

**Ofwat** (The Water Services Regulation Authority) is a non-ministerial government department. We are responsible for making sure that the water and sewerage sectors in England and Wales provide customers with a good quality and efficient service at a fair price.

# Annual report 2008-09

Protecting consumers, promoting value, safeguarding the future



Published by TSO (The Stationery Office) and available from:

**Online**  
[www.tsoshop.co.uk](http://www.tsoshop.co.uk)

**Mail, telephone, fax and email**  
TSO  
PO Box 29, Norwich NR3 1GN  
Telephone orders/general enquiries: 0870 600 5522  
Order through the Parliamentary Hotline Lo-Call: 0845 7 023474  
Fax orders: 0870 600 5533  
Email: [customer.services@tso.co.uk](mailto:customer.services@tso.co.uk)  
Textphone: 0870 240 3701

**The Parliamentary Bookshop**  
12 Bridge Street, Parliament Square, London SW1A 2JX  
Telephone orders/general enquiries: 020 7219 3890  
Fax orders: 020 7219 3866  
Email: [bookshop@parliament.uk](mailto:bookshop@parliament.uk)  
Internet: [www.bookshop.parliament.uk](http://www.bookshop.parliament.uk)

**TSO@Blackwell and other Accredited Agents**

**Customers can also order publications from**  
TSO Ireland  
16 Arthur Street, Belfast BT1 4GD  
Telephone: 028 9023 8451  
Fax: 028 9023 5401



**Ofwat**  
Centre City Tower  
7 Hill Street  
Birmingham B5 4UA  
  
Phone: 0121 625 1300  
Fax: 0121 625 1400  
Website: [www.ofwat.gov.uk](http://www.ofwat.gov.uk)  
Email: [enquiries@ofwat.gsi.gov.uk](mailto:enquiries@ofwat.gsi.gov.uk)

Photographs © Getty Images/Shine Pictures/  
iStockphoto  
Printed on Revive Silk 75, a carbon-neutral  
paper containing 75% minimum de-inked  
post-consumer waste paper

July 2009

© Crown Copyright 2009

[www.ofwat.gov.uk](http://www.ofwat.gov.uk)





## **Annual report 2008-09**

**For the period 1 April 2008 to 31 March 2009**

Presented to Parliament in pursuance of section 192B of the Water Industry Act 1991  
Ordered by the House of Commons to be printed on 16 July 2009

HC 582 London: The Stationery Office £14.35

## About this report

This report outlines the work we carried out in 2008-09 to deliver our strategy.

Our duties are primarily laid out in the Water Industry Act 1991 (as amended). We are directly accountable to Parliament and the National Assembly for Wales.

Further information about our work is available on our website at [www.ofwat.gov.uk](http://www.ofwat.gov.uk).

## Contents

|                            |    |
|----------------------------|----|
| Our strategy               | 4  |
| Chairman's foreword        | 5  |
| Who we are                 | 6  |
| Chief Executive's report   | 7  |
| <br>                       |    |
| 1. Protecting consumers    | 9  |
| 2. Promoting value         | 13 |
| 3. Safeguarding the future | 17 |
| 4. How we do our job       | 21 |
| <br>                       |    |
| Appendices                 | 25 |

© Crown copyright 2009

The text in this document (excluding the Royal Arms and other departmental or agency logos) may be reproduced free of charge in any format or medium providing it is reproduced accurately and not used in a misleading context. The material must be acknowledged as Crown copyright and the title of the document specified.

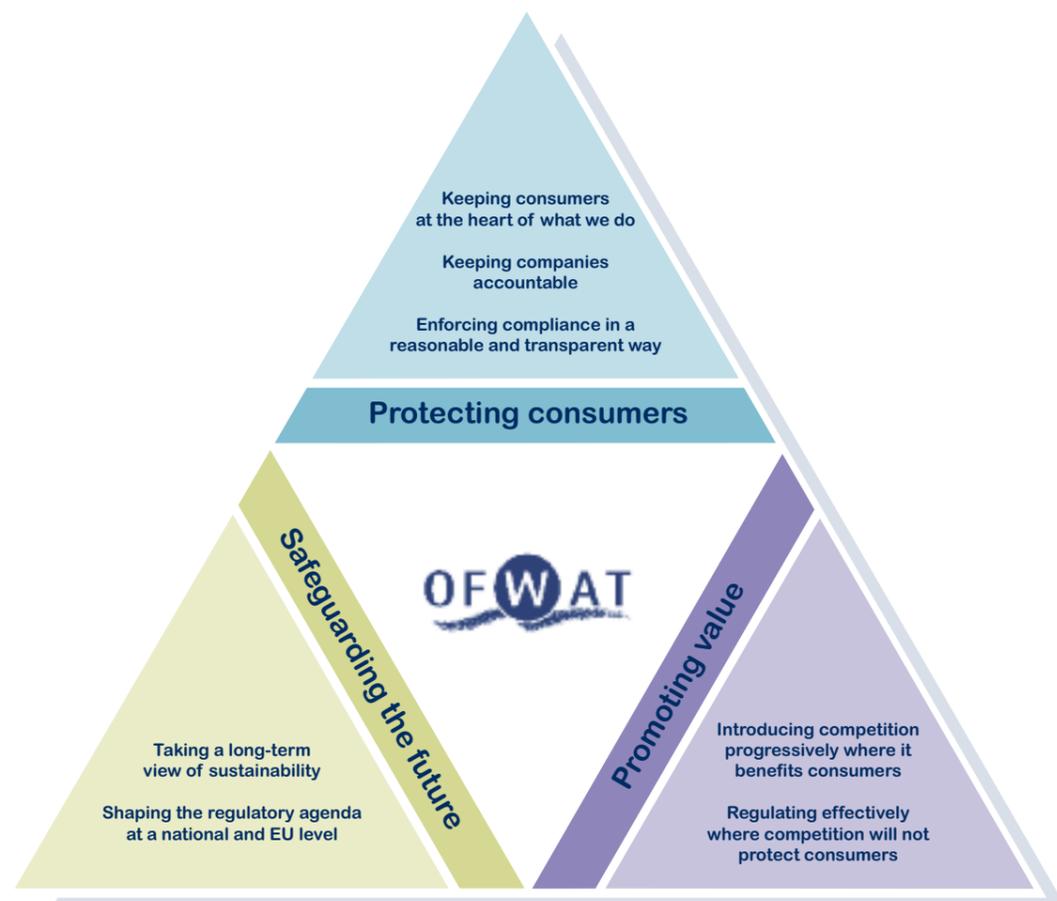
Where we have identified any third party copyright material you will need to obtain permission from the copyright holders concerned.

