

Meeting held on Thursday 25 October 2018
 Venue: Bloomsbury House, 21 Bloomsbury Street, London WC1B 3HF

Attendance

Board attendees	
Jonson Cox	Non-Executive Director, Chairman
Martin Lawrence	Non-Executive Director
Tim Waggott	Non-Executive Director
Mark Bayley	Non-Executive Director
Catherine Waddams	Non-Executive Director
Alison Munro	Non-Executive Director
Christine Farnish	Non-Executive Director
Rachel Fletcher	Chief Executive
Aileen Armstrong	Executive Director
David Black	Executive Director
Jenny Block	General Counsel and Board Secretary
Other attendees	
Lisa Commane	Senior Director, Business Improvement
Emma Kelso	Senior Director, Customers and Casework
Alena Kozakova	Chief Economist
Keith Mason	Senior Director, Thames Tideway Tunnel
Alison Fergusson	Associate Director, PR19
Ynon Gablinger	Director, PR19
Tim Griffiths	Director, PR19
Peter Jordan	Associate Director, PR19
Frederick Levett	Senior Associate, Strategy Hub
Paul Oxley	Principal, Market Outcomes and Enforcement
Ronan Palmer	Director, Strategy Hub
Anita Payne	Director, PR19
Rosanna Pellarin	Associate, PPM
Sophie Shaw	Director, Legal, PR19

Giles Stevens	Director, Strategy Hub
Stephen St Pier	Director, PR19
Gillian Tanfield	Senior Associate, PR19
Juliet Young	Director of Economics
Apologies	
Claire Forbes	Senior Director, Corporate Communications
John Russell	Executive Director

1. Opening Items and Declarations

- 1.1. The minutes of the Board meeting held on 20 September 2018 were approved subject to some minor amendments.
- 1.2. There were no conflicts of interest to declare by reference to the matters on the agenda.

2. Chief Executive's Report

- 2.1. The Chief Executive gave an update on the internal and external environments highlighting the following:
 - EFRA Committee report: the Board discussed the findings of the EFRA Committee on water regulation and noted the recommendations made. Ofwat would work closely with Defra on a formal response.
 - NIC review: the Board discussed the announcement of a review to be undertaken by the National Infrastructure Commission of energy, water and telecoms regulation, the Terms of Reference for which are yet to be finalised. The Board noted and agreed with the Executive the importance of Ofwat's positive engagement with and pro-active support to this review, bringing more minds together to address common problems.
 - The Board highlighted the importance of remaining neutral on any proposals to change the regulatory model, it was not our role to defend it, whilst being open to opportunities and continuing to provide information to help inform the wider debate.

- The Chief Executive reported on ongoing work within UKRN to consider the opportunities to work more closely together, sharing expertise on a range of common issues, for example, consumer insight and customer vulnerability. The Board was supportive of further work to explore the scope for further collaboration through the UKRN.
- Water transfers: The Board noted and supported the ongoing work to develop a targeted and structured approach to exploring regional transfer arrangements and the collaborative approach required between companies and regulators.
- The Board noted the update on the Executive's ongoing work on financial resilience and the provision of consents to certain financing arrangements.
- In relation to Ofwat's risk appetite, the Board agreed with the additional suggestion from the Chief Executive and approved the risk appetite.

3. Market Outcomes and Enforcement

Retail Exit Code: Consultation on future price protections in the business market

- 3.1 The Executive presented proposals for future price protections for customers of the business retail market after the current controls expire in March 2020 on which Ofwat intended to consult.
- 3.2 The Board discussed the need to continue to protect customers with low volume usage, and the potential benefits that could arise from relaxing protections for higher volume users, in terms of promoting competition. The Board noted that these proposed protections would be transitional.
- 3.3 The Board agreed that further work was required to address other sources of friction in the business retail market. The Board also noted the other proposals on which Ofwat intended to consult in relation to non-price terms with a view to providing appropriate protections to business customers.

4. PR19

Emerging issues from initial assessment of business plans (IAP)

Overview

- 4.1. The Executive presented an overview of the PR19 programme highlighting the approach to the IAP, to ensure consistency of approach and an efficient process. The Board discussed the company presentations and the other engagement being undertaken. The Board noted the work being undertaken to ensure that PR19 is delivered in a way that promotes Ofwat's SAILOR values and the steps taken to continue ensuring the well-being of our people.
- 4.2. The Board noted the early views on a range of issues including resilience, innovation, affordability, direct procurement and the use of markets in company business plans, in addition to the two drawn out as separate agenda items. The Board agreed the proposed approach to assessment of company boards' assurance.

Cost assessment

- 4.3. The Executive presented the key issues arising from company business plans relating to cost projections for 2020-25, highlighting the areas where we see a significant increase in cost relative to PR14, significant proposals for new investments, and those with wider significance for stakeholders and/or implications for future periods. The Board noted in particular the substantial increase in proposals for enhancement expenditure, and stressed the importance of testing the efficiency of proposed enhancement expenditure, whilst recognising the need for expenditure legitimately to fulfil environmental obligations, meet the resilience challenge and to address growth and the supply/demand balance.
- 4.4. The Board discussed the proposed approach to setting an efficient level of cost allowance so that customers do not pay for inefficiency, including early considerations relevant to our approach to static or catch-up efficiency, frontier shift or dynamic efficiency, and to real price effects.

