

FINES FOR FAILURES

A clear message was sent to the water industry when we announced proposals to impose financial penalties on two further water companies for failures to accurately report information and to maintain acceptable standards of customer service.

In September, we announced our [proposal](#) to impose fines totalling £12.5 million on Thames Water. And earlier this month, we announced our [proposal](#) to impose fines totalling £20.3 million on Southern Water.

The penalties for Southern are higher than for Thames, because of the more serious nature of the contraventions at that company. Southern deliberately misreported information, with the intention of improving the company's reported performance.

Water is a monopoly industry and customers are unable to directly influence the level of customer service they receive by switching supplier when they are unhappy. We act as a proxy for competition and we rely on the information that the water and sewerage companies provide to

compare performance. If companies misreport information it damages the entire regulatory regime as each company's relative performance will be distorted where comparisons are made based on poor information.

Since discovering the failures, both companies have taken steps to remedy the failings. Penalties are intended to provide an incentive for companies to comply with their statutory and regulatory requirements now and in the future.

Earlier this year, we confirmed our decision to impose an £8.5 million fine on United Utilities Water plc, which supplies consumers in the north-west of England, for breaching its licence condition on trading arrangements with associate companies.

Last year, we also gave notice of our intention to fine Severn Trent Water for failing to achieve service standards prescribed by the guaranteed standards scheme (GSS) regulations. We will announce our decision in due course.

Fines by numbers

£20.3 million: Total fines proposed for Southern Water for failures to accurately report information and to maintain acceptable standards of customer service.

£12.5 million: Total fines proposed for Thames Water for failures to accurately report information and to maintain acceptable standards of customer service.

£8.5 million: Fine paid by United Utilities Water for breaching its licence condition on trading arrangements with associate companies.

Mike moves from mesosphere



Mike Keil, Ofwat's first Head of Climate Change Policy.

Whether studying the impact of high-altitude balloons carrying mobile phone masts or investigating how changes in the atmosphere on the edge of space affect our weather, Dr Mike Keil really is a high flyer.

Our new Head of Climate Change Policy joins us after ten years at the Met Office in Exeter, where he led a team researching the middle atmosphere – the 'mesosphere'.

His team's remit started where most airliners fly – at about six miles up – to the outer limits 60 miles above our heads. Mike headed up the drive to find weather-related applications in this area that would improve forecasting.

Mike has graduate and postgraduate qualifications from Edinburgh and Reading.

What attracted him to Ofwat?

"I've always tried to make a difference in my meteorological work, but the position at Ofwat stood out as an opportunity to make a big contribution by helping the water industry to adapt and mitigate against the effects of climate change," he explained.

"It is good to see Ofwat taking the issue so seriously. We face an uncertain future, but one thing is clear: the only guarantee is that our changing climate will throw us a few surprises along the way."

The new post is an important development of our commitment to encouraging a sustainable water sector. Mike is looking forward to helping the industry meet consumers' future needs without placing extra burdens on the planet.

"Sustainable development is integral to all Ofwat's work and we have an important duty to encourage the industry to take sensible and measured steps that will make a big difference in the future."

Cutting carbon costs

The water industry is a significant contributor to greenhouse gas emissions in England and Wales. We expect each company to help lessen the effects of climate change by managing the amount of greenhouse gases it produces.

We have asked each company to publish a 25-year strategic direction statement setting out how it intends to meet consumers' longer-term needs. This allows companies to set out their plans for sustainable development, which is at the heart of our price review for 2010 to 2015.

Each company should examine and analyse how its proposed strategy will affect the amount of greenhouse gases it produces. This will allow companies to select the best mix of options to lessen the impact of greenhouse gases. These could include developing renewable energy sources.

We will support further work on more comprehensive carbon accounting. Starting next year, we will ask companies to report to us the amount of greenhouse gases they produce.

Further information on our approach to carbon emissions can be found in our [PR09 methodology paper](#) (see page 3).

PR09 paper published

We have recently published our consultation paper, '[Setting price limits for 2010-15: Framework and approach – a consultation paper](#)', on how we will approach our next review of price limits in 2009. At the same time, we have also officially launched the 2009 price review process (PR09).

Every five years we set limits on the prices that all appointed water companies in England and Wales can charge their customers. The price limits we set in 2009 will be for the period 2010-15. We last set them in 2004 for the current five-year period.

The consultation paper is our 'how-to' guide on setting price limits in 2009. We are asking our stakeholders for their views before we finalise our approach in March next year. We have already held two stakeholder workshops, on [15](#) and [16 November](#), to discuss the issues raised in our consultation paper with the rest of the industry and consumer groups respectively – and there will be further opportunities for stakeholders to contribute to the process over the next two years.

