

Information notice

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2014 price review – companies' compliance with statutory obligations

This information notice confirms the approach we set out in our methodology for the 2014 price review about how we will assess whether companies' plans appropriately demonstrate that they will comply with future legal ('statutory') obligations. This includes those obligations governed by other regulators, including:

- the Environment Agency;
- the Drinking Water Inspectorate (DWI);
- Natural England; and
- Natural Resources Wales.

In this information notice we also set out an additional step we will include in our process to allow the other regulators to raise new material issues that arise after 2 December and before the end of the risk-based review with us. This is also part of our 2014 price review.

Background

The 2014 price review is our process for setting the price and service packages ('price controls')

that each of the monopoly water and sewerage and water only companies in England and Wales must deliver over the five years between 2015 and 2020. Each company will send us its business plan, setting out their plan for prices and services for its customers, by 2 December 2013.

In '[Setting price controls for 2015-20 – final methodology and expectations for companies' business plans](#)' (our 'methodology') we set out how we will reach our decisions on companies' price controls.

A key part of our methodology is carrying out a series of tests (a risk-based review) on each company's plan. We will use this to classify the quality of each company's plan as one of three categories – 'enhanced', 'standard' or 'resubmission'. The category a company receives for its plan will determine how and when we set their price controls. Companies with enhanced plans will receive rewards such as early draft decisions ('determinations') on their price controls.

Assessing companies' compliance with statutory obligations during the risk-based review

We set out in our methodology that we recognise that the environment and drinking water quality regulators have important roles in the price review process.

Companies must meet their statutory obligations. To do so we expect them to work closely with other regulators in developing their plan. This is to ensure that companies:

- understand their future statutory obligations; and
- have enough information to plan where these obligations are currently uncertain.

We stated in our methodology that where future statutory obligations are uncertain, we expect companies to:

- base their plans on reasonable assumptions about those obligations; and
- explain how they think the

This is a formal document that alerts our stakeholders to a change in the way that we regulate the water and sewerage sectors in England and Wales.

uncertainty should be dealt with within their price controls.

In our methodology we explained that companies need to demonstrate that they will comply with future statutory obligations in their plans. So a key feature of our risk based review is to assess whether companies have demonstrated that their long term objectives ('outcomes') and performance commitments are consistent with their future statutory obligations.

To support our assessment we have introduced specific tests (on pages 77 and 78 of our methodology) that require each company to set out how it is complying with its statutory obligations. As we noted in our methodology, preparing a high quality plan will require a company to:

- provide a high level of assurance that it will comply with its statutory obligations; and
- enable the relevant regulators to support this in the customer challenge group (CCG) report.

We expect each company's Board to provide an evidence-based statement as part of its Board assurance that the plan will ensure that the company is able to meet all of its statutory obligations.

In addition to what companies say in their plans, we will be taking into account the views of the independent CCGs.

CCGs are independent groups of customers and customer representatives that will challenge

how well each company engages with its customers in developing its plan. They will also challenge the degree to which this customer engagement is reflected in the company's plan. Each CCG will send us a report on the quality of its company's customer engagement at the same time as we receive companies' plans in December.

As we noted in our methodology, the CCGs provide a new and powerful forum through which each company can engage with stakeholders, such as other regulators. Environmental and drinking water quality regulators, who are members of the CCGs, can make a critical contribution to each CCG. They can make sure that each CCG understands how companies should reflect their statutory obligations in their plans.

We would expect the environment and drinking water quality regulators to highlight in each CCG's report whether or not a company has provided adequate assurance that it will meet its future statutory obligations. Where we think, after considering the CCG report, a company's plan is unlikely to allow it to meet its future statutory obligations then it will directly affect the outcome of our risk-based review.

We will not classify the quality of a company's plan as 'enhanced' if it fails to adequately demonstrate that its plan will meet its future statutory obligations. Instead we will classify its plan as 'standard' or 'resubmission', depending on the issues we find and on how it performs in our other risk-based

review tests. We would then ask such companies to work with the other regulators to address any deficiencies in their plan and ensure they comply with their statutory obligations.

Interaction with other regulators

Before 2 December

On 2 December companies are required to submit their plans and CCGs are required to submit their reports.

As we have explained, the CCG report is a critical source of information in our risk-based review. We will use this report to help assess whether a company will comply with its future statutory obligations. This is particularly relevant given that a number of the other regulators sit on each company's CCG.

We would expect that each CCG report includes an assessment from the other relevant regulators. As we set out in our methodology this assessment should highlight whether a company's proposals put compliance with its future statutory obligations at risk. If the relevant regulators consider that a company has provided adequate assurance that its performance commitments are consistent with meeting current and future statutory obligations, then it would be helpful if the CCG report could also make this clear.

In our methodology we emphasised that where individual members of CCGs have different views that cannot be resolved – including on a company's

approach to meeting its statutory obligations – then the CCG report should:

- highlight any differences clearly; and
- set out the impact that they have had on the final position of the CCG report.

We would then expect the company to explain how it has sought to balance these different views in its plan.

We also want to emphasise that we are not seeking to undertake a review of the evidence that the other regulators have analysed in reaching their assessments. However, it would be helpful if each CCG's report includes a short narrative to explain the considerations that the CCG has made in forming its assessment. This is especially true where CCG members have different views that cannot be resolved.

During our risk-based review (2 December to 4 April 2014)

After each company has sent us its plan we will focus on assessing the quality of those plans as part of our risk-based review.

To maintain a fair process, we will be very constrained in how we can take into account additional representations we receive from any stakeholders after 2 December 2013. This includes those made by other regulators and other CCG members.

But we recognise that the status of issues may change during our risk-based review. For example,

another regulator may decide to take enforcement action against a company for its current performance.

To ensure that we consider all relevant information we will write to each regulator that has specific enforcement powers in December. In those letters we will:

- identify those companies that state their plan allows full compliance with all statutory obligations; and
- ask each regulator to confirm to us that since each company submitted their plan there are no new or significant outstanding enforcement (or other material) issues that have come to light relating to those companies.

Other regulators will need to provide their response to us by 1 March 2014 to ensure that we can take into account this information in our risk-based review. We would also expect that they will provide such information to the companies when it becomes available. This will give those companies a chance to respond to the concern and engage with the other regulator before issues are raised with us.

After our risk-based review (From 4 April 2014 onwards)

On 4 April 2014 we plan to announce the outcome of our risk-based review and the classification we have given to each company's plan. The future involvement of other regulators in the price review process for each company will depend on the classification we give individual companies' plans.

Where we classify the quality of a company's plan as enhanced, we will accept its plan in the round and will make limited changes to it. But to become enhanced a company's plan must be of a very high standard. It must provide a high level of assurance that it will comply with its statutory obligations, which must also be supported by the relevant regulators in the CCG report.

Where we classify a company's plan as enhanced there will be no further significant opportunity for the other regulators to input into the price review process. This is because we have committed to publish early draft determinations for these companies.

If we classify the quality of a company's plan as 'standard' or 'resubmission', then the company may need to re-engage with other regulators. This will ultimately depend on the reason why we classified their plan as standard or resubmission.

We will set out in further detail the process for other regulators to engage further with the price review process for standard and resubmission companies after we have announced the outcome of our risk-based review.

Enquiries

If you have any questions about this information notice please send them to price.review@ofwat.gsi.gov.uk.

More information

Setting price controls for 2015-20 – final methodology and expectations for companies' business plans, July 2013

2014 price review [web pages](#)

Customer challenge group [web pages](#)

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November 2013

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