South Staffs Water Cambridge Water

Ofwat

4th Floor
21 Bloomsbury Street
London WC1B 3HF

22nd July 2021

SSC Response to 'PR24 & Beyond: Creating tomorrow, together.'

Dear Ofwat,

Thank you for the opportunity to respond to the 'PR24 & Beyond: Creating tomorrow, together' consultation. Please find our detailed response below.

Overall, we are very supportive of the approach and the four themes outlined in the guidance. We understand the importance of long-term planning when tackling the significant challenges around resilience and the environment that we face as a sector, so we welcome the recognition Ofwat gives this. We agree that it is important to maximise the social and environmental value of the Price Review process by streamlining where possible and reducing regulatory burdens, in order to focus on the areas that matter most. We also support the continued work around understanding customers and communities, as their views are at the centre of our planning. Efficiency continues to remain essential for maintaining best value for customers and we believe innovation will enable us to do this.

However, in order for us to meet Ofwat's expectations in these areas, we would ask for early information and engagement on all the suggested areas of change from PR19. We will also seek to understand how Ofwat will take account of long-term planning, whilst maintaining the five-year price controls. Also, to ensure there is sufficient time for engagement with our customers and stakeholders, we urgently need clarity on Ofwat's approach to nationwide engagement. We welcome Ofwat's plan to give early sight of cost models and provide the expectations on ODIs as this will streamline the process and allow us to focus on what is most important. With this early insight, we believe we will be able to produce a high-quality plan which will ensure maximum benefit for our customers, communities, and the environment.

We look forward to engaging with Ofwat further on these areas as we plan for the next period.

Yours sincerely,

[redacted]

Caroline Cooper

Strategy and Regulation Director

SSC Response to ‘PR24 and Beyond: Creating tomorrow, together.’

2. Ambitions for PR24

Q2.1: Do you agree that the themes we have suggested for PR24 are appropriate for England and for Wales?

We welcome the focus on the long-term as we know it is vital for our customers and the environment to take a holistic long-term strategic view of our actions. However, there are challenges associated with delivering a long-term strategy within the constraints for five-year planning cycles, as recognised in the guidance. We will explore these challenges further in section four.

It is pleasing to see that environmental and social value are being pitched at the same level as customers. We are custodians of our environment, and it is part of our role as environmental stewards to ensure we maintain and enhance for future generations. In our early customer insight work, it is pleasing to see this also reflected in our customer views.

We are keen to build on our customer engagement work undertaken at PR19. The learnings from all that work have positively defined and shaped our delivery of AMP7 and we believe our focus on the local community distinguishes us from the sector. Therefore, we welcome the recognition of understanding customers and communities in the PR24 themes.

We recognise that delivering efficiency for our customers is key, and we see innovation as a key enabler in delivering some of the longer-term sector level targets. We must have the ability to better advance technical innovations moving forward. Whilst not all investments will work, some will and will be beneficial. Sharing the learning from Innovation Fund projects could support the delivery of long-term goals.

Q2.2: Do you have comments on the considerations we've identified as relevant to the design of PR24?

Early clarity of the regulatory framework for PR24 will enable us to think more strategically over the long-term so we welcome early engagement and publication of expectations. We are still concerned that 5-year price reviews make multi-AMP investment proposals a challenge and trust Ofwat will consider this in its methodology. We consider this issue further in section 4 and suggest Ofwat includes specific assessment for long-term delivery to avoid continued short term focus.

Our customers have seen the value of using outcomes as they have driven service improvements over the last two AMPs, and we believe they will continue to do so. However, they can often drive short term behaviours to the detriment of longer-term investment needs that do not necessarily deliver in AMP service improvements. We are pleased to see Ofwat recognise this and are willing to support any workshops where this is explored.

We appreciate Ofwat’s recognition of the impact of regulatory burden and the need to minimise this where possible. Although, we were disappointed that there were no recommendations specific to small water only companies as our resources are particularly stretched by price review processes compared to WaSCs. We are happy to work with our WoC peers to suggest how this could work.

We are generally supportive of collaborative customer engagement and understand the benefits of setting sector wide commitments of service levels, we still believe that regional values are important and should be recognised in company plans. We also need to ensure we consider future customers' values when setting long-term service levels as we are aware that customer priorities can develop and evolve quickly.

Q2.3: How should we evaluate our progress, and how can we best develop or use appropriate metrics to do so?

We encourage Ofwat to measure its progress by assessing its general project management throughout the process. For companies to submit and deliver the best business plans possible, we require a set timeline for the process so that we can ensure the appropriate resourcing. We also need a reasonable amount of time to respond to Ofwat publications and information requests.

Regular touchpoints with companies and stakeholders to listen to feedback will help inform Ofwat of where there are challenges. We think having a company liaison individual at PR19 worked well when we had queries about the process.

3. How we regulate

Q3.1: How can we best regulate the water sector to deliver value for customers, communities and the environment? Do you agree, or have comments on, our suggestion to maintain our 'building block' approach based on outcomes, costs and risk and return?

Please see our specific responses to questions below.

Q3.2: To what extent is greater co-ordination required across the sector? In what ways might we promote better co-ordination across companies and with other sectors, and how might this benefit customers?

We discuss coordination across regulators in section 7 as we believe there are synergies with other regulatory processes.

We already benefit from collaborating with other WoCs collaboration as we face similar challenges that we can tackle together. The industry will also benefit from the shared findings from the innovation fund.

4. Increasing focus on the long-term

Q4.1: What are your views on the need for greater focus in companies' regulatory business plans on how they will deliver for the long-term?

We agree with Ofwat that long-term plans are vitally important for the water sector. Although it will be challenging, we think that setting our five-year plans within the context of a longer period will be a positive move and allows some longer-term sensible conversations to be had on growth, resilience, asset health but also on customer service, affordability, and wider economic planning. This can only benefit future customers if done well.

However, uncertainty increases as we project further into the future. Any long-term framework needs to be able to accommodate that uncertainty and deal with it in a pragmatic way that does not hinder the incentives on companies to plan more than five years into the future.

Another challenge is five-year price review periods will always mean the focus will be short term, unless the long-term is somehow enshrined in the process. We urge Ofwat to also not fall into a trap of having a short-term mindset when it is working with the industry on these long-term goals, its costs, incentives, and activity and service levels. Whilst affordability is a key concern for our customers, the priority should not be to cut bills in the short term at the cost of sustainable long-term investment. This is not beneficial for customers or the environment and will likely impact on future generations of water customers. Therefore, regulators have as much of a role to play in enabling the long-term vision as companies do. Ofwat must design a price review process that makes allowances for us to plan for the future.

One suggestion that could mitigate short term focus in the price review is having a specific assessment for long-term delivery. This could be assessed based on the long-term service improvements, achieving net zero and environmental improvements. There must also be an understanding that there are constraints from an affordability perspective in reaching these long-term goals as we endeavour to keep bills stable in real terms. We welcome that this consultation is asking these questions and we hope for an open and free-thinking debate on how it is achieved.