For any other use of this material please write to Office of Public Sector Information, Information Policy Team, Kew, Richmond, Surrey TW9 4DU or email [licensing@opsi.gov.uk](mailto:licensing@opsi.gov.uk)

ISBN: 978-0-10-295979-6

## Our strategy

We published our [strategy](#) in April 2008. It sets out our priorities for developing economic regulation of the water and sewerage sectors in England and Wales over the long term. It also describes how we will protect consumers, promote value and safeguard the future. This aim, and the priorities that relate to it, are illustrated below.



## Chairman's foreword

We published our [strategy](#) at the start of the 2008-09 reporting year. Since then, we have put in place many of the building blocks to implement the strategy.

Our job is to protect consumers. The most important lever for doing so since the sectors were privatised has been the cap we set every five years on water and sewerage prices. There have been big improvements in the past 20 years in service, drinking water quality and environmental enhancements. And while these improvements have come at a cost, average water bills today are still about £100 lower than they would have been without Ofwat's efficiency challenge to the water companies.

In 2008, we required the companies to focus first on the need to plan for the long term by preparing 25-year [strategic direction statements](#). These took account of our developing understanding of climate change and the need to protect the environment, as well as making sure customers receive value for money.

We tested the companies' proposals in consultation with the environmental and quality regulators, and the Consumer Council for Water. We have also tested the detailed proposals in the companies' [final five-year business plans](#). We will set out our response when we publish our draft price limits in July, and final price limits in November 2009.

Despite improvements, it is increasingly clear that relying on top-down regulatory instruments to protect consumers is not going to deliver the best value to them forever. So, over the year we have urged the Government, Parliament and the Welsh Assembly to change the statutory regime to deliver even better value. In particular, we want the flawed statutory regime for introducing market signals into water pricing improved. We also want to encourage vigorous debate on the best means of charging for

water in a way that will deliver social, environmental and economic benefits. We have welcomed the open response we have received.

We also welcome the Government's establishment of independent reviews on competition and innovation and on social aspects of water charging, carried out by Professor Martin Cave and by Anna Walker, respectively. We have significantly increased our own capacity to develop such proposals and respond to the increasing sophistication and complexity of economic regulation.

### We want to encourage debate on the best means of charging for water

In preparing for the future, we have also tackled the issues of the present. As Regina Finn's report shows, we have enforced penalties for breaches of regulatory requirements, monitored the companies' delivery of their obligations closely and pressed for improvements in customer service where these have been lacking.

I am grateful to my colleagues on the Ofwat Board who have worked hard to protect consumers, promote value and safeguard the future. And I pay tribute to the work of Regina Finn and Ofwat staff. They have tackled the task of implementing our strategy with skill and determination. We look forward to the continuing challenges of the future.

**Philip Fletcher**  
Chairman

## Who we are

### Board



**Philip Fletcher**  
Chairman



**Regina Finn**  
Chief Executive



**Penny Boys**  
Non-executive  
Director



**Michael Brooker**  
Non-executive  
Director



**Peter Bucks**  
Non-executive  
Director



**Jane May**  
Non-executive  
Director



**Gillian Owen**  
Non-executive  
Director



**Keith Mason**  
Director of  
Regulatory Finance



**Cathryn Ross**  
Director of  
Markets

### Executive

**Regina Finn**  
Chief Executive

**Rob Ashley**  
Interim Director  
of External  
Affairs

**Huw Brooker**  
Director of Legal  
Services and  
Secretary to the  
Board

**George Day**  
Director of  
Network  
Regulation

**Andrew Dunn**  
Director of  
Consumer  
Protection

**Roger Dunshea**  
Director of  
Operations

**Keith Mason**  
Director of  
Regulatory  
Finance

**Cathryn Ross**  
Director of  
Markets

## Chief Executive's report

The past year has been a difficult one. The economic downturn has created financial worries for everyone. Protecting the services that water customers receive and the bills they pay has never been more critical. We have worked to do this for customers now and in the next five-year period. Our focus is also on delivering sustainable water services now and in the long term.

We have held the companies to account for the service they give customers. In 2008-09, we took enforcement action against monopoly companies that failed to meet their obligations and their customers' expectations. For example, we imposed penalties and secured redress for customers of more than £70 million. Our new customer service measures will drive the companies to improve further. In our [contribution](#) to the Walker review of charging and metering, we restated our belief that charges should be cost-reflective.

To inform the price limits we set for 2010-15, we carried out [joint customer research](#) for the first time with seven stakeholders, including the Consumer Council for Water. This has allowed us to keep consumers' views and interests at the heart of the price-setting process. We developed new regulatory tools for this price review, such as the [capital expenditure incentive scheme](#) and the revenue correction mechanism. These give the companies an incentive to improve their performance even after we have set final price limits in November 2009.

Although the price review has been our focus for the past year, we are not standing still. We are finding creative ways to address the future challenges of population growth and climate change against a backdrop of economic pressures. The Water Innovation Platform we are developing with the Technology Strategy Board will help fund innovation in the water and sewerage sectors.

We aim to give the companies the right incentives to deliver the solutions and services customers want. Companies and customers need to understand the value of water in their area so that charges can be fair and transparent. That is why we are exploring the role of markets, working closely with the Cave review of competition and innovation in water markets. Our work to uncover the value of water included steps to separate accounting.

This year, we published our [climate change policy statement](#), and other guidance, on how the companies can adapt to and mitigate against changing weather patterns. We also required the companies to report on their carbon emissions for the first time, encouraging them to take responsibility for their actions. We welcomed Sir Michael Pitt's [report](#) and recommendations on how society should deal with flood risk.

