

Ofwat forward programme 2014-15



About this document

This document sets out our forward work programme for the coming financial year. We focus on the projects we plan to carry out rather than routine activities.

This document reflects changes since, and as a result of, the consultation on our [draft forward programme for 2014-15](#). We held the consultation between 15 January and 11 February 2014.

Under the Water Industry Act 1991 (as amended by the Water Act 2003), we have a duty to consult on, and publish, our forward work programme ahead of the coming financial year.

Further information about what we do can be found on our website at www.ofwat.gov.uk.

Contents

Foreword	2
Strategic assessment 2014-15	5
Key dates in 2014-15	8
How our work programme aligns with the priorities of the UK and Welsh Governments – a summary	10
Our work programme	12
Financing the delivery of our work programme	38
Changes to our work programme and budgets	39
Summary of responses to our draft forward programme consultation	40



Foreword

Welcome to our final forward work programme for 2014-15. In January, when we published our draft forward programme for consultation, we announced that we were reviewing our long-term strategy for regulating the water sector in England and Wales. We also stated that this was just the start of a dialogue we wanted to have with our stakeholders about the future direction of the sector and Ofwat.

We welcome the positive and open conversations we have had with many of our stakeholders so far. This includes the responses we received to our draft forward programme consultation, which we have used to develop this final programme of work.

We look forward to continuing this engagement – or beginning it with those stakeholders we are yet to meet – as we develop, refine and begin to implement our new strategy over the coming 12 months. Our aim remains to develop a strategy that helps us stay at the top of our game: helping all parties with an interest in water and wastewater

services meet the challenges ahead in the best interests of current and future customers and society more widely.

Of course, alongside the development of our strategy this year, we will be carrying out a crucial set of projects that will also contribute directly to how we continue to regulate the sector. This includes the following.

- Delivering the 2014 price review and continuing to encourage companies to place the needs of customers at the heart of their business decisions in 2015 and beyond.
- Putting in place a business transformation programme to help us deliver our strategy.
- Challenging companies to deliver an even greater focus on their customers and to meet high standards of corporate leadership, transparency and governance.
- Looking to secure the best outcomes for customers who are dissatisfied with the service they receive from their water company by, for example, continuing to work with the sector to



A handwritten signature in blue ink, appearing to read 'Jonson Cox'.

Jonson Cox
Chairman



A handwritten signature in blue ink, appearing to read 'Cathryn Ross'.

Cathryn Ross
Chief Executive

establish an alternative dispute resolution process that will help to ensure complaints are dealt with quickly and effectively.

- Carrying out prudent preparation for the changes to the sector proposed in the UK Government's Water Bill. This includes contributing to the work necessary to allow all non-household customers in England to choose their water and wastewater retail services supplier from April 2017 onwards. It also means making sure that our work remains consistent with the planned new resilience duty for Ofwat.
- Making full use of our powers as a regulator under the Competition Act 1998 and the Water Industry Act 1991 in relation to strategic cases, which will help ensure that the sector meets its obligations efficiently and effectively in the best interests of customers.
- Playing our part to ensure that efficient companies can attract debt and equity investment and an appropriate approach to risk and return in financing both asset infrastructure and retail services.

We look forward to working with all of our stakeholders during 2014-15 to help the sector meet the needs of customers now and in the future.

We aim to develop a strategy that ensures we remain at the top of our game





Strategic assessment 2014-15

Water and wastewater services are essential for life. Customers of water companies deserve a good service at a fair price. Currently, most customers in England and Wales are unable to choose their supplier and receive services from their local monopoly provider.

The water sector faces many challenges, such as climate change and population growth, that together create an unpredictable environment. These challenges mean that the sector as a whole needs to become more responsive, innovative and forward looking in responding to customer needs.

Because most customers are unable to choose their supplier, it is our role to protect both their interests and those of future customers. As part of this, we ensure that water companies are both able and incentivised to invest in their businesses efficiently, while maintaining their access to private capital markets at reasonable cost.

In recent years, we have made improvements to the way we regulate, to drive a necessary change in culture and to help overcome the challenges the sector faces. These improvements include introducing:

- an outcome-focused approach to regulation that looks at what really matters to customers, and gives the sector space to innovate in products and customer service;
- a risk-based approach to regulation that gives companies greater managerial freedom and ensures greater accountability to their customers for their own performance; and
- an improved approach for setting the price and service packages ('price controls') that monopoly water companies must deliver. This will help

encourage them to provide more customer-focused, efficient and sustainable water and wastewater services, enabling investment and supporting economic growth.

2014-15 – a transition year

The coming year is a transitional one for Ofwat for the following reasons.

- We are carrying out the [2014 price review](#) (PR14), which will result in us setting the price controls that monopoly companies will deliver to their customers in the five years between 2015 and 2020. This will include us implementing many of the regulatory innovations we have developed over the past three years in close consultation with stakeholders.
- The UK Government has introduced legislation into the UK Parliament that will make changes to how the sector operates and our role, including the proposed introduction of non-household retail competition. Subject to parliamentary process, the [Water Bill](#) is likely to become law by spring 2014.
- The UK Government published new [strategic guidance and social and environmental guidance](#) for us in 2013.
- The Welsh Government has published its new [social and environmental guidance](#) to us, which came into force in February 2014.
- The majority of both our [Board and the senior leadership team](#) have been appointed recently. This includes:
 - a new Chair in late 2012;
 - four new Non-executive Directors during 2013;
 - a new Chief Executive in late 2013; and
 - four new members of the senior leadership team.

Given the changes and challenges highlighted above, we consider that now is the right time to develop a new long-term strategy for regulating the water sector in England and Wales. A vision is required for the sector, which encompasses service providers and customers. And a vision is required for Ofwat, which will set out how we will regulate the sector from 2015-20 and beyond.

We will set out a new strategy, which will inform both what we do and how we work. In developing our strategy, we are reflecting on our experience to date in changing our approach to regulation. This includes what we have achieved by:

- changing the way we set price controls in PR14;
- our work on Board leadership and corporate governance in regulated companies;
- our challenge to companies' management to share with their customers pain and gain from factors outside companies' control; and
- our work with the sector on an alternative dispute resolution scheme.

We are also reflecting on what we have heard already in our discussions with stakeholders. This includes:

- customer groups;
- environmental organisations;
- investors;
- companies;
- policy-makers; and
- other regulators.

We will develop our new strategy over the next 12 months. We will do this in consultation with the many other groups and organisations that play an important role in the water sector. We consider that engaging in such a dialogue will help us determine a strategy that will provide a robust basis for our regulation in years to come. Such a strategy would:

- recognise that water and wastewater are essential public services and put the customer at the centre of everything we do;
- reflect the needs of everyone who benefits from water and wastewater services, including current and future customers, and wider society;
- address the relationship between water and wastewater services and the wider environment;
- understand that, although the regulated water companies have a crucial role to play in delivering what customers need and want, other companies and organisations also have important roles and effects upon, and within, the sector;
- recognise the need for certain standards to be set and maintained – for example, in public health, environmental protection and core levels of service – and Ofwat's role in their delivery;
- focus on Ofwat's role in ensuring effective relationships between water companies, investors and customers;
- continue to harness the benefits of competition and market forces where appropriate to drive efficiencies and give better outcomes for all customers; and
- continue to see Ofwat supporting conditions under which efficient companies can finance their water and wastewater businesses.

