



David Black
Chief Regulation Officer
Ofwat

Via email : pr24@ofwat.gov.uk; [REDACTED]

29 January 2021

Dear David,

Ref: PR24 and beyond: Reflecting customer preferences in future price reviews – a discussion paper

Thank you for the opportunity to respond to Ofwat's discussion paper to reflect our customer preferences in future price reviews. We very much welcome Ofwat's early engagement on this topic, at a time where our sector is facing unprecedented challenges – including climate change, population growth, protection of the environment and increasing expectations from customers.

Our customers' demands are changing (and societal changes are further accelerated by the pandemic) and we need to make sure we keep pace and remain affordable for all. We must also need to ensure customers' diverse needs, and particularly those in vulnerable circumstances, are properly met.

As discussed when we last met in December, we are in the process of refreshing our 2050 Strategic Direction Statement (SDS) and our long-term ambitions will be articulated around our customers' priorities. Our SDS is an essential step in our PR24 preparation, and it will help us framing our plans to deliver our Purpose and promises to customers.

Overall, we strongly support the six goals set out by Ofwat in the paper (i.e. enabling water companies in researching customer views, recognising differences in customers preferences across the country, fostering collaboration within the industry, promoting transparency between Ofwat and water companies, increasing proportionality to focus on the key areas that matter to our customers and considering the wider public value that companies can create).

While we fully support this early opportunity to establish a shared understanding on how customer preferences are to be reflected at PR24, our customers' expectations do not necessarily align with the industry's 5-year regulatory cycles. Our approach to customer engagement is part of a wider customer insight programme, to understand the changes, opportunities, and challenges our customers face in their day-to-day.

We welcome the three ideas set out by Ofwat in the paper, for how the customer views might feed into future price reviews, in particular around the degree of collaboration needed at national level. The obvious place for such collaborative research is where it can offer efficiencies in delivery and enable comparability and consistency of outputs, and where customers interest and needs are not driven by regional or local circumstances (for example protection of the environment or customer vulnerability). We do not think however that



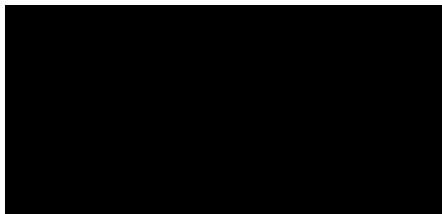
collaboration on research that is more qualitative in nature has significant benefit and introduces risks that local nuances are lost within an average, national view.

Notwithstanding the above, we recognise the work done over the years by companies to build meaningful relationship with their customers. It is therefore important that companies continue to own their customer research, and that any plans for collaborative research should be driven by and owned by companies.

We have provided more detailed to the questions set out in the discussion paper in an annex to this letter.

We would very much welcome further dialogue with Ofwat on the role that our customers should play in the price review process, and I look forward to further discussions over the coming months as the plans for PR24 continue to develop.

Yours sincerely,



Stève Hervouet
Director of Regulation and Strategy

cc.

Pauline Walsh, CEO, Affinity Water
Joe Brownless, Director of Customer Operations, Affinity Water
Carolyn Cooksey, Head of Business Planning, Affinity Water
Katy Taqvi, Head of Customer Strategy and Experience, Affinity Water

Annex

Within this annex we set out our thoughts on the questions included within Ofwat's discussion paper. We would be very happy to discuss any of these areas in more detail.

Q1: Do you agree with the goals we have proposed for customer engagement at future price reviews? If not, why not?

We broadly agree with the proposed goals that Ofwat has set out. The goals encompass the key aspects of engaging with customers that we would expect to see within a price review.

Recognise preferences – we are pleased that Ofwat notes the distinction between needs and expectations that are common across the country, and local differences that can arise due to geographical, economic or historic factors. Given Ofwat's consideration of collaborative, nationwide research, we think it is important to draw that distinction and to carefully consider where local needs arise, to ensure they are not missed or overwritten by a national average view. We would also expect Ofwat's assessment frameworks to recognise these differences and ensure that where supported by evidence, variations in plans or performance commitments are accepted in plans.

Increase proportionality – we welcome Ofwat's view that greater use can be made from wider evidence, for example from day to day interactions with customers as these provide powerful insights into specific elements of service provided. However we consider it is important to understand how much reliance we can place on such insights, as only a small proportion of customers contact companies each year, and these contacts are not necessarily representative of the wider customer base on all issues. Insights derived through customer interactions should be balanced with engagement channels that include representation from the customer base, and representative sample sizes.

We also note Ofwat's intention that engagement should focus on quality not quantity. We agree with this intention and suggest Ofwat considers how it can avoid inadvertently creating expectations that companies should engage with a large number of customers. Specifically, Ofwat should avoid including numbers of customers engaged with in the data tables, as this creates the impression that Ofwat expects to see a large number. It would be helpful if Ofwat set out its view of what high quality engagement looks like so that companies can set out how they have met those expectations in business plans.