Q4.2: What should long-term strategies seek to cover and what details should we expect companies to set out in business plans? Would common requirements help us and other stakeholders to understand each company's approach?

The core of the water sector's activities are asset operation to deliver today's service; enhancement to meet new obligations, growth, or to improve service; asset health (maintenance) investment and long-term resilience planning; and customer service, affordability and vulnerability. And to enable all this, a strong and resilient financial structure with appropriate returns and incentives to encourage investment and innovation.

We do think that setting a number of common areas (such as those we have outlined in section 9) would make it easier for Ofwat to understand companies plans, easier for companies to be consistent with each other, and make it easier to set out the overall effects and net benefits across the sector. It will also allow conversations to be had on long-term aspirations and policy direction for these themes and to set some top-down nationwide aspirations if appropriate to do so.

Some of these aspirations are already in play, such as net zero carbon or leakage reduction. Others are still to be defined, such as the long-term asset health, resilience or water resource objectives.

As Ofwat is considering how to set more common service levels, it is imperative these fit within a long-term policy aspiration that has been tested and is beneficial over the long-term.

Q4.3: How would this build on the work completed in strategic planning frameworks?

Please see detailed answers in section 7.

Q4.4: How can we allow such strategies and plans to adapt to new information at future reviews while continuing to hold companies to account to deliver expected benefits into the future?

It is inevitable that longer term plans come with more uncertainty and it is right that plans embarked on now have sufficient break points for review in future. Adopting a coherent vision across the sector will enable this, as this vision and the long-term aspirations it derives can be continually reviewed. It is unlikely that certain strategic goals will ever be dropped or reversed - for example reducing leakage or consumption is always going to be a thing - but plans and technologies can change and the five-year cycle still provides an opportunity to adapt to new information and modify short term plans accordingly.

Q4.5: Would providing our views on comparable aspects of companies' plans in advance of business plan submission streamline the price review process?

Yes, and we see this as an absolutely essential step in the build-up to submission under Ofwat's proposed framework in the round. We believe it would help to streamline the price review process as it should help ensure that company submissions are more closely aligned to Ofwat expectations, or at the very least differences would be more clearly understood.

Fundamentally, Ofwat's desire to look at common service levels (with deviations from common targets only by well evidenced exception) means that conversations and studies need to be happening very soon to derive appropriate levels of stretch for those themes. The sector including Ofwat needs to have a long-term view of what service levels are appropriate to set, what those ambitions are over the long-term and what five-year targets should be within that.

We do not want to see a repeat of the back and forwards discussion that we experienced on leakage (as an example) at PR19. An open and collaborative discussion up front, setting the core themes and long-term aspirations will allow all companies and Ofwat to deliver a better long-term outcome with appropriate efficient costs as well. We encourage Ofwat to start getting this buy in from companies now and begin to generate the long-term aspirations in conjunction with the sector.

Q4.6: Should we adopt a collaborative approach to developing Welsh companies' plans at PR24? If so, how should we go about doing this?

We have no comments.

Q4.7: What are your views on how we could provide clarity over the long-term regulatory framework?

The key to providing clarity is commitment from all parties, including Ofwat and other regulators. We need to know what we are working towards, in terms of long-term service, and then we can start to set meaningful shorter-term steps towards those long-term goals. To do this, more work needs to be done on what long-term aspirations should be and if they are genuinely beneficial. For example, on leakage, on metering technologies, on live networks – these areas have potential to shape the future but need strategy and investment commitment over the long-term to be successful.

Additionally, we think that the successful approach of Green Recovery bids could be adapted to be incorporated into the long-term regulatory framework. This has shown how it is possible to adapt approaches quickly to meet changes to future needs by securing a commitment to funding in future periods for environmental investments today without having to wait until the next Price Review.

Q4.8: Are there barriers to water companies changing how they deliver their core functions to deliver greater environmental and social value? How can we address any barriers?

We do not think there are barriers directly as if the long-term vision and commitment is there from all parties then companies can work to deliver this. In the past, the issue previously has been short term policies but, as discussed in Q4.7, a focus on sector wide long-term aspirations at PR24 and beyond would mitigate this.

Q4.9: Do you have any further suggestions for increasing the focus on the long-term? If so, what are these?

The approach to setting long-term strategies and aspirations for the sector should be collaborative between regulators and companies. We need to work together with Ofwat to set expectations on what the sector should deliver in the next 25 years including leakage levels and consumption as examples.

5. Strengthening incentives

Q5.1: Should we undertake an initial assessment of plans at PR24? If so, what areas should we focus on in this assessment?

We welcomed the Initial Assessment of Plans at PR19 as it gave us the opportunity to reflect on key areas where we had not met Ofwat's expectations and enhance our plans when comparing ourselves to the industry. The areas assessed through the IAP at PR19 where targeted and focused and we consider we delivered a better business plan due to the feedback we received. Whilst we support streamlining the process where possible, the IAP and subsequent resubmission helped us resolve some issues earlier, thereby reducing the regulatory pressure later in the process.

If Ofwat were to remove this stage, we would require robust and timely guidance to support our initial plan so that we could ensure alignment to Ofwat's expectations. This would include well defined ODI policies, early publication of cost models and completion of customer engagement prior to the first submission. We did not have this information at PR19, hence the importance of the IAP. We would also request a longer period to respond to the draft determination if this approach were to be adopted.

Q5.2: Should we consider adopting a more light touch approach at PR24 for companies with a strong track record of delivery during the PR19 price review period? If so, what factors should we consider in our assessment and why?

Yes, companies with a strong track record of delivering for customers should be rewarded with a more straightforward price review process. It would also act as a further incentive for high performance.

We believe this should be assessed based on:

- Efficiency benchmark for Botex (UQ)
- Service performance
- Financial resilience
- Delivery of funded enhancement programme

However, we support the return of the 'do no harm' principle to safeguard against companies losing out from any betterment from the price review process outcomes.

Q5.3: Should we streamline the price review by combining different steps in the process? If so, which of the three options outlined in this paper should we consider? And are there other options we can usefully consider?

As outlined in Q5.1, we support options 2 and 3 as we believe we delivered a better business plan as a result of the IAP stage.

Q5.4: Is a different approach needed for the initial business plan assessment for companies in England and in Wales?

We have no comments.

Q5.5: What incentives should we provide for high quality plans at PR24? If we don't make use of early draft determinations, how else might we strengthen incentives to table high quality plans on first submission?

We believe that the assessment of high-quality plans should focus on the strength of aspirations and customer benefits over the long-term, as the focus on cost efficiency my counteract the long-term strategy goals.

The reward for a high-quality plan should mean that minimal changes are required to the plans submitted. We support the 'do no harm' principal across all areas.

