

Members in attendance

Board attendees	
Jonson Cox	Non-executive Director, Chairman
Chris Burchell	Non-executive Director
Christine Farnish	Non-executive Director
Martin Lawrence	Non-executive Director
Catherine Waddams	Non-executive Director
Alison Munro	Non-executive Director
Tim Waggott	Non-executive Director
Mark Bayley	Non-executive Director
Cathryn Ross	Chief Executive
Keith Mason	Executive Director
Richard Khaldi	Executive Director
Elizabeth Hillman	General Counsel
Rachel Wright	Board Secretary
Other attendees	
Claire Forbes	Senior Director, Corporate Communications
David Black	Senior Director, Water 2020
Bev Messinger	Senior Director, Business Improvement
Aileen Armstrong	Observer
Stephen St Pier	Associate Director, Strategy and Policy
Andrew Beaver	Director, Strategy and Policy
Jamie Tunnicliffe	Director, Analytics
Georgina Mills	Director, Analytics
Andrew Walker	Director, Analytics
Adam Cooper	Director, Retail Market Opening
Tim Griffiths	Director, Retail Market Opening
Iain McGuffog	Director, Strategy and Planning
Ronan Palmer	Director, Strategy and Planning
Rob Powell	Director, Operations

1. Opening Items and Declarations

- 1.1. Jonson Cox welcomed the new Non Executive Board members Mark Bayley, Tim Waggott and Alison Munro who joined the Board on 1 April 2016.
- 1.2. Jonson Cox, on behalf of the Board gave thanks to Chris Burchell as it was his last Board meeting. Chris would be retiring at the end of the month as it was the end of his term.
- 1.3. Jonson Cox also gave thanks to Keith Mason as it was his last Board meeting, noting that he will continue to play an important role as a member of the Senior Leadership team.
- 1.4. Jonson Cox noted that the fund he advises was acquiring a generation and supply business in Ireland with which is he may be involved in shareholder oversight.
- 1.5. The minutes of the previous Board meeting were agreed subject to minor comments. The minutes would not be published until after the publication of the May Water 2020 documents recognising the price sensitive nature of some of the decisions taken.

2. Chief Executives Report

- 2.1. The Chief Executive gave an update on the internal and external environments, highlighting:
 - the meetings which had taken place at Executive level during March and April with incumbent companies on the Water 2020 policy proposals;
 - observations on progress being made across the sector to build and maintain trust and confidence in the services, including the continued change in culture set out in PR14;
 - the increasing pace of change in the sector and the future direction of travel towards PR19, following the Water 2020 publications due out in May; and,
 - the need for licence changes to support Ofwat's change in approach to regulation in line with its strategy.

3. Water 2020

- 3.1 The Executive gave an overview of previous decisions made by the Board, and the set the wider context of Ofwat's strategy within which those decisions were made.
- 3.2 The Executive presented a summary of the discussions to be had at this Board meeting.

Direct procurement for customers

- 3.3 The Executive presented a paper on the options for market design of direct procurement for customers, which are those arrangements whereby a water company procures services, particularly infrastructure projects in a similar way to Thames Water's procurement of the Thames Tideway Tunnel, on behalf of customers. The Executive noted that this can include the financing of a project.
- 3.4 The Board discussed the alignment of the risk between companies and customers associated with procurement.
- 3.5 The Board discussed the reasons why companies were not doing this at the moment, which included the RCV addition companies receive from providing infrastructure themselves, and the impact this has on companies' valuations.
- 3.6 The Board agreed to set clear expectations and strong incentives through the risk based review of business plans in PR19 for companies to use direct procurement for customers for suitable high value projects.
- 3.7 The Board discussed an appropriate threshold above which it would expect companies to consider direct procurement at PR19. The Board agreed to set the threshold at £100million, although noted the responsibility of companies to act in the best interests of their customers in any procurement, and hence excluding a project of £99million from any direct procurement considerations would not be in this spirit.
- 3.8 The Board agreed to signal in the May publication document that Ofwat would be assessing PR19 business plans in this area, particularly in the allocation of risk between company and supplier.

Water 2020 Outcomes

- 3.9 The Executive presented proposals for the May Water 2020 document on long term commitments for customers and in-period outcome delivery incentives (ODIs) and, for information only, its planned approach to developing comparative information on company performance.
- 3.10 The Board noted that there was a need to balance the future changes in technology and external environment, with the need for companies to commit to their customers in the longer term, beyond the five year price controls.
- 3.11 The Board agreed with the Executive proposal to consult on for options for longer term commitments in its May publications.
- 3.12 The Board endorsed Option 2 as the preferred option for consultation, where 5 year performance commitments and ODIs are set at each price review, but companies are transparent about their longer term plans for performance (“longer term non-binding PCs”). Companies could still propose their own longer term performance commitments which Ofwat would review.
- 3.13 The Executive presented a proposal to pursue a licence modification for in-period ODIs for all companies that will facilitate (but not require) payment of ODI rewards and penalties in-period.
- 3.14 The Executive noted that in-period ODIs were resulting in a behavioural shift for some companies by linking ODIs more closely in time with management performance rewards.
- 3.15 The Board agreed with in-period ODIs but noted that the proposals should take account of the need to avoid undue peaks in customer bills within period.
- 3.16 The Executive presented, for information, its proposals for developing comparative information on company performance which could be used to engage on the contents of the sector strategic dashboard (being led by Water UK).
- 3.17 These comparators were developed taking into consideration customer priorities at PR14, work by UKWIR and feedback from Customer Challenge Groups.
- 3.18 The Board discussed the importance of transparency and trust in the data and the role of third party assurance in achieving this.

