



**Setting price limits for 2015-20 – final methodology and expectations for companies’ business plans
Water only companies briefing session: questions and answers**

Q1: Can you clarify the exact role of the Customer Challenge Groups (CCGs) and how you see these evolving in the future?

- The CCGs are playing an important role in shifting the emphasis away from the regulator and placing customers at the heart of company’s business plans. They have delivered benefits already and are driving positive changes in behaviour.
- The methodology statement makes it clear the CCG should focus on the quality of the company’s engagement with customers and how well this is reflected in its plan. CCGs are not a substitute for customer engagement and are not intended to represent customers’ views. A CCG report which solely comprises a glowing report of the company will not constitute a good CCG report. A good report will be one which demonstrates the CCG has effectively challenged the company on the way in which the company has engaged with its customers and how their plan reflects this engagement.
- The future role of the CCGs in PR14 will partly depend on the company’s status. For example resubmission companies will require a new CCG report to accompany their resubmitted plan.
- For enhanced companies these companies could think about how to use their CCG to embed customers’ interests in the development of future strategy and outperformance under PR14. However this is for the company to decide.

Q2: What if customers want things that they are not then willing to pay for? What if customers tell us they want things that cost more money?

- Customer engagement needs to focus on the outcomes that customers want and it also needs to focus on whether they are willing to pay for those

outcomes. If a company's outcomes are well-evidenced and clearly reflect customers' preferences and interests, we do not see why we should substitute the company's proposals with our own.

Q3: Could a company achieve enhanced status if the plan proposes a bill increase?

- We do not have a preconceived idea about what should happen to prices. However we acknowledge the general evidence that customers are stretched.
- It is for companies to demonstrate that they have engaged with their customers and their plan reflects the preferences and interests of their customers and is affordable. We acknowledge that there could be differences between areas in terms of customer preferences, willingness to pay etc, but it is for the companies to provide compelling evidence to demonstrate their plan reflects their customers interests.

Q4: What about the trade-off between affordability and meeting environmental standards?

- Companies have to meet their statutory requirements and this is made clear in the methodology statement. However they will have flexibility to determine the most efficient way of meeting these.
- In general the focus on outcomes gives companies greater freedom to decide how to deliver the services customers want. The dialogue with customers should be driving this, subject to companies meeting their statutory obligations in the most efficient way possible.

Q5: Will there be an opportunity to seek Ofwat's views on our business plans before they are submitted in December?

- Ofwat will not be providing views on companies' plans before they are submitted on 2 December.
- Companies need to own their plans and they need to be confident that these reflect their customers' interests.

Q6: We understand you are currently in a period of clarification – if you identify an industry-wide issue in your bilateral meetings with individual companies will you inform everyone?

- Yes. The recent [information notice published](#) makes it clear that we are currently in a period of clarification until 30 September 2013. During this time we are happy to meet bilaterally with companies to clarify any issues they have. If we identify an industry-wide issue as part of this then we will inform everyone. Other than that the conversations will remain private. Companies should contact their portfolio lead if they want to clarify issues with us during this time.
- From 1 October 2013 until early 2014 we will enter into a period of restricted and formal communication with the companies on the 2014 price review. During this period companies will be concentrating on finalising their plans and we will be conducting our risk-based review (RBR) following submission of business plans.

Q7: If you have questions about business plans during the RBR process will you seek clarification from us?

- If there are specific and very discrete issues then yes we will seek clarification from the company. However if there are more fundamental or systemic issues then we will not seek clarification as this demonstrates that the plan is not a high quality plan.
- It is important that the business plan contains a golden thread of evidence throughout.

Q8: Does the presentation of the company's business plan count towards its performance in the RBR?

- No. The RBR will be conducted on the plan as submitted by the company on 2 December. The offer of a meeting is to allow you to present and explain your plan.

Q9: What happens if the WOC plan is high quality but the plan submitted by the WASC supplying the same customers with wastewater services isn't?

- If the WOC is providing retail services to customers for both water and waste water services, then the WOC's plan will need to demonstrate how it will

maintain the quality of retail services provided to both types of customer. For example it will need to ensure it can obtain timely information on customers from the upstream WASC.

- If the WOC does not provide retail services to waste water customers then it is a separate plan and will not be affected by the WASC's performance.

Q10: Is innovation going to be considered as part of the RBR?

- It is for companies, in consultation with customers, to determine the most efficient ways of delivering the outcomes that customers want.
- The PR14 methodology is trying to drive allocative, productive and dynamic efficiencies. Dynamic efficiency is essentially innovation and in general we would expect to see more of this.
- It is not for Ofwat to prescribe how companies should deliver outcomes for their customers. However it is difficult to envisage an enhanced company that is not introducing any innovation.

Q11: We are concerned about failing the RBR on a technicality and ending up in the resubmission category.

- We will not use a tick box approach to the risk-based review which means firms will not fail on a technicality. If their business plan is excellent and reflects customers' interests then it will be enhanced.

Q12: What if our costs increase due to statutory requirements? Will this undermine the golden thread of our plan and affect my RBR status?

- It will be important to demonstrate in your plan that you are meeting all statutory requirements in the most efficient way possible.
- We will use a totex corridor but companies won't automatically fail this test if they fall outside the corridor as long as they can provide compelling evidence to explain why this is the case.

Q13: What if some price increases are driven by new statutory requirements and are not customer-driven?

- Companies must meet their statutory requirements and we want to see evidence that you are meeting these as efficiently as possible. Dialogue with customers is important to determine exactly how you should meet those requirements.

Q14: How different can our cost estimates be compared to yours?

- We will not publish our preferred totex models or the corridors before the RBR. We want companies to focus on developing the best possible plan for their customers rather than focussing on meeting our tests.
- We will use a totex corridor but companies won't automatically fail this test if they fall outside the corridor as long as they can provide compelling evidence to explain why this is the case.

Q15: How will you test the effectiveness of Company's Board?

- The methodology statement provides information on how we are going to assess Board assurance as part of our risk-based review.
- It is key that Boards own the decisions made in their plans and for companies to explain their governance process. For example if the Executive is proposing a step change in performance then we would expect the Board to challenge this and scrutinise how it will be achieved.

Q16: Are you planning on publishing the August cost data?

- Yes, we are planning to publish this data.

Q17: There is less information available this time round so NEDs cannot challenge companies so effectively. For example they cannot challenge companies to deliver cost efficiencies in line with the industry frontier.

- There is no draft business plan for PR14 so we won't have information on how companies are performing relative to one another until we see business plans.
- We have explained why we are not publishing our preferred totex models or corridors before the RBR but we are planning to publish the raw August data.

Q18: Are you planning on sharing your financial model?

- Yes. We aim to publish this mid-late September.
- We expect companies to continue to use their own financial models for their plans.
- We should work together to understand any differences in our financial model and the models that companies have used to develop their plans.

Q19: Is Ofwat hiring a delivery partner to support it in delivering PR14?

- We are entering our busiest period so inevitably we will need more resources than at other times. Rather than employing permanent resources or entering into lots of smaller contracts with consultants we believe it is better value for money to enter into contract with a single delivery partner.
- We should be in a position to publish the name of the Delivery Partner shortly.

Q20: What do you think is an acceptable return for a WOC?

- It is for companies to determine what an acceptable rate of return is for their individual plan.
- An enhanced company will by definition have proposed a rate of return that fell within an acceptable range and this will become clear once the RBR has been conducted and the results published.

Ofwat
7 August 2013