New proposals in the paper



include a requirement for each company to submit a single core business plan, as well as carry out cost benefit analysis across all parts of the business.

Alongside the consultation paper, we have published a number of supporting documents, including companies' [strategic direction statements](#), which are also available on the [PR09 section](#) of our website.

The consultation on our approach to PR09 closes on 24 January 2008.

You can send responses to our consultation by [post](#) or by e-mailing them to rhiannon.mchugh@ofwat.gsi.gov.uk.



Promoting PR09

We want to keep you informed of what's happening during the 2009 price review so we have launched our first PR09 newsletter, '[Price review update](#)', which sets out the key dates for the diary for the next two years, as well as the key messages that underpin the price setting process.

But that's not all.

We have also launched a brand new section on our [website](#), which is devoted to the price review. There's no catchy name for this section, but plenty of catchy information about PR09. For example, it provides specific information and publications for each stage of the four-step process for setting price limits in 2009. There's also a handy glossary of terms if you are unsure about any of the words used.

And don't forget, if you want to be the first to know when we publish something new on the website – whether PR09 related or not – you can sign up for our [update alerts](#) on the website.



Competition continues

In July 2007, we published our consultation paper on the review of competition. Although this consultation has now closed, our review of competition in the industry continues.

We received a good number of responses to the consultation from water companies, licensees, customers and other key stakeholders. Most respondents were in favour of the majority of the [proposals](#) we set out.

One of the areas where there has been a particularly positive response is our proposal to develop accounting separation. This would require each company to identify clearly and report separately on each key area of its business. This will lead to transparency of costs, help identify competition opportunities and make entry to the market simpler.

We are currently analysing all of the responses. We will include a responses document, responding to the points raised in submissions to us, as part of a further consultation to be published in December.

This will set out our firm proposals for developing the current competitive regime. These proposals will be set out in the context of the wider issues for change that will be covered in more detail in an additional consultation in March.

With stakeholders' help, we are also carrying out analysis to identify different markets within the wider water and sewerage industry where competition could be introduced.

For each area we will identify the key characteristics, the current level of competition and the features that restrict

Competition – next steps

- Consult on proposals for changes to the current regime – **December 2007**.
- Consult on proposals for wider changes to competition and publish on the results of our market analysis work – **March 2008**.

or prevent market entry. We will use this work to inform our proposals on how competition can be promoted in the interests of customers.

In other competition news, we have appointed a second new company, [Independent Water Networks Limited \(IWNL\)](#), to supply water and sewerage services to domestic customers.

If you would like to know more about competition you can visit the [competition section](#) on our website.

In competition-related news, we have launched a [consultation](#) for South East Water to replace Mid Kent Water as the water service provider to nearly 250,000 customers in the Kent area. This follows the merger of South East Water and Mid Kent Water, which was cleared by the Competition Commission in May. This is the final stage in the process for the two companies to merge.



Extending Explain

In the last issue of *H₂Ofwat* (August 2007), we reported on Project Explain, our review of the information we communicate to stakeholders and how we do it.

Since then, three of our annual industry reports have been given the Project Explain treatment. The reports on each company's [financial performance and expenditure](#) (published in September), [security of supply](#) (published in October) and [levels of service](#) (published in November) focus on the headline issues affecting the industry in the last reporting year.

The reports are now primarily web based. This has resulted in documents that are delivered efficiently and effectively to the right audience. It has also brought about considerable cost savings for us and is more sustainable as we are printing fewer hard copies. The reports are accessed through their own pages on our [website](#) and are supported by the detailed data and regulatory information that stakeholders value.

The key message from this year's reports is that the industry is generally performing well, but there are problems in some areas and with some companies. We are monitoring those companies that fail to deliver

standards of service that customers expect, and will take appropriate action where necessary.

We welcome your feedback on the new format of our reports. Please e-mail the Explain Project Manager at louise.bickley@ofwat.gsi.gov.uk.

