



Attention: Rachel Fletcher
Chief Executive Officer
OFWAT
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By email

31st October 2019

Dear Rachel,

Thames Water's Business Plan 2020---2025 - Comment on draft determination

Ofwat uses emotive language early (Page 1, Para 1.1 Line 1 "For monopoly water companies.) in response to pricing suggestions in the TW Business Plan in its Ofwat Draft Determination of Price Controls document. The use of such emotive and pejorative language suggests a closed mindset on behalf of the regulator in its dealings with water suppliers in general and is not what one might reasonably expect of a regulator without a political position to defend.

All water companies are locally monopolies. That was a political choice and not of the investors or companies doing. The fact that such companies are locally monopolies has no bearing on the delivery, development, investment in infrastructure, environmental impacts or skills employed in the industry. It should have no bearing on the attitude of the industry regulator to the companies operating within that industry.

The use of such a statement so early in the document colours not only language later used in the response but the colouring of the response itself and the thinking behind it. It devalues the Ofwat response considerably as a thoughtful and constructive document in representing the needs of consumers, the water industry, the environment or the independence of the regulator.

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"The company has proposed an alternative sharing mechanism where the 50% sharing with customers applies to outperformance above 3% of Return on Regulatory Equity (RoRE) over the whole 2020-25 period instead of each year. We are intervening to impose our standard outperformance sharing mechanism so that sharing will apply each year. We are undertaking further work on the detail of the mechanism and the process for annual reconciliation. We will publish our final decisions on these aspects of the mechanism (including how it will affect the inperiod assessment of ODIs) as part of the final determinations in December 2019."

This decision is short sighted and does not allow long term strategic investments to be adequately financed. Long term investment requires long term thinking behind the investment. The decision proposed by Ofwat is short termism and potentially damaging to the environment and to TWs customers' interests in the development of sustainable infrastructure. This is a political decision driven by interests outside the needs of customers and the environment. (reflected by our opening remarks regarding "monopolies".

With respect to the determination of the Thames Water Business Plan 2020---25 we have the following thoughts.

There are two key issues of concern to CVFC; the damage to the environment of ongoing abstractions of water from our river courses and aquifers and the constant pollution, at a low level, from an overburdened and underinvested sewage system and treatment regime. The ecological cost of low level ongoing pollutions has been underestimated for many years but recent work in Japan is demonstrating how badly damaged the environment is from out of place pollutants and how damage at the bottom of the food chain to invertebrates sees the disappearance of higher animal and plant forms as a consequence of the biological damage lower down.

Amongst all the papers produced by Ofwat we are struggling to find any answers to how Ofwat plans to reconcile two incompatible requirements of trying to maintain low water prices while ensuring no (further) damage to the environment?

In any market place price is a key driver of the demand curve. Continuous low pricing of domestic water supplies does not assist in limiting demand and/or water usage, to the detriment of the environment. With climate change there is an increasing risk to the long term security of supply. The population is increasingly paying upwards of £0.05 per 100ml of water, bottled to carry and consume during the working day, yet Ofwat seems determined that water delivered via the tap should be so cheap as to almost not figure in most people's domestic budgets. The long term sustainability of water supplies in many parts of the country, including parts of the Thames Water supply area are dependent on reducing consumption. The key to demand limitation is price flexibility and Ofwat is working against the market by imposing short term strictures on potential pricing structures.

We note the criteria for water company investment gives little headroom for volume tolerance. How does this sit with recent climate events, long dry periods and short sharp deluges? With climate change we have had many highs and lows in rainfall and the Environment Agency is forecasting that extreme weather events will become more extreme and more common, implying long term droughts and short term deluges.

In the Chilterns and Colne valley we have witnessed three of the lowest historic rainfall years in the past five year period. We are now in November with a recently declared drought condition, yet subject to deluges, five in 2019 already in the Thames catchment alone. This indicates that water infrastructure needs to have significantly more resilience built into investment decisions, swiftly and with the support of the regulator. If this is not addressed in the Business Plan 2020-25 Determination, Ofwat will be responsible potentially for three and half million people not having water coming from their taps.

There has been a strong steer for water companies to reduce demand for water, keep prices low, reduce leaks, reduce costs, and invest in major and significant infrastructure. Many of these objectives are mutually exclusive, yet Ofwat seems itself confused as to priorities. Shareholders, of course, expect dividends from their investment but the new ownership model for Thames Water has accepted that they are invested for the long term and are seeking long term growth as opposed to a quick buck return. Ofwat does not seem to have understood this and appears to wish to punish stockholders/investors in insisting on an annualised model in an industry which is necessarily long term in planning, investment and return. The water industry is not one suitable to short term profit objectives, yet the Ofwat response and insistence on an annualised business model appears to favour just such short termism and ignores the structural needs of the investment and return planning of the business, thereby weakening the attachment that any investor will have to the industry, against the interests of consumers. Debt needs to be serviced but it appears that the business model which Ofwat is seeking to impose won't permit that servicing to be soundly based.

There is rightly a focus on reducing losses of water from the distribution system. Repairs in one location increase the likelihood of failures in pipework elsewhere and Thames Water is apparently attempting to take a radical view by wanting to replace whole parts of its distribution system at one time because research shows that this really does reduce losses from the system, To enable that radical approach, Ofwat is challenged to allow a similarly radical financial model to be run, both in planning and investment returns, otherwise Ofwat will stand in the way of progress and not be a motivator of it. There is now a long history of leakage targets being missed. Are those targets achievable under the present regime? Apparently not, so a radical solution must be found for dealing with a Victorian distribution system.

We fear that the long years of focus on loss reduction has delayed attention on the real issue, investing in alternative non-abstractive water resources and creating a robust resilient wastewater infrastructure to stop the constant dripfeed of degrading pollutions into our waterway and environment.

Yours sincerely

Tony Booker

Chairman CVFC

Mike Heylin OBE

Secretary CVFC