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Water Supply and Regulation Division Area 2C
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20 June 2008

Dear Dawn

YORKSHIRE WATER SERVICES LTD DRAFT WATER RESOURCES MANAGEMENT PLAN FEEDBACK

Yorkshire Water published its draft Water Resources Management Plan (DWRMP) on 1 April. This letter summarises our preliminary views, while the attached annex provides more information.

We will explore these issues in more detail over the coming months, both with the company and with other stakeholders, including the Environment Agency. We will look closely at the links between Yorkshire Water's DWRMP and its draft Business Plan for the period 2010-11 to 2014-15, which it will submit to Ofwat in August 2008.

We have summarised our preliminary views below.

- Yorkshire Water's investment is driven predominantly by the impact of climate change on supply and demand. The company considers the impact its water balance is immediate, and triggers the need for investment in its Grid water resource zone as soon as 2009-10. While the company has followed the Environment Agency's guidance to an extent to determine the impact of climate change, we expect to see more evidence to support the company's position given the implications for investment that it triggers. For example, we would like to see a catchment model to validate the company's conclusions on the impact of climate change on supply, as referred to in the Effects of Climate Change on River Flows and Groundwater Recharge: Guidelines for Resource Assessment and UKWIR06 Scenarios (UKWIR 2007a) guidance.
- We cannot determine from the plan whether the proposed solution is the optimal economic solution, taking into account environmental, social and carbon costs. We commissioned Strategic Management Consultants (SMC) to carry out an independent review of the DWRMP, and its view was that the proposed solution is not optimal.

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- The company's investment strategy is partly driven by aspirations in the company's strategic direction statement to have no water usage restrictions and to halve leakage by 2035. It is for the company to determine its overall strategic direction, but it must be able to demonstrate that it has adopted the most economic solution to balancing supply and demand. This solution might include enhancing service levels or reducing leakage significantly, but the company must demonstrate that this generates sufficient benefit to outweigh the cost. The company must provide convincing evidence to support its proposal, such as survey evidence that its customers are willing to pay for it.
- We expect all companies to achieve the economic level of leakage. This economic level should incorporate the value of customers' preferences. If Yorkshire Water considers that its customers are willing to pay for it to halve leakage by 2035, then its economic level of leakage calculation should be consistent with this. Yorkshire Water must demonstrate that its evidence on willingness to pay is robust and that customers understand the permanent effect of their preferences on their bills.
- SMC's review questioned the validity of the leakage reduction costs that Yorkshire Water had used to determine the economic level of leakage. However, we understand that Yorkshire Water disagrees with SMC's claims. We expect to see a full exposition of the costs that the company has assumed in its economic level of leakage appraisal.
- Given the uncertainties surrounding the impact of climate change, we are surprised that the company plans a significant investment for a 22 Ml/d extension to the River Ouse treatment works at a relatively early stage. We would have expected a more precautionary approach, deferring such a major investment decision until the need for it is clearer.

Should you require any clarification of the issues raised in this letter please contact David McGrath on 0121 625 1398. I am copying this letter to Bob Garrett at SMC for his information.

Yours sincerely

Paul Hope