### Protecting the services that water customers receive and the bills they pay has never been more critical

We worked closely with stakeholders this year, including the Government to develop the [draft Flood and Water Management Bill](#), and the Environment Agency on a [review](#) of abstraction rights trading.

I would like to thank our stakeholders for their continued contribution to our work.

Finally, I would like to thank my colleagues for their dedication in continuing to protect consumers, promote value and safeguard the future.

**Regina Finn**  
Chief Executive

## 1. Protecting consumers

We made good progress in preparing for the 2009 price review (PR09) where we will set price limits for the companies we regulate for the period 2010-15. We will publish our draft price limits for consultation in July, and final limits in November 2009. As part of this work, our approach to protecting consumers included:

- challenging the companies' business plans, and making sure that they were based on sound evidence, including customers' willingness to pay; and
- jointly commissioning research into consumers' views of water and sewerage services. This informed the companies' final business plans and will be taken into account when we set price limits.

In March 2009, we published our approach to enforcement (see 'A case study: securing compliance and changing behaviours' on page 11). This outlined how we will use our powers to protect consumers' interests where companies fail to comply with their obligations. In 2008-09, we took action and sought redress for customers where

companies had not provided us with reliable, accurate and complete data.

We fined Severn Trent Water £35.8 million. This was in response to the company's deliberate misreporting of customer information and failure to deliver a minimum standard of service. We also fined Tendring Hundred Water £42,000 for misreporting information. In each case, we made sure that customers received recompense and that the companies did not benefit from the misreporting.

During the year, we completed an investigation into deliberate misreporting of information on bills for metered customers at Three Valleys Water. We could not impose financial penalties because of statutory time restrictions. However, the company has established a charitable fund to help customers who are having difficulty paying their water bills. This is in recognition of the damage to its customers and to the integrity of systems we use to regulate. The company also reduced its price limits to return money to customers that it should not have received as part of the 2004 price review.

Keeping consumers at the heart of what we do • Keeping companies accountable • Enforcing compliance in a reasonable and transparent way



**24,121**

The total number of customers who successfully applied for a 'Watersure' tariff in the last reporting year (2007-08). The tariff protects customers with a water meter, and who meet certain conditions, from high water bills.



**£35.8 million**

The amount we fined Severn Trent Water for deliberately providing false information to us and for delivering poor service to its customers.

**“We need sustainable charging policies so that we can achieve the sustainable services that consumers want. Publishing our future strategy for customer charges this year was a key part of this.”**

**Andrew Dunn**  
Director of Consumer Protection

In September 2008, we secured a legal agreement from United Utilities to address problems at properties in the Penketh area of Warrington that were affected by sewer flooding. We are monitoring progress. We also took action against the company in a number of other areas.

- In response to our concerns about the company's processes, United Utilities has put in place new systems to investigate and record sewer flooding incidents. A third party will check that these systems are robust.
- The failures in its systems and processes led to United Utilities misreporting information on the number of sewer flooding incidents and the number of properties on its 'at risk' registers. The company has agreed to invest in engineering solutions to help mitigate the sewer flooding problems faced by all the customers whose properties are now on the 'at risk' registers. Shareholders will meet this cost. United Utilities is also providing payments, under the guaranteed standards scheme, to customers who were entitled to them but did not receive them.
- Early in 2008, a consultant provided evidence that United Utilities had in the past identified increases in business rateable values and backdated charges to reflect those values. We investigated and found that United Utilities had not accurately reported this activity to us. As a result, the company has agreed to continue to offer refunds to customers whose rateable value has reduced, plus an additional 10%.

During the year, we received more than 400 complaints about companies' proposals to charge non-household customers for surface water drainage on a site area basis. More than 75% of these complaints were from United Utilities' customers. Most complaints were from representatives of churches and sports clubs.

United Utilities has acknowledged it made mistakes affecting some customers in implementing the change to its system of charging. These errors led to confusion and inconvenience for the customers concerned. We were pleased that the company decided to suspend the charge for one year for places of worship, certain sports clubs, and Scout and Guide Association properties at its own expense, in order to work more closely with customers to explain the benefits of the change.

In November 2008, we rejected Sutton & East Surrey Water's application to raise its prices by an average of 10.2% (before inflation) in 2009-10. The increase would have resulted in higher bills for more than 250,000 customers. The case has now been referred to the Competition Commission.

We published our [future strategy for customer charges](#) for water and sewerage services in August 2008. This is to encourage the companies to develop charging systems that help consumers understand the value of the water they use. We also approved several tariff trials to test some innovative forms of charging. These included Dŵr Cymru's Water Direct and Water Collect schemes, which aim to help eligible customers to pay their bills.

During the year, we updated our [guidance](#) on the help companies should offer disabled or elderly consumers. Examples of the special assistance that companies provide include password schemes to prevent bogus callers and providing bills in large print or Braille. We also published [guidelines](#) to strengthen the companies' procedures when dealing with customers who are affected by sewer flooding.

Other work this year included:

- piloting new ways to [measure](#) customers' experience when dealing with their company.

These measures will form part of a revised approach to drive further improvements in customer service;

- checking and approving the companies' [charges](#) for 2009-10; and
- working with the Welsh Assembly Government, the PR09 Forum for Wales and other Welsh stakeholders. We have built positive relationships which support the continued protection for Welsh consumers within the context of a devolved administration.

## Protecting consumers: a case study

### Securing compliance and changing behaviours

In competitive markets, customers can choose alternative suppliers if they do not receive the service they pay for, or if the company fails to deliver in some other way. In the water and sewerage sectors most customers have no choice of supplier, so it is our role to protect their interests.

We expect each company to deliver the high-quality, sustainable services that their customers expect, and at a fair price. If a company does not do this, we take action.

Our [approach to enforcement](#), which we published this year, will ensure that the companies are clear about the action we will take if they fail to deliver. Companies should comply with their statutory obligations and change their behaviours where necessary in order to do so.