Alongside developing our strategy, we are putting in place a business transformation programme to help us deliver it. This will ensure that what we do, the type of organisation we are and the way we work all add up to enable us to fulfil our vision. We are also developing our plans for areas of new work. This includes:

- developing our strategy for ensuring that vulnerable household customers and small businesses are listened to and their needs are met; and
- considering the best way we can hear and reflect customers' views in our work.

We will seek to involve all relevant stakeholders in developing these plans.

2014-15 work programme

In this document, we set out the core projects we plan to deliver over the next year. They reflect our statutory duties and are aligned with strategic guidance to us from the UK and Welsh Governments. For each project, we describe:

- what it is;
- what we aim to deliver;
- how we will do it;
- the benefits it will deliver;
- the key dates in 2014-15; and
- how it aligns with both the policy priorities of the UK and Welsh Governments.

We thank those stakeholders that responded to our draft forward programme consultation. We set out a summary of the main issues raised on page 40 and our response. We will also consider comments we received on specific projects as we deliver them.

In delivering our work programme we will seek to involve all relevant stakeholders. This includes but is not limited to:

- customers and their representatives;
- environmental bodies;
- water companies;
- the UK Government;
- the Welsh Government; and
- other regulators.

We welcome the continued contribution that all stakeholders make to our work.



Dialogue will help us determine a strategy that will provide a robust basis for our regulation in years to come

Key dates in 2014-15

<p>April to June</p>	<p>All regulated companies to have voluntary codes on governance on 1 April 2014 (Board leadership, transparency and governance).</p> <p>Publish our final principles for holding companies (Board leadership, transparency and governance).</p> <p>Publish a commentary on what we have seen in companies' codes, highlighting areas of best practice and areas where we consider there is room for improvement (Board leadership, transparency and governance).</p> <p>Confirm enhanced company status (2014 price review).</p> <p>Publish draft determinations for companies with enhanced business plans (2014 price review).</p> <p>Publish draft determinations for companies seeking a June determination (2014 price review).</p> <p>Publish a draft Ofwat vision statement for consultation (New strategy).</p> <p>Consult on proposed market governance arrangements for the new retail market for non-household customers (Choice and trading arrangements).</p> <p>Publish the framework for market codes (Choice and trading arrangements).</p>
<p>July to September</p>	<p>Consult on how we can achieve a level playing field in water and wastewater markets (Choice and trading arrangements).</p> <p>Publish draft determinations for other companies (2014 price review).</p>

October to December

Publish final determinations for all companies (2014 price review).

Publish a final vision statement (New strategy).

Consult on our strategic priorities (New strategy).

Consult on how we will monitor our external environment and our progress towards our strategic goals (New strategy).

Establish a roadmap and approach for conducting licence review work (Licence review).

Publish our final strategic priorities (New strategy).

Publish our conclusions on how we will monitor our external environment and progress towards our strategic priorities (New strategy).

January to March

Publish a decision statement on our approach to ensure a level playing field (Choice and trading arrangements).

Consult on changes to the standard conditions in water supply licensees' (WSL) licences to remove the ban on them trading in their associated appointee's area ('in-area trading ban') to implement the changes set out in the Enterprise and Regulatory Reform Act 2013 (Choice and trading arrangements).

Consult on developing the information published by monopoly companies on the different parts of their businesses – known as 'accounting separation' (Choice and trading arrangements).

Publish updated guidance on which customers we consider are eligible to choose their retail water and wastewater supplier (Choice and trading arrangements).

All regulated companies fully meeting our Board leadership, transparency and governance principles – as a minimum – by April 2015 (Board leadership, transparency and governance).

Set out our approach to considering special administration arrangements (Special administration arrangements).

Consult on and publish our forward work programme for 2015-16 (New strategy).

How our work programme aligns with the priorities of the UK and Welsh Governments – a summary

UK Government priorities

Ofwat project	1	2	3	4	5	6	7	8	9	10
2014 price review	✓	✓		✓	✓	✓		✓		✓
Choice and trading arrangements	✓			✓					✓	
Board leadership, transparency and governance	✓	✓	✓		✓					✓
Licence review	✓	✓							✓	
Thames Tideway	✓	✓		✓	✓		✓		✓	
Casework		✓					✓		✓	
Special administration arrangements	✓			✓			✓			
New strategy	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓

1. Impacts of regulatory changes on sector investment prospects
2. Proportionality of the regulatory framework
3. Impacts of the regulatory framework on sector investment profile
4. Contribution to the Government's sustainable development objectives
5. Impacts of the regulatory approach on the sector's preparation for long-term challenges, such as climate change
6. Impacts of the regulatory approach on company innovation, such as catchment management
7. Impacts of the regulatory approach on sector resilience and sustainable water resource management
8. Sufficiency of company action to help customers struggling to pay bills
9. Progress on competition, to ensure this is in step with the Water White Paper and Government boundaries
10. Effectiveness of the 2014 price review in delivering outcomes sought by customers and other stakeholders

Welsh Government priorities

Ofwat project	1	2	3	4	5	6	7	8	9	10
2014 price review	✓	✓	✓	✓	✓	✓		✓	✓	✓
Choice and trading arrangements	✓									
Board leadership, transparency and governance	✓	✓	✓							
Licence review	✓									
Thames Tideway	n/a									
Casework	✓	✓								
Special administration arrangements	✓		✓			✓				
New strategy	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓

1. Regulatory proposals: assess impacts of regulatory changes on consumers and investors
2. Environmental and statutory obligations: facilitate compliance with domestic and European legislation
3. Sustainable development: contribute to the Welsh Government's sustainable development objectives
4. Affordability: take account of affordability issues in Wales
5. Efficiency and cost effective solutions: drive innovation within the boundaries set by the Welsh Government to ensure improvements in efficiency
6. Resilience and joined up outcome-based solutions: enable resilience against natural and other hazards
7. Research and evidence-based decisions and policy making: take account of research and costs in making decisions
8. Drinking water quality: ensure compliance with drinking water quality obligations
9. Integrated water management solutions: encourage sustainable and innovative water management solutions
10. Future resource management: encourage integrated long-term planning and solutions

2014 price review



What we aim to deliver

A proportionate price setting process that:

- puts an assessment of companies' business plans at the heart of the process;
- enables the companies to deliver services that customers want in an efficient way at prices they can afford;
- is consistent with our long-term price setting principles; and
- takes account of companies' statutory environmental and quality obligations.

What it is

In 2014-15, we will decide the price and service packages ('price controls') that each of the monopoly water companies in England and Wales must deliver for customers in each of the five years between 2015 and 2020.

We are following our final methodology statement, which we published in July 2013. The formal process of price setting began when each company sent us its business plan, which they did on 2 December 2013.

We will continue to deliver this project after the end of 2014-15.

How we will do it

- We will publish our draft decisions on companies' price controls ('draft determinations'). This includes our view of the minimum amount of expenditure that companies need to make ('baselines') and the rewards and penalties they can choose from in deciding their level of expenditure ('menus').
- Following representations from the companies and other stakeholders, we will make our final determinations of their price controls.
- We will review our approach for monitoring companies' delivery of their price controls during 2015-20, including our expectations for the information they publish about their performance for customers and other stakeholders.
- If any companies ask us to, we will refer our decisions on the final determinations to the Competition and Markets Authority.
- We will review lessons learned from the 2014 price review.