Q5.6: How might we set cost sharing rates at PR24? Should we consider an approach based on our ability to monitor companies' asset health status?

We think that cost sharing rates should be set based on how efficient companies are ranked on their botex. For the frontier and upper quartile companies, additional incentives should encourage further efficiencies to be targeted and so cost sharing rates should be set in this way, for example keeping 60% of outperformance.

Q5.7: Which areas should we be considering targeted challenges for at PR24, and why?

We believe there is benefit in having targeting challenges for areas where a collaborative approach across government, regulators and companies to help us achieve a common goal for example specific environmental challenges.

Q5.8: Should we use innovation specific incentive mechanisms at PR24? If so what would these be, and what would they add in addition to the other mechanisms outlined in this chapter?

We have welcomed the innovation fund and see particular benefit coming from companies sharing their findings. This will help drive improvement across the sector for challenging areas.

We are unsure how an innovation specific incentive mechanism would work in relation to this. It is important to consider the fact that not all innovation is successful in delivering improvements in assessing this mechanism. Therefore, we request clarity on the methodology.

Q5.9: In what ways might we promote the themes of EBR through PR24?

We agree with the principles of Ethical Business Regulation and believe we incorporate this already through our ESG board committee where we measure our won improvements on a range of metrics.

6. Reflecting customers’ preferences

Q6.1: What are your views on the merits of our proposals for a collaborative approach to standardised and/or nationwide customer research to inform company business plans and our determinations?

We continue to support that there is a need for collaborative national and standardised research approaches to support local engagement. However, there needs to be a clear framework in place to map out the national, regional and local led customer engagement activities based around the following points and the decisions should be made in the context of the long-term vision for the sector and not be based solely around Price Reviews. In addition, any collaborative projects should have clear terms of reference in place with Ofwat guiding the process to ensure an equal stake in terms of input between water companies to ensure fairness:

- What decisions are the insights going to drive: strategic long-term common issues (e.g. Customer preferences around investment decisions to ensure long-term resilience of clean water supplies) vs tactical decisions (e.g. developing a company website) that will improve the service/experience for customers in the shorter term.
- How important combability of the insights are to ensuring best outcomes for customers – e.g. setting ODI rates for common performance commitments vs the best way to implement a local level community partnership scheme.
- The level of risk that the outputs of a national study would end up needed to be duplicated at a local level to provide water companies with robust insights to have confidence in these to support decision making.
- Whether national/regional studies can be co-ordinated in a timescale that does not impact on water companies' ability to make decisions and/or take appropriate action in response to customer feedback.
- Consideration over where innovation may be stifled by making a project nationally led vs letting companies engage locally using a new technique or an approach more suited to the challenges they face in their supply region.

Over time, there is clear and obvious need for national research to determine customers’ preferences of the following areas to prevent duplication of effort and resource and ensure comparability. We fully support the approach of national collaborative research as long as it is designed to enable any regional differences to be drawn out and the approach then allows water companies to understand these and take appropriate action in their plans in response. The development of a national approach should be geared around best outcomes for customers up to 2050 and not around what is best for PR24, although the two should support each other. This would align too Ofwat’s direction of travel around looking at a business plan over the longer-term. The current guidance from Ofwat is perhaps too focussed on just PR24 and not the long-term picture and how PR24 fits into this.

It is our view that the following types of projects would benefit from a **national led approach.** Many of these are ones where companies already have a bank of existing insight that can be built upon and ensure the whole sector moves forward to meet customers’ and wider stakeholders’ changing expectations:

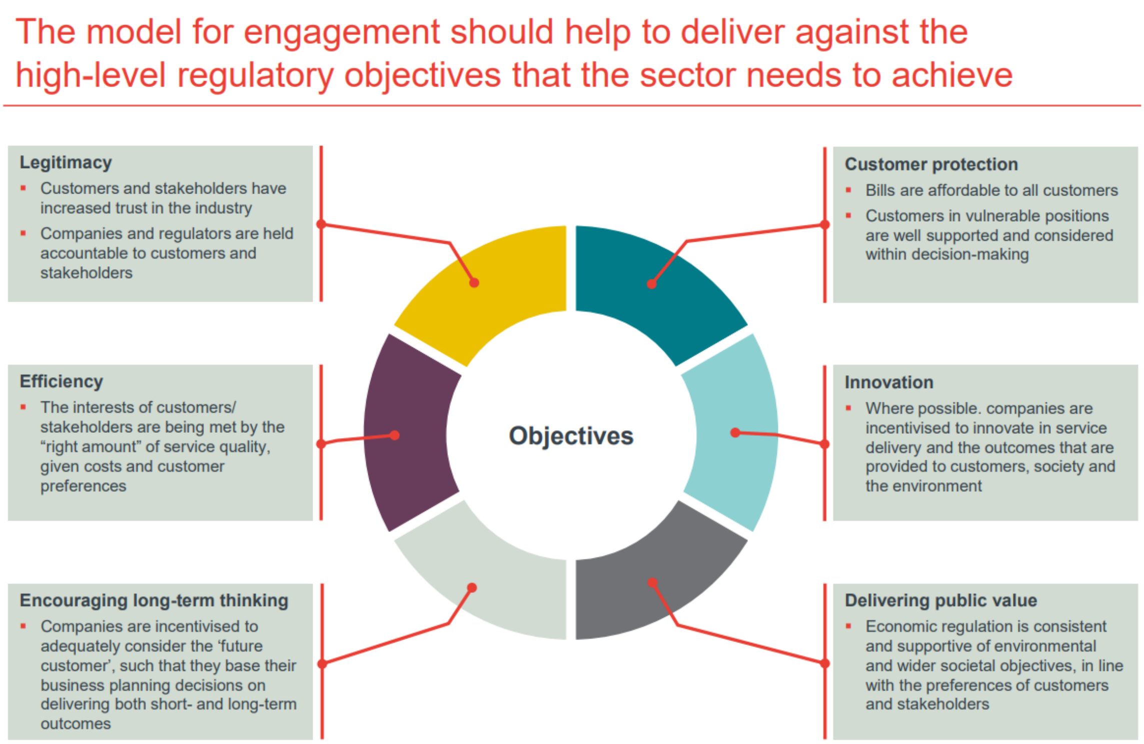
- Customers’ priorities for the services water companies offer and investment decisions they should make. With our Customer Priorities Tracker evidencing that customers’ priorities are changing at an ever-quicker pace (some of these due to COVID-19) then Ofwat also needs to consider how it will best enable water companies to flex its plan within 5-year Price review cycles in order to make the right investments to deliver what customers expect.
- Engagement around governance (ESG) matters, including corporate structures and where consistency is required to ensure trust in the water sector is achieved long-term
- Engagement to underpin the setting of national targets (e.g. PIC), the industry’s vision of what role the water sector should play in adding value to society and the environment and understanding the differences between customers’ views of their water services in the context of their household/business/organisation and that as a citizen.
- Studies among customer groups who deal with multiple water companies, where to deliver customer value, national approaches to service delivery (and therefore engagement) are needed – such as NHH retailers and developer engagement
- Engagement related to national challenges to ensure consistency of the approach – such as where a common policy framework is needed to lead to positive customer outcomes to address affordability issues (e.g., adopting CCW’s recommendations of a single national tariff), lead pipe replacement and supply pipe ownership, smart metering roll-out, how to tackle climate change/reach zero carbon. Citizen Forums for example cold play an important role here, compromised of customers from across all regional areas.
- Engagement around customers preferences into the setting of ODI rates for common performance commitments - Willing to Pay (WTP) studies – providing the many challenges can be overcome. For example, would the national study undertaken be just focused on the agreed “Common” Performance Commitment areas for PR24, or would each company also bring into the study a list of attributes to test that are bespoke to their customer supply areas. If both, then this would still have implications for comparability as customers in different regions are trading off different service valuations. However, industry level WTP analysis reviews highlight that the biggest influencer on WTP value incomparability is the importance of scope sensitivity to customer valuations. If you offer more units of service change in a WTP study you get a lower value per unit, and vice versa. Consequently, if you control for the scope of service change offered and is presented to customers in a clearer way to allow them to better evaluate the level of risk vs their priorities, then the industry has an opportunity to eliminate a significant part of the difference across companies in valuations. If a national study for WTP looks unachievable there is an argument to just set national guidance that companies to adhere to around methodology, question framing and scope of service change for all the key attributes to be tested to ensure a more consistent approach and better comparability of results. There is also the issue of timings to set-up the collaborative approach given what is being proposed in terms of having a steering, advisory and delivery group. Given the challenges of building this approach from scratch, it is problematic whether a fully scoped and collaborative WTP study could be agreed and undertaken during 2022 to support the development of companies’ PR24 plans. It might be at this stage of the 5-year PR cycle that standardised research is the best option to deliver WTP customer valuations research for CBA to support investment decisions.

