

CONSUMER COUNCIL FOR



CYNGOR DEFNYDDWYR



# Reliable services for customers - consultation on Ofwat's role in resilience

## 1 Introduction

1.1 The Consumer Council for Water (CCWater) is the statutory consumer organisation representing water and sewerage consumers in England and Wales. CCWater has four regional committees in England and a committee for Wales. We welcome the opportunity to comment on how Ofwat proposes to take forward its duty on resilience.

## 2 Executive summary

- 2.1 We support Ofwat's proposed definition of resilience as it builds on existing definitions in UK and Welsh Government policy and guidance, and it encompasses what we see as key requirements for delivering service resilience.
- 2.2 We believe the resilience of water and sewerage services depends not only on the resilience of each element within the system, but also on the links and communication between these elements. In order to ensure the provision of resilient services, companies need to have a strong relationship with a variety of stakeholders.
- 2.3 We welcome the emphasis on customer engagement with real influence over service provision.
- 2.4 We are pleased with Ofwat's emphasis on the affordability of water and wastewater services in delivering long term resilience - affordability and acceptability should remain key considerations in investment decisions alongside their long term impact. Without high levels of customer acceptability and trust, the water sector will not be resilient.
- 2.5 We support service providers taking ownership of their activities and decisions in relation to resilience, based on customer expectations. This should allow each company to make the most effective and efficient decisions on its own resilience issues.
- 2.6 We support the 'suggested risk-based' approach to resilience, where not every risk to service provision needs to be, or should be, mitigated. Nonetheless, these risks need to be identified, understood and managed in a cost-effective way.
- 2.7 We understand the rationale for not setting sector-wide standards. However, we expect Ofwat to monitor resilience through, for example, core performance ODIs and independent reports on cross-cutting resilience issues. This would demonstrate transparency and enable engagement with customers and stakeholders. It could also provide the basis for incentivising progress on resilience.
- 2.8 We support the principles presented in the consultation<sup>1</sup> (page 26), as they are clearer than those contained in previous Ofwat guidance.
- 2.9 We think resilience will be a big component of Ofwat's forward planning (and work), including:
  - The development of markets through the value chain;
  - PR19;
  - How Ofwat will support the retail market in England;
  - How Ofwat handles investigations;
  - How the information gathered and published by companies will evolve and other issues of importance to customers.

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<sup>1</sup> [http://www.ofwat.gov.uk/regulating/tools/pap\\_con20150708resilience.pdf?download=Download#](http://www.ofwat.gov.uk/regulating/tools/pap_con20150708resilience.pdf?download=Download#)

- 2.10 We think that Ofwat's commitment to 'regulate in a way that promotes the development and better functioning of markets' is appropriate. More specifically we would support an evaluation of how well the new retail market contributes to the overall resilience of the sector, including whether any groups of customers may not be benefiting as much as others.
- 2.11 We would also wish to ensure that the opening up of competition neither discourages investment in important 'resilience' assets, such as reservoirs, nor deters companies from working together on initiatives where these have benefits for customers, the economy and the environment.

### 3 Consultation questions

Q1 Is our basic understanding of resilience aligned with your own - are we addressing the right things in the right way?

#### General views about resilience

- 3.1 We agree that reliability is how most customers view resilience. Customers want to have confidence that a clean, safe drinking water supply will be available when they turn the tap on and that their wastewater will be taken away and dealt with appropriately. Continuity of service over the longer term is a key aspect of resilience. Companies' customer research during PR14 shows that customers also want the environment to be protected (now and for future generations).
- 3.2 Our research<sup>2</sup> indicates that in 2014, 94% of customers were satisfied with their water supply. Satisfaction with sewerage services was at 91%. In addition, the majority of water and sewerage customers were satisfied with value for money - 75% for water and 77% for sewerage.
- 3.3 The same research also shows that customers continue to consider water companies (75%) to be more caring about the service they provide than energy suppliers (69%). Water companies are also ahead in terms of trust - 7.82 (out of 10) compared to 7.42 for energy companies. The energy sector currently has serious customer trust issues, and it is important that trust and satisfaction in water are maintained and improved to ensure a resilient future for the water sector.

