paul Le Masurier reassured the Sub Group that the Interviewers will be guiding the participants through the Material.

Victoria Weston enquired about the Interviewers Training. Paul Le Masurier advised that MVA subcontract their Interviewers who are fully trained to Industry Standard.

Jon Stuart asked if the Interviews are recorded for quality purposes. Paul Le Masurier confirmed that this has been discussed as sometimes the Interviewer would be accompanied so that somebody could note the interest through facial expressions and answers, however, this made the Customers less inclined to take part having two men on the door. Agreed recordings would be a good idea.

Paul Le Masurier took the Sub Group through the revised Questionnaire section by section.

Jon Stuart asked with reference to Question 13b re Southern Water increasing their sewerage bill, if Portsmouth Water would be sharing this information with Southern Water.

Nick Sheeran confirmed that Portsmouth and Southern are currently undertaking separate research to investigate the confusion with Customers.

Discussion was had on Inset Appointments and the further layer of complexity and confusion these may cause.

Paul Barfoot commented that in PR09 the Willingness to Pay results were addressed by looking at the most financially stretched customers and establishing their willingness to pay and putting that forward to Ofwat.

Nick Sheeran suggested that the Southern Water annual charge quoted in Question 13 be updated to reflect the recent Increase Announcement.

Nick Sheeran requested that Showcard C – Environmental & Social Issues be updated to include abstraction from rivers as this information is needed for some other work that is being carried out.

Paul Le Masurier was concerned that this wasn't meaningful to Customers and agreed to discuss it with Gareth Simmonds before printing a final version of the Questionnaire and Research.

Nick Sheeran requested that any further comments / amendments be sent directly to Paul Le Masurier by Midday Monday as the show materials had to be printed on the Tuesday, and the Research will commence next Friday 15 February 2013.

It was agreed that the group had no further significant changes to make to the research material and that the group was happy for MVA to proceed with the quantitative research, subject to the minor alterations discussed.

**3. Date of Next Meeting**

**Wednesday 6 March 2013 10.00 am** to discuss Topline Report.

**4. Any Other Business**

Nothing to Report

# PORTSMOUTH WATER Ltd

## CUSTOMER FORUM – MARKET RESEARCH SUB-GROUP

### MEETING HELD ON THURSDAY 21 MARCH 2013

**PRESENT:** Paul Barfoot (Portsmouth Water), Amy Denford (Portsmouth Water - Secretary), Karen Gibbs (Consumer Council for Water), John Havenhand (Consumer Council for Water) Paul Le Masurier (MVA Consultancy), Nick Sheeran (Portsmouth Water) and Jon Stuart (CAB)

**APOLOGIES:** Cllr David Collins (Havant Borough Council), Cllr Paul Dendle (Arun District Council), Douglas Kite (Environment Agency) and Victoria Weston (Winchester City Council)

#### 1. Minutes of the Meeting held 7 February 2013

The minutes, which had previously been circulated, were approved.

Nick Sheeran commented that the only matters arising from the minutes was the subject of other areas of engagement / research which were discussed at the previous meeting, especially those regarding engaging with the younger demographic. He confirmed that a revised Engagement Strategy had been drafted and circulated to the wider CCG for discussion at their meeting on 26 March 2013.

#### 2. MVA Draft Final Report

Paul Le Masurier of MVA Consultancy presented to the Sub Group on the Final Results of the Customer Research.

John Havenhand raised concern over the reason for certain options given to customers being too obvious, one choice clearly stronger than another. Paul Le Masurier reassured the Sub Group that certain options are deliberately made to appear stronger to provide a logic check and to break down the correlation in the results.

John Havenhand raised concern over contextualising WtP. His impression was that customers were being forced to prefer something when they may not prefer any of the options thereby leading them to give answers which were meaningless. Paul Le Masurier confirmed that three of the four exercises were not related to WtP at all just asking customers to choose their preferred improvements, then in the final exercise they had to decide which improvements they would be WtP for. John Havenhand expressed that customers may be linking their preference to money even if the survey hadn't indicated that it was and therefore the results may be slightly misleading and need to be looked at with caution.