Key dates in 2014-15

- Confirm enhanced company status (4 April 2014).
- Publish draft determinations for companies with enhanced business plans (30 April 2014).
- Publish draft determinations for companies seeking a June determination (25 June 2014).
- Publish draft determinations for other companies (29 August 2014).
- Publish final determinations for all companies (12 December 2014).

Benefits of this project

Independent analysis carried out for us by PwC showed that changes we have made to our methodology for the 2014 price review could bring more than £2 billion in benefits to customers. This includes:

- empowering customers today by giving them a stronger voice in how companies deliver services and how much they pay for them;
- protecting the needs of future customers by ensuring companies plan how they will deliver secure and sustainable supplies over the long term;
- encouraging companies to produce high-quality plans based on their legal obligations and effective customer engagement – and giving them greater ownership for delivering those plans;
- challenging companies to keep costs low and deliver improved value to customers and the environment;
- ensuring that the balance between risk and reward is sufficiently aligned with the best interests of customers;
- maintaining the stability and transparency that investors value and which will encourage them to continue to finance long-term investment; and
- revealing new information from companies to improve how we set price controls in future and continue to protect customers' interests.

How this project contributes to the UK Government's strategic policy priorities

Priority and contribution

1. Impacts of regulatory changes on sector investment prospects

We have retained many aspects of our approach to price controls which worked well in the past to provide certainty and stability for companies and investors. We have also introduced opportunities for greater rewards for companies that do well.

2. Proportionality of the regulatory framework

We did not set detailed rules for companies' business plans. Instead, we are using a series of tests (our 'risk-based review') to review the quality of each company's plan and focus on those areas where the biggest risks are for customers and the environment.

4. Contribution to the Government's sustainable development objectives

Our price review process has tackled the bias companies had towards building new large-scale capital solutions, allowing them to propose more innovative and sustainable solutions such as catchment management and water efficiency in their business plans. Companies will also deliver services based on the outcomes their customers want, taking account of the long-term implications and their environmental obligations.

5. Impacts of the regulatory approach on the sector's preparation for long-term challenges, such as climate change / 6. Impacts of the regulatory approach on company innovation, such as catchment management / 10. Effectiveness of the 2014 price review in delivering outcomes sought by customers and other stakeholders

Our price review allows companies to deliver services based on the outcomes that their customers want and that take into account the long-term implications and their environmental obligations. Our methodology allows companies the flexibility to deliver solutions that meet these outcomes in the most cost-efficient way. This includes using more innovative solutions to delivering the services their customers expect. Companies provided a report from their customer challenge group (CCG) as part of their business plan submissions. These groups play an important role in challenging how the company has incorporated the views of customers and other stakeholders into its plans. We continue to recognise this important role and will take the views of CCGs into account as we reach draft and final determinations.

8. Sufficiency of company action to help customers struggling to pay bills

Affordability is one of our key tests in assessing how well companies' plans deliver for their customers now and in the long term. As part of this, we look at how well companies are managing bad debt and interacting with those customers who are struggling to pay their bill.

How this project contributes to the Welsh Government's policy priorities

Priority and contribution

Regulatory proposals: assess impacts of regulatory changes on consumers and investors

We have retained many aspects of our approach to price controls which worked well in the past to provide certainty and stability for companies and investors. We have also introduced opportunities for greater rewards for companies that do well.

Environmental and statutory obligations: facilitate compliance with domestic and European legislation

We did not set detailed rules for companies' business plans. Instead, we are using a series of tests to review the quality of each company's plan and focus on those areas where the biggest risks are for customers and the environment.

Sustainable development: contribute to the Welsh Government's sustainable development objectives

Our price review process has tackled the bias companies had towards building new large-scale capital solutions, allowing them to propose more innovative and sustainable solutions such as catchment management and water efficiency in their business plans. Companies will also deliver services based on the outcomes their customers want, taking account of the long-term implications and their environmental obligations.

Affordability: take account of affordability issues in Wales

Affordability is one of our key tests in assessing how well companies' plans deliver for their customers now and in the long term. As part of this, we look at how well companies are managing bad debt and interacting with those customers who are struggling to pay their bill.

Efficiency and cost effective solutions: drive innovation within the boundaries set by the Welsh Government to ensure improvements in efficiency / Resilience and joined up outcome-based solutions: enable resilience against natural and other hazards / Drinking water quality: ensure compliance with drinking water quality obligations / Integrated water management solutions: encourage sustainable and innovative water management solutions / Future resource management: encourage integrated long-term planning and solutions

Our price review allows companies to deliver services based on the outcomes that their customers want and that take into account the long-term implications and their environmental obligations. Our methodology allows companies the flexibility to deliver solutions that meet these outcomes in the most cost-efficient way. This includes using more innovative solutions to delivering the services their customers expect. Companies provided a report from their customer challenge group (CCG) as part of their business plan submissions. These groups play an important role in challenging how the company has incorporated the views of customers and other stakeholders into its plans. We continue to recognise this important role and will take the views of CCGs into account as we reach draft and final determinations.

Choice and trading arrangements



What it is

In June 2013, the UK Government published its Water Bill. If it formally passes through the UK parliamentary process, this legislation will, among other things:

- allow all non-household customers in England to choose their supplier of customer-facing ('retail') water and wastewater services;
- allow the introduction of markets into wholesale water and wastewater services; and
- give us a primary duty to further resilience of water and wastewater services.

We recognise that the Welsh Government does not wish to extend competition in Wales. We are working with UK and Welsh Governments and other stakeholders to plan how we will implement the proposals in the Bill. This includes working with the Open Water programme to prepare market reforms.

We will continue to deliver this project after the end of 2014-15.

What we aim to deliver

Subject to UK Government legislation:

- a market for retail water and wastewater services that gives non-household customers in England a choice of retail supplier from 1 April 2017;
- a roadmap for introducing markets for wholesale water and wastewater services to increase the scope for entry and more efficient outcomes and innovation; and
- changes to our regulatory framework that deliver the reforms included in the Water Bill effectively and efficiently. This includes setting separate price controls for the monopoly companies' retail and wholesale businesses.

How we will do it

We will work with the Open Water programme to prepare for delivering the market reforms set out in the Water Bill. In particular, we will:

- develop market arrangements that allow all non-household customers in England to choose their retail supplier, while at the same time ensuring they have effective protection;
- work with the Welsh Government and other stakeholders to ensure that the arrangements for the non-household customers of companies wholly or mainly in Wales that can choose their supplier under the existing water supply licensing (WSL) provisions are compatible with the new market arrangements in England;
- consult on the design of retail water licences, retail wastewater licences and retail market arrangements, including market governance and market codes (the rules and principles that suppliers must observe);
- engage with stakeholders across the sector on the design of wholesale water and wastewater licences, including market governance and market codes;
- consult on how we can achieve a level playing field for new entrants and avoid undue discrimination;
- consult on charging issues related to the implementation of market reforms; and
- work with the Water Industry Commission for Scotland (WICS), the UK Government and the Scottish Government to take steps towards a possible joint England–Scotland market for retail water and wastewater services. This will include agreeing joint licensing arrangements.