We investigate in cases where the companies may not be meeting the standards required. The action we take depends on the nature, seriousness and impact of the failure. A key feature of our approach is to restore any harm caused to customers. We also use our fining powers for the most serious failures.



During 2008-09, we conducted investigations and took enforcement action at a number of companies. This included imposing fines and securing redress for customers of more than £70 million.

**Ingrid Olsen**  
Head of Enforcement Policy



## 2. Promoting value

As part of our preparations for the 2009 price review, our approach to promoting value included:

- challenging each company's draft capital investment proposals to make sure that they provided value for money for customers and the environment. This included publishing a [draft baseline](#) for the capital expenditure incentive scheme in December 2008 (see 'A case study: encouraging fresh thinking and new ideas' on page 15);
- challenging each company's draft cost base submission. This includes estimates of what they will need to complete a range of standard projects, helping us to compare costs across the water and sewerage sectors;
- publishing a [report](#) on the likely scope for efficiency improvements in the water and sewerage sectors between 2010 and 2025. We will take account of these

findings, among other evidence, to inform the efficiency assumptions that we make at the review; and

- working with the Environment Agency and Drinking Water Inspectorate to identify the most cost-effective and cost-beneficial solutions to meeting environmental and drinking water quality improvements, and legislative requirements.

We also worked with the Technology Strategy Board to develop initial proposals for a Water Innovation Platform. As well as delivering other benefits, this could provide funding to support innovation within the water and sewerage sectors over the next decade.

In May 2008, we published the [second part of our review of competition](#) in the water and sewerage sectors. In it, we recommended that parts of the water and sewerage market should be opened up to competition where this would benefit consumers, including

Introducing competition progressively where it benefits consumers · Regulating effectively where competition will not protect consumers



**8.1%**

Water companies in England and Wales invested £4.9 billion in the last reporting year (2007-08) into maintaining assets and investing in new facilities – an 8.1% increase on the previous year.



**32**

We received 32 applications for new appointments in 2008-09, compared with only five in 2007-08. New appointments are where a licensed water or sewerage company replaces another to serve customers in a specific area of England and Wales.

“The sectors we regulate face many challenges. We need better, more flexible regulation to deliver the sustainable solutions we need – and that includes harnessing market forces.”

**Cathryn Ross**  
Director of Markets

greater choice and innovations in service delivery. We also set out the work we will be doing to make this happen.

In addition, we contributed to the Government’s independent review of competition and innovation in water markets, led by Professor Martin Cave (the ‘Cave review’). This included publishing our [response](#) to the Cave review’s interim report in December 2008.

As part of this, we worked with the Environment Agency to improve abstraction rights trading. This is where licences to abstract water are traded on a market, thus revealing information about the relative environmental, social and economic value of water taken from different locations. This is vital to send efficient signals about where innovation and investment is needed to ensure sustainable services to customers. We submitted a [joint summary](#) with the Environment Agency to the Cave review about this work.

This year, we approved four applications for new appointments. This included applications from two new companies, one of which will use low-carbon, on-site sewage treatment to deliver sewerage services to a village in Hampshire.

In September 2008 and March 2009, we consulted on the [first](#) and [second](#) phases of our approach to implementing formal accounting separation for the companies we regulate. Accounting separation will require each company to produce clear information about separate parts of its business. Having a greater understanding of costs can bring benefits to consumers as it helps inform regulation and reveals opportunities for competition and innovation.

Finally, we published revised [guidance](#) for competition in providing water mains. This extends the scope to allow self-lay organisations to make service pipe connections to appointed companies’ water mains. It should make this market more competitive.

## Encouraging fresh thinking and new ideas

To overcome the many new challenges they face over the coming years, the companies will need to find innovative ways to deliver services. For our part, we shall need to regulate in a way that encourages innovation while continuing to make sure that the companies deliver sustainable services to consumers.

For these reasons, we have developed a capital expenditure incentive scheme (CIS) for PR09. Capital expenditure is the investment the companies need to make to enhance capacity, improve services to consumers, and maintain and renew their infrastructure and other assets.

Capital investment accounts for the majority of customers’ bills. So, it is important that they get the best possible deal from this. We challenge the companies to deliver this investment effectively and efficiently. The CIS does two things.

- It encourages the companies to submit challenging business plans to us, based on realistic information on what they need to invest.
- It gives the companies financial incentives to continually seek out more efficient ways of delivering their investment programmes effectively. The companies keep the rewards until we next set price limits; they are then returned to customers through lower bills.

Much of our work this year has focused on the analysis and challenge that is required for us to deliver the CIS. It will form a key part of our final decisions on price limits in November 2009.

Each company submitted its [draft business plan](#) to us in August 2008. We reviewed and challenged these plans, and published the initial results of our analysis in ‘[Capital expenditure for 2010-15: Ofwat’s view on companies’ draft business plans](#)’ in December 2008. As a new stage in the process of setting price limits, this gave the companies our view of their investment plans at an earlier stage than ever before.

We concluded that the companies did not provide sufficient evidence or justification for about 30% of the £24.7 billion investment they proposed. As well as allowing the companies to focus on what they needed to improve for final business plans, publishing this information enabled them to plan their investment with greater clarity. This is important as it can take years to deliver some assets. It also helps the companies maintain sustainable supply chains by avoiding sharp increases or decreases in their expenditure. This benefits consumers as it leads to fewer delays and more efficient investment.



**Helen Twelves**  
Head of Comparative Efficiency



### 3. Safeguarding the future

Our approach to safeguarding the future as part of our PR09 work this year included:

- introducing **targets** for increased water efficiency savings from the companies. We expect the companies to increase water efficiency savings by 40%, in addition to the savings we expect them to make from their leakage targets and through increased metering;
- reviewing and challenging each company's draft and final 25-year water resource management plans (which we published in **advice** to Defra). These set out how the companies intend to provide sufficient water to meet their customers' needs;
- working closely with the Environment Agency to produce updated **guidance** for companies on planning water resource investments;
- publishing **guidance** on how the companies should take the risk of flooding and climate change into account. This will

enable them to improve the resilience of their services transparently and systematically;

- analysing the carbon implications from the companies' draft business plan submissions. We expect each company to play its part in mitigating climate change by taking carbon emissions into account when planning investments; and
- publishing **guidance** for the companies on using renewable energy. This is so that we can be sure consumers will benefit from the appropriate use of renewable energy generation and are not subject to undue costs or risks.

