

Appendix 1

Information for members, including Terms of Reference



Your local supply, on tap

Customer Challenge Group Information for members

October 2012

Version 2

Reference: CC-Info

Introduction

This briefing pack has been compiled to help you gain an understanding of our business, the evolution of Customer Challenge Groups (CCGs) and an introduction to the way we are planning our engagement activity.

We hope this brief insight will help you understand the role of the CCG and the contributions that members can make. It is not designed to be a full induction pack and members will receive further information as we work through the induction phases.

We have included the following information

- 1 Background information about our business
- 2 The development of Customer Challenge Groups and the role of members
- 3 Ways of working
- 4 Our approach to engagement
- 5 Terms of Reference for the CCG
- 6 Ofwat requirements for stakeholder management (summary)

1 Business Information

About Affinity Water:

Affinity Water aims to be a leading community-focused company serving a population of 3.5 million people. We provide 900 million litres of water each day to people in parts of Bedfordshire, Berkshire, Buckinghamshire, Essex, Hertfordshire, Surrey, the London Boroughs of Harrow and Hillingdon and parts of the London Boroughs of Barnet, Brent, Ealing and Enfield; and the Tendring peninsula in Essex and the Folkestone and Dover areas of Kent.

www.affinitywater.co.uk



- Providing over 900 million litres
- of water each day
- Serving 3.5 million customers
- Maintaining over 16,500km of pipework
- A community focused company
- A passion to deliver high quality service

Our Regulators



**Economic regulation:
price limits**

www.ofwat.gov.uk



**Environmental regulation:
environmental permits**

www.environment-agency.gov.uk/



**Drinking water quality
regulation: drinking water
standards**

www.dwi.gov.uk



**Consumer representation:
consumer protection**

www.ccwater.org.uk/



**Governmental regulation:
legislative and policy
framework**

www.defra.gov.uk/

2 Development of Customer Challenge Groups and the role of members

Leading organisations listen and respond to what their customers and other stakeholders tell them. This helps them adapt to changing demands and expectations, so they can continue to run successful businesses. While we recognise that the majority of our customers cannot choose who supplies their water, we are always keen to listen to our customers and stakeholders to help us improve the services we provide.

We define our stakeholders 'as individuals or groups who affect, or are affected by what we do and how we do it'. We believe that effective engagement 'promotes two way communication that takes into account views which should be heard, acknowledged and considered when developing future plans'.

The constructive feedback and communication we have with others has helped us develop innovative ways to deliver services and solve problems in both day to day operational activities and long term investments. By taking account of alternative views and perspectives, we continue to challenge and test our plans, this also helps us build and strengthen our relationships with others.

In developing our future plans and strategies we want to make the best use of the existing engagement activity we undertake, as well as plan other events as needed, to ensure we appropriately reflect customers' needs in our investment plans.

One of our regulators, Ofwat, sees the importance of customer and stakeholder engagement. In 2011 they published a policy document setting out an innovative approach to engagement which expects water companies to establish an independent group, to challenge the way they engage with their customers to support their preparations of business plans and proposed pricing for the period 2015-2020. This has not been tried to the same extent in any other industry.

Our independent Customer Challenge Group (CCG) will challenge and support us to produce and submit a business plan that is accepted by customers. The CCG's Terms of Reference say it will:

- Review the company's customer engagement process and the evidence emerging from it to ensure customers' views are considered as the company develops its business plan

- Challenge the phasing, scope and scale of work required to deliver outcomes, including legally prescribed standards and the requirements of the Drinking Water Inspectorate (DWI) and Environment Agency(EA)
- Advise Ofwat on the effectiveness of the company's engagement, and on the acceptability to customers or otherwise of the company's overall business plan and bill impacts

To meet these demanding goals we are inviting a maximum of 20 people to represent all our customers and stakeholders and be members of the Affinity Water Customer Challenge Group. With more than three million domestic customers and more than 70,000 commercial customers, we want CCG members to reflect the diversity of communities we serve.

Following the appointment of Robin Dahlberg as the independent Chair of the CCG, we are recruiting individuals who can represent customer and stakeholder interests. We need to restrict membership to a workable number. Therefore we need individuals who are prepared to represent sectors of the communities' we serve and not just their personal view points.

To reach the diverse communities we serve, we are approaching representatives from each of our regulators, from large and small commercial customers as well as local authorities, pressure and support groups. The CCG has the role to challenge us to ensure that all communities' interests have been covered and appropriate links and engagement activity made – especially if they are not directly represented on the CCG itself.

3 Ways of Working

What can members of the CCG member expect?

This is an opportunity to participate in a new and innovative way for water companies to involve customers in the formation of their plans and pricing proposals for the period 2015-2020. This opportunity will allow you to learn about the challenges, risks and opportunities which we balance when providing a water service. You will play a key role in assuring we get the mix right.

We have agreed with the chair that we will aim to be as open and transparent as possible about all significant issues.

At the conclusion of the process, the CCG will submit a report to Ofwat providing their views on how well we engaged with our customers during the process for preparing our plan and pricing proposals.

What we expect from members of the CCG?

The business planning cycle will last until late 2014 and we would like all members of the CCG to stay with us over that period.

We hope that members understand the need for them to represent and reflect the wider communities we serve. They should bring their specialist knowledge to represent these sectors, not see themselves as representing single interest groups.

We are hoping to learn from your expertise and knowledge. You will bring an alternative view to our business which we want to be able to learn from.

How we will keep in touch?

We are setting up a dedicated secure site on our web site. This will be password protected and will provide the CCG with a place to access and store information and

papers. In addition we will promote electronic communication and email will be the preferred tool.

How much time are CCG members expected to commit?

Members of the CCG are expected to commit at least one day a month from July 2012 through to September 2014.

Meetings of the CCG have been scheduled for the next two years. These meetings will take place every two months and will usually be held at our offices in Hatfield. The dates are shown below.

Video conferencing facilities will be available for meetings at Hatfield, Folkestone and Manningtree (it is hoped that all CCG members will attend in person the first meeting scheduled on 5 September 2012, in part so that they can meet their fellow members).

There is an expectation that there will be activity between meetings to be agreed and directed by the Chair. For example we have tentatively decided that we will need sub-committees to ensure that sufficient attention is given to the needs of the customers in East and Southeast regions.

Dates:

Interviews with prospective members will be arranged with the Chair Robin Dahlberg.

Induction sessions will be arranged as needed.

Planned Meeting dates

2012	2013	2014
5 September	23 January	22 January
21 November	13 March	19 March
	22 May	21 May
	24 July	23 July
	18 September	17 September
	20 November	

Compensation

Prospective members should note that these positions are unpaid.

Expenses

Out of pocket expenses will be paid when supported by an appropriate receipt. This includes travel expenses and carer or child minding costs. Car mileage will be paid at the standard HMRC rates.

4 Our Approach to Engagement

Background

Leading organisations engage with their stakeholders in many ways in order to improve their decision making and to build trust. The scale of the engagement with and influence of each group of stakeholders is determined by the business. Ofwat recognise the value of a structured and assured process as part of the development of the business plan for the next planning cycle, and require all regulated business to follow an assured and risk-based approach.

At present, we maintain contact with and seek to involve a wide range of interest groups in the day-to-day and strategic running of the business. These and other opportunities will form the foundation of the direct engagement with customers and selected stakeholder groups.

Assurance of the content, scale and scope of the engagement will be provided by the CCG.

Benefits of stakeholder engagement

We see the benefits of structured stakeholder engagement will include:

- Building constructive two-way engagement that can contribute to learning and innovation, to deliver services better
- Increasing awareness of challenges and participation in decision making
- Gaining buy-in and support for decisions
- Ensuring that sustainable solutions, supported and valued by customers at a price they are willing to pay, are represented in the business plan
- Demonstrating that solutions and opportunities have been developed through a constructive and assured engagement process, endorsed by Ofwat
- Building trust in the business

The engagement process

The engagement processes we use will reflect best practice and will follow a systematic and iterative approach to plan, deliver and review outcomes.

The appropriate engagement activity or channel will be determined by a number of factors including the purpose, the desired outcome, the need to stimulate responses from identified groups, levels of interest and constraints such as time, people and resources.

In addition the activities of neighbouring water and sewerage service providers will be considered within the planning process.

Assurance

Assurance of the process will be provided by existing, internal decision-making groups and internal controls whenever possible and will include working with the CCG and maintaining qualitative and quantitative records.

Our approach

The results of engaging with our stakeholders will influence the development of the business plan and will take account of the following:

- Evidence based, with facts gathered through an appropriate range of tools
- Understanding and balancing the differences between different customer groups, including current and future customers
- Working with customer representatives and stakeholders, not only in planning and conducting engagement, but also in interpreting responses
- Objective and impartial – with an open approach to understanding and reflecting views on a range of issues, rather than generating support for a specific course of action
- Offering choices and seeking views on preferences, both on what to do and how things can be achieved in a balanced and cost effective manner
- Informing the development of business plan at all stages, not merely a validation tool once a plan is developed
- Based on realistic price-service trade offs, informed by clear and reasonable assumptions
- Reviewing the range of opex and capex solutions, including demand management and behaviour change as part of supply/demand balance
- Using reputable contractors and making use of best practice
- Providing auditable and traceable evidence

Item 5

Terms of Reference for Affinity Water Limited Customer Challenge Group

V1 Approved by Robin Dahlberg

26 June 2012

V2 Updated to reflect change of name to be approved

Document Reference

ToR CCG

Context

The Affinity Water Customer Challenge Group (CCG) has developed from the PR09 Quadripartite Group. The Ofwat policy statement ¹ illustrates the Terms of Reference and ² Consumer Council for Water (CCW) suggested terms, have been considered in the writing of these terms of reference.

The purpose of the CCG is to advise, support and challenge the development of a constructive dialogue with Affinity Water stakeholders, that will take serious account of their views when planning and delivering the strategic water services.

The outputs of the CCG will include reports to Ofwat, and the business, about company engagement process and the company's strategy and business plan on its consistency with requirements.

Role of the CCG

The role of the CCG will be to operate independently of the company to:

- Review the company's customer engagement process and the evidence emerging from it, to ensure customers' views are considered as the company develops its business plan
- Challenge the phasing, scope and scale of work required to deliver outcomes, including legally prescribed standards and the requirements of the Drinking Water Inspectorate (DWI) and Environment Agency (EA)
- Advise Ofwat on the effectiveness of the company's engagement, and on the acceptability to customers or otherwise of the company's overall business plan and bill impacts

The CCG will consider whether the company's business plan reflects a sound understanding and reasonable balance of customers' views, and whether the phasing, scope and scale of work required to achieve outcomes – including legally prescribed standards and the requirements of the DWI and EA – is socially, economically and environmentally sustainable.

A key part of the role will be a debate between the company, customers, other local stakeholders and the DWI and the EA, to establish whether the scope for sustainable delivery of legal outcomes has been properly considered.

¹ Involving Customers in price setting – Ofwat's customer engagement policy statement

² Customer Challenge Group – Suggested Terms of Reference CCW

CCG Deliverables

The output from the CCG will be to provide a report to Ofwat, alongside the company's business plan, on the company's engagement process and the company's strategy and business plan. It will specifically cover:

- The effectiveness of, or any concerns with, the company's engagement with its various customers and with the CCG (taking account of Ofwat's characteristics of good engagement)
- Whether the level of engagement and assurance is proportionate to the materiality of the company's business plan proposals
- Whether the plan delivers the required legal outcomes
- Whether the company has actively considered the opportunities for more innovative and sustainable approaches to delivering the required or desired outcomes
- Whether the company's longer term strategy and business plan is an appropriate response to customers' views
- Whether the company's business plan strikes a reasonable balance between the views of different customers and stakeholders, highlighting any areas where particular segments of current or future customers are likely to have outstanding concerns
- Whether the company has explored the range of cost-effective solutions and phased delivery of its various outcomes to maximise acceptability to customers
- Whether the company's overall final business plan appears likely to be acceptable to the majority of customers, highlighting any areas of concern

Membership

The CCG will be independently chaired with a membership of no more than twenty. The quorum will be six and substitutes will be allowed with prior agreement of the Chair. Core members will represent bodies that have a key interest and statutory remit in the water sector and / or represent customers. As a minimum membership will include:

- Environment Agency
- Drinking Water Inspectorate
- Natural England
- Consumer Council for Water

- Domestic Customer
- Business Customers
- Local and Regional government representatives of customer interests
- Community representatives of customer interests

The Chair will play a role in the selection of members. The CCG may establish sub-committees, to review specific areas, who will report back on various subjects covered by the Terms of Reference.

As required, technical advisers, observers or other relevant representatives will be invited to the CCG as necessary and may include:

- Ofwat representatives
- Specialist advisers and business experts
- Representatives from other water and sewerage providers in the region

Critical Success Factors for the CCG

- Ensuring a good understanding by members of the main obligations, issues and priorities in the planning and provision of water services
- Advising and challenging the company to develop a customer supported, long-term strategic business plan that will provide appropriate outcomes, aligned to legal and regulatory obligations
- Reconciling the long-term strategic direction of the company with its AMP6 business plan
- Ensuring that customer outcomes have been sufficiently tested and challenged and are proportionately reflected in the AMP6 business plan
- Facilitating informed discussion on and achieving resolution of conflicting priorities as they arise

Governance

The Chair will be independent of the company to ensure it and the regulators can be effectively challenged. The Chair will be accountable to the non-executive directors who will agree terms and remuneration.