Benefits of this project

This project will ensure an effective market for retail water and wastewater services for non-household customers in England. This will:

- allow these customers to choose the retail price and service package they consider to be best for them;
- keep suppliers accountable to their customers because customers have the ability to switch if they are dissatisfied;
- challenge wholesale and retail companies to be more efficient in delivering services and offer new products and services to customers; and
- allow us to withdraw regulation – and reduce regulatory burdens – in areas where market forces are sufficient to protect customers' interests.

This project will also work towards the introduction of markets for wholesale services. Among other things, this could:

- improve the resilience of services to customers by giving greater flexibility for suppliers to trade water and;
- lessen environmental damage by giving suppliers greater opportunities to reduce the removal of water ('abstraction') from areas where it is scarce.

Key dates in 2014-15

- Consult on proposed market governance arrangements for the new retail market for non-household customers (April to June).
- Publish the framework for market codes (April to June).
- Consult on how we can achieve a level playing field in water and wastewater markets (July to September).
- Publish a decision statement on our approach to ensure a level playing field (January to March).
- Consult on changes to the standard conditions in water supply licensees' licences to remove the ban on them trading in their associated appointee's area ('in-area trading ban') to implement the changes set out in the Enterprise and Regulatory Reform Act 2013 (January to March).
- Consult on developing the information published by monopoly companies on the different parts of their businesses – known as 'accounting separation' (January to March).
- Publish updated guidance on which customers we consider are eligible to choose their retail water and wastewater supplier (January to March).

How this project contributes to the UK Government's policy priorities

Priority and contribution

1. Impacts of regulatory changes on sector investment prospects

We have already committed to allocating all of the monopoly companies' regulatory capital values (RCVs) to their wholesale price controls as part of the 2014 price review. This protects investors from the risk of an expanded market for retail services for non-household customers. We will consult extensively before we make any decisions that could significantly affect investor confidence.

4. Contribution to Government's sustainable development objectives

Based on the experience of a similar market in Scotland, the expanded market for retail services in England is expected to increase significantly water efficiency by non-household customers. It will also help them reduce their bills and decrease greenhouse gas emissions.

9. Progress on competition, to ensure this is in step with the Water White Paper and Government boundaries

We are helping to prepare for the implementation of an effective market for retail water and wastewater services in England by April 2017 – subject to the Water Bill becoming law. This is in line with the UK Government's policy.

How this project contributes to the Welsh Government's strategic policy priorities

Priority and contribution

Regulatory proposals: assess impacts of regulatory changes on consumers and investors

In delivering this project, we are taking account of the distinct policy position taken by the Welsh Government on competition. We will work with the Welsh Government and other stakeholders to ensure that the arrangements for non-household customers of companies wholly or mainly in Wales that can choose their supplier under the existing WSL provisions are compatible with the new market arrangements in England.

Board leadership, transparency and governance

What it is

The water sector – and the way that we regulate it – is evolving. If we are to take a less intrusive approach to regulation, we need to have confidence that regulated water companies – and their owners ('holding companies') – are acting in the public interest and that their leadership, transparency and governance reflects this.

In September 2013, we published '[Board leadership, transparency and governance – principles](#)', which set out the standards that we expect the regulated companies to adopt as a minimum. This also set out our expectation that all regulated companies will have voluntary codes in place by April 2014 that set out their approach to governance.

This is an evolutionary approach that places accountability on each Board for making sure their company adopts and demonstrates high standards of Board leadership and governance. We consulted on [principles for holding companies](#) in early 2014. We plan to publish final principles in 2014-15.

We will continue to deliver this project after the end of 2014-15.

What we aim to deliver

A sector that:

- operates to the highest standards of leadership, governance and transparency;
- maintains the confidence of customers so they continue to pay their water and sewerage bills; and
- maintains the confidence of investors and can continue to attract investment at competitive rates.

Key dates in 2014-15

- All regulated companies to have a voluntary code on governance on 1 April 2014 (April to June).
- Publish final principles for holding companies (April to June).
- Publish a commentary on what we have seen in companies' codes, highlighting areas of best practice and areas where we consider there is room for improvement (April to June).
- All regulated companies fully meeting our Board leadership, transparency and governance principles as a minimum by April 2015 (January to March).

How we will do it

We will:

- examine each company's code and seek improvements where necessary;
- draw companies' attention to examples of best practice;
- consider developments to companies' licences to support our approach; and
- where companies' owners change, we will make sure that new investors adopt high standards of Board leadership, transparency and governance that meet our principles as a minimum.

Benefits of this project

This project:

- ensures that customers have confidence that each regulated company's Board takes full account of customers' interests;
- encourages Boards that are focused on the long-term viability of the regulated company;
- encourages regulated companies and the groups to which they belong to voluntarily develop codes and adopt best practice;
- promotes a sector that has the confidence of customers and investors;
- encourages Boards of regulated companies to focus on long-term sustainability; and
- supports less intrusive regulation.

How this project contributes to the UK Government's strategic policy priorities

Priority and contribution

1. Impacts of regulatory changes on sector investment prospects

This project provides clarity for investors on governance issues in the sector.

2. Proportionality of the regulatory framework

This project encourages self-regulation, which does not add to the regulatory burden.

3. Impacts of the regulatory framework on sector investment profile

This project encourages long-term investment.

5. Impacts of the regulatory approach on the sector's preparation for long-term challenges, such as climate change

This project encourages company Boards to focus on the long-term sustainability of the sector.

10. Effectiveness of the 2014 price review in delivering outcomes sought by customers and other stakeholders

Our new approach to the business planning process places the onus on company Boards to own and be accountable for their plans. We required that each company's Board provide assurance that its plan is high quality and will deliver good outcomes for current and future customers and the environment.

How this project contributes to the Welsh Government's policy priorities

Priority and contribution

Regulatory proposals: assess impacts of regulatory changes on consumers and investors

This project provides clarity for customers and investors on governance issues in the sector.