Broaden value – we agree that companies have a role to create and grow public value, and that this has been an intrinsic part of the sector since privatisation. We were pleased to sign up to the industry's Public Interest Commitments in 2019 and recognise our unique place as a purpose-driven company to deliver wider benefits to the communities we serve, and to the environment in which we operate. It will be important that Ofwat's approach and assessment of plans clearly and explicitly takes this into account and does not constrain itself to a narrow assessment of providing water services (and wastewater for WaSCs) alone.

Q2: Are there any other goals which you think we should have for customer engagement at future price reviews?

Attitudes to water and the environment, and behaviour change in water usage, will become increasingly important, to protect our natural environment from harm. We think this should be recognised as a goal for ongoing customer engagement, as well as in preparation of companies' plans, for example testing the extent to which customers prioritise demand-side measures, and the propensity of the customer base to change their behaviours. We think that engaging with customers on protecting the environment should also be a priority and recognised as an important goal for Ofwat.

A further point that we think Ofwat should take into account is how customer research is used in plans and in developing and delivering services to customers. A clear indicator of a good outcome is to be able to clearly see the path between customer research, insights gained, and how plans have developed or changed as a result of those insights.

Q3. Do you agree with the principle that in areas that are of common concern to all customers within a nation, evidence of customers' preferences should be generated in a consistent manner such that results are comparable? If so, why? If not, why not?

We agree that gathering evidence in a consistent manner should ensure comparability, and it will remove any variations in results that are caused by differences in timing, supplier, question design and framing, and methodology.

We also think it would allow for insight to be gained more efficiently for customers. In previous price reviews, engagement, particularly for valuations, has been costly and repeated in each company, largely for identical service attributes.

We think there needs to be careful consideration of the scope of any national research, and that national research should be undertaken where there are clear benefits of doing so. For example, we can see a strong argument for national research informing some of the common performance commitments. The evidence gained from customer engagement at PR14 and PR19 shows us that there is little variation between customers' views on the key priorities for companies such as tackling leakage and providing high-quality water. However the valuation research showed very different valuations for those same priorities, which is difficult to reconcile even when accounting for differences in timing, methods, supplier and survey instrument. National research would enable simultaneous engagement to produce consistent and comparable results, delivering considerable economies of scale in the process.

However, we think other types of research, for example qualitative research into support for vulnerable customers, have a much less compelling case. Results do not need to be directly comparable, there are few economies of scale to realise, and companies will be best placed to understand the local issues that customers will be concerned about.

In addition, there will need to be careful consideration of how any national research can be dovetailed into companies' local engagement. While using national engagement removes some of the problems we have seen at previous price reviews as set out above, it also risks introducing new issues. Ensuring that the process and methodology take account of integration and calibration of, for example, nationally gained valuations alongside the results of local engagement, will be necessary. For example, we note the current CMA consultation

on leakage, which proposes different approaches to calculating targets for different companies. Should Ofwat adopt that approach for leakage or indeed more widely for PR24, this could impact on the comparability of engagement on those targets.

For the avoidance of doubt, we do not support third-party organisations such as CCW or Ofwat engaging with customers on behalf of companies and providing customer insight to companies (as this could undermine the direct relationship with customers that companies across the industry have created). It would also be very confusing to customers who have low awareness of industry organisations other than their own supply companies.

What we would support is wider and more transparent sharing of customer research by such organisations, so that companies can benefit from the third-party insight. This would provide a useful triangulation point and valuable cross check, to help assure that customer insights do accurately represent customer preferences.

Q4. If we make use of collaborative nationwide research in future price reviews: Which aspects of business plans do you think should fall within the scope of this research? Which organisations do you think should be involved in steering this research? When should this research be undertaken? How should this research account for differences between England and Wales?

Scope of national research - we support the principle that preferences such as valuations for common performance commitments should be gathered at a national level, with appropriate sample sizes to enable any local variations to be identified. As we have previously set out above, we think it will be important to consider carefully what engagement benefits from a national approach, and what needs to be carried out at a local level, to ensure local priorities are not overridden.

Steering of national research – we think the organisations paying for the research and using the results should steer the work. In practice, this means representatives from each company would need to be involved which may be cumbersome, so consideration should be given to use of an existing industry body such as Water UK or UKWIR to act in a steering capacity. In that case, some companies may wish to exert direct membership of any steering committees, while others may decide that those industry bodies are well placed to steer the work on their behalf.

Timing of research – the timing clearly needs to reflect the timing of the price review. We urge Ofwat to consider and publish a timetable at the earliest opportunity possible, setting out the key submission dates. In any case, we think there is an urgent need to start any national research within the coming months, to enable it to feed into the Water Resources Management Planning process, although we note there is already a co-ordinated approach to a large extent being driven through the regional water resources groups. Research around other areas of companies' plans is needed very soon, in order to help inform the WRMP process in the context of customers' priorities and valuations for the whole business plan.