A memorandum of understanding will be signed by all members of the CCG, permanent and ad-hoc, and the business to maintain appropriate commercial, Intellectual Property and personal data confidentiality.

The company will provide secretariat and administrative support and costs of meetings. Expenses will be paid according to an agreed policy.

A work programme will be established by the CCG and will include:

- Ways of working with the business and the relationship with the decision making processes
- Establishing objectives with appropriate qualitative and quantitative measures and metrics
- Frequency and location of meetings, attendees, substitutes etc
- Assurance and audit programmes
- Boundaries of disclosure, including meeting outputs
- Recording and reporting

Agendas and other materials will be provided in a timely and accessible way.

Minutes and records of meetings will be maintained and kept in a suitable format.

6 Ofwat requirements for Stakeholder Engagement

The following is a summary of the policy requirements published by Ofwat.

In August 2011 Ofwat published a policy statement ³ detailing what it expects water companies to do on engagement and pricing that will affect customer bills for the business plan covering the period 2015-2020.

Engagement will be at 3 levels. Company managed engagement will be:

- 1 local, and direct engagement
- 2 challenge panel

and Ofwat managed engagement will be:

- 3 sector wide Customer Advisory Panel

1. Local and Direct engagement

The company is responsible for designing and managing the local engagement process effectively to engage:

- with individuals and organisations on local priorities and issues that could have a significant impact on the services customers receive
- on issues that may affect the broader local community (such as local levels of services, investments, tariffs)
- to test views on the acceptability of future plans

Appropriate quantitative evidence must be gathered to evidence the acceptability of investment and demonstrate the inclusion of stakeholders in price setting.

³ http://www.ofwat.gov.uk/future/monopolies/fpl/customer/pap_pos20110811custengage.pdf

Future work with customer / interest groups will evolve following identification and characterisation of stakeholders and the clarification and prioritisation of the issues.

2. Challenge Panel

The company is expected to establish a Customer Challenge Group to examine both the process of engagement and the outcome from the activity. They will have to report to Ofwat on:

- The appropriateness of the engagement process, proportionate to the expected impact on customer bills
- The materiality of the issues reviewed and the completeness of the process used
- The balance of the content of the business plan and that it reflects customer views
- Use of innovation and the delivery of sustainable (social, economic and environmentally balanced) solutions

The Panel will consider evidence of the direct engagement, discussing and challenging how the company has responded to comments and outputs.

Ofwat may attend meetings, but will not be a full time member.

There will be an independent chair and formally approved terms of reference.

3. Sector-wide Customer Advisory Panel

Ofwat will set up and run a panel of national experts. They will inform and challenge Ofwat on a number of key sector-wide assumptions, such as the cost of capital and provisions for pensions and energy.

Membership will include CCWater as the statutory water consumer representative. It can invite other representative organisations. The panel will not duplicate what is happening at company level and will not advise or challenge individual company business plans.

Ofwat 7 Principles of Stakeholder Engagement

Proposed by Ofwat to shape the engagement process:

1. Water companies should deliver outcomes that customers and society value at a price they are willing to pay
2. Customer engagement is essential to achieve the right outcomes at the right time and at the right price
3. Engagement should not simply take the place during price reviews. Engagement means understanding what customers want and responding to that in plans and ongoing delivery
4. It is the companies responsibility to engage with customers and to demonstrate that they have done it well
5. Customers and their representatives must be able to challenge the companies throughout the process. The engagement process should ensure this challenge happens. If this is not done effectively we must be able to challenge on customers' behalf. In doing so, we will fulfil our duty to protect customers.
6. Engagement is not 'one-size-fits-all' process, but should reflect the particular circumstances of each company and its various household and non-household customers.
7. The final decision on price limits is entrusted to Ofwat. We will use a risk-based approach to challenge company plans if this is necessary to protect customers' interests.

Appendix 2

Assurance Reports

Drinking Water Inspectorate

Environment Agency

Atkins Ltd



Drinking Water Inspectorate Statement for Affinity Water's Customer Challenge Group Report to Ofwat

1. Introduction

- 1.1 The Drinking Water Inspectorate (DWI) is the independent regulator of drinking water quality in England and Wales. We protect public health and maintain confidence in public water supplies by ensuring water companies supply safe clean drinking water that is wholesome, and that they meet all related statutory requirements. Where standards or other requirements are not met, we have statutory powers to require water supply arrangements to be improved.
- 1.2 We publish information about drinking water quality and provide technical advice to the Secretary of State for the Environment, Food & Rural Affairs, and to Welsh Ministers.
- 1.3 For PR14, water companies are expected to ensure that their business plans make provision to meet all their statutory obligations, including the need for public water supplies to be safe, clean and wholesome, and that provision is made for a sustainable level of asset maintenance to maintain public confidence in drinking water quality. Ministers summarised these requirements in Defra's Statement of Obligations¹ and in their further guidance on PR14 matters to Ofwat. In addition, the Inspectorate set out in **DWI Information Letter 01/2013 – The 2014 Periodic review of Prices – Guidance for water companies**, published on 1st February 2013 supplementary guidance to companies on the regulatory framework for drinking water quality, statutory requirements, the Inspectorate's role in the Price Review process and our requirements for companies seeking technical support. The Inspectorate also published separate PR14 guidance on a range of specific issues. All of the Inspectorate's published PR14 guidance is available on the DWI website.
- 1.4 It is worth noting the particular emphasis that Ministers placed in their Guidance on the resilience of supply systems, and that the Inspectorate placed on existing duties to manage the introduction of new sources and to plan supply arrangements to protect consumers and ensure no deterioration in the quality of their supplies.

¹ <http://www.defra.gov.uk/publications/files/pb13829-statement-obligations.pdf>

1.5 The Inspectorate has a position on all of the water companies' customer challenge groups in England and Wales. The Inspectorate's representative on Affinity Water's Customer Challenge Group has supported the process by acting as an independent member with the overall remit of ensuring that the Company business plan proposals reflect the views of consumers and place drinking water quality at the forefront of such plans.

2. Formal Drinking Water Proposals Requiring DWI Technical Support

2.1 As with previous periodic reviews, water companies seeking technical support from the Inspectorate must demonstrate the need for each proposal. The case for justification must be accompanied by evidence of the company's options appraisal process to identify the most robust, sustainable and cost-effective solution, with evidence that the preferred solution will adequately address the risk and deliver the required outcome within an appropriate timescale.

2.2 Affinity Water submitted 5 formal proposals for drinking water quality to the Inspectorate, listed in the table below:

PR14 DWI Ref.	Scheme Name	Quality Parameter(s)	Scheme Type	Preferred Option	DWI Final Decision
AFW29	Iver WTW	Pesticides including carbetamide, propyzamide & metazachlor	Treatment + Catchment Management	Combination of approaches, including increased GAC capacity and pilot studies of treatment options to mitigate metaldehyde	Regulation 28 Notice
AFW30	North Mymms WTW	Pesticides, including metaldehyde	Treatment + Catchment Management	Treatment to be investigated + Catchment Actions	Undertaking
AFW31	Ardleigh WTW	Pesticides, including metaldehyde & clopyralid; and Disinfection Byproducts	Treatment + Catchment Management	Installation of On-site metaldehyde monitor + Catchment Actions	Undertaking
AFW32	River Thames Metaldehyde - 4 sites	Metaldehyde	Catchment Management	Catchment actions	Undertaking
AFW33	Lead Strategy	Lead	Company lead strategy	Package of measures	Regulation 28 Notice

2.3 The Company is to be commended on the quality of the submissions to the Inspectorate, which complied with our PR14 guidance. The Inspectorate met with the Company before the proposals were submitted, and there were further discussions at CCG meetings. Therefore we were broadly aware of the Company's plans for drinking water quality and we are generally supportive of the Company's approach.

2.4 The Inspectorate proposes to support the Company's proposals as indicated above and discussed below and we will put legal instruments in place to make

the proposals legally binding programmes of work. Our final decision letters were sent to the Company on 14th and 28th October 2013.

- 2.5 Four of the proposals are to implement measures to address increasing levels and types of pesticides in the raw waters at Affinity's major surface water treatment works. Metaldehyde is widely used in agriculture for the control of slugs, and is not removed by existing treatment processes for pesticide removal. 2012 was a very wet year and Affinity Water, like most companies with lowland surface water abstractions, experienced high levels of metaldehyde in raw waters which lead to failures of the standard in water supplied to customers. Proposal AFW32 is to implement catchment actions to aim to reduce levels of metaldehyde reaching water courses in the Thames catchment and covers 4 water treatment works: Chertsey, Egham, Iver & Walton. The proposal includes investigating options to subsidise farmers to use an alternative product. The costs of all the catchment management programmes of work included in the above table are allocated to the NEP.
- 2.6 The proposal for North Mymms includes investigation of treatment options to address metaldehyde. North Mymms treats water from four different groundwater sources that are vulnerable to pollution from various sources. In two of the sources metaldehyde has been detected where its origin is thought to be a local landfill site. In this case catchment actions are unlikely to achieve significant benefits, and the Company is proposing to install powdered activated carbon dosing (PAC) at North Mymms treatment works to assess its ability to reduce levels of metaldehyde to achieve compliance with the standard in the treated water. Since issuing our final decision letter, the Company has indicated that the target date for completion of North Mymms to treat pesticides will be March 2017 and not March 2016 as previously indicated.
- 2.7 The proposal for Ardleigh WTW is partially supported by the Inspectorate. An Undertaking will be put in place to cover the catchment and abstraction management proposals to mitigate metaldehyde and clopyralid. The inclusion of disinfection byproducts (DBPs) as a parameter in the proposal relates to the new Regulation 26(1A) in the Water Supply Regulations 2010, which requires companies to minimise the formation of DBPs during treatment and in distribution, without compromising the effectiveness of any disinfection stages. The proposal involves increasing the frequency of regeneration of granular activated carbon (GAC) from an average of once every 8 years to once every 5 years. We declined to support this proposal on the basis that there were no grounds for enforcement. The proposal also included plans for enhanced monitoring for DBPs and precursor compounds within the treatment process with a view to identifying options for optimising the process to minimise formation of DBPs. We commended for support this element of the Ardleigh proposal because we consider that this work will add to the Company's understanding of the contribution of the treatment processes and other factors towards the formation of disinfection byproducts, which will inform future investment needs to improve compliance with Regulation 26(1A). Ardleigh WTW is managed by the Ardleigh Reservoir Committee on behalf of Anglian Water and Affinity Water, and each company contributes 50% of the costs.

- 2.8 The Company submitted a proposal to address lead in drinking water that is generally consistent with Guidance. The standard for lead will reduce from 25µg/l to 10µg/l in December 2013, and the package of measures included in the Company's proposal will improve compliance with the new standard and reduce consumers' exposure to lead from drinking water.
- 2.9 It should be noted that these improvement schemes will make only a small contribution to enabling the Company to meet its legal obligations in respect of drinking water quality. These obligations are met overwhelmingly by the Company making sufficient provision for operational and maintenance requirements in its business plan, and by its use of those resources. These are matters for the Company to determine and deliver. For its part, the Inspectorate will continue to keep under review, and report on, the performance of the Company in meeting its legal obligations. Statutory powers are available to secure or facilitate compliance, if necessary.
- 2.10 The summary of improvement schemes above reflects the position at the time of writing this statement. Further discussions are needed with the Company to finalise details. We will advise the CCG and Ofwat of any material changes.
- 2.11 This statement will be copied to Fiona Waller of Affinity Water. Any queries arising should be directed to Jacqueline Atkinson, Inspector, Drinking Water Inspectorate, telephone number: 03000686402; email dwipricereview@defra.gsi.gov.uk.



Milo Purcell
Deputy Chief Inspector (Regulations)

Drinking Water Inspectorate

Area 7e, 9 Millbank
c/o Nobel House
17 Smith Square
London SW1P 3JR

29th October 2013



Richard Bienfait
Affinity Water
Tamblin Way
Hatfield
Hertfordshire
AL10 9EZ

Date: 1 November 2013

Dear Richard

Affinity Water Business Plan Evaluation Response

I would like to thank Affinity Water for providing the Environment Agency with material from your draft business plan.

In the attached report, we have used this information to assess the extent to which your business plan will meet your statutory requirements, and the environmental obligations set out in Defra's Statement of Obligations.

When making our assessment, we have reviewed how quickly you are planning to deliver your obligations, together with your overall level of performance. For your river basin management plan obligations in particular, Ministers are looking for assurance of early delivery wherever possible.

My team would be happy to discuss the report with you. We would be pleased to include any clarifications before we contribute to the Customer Challenge Group report and prior to our submission to Defra in mid November.

We look forward to continuing to work with Affinity Water to help ensure that your investment protects and improves the water environment, for the benefit of your customers and the economy.

Yours sincerely

Howard Davidson
Director South East Region

Cc: Dr Paul Leinster CBE, Chief Executive, Environment Agency
Ian Barker Head of Land and Water, Environment Agency
Robin Dahlberg, Affinity Water CCG Chair
Sonia Brown, Ofwat,
Tim Collins, Natural England
Milo Purcell, Drinking Water Inspectorate

Response to Affinity Water

Introduction

The final price review methodology confirms that Ofwat expect the Environment Agency to highlight in the Customer Challenge Group (CCG) report whether your business plan will meet your statutory obligations (section 4.2.1 Setting Price Controls for 2015-2020, Ofwat, July 2013). As part of our engagement with your CCG, we have been working with you to be assured that your business plan is in accordance with these requirements.

