

Response: to Ofwat Consultation on Methodology for PR24

From: Independent Challenge Group for Affinity Water

Written by: Independent Challenge Group Chair, [REDACTED] on behalf of all members.

Scope

This response is restricted to questions that are directly relevant to independent challenge work.

Questions asked by Ofwat and responses from ICG for Affinity Water

Chapter 2 - Regulating through the Price Review

Q2.1: Do you agree with the challenges facing the sector and the ambitions for PR24 that we have identified?

- We agree that the four key ambitions laid out in Chapter 1 and underlined in Chapter 2 align with customer priorities as far as we are aware.
- We are pleased to see a raised emphasis on longer term resilience. We note that engagement insight indicates that customers identify the top priority as a sustainable and safe supply of water now and in the future. We are also pleased to see that there will be an expectation for companies to demonstrate the intergenerational fair sharing of costs and benefits of resilience plans.
- We are pleased to see a raised emphasis on positive environmental solutions. Evidence suggests that the majority of water users now support this direction of travel.
- We are pleased to see a clear commitment to promoting and encouraging innovation and, particularly, innovation that may benefit from collaboration. All ways to incentivise such endeavours, including via the Innovation Fund, will have our full backing. We would especially support the development of innovation incentives that encourage the detailing of how the re-investment of any learnings/profits will be taken for forward into further generations of innovation. We would also like to understand how innovation will be evaluated and how successful innovations will be encouraged to be rolled out.
- We suggest that a clearer distinction could be made between the various aspects of any environmental strategy: 1) the security and resilience of water supply that will mitigate climate change impacts eg long term infrastructure projects 2) environmental improvements to water ways, rivers and oceans eg biodiversity targets 3) company contributions to overall environmental goals eg net zero targets.
- We also suggest a clearer line of sight as to why inviting and listening to customers' voices is vital and why this is important all the time, not just for Price Reviews. We believe that continuous engagement with customers is most likely to lead to continuous improvement cultures, including the use of citizen co-design, that will be focused to deliver better outcomes for the population.
- We also suggest clarity that the ambition of listening to customers and communities is a means not an end. It might be worth laying out what might seem obvious - companies should have mechanisms for continuous listening to citizens and stakeholders so that they can learn and then act on insights gathered from such

engagement to deliver better outcomes. Understanding priorities and willingness to agree trade-offs is also relevant to this.

Q2.2: Do you agree that continuing to use our three building blocks helps push companies to meet our ambitions for PR24?

- We agree. Our only addition would be a question about if there is a shared understanding of what is meant by 'affordable bills for all'? CCW and others now suggest that affordable does not necessarily mean lowest bills for all but rather an intergenerationally fair and balanced offer that seeks to eliminate water poverty and support debt management while allowing for required investment in resilience and environment. We do think that the consultation indicates this but a sector-wide agreement on the definition of 'affordability' may be helpful.
- Additionally, it is yet to become clear how customers will be engaged on what the 'single water affordability discount scheme' means for them and their communities vs current mechanisms. One immediate concern is that the cost-of-living crisis is worsening and fast. There are difficult implications for a cross subsidy mechanism if the proportion of customers who need financial support substantially increases during a short time frame. How will any national social tariff remain agile in this fast-changing economy? How much will households be prepared to pay for a cross subsidy in these circumstances? Does a cross-subsidy model in fact reach its limit in such circumstances and might alternative progressive tariffs be considered? How can the regulator ensure that the urgency of addressing these questions can be taken account of prior to 2025?

Q2.3: Do you agree that we have struck the right balance between what's in and what's outside of the price control?

- We agree overall.
- We note is that there is little mention of non-financial vulnerability, and we would hope that companies will be incentivised to take particular care to listen to groups who are often harder to reach and need extra support.
- Additionally, we did not notice any mention of resilience in the context of extraordinary events eg. cyber-attacks, physical warfare including nuclear, pandemics. This aspect of resilience may now be of increased interest to customers following recent events with Covid-19 and the war in Ukraine.

Q2.4: Do you have any comments on our approach to evaluating progress? What specific evaluation questions (based within our four key ambitions) do you think an evaluation should look to answer?

- We are aligned with the direction of travel especially the encouragement of joining up long- and short-term plans, the greater focus on innovation & positive environmental solutions and the creation of collaborative horizontal links in-sector and inter-sector. However, it is not entirely clear how any rewards/performance delivery monitoring might be structured to underline the importance of these potential progressive solutions. We also note that innovations involve risk. New

ideas cannot always work and if Ofwat only reward companies who can deliver certainty, innovation will be risk averse and limited.

- We support the 2-stage process and agree that it is more efficient to structure these determination stages so that companies are obliged to put their best foot forward from the outset. However, we cannot see how companies will be incentivised to take feedback following draft determinations and improve their plans if they have no opportunity to be regraded. We accept that we may not yet have understood the full picture.

Chapter 4 – Reflecting an understanding of customers and communities

Q4.1: Do you agree with our approach to making sure that companies' price review submissions and our determinations reflect and understanding of customers', communities' and environmental concerns?

