

Meeting note

Wednesday 2 February 2022
10:00 – 12:00

PR24 Cost assessment working group

Attendance

Affinity Water	Martin Hall
Anglian Water	Richard Goodwin
Anglian Water	Matt Humphrey
Bristol Water	George Clarke
Bristol Water	Tamsin Kashap
Dŵr Cymru	Charlotte Beale
Dŵr Cymru	Georgia Hilling
Hafren Dyfrdwy	Kristinn Mason
Northumbrian Water	Geoffrey Randall
Northumbrian Water	Crawford Winton
Portsmouth Water	Caroline Jemphrey
SES Water	Van Dang
Severn Trent Water	Kay Orsi
Severn Trent Water	Rob Holdway
South East Water	Matt Hersey
South Staffs Water	Daniel Haire
South West Water	Judith Corbyn
South West Water	Ben Ward
Southern Water	Michael Kearns
Thames Water	Carlos Pineda Bermudez
United Utilities	Sam Crook
Wessex Water	Harriet Cutts
Wessex Water	David Peacock
Yorkshire Water	Daniel Chubb
Ofwat	Tim Griffiths, Simon Harrow, Daniel Mitchell, Jennie Seymour, Everardo Quezada, David Watson, Paul Martin, Gilda Romano, Eugenia Vela, Stewart Loftus

Introduction

Ofwat opened the meeting and set out the agenda:

- Enhancement assessment at PR19, look forward to PR24, and data updates – Ofwat
- Enhancement benchmarking models and focus areas – Severn Trent Water
- Historic and forecast costs in enhancement assessment – United Utilities
- Breakout discussion and feedback – all
- Closing remarks – Ofwat

Enhancement assessment at PR19, look forward to PR24, and data updates

Ofwat highlighted the upcoming key milestones in the run up to business plan submissions for PR24 and the tight deadlines for collecting and reporting additional data to improve benchmarking. Ofwat then summarised the approaches to enhancement cost assessment taken at PR19. These included benchmarking models, deep dives, shallow dives and in the round assessments providing examples of each approach. The PR24 approach of aiming to use benchmarking models where possible and appropriate was discussed including updates to current data reporting to facilitate improved benchmarking.

Enhancement benchmarking models – Severn Trent Water

Severn Trent Water presented its reflections on PR19 and its proposals to improve the approach to cost assessment for PR24. This included where this may require earlier data collection and sharing by companies to facilitate this. Severn Trent Water set out some principles for where enhancement modelling would be most appropriate and suggestions for additional data reporting in the areas of lead reduction and surface water flooding were proposed.

Historic and forecast costs in enhancement assessment – United Utilities

United Utilities provided its thoughts on how to improve the approach to cost assessment for PR24 including proposals for where the inclusion of historical data might improve the assessment. United Utilities also set out thoughts on where in the round assessments might be appropriate and thoughts on capping and unmodelled uplifts.

Breakout questions

1. What are your thoughts on approaches to enhancement cost benchmarking?

2. Where is more historic data needed to help benchmarking, how can we incorporate historic costs into the assessment and how quickly can the data be available?
3. What changes are needed to enhancement cost and benefit lines and their definitions to aid benchmarking?
4. How can we improve cost and benefit data reporting for green (nature based) solutions?

Based on the company presentations questions 2, 3 and 4 were set in the context of the enhancement areas that are best for us to focus on including whether others agree with Severn Trent Water's list (slide 17)

Breakout group feedback

What are your thoughts on approaches to enhancement cost benchmarking?

- Most companies agreed that the key issues for enhancement benchmarking raised in the presentations were appropriate and should be an area of focus and further development.
- Companies agreed that the objective should be to find good independent cost benchmarks. Some companies raised concerns about the potential trend towards more complexity and data which could be a challenge for smaller companies to collect. Companies suggested a need to prioritise data collection and focus on the most material areas.
- The scale of costs covered by a single model was raised in Severn Trent Water's presentation but others considered that the scale of investment as not being key but the quality of the model. If the model is robust and applicable, the coverage of the model shouldn't matter.
- Companies recognised the struggle at PR19 to evidence cost efficiency where costs were deep dived. Some companies suggested that it may be possible to benchmark a subset of costs that are part of a deep dive submission and then apply this efficiency across the wider requests that cannot be benchmarked as robustly.
- Companies supported identifying the key evidential gates that need to be passed in a deep dive for different areas of enhancement investment. Companies suggested that they already collect most of the deep dive evidence and data required to justify expenditure.
- A company requested early sight of the tools and models Ofwat will apply to different types of enhancement expenditure in advance of business plan submissions. Ofwat explained that models can be difficult to establish in advance without knowing content of business plans.
- Companies recognised that they need to provide robust business plans regardless of assessment tool used. It was suggested that Ofwat provides further clarity on high-level methodology in advance of business plans, ie. under what circumstances it will apply different tools and approaches.