The following report summarises our views of the draft plan and evidence provided. These views are based on a high-level review of the processes as described in the letter explaining our expectations sent to you in August 2013.

Overview

We have had good ongoing dialogue with you during development of your business plan.

We note that your customer survey work and your willingness to pay surveys show that customers are willing to pay for some modest level of service improvements.

However, we have some real concerns with your plan around implementation of sustainability changes, the return period for emergency drought orders and lack of a change mechanism.

We will continue to work with you to resolve any outstanding issues throughout the remainder of the planning process.

We welcome:

- Your assurances that you will meet your environmental obligations.
- The level of metering, leakage and water efficiency in your Water Resources Management Plan (WRMP) and the development of associated performance measures.
- Your approach to managing risk from future climate change, development growth and extreme weather events.

We are pleased to note that:

- You have included an environmental outcome.
- You are adopting Water Resources in the South East (WRSE) solutions in your WRMP.

We do not support:

- Your challenge to sustainability changes late in the process. You need to recognize that a weak cost benefit case could still result in an alternative objective being set and you need to allow for this.
- The discrepancy between your WRMP and your drought plan concerning return periods of drought management measures.
- You originally proposed a return period of 1:50 for emergency drought orders, now recalculated to 1:118. We have yet to see clear acceptance by your customers for either of these.
- Your lack of a proposed change mechanism. Without one there is a risk that you could be left, with unfunded obligations which may arise from the Second cycle River Basin Management Plan (RBMP).

We need to see:

- Consideration being given to a greater allowance for measures arising from the second cycle of River Basin Management (RBMP) plans to prevent compliance with the Water Framework Directive (WFD) being too 'back end loaded'.
- Confirmation that sustainability changes will be included in the plan and delivered in AMP6
- An assurance that there will be consistency between your Business Plan and WRMP
- Further development of your thinking around outcome delivery incentives and associated rewards/penalties.

We have made more specific comment on the following areas:

These are our observations on the replies you have made to the questions posed in response to the expectations letter.

1. Delivery of statutory and environmental requirements

Based on the information provided in your submission we believe that there is a risk of your company not being able to fulfil all of its environmental obligations during AMP6. We believe that the following areas of your business plan require strengthening to ensure you meet all of your statutory requirements: Water Framework Directive, Water Resources Management Plan and the England Biodiversity strategy. We would strongly encourage you to revisit your plan ahead of final submission to Ofwat.

2. Measures identified within the National Environment Programme (NEP)

Thank you for the letter of assurance (25th October 2013) stating that, based on a revised NEP3 dated 22 October, you have included all schemes within your business plan. We believe the Sustainability Changes proposed in this revised NEP3 (to be formally confirmed as NEP4) will achieve a positive environmental outcome. However, where we have agreed that you can retain a reduced average and peak capability to reduce the cost burden on your customers, you need to be aware that this capability will continue to be reviewed and may need to be revoked if it is found to be preventing environmental commitments being met. This could result in environmental obligations that you need to make an allowance for.

You also need to recognise that for a sustainability change with a weak cost benefit case the water body could be given an alternative objective and if it is included in the final RBMP it is statutory and it will have to be implemented irrespective of customer support as defined by willingness to pay (WTP).

2.1 Transition investment programme

We are pleased to see the specific proposals you are considering for transitional investment before the start of PR14, including ramping up the catchment management programme and the early launch of the communications programme for your compulsory metering programme.

3. Provision for the outcome of second cycle river basin management plans and delivery of Water Framework Directive (WFD) obligations

We are concerned that you do not appear to have made an allowance within your business plan for achieving outcomes from the second cycle river basin management plan. We were disappointed to note from a recent meeting with you that you believe that there is no regulatory provision for inclusion of unknown implementation work and due to the scale of potential costs and your ability to predict what these would be, you do not consider it is appropriate to include these in your PR14 submission. We encourage you to make provision for these outcomes in line with the requirements of the Statement of Obligations. This will help mitigate towards having a large number of WFD obligations later in AMP7 and AMP8. Early delivery of WFD measures is essential if England is to make progress towards the necessary environmental improvements by 2027.

4. Evidence of options and proposals for reducing the impact of a company's abstractions from the most seriously affected sites

It is important to manage the impact of abstractions at sites that are, or are likely to be, causing damage to the environment. We now have an agreed revised NEP3, but the success of the revised schemes to achieve the desired environmental outcomes will be kept under review.

Given this uncertainty, we would like further clarity on how you intend to ensure that your abstraction activity will not damage the environment. Defra expects you to plan for all confirmed and likely sustainability changes. We expect you to demonstrate how you will deliver the currently unknown sustainability changes, should these be confirmed at NEP phase five. You should also show that any proposals to increase abstraction at existing or new sites will not cause deterioration in water body status.

5. Alignment of the Water Resource Management Plan (WRMP) options and business plans.

We expect WRMP options to form the supply-demand component of the business plan, asking that any material differences between the two plans be justified. Currently we do not feel that you have provided sufficient assurance that the main water resources supply-demand components of your business plan will be consistent with your WRMP statement of response.

We have already expressed in our representation on your WRMP that we have a concern with your water resources management plan, where it proposed a return period of 1 in 50 years (recently recalculated to 1 in 118) for emergency drought orders. At our business plan meeting in September you stated that your customers were happy with the level of service they receive and they weren't

seeking improvements. We would ask you to justify this statement using specific evidence from your customer engagement.

The return periods quoted on a number of drought management measures were inconsistent with the return periods quoted in your drought plan. You have recently informed us that you will be updating your drought plan to make it consistent with your WRMP and await confirmation this has happened.

6. Reservoir safety

We note your intentions to maintain reservoir safety although you have provided limited information on the programme of work. This is an important duty given the potential high impact your reservoirs pose to public safety. Your continued maintenance and capital investment is essential for public safety.

You have referenced the recent changes in reservoir legislation. Please confirm how you will implement these changes during the next AMP.

Defra set out its expectation in the Statement of Obligations that companies will prepare reservoir plans. We would expect you to continue to develop and maintain on-site plans. You do not refer to incident planning and working with partners to reduce impacts to downstream communities, should an incident occur. We encourage you to co-operate with relevant authorities and partners on the development and maintenance of site plans and on incident planning.

7. Mitigation measures adopted to manage future risks

We are satisfied with your response on climate risks and resilience. You have said you have followed relevant guidance from Ofwat and others, and provided evidence that you have done so. It is important to keep raising awareness of these issues so that the impacts are fully understood.

8. Environmental outcomes

We are satisfied with the outcomes and indicative performance measures included in your business plan which accurately reflect the important role that your company plays in protecting the environment. At the time of writing you are still working on your performance measures and targets and we look forward to receiving an update.

8.1 Delivery and incentives.

The information provided in your submission about incentives and setting of delivery levels was insufficient. We recognise that this work is still being developed but we cannot be sure that your ambition reflects both statutory requirements and customer preferences, nor that you will be sufficiently incentivised to meet your goals. The Environment Agency is keen to promote use of outcome-focussed measures of success, which reflect the delivery of environmental benefits that should follow on from compliance. We also believe it may be appropriate to use financial penalties to incentivise delivery of those statutory obligations, and rewards if customer preferences justify going further or faster than those obligations. Reference to customer preferences, as well as legal obligation, is essential.

9. Compliance

You have told us that your target compliance rate is 100% for discharges from your operations that embrace water treatment waste and water from excavations. We assume that you have a target compliance rate of 100% for abstraction licences too. All water companies should be planning to achieve 100 per cent compliance for all licences and permits, as they are legal obligations. We expect to see this included as a target within your business plan.

10. Change mechanism

At previous price reviews, Ofwat has used the change protocol for managing in-period changes to the risks and costs. This time you are being asked to put forward proposals for dealing with such changes. It is imperative that new statutory requirements, for example schemes arising from the 2nd River Basin Management Plan can be delivered whilst maintaining levels of ambition around customer priorities. We would like to see a clear process for dealing with predictable but, nonetheless uncertain new commitment you could face during AMP6.

To be assured that important “discretionary” outcomes are not prejudiced by additional legislative requirements, we believe you do require an explicit change mechanism for dealing with such changes. We acknowledge your assurance that you are developing one.

11. Natural England

In so far as the comments herein relate to the natural environment, they also reflect the advice of Natural England. In addition, Natural England expects the business plan to explain how your company will deliver its statutory duty to conserve and enhance biodiversity, including on Sites of Special Scientific Interest (SSSIs) which Affinity Water owns or manages. You have told us that these obligations will be met through estates management and the continuation of your biodiversity programme into AMP6, but at present there is insufficient information to reassure us that biodiversity has been considered in development of your plan. Performance measures and targets relating to biodiversity enhancement and SSSI management should be included in the final plan.

Concluding remarks and recommendations

Overall we support many of the proposals contained within your business plan but presently have doubts that you have produced a plan that will meet your statutory requirements and environmental obligations.

The areas where significant improvement is needed as follows:

- Planning to a more appropriate return period for an emergency drought order, or demonstrating that your customers understand and support the one you are proposing.
- Ensuring that your business plan is consistent with your WRMP.
- Clearly demonstrating your approach to Managing Uncertainty.
- Development of a change mechanism.

We look forward to working closely with you over the next few weeks to finalise your business plan. Our aim is to help you produce a plan that delivers its statutory obligations and facilitates the continuing achievement of better environmental performance.

David Howarth
4 November 2013

Mike Pocock
Physical Asset Strategy Manager
Affinity Water
Tamblin Way
Hatfield
Herts
AL10 9EZ

Date: 21 November 2013

Dear Mike

Affinity Water Business Plan Evaluation Response

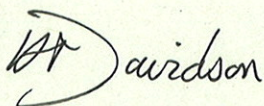
Thank you for the notes of the meeting held on 5th November 2013 where you provided further information on your Business Plan.

From the information you have provided, we understand that you are planning to meet your statutory environmental requirements set out in Defra's Statement of Obligations. The questions we sent you (Questions to water companies to support the evaluation of business plans) in advance of our meeting of 19th September 2013 asked you to provide a letter of assurance from your board that the measures set out in the National Environment Programme have been included within your Business Plan. While we are in receipt of a letter from you (25th October) giving the assurance we are seeking this unfortunately does not meet our requirements of this letter needing to be from your Board. I would be grateful if you could provide a letter of assurance from your Board.

I have attached an annex which includes our comments on your notes of that meeting, which you can include as an addendum to our original report.

I hope that you find this additional response useful. If you have any further queries please do not hesitate to contact us again.

Yours sincerely



Howard Davidson
Director, South East

Cc: Dr Paul Leinster CBE, Chief Executive, Environment Agency
Ian Barker, Head of Land and Water, Environment Agency
Robin Dahlberg, Affinity Water CCG Chair
Sonia Brown, Ofwat
Tim Collins, Natural England
Milo Purcell, Drinking Water Inspectorate

Response to Affinity Water

21 November 2013 - Update following further communication with the company

Following receipt of our evaluation report on 4 November 2013, we have been involved in further discussions with you regarding our recommendations in the report. This note provides an update to our response based on those discussions.

The following table summarises the company's response to Environment Agency recommendations. Based on the further information provided to us, we now also make the following additional observations:

Environment Agency statement/ recommendation	Company response and date (meeting minutes 5/11/13)	Environment Agency comment 21/11/13
We are concerned that you do not appear to have made an allowance within your business plan for achieving outcomes from the second cycle river basin management plan. We were disappointed to note from a recent meeting with you that you believe that there is no regulatory provision for inclusion of unknown implementation work and due to the scale of potential costs and your ability to predict what these would be, you do not consider it is appropriate to include these in your PR14 submission.	1.Affinity Water indicated they would be keen to contribute information to the RBMP process to support consultation on the measures. In particular would like to cover the affordability, customer acceptability and proportionality of WFD driven sustainability reductions so that we can confirm existing proposals and future sustainability reductions and further obligations and investment needs. The Agency confirmed this round of RBMP would cover the period to 2027 rather than the next six year period (to 2021) as the first round of RBMPs. Affinity Water welcomed the RBMP and confirmed agreement	We note your willingness to review the priority and programme for sustainability reductions as new obligations emerge.