Customer engagement and outcomes

- 4.5. The Executive presented an overview of the key issues arising from some common Performance Commitments (PCs) and information on key features of the

Outcome Delivery Incentives (ODIs) proposed by the companies and some key issues that are emerging. Among other issues, the Board considered the stretch targets for leakage.

In-period ODI draft determinations and Severn Trent Water's wastewater cap

- 4.6. The Executive presented to Board for decision the proposed approach to the 2017-18 in-period ODI draft determinations and proposals on how to consider Severn Trent Water's application to lift its wastewater ODI cap which would be published together for consultation on 31 October 2018.
- 4.7. In relation to Severn Trent Water's application, the Board agreed with the recommendation to consult on the proposed approach rejecting Severn Trent Water's proposal and inviting Severn Trent to accept a proposal including an increased cap, revised outperformance and underperformance incentive payment levels and a revised performance commitment level for external sewer flooding as being in customers' long term interests. The Ofwat proposal would reset the level for performance and lock in the performance levels already achieved to create the right incentives for Severn Trent Water's future performance.
- 4.8. The Board discussed the key issues and the recommended approach to dealing with other matters relating to in-period ODI draft determinations.
- 4.9. The Board agreed that the Senior Director, PR19 Policy and Programme Delivery may sign off the in-period ODI final determinations and Severn Trent's revised wastewater ODI cap, subject to there being no material changes to the proposals following consultation.

Company monitoring framework

- 4.10. The Board discussed initial recommendations on company categorisations under the company monitoring framework. The Board agreed with most initial recommendations and provided a steer on the approach to the marginal decisions.

5. Strategy Hub

Project Thaw:

Company responses to the review

- 5.1 The Executive presented their initial assessment of water company responses to the Ofwat 'Out in the Cold' report. The Board considered the proposed approach for responding to company submissions and the intention to publish a response in November 2018.
- 5.2 The Board agreed with the proposed approach, including the importance of engaging with companies on our initial views where appropriate. The Board also agreed with the importance of sector ownership of these issues to meet their responsibilities and the important related role of Defra in supporting this through the Security & Emergency Measures Direction process.

Recommended changes to the Guaranteed Standards Scheme (GSS) compensation scheme

- 5.3 The Board received an update and considered the proposed recommendation to the UK and Welsh Governments about changes to the GSS arrangements.
- 5.4 The Board considered and agreed the twin-track approach which includes: 1) making a recommendation relating to some narrower areas of the GSS in the short term, and 2) undertaking a fuller review going forward into more complex areas.

Brexit update

- 5.5 The Board received an update on the issues that Brexit might bring to the water sector. Ofwat is participating in a Defra-led, UK-wide group to ensure that water companies are actively engaged in planning and risk management, for all scenarios, including the "no-deal" scenario, through collaboration to share key resources.

6. Update from Committee Chairs

Thames Tideway Tunnel Committee

- 6.1 The Chair of the Committee reported on the September meeting at which the Committee discussed recent developments on the project. The Committee also received an update on the key findings of the 2 year review of the TTT project.
- 6.2 The Committee agreed the proposal to modify Condition B of Thames Water's Instrument of Appointment in order to extend the separate TTT price control for a further five year period, and delegated the final sign off of the modifications to the SRO.
- 6.3 The Committee also agreed to grant the application from Tideway for a waiver of its procurement obligations, and delegation to the SRO for final sign off of the waiver.
- 6.4 The Committee also agreed to grant a more general delegation to the SRO of the TTT Programme in respect of future requests for waivers from Tideway's procurement obligations, subject in particular to the condition that any such request does not raise new major issues of principle and is not particularly sensitive.

Audit Risk and Assurance Committee

- 6.5 The Chair of the Committee reported on the September meeting at which the Committee discussed the new risks and opportunities register and proposed approach to the register and to its future management. The Committee noted the significant progress made and the considerable work that had gone into the developing model, and the thought given to how effective risk management would be further embedded in the organisation.
- 6.6 The Board noted the advice from the Committee to delegate the final risk strategy document to the General Counsel for sign off (having regard to the feedback and subject to there being no substantial change that is not approved by the Board).
- 6.7 The Committee also discussed the governance arrangements for PR19 and received an update on progress with the Alternative Delivery Model. The Committee noted the internal audit progress report presented by Mazars and the two internal audit reports: an advisory report on PR19 risk, and an audit on customer complaints and enquiries. Finally, the Committee noted the

recommendations highlighted in the NAO's management letter on the 2017-18 financial statement audit.

7. Any Other Business

7.1. There was no other business and the Chairman closed the meeting.

Jenny Block

Board Secretary

25 October 2018