- We agree with the principles described to understand better customers and communities that are laid out in this consultation paper and that build on the content of previous publications on this subject.
- We strongly support the principle of citizen co-design that is alluded to and would support further encouragement for this.
- Proposals for customers in vulnerable circumstances appear skewed to financial vulnerability vs non-financial vulnerability. We would like to see companies incentivised to appreciate both.
- We support the development of a national social tariff in principle but wonder how the regulator is expecting to encourage citizen engagement on this mechanism in a fast-changing economy. Will the regulator also welcome engagement on a variety of alternative or additional possible mitigations to water poverty eg innovative/ progressive tariffs. Would engagement on options of this nature, perhaps collaborative endeavours by companies, be welcomed by Ofwat?

Q4.2: Do you agree with our proposal to conduct open challenge sessions?

- We agree that the most open and transparent mechanisms to invite debate, challenge and input from water users are to be encouraged and we will support fully any agreed mechanisms that are decided by the regulator to be used in common for all companies.
- We would appreciate clarity that this single challenge mechanism will not be given a disproportionate degree of importance vs the rest of complex challenge arrangements that have now been designed for newly constituted or reconstituted ICGs.
- Currently the proposal for open challenge sessions has yet to be developed and we will support any such development fully. In the meantime, we note the following risks and difficulties to public meeting mechanisms:
 - Harder to reach voices are unlikely to be forthcoming in these public environments without some choreography
 - Special or single interest groups or individuals with confident positions can take a great deal of airtime without some choreography

- Meetings are usually choreographed by the hosts to keep content relevant and avoid tangents. The balance between sincerely open challenge and a degree of choreography might be difficult to strike
- In the restricted time available for Q&A it is only possible to scratch the surface of complex issues, especially if the overall parameters for discussion are wide, which risks oversimplification
- It is notoriously difficult to attract a balanced and strong independent turnout (see CCW public meetings over many years)
- The question of the right venue is vexed given that most geographies are large
- Opportunities for wider input and even co-design can exist in these forums. 'Slido' style 'ask the audience' mechanisms can be useful although these require careful organisation from experienced hosts
- Timings are difficult to plan to suit participants, especially if there are to be 2 public meeting open challenge sessions for each company
- Facilitation of these meetings takes experience and skill – does Ofwat and CCW really have the resource to cover this number of meetings at this level?
- Evaluation is vexed – it would help to better understand how the regulator plans to evaluate these sessions in the context of the complex and comprehensive designs for citizen challenge and assurance the companies and ICGs are now building in answer to the ambitious expectations laid out in previous papers from the regulator?

Chapter 5 – Delivering outcomes for customers

Performance commitments

Q5.1: Do you agree with our proposed package of common performance commitments? Is water demand best incentivised through separate performance commitments on household and domestic consumption and leakage or through a performance commitment measuring total demand?

- Our view is that the joint total demand PC is an interesting idea in principle and might be worth exploring further with customers. We are attracted by the possibility that a single total demand target inclines to co-designed 'community deal' arrangements (this has worked well for Affinity in pilot form). However, on balance we probably are convinced by CCW's position that citizens may feel that companies' responsibilities for leakage reduction targets are being concealed by aggregating total demand. If there was a way to link the 2 targets while keeping both measures transparent, that might be the best of both worlds.
- Additionally, we support the proposals for new common performance commitments to incentivise improvements in environmental matters - biodiversity, for reductions in operational greenhouse gas emissions, for serious pollution incidents, for reducing the impacts of storm overflows as well as for bathing water and river quality.

Q5.2: Do you agree with our proposed guidance for bespoke performance commitments?

- We have no objection to the minimisation of the number of bespoke performance commitments in principle although the benefits of this minimisation for customers have not perhaps been described. For AMP 7, the Affinity CCG was responsible for convincing the company to include a bespoke PC for Environmental & Innovation pilot projects. Useful learnings are being taken from these programmes of work and roll outs of successful projects will be of benefit to customers for years to come. The flexibility to incentivise new thinking in this way would no longer exist under new proposals. These projects would not be underway without a bespoke PC. We wonder if there might be another incentive mechanism that might fill any gap?

Standard incentive rates

Q5.4: Do you agree with our proposed approach to the measures of experience performance commitments, including to increase the size of C-Mex?

- We support fully the goal of measuring customer experience. However, we remain concerned about the relative nature of achieving standards (and therefore achievable and truly incentivising opportunities for rewards) given that if all companies outperformed some would still fail. C-Mex measures are also affected by long established and variable 'brand' value and awareness levels for the different companies which are not always pegged precisely to service levels. It is difficult to compare accurately like with like in these circumstances. Ideally, we would like to better understand what it is that customers would like the sector to track when it comes to the service they receive and then design a PC accordingly. That said, we understand that this is unlikely to occur prior to or during PR24 process and we will continue to challenge, and record the challenge, of the company on all aspects of service that are intended to be wrapped into the C-Mex measure.