	<p>with the aim of early delivery of WFD measures, as evidenced by the leading role the company has taken to date to secure agreement on sustainability reductions for PR14.</p> <p>2. The Agency indicated that they recognised the risk of substantial further sustainability reductions arising from the 'unknown' list was low. They reiterated their advice that Affinity Water needs to make provision for potential new obligations. Affinity Water welcomed the advice and agreed with the assessment of 'low risk' based on the history of studies in the Colne Valley in particular which constituted the bulk of the 'unknowns'. This was noted by the Agency. Affinity Water stated it is willing to review the priority and programme for sustainability reductions as new obligations emerge. It recognised that, whilst the Agency has hitherto stated that implementation SRs would not prejudice public water supplies, this priority could change and therefore Affinity preferred to agree a pragmatic approach with the Agency to complement the existing programme. This was welcomed by the Agency.</p> <p>3. Affinity Water expressed its concerns over the inclusion of substantial investment where there was no evidence of a requirement. We noted that without clear justification, investment was</p>	
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	unlikely to gain approval from Ofwat and reminded the Agency of the penalties incurred at Pr09 when they proposed such investment and pressure for flat prices. The Agency is aware of the recent letter from the Secretary of State but also highlighted discussions which had taken place with Ofwat, where Ofwat had given the Agency guidance that provision for potential new obligations would be considered by Ofwat	
<p>At previous price reviews, Ofwat has used the change protocol for managing in-period changes to the risks and costs. This time you are being asked to put forward proposals for dealing with such changes. It is imperative that new statutory requirements, for example schemes arising from the 2nd River Basin Management Plan can be delivered whilst maintaining levels of ambition around customer priorities. We would like to see a clear process for dealing with predictable but, nonetheless uncertain new commitment you could face during AMP6.</p> <p>To be assured that important “discretionary” outcomes are not prejudiced by additional legislative requirements, we believe you do require an explicit change mechanism for dealing with such changes. We acknowledge your assurance that you are developing one.</p>	<p>1. Affinity Water confirmed it had considered a range of mechanisms to finance new obligations such as those that may arise from the current ‘unknown’ sustainability reductions including outcome incentives, AIM and a change process. Affinity had emailed their outline proposal for a change process to the Agency and invited comments.</p> <p>2. Affinity Water confirmed it would include a change process in the Business Plan to make allowance for future investment to meet currently unknown statutory obligations such as those arising from River Basin management Plans. It had emailed an outline proposal to the Agency for comment. This was acknowledged by the Agency. Affinity Water noted that they have not found it necessary to use the change process to date. We also noted that it was not our experience that Ofwat would agree investment in principle ahead of an obligation arising. The</p>	<p>We note that you will not be making an allowance within your business plan for achieving outcomes from the second cycle river basin management plan. We understand that, should you be faced with unfunded obligations arising from for example, RBMP, you will plan to meet these from either the use of you change mechanism, alternative financing arrangements or a combination of the two.</p>

	<p>Agency stated that Southern Water had employed the change process to fund new obligations on sewerage operations and might offer information on their process. Affinity Water welcomed the suggestion.</p> <p>3. The Agency indicated that the difference between its position and that of Affinity Water wasn't the lack of a change process proposal. The Agency noted that it had indicated to us that the concern related to the need for the Agency to have clear confirmation of Affinity recognition of responsibilities for new obligations. In particular the Agency wanted confirmation that we were not simply intending to rely on a change process mechanism to carry the financial risk. It wanted reassurance on how Affinity Water will finance new obligations, including if necessary, justification for inclusion in prices. Affinity Water confirmed that it has an absolute responsibility to deliver against statutory obligations even if these were not included in prices – this risk is one that our shareholders carry – but we noted we would provide further assurance on financeability.</p>	
<p>Thank you for the letter of assurance (25th October 2013) stating that, based on a revised NEP3 dated 22 October, you have included all schemes within your business plan. We believe the Sustainability Changes proposed in this revised NEP3 (to be formally confirmed as NEP4) will achieve a positive environmental outcome. However, where we have agreed that you can retain a reduced average and</p>	<p>Affinity Water repeated the assurance in its recent letter that agreed sustainability reductions will be included on the Business Plan. The Agency expressed concern over substantial changes in Affinity Plan. Affinity confirmed their strategy for their revised plan was largely unchanged from the dWRMP with leakage</p>	<p>Thank you for providing additional information. We are looking for assurance from your Board that your Business Plan will include the National Environment Programme in its entirety. While you have written to us (25th Oct) stating this to be the case we still need a letter of assurance from your Board.</p>

peak capability to reduce the cost burden on your customers, you need to be aware that this capability will continue to be reviewed and may need to be revoked if it is found to be preventing environmental commitments being met. This could result in environmental obligations that you need to make an allowance for.	reduction below the SELL, compulsory metering in all Central Region zones, albeit at a marginally slower rate to reduce the effect on prices and water efficiency. Affinity is committed to achieve the upper bound of demand savings to be able to leave most water in the environment. Affinity explained they have proposed one minor volume change of 2 Ml/d at average only and this to allow for retention of peak licence at Whitehall pumping station. The Agency said it was reassured by this explanation.	
Currently we do not feel that you have provided sufficient assurance that the main water resources supply-demand components of your business plan will be consistent with your WRMP statement of response.	Affinity confirmed its statement in the letter of assurance that the Business Plan supply/demand submission is based upon the same data as WRMP and wholly consistent with it. EA stated they were satisfied with this further assurance.	Thank you for your assurance.
The information provided in your submission about incentives and setting of delivery levels was insufficient. We recognise that this work is still being developed but we cannot be sure that your ambition reflects both statutory requirements and customer preferences, nor that you will be sufficiently incentivised to meet your goals	Affinity Water stated that their proposals for outcome delivery incentive mechanisms were shared with their CCG on 4 th November. Jim Barker confirmed that was so and the Agency were considering these.	Noted.
Cost-benefit of sustainability reductions	Affinity confirmed that Agency local staff had met with them on 4 November and provided the outstanding information on the outcome of Agency work to define the benefits of sustainability reductions. Both parties had committed to an agreed cost-benefit statement confirming a robust cost benefit case for inclusion in the revised WRMP. Ref: attached draft extract from Affinity Water revised WRMP. Affinity Water noted that they were pleased that	Noted.

	this would resolve the concerns they had raised with the Agency in August.	
With one of the highest pccs in the country the company could show more ambition in reducing it.	The Agency stated that this issue was omitted from their recent report but they expected Affinity Water to be ambitious with demand reductions in view of its high PCC. We confirmed our commitment to support customers to reduce their consumption and have proposed a comprehensive programme of leakage reduction, compulsory metering and water efficiency. Affinity Water aim to maximise demand reductions in AMP6 and plan to achieve their metering programme 13.6% from the metering programme, in line with our experience of compulsory metering in our Southeast Region (16%).	Noted.
We have already expressed in our representation on your WRMP that we have a concern with your water resources management plan, where it proposed a return period of 1 in 50 years (recently recalculated to 1 in 118) for emergency drought orders. At our business plan meeting in September you stated that your customers were happy with the level of service they receive and they weren't seeking improvements. We would ask you to justify this statement using specific evidence from your customer engagement.	Affinity thanked Agency staff for their assistance to verify their LoS drought restrictions assessment. Affinity have clarified the LoS measures in the revised WRMP (extract provided) and explained the difference from draft caused by an over-cautious interpretation of how the probability of return event occurrence transposes to what customers experience. The Agency confirmed they were now satisfied with the outcome of the review and clarification of the Affinity position	We have noted your recalculation and we are aware that this is included in the Statement of Response for your WRMP.
No deterioration. Affinity Water to clarify how it will show its abstractions will not damage the environment.	Affinity has been working in partnership with the EA since 1992 to identify potential effects of abstraction on the environment and voluntarily	Noted.

	<p>implemented operating agreements on the Ver, Misbourne, Hiz and Ashwell Springs. In preparing the current WRMP we have assessed the environmental impacts of all feasible options both through our SEA and also in discussion with the EA on a number of occasions to screen out any schemes with significant environmental concerns. Groundwater abstraction has the lowest cost and highest quality and therefore abstraction under current licences is maximised which means there is a low risk of 'deterioration'. We have an on going programme of environmental monitoring and will continue to assess performance and local effects at all sites during AMP6. We will include all environmentally sensitive sites in our AIM reporting to show how we manage our abstractions. New abstractions or modifications to licences on existing sites will be subject to the standard licensing process and any conditions set by the Agency.</p> <p>Affinity welcomed the Agency's suggestion that the assessment of deployable output should be reviewed during AMP6. We would be willing to explore this issue with the Agency as we recognise the value in improving the robustness of the current process</p>	
<p>You have referenced the recent changes in reservoir legislation. Please confirm how you will implement these changes during the next AMP.</p>	<p>Affinity is willing to participate in the risk assessment review of its reservoirs arising from the recent changes in reservoir legislation. Our initial view is that this may reduce the number of our reservoirs subject to the act but this will have only a marginal effect on our inspection programme as we currently and in</p>	<p>Thank you for providing further information.</p>

	future adopt the same standard of inspection and maintenance for all our reservoirs. We will provide details of our reservoir inspection programme separately	
You have told us that your target compliance rate is 100% for discharges from your operations that embrace water treatment waste and water from excavations. We assume that you have a target compliance rate of 100% for abstraction licences too. All water companies should be planning to achieve 100 per cent compliance for all licences and permits, as they are legal obligations. We expect to see this included as a target within your business plan.	Affinity confirm we have a 100% compliance record on abstractions and will continue to operate with that goal. We meter all our abstractions and monitor integrated flows continuously at all sites with alarms set to limit abstraction to licence conditions. We calibrate our flowmeters in accordance with EA best practice guidance	We welcome your commitment to 100% permit compliance.
We believe the Sustainability Changes proposed in this revised NEP3 (to be formally confirmed as NEP4) will achieve a positive environmental outcome. However, where we have agreed that you can retain a reduced average and peak capability to reduce the cost burden on your customers, you need to be aware that this capability will continue to be reviewed and may need to be revoked if it is found to be preventing environmental commitments being met. This could result in environmental obligations that you need to make an allowance for. You also need to recognise that for a sustainability change with a weak cost benefit case the water body could be given an alternative objective and if it is included in the final RBMP it is statutory and it will have to be implemented irrespective of customer support as defined by willingness to pay	Affinity is willing to implement sustainability reductions as required by the Agency and awaits confirmation of the mechanism to be used either through revocation, notification of environmental damage or an operating agreement. Meanwhile we remain willing to continue discussions on the details for implementation and any potential specific operating conditions relating to supply resilience at the Agency's convenience.	Noted.

Your Ref:
Our Ref: C-131280/DJH/AW.PR820

info@atkinsglobal.com
www.atkinsglobal.com

25th November 2013

Affinity Water Ltd.,
Tamblin Way,
Hatfield,
Hertfordshire,
AL10 9EZ

For the attention of Chris Offer
Assurance Update for the Affinity Water CCG

Dear Chris,

Further to your request for a final assurance letter to the CCG, below is a summary of our findings, organised according to the categories requested by Robin Dahlberg and outlined in the document you provided earlier today:

- **Item 1 - Process used to compile the Business Plan.** Our audit process and the caveats associated with that process are fully described within our audit report dated 15/11/13. We note that this includes the following statement:

'Whilst we cannot therefore confirm absolutely that no errors or omissions exist within the evaluations that underpin the Business Plan, we have taken reasonable steps to expose those areas of uncertainty, poor assumptions or errors that might have a significant impact on the Capital Programme or the integrity of those parts of the Business Plan that are included within our scope of works'

We have also raised a number of issues that we consider should be noted as part of our findings on the Business Plan, which have been previously described to the CCG in our report dated 14/11/13. However, we do not consider that any of these affect the overall integrity of the compilation of the Business Plan. We can therefore confirm that, to the extent revealed by our audits, the process that has been used to derive the Business Plan has not resulted in any material errors or deliberate bias in the assessments and models that underpin the capex and opex figures that have been produced.

- **Item 2 – Contributing evidence.** As noted in our audit report, the complex nature of the evaluations and data involved in deriving a Business Plan means that there are inevitable uncertainties that exist with data and the evidence base. This applies to all water companies, and areas of uncertainty that are specific to Affinity Water have been highlighted in our main audit report. However, we can confirm that, to the extent revealed by our audits, the data and evidence that has been used for the Business Plan has not resulted in any material errors or deliberate bias in the capex and opex figures that have been produced.
- **Item 3 – Changes from the 20/11/13 Board.** Based on the table data that we have been provided with subsequent to the Board, we can confirm that no material changes were made.
- **Items 4 to 6 – Bill Impacts.** Atkins has not been involved in the auditing of the financial model so cannot confirm projected bill impacts from the capex and opex forecasts that we have seen. We can confirm that the capex and opex inputs that are contained in Ofwat Tables W1, W3 and W12 reflect the models and cost data that we reviewed during our audit process. We have been

informed by Affinity Water that, given the WACC and financing efficiencies that it has assumed, that this level of Totex will result in a real terms decrease in bills of 0.7% per annum.

I trust that the above information meets the CCG requirements. Please do not hesitate to contact me if you would like to discuss this in more detail.

Yours sincerely
for and on behalf of Atkins Ltd.

A handwritten signature in dark ink, appearing to read 'Doug Hunt', with a stylized, flowing script.

Doug Hunt

Reporter

Appendix 3

CCG Members

Members Biographies and Autobiographies

Overview

The report to Ofwat by the Customer Challenge Group (CCG) is a collegiate effort for which we are collectively responsible. For this appendix, we decided that each CCG member would be free to draft a biography or autobiography in the individual style they preferred.

Jacky Atkinson - Drinking Water Inspectorate

I have spent more than 35 years in the water industry, initially working for a major water and sewerage company as a water quality scientist, with periods working in water quality regulation including development of compliance sampling programmes, writing quality manuals for water supply sampling, implementation of the company's Hygiene Code, monitoring progress of drinking water quality capital schemes and catchment protection. I have also worked as a water treatment process scientist, followed by a spell in operational audit and operational risk management. More recently I worked in the water company's regulations department as a point of contact with Ofwat for operational matters and regulatory reporting. I qualified as a microbiologist through the Institute of Biology in 1982.

I have been an Inspector in the Drinking Water Inspectorate since 2010 and am the Inspectorate's project manager and day-to-day contact for Ofwat's next price review and business.

Jim Barker - Environment Agency

Water Planning Manager, Environment Agency Southeast.

I have worked for the Environment Agency since its conception in 1996 in various roles including incident response, inspection and regulation and strategic planning.