In July 2008, we published a comprehensive **policy statement** on climate change and its impact on the water and sewerage sectors in England and Wales. In addition, to encourage the companies to take ownership and responsibility for their greenhouse gas emissions, we collected and reported on each company's emissions. During the year, we also participated in UK Water Industry

#### 4.5 million tonnes

The amount of carbon dioxide equivalent greenhouse gases that the statutory companies we regulate released into the atmosphere in the last reporting year (2007-08). This was the first time we collected this data.

#### 40%

The increase in water efficiency savings we expect the companies to make by 2015, based on the targets we published during 2008-09.

“We focused on some major challenges this year, including climate change, sustainability and water efficiency. We want sustainable water services for consumers.”

**George Day**  
Director of Network Regulation

Research (UKWIR) and Environment Agency carbon steering groups, and the UKWIR climate change framework project. This is to help improve the companies' knowledge about approaches to climate change adaptation and mitigation.

- implementing adaptation reporting powers from the Climate Change Act; and
- financing the Thames Tideway scheme. This is one of the largest single capital investment projects since privatisation.

We reinforced our commitment to our sustainability duty when we published 'Water today, water tomorrow – Ofwat and sustainability' at our 'Sustainable water' event in March 2009. This document sets out our broad approach to regulating in a way that allows the companies to deliver sustainable water services for consumers. At the event, we discussed with our key stakeholders how the water and sewerage sectors can deliver sustainability over the long term.

This year also saw us contributing to high-level government policy development in a number of areas, including:

- the Walker [review](#) of charging and metering for water and sewerage services;
- the Cave [review](#) of competition and innovation in water markets;
- developing the Flood and Water Management Bill;

## Adapting to and helping to mitigate climate change

The water and sewerage sectors are particularly vulnerable to the impacts of climate change. Almost every area of the companies' operations will be affected. From collecting raw water to disposing of sewage, the implications of climate change need to be understood and considered in a long-term, sustainable context.

To adapt effectively, the companies need to take into account both the impacts of climate change and the uncertainty of predictions. As high energy users, they also have a part to play in mitigating the effects of climate change by taking responsibility for their own emissions.

There are a number of areas where greater clarity and guidance is required. We recognise this, and much of our work this year has focused on addressing this need. 'Preparing for the future – Ofwat's climate change policy statement', which we published in July 2008, formed the central part of this guidance. It set out the key areas where climate change will affect the water and sewerage sectors, and what we have been doing – and plan to do in the future – to meet the challenges ahead. It also set out our views on the companies' responsibilities.

Our approach to climate change policy aims to bring multiple benefits.

- Our guidance should empower the companies to make strong cases for investments related to climate change. We have already seen some good cases set out in the companies' [draft business plans](#).
- We want to make sure that the way we regulate is effective for the challenges ahead. Our approach is helping to reveal the additional work that needs to be done.
- We aim to influence and shape wider government climate change policies. Our approach provides an evidence base to inform the debate on national and European levels so that the water and sewerage sectors deliver effective responses to climate change.

Primarily, however, our approach – and our work this year – has been to make sure that the companies understand and take ownership of the key issues. We expect each company to adopt a phased approach to climate change adaptation and mitigation which considers both the long- and short-term context. This means that future investment proposals need to be based on sound evidence and take uncertainties into account.



**Dr Mike Keil**  
Head of Climate Change Policy



## 4. How we do our job

As part of our PR09 work, during 2008-09 we:

- published detailed [reporting requirements](#) for the companies' submissions to us;
- provided regular and detailed feedback on the submissions; and
- developed our [financial model](#) and made it publicly available.

These activities have helped to improve the quality of the companies' submissions to us and the level of transparency for all our stakeholders. In addition, following publication of the Hannigan [report](#) on 'Data Handling Procedures in Government', we strengthened our information security policy. Our development team has produced a new integrated business plan capture system and financial model that underpins all aspects of PR09.

During the year, we also set up a new Markets Division to help deliver our strategic priority of introducing competition

progressively where it benefits consumers. Cathryn Ross was appointed Director of this division in July 2008. Also in July, we made a second new appointment to our senior management team, when George Day became Director of Network Regulation.

We want to be sure that we have the right people, with the right skills, in place. To that end, we launched a specific microsite for recruitment ([www.jobsatofwat.org.uk](http://www.jobsatofwat.org.uk)).

The way we develop our staff is important to us (see 'A case study: developing our people' on page 23). For example, most of our directors and team leaders have completed the Institute of Leadership and Management (ILM) level 5 development programme. In addition, all staff took part in a development programme to improve planning, team working and internal communications. We also continued to run our highly successful graduate training scheme.

We continued to be an 'Investor in People'. This includes supporting a range of



**75p**

The amount we cost each customer in England and Wales in 2008-09.



**20 years**

2009 is our 20th year as the regulator of the water and sewerage sectors in England and Wales. Since the companies were privatised in 1989, levels of service to customers have improved significantly and leakage has fallen by more than a third.

“Over the past year we have delivered a number of key pieces of work to support the delivery of our strategy – including a cross-office development programme to strengthen communication and team work.”

**Roger Dunshea**  
Director of Operations

development programmes, including specialist regulatory courses. Looking ahead, in 2009-10, we will initiate a postgraduate award in competition economics in partnership with the University of Warwick.

Other work this year has included:

- improving our business continuity arrangements, by setting up a new off-site recovery office and reviewing our business continuity plan;
- developing a new business planning process which aligns resources to delivering our strategy;
- participating in the West Midlands Travel Wise scheme (increasing the number of colleagues who travel to work by public transport); and
- continuing to promote recycling across the office.

Our new strategy required a step change in our budget compared with 2007-08. This is explained in appendix 6 on page 32.

The main drivers for this were:

- setting up the new Markets Division; and
- enforcement action.