#### Affordability

- 3.4 We are pleased with the emphasis Ofwat places on the affordability of water and wastewater services in the delivery of resilience. Our research<sup>3</sup> shows that three quarters (77%) of all customers find water and sewerage charges are affordable to them. This has increased significantly from 67% in 2013.

#### Definition of resilience

- 3.5 We support the proposed definition 'resilience is the ability to cope with, and recover from, disruption, trends and variability in order to maintain services for people and protect the natural environment, now and in the future'; it builds on existing definitions in UK and Welsh

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<sup>2</sup> Water Matters - Household customers' views on their water and sewerage services 2014. A report prepared for CCWater by DJS Research. August 2015. <http://www.ccwater.org.uk/wp-content/uploads/2015/08/CCWater-Water-Matters-2014-Report-FINAL.pdf>

<sup>3</sup> Water Matters - Household customers' views on their water and sewerage services 2014. A report prepared for CCWater by DJS Research. August 2015. <http://www.ccwater.org.uk/wp-content/uploads/2015/08/CCWater-Water-Matters-2014-Report-FINAL.pdf>

Government policy and guidance and it encompasses what we see as key requirements for delivering service resilience. Sitting beneath this, there will need to be a framework that ensures that all aspects of resilience are taken into account by the sector.

- 3.6 We believe the resilience of water and sewerage services depends not only on the resilience of each element within the system, but also on the links and communication between these elements. In order to ensure the provision of resilient services, companies need to have a strong relationship with a variety of stakeholders (such as those listed on page 11 of the consultation). As mentioned above, these relationships should be underpinned by trust and confidence as these drives customers' willingness to pay and, as a result, a secure financial position.

#### Financial resilience

- 3.7 We agree that Ofwat's duty to further the resilience objective has far reaching consequences. While it should focus on water systems and services we agree that it must extend to company finance, governance and management as well as the relationship between customers and their providers.
- 3.8 We agree with Ofwat that, 'it is important that the providers themselves are resilient, financially and corporately, so that they can continue to serve customers'. The financial structure of a company has implications for how resilient it is against cost shocks and extreme events that could affect services or prices to customers. For example, a highly geared company could be averse to more 'risky' innovative solutions as shareholders may resist such options. Similarly, a company's financial resilience could protect it from shocks caused by unexpected changes in the economy protecting its ability to deliver services to customers. We therefore support Ofwat's proposed financial monitoring and the use of 'stress tests' to assess how well company structures can withstand such scenarios.<sup>4</sup>
- 3.9 We know that where companies have complex ownership structures this can undermine trust and confidence in them, particularly when it comes to their tax arrangements. We have been pressing companies to be more open and transparent about their financial arrangements, so that customers have a better understanding of who owns their service provider, where profits go and where ultimate accountability rests. Without customer trust the industry will not be resilient.

#### Ofwat's suggested approach to resilience

- 3.10 We support the 'suggested risk-based' approach to resilience where not every risk to service provision needs to be, or should be, mitigated. Nonetheless, these risks need to be identified, understood and managed in a cost-effective way. In addition, the risk management process should take into account customers' views, priorities and willingness to pay. This is reflected in the example on page 13 of the consultation.
- 3.11 As part of this approach, we agree with Ofwat's view that, from the point of flexible regulation, the regulator needs to see evidence from companies that they have taken customers' views into account. It is also incumbent on the regulator to demonstrate how it has reached decisions on company plans and price determinations so that there is trust and confidence in the regulatory process.

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<sup>4</sup> CCWater's response to Ofwat's consultation on its proposed financial monitoring framework - <http://www.cwater.org.uk/wp-content/uploads/2015/08/CCWater-response-re-Ofwat-financial-monitoring-framework-FINAL.pdf>

Q2 Do you agree with our view of what Ofwat should deliver, including where we might step in and what is for others to deliver?