In my current role I am responsible for the Environment Agency's contribution to the Water Framework Directive, Water Resource Management Plans and the 2014 Periodic Review for the South East of England.

Representing one of Affinity's regulators with my role on the CCG is to provide insight on how Affinity's plans reflect Environment Agency guidance and their legal obligations as well as to challenge the company to take options that minimise their impact on the environment wherever possible.

Allyson Broadhurst: Managing Director of Charis Grants Ltd

I joined Charis in 2008 during a period of economic challenge which has adversely affected many households. Charis provides debt and award scheme solutions for businesses and public sector bodies, to help support vulnerable customers, individuals and families facing hardship and poverty. My current work, coupled with my background experience in a number of public sector roles including non- executive NHS Chairmanships, City and District Counsellor, and Chair and Trustee of a Community Foundation – a philanthropic charity awarding grants into community - has given me wide exposure to the issues and difficulties faced by those most in need facing severe financial challenge.

Being invited to join Affinity Water's Water Challenge Group has enabled me understand the company's vision for the future whilst representing issues on behalf of vulnerable and low income customers.

Keith Cane - Head of Housing Management, East Kent Housing

I am Head of Housing Management, East Kent Housing. I have over 30 years experience working in social housing with various housing associations and local authorities and now with the country's first 'super' ALMO, managing around 17,500 properties for Shepway, Dover, Canterbury and Thanet District Councils. I am also a customer of Affinity Water having lived in Folkestone since 1987.

Robin Dahlberg - Chair

I have over 20 years experience at Chair/Board/Chief Executive level roles in both the public and private sectors. I spent over ten years on the Boards of government bodies, including three regulators. I have also worked for Citizens Advice, in both paid and volunteer roles.

I was attracted to chair Affinity Water's Customer Challenge Group because it represented an opportunity to contribute to Ofwat's innovative approach to using the customer as co-regulator. In a number of sectors over recent years, Government policy has encouraged the involvement of customers in decisions that were previously solely the provenance of the regulators. Through its Price Review 2014, Ofwat has taken this concept further with the objective of getting water and sewerage companies to focus on identifying and delivering the outcomes their customers desire. I am delighted to have been able to contribute to the delivery of this innovative policy.

John Fox - Tendring District Council

I am the Environmental Services Manager for Tendring District Council.

The Environmental Services Team undertakes work in relation to food and health and safety and is responsible for private water supplies and in addition helps monitor water quality issues in relation to corporate assets such as swimming pools.

In addition the Team provides the port health function which includes ship inspection and checking water quality on ships.

Karen Gibbs - Consumer Council for Water

I lead CCWater's Environmental Policy Team and am the regional manager for London and the South East. I have worked in consumer representation within the water sector since 1993, initially with Ofwat and now with the Independent Consumer Council for Water (CCWater). As a consequence I have been involved in all subsequent price reviews and have a broad knowledge of water consumer issues. I am particularly keen to ensure that Affinity Water does all it can to engage with its customers through the business planning process in order to raise awareness of the issues affecting the water service and the company's plans for the future. We will want to see that the feedback from customers has influenced the company's strategy and that their plans will address customers' priorities.

Karen is an Affinity Water customer.

Dr David Howarth - Environment Agency

Water Resources Project Manager, Environment Agency Southeast.

I have worked for the Environment Agency and one of its predecessor bodies since 1994 in roles that have encompassed demand management, water efficiency, water resources planning, regional strategic planning, the water resources in the south east project, drought management (2004-06 and 2011-12) and the 2009 and 2014 Periodic Reviews. I was an expert witness at the Public Inquiry into SE Water's Water Resources Management Plan in 2010.

In my current role I am the Project Executive of the Environment Agency's input to the Periodic Review in the Southeast and have attended a number of CCGs as Jim Barker's deputy.

Tim Hutchings - former Chief Executive of the Hertfordshire Chamber of Commerce & Industry

I spent 18 years as the Chief Executive of the Hertfordshire Chamber of Commerce & Industry supporting businesses ranging from the smallest start-up to numerous well known multi-national companies across a wide range of sectors. During my time at the Chamber I developed knowledge and expertise in a variety of areas including sustainable economic development, education, the public sector and business development. Whilst in this role I also represented business interests on the Employers Education Taskforce, the Tomlinson enquiry and the Higher Education Funding Council's Business and Enterprise panel. I continue to sit on the Board of Young Chamber UK which was set up to promote Education Business Links.

Whilst playing a leading role in the Chamber movement I also developed an interest in International Trade travelling to many parts of Europe, Dubai and China to foster relations and promote trade links with the UK.

I currently act as a Business Consultant and Executive Coach and have a particular interest in organisational, people and team development. I am a Visiting Lecturer at the Hertfordshire International College and The University of Hertfordshire where I lecture on Enterprise Development and Business Operations. I also sit on the Hertfordshire Business School Advisory Board. I am also an elected member on the Borough of Broxbourne Council, a member of the Lee Valley Park Regional Authority, a School Governor and am currently seeking election to the Hertfordshire County Council.

I am a graduate of the University of Hertfordshire where I obtained a First Class BA (Hons) Degree and am currently studying for a Post Graduate Certificate in Higher Education.

Allan Johnson - Tendring District Council

I work within Food and Health and Safety at Harlow District Council.

I worked for 3.5 years at the Health Protection Agency's Food, Water and Environmental Laboratory Service in Colindale. I previously worked for Tendring District Council and had additional responsibility for Port Health and Private Water Supplies.

I am involved with the European Shippers programme and speak at international seminars on water safety.

Mark Kibble - Dacorum Council

I am the team leader responsible for repairs at Dacorum Borough Council.

Dacorum is a major user of water and having the chance to work with Affinity Water in future changes assists us to plan our future strategy.

This has also provided me with the opportunity to understand the process of delivering value for money water and the problems Affinity Water incur in delivering this service.

Lucy Lee - Manager WWF - UK's UK Rivers Programme

Lucy joined WWF- UK in November 2012 and is currently responsible for managing the organisations UK Rivers Programme. The programme works to inform the development of the UK's water policy and water resources management processes to ensure they achieve the most positive outcomes for the freshwater environment. Lucy was previously employed for 6 years as a senior consultant at TRL specialising in sustainable transport and climate change adaptation and mitigation.

Lucy's role on the Affinity Water CCG is to represent the views of the Blueprint for Water NGO Coalition (<http://www.wcl.org.uk/blueprintforwater.asp>), to ensure that the environment is considered in the group's decision making and that communication with customers reflects environmental concerns effectively.

Hazel Smith, UK Environment Manager, GlaxoSmithKline R&D

I am the UK Environment Manager for GlaxoSmithKline Research and Development based at a site in Stevenage. I work towards the achievement of our EHS target of zero harm to both our people and the environment. This involves acting as an internal consultant to ensure we are striving for best practice in our activities, ensuring compliance as a minimum and auditing to drive continual improvement.

I have worked in the Environmental management field for over 20 years, the last ten with GSK. Previously I have worked for a range of industries from construction materials to cosmetics.

I am also a resident in the Affinity Water catchment area.

I sit on the CCG with two hats, one representing a significant business water user and as a direct customer of Affinity Water.

Jill Thomas - Consumer Council for Water

Local Consumer Advocate, Consumer Council for Water (appointed 2005) representing water consumers in London and the South East.

My fifteen years as a researcher/policy maker on *Which?* magazine starting in 1976 set me on a career path which has mostly involved representing consumers and local residents. Even in those days I had an interest in water and I was the *Which?* spokesperson on water efficiency in the dry years of the 1980s. In 2005, I was appointed as a member of the South East committee of the Consumer Council for Water. In this role I work on behalf of consumers with all the water and sewerage companies in the region and I was closely involved with the last price review.

My first degree in Geography-with-Geology helps with the environmental and water resources issues that Affinity Water faces; my *Which?* Training gave me skills in communication and customer research. I have lived and worked in London and the South East all my life and I am therefore familiar with the communities that Affinity Water serves not only in and around London but also its outlying Dour region in East Kent where I have been the secretary of a river management group since 2001.

I am a member of the Environment Agency's liaison panels for both the Thames and the Southern River Basin Districts and have a good understanding of how Affinity Water customers will both benefit from and be impacted by the requirements of the Water Framework Directive. As the lead member for Affinity Water within the Consumer Council for Water, I take a strong interest in the how the company deals with its customers on a day-to-day basis and also its water resources and business planning.

Mark Tomkins - Water & Environment Manager, Heathrow Airport

I am the Water and Environment Manager at Heathrow Airport, part of a wider Environmental Management team working to minimise the environmental impact of airport operations. My role has a particular focus on water management including water use efficiency and conservation, water quality and flood risk. I have been with the company for 5 years. Previously I worked in other UK companies to implement higher standards of sustainability. Heathrow Airport is Affinity Water's largest customer.

Damian Williams - Tendring District Council

I am the Facilities Manager for Tendring District Council.

I am responsible for facilities provision within the Council which includes ensuring water services within the council buildings are appropriately maintained.

I am also responsible for emergency planning. I look forward to working with Affinity Water to help support the community in extreme weather and any other emergency situation.

Appendix 4

Chronology

Chronology

2012

- 6 July – Ofwat seminar “Putting Customers First” attended by the CCG Chair
- 18 July – First meeting of the Southern CCG Chairs
- 20 July – DWI Chief Inspector’s Report launch in London, attended by the CCG Chair
- 15 August – Induction for CCG members
- 5 September – First CCG meeting
- 10 September – Meeting of the Chair of Consumer Council for Water and the CCG Chair
- 17 September – First stage focus group sessions in Hemel Hempstead, Hertfordshire
- 18 September – First stage focus group sessions in Staines, Surrey
- 19 September - First stage focus group sessions in Luton, Bedfordshire
- 19 September – Second meeting of the Southern CCG Chairs
- 20 September – First stage focus group sessions in Folkestone, Kent
- 24 September – First stage focus group sessions in Clacton-on-Sea, Essex
- 30 October – CCG Chair attended the Affinity Water Board meeting to brief the independent and shareholder non-executives
- 5 November – Ofwat seminar on re-thinking leakage attended by the CCG Chair
- 6 November – Third meeting of the Southern CCG Chairs
- 14 November – Second stage focus group for SMEs, Harlow, Essex
- 15 November – Second stage focus group meeting in St Albans, Hertfordshire, observed by a CCG member
- 17 November – Second stage focus group meeting in Luton, Bedfordshire, observed by a CCG member
- 19 November – Environmental Workshop, Hatfield, Hertfordshire; a CCG member participated as the representative from CCWater
- 21 November – Second CCG meeting
- 22 November – Second stage focus group meeting in Clacton-on-Sea, Essex, observed by the CCG Chair
- 26 November – Second stage focus group meeting in Stevenage, Hertfordshire
- 27 November – Second stage focus group meeting in Dover, Kent
- 29 November – Second stage focus group meeting in Uxbridge, London Borough of Hillingdon, observed by a CCG member

4 December – Second stage focus group meeting in Great Missenden, Buckinghamshire

6 December – Second stage focus group meeting in Woking, Surrey

11 December – Ofwat meeting on previewing the price setting process attended by the CCG Chair

2013

16 January – Validation workshop to review and check Dialogue by Design's reports from the focus groups, attended by CCG members

23 January – Third CCG meeting

19 February – Fourth meeting of the Southern CCG Chairs

26 February – Second Environmental Forum in Hatfield, Hertfordshire

6 March – Ofwat workshop on PR14 attended by the CCG Chair

13 March – Fourth CCG meeting

1 April – Dr Phil Nolan appointed Executive Chairman of Affinity Water Ltd.

20 April – First pair of precursor focus group sessions on "Willingness to Pay" in Hatfield, Hertfordshire, observed by the CCG Chair and a CCG member

23 April – Second pair of precursor focus group sessions on "Willingness to Pay" in Harwich, Essex

24 April – Third pair of precursor focus group sessions on "Willingness to Pay" in Dover, Kent

29 April – Fifth meeting of the Southern CCG Chairs

9 May – CCG Chair observed part of a meeting of Affinity Water's PR14 Project Board

13 May – Ofwat workshop on business planning attended by the CCG Chair

13 and 14 May – ICS Consulting conduct two pilots at Harwich (Essex) and Clacton-on-Sea (Essex) with 25 customers to test the survey questionnaires for willingness to pay and water resources

20 May – Sixth meeting of the Southern CCG Chairs

21 May – CCG Chair attended the Affinity Water Board meeting to brief the Board on the CCG's work and plans

22 May – Fifth CCG meeting

19 June – Water UK Future Forum on "Active customer engagement," attended by CCG Chair

27 and 28 June – ICS Consulting conducted two pilot tests in Folkestone (Kent) and Clacton-on-Sea (Essex) with five domestic customers and five business customers to test the acceptability survey