- Companies requested further guidance on what is considered base and enhancement expenditure but accepted that updates to enhancement cost line definitions may assist with this.
- Some companies requested clarity on how to factor in productivity gains into business planning tables.
- A company felt that some enhancement schemes are bespoke and so deep dives are likely to be a more appropriate tool (than models) for some types of schemes.
- Some companies requested further engagement on enhancement costs including a consultation similar to the consultation on the approach to base costs. Ofwat stated that the base cost consultation was prioritised due to companies requests for early sight of models. Ofwat suggested that it would try and take key elements of the approach to enhancement through CAWG where possible and appropriate, although this was in part reliant on companies volunteering to present on issues of interest.

Where is more historic data needed to help benchmarking, how can we incorporate historic costs into the assessment and how quickly can the data be available?

- Most companies supported the use of historical data for enhancement benchmarking. Some companies felt that that forecast data was better suited as a benchmark as enhancement expenditure is forward-looking by nature and historical data should be used as a cross check.
- Some companies suggested that whether historical or forecast cost benchmarking was most appropriate was dependent on the type of expenditure and individual circumstances. As with forecast data, there is the risk of inconsistencies across historical company data if long term data sets are used. Companies agreed that consistency is less of an issue if data from the 2020-25 period was used.
- Some companies stated that it was important to understand the drivers of enhancement costs, including exogenous drivers. Companies suggested that cost drivers needed to be clearly defined, and the right sources of data used for exogenous factors.

What changes are needed to enhancement cost and benefit lines and their definitions to aid benchmarking?

- Most companies agreed with the list of enhancement focus areas proposed by Severn Trent Water to be explored further or improved.
- Some companies noted that climate change impacts in some areas can be significant so while flood resilience is important, climate change may mean that some areas will be more affected by droughts than others, which also needs to be considered.

- Several companies requested a future session on resilience enhancement to better understand the relationship between base and enhancement expenditure and the interactions with other enhancement lines.
- A company suggested that smart network investments for the wastewater networks may become more material over time and may be useful to better understand these costs.
- Companies highlighted that there is some uncertainty around lead reduction requirements and this is dependent on the SPS and DWI guidance. Companies stated that there are several issues that could drive lead replacement enhancement costs up and down and therefore unit cost modelling could be challenging. Companies suggested that the key cost drivers were internal property work and pipe length.
- Companies suggested that metering should be an important area of focus for historical data collection and benchmarking. Two companies suggested factors that might impact metering costs including population density for smart metering (which reduced costs of associated infrastructure) and operational decisions over data collection frequency eg 15 minutes compared to daily data retrieval.
- Most companies flagged net zero as a key area for collecting additional data although some suggested that detailed reporting of costs and benefits could be difficult. A company requested further clarification on how to present standard and lower carbon solutions across companies for comparisons. Companies suggested additional research into net zero reduction costs and applying knowledge from other industries on the costs of achieving targets.
- Some companies suggested collecting additional data on cyber security investments as the shift has moved away from physical security. Similarly to net zero this can apply to all industries so a wider look at costs may be beneficial.

How can we improve cost and benefit data reporting for green (nature based) solutions?

- A company suggested that different types of solutions should be assessed separately (eg conventional/grey and nature based solutions), but should be assessed at intervention type level rather than split by driver.
- Some companies suggested that more needs to be communicated about supporting delivery of nature-based solutions and disincentivising short term solutions. A company requested that long term solutions should not be modelled with short term ones as the costs may be very different.
- Several companies agreed that the interaction between regulator and companies is critical in holding companies to account to deliver the intended output from nature-based solutions.
- Some companies requested a session on best value and how best value can be incorporated into the cost assessment approach

Post-meeting request (emailed Thursday 3 February)

1. What current enhancement areas that are already modelled would benefit from additional historic data and what should this data be? Our initial thoughts primarily based on the company slides and discussions yesterday are as follows:
 - a. Storage schemes in the network to reduce spill frequency at CSO (eg totex, number of schemes, storage provided)
 - b. Storage schemes at STWs to increase storm tank capacity (eg totex, number of schemes, storage provided)
 - c. Schemes to increase flow to full treatment (eg totex, number of schemes, increase in flow to full treatment)
 - d. Sewage treatment works/network flow monitoring (eg totex, number of schemes/monitors)
 - e. WINEP investigations (eg totex, number of investigations, by type and driver)
 - f. Reduction of sanitary parameters (eg totex, number of sites and PE with tighter standards)
 - g. Meeting lead standards (eg totex split by pipe replacements and treatment dosing, length of pipe replaced, number of pipes incl number of pipes to compliance point)
2. Building on the presentations and discussions in the call what other new areas of potential enhancement spend do we need to focus data gathering on (eg net zero), and does this need to be all companies or a limited number that are already undertaking the work and collecting data?
3. What additional data would we need to help improve the fair assessment of nature based schemes (eg. splitting enhancement lines, additional opex and capex, additional benefits information)?