

RESPONSE TO OFWAT CONSULTATION PR14 Reconciliation Rulebook

Summary

Ofwat has published a consultation on its approach to the reconciliations required at the end of the 2015-20 price control to take account of past performance and different incentive mechanisms. The Environment Agency welcomes the opportunity to comment on the consultation. We support the process of making adjustments to take account of past performance, and agree that publishing the reconciliation rules at this stage will provide transparency throughout the period.

The main points of our response are:

- The reconciliation rules must ensure water companies act in the best interests of the environment as well as customers.
- We would like Ofwat to do a mid-term review of company major schemes.
- Water companies should share a detailed outcome delivery incentive (ODI) methodology with their Customer Challenge Groups.
- When reconciling totex, Ofwat needs to recognise that Water Framework Directive (WFD) investment will be required over the next two price review periods.

1.0 Introduction

- 1.1 The Environment Agency has been working with Ofwat and the water industry throughout Price review 2014 to ensure that the water companies deliver outcomes that enhance the environment.
- 1.2 As the environmental regulator of the water industry in England, we want water companies to implement their business plans in a way that enables them to meet their statutory obligations and maximizes environmental outcomes. The reconciliation rules and framework should help ensure this happens.
- 1.3 In making our response we have limited our comments to specific issues that we feel are relevant to our regulatory role within the price review process.

2.0 Specific issues

2.1 Assessment Framework

- 2.2 The reconciliation rules should ensure that water companies act in the best interests of the environment as well as customers. We would like to see the assessment criteria used for comparing options to specifically mention the environment. In particular we expect companies to profile the delivery of their

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statutory environmental programmes in line with their business plan commitments.

2.3 Outcomes

2.4 Scheme ODIs

- 2.5 We support Ofwat's proposal to develop a set of principles for the assessment of major schemes as set out on p.25 of the consultation. Given the significance, we believe Ofwat should also carry out an interim review of progress in 2017-18. This should be done in addition to the annual regulatory reporting by water companies.
- 2.6 Major schemes such as the Thirlmere Link and Thames Tideway Tunnel will protect people and the environment and ensure the UK complies with EU Directive requirements. These are large scale projects that involve extended periods of negotiation. If schemes are not delivered, the expected benefits to the environment will be lost and the country will be put at risk of European commission infraction proceedings.
- 2.7 Those major schemes that form part of our National Environment Programme (NEP), will need to be progressed in line with the requirements of the NEP or the Environment Agency's guidance on '*Water Industry Planning: Catchment Measure Specification, Tracking updates to and signing off the PR14 National Environment Programme (NEP)*'.
- 2.8 Where there is inconsistency between major scheme ODI completion dates in the final determination and the NEP, we expect the requirements of the NEP to take precedent. We will be reporting on water company performance ourselves throughout the Asset Management Programme (AMP) 6 period, through our annual Environmental Performance Assessment (EPA).
- 2.9 We agree that there could be cases where water companies deliver the outcomes related to a scheme by finding an alternative, more innovative solution. Water companies are free to decide how they meet their NEP requirements, as long as these solutions provide the same benefits to the environment and customers as they would with the traditional solutions. The delivery will also need to be in accordance with the approach outlined in the guidance '*Water Industry Planning: Catchment Measure Specification, Tracking updates to and signing off the PR14 National Environment Programme (NEP)*'. We would support the adjustment of non-delivery incentives in these cases.
- 2.10 We are happy to provide what support Ofwat require on any assurance around delivery of the NEP or environmental performance.

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3.0 Asset Health / Other ODIs

3.1 We ask that companies are required to publish further information on their ODI's, and present their methodologies to Customer Challenge Groups. This will make the approach more transparent to their customers. We would also like to see this additional information as soon as it becomes available.

3.2 Wholesale water and wastewater costs and revenues

3.3 Wholesale water and wastewater totex

3.4 Wholesale water and wastewater totex allocations cover some important environmental programmes of work including the NEP phase 5 WFD. In reconciling company performance, we would like consideration to be given to the fact that WFD is a multi AMP commitment and that further investment will be required during AMP7 and AMP8.

4.0 Conclusions

We welcome the development of Ofwat's PR14 Reconciliation Rulebook. We broadly agree with the proposals but would like to see reference to the reconciliation rules working in the interests of the environment as well as customers. ODI's remain a developing area and we need to share and learn from each step as evidence becomes clear on how they are working. The publication of more detailed descriptions and methodologies would greatly contribute to this. It is important that the reconciliation process aligns with wider price review reporting such as the EPA and we are happy to continue to contribute in this area where we can.

Further information

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