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Please ask for
Our Ref
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Dear Sir/Madam

Ofwat Consultation: PR24 and beyond: Reflecting customer preferences in future price reviews

We welcome this consultation and the proposals set out within it. Whilst we understood, and indeed strove for a step change in meaningful customer engagement it was clear that Ofwat felt we and the wider industry fell short of expectations – particularly on how best to establish customer preferences to inform the Business Plan.

One particular challenge that we faced arose where our customer research did not support the incentive mechanism framework related to ODIs. In particular customer research indicated significantly lower valuations (for rewards and penalties) that Ofwat's indicative range. This may have been because:-

- a) in general our customers receive a good level of service and therefore did not expect significant improvements,
- b) our average household bill is £100 per annum and thus any significant monetary sum, driven by rewards and penalties, could represent a material percentage of the bill
- c) our methodology for determining this complex issues was not appropriate.

For these issues in particular we welcome Ofwat proposing to be involved in the process. We do not see this issue as being company specific. The benefit of one exercise being undertaken at the same time using the same methodology will at least ensure consistency across the results. It will also reveal how the customers we serve feel about their wastewater service and indeed how it may change their valuations when asked about both services together.

However, to ensure legitimacy in the process and that all stakeholders have confidence in the results, there will need to be clear independence in both the development of the programme and the interpretation of the results.

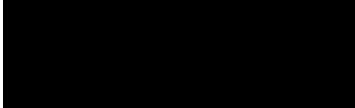
We appreciate this will not be a straight forward exercise, but in previous reviews there has been evidence that industry-wide research has worked well. Finally we will willingly contribute to the cost and development of such exercise(s) and feel that this could in fact drive an efficient approach to elements of customer engagement.

We do, however, feel that there will still be a need for additional company research to address company specific issues. This may include support for enhancement expenditure, for company specific programmes (such as enhanced metering) and for community based activities.

Finally we did not experience the issues raised in the consultation relating to the independence of our Customer Challenge Group. Whilst acknowledging that our members are not all experts in customer engagement, they are well informed and more than capable to critically review the results of the research and ask how the company how this drives its plan. We intend to continue to use our CCG as a genuinely independent body, holding the company to account on delivery. We believe they were effective in challenging the aspirations in our plan and do not recognise the observations made.

We have set out below our observations in relation to each of the questions. We would be happy to discuss any of our points further if it would be helpful.

Yours faithfully



HELEN ORTON
Finance and Regulation Director

Questions

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

We strongly agree and support the six goals for customer engagement.

We would suggest that at PR19 we had sole responsibility for engagement with our customer base, and ultimately this will remain our responsibility.

We note the expectation to develop the scope of the research to ask questions relating to citizenship. Historically guidance for valuations and acceptability focused solely on bill payers. Whilst at PR19 we did engage with future bill payers, obtaining the views of citizens appears more challenging. Each company will need to determine its programme given its circumstances and responsibilities. We will need to provide appropriate supporting information and be involved in determining the scenarios being tested with all customers and citizens.

We strongly support the goals of:-

- proportionality – with higher quality research which is trusted by all stakeholders
- transparency – so that stakeholders can see why decisions have been made
- collaboration – with other stakeholders (including the wastewater provider) to ensure we are using appropriate techniques

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

We would also add the goal of consistency. Variations in results across the country will be the result of customer preferences not methodological approaches.

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 strongly support this approach, as outlined in our introduction.

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?**

We would suggest the issue of ODIs – both targets and incentive rates would be appropriate for nationwide research. Further, acceptability testing of the company plans, draft and or final determinations would also be efficient. Finally there would be merit in considering the approach to vulnerability and affordability at a national level.

The industry will need to identify a small team (of say no more than 4 people) to work in a group with Ofwat, CCW and indeed chairs of the Customer Challenge Groups. It could be expanded to include other regulators including Environment Agency, DWI and Natural England. Although we note that in our experience widening the membership increases the time required to make decisions. We would suggest Ofwat should ensure the views of other regulators are reflected in this process.

We assume research will be undertaken in each company area with sufficient sample size to ensure the results are representative of the customer base.