Our expenditure in 2008-09 of £14.9 million represented an underspend of £3 million against budget. The main reason was that contingency provision against litigation was not required. Some projects were deferred to 2009-10.

The underspend will be used to either offset future licence fees or as a contingency for major unplanned cost pressures.

## Developing our people

As an organisation we are going through a very exciting time. The companies we regulate are facing significant challenges and our regulation must be flexible enough to ensure that they meet these challenges. Our strategy sets out how we will develop economic regulation in the water and sewerage sectors over the long term. To deliver this, we need to develop our main asset – our colleagues.

Part of this is about making sure we recruit the right people. This year, we developed a new recruitment website to target top-quality professional candidates for a number of roles. Our small London office, which we set up during the year, means we can offer more flexible careers than ever before.

Another important part is developing the skills we already have. During the year, most of our directors and team leaders took part in a skills development programme. This has helped to develop leadership practice within the office. Following this, all staff have received training on key elements of the programme. The benefits have included:

- reinforcing the idea of common purpose across the organisation;
- building and applying learning to improve our performance and help us to deliver our strategy;
- strengthening the relationships between colleagues across the office; and
- helping to improve communication.

To help with succession planning and to develop aspiring or practising line managers for the future, we now offer colleagues the opportunity to take the ILM Certificate in First Line Management (level 3).



Next year, we will again seek Investors in People reaccreditation. We are committed to continuously learning from experience and to developing our people.

**Elizabeth Davidson**  
Head of Human Resources

## Appendix 1: How we performed during 2008-09

In 'Ofwat's strategy – taking a forward look', we set out a number of specific actions for the 2008-09 financial year. The table below shows our performance.

| Section   | Comments  |
|---|---|
| Keeping consumers at the heart of what we do                        | <p>We completed most of our work as planned. However, during the year some of our planned work was changed, delayed or no longer deemed necessary.</p> <p>We will carry out research into customer priorities to inform our review of consumer service incentives in 2009-10.</p> <p>We will contribute to the Government's review of future consumer representation for water when it is announced.</p> <p>We are considering the consumer literature we publish as part of the ongoing development of our website.</p>  |
| Keeping companies accountable                                       | <p>We completed or continued with most of our work as planned. However, there were two changes.</p> <p>We are developing and will consult on a strategic framework for keeping companies accountable that minimises regulatory burdens.</p> <p>We will publish each company's 2008-09 regulatory information soon after it is submitted in June 2009.</p>   |
| Enforcing compliance in a reasonable and transparent way            | <p>We published our <a href="#">approach to enforcement</a> in March 2009. We will consult on our review of our policy on financial penalties in 2009-10.</p>   |
| Introducing competition progressively where it benefits consumers   | <p>We completed or continued with most of our work as planned. We have started making improvements to the new appointments application process and expect to implement further reforms in 2009-10.</p>  |
| Regulating effectively where competition will not protect consumers | <p>We completed or continued with most of our work as planned. But instead of producing an innovation policy statement, we set out our policy in our published <a href="#">responses</a> to the independent Cave review of competition and innovation in water markets.</p>   |
| Taking a long-term view of sustainability                           | <p>We completed or continued with most of our work as planned. However, there were three changes.</p> <p>We commissioned a consultant to review the case for an alternative methodology for setting leakage targets, but concluded that it would not improve upon the current approach. We published our findings, with the consultant's report, in <a href="#">PR09/16</a>, 'Cost base feedback report'.</p> <p>Instead of publishing environmental and social policies, in March 2009, we published '<a href="#">Water today, water tomorrow – Ofwat and sustainability</a>' – an update of our approach to sustainable development.</p> <p>We will publish details of a systematic review of companies' sewer flooding 'at risk' registers in 2009-10.</p> |
| Shaping the regulatory agenda at a national and EU level            | <p>We completed or continued our work as planned.</p>   |

## Appendix 2: Having regard to the social and environmental guidance from Government

Under the Water Industry Act 1991 (as amended), the Secretary of State for Environment, Food and Rural Affairs and the Welsh Assembly Government have powers to issue separate social and environmental guidance to Ofwat (The Water Services Regulation Authority). We are required to have regard to both sets of guidance when discharging our statutory functions.

The Secretary of State published his final, statutory social and environmental guidance to us on 22 September 2008. The Welsh Assembly Government published its guidance on 23 February 2009.

Both the Secretary of State and the Welsh Assembly Government have made it a requirement that we demonstrate in our annual report each year how we have contributed to delivering the policies set out in their respective sets of guidance. The tables below show how we met this requirement in 2008-09.

### Guidance from the Secretary of State for Environment, Food and Rural Affairs

| Policy area                   | Example of contribution  |
|-------------------------------|--|
| Sustainable development       | 'Water today, water tomorrow – Ofwat and sustainability' (March 2009)  |
| Future water                  | 'Setting price limits for 2010-15: Framework and approach' (March 2008)  |
| <b>Social policies</b>        |  |
| Fairness and affordability    | 'Ofwat's future strategy for customer charges for water and sewerage services: consultation conclusions' (August 2008) |
| Competition                   | 'Ofwat's review of competition in the water and sewerage industries: Part II' (May 2008)                               |
| Better regulation             | See appendix 4 (page 29)   |
| <b>Environmental policies</b> |  |
| (Climate change) mitigation   | 'Preparing for the future – Ofwat's climate change policy statement' (July 2008)                                       |
| (Climate change) adaptation   | 'Preparing for the future – Ofwat's climate change policy statement' (July 2008)                                       |
| Supply/demand balance         | 'PR09/20: Water supply and demand policy' (November 2008)  |
| Surface water flooding        | 'Surface water drainage charges: the current position' (web pages)   |
| Resilience                    | 'PR09/12: Asset resilience to flood hazards: development of an analytical framework' (June 2008)                       |
| Water quality                 | 'Setting price limits for 2010-15: Framework and approach' (March 2008)  |

