



David Black  
Chief Executive  
Ofwat

Date: 6 December 2022

Contact: 

By email - 

Dear David & Emma

### **Supporting Customers through Cost of Living Pressures**


Thank you for your letter of 17<sup>th</sup> October relating to supporting customers through cost of living challenges. Like Ofwat and CCW, we have recognised that our customers are needing even more support in the current challenging economic circumstances.

We are also conscious that there will be continued financial challenges for our customers in the next financial year. Our bill profile throughout AMP 7 sought to keep bills as flat and predictable for customers as possible. This financial year we even managed a reduction to the average household bill in nominal price-base of (1.3%) and a reduction in real terms of (5.3%). We purposely deferred £15m wholesale water revenue to ensure that no customer group experienced an increase of greater than 5%.

The Board carefully considered the need for mitigating action in relation to next year's bill levels, including the option of deferring revenues from year 4 into year 5, but unfortunately, the current levels of inflation are having a significant impact on our own costs and it just isn't possible for us to maintain this downward trajectory through to the next financial year. We also cannot defer any further revenue if we wish to maintain our financial resilience whilst continuing to invest material sums into operational and environmental improvements. We have worked hard to minimise the overall impact of inflation on bills, keeping our increase to under 10% (just 1.6% in real terms). Nevertheless, we understand that this will still be difficult for our financially vulnerable customers and have therefore taken action.

We help our customers who are struggling by:

- increasing our basic social tariff discount from 20% to 45% with effect from 1<sup>st</sup> October and also retained our elevated income threshold eligibility criteria (first introduced as part of our response to COVID). We have also increased the number of customers we plan to support from 108,000 to 124,000 by the end of the AMP.
- Continuing our Hardship Fund for a second year. This £250,000 fund supports some of our most vulnerable customers with debt write offs, bill reductions and also grants for white goods.
- Looking to find different and more innovative ways of supporting our customers, for example over the Easter period we worked with Kent County Council to provide a £30 food voucher to all those families in Thanet District who were in receipt of free school meals and we are repeating the exercise with West Sussex County Council for the Christmas period.



More widely, we welcomed the 2021 CCW Affordability Review and have already implemented the vast majority of the recommendations and are working towards the remaining few. Equally we welcomed Ofwat's Paying Fair guidelines and are proud to say we already had most of them in place (we will be writing to you by the end of December in response to the Paying Fair Information Notice with more detail in relation to these guidelines)

## Challenges in the next Financial Year

We are conscious that more needs to be done in the next financial year, so we are focusing our mitigation of our bill increases around three main areas –

- Maintaining our increased level of discount through our social tariff and allowing more customers to benefit and making it easier for customers to apply
- Increasing efforts to identify customers who need our help
- Flexibility in payment arrangements for customers – allowing customers who are struggling to set a payment plan that meets their needs

The 45% discount will provide a meaningful reduction for qualifying customers (we will also automatically apply this discount to waste-only customers who have qualified for a social tariff with their freshwater supplier). In addition, we will be making it easier for our customers to apply for assistance online by creating a simplified application form.

We will also maintain our higher discount levels of 65% and 90% so we can provide even greater assistance for those most in need. This is in addition to the support provided through our longstanding assistance schemes – Watersure (the nationally mandated capped tariff) and our debt matching scheme. Our hardship fund will continue to support those who need enhanced levels of support.

We will be seeking to build on our existing work to identify customers in need of support –

- Being out and about in communities, providing face-to-face advice in locations such as Food Banks and Job Centres
- Leveraging our Data Sharing Agreements with Housing Associations
- Working with new partners, such as Kidney Care UK, to extend our reach into vulnerable communities
- Building on existing partnerships, such as the Home & Well initiative (a partnership with Citizens Advice Hampshire, SSEN and the local NHS trust), to provide holistic, cross utility, support directly to customers

Offering flexible payment options is a really important element of our mitigation efforts. If customers have low or fluctuating income, the ability to make a payment arrangement that suits their own individual circumstances can make a significant difference. We offer payment holidays, a range of payment options and the ability for customers to agree an under-paying payment plan if they are struggling to keep up with payments.