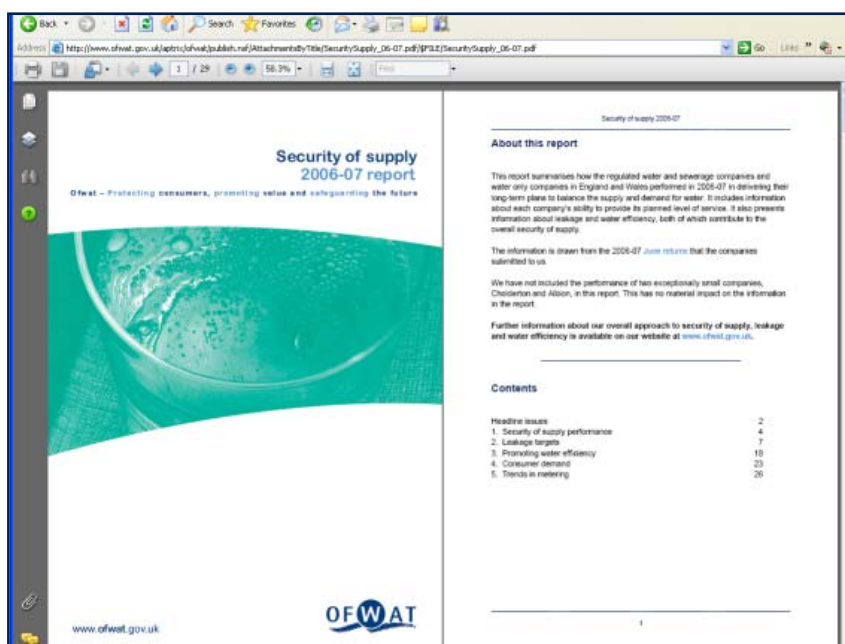
So, what's next for Project Explain? We will be publishing companies' relative efficiency assessments before Christmas. For the first time, this information will be published in a letter to regulatory directors of the water companies on our website, alongside supporting information previously published in our 'Unit costs and relative efficiency' report.

In addition, having moved very quickly to primarily web-based publishing for all our key documents (including the

consultation on our [methodology for 2009 price review](#)), we are now turning our attention to the next and more long-term phase of the project. We will be looking at all of the information we collect and publish, and the audiences for that information so that everything we publish is relevant, focused and timely.

This second phase of the project links closely to the work that we are carrying out on developing our website and our information capture systems. These work streams are part of the development of our simplification plan that we aim to produce to reduce the burden of regulation and streamline the information we collect.

We will provide regular updates on this work in future editions of *H₂Ofwat*.



Consultation on charges changes

We have [announced](#) that the limits on the prices that two small water supply companies can charge their customers may rise from next April, but by less than what the companies wanted.

Our draft decision, on both [Bristol Water plc's](#) and [Dee Valley Water plc's](#) individual applications to increase the limits on their prices from April 2008, will allow both companies to increase the prices to their customers for the water they can supply

We last set price limits for all

appointed water companies in 2004 for the period 2005-10. We limit the bills customers pay upfront when setting price limits by excluding costs that are uncertain. But under the terms of their conditions of appointment, companies can apply to us to review their price limits (an 'interim determination') if they experience significant changes to their costs. They must meet strict qualifying criteria before we will consider revising customer's bills.

In September this year, both Bristol Water and Dee Valley Water asked us to consider increasing their price limits on the basis of significant changes to their costs. We have reviewed and challenged each company's proposals, and have agreed to increases in their price limits, but by less than either company wanted.

We consulted on our draft decision, seeking views from all interested parties. We will announce our final decision on 14 December 2007.

News in brief...

We have published [details](#) of our leakage methodology review.

We have responded to the Environment Agency's [consultation](#) on water resources, as well as providing our [evidence](#) to the Department for Environment, Food and Rural Affairs (Defra) on its consultation on implementation options for the transfer of private sewers.

We submitted our [written evidence](#) to the Environment, Food and Rural Affairs Select Committee inquiry into this summer's flooding.

Regina Finn spoke at the Beesley Lecture in London on 1 November. Regina spoke on the subject of '[Competition and regulation in water: striking the right balance](#)'. And both Philip Fletcher and Regina Finn spoke at our [City briefing](#) on 6 November in London.

[Melinda Acutt](#) (Director of Network Regulation), who is currently on maternity leave, has decided not to return to Ofwat and has resigned from our Board.

Key dates

The period between now and Christmas will see us publish a number of documents, including:

- Competition Act 1998 (CA98) guidance – **early December**.
- our draft forward programme for 2008-09 to 2010-11 for consultation – **early December**.
- companies' relative efficiency assessments for 2006-07 – **mid-December**.
- our consultation on customer charges strategy – **mid-December**.

Next issue – February 2008

For more information about Ofwat and the work we do, visit our website at www.ofwat.gov.uk. If you have any comments about this issue, or suggestions for future issues, e-mail the editor at dylan.spedding@ofwat.gsi.gov.uk.