John Havenhand questioned why the report states that ¼ of customers were not WtP anything for improvements but these were left out of the results. Paul Le Masurier confirmed that this was standard practice as there is an economic theory that there are protest voters e.g. not WtP for services they feel they should receive anyway for the public good. He did however; reassure the Sub Group that these customers did add value to the results as you can assess what improvements they value from their preference exercises. John Havenhand made the point that value and price is not the same thing; therefore he felt the way the results were interpreted was not entirely realistic.

Karen Gibbs suggested that the Company does not have to fully fulfil improvements and can therefore reduce the cost to the customer e.g. water softening, the Company could provide more information and advice on hard water rather than carry out complete water softening. However, Paul Le Masurier confirmed that if the Company did not fully fulfil improvements then WtP comes down.

Paul Le Masurier concluded confirming that Ofwat will need evidence that customers support the Plan and MVA could do a final exercise.

Nick Sheeran informed the Sub Group of the Draft Outline Business Plan that was sent to all the CCG Members recently which took into account MVA's Interim Report on the Customer Research and tying it into the Company's Outcome Statements. The Feedback Questionnaire in the back of the Plan should provide some top line feedback from customers on their views on the overall Plan.



Nick Sheeran welcomed the Sub Groups overall feedback on the results of the Customer Research.

John Havenhand confirmed that he felt the Survey was done well but interviewer bias was an inherent and unavoidable possibility. Additionally He feels that the Stated Preference Theory is not 100% accurate and there are problems if Customers indicated their WtP without proper consideration of the wider context of rising prices in general. He also therefore reiterated that the WtP figures are indicative only and not to be taken too literally. Karen Gibbs confirmed that John Havenhands views were an observation of the type of research undertaken not a criticism of MVA. Nick Sheeran made the point that all other water companies were undertaking a similar style of research and that this was the accepted style of research being used (albeit with the recognised limitations).

Paul Le Masurier agreed that this type of research is limited as just taking a point in time and a small sample and you are always going to be talking about estimates. He made the point that most customers did not even know how much they paid, therefore, customers may well not notice the increase in their bill but would notice the improvements made.

Karen Gibbs commented that she thought the Outline Business Plan was a good idea and asked whether the Company would be doing acceptability testing once customers feedback has been received as the results do come down to interpretation / trade off so this would just check it still conforms to what customers said they originally wanted. Paul Le Masurier advised that the Company should take Ofwats guidance on this and Nick Sheeran agreed it would be a good idea, however, raised concern that the timetable may not allow for such testing.

Nick Sheeran summarised that overall the Sub Group appeared to be happy with the report but noted the limitations of the methodology involved. John Havenhand confirmed that he was comfortable with the way the survey was conducted but emphasised the need to be careful not to take the WtP figures too literally. They were only indicative but care will not to be exercised with the interpretation of Results. The Sub Group were in agreement.

### **3. Next Steps**

Nick Sheeran confirmed that the Results will be discussed with the wider CCG at their Meeting on 26 March 2013 and a decision reached on what to do in respect of further research.

### **4. Date of Next Meeting**

TBC

### **5. Any Other Business**

Nothing to Report

## PORTSMOUTH WATER Ltd

### CUSTOMER FORUM – MARKET RESEARCH SUB-GROUP

#### MEETING HELD ON FRIDAY 8 NOVEMBER 2013

**PRESENT:** Nick Sheeran (Portsmouth Water), Paul Barfoot (Portsmouth Water), Jane Day (Portsmouth Water - Secretary), David Guest (Independent Chair), Karen Gibbs (Consumer Council for Water), John Havenhand (Consumer Council for Water), Doug Hunt (Atkins), Paul Le Masurier (MVA Consultancy), Cllr Kirk Phillips (Winchester City Council) and Jon Stuart (CAB)

#### 1. **Apologies for Absence**

Apologies were received from Mr D Kimber.

#### 2. **Outcomes WtP Research Results**

Paul Le Masurier of MVA Consultancy explained to the Sub Group that the purpose of the meeting is to consider the latest research and decide the next steps forward. It is to ensure whether we have received an informed view from the customers with regards to the proposed Business Plan. The main objective is to test customer acceptance and the insight implications for over and under delivery.

It was reported that a structured questionnaire was used to both domestic and business customers.

David Guest questioned whether MVA had shown the Business Plan to the domestic and business customers?