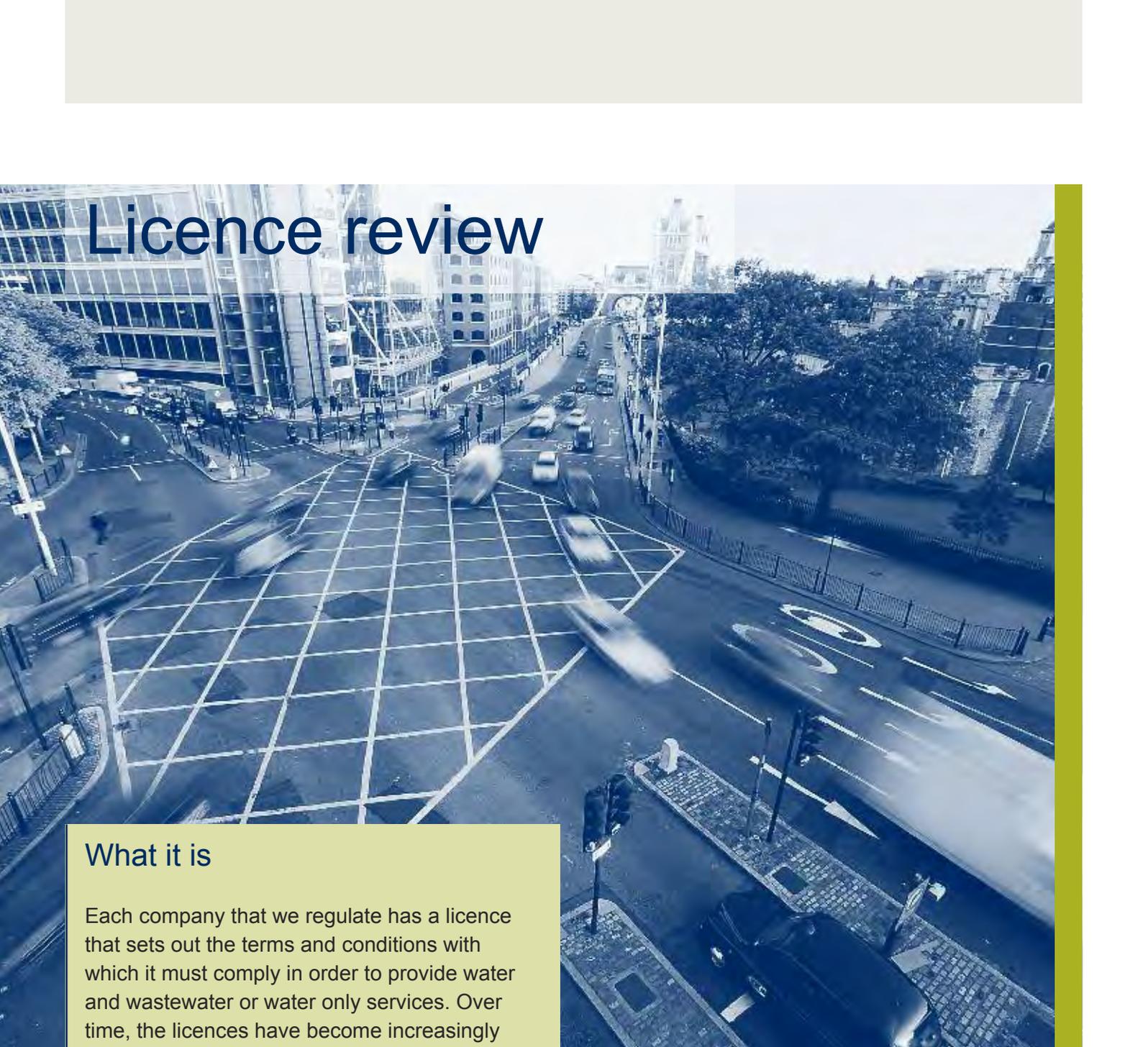
Environmental and statutory obligations: facilitate compliance with domestic and European legislation

This project ensures that each Board understands its company's obligations and directs the way in which they are met.

Sustainable development: contribute to the Welsh Government's sustainable development objectives

This project encourages company Boards to focus on the long-term sustainability of the sector.

Licence review



What it is

Each company that we regulate has a licence that sets out the terms and conditions with which it must comply in order to provide water and wastewater or water only services. Over time, the licences have become increasingly complex and some parts are now obsolete. We want to improve them by:

- making them clear and concise; and
- making sure they are fit for purpose and reflect the changes we are making to our overall regulatory framework.

In delivering this work, we plan to build on the lessons learned and the constructive discussions we had with stakeholders when we previously changed companies' licences.

We will continue to deliver this project after the end of 2014-15.

What we aim to deliver

- Company licences that are clear, concise and consistent.
- Licence obligations that are effective and appropriate to our evolving regulatory framework and the Water Bill.
- A modular licence structure that reflects the activities that companies operating in the sector carry out.
- A mature environment that facilitates a constructive approach to licence modifications between the regulator and the sector.

How we will do it

Building on our previous work to simplify licences and constructive discussions with companies on modifying their licences, we will develop our plans for carrying out a holistic review of:

- the licence obligations on companies in the water sector;
- the approach to conducting the review; and
- the way in which companies' licence conditions will need to adapt and change to meet future challenges.

We will use the results of the review to set the framework for evolving company licences so that the content and structure are fit for purpose and can be adapted readily to meet the way in which regulation and the sector develops.

Key dates in 2014-15

- Establish a roadmap and approach for conducting licence review work (October to December).

Benefits of this project

This project will ensure:

- companies' licences that reflect changes to the way we regulate and the environment in which we regulate, such as changes to our price setting process and to the framework for competition in England;
- up-to-date licence obligations that allow customers to understand what services they can expect from the companies that supply them;
- investors have clarity about companies' obligations;
- companies demonstrate how they meet their licence obligations;
- licence obligations that are designed to meet the particular services that a company provides;
- clarity for new companies that want to supply services about the obligations they will need to meet; and
- licences that are fit for purpose and place accountability on each company's Board for meeting its obligations, allowing us to adopt less intrusive regulation where companies are demonstrably doing so.

How this project contributes to the UK Government's strategic policy priorities

Priority and contribution

1. Impacts of regulatory changes on sector investment prospects / 3. Impacts of the regulatory framework on sector investment profile

This project ensures investors understand fully the obligations on companies operating in this sector and have confidence in the regulatory environment.

2. Proportionality of the regulatory framework

There is likely to be a short-term impact on the regulatory burden from the work needed to revise licences. But this will have long-term benefits.

9. Progress on competition, to ensure this is in step with the Water White Paper and Government boundaries

We want to deliver licence obligations that are appropriately focused and consistent with the Water Bill.

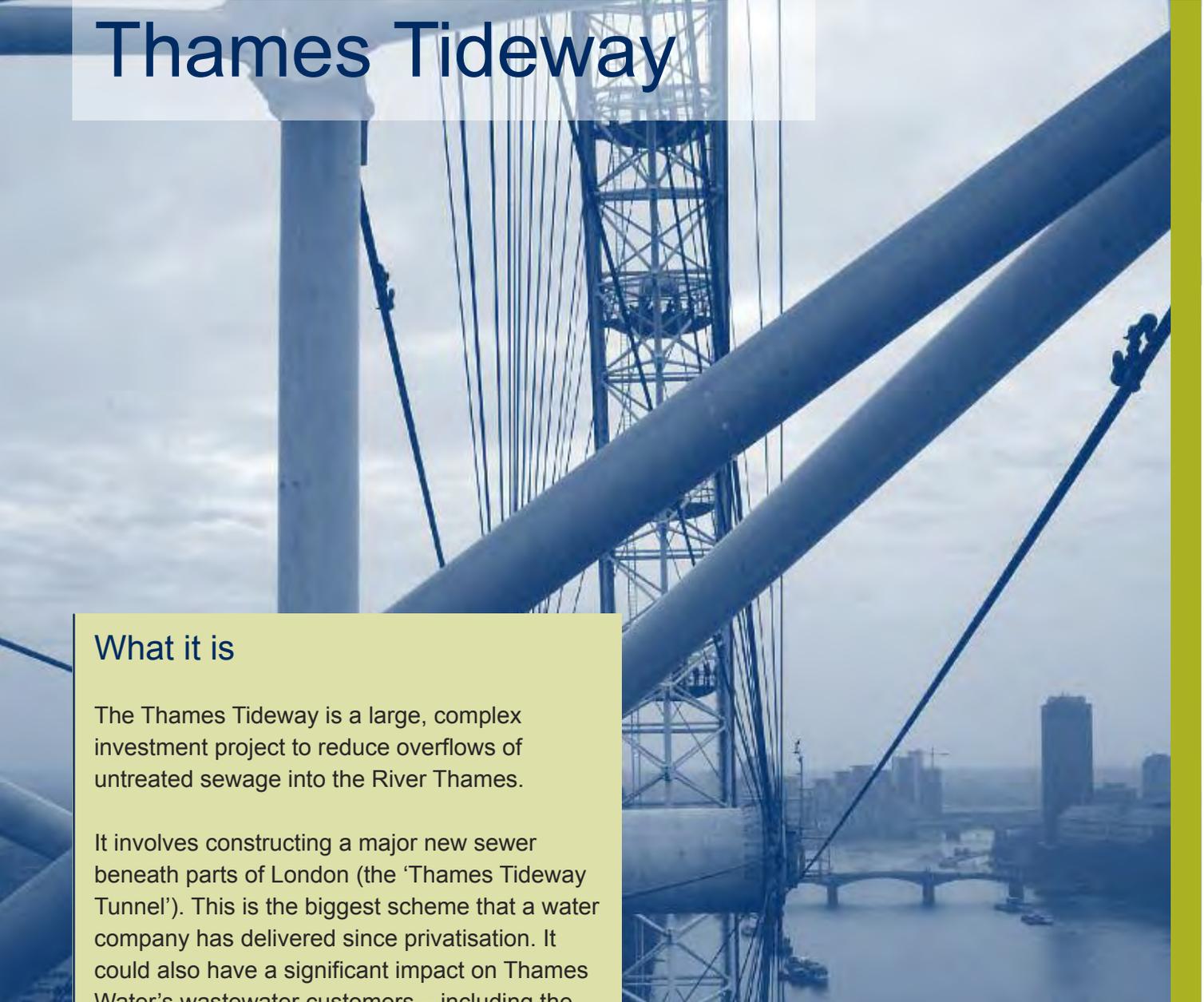
How this project contributes to the Welsh Government's policy priorities