2 July – Meeting of Ofwat's Delivery Director and the CCG Chair

6 July – Affinity Water "Deliberative Forum" in Clacton-on-Sea, Essex

9 July – Ofwat meeting of CCG Chairs attended by the CCG Chair

10 July – meeting between Affinity Water Executive Chairman and CCG Chair

13 July – Affinity Water “Deliberative Forum” in Harrow, London, observed by the CCG Chair

15 July – Seventh meeting of the Southern CCG Chairs

17 July – DWI Chief Inspector’s Report launch in Birmingham, attended by the CCG Chair

19 July – DWI Chief Inspector’s Report launch in London, attended by the both CCWater representatives on the CCG

19 July – Affinity Water Environmental Forum in Hatfield, Hertfordshire

20 July – Affinity Water “Deliberative Forum” in Dover, Kent

22 July – Affinity Water Environmental Forum in Folkestone, Kent, observed by the CCG Chair and two CCG members

24 July – Sixth CCG meeting

27 July – Affinity Water “Deliberative Forum” in Bishop’s Stortford, Hertfordshire

8 August – Ofwat workshop for CCG Chairs, attended by the CCG Chair

13 August – Eighth meeting of the Southern CCG Chairs

5 September – CCG Chair meeting with Ofwat’s new Portfolio Lead and Portfolio Manager responsible for Affinity Water

9 September – Ofwat meeting for CCG Chairs

17 September – Ninth meeting of the Southern CCG Chairs

18 September – Seventh CCG meeting, when the Affinity Water Executive Chairman and two non-executive Board members attended the morning session

7 October – First deliberative forum on metering in Harlow, Essex, observed by the CCG Chair and by a CCG member

9 October – First vulnerable group workshop (long term unemployed) in Folkestone, Kent, observed by the CCG Chair

9 October – Second vulnerable group workshop (low income families) in Folkestone, Kent

11 October – Third vulnerable group workshop (urban state pensioners) in Watford, Hertfordshire

11 October – Ninth meeting of the Southern CCG Chairs

14 October – Fourth vulnerable group workshop (rural state pensioners) in Clacton-on-Sea, Essex

14 October – Second deliberative forum on metering, in Rickmansworth, Hertfordshire

15 October – Fifth vulnerable group workshop (people with disabilities) in Woking, Surrey

15 October – Sixth vulnerable group workshop (ethnic minorities) in Wembley, London Borough of Brent

23 October – CCG Chair gave the Affinity Water Board meeting a presentation on the CCG Report, highlighting key issues

4 November – Eighth CCG meeting

18 November – Ninth CCG meeting

20 November – CCG Chair presented final report at the Affinity Water Board meeting

Appendix 5

Agendas and Minutes of Meetings

Meeting 1	5 September 2012
Meeting 2	21 November 2012
Meeting 3	23 January 2013
Meeting 4	13 March 2013
Meeting 5	22 May 2013
Meeting 6	24 July 2013
Meeting 7	18 September 2013
Meeting 8	4 November 2013
Meeting 9	18 November 2013

Agenda

Veolia Water Customer Challenge Group

Date: 5 September 2012
Location: Hub, Tamblin Way, Hatfield, AL10 9EZ
Meeting Room: Board Room, first floor

Timing	Content	Presenter
9:30 – 10:00	Arrive and coffee (coffee will be available throughout the morning)	
10:00	Introductions, apologies Health and safety Updates from August	Robin Dahlberg
10:15	Regulator presentations DWI EA CCWater	Milo Purcell Jim Barker Karen Gibbs
11:30	Introduction to Debt	Nick Carney
12:30	Lunch in the Winter Garden	
13:15	Lessons learned from PR09 Approach to consultation for PR14 Pre-consultation on dWRMP	Tim Monod Liz Allen Mike Pocock
14:30	Introduction to web area	
15:00	Round up of day Ways of working - challenges	Robin Dahlberg
15:30	Finish	

Customer Challenge Group

Purpose of Meeting: Customer Challenge Group planned meeting Number 1 Location: Hub Date of Meeting: 5 September 2012 Present: Chair Robin Dahlberg Jim Barker, Environment Agency Kirstie Berridge, Charis Grants (Deputy for Allyson Broadhurst) Karen Gibbs, CCWater Allan Johnson, Tendring Council Mark Kibble, Dacorum Council Milo Purcell, DWI (Deputy for Jacky Atkinson) Hazel Smith, GlaxoSmithKline Jill Thomas, CCWater Mark Tomkins, Heathrow Airport Ltd		
Observers		Presenters Nick Carney, VWC Tim Monod, VWC Mike Pocock, VWC Liz Allen, VWC
Apologies:	Jacky Atkinson (Milo Purcell to attend) Allyson Broadhurst (Kirstie Berridge to attend) Tim Hutchings, HCCI	
Distribution:	As above and web site	
Originator:	Liz Allen	

No	Notes of Meeting	Action
1	<p>Introductions and purpose.</p> <p>New members, who were deputising for the primary contact from DWI and Charis Grants were welcomed.</p> <p>The Chair explained that the meeting aimed to cover 3 core areas:</p> <ol style="list-style-type: none"> 1 role of the regulators and their expectations from the PR14 process and the CCG 2 introduction to debt – as a subject for discussion and as a means for developing a challenge process 3 review of findings from the last price review, lessons learned by VWC and how these are being addressed in PR14. 	
2	<p>Regulator Presentations</p> <p>While they are not a regulator, CCWater were also invited to present to better inform the CCG.</p> <p>1 CCWater</p> <p>2.1 A presentation was made by Karen Gibbs, Policy Manager London and South East, highlighting key purpose of CCWater as a customer representation organisation who will act on behalf of customers as needed.</p> <ul style="list-style-type: none"> • Expectations of PR14 include: <ul style="list-style-type: none"> • The final bills should be acceptable to customers as shown through assessment of satisfaction • There is buy-in for long term investments which will improve services • Plans reflect evidence output from consultation • Good practice in engagement and consultation can be demonstrated • Trade off's, compromises are part of the discussions • Expectations of the CCG <ul style="list-style-type: none"> • Challenge company constructively • Provide additional information and support from other research. <p>In the discussions, the followed points were made:</p> <ul style="list-style-type: none"> • The number of formal complaints received by CCWater is relatively small as each 	

Customer Challenge Group

	<p>company has a robust process for managing issues and CCWater will direct customers back to the company if they have not been through the full internal complaints process.</p> <ul style="list-style-type: none"> • CCWater also provide information and advice to customers on a broad range of issues • Veolia have good processes in place to follow up customer issues and to address root causes. 	
2.2	<p>2 DWI</p> <p>A presentation was made by Milo Purcell, Deputy Chief Inspector, covering a comprehensive range of issues including role of DWI, issues for PR14 and the role of the CCG.</p> <p>The Chief Inspector of the DWI is separately appointed by the Secretary of State and has powers to prosecute water companies for breaches of regulations. The team of inspectors work with the companies to ensure adequacy of controls and completeness of any investigations. The two core objectives are to protect public health and to maintain public confidence in water quality.</p> <ul style="list-style-type: none"> • Expectations of PR14 <ul style="list-style-type: none"> • Use of risk based approach to assesses and manage the adequacy of the existing treatment and identify what additional investment is required • Addressing specific pesticide issues and evaluating the success of different approaches – ie catchment management • Adequate investment in maintenance of asset to maintain compliance • Company demonstrates a rounded use of indicative data, not just water quality, to prioritise future investment • Expectations of the CCG <ul style="list-style-type: none"> • Ensure that adequate assurance of process is provided • Define the scope and content of the report at early stages so that the right information and assurances can be provided • Align effort and topics to the regulatory timetable. 	
2.3	<p>2 Environment Agency.</p> <p>A presentation was given by Jim Barker, Water Planning Manager, on the role of the EA with particular reference to regulation of water.</p> <p>The EA grant licences for abstraction, delivers EU and UK legislation and are the technical adviser to Defra on the statutory Water Resources Management Plans which feed into the company business plans. The aim is to deliver integrated water planning and regulation.</p> <ul style="list-style-type: none"> • Expectation of PR14 <ul style="list-style-type: none"> • Key interest is WRMP and awareness of the challenges from climate change, population growth and uncertainty including management of flooding in catchment and coastal areas and long term resilience • Joint working with the WRSE (Water Resources in South East) to look at innovative and regional action • Delivery of WFD (Water Framework Directive) requirements and promotion of ecological status of water bodies and the 'no deterioration' obligation • Want to see less water abstracted and for companies to come up with innovative solutions (both supply side and demand side) • Burden of proof and development of options shifts towards the water companies and away from the regulator • Expectations of the CCG <ul style="list-style-type: none"> • EA will be holding separate meetings with company and would hope to share outcomes with the CCG • Duty on the company to articulate assumptions which can be scrutinised. 	
3	<p>Debt</p> <p>A presentation on debt in the water industry was made by Nick Carney, Debt Collection Manager.</p>	

Customer Challenge Group

	<ul style="list-style-type: none"> The presentation highlighted the challenges of debt management in the water sector which are different to other utilities. While the value of water bills is only about 30% of amount of the bills from other utilities, the level of debt in the water sector is three times higher. Debt from water is not counted as a priority debt. Customers cannot be disconnected for failing to pay bills. The challenge for the industry is to identify early on when customers are having difficulties and put in interventions to support. These include Water Sure and Water Direct and help for vulnerable customers through the Veolia Trust. The Walker Review in 2009 makes some recommendations for the water sector which are currently under consultation with Defra. An Ofwat report in 2010 highlighted that debt added approximately £15 to every bill across England and Wales. Initiatives taken by the company are aimed at getting customers to get in touch as soon as possible so that appropriate arrangements can be made to manage the debt. Each individual will be treated as a unique case who will require a solution appropriate to their situation. <p>The following discussion raised a number of questions which will be developed into a challenge which will go forward to the company for a response and further discussion at a future CCG meeting.</p> <ul style="list-style-type: none"> Action. The Chair will work with the representatives from CCWater to shape the challenge for the business. <p>Discussion Points included:</p> <ul style="list-style-type: none"> Recognition that the issues of debt are likely to get worse, as a result of changes to the benefits system Transparency of information to customers about the amount of debt and what that means to their bills could be linked to information about how to reduce consumption to 'trade off' potential increases The opportunities to use social tariffs and how they apply and additional impacts on bills Constraints of current regulation where water providers do not have a contract with an individual and cannot seek redress from landlords if tenants default Should debt and social tariffs be discussed together? How do domestic and commercial tariffs account for debt? Does one group of customers subsidise the others? 	RD
4	<p>Lessons learned from PR09</p> <p>A presentation was made by Tim Monod, Veolia Water Company Secretary and Regulations Director.</p> <p>Ofwat use a range of economic comparators to rank the relative performance of water companies. At the last price control, Veolia ranked in the lower half of the industry for many measures.</p> <p>By understanding why and where they performed badly, decisive action is being taken. This includes: improving data sets and understanding how they are used; working more closely with Ofwat to better understand their expectations; showing Ofwat through improved performance that the company is delivering against its regulatory requirements.</p>	
5	<p>Water Resources Management Plan and Water Resources in the South East</p> <p>A presentation was made by Mike Pococok, Physical Asset Strategy Manager.</p> <p>Water Resources Management Plans are statutory reports which address a range of legislation and are submitted to Defra every 5 years. They cover long term water resource planning for a 25 year period.</p> <p>The water companies working in the South East of England have similar issues with water resources and have been working collaboratively to understand potential opportunities for considering water resource planning across the region. Their findings will feed into the options</p>	

Customer Challenge Group

	<p>which will be part of the discussion for the WRMP the outcomes from which will shape a significant part of the Business Plan.</p> <p>The challenges for the company are around meeting increased demand from population growth, with a reduced supply as a result of sustainability reductions and increased uncertainty about winter rainfall.</p> <p>As part of the discussion and consultation on WRMP, the company are seeking to understand customer preferences, now and in the future; differences in wants and needs in different communities; understand the range of the impacts of reductions in abstraction; and weighing up the views of different community and customer groups.</p>	
6	<p>Approaches to Consultation in PR14 A presentation was made by Liz Allen, Stakeholder Engagement Manager</p> <p>The company recognises the importance and value of involving customers and stakeholders in decision making. Ofwat and CCWater have provided some guidance and the business is using external experts to develop the strategy and processes for engagement to ensure the outcomes can be used to help shape the business plan.</p> <p>Planning is important – the questions of why, what and who to engage with, needed to be answered before performing any engagement. The type and level of engagement chosen will be appropriate to the issues under development. In the early stages of the engagement programme work will be focused on gaining information from customers which can be used to help shape more detailed consultation and participation later.</p> <p>The outline programme was shared. The first benchmarking exercises will take place in September. The results of that activity will be used to shape the questions for the next sessions later in the year.</p>	
7	<p>Discussion items and follow up actions</p> <p>Working of the CCG meetings</p> <ul style="list-style-type: none"> • All papers which lead to a discussion at CCG meetings should be available in advance of the meeting • Information papers / presentations should be identified as such and linked to the agenda • Decision papers should be kept short and clearly identify desired outcomes • There needs to be alignment of subjects for the CCG to review with the regulatory timetable <ul style="list-style-type: none"> ◦ Action Chair to meet with company to review regulatory timetable and align subjects to CCG meetings • Assurance – what 3rd party assurance will be available to the CCG <ul style="list-style-type: none"> ◦ Action Liz Allen to inform CCG about use of third parties and their access to the CCG <p>What does success look like for the CCG?</p> <ul style="list-style-type: none"> • Needs to be clarified as this will help structure reports and to identify subjects for challenge. 	<p>RD</p> <p>LA</p>
8	<p>General information The Chair will be meeting with the Chairs of the other CCG's and will be sharing experiences and knowledge.</p> <p>CCG members will be provided with access to a secure section on the Veolia web site. A simplified access route will be provided after brand changes have taken place.</p> <p>A glossary of terms will be made available on the CCG web area.</p>	