Paul Le Masurier replied that customers were given a summary of the Business Plan to make informed views.

It was noted that the CCG would have preferred before and after answers (informed and uninformed).

Doug Hunt questioned 'real terms' where inflation was concerned and questioned whether Portsmouth Water checked if customers understood what this meant. Paul Le Masurier replied that it had been piloted and customers preferred to understand things in today's money.

David Guest agreed that customers have difficulty in understanding inflation until it affects them financially. Paul Le Masurier pointed out that it is not constructive to put figures in the show cards as it over complicates matters. MVA's approach is to keep the questionnaire simple and concise.

Kirk Phillips agreed with this approach.

David Guest questioned the Company's affordability/handling of inflation in their questionnaire. It was agreed that inflation does cloud the issue. Paul Le Masurier responded that he was happy with their approach. The simple approach is the best for the general customer.

Karen Gibbs stressed that she feels uncomfortable and concerned that other Water Companies have included inflation figures but the CCG has challenged this point and Portsmouth Water must take a view.

Karen Gibbs also questioned how many vulnerable customers would have been interviewed out of the 200 surveyed.

Paul Le Masurier confirmed that a proportionate representation of customers would have been interviewed. There is further scope to investigate more if required in more details.

Kirk Phillips questioned what is the definition of a vulnerable customer?

John Havenhand replied that the definition is a political point of view.

David Guest stated that Ofwat will be looking for vulnerable customers and would want prices to be reduced in real terms.

Paul Le Masurier reported that it is important to appreciate income/financial groups. It is important that the report includes vulnerable persons.

John Havenhand confirmed that Portsmouth Water need to define 'vulnerable persons' which doesn't affect MVA's approach and plan.

Nick Sheeran reported that Portsmouth Water have looked into reducing bills, below inflation but the Company did not believe this was financeable unless capex programme was curtailed but this would result in increased risk to assets/customer in the longer term.

Paul Le Masurier commented that this stage 4 research does not supersede all the previous research that has been carried out. It was noted that all reports will contribute towards the Business Plan.

David Guest stated that this is very important information for the CCG to consider.

David Guest questioned what is the Company doing to improve service to business Customers? Paul Barfoot outlined new aspects to service which will be contained within the Non-Household plan.

John Havenhand questioned whether informing customers that Portsmouth Water is the cheapest Water Company in the country was a leading question?

MVA challenged this and it was agreed that because this is a fact it was satisfactory to include this detail in the research.

Kirk Phillips questioned whether a reduction in PCC is achievable. General discussion took place on whether the Company has the power to influence PCC, for example, water efficiency, metering, water efficiency gadgets and re-educating the customer on water usage.

Acceptability of the Plan was then discussed. It was reported that 99% Domestic customers and 94% Business customers accepted the Plan. In the Segment breakdown the more vulnerable customers D/E have actually given a more favourable percentage than the more affluent customers. The general view was that this was them showing relief as every other cost is increasing – not seen elsewhere in the market place.

Karen Gibbs stated that 2% found the Plan unacceptable and felt that Portsmouth Water should be performing at a higher level without the need for an inflation price increase.

Kirk Phillips responded that 2% is a very small percentage.

David Guest replied that customers are more concerned about inflation; customers are more likely to understand inflation. A/B not a high percentage.

Doug Hunt stated 2% of C1/C2 though it was unacceptable. This gave assurance that the understanding of inflation had been covered correctly in this research.

Karen Gibbs stated that D/E customers are likely not to understand, which is why there is a high level of support.

Doug Hunt commented that initially he had had concerns about whether inflation had been dealt with sufficiently in the research. However following the discussion he was satisfied it had been dealt with appropriately.

Paul Le Masurier replied that 2% is still not a significant figure to cause any problems.

There was general consensus that the approach was reasonable and the results too.

Paul Le Masurier reported that there were Five Outcomes researched.

1. Leakage
2. Safe, secure and reliable water supply
3. Value for money & Customer service
4. Environment supporting wildlife, public amenities and recreation
5. Supporting the community by support the local economy

John Havenhand stated that this requires us to use our judgement again. I think we have to be very careful with these figures. I believe that the methodology is questionable.