### Customer engagement

3.12 We strongly agree with Ofwat's commitment (on page 16 of the consultation) that customers must remain at the heart of all decision making. Companies will be expected manage their own risk in delivering customer supported outcomes. There were examples where companies undertook some customer engagement at the last Price Review, e.g. Severn Trent's resilience customer research. It is important that companies are able to confirm local priorities with their customers and that Ofwat's framework allows for this flexibility.

### Transparency and monitoring

3.13 We support the ways in which Ofwat 'might enable, incentivise and encourage resilience in the sector' (the bullet points on page 16 of the consultation). This is particularly true of keeping customers' views 'at the heart of the process', encouraging service providers to take ownership of the delivery of resilient services and long-term planning and adequate investment.

3.14 Stakeholders will continue to rely on Ofwat to share comparative information on company performance in relation to resilience. Local customers and Customer Challenge Groups will need to have access to independent data that allows them to see where their company is positioned in relation to the wider sector. Encouraging companies to strive to improve will only help make them more resilient.

3.15 We feel that although Ofwat appears to avoid prescriptive approaches to regulation (i.e. no standards, no targets), it might still be necessary for Ofwat to require certain core performance related ODIs in business plans for the next Price Review(s).

### Competition and resilience

3.16 Given the changes being brought by competition through the opening of retail markets in England, we feel that Ofwat's commitment to 'regulate in a way that promotes the development and better functioning of markets' is appropriate. Markets can support resilience by ensuring a wider choice of providers and resources, (ideally) allowing greater flexibility and sustainability.

3.17 Ofwat's commitment is also relevant to the regulation of services in Wales where competition will not be extended. Resilience and innovation should also be encouraged in the Welsh policy context and within the new integrated natural resources management framework introduced by the Welsh Government.

3.18 We recommend an evaluation of how well the new retail market contributes to the overall resilience of the sector, including whether any groups of customers (perhaps in areas where the retail market is not so active) may not be benefiting as much as others. An evaluation will also be needed if upstream competition is introduced in the future. For example, creating a market for water resources may help increase resilience by allowing more market participants, possibly encouraging further water trading and fostering innovation. On the other hand, it is vital that uncertainty of return arising from greater upstream competition does not deter timely investment in major long-term assets that will provide further resilience, such as reservoirs.

3.19 We would also wish to ensure that the opening up of competition neither discourages investment in important ‘resilience’ assets, such as reservoirs, nor deters companies from working together on initiatives where these have benefits for customers, the economy and the environment. Regional water resources planning and tariff development are two such activities.

#### Links with ‘Towards Water 2020’

3.20 We support the integrated approach Ofwat is applying to its forward thinking on the way it balances its various duties and regulates the water industry in the coming years. In terms of the resilience of the water industry, we feel that the main topics addressed by the ‘Towards Water 2020’ consultation are a step in the right direction to achieve this.

3.21 *Use of Outcome Delivery Incentives (ODIs)*: As we mention in paragraph 4.5 these, in combination with other tools, can be a way to measure and keep track of what companies are doing in terms of resilience in the short and long-term.

3.22 *Customer engagement*: This will be a key aspect of the work companies plan to do in the future. Only by understanding customers’ priorities, acceptability, willingness to pay and affordability, will companies be on the right track to deliver the outcomes that are important and maintain the trust customers place on them.

3.23 We will be providing detailed comments in response to Ofwat’s Towards Water 2020 consultation in due course.

## 4 Resilience principles and way forward

4.1 We support the principles presented in the consultation<sup>5</sup> (page 26), as they are clearer than those contained in previous Ofwat guidance.

4.2 Resilience should be a big component of Ofwat’s forward planning (and work) in years to come, including development of markets through to the value chain, PR19, how Ofwat will support the retail market in England, how Ofwat handles investigations, how the information gathered by companies will evolve, and other issues of importance to customers.