Customer Challenge Group

Minutes of 1st CCG meeting held on 5 September

Approved by



Date

21 November 2012

Agenda v2 13 November 2012

Affinity Water Customer Challenge Group

Date: 21 November 2012
 Location: Hub, Tamblin Way, Hatfield, AL10 9EZ
 Meeting Room: Board Room, first floor

Timing	Content	Presenter
9:30 – 10:00	Arrive and coffee	
10:00	<p> Introductions, apologies Housekeeping Approval of minutes from 5 September Chairman's report Objectives for meeting </p> <ul style="list-style-type: none"> Support and challenge the process for engagement on draft Strategic Direction Statement and pre-consultation on draft Water Resources Management Plan <p>The day will be broadly split in two sessions.</p> <ul style="list-style-type: none"> Morning – Review and discuss first phase of research Afternoon – Receive updates and information on subjects which will be under future review by CCG. <p>Updates to challenges</p>	Robin Dahlberg
10:15	<p>Receive a reports on:</p> <ol style="list-style-type: none"> First round of customer consultation in September (circulated in advance) Development of consultation on draft SDS and pre-consultation of the draft Water Resources Management Plan (circulated in advance) 	<p>Liz Allen</p> <p>Mike Pocock/Chris Offer</p>
10:45	CCG discussion and deliberation to challenge and support the process for engagement	Robin Dahlberg
12:30	<p>Lunch</p> <p>Room 1.2 (next door to Board Room)</p>	

13:15	<p>Updates and Information</p> <p>3 Water Resources Management Plan – headline issues (circulated in advance)</p> <p>4 Definitions of Outcomes and means of measurement and implications for reporting (circulated in advance)</p> <p>5 Summary of current Ofwat Consultations and implications for business planning (circulated in advance)</p>	<p>Mike Pocock</p> <p>Martin Hall/Chris Offer</p> <p>Martin Hall/Chris Offer</p>
14.45	<p>Challenge record</p> <p>6 Debt</p>	
15:00	<p>Use of the CCG web Area</p> <p>Profiles</p> <p>Signed confidentiality agreements</p>	
	AOB not advised to Chair	
15:30	Finish	

Customer Challenge Group

Purpose of Meeting:	Customer Challenge Group planned meeting Number 2	
Location:	Hub	
Date of Meeting:	21 November 2012	
Present:	Chair Robin Dahlberg Karen Gibbs, CCWater Hazel Smith, GlaxoSmithKline Jill Thomas, CCWater Tim Hutchings, HCCI	
Observers	Tim Charlesworth AW (part)	Presenters Mike Pocock, AW Martin Hall AW Liz Allen, AW
Apologies:	Jacky Atkinson DWI Jim Barker, EA Allyson Broadhurst, Charis Grants Allan Johnson, Tendring Council Mark Kibble, Dacorum Council Mark Tomkins, Heathrow Airport Ltd	
Distribution:	As above and web site	
Originator:	Liz Allen	

No	Notes of Meeting	Action
	<p>Introductions and apologies.</p> <p>Actions and discussion items from the previous meeting were discussed and the minutes from the meeting 5 September were approved and signed by the Chair. These will be made available on the public web site. A forward plan of future meetings was circulated.</p> <p>Key learning:</p> <ul style="list-style-type: none"> The challenge process. The Chair thanked the members for their help in shaping the challenge. Papers and information prepared by the business. Sufficient information should be provided to promote discussion and ensure no surprises. Defining what success looks like for the CCG. The independent Chairs (from other CCG's) were struggling to find suitable metrics and ways of expressing success. The Chair will continue to be involved in these discussions. Tracking and recording Challenges was a component and the CCG would continue to develop and record activity. This would be reviewed and revisited once further Ofwat guidance was produced. <p>The Chair presented his report on key meetings and actions since September, including feedback from discussions with regulators.</p> <p>Objectives for meeting.</p> <ul style="list-style-type: none"> Support and challenge the process for engagement on draft Strategic Direction Statement and pre-consultation of the draft Water Resources Management Plan. <p>The meeting was to be split into two sessions</p> <ul style="list-style-type: none"> Review and discussion of first phase of research Receive updates and information on subjects which will be under future review by CCG 	

1	<p>Presentations supporting papers previously circulated.</p> <p>1. First round of targeted research.</p> <p>A presentation was made by Liz Allen, Stakeholder Engagement Manager, Affinity Water. The targeted research was one strand of the engagement activity. The outcomes from the first series of focus groups highlighted that customers were generally happy with the service they received. The headline outcomes will be evaluated and tested in further research. The final report was made available to the CCG. There was a discussion reflecting on the outcomes which were not consistent with issues raised by regulators, in particular leakage and environmental concerns.</p> <p>A summary of the next round of qualitative consultation, using the published document 'Investing for your Community', was introduced and headline preliminary early feedback from both focus groups and the web was discussed.</p> <p>The CCG were advised that an on-line panel was to be recruited. This panel would be broadly reflective of the customer base and surveys to 'test' issues in a quantitative manner would be developed from the qualitative work.</p>	
2	<p>2. Development of consultation on draft Strategic Direction Statement (SDS) and pre-consultation draft Water Resources Management Plan (dWRMP).</p> <p>A presentation was made by Mike Pocock, Physical Asset Strategy Manager, Affinity Water. There is no statutory requirement to produce an SDS for this round of business planning; however, Affinity Water wanted to bring together consultation of the future direction of the business with the statutory consultation and the pre-consultation dWRMP. The consultation taking place goes beyond the requirements and seeks to demonstrate Affinity Water's commitment of trying to get closer to communities it serves to understand the range and variety of needs.</p> <p>The published document has been widely circulated and advertised and is available electronically and as paper copies at drop-in events and by the post. The consultation on the expectations is open until the end of December.</p> <p>Discussion points</p> <p>The CCG members raised questions throughout the presentations to seek clarification on issues and to challenge why issues and approaches had been taken.</p> <p>In summary the CCG:</p> <ul style="list-style-type: none"> • Supported the focus on the customer • Recognised the intent was to promote discussion, not to steer the dialogue. <p>In addition they made 4 observations:</p> <ul style="list-style-type: none"> • Affinity should seek to engage with customers who are dependent on a consistent supply of water • Affinity could consider engaging with SME's on outcomes and resilience expectations • Consider the choice and use of language in consultation documents • The CCG welcomed the approach, which goes beyond the minimum statutory consultation <p>Members of the CCG have been invited to attend the focus groups sessions on the consultation during November and December as observers.</p> <p>The January meeting of the CCG will review the outcomes from the second targeted piece of research on dSDS and pre-consultation on dWRMP.</p>	

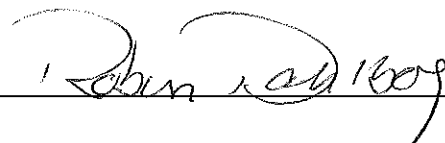
<p>3</p>	<p>Information and Updates</p> <p>3. Water Resources Management Plan (WRMP) A presentation for information was made by Mike Pocock on the timetable and key issues in WRMP.</p> <ul style="list-style-type: none"> • By working with others, as part of the Water Resources in the South East, a broader understanding and modelling of the potential challenges from climate change population growth, pollution etc. can be reviewed and potential cost effective options, including trading options, developed. The outputs from this collaborative work will contribute to the WRMP. • Sustainability reductions will be applied to the Affinity abstractions. The scale of these is under discussion with the Environment Agency. Affinity need to have some certainty around the size of the reduction in order to evaluate the relative costs and benefits of different proposals. • Other issues include leakage, metering and resilience. Companies have driven leakage down to levels set by the regulator. The economic level of leakage is determined calculating the relative cost of mending leaks compared to the benefit of the value of the water saved. Ofwat is proposing alternative mechanisms for calculating leakage whereby each company sets a 'contract' with its customers. <p>The CCG are to develop a Challenge on leakage in order to explore this subject in more detail.</p>	
<p>4</p>	<p>4. Definition of Outcomes and means of measurement and implications for reporting. Paper prepared by Chris Offer, Head of Regulation, questions answered by Martin Hall, Senior Regulatory Economist</p> <p>The summary paper covered the approach Ofwat are proposing for business plans where the focus will be on delivering customer 'outcomes'. The paper was taken as read and questions of clarification were taken. The CCG members were keen to understand how the language of outcomes would be suitably translated into measures and the Statement of Commitments. It was agreed that this subject would be revisited as the options for the business plan evolved.</p>	
<p>5</p>	<p>5. Summary of current Ofwat consultations and implications for business planning. Paper prepared by Chris Offer, Head of Regulation, questions answered by Martin Hall, Senior Regulatory Economist.</p> <p>The summary paper highlight a number of Ofwat consultations including, Ofwat approach to Future Price Limits (FPL), Retail Price Consultation, Wholesale Incentives Consultation and their implications for business planning. The paper was taken as read and points for clarification were addressed. Links to earlier papers were referenced in the document and members were encouraged to see how and where the consultation will impact the planning. This could include a requirement to produce two separate business plans to address the wholesale and retail customer requirements.</p>	
<p>6</p>	<p>Challenge record</p> <p>6 Debt and social tariffs The response to the first challenge record on debt submitted to Affinity Water was discussed. The CCG will re-visit the issue following an evaluation of the current round of consultation.</p> <p>Action</p> <ul style="list-style-type: none"> • Debt will be added to the agenda for the meeting 13 March. <p>Affinity Water tabled a challenge to the CCG to gain their feedback about the value of contributing to some collaborative work with other water companies. The steer provided by the CCG was to see whether the scope of the work could be extended, rather than participating under the scope of the existing proposal.</p> <p>Action</p> <ul style="list-style-type: none"> • Follow up opportunities to extend scope of work before making decision over collaboration. 	<p>LA 03/13</p> <p>LA 11/12</p>

Customer Challenge Group

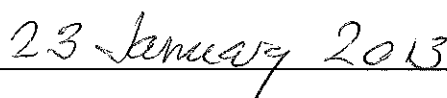
7	<p>AOB</p> <p>CCG members will review the forward plan for future meetings and feedback any comments</p> <p>CCG request an information paper on the Ofwat methodology for PR14 due December 2012 for consideration in January</p> <p>CCG members will be invited to comment on the development of questions to be answered by the on-line panel</p>	<p>All 12/12</p> <p>LA 01/13</p> <p>LA 12/12</p>
8	<p>Future dates</p> <p>The Validation workshop to review the feedback from the focus sessions in November and December consultation will be held in the Hub 16 January. All CCG members will be invited to participate, especially those who have observed the focus groups.</p> <p>Dates of next meetings</p> <p>23 January 2013 13 March 2013 22 May 2-013 24 July 2013 18 September 2013 20 November 2013</p>	<p>LA 1/13</p>

Minutes of 2nd CCG meeting held on 21 November 2012

Approved by



Date



Agenda v1 17 December 2012

Affinity Water Customer Challenge Group

Date: 23rd January 2013
 Location: Hub, Tamblin Way, Hatfield, AL10 9EZ
 Meeting Room: Board Room, first floor

Timing	Content	Presenter
9:30 – 10:00	Arrive and coffee	
10:00	<p> Introductions, apologies Housekeeping Approval of minutes from 21 November 2012 Chairman's report Objectives for meeting </p> <ul style="list-style-type: none"> Support and assure the process and selection of expectations for SDS <p>The day will be broadly split in two sessions.</p> <ul style="list-style-type: none"> Morning – responses from consultation on SDS and pre-consultation of draft Water Resources Management Plan - and how this will be used including introduction to Willingness to pay and the on-line panel. Afternoon – Service Delivery Map (Community Delivery Model) – update and further information including focus group outputs. <p>Evaluation methodology and approach</p> <p>Updates to challenges</p>	
10:15	<p>Receive a reports on:</p> <ol style="list-style-type: none"> 1 Initial review of findings from consultation on SDS. (Paper in advance) 2 Draft report from Dialogue by Design on series of Focus Group sessions. (paper in advance) 3 Draft report on Environmental Focus Group (paper in advance 19 November 2012) <p>CCG discussion and deliberation to challenge and support the process and feedback from:</p> <ul style="list-style-type: none"> Focus groups Contributions from CCG based on their experience Feedback from Validation workshop (16 Jan 2013) 	<p>Chris Offer</p> <p>Robin Dahlberg</p>

11.15	4 Willingness to Pay – The Affinity approach, focusing on two separate but similar issues – the overall bill impact and willingness to pay for different attributes. (paper circulated in advance)	Chris Offer
12.00	5 On-Line panel Background, recruitment and proposed use.(paper circulated in Advance	Liz Allen
12.30	Lunch Room 1.2 (next door to Board Room)	
13:15	Updates and Information 6 Service Delivery Map (Community Delivery Model) Introduction to approach and results of focus group meeting. (paper circulated in advance) 7 The Evaluation process - methodology and timetable (paper circulated in Advance 8 Verbal update on Ofwat consultations	Arnaud David Liz Allen Chris Offer
14.45	Challenge record	
15:00	AOB not advised to Chair	
15:30	Finish	

Customer Challenge Group

Purpose of Meeting:	Customer Challenge Group planned meeting Number 3	
Location:	Hub	
Date of Meeting:	23 January 2013	
Present:	Chair Robin Dahlberg	
	Jacky Atkinson, DWI Jim Barker, EA Allyson Broadhurst, Charis Grants Keith Cane, East Kent Housing Karen Gibbs, CCWater Tim Hutchings Allan Johnson, Tendring Council Hazel Smith, GlaxoSmithKline Jill Thomas, CCWater Mark Tomkins, Heathrow Airport Ltd	
Observers		Presenters Chris Offer, AW Arnaud David, AW Mike Pocock, AW Liz Allen, AW
Apologies:	Mark Kibble, Dacorum Council Lucy Lee, BluePrint for Water	
Distribution:	As above and web site	
Originator:	Liz Allen	