Standardised research has merits in terms of ensuring that companies use comparable methodologies for gaining customers' preferences/views on common subject areas which all water companies should undertake as part of their on-going business planning. These should focus on areas where companies need to undertake testing of very specific service improvement packages and so conducting this at a national level becomes problematic to manage. These include:

- WTP studies for CBA
- Acceptability studies of business plans or coast adjustment claims
- Small company premium testing.

However, very detailed guidance would need to be agreed for water companies and their research agency supply chains to ensure outputs were truly comparable and help overcome the challenges of differing valuations as seen at WRMP14/19. The approach should be approved and monitored by the nationally lead steering and assurance groups. However, a standardised approach will not help reduce the significant cost of undertaking only robust local research, particularly for WOCs and might be difficult to manage in practice unless a core of agencies is used to carry out the research – constraining the agencies that undertake the research may then stifle innovation. Due to this, it would be advisable to keep any standardised projects to a minimum. To avoid further duplication, CCW should also not undertake their own acceptability testing of companies' business plans if a standardised approach which they challenge is brought in.

We are also involved in the on-going UWKIR study (How should customer and stakeholder views be used in regulatory decisions?) and would stress the importance of the recommendations from this study be integrated into Ofwat's decisions on the balance of national/standardised and local engagement.



Without clarity in the next 6 months of what projects Ofwat is proposing to include in any national collaborative research project, or which ones are to be standardised it will make it problematic for water companies to scope some elements of their **local engagement plans.** It is important to avoid the situation of duplication and Ofwat then potentially giving precedent to the centralised research outputs which may not be of the best interest to customers at a local level.

Q6.2: Do you have any suggestions for how we best implement the collaborative approach to customer research for the price review?

We would agree that the proposed approach of having a steering, advisory and delivery group structure to deliver any collaborative research is the best approach. We would only support this structure if at least one appropriate representative of every water company will have a place on the delivery steering group proposed by Ofwat and that WOC voices will be part of the steering group to provide direction on the any collaborative research approaches. The terms of reference/remit of each of the 3 groups must be clear from the start and a process set-up to ensure clear and timely communication between the three to deliver the agreed programme. There would need to be certain organisations who sit on all 3 levels of the groups to enable this to happen. This structure could also ensure that any standardised research projects undertaken across the sector deliver positive outcomes.

The Terms of reference also need to cover what would happen in the situation if any water companies disrupted and/or or wanted to drop out of any national engagement led approach and there needs to be clear objectives set to ensure it can be proved that positive outcomes using of a national led approach were delivered vs the existing approach of using local engagement only to inform business plans.

Q6.3: Are there aspects of negotiated settlements that could be reflected in our price review framework?

We are supportive of the concept of negotiated settlement as it can work well, as seen in Scotland. However, it would require a big change to the regulatory approach and we are cautious about its inclusion in PR24 due to the timescales. We are also supportive of Ofwat's view and arguments that there is limited scope for using negotiated settlement in England in a widespread way, but that there is potential to investigate using negotiated settlements approach for very technical, but important, aspects of the price review process that the average bill paying customer struggles to engage with – such as caps and collars on ODIs, technical details of major cost adjustment claims and the balance of risk and reward between investors, companies and customers. However, as noted, this process could become resource intensive for all parties involved and may not reduce the regulatory burden for both Ofwat and, particularly, WOCs at PR24. The outputs from the ongoing UKWIR project "How should customer and stakeholder views be used in regulatory decisions?" will provide an important input into this decision and the role that a negotiated settlement might play at PR24.

Q6.4: What are your views on our proposals for customer challenge of business plans and assurance of customer engagement?

We are supportive of companies working developing customer challenge groups that are designed to fit their local strategic approach. The CCW recommendations on the future of customer challenge groups and the setting of minimum standards for research and assurance will also provide useful guidance for companies to develop appropriate approaches. However, there is still a concern that if challenge groups are not required to submit evidence to Ofwat of the quality of a company's local research and engagement then their role in the PR process is diminished. For example, would their voice be ignored if Ofwat decided their feedback should not be considered for a particular area of challenge?

There is currently little dialogue between CCGs and customers and the vast majority of customers are unaware that CCGs exist, although they are pleased that they do exist when they are informed about them in research studies. Thought would need to be given about who the customer challenge group is actually accountable to and how their input is evaluated in terms of delivering positive benefits for bill paying customers and the communities they live in.

There is also an issue of the level of resource it takes to manage CCGs in their current form and, if CCW's preferred recommendation is adopted, this could lead to yet more groups of stakeholders to engage with and manage on an on-going basis. As a WOC we would like the final guidance to be fully flexible to consider that WASCs with larger teams may be able to develop and manage different types of challenge groups over-time vs a WOC and that each customer challenge group should be judged on the outcomes they deliver for the companies they are challenging.

Q6.5: What are your views on whether we should develop minimum standards or provide guidance in other areas?