Q3 What views do you have on how the water and wastewater sector might measure its performance in delivering resilient services - and the best way for us to demonstrate that we are carrying out our role?

4.3 We note Ofwat’s view that, if service providers take ownership of their activities in relation to resilience, then companies will be doing different things in different ways. This is unavoidable.

4.4 The key point is that companies deliver what is right for them, taking into account that ‘resilience is not only about avoiding disruptions. It is about maintaining a quality service for the long term at a price that current and future generations can afford’, as rightly acknowledged by Ofwat. We would expect companies to be transparent to customers and other stakeholders about how they are addressing resilience.

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<sup>5</sup> [http://www.ofwat.gov.uk/regulating/tools/pap\\_con20150708resilience.pdf?download=Download#](http://www.ofwat.gov.uk/regulating/tools/pap_con20150708resilience.pdf?download=Download#)

- 4.5 Therefore, whilst we support Ofwat not setting sector wide standards, we think that monitoring the delivery of resilience could be carried out through a combination of:
- Measuring company performance against ODIs that relate to resilience. These could include<sup>6</sup> (but are not limited to) per capita consumption (including any reductions), water available for use, security of supply, hosepipe ban frequency, the percentage of customers who can be supplied by more than one source, leakage, properties affected by unplanned interruptions, resilient service, value for money, perception of affordability, number of customers helped by review of tariff and social fund, efficient debt management, carbon/energy use reduction, and supplies interrupted due to flooded sites or other instances.
  - Testing the effectiveness of markets and whether the introduction of competition has increased resilience (and to what extent), as well as whether it has allowed and facilitated necessary investment.
  - Ofwat's financial monitoring framework which will test companies' financial structures against 'shocks'.
  - Additional independent reports along the lines suggested in the consultation paper. These reports could ask companies for an assessment of how their service delivery could be affected when modelled against hypothetical scenarios (e.g. weather extremes, economic downturns, increased threat posed by higher risk of terrorism). It would be useful if these reports (or public versions that do not reveal confidential information) are published to show customers and other stakeholders the measures taken and progress made by the sector to increase its resilience.
- 4.6 This would demonstrate transparency and enable engagement with customers and stakeholders. It could also provide the basis for incentivising progress on resilience.

## 5 Concluding suggestions summary

- 5.1 Resilience should be a big component of Ofwat's forward planning (and work) in years to come, including development of markets through to the value chain; PR19; how Ofwat will support the retail market in England; how Ofwat handles investigations; how the information gathered by companies will evolve; and other issues of importance to customers.
- 5.2 Whilst we broadly support the consultation proposals, we would like Ofwat to consider the following key suggestions:
- i. We suggest that Ofwat develops a framework that ensures that all aspects of resilience are taken into account to help deliver what the definition of resilience proposes.
  - ii. We ask Ofwat to consider how it can monitor resilience through, for example, core performance ODIs, financial monitoring in relation to likely 'shocks' to companies and independent reports on cross-cutting resilience issues. This would enable transparency, engagement with customers and stakeholders, and help maintain trust and confidence in the companies and the regulator. It could also provide the basis for incentivising progress on resilience.
  - iii. We ask that Ofwat requires evidence from the companies to show how they have taken customer views into account on resilience, and that Ofwat itself also demonstrates

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<sup>6</sup> Companies already have in place a number of ODIs that are driven by resilience.

how it reaches decisions on future company plans and investment based on this evidence.

- iv. We recommend an evaluation of how well the new retail market contributes to the overall resilience of the sector, including whether any groups of customers may not be benefiting as much as others.
- v. We recommend exploring a way to ensure that the opening up of competition neither discourages investment in important 'resilience' assets, such as reservoirs, nor deters companies from working together on initiatives where these have benefits for customers, the economy and the environment.
- vi. We suggest it is spelt out that resilience risks need to be identified, well understood and managed in a cost-effective way as an essential step of the risk-based approach that the consultation document is advocating.

## 6 Enquiries

Any enquiries to this consultation response should be directed to:

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