Priority and contribution

Regulatory proposals: assess impacts of regulatory changes on consumers and investors

The obligations on companies operating in this sector are clear, fit for purpose and are in the interests of customers.

Thames Tideway



What it is

The Thames Tideway is a large, complex investment project to reduce overflows of untreated sewage into the River Thames.

It involves constructing a major new sewer beneath parts of London (the 'Thames Tideway Tunnel'). This is the biggest scheme that a water company has delivered since privatisation. It could also have a significant impact on Thames Water's wastewater customers – including the services they receive and bills they pay – local communities and the environment.

Over the past decade, we have worked with Thames Water and other stakeholders to understand the need to reduce discharges in the River Thames and the available solutions to meet European legal requirements. And the UK Government has endorsed the project as the best-value solution.

We are working with Thames Water, Defra and other stakeholders to support the development

and financing of the company's plans. Our role is to ensure:

- the Thames Tideway project is appropriately regulated;
- any costs that are incurred are efficient and continue to represent best value to Thames Water's customers; and
- Thames Water follows best practice.

We will continue to deliver this project after the end of 2014-15.

What we aim to deliver

- A scheme in which customers only finance efficient and effective costs.
- Thames Water and any third party infrastructure providers are accountable to the company's customers.
- New approaches for delivering large projects that produce better outcomes for customers across England and Wales.

How we will do it

We will work with the UK Government, the Environment Agency, Thames Water and other stakeholders to identify the most suitable implementation and financing model for the Thames Tideway Tunnel that ensures:

- it is delivered effectively and efficiently;
- it costs no more than necessary; and
- customers get the best value for money possible.

The UK Government made the Water Industry (Specified Infrastructure Projects) (English Undertakers) Regulations 2013 in June 2013. Under these regulations, we will help in the appointment of a successful infrastructure provider should the project be specified by the Secretary of State.

Key dates in 2014-15

After Thames Water has competitively procured an infrastructure provider – the preferred option for financing and delivering the tunnel – we would, following consultation, look to designate and grant a licence to the successful bidder.

Benefits of this project

This project will help to:

- ensure that the Thames Tideway Tunnel costs no more than it has to and the best value for money is achieved;
- develop an alternative funding and delivery approach that should deliver better value overall for customers;
- ensure that the risks of the Thames Tideway Tunnel are properly separated from Thames Water's appointed business so that the financing of the appointed business is not exposed;
- maximise competitive pressures in the water sector in a way that the current regulatory framework cannot achieve by developing a third party infrastructure provider model to finance and deliver the Thames Tideway Tunnel;
- support the development of a long-term investment proposition that will enable the delivery of a major infrastructure project that will bring the River Thames into compliance with the Urban Wastewater Treatment Directive; and
- provide necessary capacity in the sewer network for future generations.

How this project contributes to the UK Government's strategic policy priorities

The Thames Tideway project has been endorsed by the UK Government. It does not in itself aim to address the strategic policy priorities the UK Government set out for us. But in delivering our work, we look to ensure its outcomes are aligned with the strategic policy priorities.

Priority and contribution

1. Impacts of regulatory changes on sector investment prospects

Developing a preferred third party infrastructure provider model to finance and deliver the Thames Tideway Tunnel should provide regulatory certainty for investors.

2. Proportionality of the regulatory framework

This project aims to develop a new finance and delivery model that will allow targeted regulation through a bespoke form of licence and regulation rather than a 'one size fits all' approach.

4. Contribution to Government's sustainable development objectives

This project is supporting the development of a long-term investment proposition which will enable the delivery of a major infrastructure project that will bring the River Thames into compliance with the Urban Wastewater Treatment Directive and provide necessary capacity in the sewer network for future generations.

5. Impacts of the regulatory approach on the sector's preparation for long-term challenges, such as climate change

This project is supporting the development of a long-term investment proposition to enable the delivery of the Thames Tideway Tunnel.

7. Impacts of the regulatory approach on sector resilience and sustainable water resource management

This project is enabling investment in resilient networks by developing an alternative delivery and funding model to deliver a major infrastructure project to bring the River Thames into compliance with the Urban Wastewater Treatment Directive and provide necessary capacity in the sewer network for current and future generations.

9. Progress on competition, to ensure this is in step with the Water White Paper and Government boundaries

The work being carried out as part of this project to develop a third party infrastructure provider model to finance and deliver the Thames Tideway Tunnel provides an opportunity to maximise competitive pressures in the water sector in a way that the current regulatory framework cannot achieve.

How this project contributes to the Welsh Government's policy priorities

The Welsh Government's priorities are not appropriate to this project as it relates specifically to infrastructure in England. But we will have regard to the Welsh Government's priorities where we apply the approaches and lessons learned to infrastructure in Wales in future.

Casework

What it is

We have a range of statutory powers which we are both enabled and required to use to:

- deliver our legal duties; and
- ensure that customers get the best deal from their suppliers.

Our ability to take on and make decisions on disputes, complaints and other cases ('casework') under the Competition Act 1998, the Enterprise Act 2002 and the Water Industry Act 1991 are powerful tools that we can use.

We share many of our casework powers with other bodies, particularly our Competition Act and Enterprise Act powers. There are a number of changes under way that will affect how we use these two powers in particular. These are:

- the establishment of the Competition and Markets Authority; and
- a new competition primacy duty given to all sector regulators in the new Enterprise and Regulatory Reform Act 2013.

Over the past two years, we have focused increasingly on cases that are strategically significant. This includes cases that:

- involve the most serious harm to customers;
- allow us to set important precedents that may improve the way the water sector operates; or
- send clear signals to companies to meet their obligations, increase compliance and for their managers to be accountable for their decisions.