Setting clear guidance on minimum standards of research is vital for companies when developing their research programmes and also the level of customer challenge assurance on these needs to be in place. Guidance should cover areas such as:

- Methodological approaches and what subject areas these are appropriate for when engaging with customers on specific areas of the business plan development.
- Sampling frameworks and what constitutes a robust sample size, including what level of robustness is appropriate at sub-segment level.
- What analysis techniques can be used for different topic areas to be engaged on with customers.
- Best practice guidance for the balance of qual and quant expected when engaging with customers on specific areas of the business plan development.

The recent CCW paper into an updated triangulation framework provides useful context into minimum standards, but we would welcome Ofwat's view on these recommendations and how they will evaluate and compare water companies' approaches to triangulation at PR24.

Q6.6: How well does our proposed approach to customer engagement take appropriate account of the different regulatory frameworks in England and Wales?

The engagement programme should align to the regulatory framework to support successful outcomes in England and Wales, but it is important to ensure that water companies in Wales are also fully integrated into any national collaborative or standardised research undertaken to ensure consistency of approach and comparability of outputs.

7. Planning together for PR24

Q7.1: How can we ensure that companies bring together the outputs of the strategic planning frameworks in the most coherent and effective way for business plans?

In the case of RAPID projects, alignment across large strategic resource options that mean groundwork and consultation with Regulators undertaken prior to PR24 would reduce the onus on companies during the process, for example consistent assessments to avoid duplication of work.

Early engagement, consultation, and guidance from Ofwat on the draft regional plans and subsequent national plans would enable us to clearly understand the link from regional plans to WRMPs and through to PR24. Additionally, as we shift further towards regional and national water resource planning, Ofwat must make clear the requirements for this as part of our PR24 plans. We also need clear expectations on how we should incorporate strategic plans that we have not developed ourselves e.g., produced by councils and the EA. This would give us the clear line of sight required to knit all aspects of strategic planning together.

We are supportive of the move towards long-term planning outlined in the guidance. One area where this would be beneficial is WINEP schemes that should be over a longer period than five years.

Q7.2: What are your views of our thinking on our and companies' roles in engaging with other regulators between business plan submission and our issuing of the final determinations?

We would recommend a similar framework as in RAPID, where key updates and reviews are given to a core group of regulatory representatives. This would include consultations such as those completed within WRMPs.

Q7.3: How could we best involve a 'PR24 Challenge Panel' in the price review process to help ensure that our decisions best reflect the interests of customers, communities, and the environment?

Whilst we understand the idea behind the PR24 challenge panel, we should be cautious in avoiding duplication of effort and spend where existing processes are already in place. Our customer and stakeholder engagement when building the plan and throughout its development already captures and accounts for their views so the purpose of an additional challenge group should be clear.

As with the suggested changes to the Customer Challenge Group at PR24, we recommend that companies are able to build their own challenge and assurance processes to ensure engagement with all relevant stakeholders to reach a balanced view. This will also allow companies to build and develop relationships to allow more communication and input.

As outlined in the guidance, if Ofwat developed strong, long-term policies well in advance, then this would give companies clarity and enable Ofwat to judge plans more coherently, thereby lessening the need for a challenge panel. The challenge and research should be on the policy decisions and would not be needed later when implementing the policies.

8. Design and implementation of price controls

Q8.1: Do you agree with, or have any comments on, our general approach to the design and implementation of controls, i.e. to retain separate controls with the same broad structure as at PR19, but with improvements to our implementation?

Yes, we agree.

Q8.2: Do you agree with, or have any comments on, our proposals for specific parts of the value chain, i.e., for water resources, developer services, residential retail and business retail in Wales?

Water Resources

With respect to the change in the water resources control boundary, we would like more clarification on what this means for the reallocation of RCV and how this would be calculated. This could expose a larger proportion of the asset base to competition and change the level of regulatory risk for the sector.

We do however recognise from a cost assessment perspective that by combining raw water distribution and water treatment into a new treated water control, it will reduce the variation in approach to the allocation of costs by companies and hence improve cost modelling at PR24.

There needs to be consideration regarding the allocation of water treatment between water resources and network plus controls.

Developer Services

For developer services, we support contestable (on-site) activities being outside of the price control. It can function as a totally competitive market and should give more choice to developers.

We support a more fundamental change in the approach to regulating developer services at PR24 that would be more reliant on 'backstop' regulation ie removing developer services contestable activity from the network-plus price control.

The current arrangement whereby developer services activity features within the network-plus price control has challenges. The primary challenge is that developer services spend and revenue is expected to return to total annual value which has been set using industry average unit rates (per connection) and a series of assumptions relating to drivers of cost and revenue including connection volumes and mixes of work (proportion of unmade and made work, proportion of Self Lay market share). Inevitably there are differences between the assumptions made and the actual drivers experienced, and this makes it difficult to return to the forecast total value of revenue or cost for developer services which then has a knock-on impact on the total price control.

Further, the drivers of cost and revenue largely sit outside of the control of water companies and are generally customer driven. Whilst we can have robust forecasting approaches there will always be scenarios such as 2020/21 and to an extent 2021/22 whereby the pandemic has caused a drop in connection volumes and the Self Lay market share in our region which impacts our spend and revenue.

Removing developer services contestable activity from the price control would remove much of the aforementioned challenge.

Contestable developer services activity will still be regulated by the New Connections Charging Rules, the relevant sections within the Water Industry Act and by competition law to ensure that we recover our incurred costs and charge appropriately. Reporting within the annual tables can continue to demonstrate compliance with these regulations and principles. Moreover D-MeX provides an additional control to ensure that we are providing value for money for our customers as the cost of our services arises regularly across the industry feedback within this ODI.

Residential Retail

On residential retail, by moving away from an average revenue control, the uncertainty around property growth will increase the risk with the retail price control for companies and we don't think this represents an improvement in the regulatory framework. This is a particular issue for us due to the expected high growth rate in connections in our Cambridge region.

It also weakens the incentive to get properties into charge by reducing voids and identifying properties not on the billing system. We also don't consider that the reconciliation process is onerous in any way, the true-up being end of period only. We therefore support the continued average revenue control approach.

Q8.3: Do you agree with, or have any comments on, our proposals spanning multiple parts of the value chain, i.e. for major projects and future reconciliations?

We support the streamlining of reconciliations. There should be consideration of the materiality threshold before a reconciliation is included at PR24. We also support the incorporation of reconciliations with the financial model. This would allow more of the reconciliation models to be prepopulated with FD data and reduce the risk of error and the level of checks required by Ofwat.

9. Outcomes

Q9.1: What kinds of performance commitments should we include in the price review? What outcomes require financial incentives for all companies for the foreseeable future?