## Looking Forwards

We welcome the encouragement from Ofwat in the PR24 methodology which incentivises companies to be ambitious in supporting and enhancing customer affordability and wants companies to think more creatively about setting charges and establishing trials directed at customers struggling to pay. We have already commenced research for the ongoing development of the following changes to charges (more detail in the Annex) -

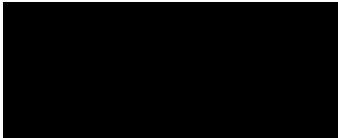
- "Summer-usage" premium charge
- Site-area-based surface water drainage charges

- Removal of large user discounts

In addition, we are also looking at what our social tariff might look like in AMP8, but this is a difficult challenge in light of the uncertainty around a single social tariff and what transitional arrangements would be needed. Early clarification of the details around the proposed single social tariff and timing of implementation would be helpful in terms of being able to develop an approach that will be most beneficial and least disruptive to customers when it comes to transitioning onto the national tariff.

As previously mentioned, we deferred £15m water revenue to ensure no customer group experienced bill increases of greater than 5% in 2022-23. We have noted that the current Revenue Forecasting Incentive mechanism for wholesale revenue penalises any revenue variances that breach the variance threshold, irrespective of when a company purposely defers revenue in the interest of maintaining bill stability and to avoid bills exceeding 5%. We believe this should be improved upon and that a mechanism should be in place to differentiate between the underlying reasons for variances. The risk of being penalised may act as a deterrent to companies in relation to charging innovation and the trialling of new structures.

Yours sincerely



Lawrence Gosden  
Chief Executive Officer

## New approaches to charging

We can confirm we have already commenced research for the ongoing development of the following changes to charges.

- i. **“Summer-usage” premium charge:** In order to make our charges more cost-reflective, we are planning to pilot the use of seasonal charges, in the form of a premium volumetric charge during the summer months. This type of tariff not only sends signals to the entire customer base for the need to use water efficiently, but also shifts the burden of cost more fairly to those using water for non-essential purposes. We commissioned a report earlier this year by Nera Economic Consulting to analyse the benefits of a differentiated tariff structure from an economic perspective. The report recommended seasonal tariffs as the most progressive and cost-reflective. We discussed the report in detail with Ofwat in a virtual meeting on 18<sup>th</sup> October this year and were very encouraged by their support and offers to help progress. The installation of smart meters is a key enabler for the full roll-out of these charges and this is expected mid-AMP 8. In the meantime, we propose bringing forward investment for 175k smart meters to be installed by 2024-25, as per response to Defra. We plan to commence extensive pilots to feed into the development of these seasonal charges.
- ii. **Surface water drainage:** We have formalised a project to adopt site-area-based surface water drainage charges by year 1 of AMP 8 to reflect our better understanding of overall the costs of surface water drainage services. The roll-out of these charges again seeks to shift the burden of cost away from households to non-households and to those contributing most to the volume entering our drainage network. In addition to being more cost-reflective, we believe the adoption of these charges will encourage the implementation of more sustainable drainage solutions. We will work closely with those customers whose charges will increase most significantly and engage in cost-sharing projects to fund more sustainable drainage. We aim to have a shadow charge for all customers by 2024-25, and for the charge to be fully effective from 2025-26. In recognition of this, we have adjusted the balance of revenue recovered via surface water drainage charges versus foul water treated for 2023-24.
- iii. **Large user discounts:** Our current tariffs for large users have a lower unit rate to reflect the fact that, typically, these customers are not connected to the local distribution network. While from this perspective this is cost reflective, it means the incentive these customers face, at the margin, to use water efficiently is lower than for other customers. As the cost of water resources has become more significant, we have decided to phase out these large user discounts so that these customers face the same price signals as other customers. This phasing out commenced on a small-scale in our 2023-24 charges.