3.19 The Board agreed with the proposal for Ofwat to engage on the contents of the sector strategic dashboard.

Engagement strategy for May publication

3.20 The Executive presented the strategy for engaging the sector on the publication of the May policies publication.

3.21 The Board noted that the Executive had done a good job in improving engagement with the sector and investors.

3.22 The Board highlighted the importance of also engaging with Non-Governmental Organisations and wider customer groups in an accessible way, recognising that not all customers are the same.

Licensing strategy

3.23 The Executive presented its proposed overall approach, including engagement with the sector, to taking forward licence changes for the Water 2020 policies.

3.24 The Board discussed the risks and opportunities to the strategy. The Board was satisfied with the strategy proposed.

3.25 The Board noted the tight timescales and the importance of front loading the licence modification process.

3.26 The Board agreed with the strategy.

PR19 Delivery Model

3.27 The Executive gave an update on it's work on the PR19 Delivery model to maximize PR19 as a lever for building trust in water, realizing Ofwat's vision and building on the achievements of PR14. As such, the project has taken into considerations lessons learnt from PR14.

3.28 The Board discussed the possible governance arrangements for PR19, including the role of any Board sub-committee and the engagement with the Board. It noted the new appointments at Executive level that would lead, under the Chief Executive, on PR19 delivery.

3.29 The Board noted the update on the delivery model.

PR16 review of business retail default tariff price case

- 3.30 The Executive presented the proposed approach to PR16.
- 3.31 The Executive gave a summary of the responses to the March consultation on the PR16 review of business retail default tariffs and set out key issues for consideration ahead of the Method Statement to be published in May.
- 3.32 The Board agreed to maintain the overall cost and margin allowances at present but if there is evidence that there may be material issues it would further consider it (in particular in relation to credit cover costs, which remain subject to further consultation by the Retail Market Opening team). The Board asked that this be discussed at its July meeting ahead of developing draft determinations.
- 3.33 The Executive presented the proposals for simplifying the default tariff caps by using gross margin bands, and the responses from the sector following the consultation.
- 3.34 The Board agreed to simplification subject to getting further information to be submitted to it following the Board meeting on the practicalities of simplification. The Board agreed that, considering company concerns about implementation, the boundary will be moved to 5 mega litres which would continue to capture most of the benefits of simplification.
- 3.35 The Executive agreed to send a draft methodology statement to the Board offline for comment.

Residential competition review update

- 3.36 The Executive gave an update on the review of the costs and benefits of introducing competition to residential customers.
- 3.37 The Executive highlighted the findings from Phase 1 of its customer engagement research.
- 3.38 The Board highlighted some of the wider costs and benefits to consider in the analysis, including those of consumers.
- 3.39 The Board noted the update.

4. Retail Market Opening

- 4.1 The Executive gave an update on the progress towards opening the market for business customers in April 2017.
- 4.2 The Executive set out the work being done to ensure Ofwat will be ready internally for market opening, including understanding what the likely impact on its casework might be.
- 4.3 The Executive highlighted the emerging points from the independent review report of the overall programme.
- 4.4 The Board noted the updated.

5. Financial Monitoring Framework

- 5.1. The Executive gave an update on Ofwat's requirements for Long Term Financial Viability Statements as part of the financial monitoring framework.
- 5.2. It also set out some worked examples on how the new rules on interest deductions for tax purposes may affect tax payable by water companies and their holding groups. These changes were included in the March 2016 UK Budget which included measures that will restrict companies' ability to reduce corporation taxes by offsetting interest against income.
- 5.3. The Board noted the update.

6. Q4 Budget report – month 12

- 6.1. The Executive presented the budget position at the end of month 12, highlighting key issues and variances at the year end. The final budget for 2016-17 was included in the Chief Executive's report.
- 6.2. The Board discussed the amount of contingency for unforeseen work, for example any CMA referrals.
- 6.3. The Board noted the update.

7. Q4 Quarterly portfolio report and Ofwat dashboard

- 7.1. The Executive presented the Q4 portfolio report, updating the Board on the strategic risks, opportunities and constraints being experienced.
- 7.2. The Executive confirmed that significant progress was made during the final quarter of 2015-16 towards key milestones.
- 7.3. The Board discussed the future direction of travel, noting the increasing pace of change in the external environments.
- 7.4. The Board noted the update.

8. ARAC Committee Update

- 8.1. Christine Farnish as a member of the Audit and Risk Assurance Committee gave an update of its recent meeting on 16 March 2016.

9. AOB

- 9.1. The Board received an update from the Chief Executive on possible structural changes in the sector.

Rachel Wright
Board Secretary
28 April 2016