Q5: To what extent do you think it would be necessary for us to provide guidance on customer engagement, assurance and other issues at future price reviews if we made – or did not make – use of collaborative nationwide engagement?

We think Ofwat should set out its expectations about engaging with customers regardless of whether national engagement is pursued. Ofwat should provide guidance on what good looks like, and be clear on its expectations and, at the same time, should refrain from providing detailed instructions on how or when to engage customers. The same principle applies to assurance. In both cases, Ofwat should be clear on how it will assess business plans, how it will consider customers' priorities, and what assurance it deems necessary, so that companies can ensure the appropriate evidence accompanies their business plan submissions. In particular, Ofwat should set out how it will use customer engagement and the insights gained from that engagement in its assessment of plans, and consequently in the level of investment included in determinations.

As we have set out above, we do not think it appropriate for intermediary organisations to conduct customer engagement, so it will be important that companies understand Ofwat's expectations in this area.

Q6: To the extent that you consider further guidance is necessary, what areas should this cover?

As set out above, we think Ofwat should set out its expectations early in the price review process. Ofwat should be clear if they consider that there are areas that should or should not be included in the scope of engagement, and also whether they have expectations over particular methodologies, such as willingness to pay. The CCG Aide Memoir was a useful tool that Ofwat provided at PR19, it would have been even more helpful if that had been produced earlier in the process so that companies knew at the outset what topics Ofwat expected companies to engage on.

Q7: Are there other models which you think we should consider for providing assurance at future price reviews? If so, what are the benefits of these alternative approaches?

No views in particular here.

Q8: To what extent do you think that the research techniques which have previously been used in the water sector are suitable to enable companies' business plans and our final determinations to reflect customer views? Do you think any particular approaches should be revisited?

When considering whether techniques are suitable, we think the key consideration is whether they were effective in understanding customers' views, particularly where they would not otherwise have been known, and ensuring they were translated into usable insight that drove companies' business plans. It is clear from companies' business plans that collectively companies have made use of a wide range of techniques, used a number of different suppliers and engagement plans were assured by separate challenge groups.

These differences and variations in techniques largely resulted in sets of similar insights, so assurance can be gained that through multiple ways of engaging, a consistent picture of customer views has emerged. This indicates that the techniques were suitable.

Another way of testing whether plans reflect customer views is to consider the outcome of consultations and acceptability testing of plans based on the insight gained. By and large, acceptability is high and feedback during consultations is positive. This should provide Ofwat with a level of reassurance that plans are in fact based on customer views, and hence the techniques suitable.

Q9: Do you think that there are alternative approaches that we might usefully adopt in water, including those used in other sectors and potentially outside the area of economic regulation? If so, which techniques and why? If not, why not?

We agree with the intent behind this question in that water companies should look outside the sector for ideas on new ways and methods to engage with customers. Customer expectations of us, in many aspects, do not differ from that of companies in other sectors. Further, these other sectors may have a longer track record of actively seeking customer views, and may be more advanced and more innovative, which we can learn and benefit from.

Q10: Are there any areas of the price review where the scope to solicit informed opinions from customers is intrinsically limited?

We do not believe there are very many areas that are intrinsically limited. We note that there have been opinions expressed recently that customers may not have understood some of the more complex topics, and indeed themselves express opinions that the topic is too difficult for them to understand, and they want to leave some questions to the 'experts'. A lack of interest is also sometimes stated.

We do not agree that this means companies should avoid attempting to gain insight on technical or complex subjects. We find when we engage with customers on things outside their immediate day-to-day awareness, if we engage in such a way as to spark their interest in water, they can become very engaged and interested in all the issues the industry grapples with. We think that engaging in ways that are interesting to customers, at a time and in a place of their choosing, creates situations where customers are able and willing to invest time in understanding sometimes the most complex topics, and providing an informed opinion on it. Clearly the use of engaging and informative material is a key part of this process, as well as committing time and effort on the company's part, to providing all the relevant information.

That is not to say that all customers will be prepared to do this but providing a small but sufficient number of representative customers do, companies can gain insights on the vast majority of topics. One topic that we do think is not appropriate for customers to give views on is the return allowed in plans for investors. This is by its nature a matter for investors alone to decide what an acceptable return is for them.

Notwithstanding the above, we do think that engagement should be focused on topics that are material, and where there is a real choice to make. We think that research should be focused on areas that will make a difference to companies' plans, and there should be recognition that further research on topics where companies already have a good understanding of customers' priorities, or where there is no choice (for example complying with legislation) is not an efficient

use of customers' money. That is not to say that companies should consult with customers over every detail of running the business, as it is the company's role to run the business, but companies should be able to engage with customers over topics that do have an impact on them.

Q11: Do you think there are other ideas we should be considering for shaping customer engagement at future price reviews? If so, how would these ideas help deliver on the goals proposed in this paper?

No views in particular here.