### Guidance from the Welsh Assembly Government

| Policy area  | Example of contribution   |
|--|---|
| Sustainable development  | 'Water today, water tomorrow – Ofwat and sustainability' (March 2009)   |
| Long-term viewpoint  | 'Setting price limits for 2010-15: Framework and approach' (March 2008)   |
| Corporate social responsibility  | 'Water today, water tomorrow – Ofwat and sustainability' (March 2009)   |
| Company reporting (better regulation)  | See appendix 4 (page 29)  |
| Community engagement and consultation  | 'Understanding customers' views – PR09 quantitative research into customers' priorities for the Water Industry Stakeholder Steering Group' (February 2009)  |
| Economic development   | We are working with the Technology Strategy Board (TSB) on developing an Innovation Platform for water. See <a href="http://www.innovateuk.org">www.innovateuk.org</a> for details of the TSB's work. |
| Wider social responsibilities  | 'Setting price limits for 2010-15: Framework and approach' (March 2008)   |
| Water affordability  | 'Setting price limits for 2010-15: Framework and approach' (March 2008)   |
| Metering and charging  | 'PR09/20: Water supply and demand policy' (November 2008)   |
| Charging   | 'Ofwat's future strategy for customer charges for water and sewerage services: consultation conclusions' (August 2008)  |
| Competition  | 'Ofwat's review of competition in the water and sewerage industries: Part II' (May 2008)  |
| Environmental policies   | 'Water today, water tomorrow – Ofwat and sustainability' (March 2009)   |
| Environment strategy   | 'PR09/20: Water supply and demand policy' (November 2008)   |
| Climate change   | 'Preparing for the future – Ofwat's climate change policy statement' (July 2008)  |
| Emission reduction and preserving carbon stores  | 'Preparing for the future – Ofwat's climate change policy statement' (July 2008)  |
| Adapting to impacts of climate change  | 'Preparing for the future – Ofwat's climate change policy statement' (July 2008)  |
| Supply/demand balance  | 'PR09/20: Water supply and demand policy' (November 2008)   |
| Water efficiency   | 'PR09/20: Water supply and demand policy' (November 2008)   |
| Leakage  | 'PR09/20: Water supply and demand policy' (November 2008)   |
| Floods and resilience  | 'Setting price limits for 2010-15: Framework and approach' (March 2008)   |
| Surface water flooding and the new approaches programme for flood and coastal risk management in Wales | 'Ofwat's response to Defra's consultation on improving surface water drainage' (March 2008)   |
| Resilience to natural hazards  | 'PR09/12: Asset resilience to flood hazards: development of an analytical framework' (June 2008)  |
| Maintaining and improving standards of water quality   | 'Setting price limits for 2010-15: Framework and approach' (March 2008)   |
| Water company partnerships working with land managers  | 'Setting price limits for 2010-15: Framework and approach' (March 2008)   |



## Appendix 3: List of impact assessments carried out during 2008-09

| Date of publication | Document  |
|---------------------|---|
| 4 May 2008          | <a href="#">Ofwat's review of competition in the water and sewerage industries: Part II (draft impact assessment)</a>                                     |
| 28 August 2008      | <a href="#">Ofwat's future strategy for customer charges for water and sewerage services: consultation conclusions (final impact assessment)</a>          |
| 31 October 2008     | <a href="#">Guidance on financial arrangements for self-lay and requisitioning agreements – version 2.0: consultation paper (draft impact assessment)</a> |
| 19 November 2008    | <a href="#">Water efficiency targets 2010-11 to 2014-15 (final impact assessment)</a>   |
| 13 March 2009       | <a href="#">Accounting separation – consultation on June return reporting requirements 2009-10 (draft impact assessment)</a>                              |

## Appendix 4: Progress in reducing regulatory burdens

The Government introduced the Regulatory Enforcement and Sanctions Act 2008 for the purposes of delivering better regulation. The Act placed a duty on us to:

- review the regulatory burdens we impose;
- reduce any that are unnecessary and unjustifiable; and
- report on our progress each year.

When we report on progress, we have to set out what we have done in the past 12 months, and what we will do in the coming 12 months, to review our functions in line with the duties set out above. We also have to set out the reasons for maintaining any unnecessary burdens.

Our forward programme sets out what we intend to do over the coming 12 months. Our report on what we have done in the past year is set out below.

### Report on progress

In our '[Forward programme 2009-10 to 2011-12](#)' (March 2009), we committed to develop and consult on a strategic framework for keeping companies accountable in the next three-year period. This work also includes a review of the information we collect from the companies.

We want to be sure that the companies are accountable to their customers and comply with their duties. The framework will minimise the regulatory burden in line with the better regulation principles of transparency, accountability, proportionality, consistency and targeting. It will also allow for the development of competition in the water and sewerage sectors.

## Appendix 5: Performance against our stated levels of service

### Improving performance

Every year, we respond to thousands of general public enquiries for information. We also investigate hundreds of disputes between customers and their water companies. Our customer charter sets out our targets for responding to customers in a timely way.

We are disappointed to report this year that we have failed to meet most of our targets. This was because of an unexpected increase in the number of complaints during 2008-09.

To help improve our performance, we have made organisational changes to merge this work into a single team and recruit additional staff. The new team is working with our internal auditors to enhance their systems and processes. We will also procure a new IT system to help manage and report this work.

### General enquiries

In 2008-09, we dealt with almost 10,000 telephone enquiries (over 160% more than in 2007-08). We also replied to more than 1,300 written enquiries.

| Standard  | Achieved |
|---|----------|
| 95% of written enquiries to be dealt with within ten working days | 69%      |

### Disputes and complaints

The Consumer Council for Water (CCWater) represents consumers in the water and sewerage sectors. It deals with most complaints from consumers about the service their water or sewerage company provides, which the company itself cannot resolve. We support CCWater's complaint handling role by providing advice on individual cases and by contributing to workshops.

Disputes and complaints we are responsible for:

- complaints about regulatory policy;
- allegations of breach of duty by a company;
- water supply and sewer connection charges;
- requisitioning of water mains, sewers and lateral drains;
- adoption and financial arrangements in respect of self-laid mains;
- sewer appeals;

- refusals by companies to install an optional meter;
- guaranteed standards scheme (GSS) payments;
- trade effluent appeals; and
- pipe laying in streets and in private land.