We think that if Ofwat adopts a smaller set of performance commitments then these should reflect the core services and be areas that persist in importance over the long-term. All companies generally have the same core themes, such as water quality, supply reliability, environmental stewardship, and customer service/support. Therefore, it is sensible to suggest that these themes continue to utilise financial incentives and the performance commitments within them should reflect the long-term aspirations for the sector, be deliverable and measurable, and do need to account for volatility and externalities that are naturally present within the measures.

Longer term thinking around specific resilience focused outcomes would encourage innovation and avoid 'fast followers' due to risk aversion. This should build on the work done during PR19 and into AMP7 around operational resilience, and utilise end of AMP or multi-AMP commitments that allow strategies to be bed in.

However, we are concerned that there may be a hidden level of complexity in this simplistic approach. How the areas that will no longer be assessed by ODI measures are reviewed must be carefully considered to avoid managing multiple complex processes as opposed to just one.

Q9.2: How do you think we should monitor outputs that are not clearly linked to the outcomes incentivised in the price control? Would it help to distinguish between PCs that monitor outcomes and PCDs that monitor outputs? What other options could we consider?

We think there are a few high-profile areas that would benefit from a more outputs focussed approach. In PR19, we applied this directly to our treatment works delivery projects. Going forward, certainly where there are major discrete schemes then we think it is right to directly protect customers for delivery of these schemes through an output measure. However, there are other longer-term programmes where this could also work, for example on asset health. We think it is important that maintenance issues are not stored up for future generations and due to the slow reaction time of measures such as mains bursts, and the difficulties associated with monitoring condition of hidden infrastructure, then it may be viable to utilise output measures on mains renewal programmes. Additionally, metering programmes might also benefit from this approach, another area where there is reasonably discrete costs.

Q9.3: Do you consider there are aspects of company performance where it would be better not to set expectations as part of the price control? What approaches should we consider in these cases, so that companies act in the interests of customers?

Broadly speaking, there are lots of day-to-day activities that companies deliver that are not directly expressed in the price control, however they broadly roll up into the themes of customer service, water quality, environment and supply reliability. This is an implicit part of giving companies sufficient flexibility to deliver day-to-day service to customers and we think that broadly speaking companies already do act in the interests of customers throughout our day-to-day service.

It is possible that existing performance commitments in some areas have become too granular, however it is a trade-off between giving companies flexibility to deliver, not increasing the regulatory burden, and also ensuring that the strategic policy aspirations are driven forward. An example is PSR validation contact, which is a very granular measure but was put in place across all companies to further a very specific goal.

If a theme or output is to be included in the price control, then there needs to be a clear business case for doing so. There is not a one size fits all answer. It may mean that some fringe themes of marginal benefit are dropped, but other areas where policy aspirations are desired to be driven forward are included. The important thing to determine first is what the strategic policy aspirations are, and the price control can be designed around these (see section 4).

Q9.4: What should be our aim in setting the levels of performance commitments? Do you agree with the proposal that performance commitment levels should be set, as a starting point, at what can be achieved by an efficient company with base costs and that deviations from this are proposed in company business plans? If not what alternative proposals should we consider?

We were very concerned at the justifications used by Ofwat at PR19 for the decision to include leakage reduction in base costs. Going forward, we hope Ofwat considers the required funding for a step change in service carefully.

Fundamentally companies are starting from different places, this is a direct result of differing areas of focus in previous investment cycles driven by differing needs and not having a common future aspiration in the past. For example, a company with no supply demand deficit in the past may not have focussed as much on metering or leakage. Now there is a desire to homogenise service levels more, which as a customer focussed aspiration is reasonable, however many of these service levels are underpinned by a legacy set of infrastructure that cannot be modified and improved quickly. It is vital to recognise this fact in setting long-term vision, and short-term service levels and costs appropriately.

We think common service levels should be set based on the long-term aspirations for the sector as a whole and a deliverable path to achieve it for each company, including ensuring step changes in service are adequately funded. An approach to set future service levels based on what has historically been delivered by an upper quartile company is quite backwards looking and does not take account of the reasons why we collectively want to improve that service level and the benefits it gives for current and future customers to do so. That should be the reason to change service levels, because of future benefits, not simply because one company has previously done better than another under different legacy pressures and constraints. Our aim is very much to achieve the best service levels whilst remaining affordable for our customers.

Where possible, we recommend that Ofwat keep the definitions for key metrics consistent so that progress can be tracked across the industry over multiple AMP period.

Q9.5: What approach should we take to setting ODIs? How should we take account of marginal costs and marginal benefits in setting ODI rates? What are the risks and benefits of the approaches that we set out, or any others that you propose?

We support lower reliance on the formulaic derivation of incentives from marginal cost and marginal willingness to pay data – this was a problematic approach because the data to effectively feed the formula was not easily obtainable in many circumstances as Ofwat has recognised in the consultation.

A national willingness to pay study would help alleviate some of the consistency issues across companies that are unavoidably present when companies undertake their own research – however it will be important to apply a sense check judgement to data coming from these surveys and to also apply a top-down strategic element to the setting of incentives. At PR19 for example, Ofwat wanted all companies to land within a range for their incentive packages however forbid companies from making top-down rebalancing of their incentives. Ofwat themselves then did this to get all companies into the ballpark they wanted by applying a common set of incentive rates. This is not a joined up nor helpful approach and the price review design should take into account from the outset that it is unlikely that any willingness to pay study will naturally land at the incentive range Ofwat wants to give companies an appropriate level of financial risk.

If national willingness to pay studies are done in advance and Ofwat has views on incentive rates out of those studies, then it is vital that these are shared with companies in advance. Companies' Boards will need to be able to sign off the risk range in its plan and they cannot do this without knowing the performance commitments, levels, and incentives.

10. Cost assessment

Q10.1: What should be the priorities for improving our approach to cost modelling and assessment?

We recognise the importance of an independent assessment of cost allowances in the regulatory framework, and we think significant progress was made to modelling and procedure for PR19 compared to PR14. We think cost assessment priorities should be:

- Ensuring that cost drivers and the way in which they are modelled make good engineering sense.
- That a range of triangulated cost models are used as a small number of models is not likely to reflect enough of the legitimately different circumstances under which companies operate regionally.

- Modelling the value chain as it actually exists – i.e this is mostly vertically integrated with many shared assets across water resources, raw water transport, treatment and distribution. The water resources models did not work well primarily due to the small size of expenditure in that price control. Water resources plus may increase the size of the pot, but it may not solve cost allocation differences or genuine crossover caused by the high degree of legacy vertical integration of these asset types in companies.
- To challenge the industry on efficiency but to ensure this challenge is genuine and does not reflect differences in levels of maintenance, enhancement or service over time. It is vital that genuine efficiency is separated out from expenditure timing and genuine cost driver differences if the goal of setting expenditure in a long-term context is to be achieved.
- To continue to seek to improve availability and consistency of cost driver data, and to use company forecasts where they are robust. Cost driver forecasts could be a candidate for early submission.
- To publish cost models and views on efficiency early – we believe this will improve the process of developing business plans within companies as it will remove the need for companies to try and second guess where its allowances might lie. Incentives can then focus on genuine efficiency improvement and robustly justifying any expenditure required above allowances in the form of cost adjustment claims.
- To work with the industry on long-term service objectives and what they cost to deliver, and to fairly recognise why there are legitimate reasons why the starting point on service levels is not homogenous across all companies.
- To continue the excellent work from PR19 on modelling enhancement costs, but to continue to deep dive areas where schemes are complex – this approach worked really well at PR19.