Doug Hunt questioned the figures for leakage. Paul Le Masurier replied that this is a complicated section to report on.

Nick Sheeran reported that this can be discussed at the Peer Review as the methodology has been challenged.

#### **4. Accent Report on Peer Review**

John Havenhand commented that the suggestion by Accent that “if respondents believe their answers will influence how much they will end up having to pay, then they have an incentive to understate their true willingness to pay when asked by an opened ended question” is incorrect. He argued that it proved the reverse. That it indicated that they weren’t seriously prepared to pay it in the first place and that the individual stated preferences taken in isolation of overall context overstated how much they were in fact willing to pay. It was reiterated that we need to be careful how we interpret the results. Doug Hunt reported that the willingness to accept vs willingness to pay is a concern.

Doug Hunt reported that there are three things to consider:

1. Uk Wir documents are best practise – this is not true in all cases.
2. Assurance – it should be clear in the report whether the survey is broadly ok or not. A response is required.
3. Portsmouth Water and Paul Barfoot stated that Ofwat have asked the question – What penalties/rewards are you willing to put up with for ‘willingness to pay’.

It was reported that Portsmouth Water are the only Water Company to report on over and under outcomes.

Karen Gibbs challenged the company to do the best by its Customers, does this include rewards/penalties. Was this asked to customers? If Portsmouth Water over perform do customers have to pay more? Did customers fully understand this?

John Havenhand replied that we haven’t got a definitive answer to customers. It is the Companies decision and to ask CCG to support or challenge it.

Doug Hunt requested that MVA do a response and circulate to the Customer Challenge Sub Group. It was agreed that Portsmouth Water will consider extra work on sensitivities.

John Havenhand stated that the ACCENT report was rather academic and not user friendly for the layman.

He also asked whether Ofwat required there to be incentive/penalties included in the Business Plan.

David Guest questioned whether this is a prudent way to go forward.

Paul Le Masurier then explained to the Customer Challenge Sub Group the mythology used.

John Havenhand questioned whether incentives/penalties were necessary? Nick Sheeran replied that Ofwat are expecting Portsmouth Water to have rewards and penalties in their plan. John Havenhand replied that, it should not be assumed that financial rather than reputational penalties would be more likely to motivate Portsmouth. He thought it may be unnecessary and could be an added cost to the customer.

Karen Gibbs stated that some companies have decided to go with 'penalty only ODI's'. David Guest stated that the CCG would not be concerned if the Company decided not to include any incentives or penalties at all. This was a matter for the Company.

David Guest replied that it is minimal to the average bill.

Karen Gibbs questioned whether there will be penalties to ensure Portsmouth Water deliver what they planned.

Paul Le Masurier stated that the remit is to try to get customers to understand the impact of under delivery or over delivery in certain areas so customers get a feel for the increased benefit for over delivery and disappointment for under delivery.

It was questioned how, if you are already very satisfied, can you be more satisfied if the Company improves its performance. Paul Le Masurier replied that the scale indicates relative indication of satisfaction, if certain improvements were made.

David Guest stated that the methodology was good considering the timescales given and that he did not believe that Accent had raised any issues which would be of concern to the CCG.

Kirk Phillips reported that it would be good to simplify the methodology.

Doug Hunt stated that according to the report customers feel that penalties/incentives are just as important as each other. Same importance for over performing and under performing.

Paul Le Masurier thought that customers put a high value for over delivery.

Kirk Phillips remarked that more and more customers now are putting the environment as a high priority.

Doug Hunt stated that customers want things to improve not deteriorate.

Karen Gibbs questioned what the conclusion is?

Nick Sheeran stated that Accent had reviewed all the research undertaken by MVA. They had challenged only one aspect of the research (the work done on assessing customers willingness to pay for under/over delivery of outcomes). However Accent were satisfied with the rest of the research and this was a good result for the Company. The Company would ask MVA to respond to the points raised by Accent and consider the way forward. However, the issue related to only a minor point in the plan and the money involved was not material.

Paul Le Masurier stated that the results are a correct interpretation, a good reflection of satisfaction over delivery, benefit of over delivery rather than under delivery.

Karen Gibbs questioned ODI's?

It was agreed that Paul Le Masurier would write a response for the CCG.