We dealt with 1,750 disputes and complaints in 2008-09, obtaining rebates or compensation of almost £4 million.

The time taken to resolve complaints depends on the nature and complexity of individual cases, but we aim to deliver our performance standards. The table below shows our performance against these standards.

| Standard  | Achieved |
|---|----------|
| 80% of non-investigated complaints to be dealt with within ten working days         | 62%      |
| 65% of investigated complaints to be resolved within three months (65 working days) | 64%      |
| 80% of investigated complaints to be resolved within six months (130 working days)  | 85%      |

## Appendix 6: Summary of our 2008-09 expenditure

The financial information provided in the tables below is the latest available forecast and is subject to external audit by the National Audit Office. Accounts are prepared in accordance with HM Treasury's resource accounting requirements.

### Our administration costs 2008-09

|  | 2007-08<br>outturn<br>£000 | 2008-09<br>estimated<br>£000 | 2009-10<br>plans<br>£000 |
|--|----------------------------|------------------------------|--------------------------|
| <b>Gross administration costs</b>  |                            |                              |                          |
| Staff  | 8,250                      | 8,992                        | 10,821                   |
| Other  | 4,987                      | 5,864                        | 7,879                    |
| <b>Total gross administration costs</b>                                    | <b>13,237</b>              | <b>14,856</b>                | <b>18,700</b>            |
| Related administrative receipts from licence fees and other minor receipts | (13,237)                   | (14,856)                     | (18,700)                 |
| <b>Total net administration costs</b>                                      | <b>–</b>                   | <b>–</b>                     | <b>–</b>                 |

### Administration costs by activity group 2008-09

|  | 2008-09 estimated outturn<br>£000 |
|--|-----------------------------------|
| Regulatory monitoring and action   | 7,881                             |
| Corporate affairs and legal services   | 2,370                             |
| Finance, human resources, facilities management, information management and technology | 3,554                             |
| Accommodation  | 1,051                             |
| <b>Total expenditure</b>   | <b>14,856</b>                     |

### Estimated income and expenditure 2008-09

|   | £000    | £000          |
|---|---------|---------------|
| <b>Income</b>   |         |               |
| Licence fees recovered                                | 17,551  |               |
| Other income (including brought forward licence fees) | 1,419   |               |
| Licence fees unused to carry forward                  | (4,114) |               |
| <b>Total income</b>                                   |         | <b>14,856</b> |
| <b>Expenditure</b>                                    |         |               |
| Permanent staff                                       | 8,992   |               |
| Personnel overheads                                   | 656     |               |
| Consultancy projects                                  | 2,799   |               |
| Accommodation   | 1,051   |               |
| Accommodation upgrade                                 | –       |               |
| Non-cash items, for example depreciation              | 206     |               |
| Other   | 1,152   |               |
| <b>Total expenditure</b>                              |         | <b>14,856</b> |

## Appendix 7: Resource management 2008-09

### Staff recruitment during 2008-09 (by gender and ethnic group)

| Level                    | Number appointed | Proportion of women (%) | Proportion from ethnic minorities (%) |
|--------------------------|------------------|-------------------------|---------------------------------------|
| Head of team/function    | 5                | 20                      | 0                                     |
| Middle management        | 27               | 33                      | 11                                    |
| Clerical and secretarial | 27               | 55                      | 15                                    |
| Total                    | 59               | 42                      | 12                                    |

### Employed staff information (as at 31 March 2009)

|  |     |
|--|-----|
| Full-time equivalent staff (as at 31 March 2009) | 210 |
| Proportion of women (%)                          | 53  |
| Proportion from ethnic minorities (%)            | 19  |
| Proportion disabled (%)                          | 1.8 |
| Members of the Senior Civil Service              | 8   |
| Number of fixed-term and casual contracts        | 16  |
| Number of staff working part-time                | 42  |
| Staff turnover (%)                               | 9.5 |

### Salaries for members of the Senior Civil Service (as at 31 March 2009)

|                     |   |
|---------------------|---|
| £100,000 – £145,000 | 3 |
| £90,000 – £99,999   | 3 |
| £75,000 – £89,999   | 2 |

### Staff training attendance 2008-09 (by ethnic group)

| Ethnic group                  | Number of training days (rounded up) | Percentage (%) (rounded to nearest whole number) |
|-------------------------------|--------------------------------------|--|
| White                         | 1,081                                | 85   |
| Other ethnic groups           | 186                                  | 15   |
| Total number of training days | 1,267                                | 100  |

### Consultancy and professional services expenditure summary 2008-09 (company contracts costing more than £50,000 excluding VAT)

| Project   | Supplier                                 |
|---|--|
| Enhancing the role of support services  | Evolve Business Consultancy              |
| Organisational development  | Field Enterprise Ltd                     |
| Executive search and advertising services for the role of Director of Markets and the Director of Network Regulation  | Odgers Ray & Berndtson                   |
| Temporary Information Technology Analyst  | Badenock & Clark                         |
| Advice on cost base submissions   | Jacobs                                   |
| Scope for efficiency studies  | Reckon LLP                               |
| Review of companies' capital maintenance plans (common framework assessment)  | Mott Macdonald                           |
| Review of tax projections and assumptions in companies' draft and final business plans  | KMPG                                     |
| Advice on cost of capital and financeability for the 2009 price review  | Europe Economics                         |
| Advice on the accounting separation and cost allocation project   | Ernst & Young LLP                        |
| Provision of expert advice and analysis on the approach to cost estimation, risk appraisal and allocation, and project management for the Thames Tideway scheme | Mott Macdonald                           |
| Advice on the financing and delivery of large capital projects in the water and sewerage sectors in England and Wales   | Pricewaterhouse Coopers                  |
| Ofwat website   | Computacenter                            |
| Interim Director of External Affairs  | Sand Resources Ltd                       |
| Assistance in Ofwat's review of bulk pricing policy in the water and sewerage sectors   | Cambridge Economic Policy Associates Ltd |
| Assistance in Ofwat's review of market competition in the water and sewerage sectors  | KEMA Ltd                                 |