To consider long-term asset maintenance cycles in modelling, or at least to appraise five-year allowances in the context of long-term expenditure requirements – this is important to evidence that the sector is sufficiently funded to deliver long-term asset health expenditure. Whilst short term deferral of expenditure can be a useful flexibility to have to help absorb enhancement expenditure peaks without excessive bill shock, over the long-term it is not sustainable.

Q10.2: In what areas (both historical water sector and external) can we improve the range of benchmarks we use in cost assessment?

Our key concern with historical benchmarking is that it is predominately backward looking and does not take account of future changes. We recommend Ofwat look to use a more forward-looking approach to cost assessment.

The use of external benchmarking may be useful to expand sample sizes and learn from other industries. However, Ofwat must ensure the data would be comparable, which may be challenging as different industries operate in different ways.

Q10.3: How can we take account of longer-term ambitions such as delivering net zero and increasing public value in our approach to assessing costs?

Please also refer to our answers to Q10.5 and Q10.6 below in terms of general approach to setting long-term aspirations and making sure they are appropriately funded and realistic.

In terms of net zero, this is a specific objective that for the most part should be implicit within all companies' cost benefit appraisals for new schemes. However, the most cost beneficial solution is not necessarily the one that delivers the most carbon reduction. If a specific goal of reducing carbon is desired then it will need to be given extra weight within scheme assessment and this may require increased costs especially to move beyond the natural rate of carbon reduction implicit within the natural asset replacement rate.

Ofwat should also examine whether there are currently regulatory disincentives to companies in constructing renewable energy generation on their sites. If net zero is to be given extra weight, then any disincentives may need to be removed to enable companies to go further than their core service functions naturally dictate.

Public value impacts driven by investment should take account of the wider framework within which companies can demonstrate a clear purpose, transparency and effective engagement around any type of capitals approach which looks to incorporate societal valuation. Clarity around the impact of investment against each capital must be clearly articulated, measured and able to be reported on to be robust and meaningful.

Q10.4: Do we need to amend our cost assessment approach to take account of nature based solutions?

In the water service, nature-based solutions are likely to apply to a subset of environmentally based enhancement schemes and not have an impact on the bulk of core capital maintenance or non-environmentally based enhancement schemes. Therefore, we do not expect it to have a significant impact on the structure of the cost models. However, nature-based solutions may be appropriate in some circumstances and as this is a new idea, perhaps a deep dive approach would be most appropriate for assessing these. We would be keen to have some shared learning with other companies on the themes under which nature-based solutions might provide a viable alternative to traditional solutions.

That being said, as a relatively new approach to defining natural capital impacts, some impressive examples have been demonstrated across the industry (and other sectors) that have highlighted examples of robust frameworks in this space. Clearly defined and measurable impacts related to waste, pollution, consumption, C02 and biodiversity suggest that there may be potential for defining clear impacts of capital maintenance activity within such a framework and thus is becoming front and centre of the cost assessment approach.

Q10.5: Where can we enhance our evidence base on the relationship between costs and service?

We welcome Ofwat's acknowledgement of cost-service relationships and hope that this is explored further in this price review process. At PR19, we argued this case for leakage as that was the area where there was a clear enhancement of service, different to the past, driven by top-down policy. It is vital that companies have adequate funding when a step change in service is required and customers are willing to pay for that change. We believe there is a weight of evidence to support this case and would support further engagement in this area.

Nevertheless, we recognise that the link between cost and service is important and yet difficult to assess, and to protect customers there is a genuine concern over what they have or have not paid for already.

We would like Ofwat to work together more closely with the companies on this area. It fits into the goal of setting the five-year price control as a staging post within a longer-term plan (see section 4 for our views on this). Service level aspirations in the long-term should be part of that plan and to ensure value for money for customers it should be a priority to understand what significant change costs, and also what is achievable over the long and short term. To some degree most performance commitments have a degree of flex within management day to day operational control – however in considering the longer-term aspirations many PCs require directed investment to make significant moves forward.

It is important to understand the fundamentals for each PC if we are to set realistic long-term targets and understand the costs. For each one, what room is there for operational improvement driven by better ways of working (innovation and efficiency) and beyond that what is needed in terms of direct investment to make continued reductions, i.e when does the legacy infrastructure become the constraint on further service improvement?

Q10.6: What mechanisms should we consider for the efficient funding of performance levels, set in a long-term context, that vary from those an efficient company would deliver through its base allowance?

As per our answer above, the first step in our view is to try and unpick what is driving service levels for the core PCs. What operational innovation can drive improvement and by how much, and when does the infrastructure itself become the constraint to further improvement?

It is unlikely there is a one size fits all answer here and so it may be a deep dive type approach is needed. Companies should be able to provide a robust case for how far service levels can be taken and what investment is needed to drive improvements beyond those than can be absorbed in base, and how quickly these can be delivered.

We stress though that the first step Ofwat must proceed with quickly is to set a view on long-term aspirations for common PCs and to then work with the industry to determine why starting points may be different and what is needed to reach those aspirations. Ofwat will then have more information on which to judge each company's circumstances and determine if inefficiency is the issue or genuine constraints which need to be overcome.

Q10.7 – Is there more that we need to do to reflect future pressure on operational resilience in our approach to cost assessment?

We believe the best way to deal with resilience enhancement is via company specific deep dives, we do not think it is viable to try and model this. Resilience improvement is a specific activity targeted at a specific identified issue and as such can be assessed on its own merits. Ofwat could set a cost threshold for resilience schemes to encourage small scale schemes to be absorbed within base costs and encourage larger schemes to come forward to be individually assessed.

Q10.8: Are the most significant challenges to the operational resilience of the sector adequately captured within current strategic planning frameworks?

The recently undertaken Asset Management Maturity Assessment (AMMA) provided a review of companies' current capability in terms of their assessment of long-term operational resilience challenges. While the water resource strategic planning frameworks do promote an in-depth understanding of future resilience challenges in terms of the supply demand balance, the AMMA has consolidated this with an effective review of asset related aspects driving resilience challenges. Importantly, this included an understanding of the role of the organisation and people along with customer and stakeholder engagement, critical factors in long-term resilience planning. Outputs must be kept relative to the size and asset base of companies across the sector to promote an understanding across planning frameworks of proportionality.