This is helping to deliver better overall outcomes for customers.

In 2014-15, we expect to continue to implement and develop our approach. This includes preparing to use new arrangements that the UK Government has proposed in its Water Bill to give us improved scope to exercise some discretion over which cases we take on. This would allow us to transfer some of the smaller, routine complaints and disputes that we currently handle to an independent third party adjudicator acting on our behalf and under our guidance. In this way, individual customers can get better outcomes for their complaint or dispute. We can also focus more of our resources on strategic cases that would deliver greater benefits for all customers.

We will only be able to transfer cases once the Water Bill has become law, the relevant provisions are enacted by the Secretary of State and we have established the transfer arrangements. This includes consulting on and publishing guidance to the third party on the disputes it deals with.

Also, to help customers and companies resolve disputes they have, we are helping the companies – along with the Consumer Council for Water (CCWater) and Water UK (the representative body for companies) – to set up an independent alternative dispute resolution (ADR) scheme.

What we aim to deliver

- Efficient, effective and timely decisions on strategic cases.
- Effective working arrangements with a third party for transferring routine cases to them, subject to the arrangements set out in the Water Bill becoming law.

How we will do it

We will:

- use our resources effectively and pick strategic cases that deliver greater benefits to all customers;
- prepare for the new arrangements for transferring routine cases in anticipation of the Water Bill becoming law and the relevant provisions becoming enacted;
- work closely with companies, CCWater and Water UK to help set up an independent ADR scheme; and
- explore areas where we could engage in effective partnership working with other regulators and organisations.

Key dates in 2014-15

Subject to the Water Bill becoming law, we will prepare for the transfer of our less complex and customer-facing casework cases to a third party body in anticipation of the relevant provisions being enacted.

We expect the companies' ADR scheme will begin during 2014-15.

Benefits of this project

The project will:

- deliver better outcomes to customers;
- give us greater flexibility to focus on cases that have the potential to deliver the greatest benefits to customers; and
- allow us to continue to develop a more transparent, effective and efficient approach to casework. By focusing on strategic cases and making our decisions more accessible, we hope to:
 - set clear precedents;
 - give greater visibility on the types of cases we are targeting; and
 - ultimately encourage compliance by companies, stimulate better outcomes for customers and help avoid future cases into similar matters in future.

How this project contributes to the UK Government's strategic policy priorities

Priority and contribution

2. Proportionality of the regulatory framework

This project will give us greater discretion to focus on the cases that are most strategically significant and the potential to deliver the greatest benefits to customers.

7. Impacts of the regulatory approach on sector resilience and sustainable water resource management

This project will enable a clear framework for the continuation of services to customers. Our work is likely to target cases that establish important precedents for the trading of water, which can help improve resilience of supplies to customers.

9. Progress on competition, to ensure this is in step with the Water White Paper and Government boundaries

Our work is likely to include cases that establish important precedents for encouraging competition in England as set out in the Water Bill.

How this project contributes to the Welsh Government's policy priorities

Priority and contribution

Regulatory proposals: assess impacts of regulatory changes on consumers and investors / Research and evidence-based decisions and policy making: take account of research and costs in making decisions

We will ensure that our casework interventions and subsequent decisions are proportionate and evidence based. Where we have the discretion to choose cases, we prioritise our casework and enforcement activity in those areas where the conduct in question raises the greatest risk to customers. And, when prioritising our casework, we consider the benefits we can deliver to customers against the costs of the case.

Environmental and statutory obligations: facilitate compliance with domestic and European legislation

This project will hold companies to account and ensure that they meet their legal and regulatory obligations in relation to licence conditions, their obligations under UK and EU Competition Law and statutory duties under the Water Industry Act 1991.

Special administration arrangements

What it is

We have duties to ensure efficient companies can finance their functions and meet their legal obligations. There may be circumstances under which a company:

- fails to meet its legal obligations and does not or cannot take remedial action; or
- is unable to finance its functions due to, for example, poor decisions by its management or significant unexpected changes to its costs (a 'cost shock').

In these circumstances, we have powers to appoint a Special Administrator to oversee the running of the company. This ensures that services to customers are maintained. Fortunately, we have never had to use the special administration arrangements, but it has been a number of years since we reviewed them. So, we plan to work with the UK and Welsh Governments during 2014-15 to review their effectiveness.

We will continue to deliver this project after the end of 2014-15.

What we aim to deliver

- A report on the effectiveness of the current special administration arrangements.
- If necessary, changes to those arrangements.

How we will do it

We will:

- review the effectiveness of the current special administration arrangements;
- consult on our draft findings and any changes we propose to make; and
- publish our final findings – and implement any changes.

Benefits of this project

The project will:

- provide transparency to all stakeholders about the operation of the special administration arrangements; and
- ensure that customers are protected in the event that we place a company into special administration.

Key dates in 2014-15

- Set out our approach to considering special administration arrangements (January to March).

How this project contributes to the UK Government's strategic policy priorities

Priority and contribution

1. Impacts of regulatory changes on sector investment prospects

This project provides clarity for investors and other stakeholders on the operation of the special administration arrangements.

4. Contribution to Government's sustainable development objectives / 7. Impacts of the regulatory approach on sector resilience and sustainable water resource management

This project enables a clear framework for the continuation of services to customers.

How this project contributes to the Welsh Government's policy priorities

Priority and contribution

Regulatory proposals: assess impacts of regulatory changes on consumers and investors

This project provides clarity for investors and other stakeholders on the effectiveness of the special administration arrangements.

Sustainable development: contribute to the Welsh Government's sustainable development objectives / Resilience and joined up outcome-based solutions: enable resilience against natural and other hazards

This project enables a clear framework for the continuation of services to customers.

New strategy



What it is

We are reviewing our long-term plan ('our strategy') for regulating the water sector in England and Wales. We will develop a strategy that sets out how we plan to:

- deliver our legal duties;
- meet our other obligations (for example, our obligation as a public sector organisation to deliver value for money); and
- contribute to the priorities of the the UK and Welsh Governments.

The new strategy will replace 'Delivering sustainable water – Ofwat's strategy', which we published in March 2010.

What we aim to deliver

- A document that sets out our long-term vision for the water sector and Ofwat (our 'vision').
- A strategic business plan that sets out how we will implement our vision in 2015-16 to 2017-18.
- An operational delivery plan and forward work programme for 2015-16.
- A document that sets out how we plan to monitor our external environment and measure our progress towards our vision (a 'dashboard').
- A programme of business transformation to support the implementation of our new strategy.

Key dates in 2014-15

- Publish a draft vision for consultation (April to June).
- Publish a final vision (October to December).
- Consult on and publish our final strategic priorities (October to December).
- Consult on how we will monitor our external environment and progress towards our strategic priorities (October to December).
- Publish our conclusions on how we will monitor our external environment and our progress towards our strategic priorities (October to December).
- Consult on our forward work programme for 2015-16 (January to March).
- Publish our final forward work programme for 2015-16 (January to March).

How we will do it

- We will consult on our draft vision in summer 2014.
- After considering responses to our consultation and other engagement we have with our stakeholders, we will publish our final vision in autumn 2014.
- Based on our vision, we will develop and consult on our strategic priorities.
- We will use our vision and strategic priorities to develop our strategic business plan for 2015-16 to 2017-18 and our operational plan and forward work programme for 2015-16.
- We will consult on and publish our performance framework for measuring our progress towards our vision.