It was questioned should we not have incentives, correct value, not always financial.

Nick Sheeran to reply by the next Customer Forum Challenge Group Meeting on Tuesday 12 November 2013.

Doug Hunt questioned whether all challenges have been addressed? This will be addressed in the report.

Doug Hunt to feed back to the CCG on Tuesday 12 November 2013.

## **5. Next Steps**

1. Should we have included penalties/incentives in the Business Plan?
2. If we do how much should they be for?
3. Have all challenges been addressed?

**6. Any Other Business**

Nothing to Report

# PORTSMOUTH WATER LTD

## CCG – OUTCOMES SUB-GROUP

### MEETING HELD ON THURSDAY 1 AUGUST 2013

**PRESENT:** Amy Denford (Portsmouth Water - Secretary), David Guest (Independent Chairman), John Havenhand (Consumer Council for Water), David Howarth (Environment Agency), Nick Sheeran (Portsmouth Water) and Neville Smith (Portsmouth Water)

**APOLOGIES:** Karen Gibbs (Consumer Council for Water) and Milo Purcell (DWI)

#### 1. High Level Outcomes and Measures of Success

David Guest outlined the purpose of the Sub-Group following the concerns raised at the last CCG Meeting of the importance of the Company's Outcomes being worded appropriately. Removing the passive and creating active outcomes and measures.

Following the CCG Meeting and subsequent PR14 Board Meeting Portsmouth Water had revised the High Level Outcomes and Measures and circulated it to the Sub-Group for discussion at the Meeting.

The Sub-Group also had sight of an extract from the Minutes of the CCG Meeting held on 25 June 2013 for information.

David Guest circulated Comparative Draft Outcomes produced by Ofwat for a recent CCG Chairs Workshop, showing how other Water Companies approached their draft Outcomes.

John Havenhand commended the Company for following Milo Purcell's advice from the last CCG Meeting and reducing the number of Measures for the Outcomes as the Company had made themselves vulnerable and open to penalties. Only concern was that the Company may have reduced them too far.

Neville Smith reassured the Sub-Group that the Company have other internal KPI's, these were just the key measures to the output of the Business Plan. There will be other low level metrics but these were how the Business would be measured.

John Havenhand recommended that it needs to be clear when the Outcomes would be achieved, after one year each and every year or at the end of the period.

David Guest suggested the Sub-Group start by reviewing the Comparative Draft Outcomes to assess how Portsmouth's Outcomes measure up compared to the rest of the Country. Were their Outcomes sufficient, well worded, and complete?

David Howarth commented that Outcomes should be written in the past tense, something that has been achieved. Most Water Companies appear to have just written a 'shopping list' of 'we will..'

John Havenhand agreed and commented that they have listed aspirations not outcomes, they need to state the end result.

Neville Smith suggested the Sub-Group review Portsmouth Outcomes in turn.

**Outcome: *'Have a culture of health and safety through all our activities and have a highly motivated and skilled workforce delivering a high quality service to our customers.'***

John Havenhand suggested that this be amended to reflect that this is recognised by Stakeholders.

Neville Smith agreed he liked the term 'recognise' but within the Industry and by Portsmouth's Customers.

John Havenhand asked if the KPI's will be delivered in the first year.

Nick Sheeran advised that the target is by 2020.

John Havenhand commented that the KPI to 'improve overall SIM survey score each year' implies a weakness 'to improve' and suggested adding the wording 'remain within the top quartile'.

**It was suggested that the Outcome be changed to: '*Recognised within the Industry and our Customers that we have a culture of health and safety through all our activities and have a highly motivated and skilled workforce delivering a high quality service to our customers.*'**

David Howarth commented that there has been advice not to use the term 'deliver' anymore but to use 'provides'.

Neville Smith commented that all the Outcomes were about trust. Where the Company wants to be so Customers, outside bodies and employees can trust that they will provide all the Outcomes.

Neville Smith advised that the Company is not asking Customers to pay for improved service and therefore other than the standard incentives, penalties / rewards, imposed by Ofwat there are not many included except for Leakage and Environmental. Customers only get something back if they have lost something.

John Havenhand commented on the risk of setting low targets to avoid penalties and also setting high targets to improve when already performing at a high level.