The resilience action plans developed at PR19 should also provide specific focus around operational resilience as part of wider company resilience outlooks. Significant work went into these to identify short- and longer-term plans, incorporating high value investment, to reach desired states of operational resilience.

Please also see section 7 where we discuss the current strategic planning framework for regional and national planning.

Q10.9: How can we strengthen incentives for long-term operational resilience and improve the assessment of resilience enhancement expenditure while continuing to protect customers' interests?

We recognise also that the level of evidence on resilience schemes in PR19 could have been better. In part this is due to uncertainty – high consequence low probability risks are hard to quantify and harder to robustly evidence need on. Both Ofwat and companies need to meet in the middle and try to reach agreement on a robust level of evidence, where customers are protected, but where uncertainty is reasonably allowed for given the nature of these schemes. In other words, companies need to do more on the need and evidence base, and Ofwat needs to be more flexible in what it allows through in the face of uncertainty for these types of schemes. And critically, resilience schemes need to align to the long-term aspirations. E.g., if more interconnectivity is the goal, then companies can go in that direction. Pin some colours to the mast – is needed. We were pleased to see at PR19 that there was a clear recognition in our WTW long-term plan proposals (CAC) of the extent of customer co-creation that went into our proposal, and of our approach in evidencing need/optioneering solutions through innovative modelling techniques.

11. Risk and return

Q11.1: Are there areas of our risk allocation framework where mechanisms could be added, simplified or removed in a way which would benefit customers?

We have no comments.

Q11.2: How should we improve our use of RoRE risk ranges to provide insights into the balance of risk and reward, and improve comparability across companies?

We support the use of Monte Carlo analysis for understanding RORE risk ranges. At PR19, we took this approach to understand our ODI range and we have used Monte Carlo when formulating our Long-term Viability Statement in this year's Annual Performance Report.

Different companies will have different risk profiles and water only companies in particular are more exposed to risk, for example long-term RPI-linked embedded debt. We therefore think that RORE ranges for WoCs and WaSCs should be considered separately.

Q11.3: Should we index the allowed return on equity, and if so, how ought this to be implemented?

We think that indexing the allowed return on equity would be inappropriate and we do not understand how it would work.

Q11.4: To what extent should we place weight on a) balance sheet data; and b) index data when setting the allowed return on debt?

We support the use of balance sheet data which would more accurately reflect the debt costs faced by companies. This is particularly relevant to companies with long-term embedded debt which cannot be changed. It would also be important to use the lender definitions of debt which are not necessarily the same as the accounting definition.

Q11.5: Should we allow adjustments to the sector allowed return based on company size -and how should this be assessed?

The recent CMA decision recognises that smaller companies do face higher debt costs than larger companies, particularly on embedded debt and higher transaction costs. Smaller companies cannot diversify their debt portfolio as debt issuance is less frequent and of smaller size which impacts on both the cost of debt that can be secured and also the tenor of the debt.

We therefore think that embedded debt for smaller WoCs should be recognised when setting the allowed return in full if it can be demonstrated that it was efficient when it was issued.

Q11.6: Should we make different assumptions for the PR24 notional structure compared to PR19, and how should such a change be implemented?

By changing the notional structure with a gearing level lower than the current 60%, it will move Ofwat's view of an efficiently structured company further away from the actual position of the sector. This will increase the pressure on companies' financeability under their actual structure which could reduce the attractiveness of the industry to new investors and make it harder to secure efficient financing.

Therefore, if any changes to the notional company are made, this needs to be done with consideration of the industry's actual financing structures that are consistent with their target credit rating.

Q11.7: Do you have any suggestions for mechanisms which could incentivise financial resilience within the price control process?

Financial resilience is closely linked to the credit rating a company holds. Maintaining its target credit metrics should act as a significant incentive. There is also a licence condition that requires companies to maintain an investment grade credit rating. We think this should be sufficient but does require Ofwat to continue to make proportionate decisions on the cost of capital and cost allowances.

We support the CMAs decision to remove the Gearing Outperformance Sharing Mechanism (GOSM) as there is no evidence that it will help to improve financial resilience.

Q11.8: To what extent should we further increase the share of the notional company RCV which is indexed to CPIH in our assumptions for the period 2025-30, and how should this be implemented?

By moving further to CPIH, this will widen the disconnect between the indexation of RCV and where companies have RPI index-linked debt. The changes at PR19 have already had a significant impact on our RORE calculation for 2020-21 which was driven partly by the difference between RPI used on our index-linked debt and CPIH. We would like to understand better how Ofwat would take account of this legacy RPI debt. If a larger share of RCV is indexed to CPIH, then the proportion should take into account the tenure of any outstanding RPI linked debt which could be up to 25 years.

12. Next steps for PR24

Q12.1 - What are your views on the draft timetable for PR24?

Please see question 5.1.

Appendix - Examining the boundary of the targeted control for water resources

Q14.1 + Q14.2 - How can costs and incentives for the existing water resources control be targeted more effectively? Would amending the boundary to include raw water distribution or to extend it further to include water treatment improve the operation of the control? What are the issues involved?

We answer question 14.1 and 14.2 combined as there is cross over in our response.

We are in agreement with the issues that the consultation appendix draws out on the water resource price control and the water resources market in general.

For legacy assets, we do not think there is any benefit from the separate control. As the consultation identifies, there is a high degree of integration within existing water resource assets and their associated treatment and pumping assets. Whilst we agree this is likely to lead to difficulty and inconsistency in allocating costs, we do not agree that it is not an efficient means of delivering service for these assets, nor that it requires a separate price control to draw out those future efficiencies with incentives. Co-location of water resource, treatment and pumping assets is an efficient means of delivering service from these assets.

We can understand the desire to try and incentivise market involvement in new water resource assets. Up to now however this has been unsuccessful. We do not think the issue is with the structure of the price control – the issue more fundamentally is about the practicalities of a 3rd party being able to deliver an independent water resource. We would expect these practicalities to be even more of a constraint if it was extended to water treatment, as it is less likely a 3rd party entrant would find the stringent entry requirements (water quality regulations, location of source etc) to be an attractive standalone investment without a substantial financial premium that is therefore unlikely to undercut existing water company capital costs and returns, and may in turn increase operational risk for customers. We therefore believe water companies are still best placed to deliver these investments integrated with their own networks and financial structures - it is fundamentally one of the core aspects of a water company's function to deliver these services.

We agree that the cost modelling process may work better when modelling water resources plus. This is primarily due to the small size of the water resources control on its own. However as was done at PR19, this does not require a separate control in order to construct the models this way. The necessary cost allocation is already carried out in the annual reporting tables.

Given that at PR19, the addition of the new price control required extensive work to undertake the business changes relating to RCV, tariffs and other areas, and has resulted in limited benefit, we would question whether extending the price control further creates any additional benefit. Before extending the control further it would be wise to establish more firmly whether there really are market opportunities available in this area.