Benefits of this project

- A clear plan for how Ofwat will deliver its duties and other obligations.
- Opportunity for stakeholders to inform how we do our job.
- Certainty and transparency for stakeholders on our long-term priorities and focus of our work.
- Ensuring that the companies we regulate put their customers at the heart of their decision making.

Priorities of the UK and Welsh Governments

Our new strategy will contribute to all the priorities of the UK and Welsh Governments.

Financing the delivery of our work programme

We aim to deliver our legal duties effectively and efficiently, and provide value for money. Our expenditure requirements are met by licence fees that are recovered from the companies we regulate.

In our draft forward programme we explained that we needed to increase our budget and licence fee. This was mainly due to significant one-off costs of delivering the 2014 price review and our business transformation programme.

In 2014-15, our licence fee will be £29.94 million. This will be offset by a credit note of between £700,000 and £900,000, which we have returned to companies in 2013-14. So, our net licence fee will be between £29.04 million and £29.24 million. This is equivalent to about 0.3% of the sector's turnover.

We will recover the cost of regulating the Thames Tideway Tunnel project separately from Thames Water. The proposed estimate for this special fee is £1.5 million.

The higher budget for 2014-15 reflects the additional one-off costs required to transform Ofwat into a leaner, more focused and efficient organisation. It will ensure we deliver the significant efficiencies and cost reductions we require to deliver our new strategy while operating within a much tighter budget from 2015-16 onwards – when we will be subject to a settlement imposed by HM Treasury through the Comprehensive Spending Review.

We recognise the importance of being transparent about how we intend to use our budget in 2014-15. So we will be publishing further information for our stakeholders in early 2014-15.

Changes to our work programme and budgets

Our work programme could change further in the light of our new strategy and new UK and Welsh Government policies and legislation.

For example:

- the scale and pace of our choice and trading arrangements project will be determined by the progress of legislation that the UK Government introduced in the UK Parliament in summer 2013; and
- the Welsh Government is expected to publish its revised water strategy during 2014, which could give us new responsibilities.

Our forward programme also excludes any routine work we may be required to carry out during the year. This includes:

- investigations;
- enforcement;
- disputes; or
- legal cases.

Our forward programme excludes any routine work we may be required to carry out during the year

While we aim to make prudent assumptions – based on past experience – on how much routine work we may reasonably expect, we may receive more or less than we anticipate.

If our work programme changes, we will review our current and future budgets accordingly.

Summary of responses to our draft forward programme consultation

We consulted on our [draft forward programme](#) between 15 January and 11 February 2014. We received [16 written responses](#). We also received some further feedback direct from stakeholders through discussions we had with them.

The majority of the comments we received were in relation to how we deliver specific projects. We will consider these as we deliver our work programme over the coming year.

Most respondents broadly supported our work programme, particularly our project to develop a new strategy. They welcomed the presentation of the work programme, including how we demonstrate how our work programme aligns with the UK Government's strategic policy priorities. We have used a similar approach to voluntarily report on how our projects align with the Welsh Government's priorities.

Below we highlight the main themes that came out of the consultation and our response to the issues raised.

2014 price review

Most respondents highlighted the importance of an efficient and effective price review over the coming year. We recognise the importance of delivering the price review, which will be our highest priority during 2014-15.

Choice and trading arrangements

Some stakeholders thought that we were not explicit enough in our draft forward programme that the

Welsh Government has adopted a different policy to competition in Wales. We are happy to clarify this and have done so on pages 16 to 18.

Charging issues

Some stakeholders asked us to clarify a number of issues related to our work on charging as part of the price review and choice and trading arrangements projects. This is a complex and interlinked policy area. But among other things, we have done the following.

- We set up working groups in January 2014 as part of our PR14 work and in response to the Water Bill. The terms of reference for this group includes informing our policy development on future charging reforms, such as advising on practical implementation issues.
- We published an initial consultation on wholesale and retail charges in January 2014. Without pre-judging the outcome of the UK Parliamentary process, we will consult further in this area – which will help companies prepare their charges for 2015-16 – once the Water Bill becomes law and the UK Government consults on its draft charging guidance.
- We have already begun to consider charging issues related to introducing competition into upstream services, including publishing a discussion paper on access pricing in 2013. Subject to the Water Bill becoming law, these reforms are expected to begin towards the end of the decade. So this is a long-term piece of work.
- We have already started to look at charging for new connections, including publishing a discussion paper on this area of work in 2013. Once the

Water Bill becomes law and the UK Government issues guidance, we will be able to publish new rules about this.

We will seek to clarify the specific issues raised by individual stakeholders in our conversations with them.

Board leadership, transparency and governance

A number of stakeholders welcomed the work we have already done in this area. Two of them also asked whether we will be making our review of companies' codes on governance public.

We will be publishing the findings of our review of companies' codes. As part of this, we will highlight areas of innovative and leading practices. We will also highlight areas where companies have not met our expectations and there is further work for them to do.

Licence review

Most stakeholders welcomed our proposal to continue our work in this area, which we delayed until after the price review. Some stakeholders asked for reassurance that we will continue the constructive dialogue that we developed with them during our previous changes to companies' licences. We are happy to provide this reassurance and have stated our intention on pages 23 to 25.

Casework

One stakeholder thought we should have been clearer in our draft forward programme that our

ability to transfer our routine cases to an ADR provider is dependent on the:

- Water Bill becoming law; and
- relevant provisions within the Bill being enacted.

Another stakeholder asked whether we would issue guidance to the ADR provider in dealing with the cases we transfer to them.

We have made the text describing the project on pages 30 to 33 clearer on both points.

Special administration arrangements

A number of stakeholders welcomed our work in this area. One of them highlighted that we need to be clearer that we will take account of the work the UK Government is planning to do in this area during 2014-15. Another highlighted the need for us to engage with all stakeholders in reviewing arrangements.

We have made the text on pages 34 to 35 clearer. We will also be carrying out engagement with water companies and other stakeholders in delivering this work.

New strategy

We welcome the support we received on our proposal to develop a new strategy. We will consider the comments we receive as we continue our discussions with stakeholders over the next 12 months.

Related to our strategy, some respondents asked about the outcome of 'Appendix 1: A consultation

on measuring and reporting our performance', which we published alongside our draft forward programme for 2013-14 to 2015-16 in November 2012. We will be using this work and the responses we receive as we develop a performance framework for our new strategy.

Financing our work programme

A number of stakeholders noted the large increase in our licence fee we proposed for 2014-15. Some asked for a further breakdown of our costs in order to demonstrate transparency to customers and others about how we plan to use our licence fee. One stakeholder also noted the impact of our cost on customers' bills.

We recognise that our licence fee is higher than in previous years. This is due to significant one-off costs to support the delivery of our price review project and work on business transformation. These costs will ultimately allow us to work within a significantly reduced budget in 2015-16. They will also support the delivery of a price review process that we anticipate will help support more affordable bills for customers. We have returned unspent licence fees in 2013-14 to customers by way of a credit note to companies, which will offset their licence fees for 2014-15. We will publish extra information on how we plan to use our budget in early 2014-15.



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



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