Nick Sheeran raised concern that if the Company doesn't have many incentives, Ofwat may think the Plan isn't challenging enough. Ofwat wanted to see Companies stretching and challenging themselves, but Portsmouth's focus is on not increasing prices.

Neville Smith commented that Portsmouth's challenge is to improve services without increasing prices.

David Guest advised that Customers can see where the Company ranks overall in the Country and where / if they can improve.

Neville Smith confirmed that he would prepare a report for the next CCG Meeting detailing where Portsmouth rank within the Industry against each KPI.

**Outcome: '*Continue to be attractive to investors and provide a long term financially sustainable business.*'**

Nick Sheeran suggested removing the words 'Continue to be'.

John Havenhand questioned why the Company had used the words 'Continue to'.

Nick Sheeran advised that Portsmouth Water believed it is attractive now which must continue.

John Havenhand asked whether there would be an issue maintaining credit rating.

Neville Smith confirmed that it might be an issue if determination isn't good.

David Howarth commended the Company for putting the financial position in the Outcomes as some Companies have left them out.

John Havenhand questioned if the 2% Dividend growth was per annum.

Nick Sheeran confirmed that it was.

Neville Smith confirmed that this is what Ofwat allowed last time.

John Havenhand suggested incorporating some wording about Customers benefiting from Company's financial position.

Nick Sheeran said this could be covered in the Outcome regarding customers receiving a high quality service and value for money.

Neville Smith commented that the Company could include an Incentive saying that any outperformance would be shared 50:50 between Customer and Shareholders which would also reduce gearing.



**It was suggested that the Outcome be changed to: *'Attractive to investors and provide a long term financially sustainable business.'***

**Outcome: *'Support the community we serve by taking opportunities to support growth and development.'***

David Howarth asked for clarification on the term 'growth'.

Neville Smith advised that this was economic growth. Encompassed far more than just housing and population growth but also employing from within the local community and using local suppliers.

David Howarth commented that as Portsmouth is a smaller Company it has a closer relationship with the Community.

**It was suggested that the Outcome be changed to: *'Support the community we serve by taking opportunities to support the local economy and development.'***

**Outcome: *'Promote a high quality environment that supports biodiversity, public amenities and recreation.'***

David Howarth commented that the KPI for all sites impacted by WFD to be in good condition by 2020 is slightly ambitious as currently the WFD is only in Phase Two with a deadline of 2021 and Phase Three being completed by 2027.

Neville Smith advised that he would liaise with the Manager responsible and have the KPI updated with a refined deadline.

David Howarth suggested removing the word 'promote' from the Outcome. Would prefer protect and enhance, although he realises that is more of an objective than an end result.

**It was suggested that the Outcome be changed to: *'An improved environment supporting biodiversity, public amenities and recreation.'***

**Outcome: *'We deliver a high level of service and value for money.'***

Neville Smith suggested that the 'we deliver' should be changed to Customers recognise as the desired Outcome.

John Havenhand suggested that the KPI 'Improve overall SIM survey score each year' should say within the top quartile.

**It was suggested that the Outcome be changed to: *'Customers recognise we provide a high quality service and value for money.'***

**Outcome: *'Provide a safe, secure, sustainable and reliable supply of drinking water over the long term.'***

Nick Sheeran suggested removing the word provide to word it like an end result.

David Guest suggested amending some of the Measures to read as an end results e.g. improving to improved and reduce to reduced.

John Havenhand recommended removing the word 'Avoid' from the Measure regarding temporary use restrictions and replacing with 'no'.

Neville Smith advised that the standard was to have no more than 1 in 20 years temporary restrictions and maybe this should be incorporated into the wording.

Nick Sheeran suggested removing the words 'over the planning period' after the Measure 'Reduce Leakage'.

**It was suggested that the Outcome be changed to: *'A safe, secure, sustainable and reliable supply of drinking water.'***

Neville Smith confirmed that the Final Outcomes would be communicated to Customers in a Draft Plan being published in September outlining where the Company is now and what the improvements will be.

John Havenhand asked when the Incentives would be agreed and Nick Sheeran confirmed that this will be addressed later in the process.

It was agreed that the revised High Level Outcomes and Measures of Success will be circulated ahead of the next full Meeting of the CCG.