To ensure legitimacy in the process there must be a high degree of independence – both in establishing the methodology & approach and in interpreting the results. Even the most rigorous research can be skewed by unconscious or conscious bias and interpretation of results can be subjective. It will be critical, therefore, that all stakeholders can have confidence in the results and as such there will need to be an opportunity for industry representatives to be appropriately involved in developing the approach taken and for a level of third party independent oversight.

Additionally, companies will need to provide support data on agreed topics and scenarios they wish to engage on. For example if we are trying to understand further improvements in leakage of say 10%, customers will need to understand the bill impact, which will vary by Company.

We are not sure of the PR24 timetable yet, but would suggest results from ODI research and affordability research will need to be available no later than 9 months before we are required to submit Business Plans. Acceptability testing (of the company plans) should provide results no later than 3 months before submission of Business Plans, to allow companies to respond to these findings. Rolling the PR19 timetable forward 5 years, with Business Plans being submitted on 30 September 2018, would give ODI and affordability work completed end calendar year 2022 and acceptability research complete end June 2023.

We are not really sure of the differences required to meet Welsh expectations, but would suggest these three areas of research would apply equally to Wales.

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 would still welcome guidance on all of these issues irrespective of the degree to which collaborative national engagement work is undertaken.

This will not be the only piece of engagement work we will need to undertake and whilst we may observe best practice being applied in any national study, guidance would ensure our Business Plan

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

At PR14 and PR19 Ofwat consciously did not provide guidance predominantly because they felt it would result in all plans complying with a tick list and stifling innovative approaches.

Whilst we understood this position, we feel that the lack of guidance did contribute to the assessment Ofwat made of the quality of customer engagement.

If the “competitive” element of preparing plans is removed then greater guidance would be of help to all companies.

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?

We felt the current model was effective. We presented our research programme to our CCG and they actively challenged the methodologies given their varied experience in this issue.

They also made time to understand the results. Whilst acknowledging that our members are not all experts in customer engagement, they are well informed and more than capable to critically review the results of the research and ask how the company how this drives its plan.

We intend to continue to use our CCG as a genuinely independent body, holding the company to account on delivery. We believe they were effective in challenging the aspirations in our plan and do not recognise the observations made by Ofwat.

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?

We would look to the experts to advise on how best to approach any issue to meet any guidance provided by Ofwat. We do not currently have a great deal of experience of the use of big data or Social Media to form an understanding of customers’ preference.

In general we have relied on stated preference techniques to be the main methodology for collecting customer views. We see feel that this has a strong part to play in capturing customer views.

Customers always engaged well in our focus groups, and these were an effective way of understanding the detail of any issues.

We successfully engaged with a Customer Advisory Panel for 6 meetings, which was very beneficial. However, the observations made by Ofwat about the CCG could more easily apply here; there were very few genuine challenges.

Our preference would be to be in a position to utilise revealed preferences to determine valuations. We are aware of the novel work employed by some in this area but typically these were undertaken in “laboratory” conditions. What we actually need is real “in-time” customer responses to events, for example when an interruption to supply has just occurred at 8am in the morning, seek the customer view of how much of an impact it had.

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?

Your discussion document has highlighted the use of the Citizen Assembly to ascertain customer views. This is similar to our customer panel.

In many cases customers do not expect to be asked many of these questions. They expect that there are experts who act in the interest of all. This is certainly true of water quality issues, where the Drinking Water Inspectorate “represent” the interests of the consumer. We would also suggest the Environment Agency act in a similar mode to protect the environment.

It is often difficult for individual customers to act in the interest of all consumers, rather than act on their own behalf. We saw this issue in our CAP when we spoke about making greater bulk supplies available to Southern Water’s customers in Hampshire. Customers supported transfer as long as there was no detriment to their supply. Based on this experience regional decisions need to be taken at a higher level than the individual customer.

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

We would suggest there are limitations to much of the research programmes. At an individual customer level it is difficult to value improvements in a service if you have never experienced a failure. In many cases therefore our stated preference work is based on judgements, not experience.

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?

There is already considerable customer engagement undertaken by companies when they prepare their Water Resource Management Plans. The need for more engagement arises for the next round of plans as a result of the need to develop regional plans.

We would support a programme of research which could be used for both water resources and business plan purposes. Such combined research could include wider stakeholders including Defra and genuinely test and inform issues such as metering.