No	Notes of Meeting	Action
	<p>Introductions and apologies</p> <p>Actions and discussion items from the previous meeting were discussed and the minutes from the meeting on 21 November 2012 were approved and signed by the Chair. These will be published on the public web site.</p> <p>The Chair welcomed two new members to the CCG (Keith Cane and Lucy Lee) stating that their additional experience and specialist knowledge would complement the group. Induction sessions to be arranged.</p> <p>The Chair presented his report on key meetings and actions since November including a meeting with other CCG Chairs and Ofwat. Ofwat had asked that the CCG Chairs treat the material provided as confidential until Ofwat had released their methodology for consultation. The Chair said that, of course, he would respect Ofwat's request for confidentiality. The Chair added that he felt it was fair to note that Ofwat clearly expect companies and their CCG's to respond to local conditions and to make assumptions as necessary, in the absence of direction from Ofwat. The Chair reiterated that while Ofwat are not providing direction on the content and the format of reports, the CCG Chairs (in the south east) are sharing ideas and best practice.</p> <p>Objectives for the meeting.</p> <ul style="list-style-type: none"> To discuss the responses from the consultation and focus groups and to gain support from the CCG that the process used to evaluate the outcomes is robust and appropriate. To explain and inform the CCG about the planned approach for developing material 	LA 02/13

	<p>and selecting expert support to carry out willingness to pay research and to define how the CCG can be involved.</p> <ul style="list-style-type: none"> To advise and inform the CCG about the learning from a specific focus group about the use of an emerging approach to test how communities can begin to make choices about their services. <p>Reports, presentations and papers were circulated in advance.</p>	
1	<p>Receive reports on consultation</p> <p>Receive reports and facilitate discussion on findings from SDS consultation;</p> <ul style="list-style-type: none"> agenda paper 1 Initial review of findings from consultation on SDS including focus groups and written responses: agenda paper 2 Affinity Water – Investing in your community, Qualitative Research – Key Findings, Dialogue by Design: and agenda paper 3 Affinity Water Environmental Workshop, Dialogue by Design. <p>Presented by Chris Offer, Head of Regulation.</p> <p>The purpose of the seven week consultation was to gather information from customers about the issues they considered to be important. The following approaches were taken:</p> <ul style="list-style-type: none"> A consultation document was widely advertised, hard copies circulated and promoted on-line with a structured response sheet. A series of targeted focus group sessions were planned by AW and facilitated by an independent expert organisation. A range of open drop-in events were advertised. <p>Affinity Water (AW) received more than 200 written responses to the consultation, and consider this to be a very successful outcome.</p> <p>The focus groups successfully elicited information on a range of subjects from a diverse sample of the community.</p> <p>The drop-in events were not successful either in attracting the general public or as a means of gaining feedback on the consultation document.</p> <p>A review of findings and activities will be included in the evaluation, and the learning will be used to help shape future consultations.</p> <p>CCG members attended 5 of the 10 focus group sessions and attended a validation workshop.</p> <p>CCG members shared their experiences and made the following comments about the process.</p> <ul style="list-style-type: none"> Facilitation - good Venues – OK for focus groups, not all were suitable for drop in events Structure of discussions - good, the facilitators did not lead the attendees and encouraged debate and discussion across a wide range of issues Audience – provided a good cross section sample of communities Key findings by the facilitators – supported by the CCG members <p>The information generated from the focus groups and from the written responses has been reviewed. There was a lot of consistency in the views expressed by attendees, and these views will be subject to a further evaluation.</p>	

Customer Challenge Group

The findings related to the consultation on the draft Strategic Direction Statement were discussed and included the output from the four main questions – summarised below. The output will be used to inform the final SDS.

- Support for the expectations?

These were strongly supported and were considered by most participants to represent the minimum service attributes customers expected from their water service provider.

The majority agreed with expectations but some respondents, in particular those with an environmental interest, felt there should be some explicit mention of protecting the environment and operating in a sustainable manner.

- Should water companies be responsible for supply pipes between meters and homes?

These responses were less clear. This issue will be revisited and further work will need to be carried out.

(Ofwat have asked companies to re-think their approach to leakage and options for ownership of supply pipes is an element; however, there would need to be a change to existing legislation to make this happen.)

- Implementation of social tariff?

No clear response. This issue is to be revisited and further work will need to be carried out. Members of the CCG reiterated that AW should consider a range of interconnected issues and the company's strategies, such as compulsory metering and the potential impact on specific segments of the community.

- Investment for future generations?

The principle was strongly supported as the responsible thing to do. Further work is needed to test the level of investment that is acceptable to customers. This initiated a conversation about customers' awareness of the constraints of the current regulatory investment model.

The feedback from the consultation, both the written responses and the focus group feedback, will be evaluated following a structured process and used to inform the final Strategic Direction Statement for AW to be published in March 2013.

AW will define the customer expectation within the Ofwat reporting framework to deliver defined 'Outcome Measure for Customers'. This process will include the identification of tangible measures against 7 defined criteria using an industry accepted methodology published by UK Water Industry Research (UKWIR).

The CCG concluded that AW should also determine a timeframe for reporting against targets, as part of the CCG's role will be to comment on AW's performance against Ofwat's price determination.

After the presentation and discussion the CCG:

- Had become familiar with the consultation process used
- Understood the high level feedback from customers and accepted the process for gathering and distilling the issues was robust and appropriate
- Understood that AW would use a structured process to further evaluate the findings in

	<p>which will be used to inform the SDS</p> <ul style="list-style-type: none"> Understood and accepted the concept of the 'Outcome Measures Framework' and how this will be used to demonstrate the achievements to AW customers. <p>The discussion ended by agreeing how CCG members can be involved in reviewing material between scheduled meetings. Members agreed to use the web portal to record comments on any documents electronically. This means all members will be able to view colleagues' comments and that there will be an auditable chain of comments to demonstrate involvement and challenge by CCG.</p> <p>ACTION Notification of documents for comments will be emailed to members. This notification will include information about purpose of document and direction as to how members can contribute and the deadline for responses. Members will access the web portal and record their comments.</p>	LA as needed
2	<p>Willingness to pay</p> <p>Receive a paper and lead a discussion to increase understanding of the process to determine Willingness to Pay (agenda paper 4). Presented by Chris Offer, Head of Regulation.</p> <p>Willingness to Pay is a term commonly used to cover a range of activities. For AW this refers to:</p> <ul style="list-style-type: none"> Stated preference research to assign a monetised value to a service or impact etc (used in cost benefit analysis and derived from choice experiments and contingent valuation research) Willingness to pay (used to test bill level and investment options etc.) <p>The stated preference work will seek to place a value on things not commonly given a monetised value. This will ensure that a wider range of costs and benefits can be considered when optimising investment. The methodology used by AW is consistent with published work commissioned from UKWIR.</p> <p>During discussions, the CCG asked AW whether they benchmarked their cost benefit outcomes against those of other water companies. AW advised that there not been any recent benchmarking of values as some companies were seeking to use their CBA as a competitive differentiator.</p> <p>AW will be using a dedicated optimisation package to help prioritise investment choices. The more robust the data used in CBA the greater the confidence AW will have in the output.</p> <p>Further explanations of the methodology used in developing choice experiments and contingent valuation were discussed.</p> <p>The CCG noted how difficult it was to establish a series of choice experiments to make sure that they provide objective and robust results, but they also understood its importance. They wanted assurance that commercial customers would be included in the process. The discussion resulted in the CCG agreeing to issue a Challenge Record on the subject.</p> <p>ACTION RD to draft a Challenge Record to AW on investment options. The response to include how AW will ensure that the 'values' are validated, how the methodology is applied to commercial and domestic customers and that the options considered are realistic.</p> <p>The CCG expressed an interest in being involved in the process to design and review the</p>	RD 03/13

Customer Challenge Group

	<p>development of the choice experiment, as part of the stated preference work.</p> <p>ACTION A timetable for WTP work to be finalised and shared with CCG indicating times and activities where they can be invited to comment.</p> <p>Willingness to pay research will seek to gain an understanding of acceptability of overall bill levels. It was accepted that some elements of the investment plan would be determined by figures provided by Ofwat, and that these would not be available for some time. The CCG advised that AW should be making their own assumptions and not waiting for Ofwat. This was recognised by AW; however, they pointed out that some of the key factors determined by Ofwat will have a significant impact on total bills, and these factors will be as important as anything driven by company choices. A number of scenarios will be reviewed, and the CCG will be invited to comment on the range of assumptions.</p> <p>The CCG were concerned that the range of potential impacts on customer bills were appropriately tested as part of the willingness to pay work and will be raising a Challenge Record on the subject.</p> <p>ACTION RD to draft a Challenge Record to AW on total bill levels and customer willingness to pay in order to assess whether the bill level is justified. The response should provide information on how factors such as debt, avoided cost, efficiencies (especially as a result of the unification) and the 'break point' for acceptability is tested across representative demographic and income groups. AW should also report on the assurance of the process and outcomes and how it has been applied to both domestic and commercial customers.</p> <p>After the presentation and discussion the CCG:</p> <ul style="list-style-type: none"> • Gained an understanding of the difference between willingness to pay in terms of bill level acceptability versus a technique to value non-market benefits of investments that can be used as a key input to cost benefit analysis • Understood the overall timetable for research and that they will be invited to contribute at defined stages. 	<p>CO 03/13</p> <p>RD 03/13</p>
3	<p>Challenge updates</p> <p>A tracking system for all challenges will be shared at the next meeting so that CCG members can make decisions about the status of all challenges.</p> <p>Summary: Challenge ref 0001 raised 13/09/12, subject Debt. Response accepted by Chair 16/11/12. Discussed at meeting 21/11/12 with action to re-visit 13/03/13</p> <p>ACTION – CCG to confirm any specific requirements to be covered in March 2013</p> <p>Challenge ref AW000A raised by AW 21/11/12, subject Collaborative Research. Response given verbally at meeting 21/11/12. Updated response tabled 23/01/13</p> <p>ACTION – CCG to accept or request further information</p> <p>Challenge ref 0002 raised 19/12/12 subject, Leakage. Verbal update provided 23/01/13. Written response on progress for 13/03/13</p>	<p>LA 03/13</p> <p>RD 02/13</p> <p>RD 02/13</p>

Customer Challenge Group

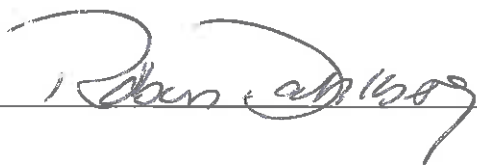
	<p>ACTION – AW to provide response for March CCG</p> <p>Challenge ref 0003 discussed 23/01/13, subject Investment Options. To be presented. Challenge ref 0004 discussed 23/01/13, subject Willingness to pay. To be presented.</p>	<p>MP 03/13</p>
4	<p>Service Delivery Map</p> <p>Discussion and presentation on Service Delivery Map highlighting lessons from focus group meeting (agenda item 6). Presented by Arnaud David, Intervention Manager.</p> <p>The concept of the Service Delivery Map was presented at the induction of the CCG in August 2012. It is both an operational concept, to help AW be more efficient, and a service delivery model to help determine investment for the community.</p> <p>The approach was tested with a local group of customers to understand how their perception of investment options changed when provided with information about relative costs.</p> <p>This first testing of the concept was successful and further testing – to understand perceptions of 'community' will be planned in different size geographical areas.</p> <p>After the presentation and discussion the CCG</p> <ul style="list-style-type: none"> Recognised that the concept was a useful approach to begin to understand community needs Understand that further consultation will take place that will contribute to and challenge our plans 	
5	<p>On-line Panel</p> <p>Receive a paper and discuss the On-Line Panel, focusing on how the panel will be used to support other engagement activity (agenda paper 5). Presented by Liz Allen, Stakeholder Engagement Manager.</p> <p>An on-line panel of customers has been recruited to provide quantitative feedback to complement the qualitative research. A panel provider has recruited a panel which is made up from a population which broadly reflects the social-economic mix of AW's customer base.</p> <p>The responses from the panel will be analysed to identify the statistical significance of the responses. A confidence level of 95% has been chosen.</p> <p>After the presentation and discussion the CCG:</p> <ul style="list-style-type: none"> Understood how the on-line panel will operate and the value and purpose of quantitative surveys Supported the confidence levels for analysed data 	
6	<p>Evaluation Process</p> <p>Receive a paper and discuss The Evaluation Process (agenda paper 7) to provide assurance that a robust process will be used to evaluate all engagement activity. Presented by Liz Allen, Stakeholder Engagement Manager.</p> <p>There are different stands to the engagement work carried out. This includes regular and on-going feedback from customers about day to day activities as well as targeted pieces of research.</p> <p>A consistent approach to evaluation has been deployed in order to allow different data sets to</p>	

Customer Challenge Group

	<p>be compared making allowance for factors such as representativeness and bias.</p> <p>The outputs from the process will help determine where messages from customers are consistent and need to be reflected in investment and whether further action is needed to test or provide further evidence to clarify other issues.</p> <p>After the presentation and discussion the CCG:</p> <ul style="list-style-type: none"> • Recognised and supported the process for evaluating data from different sources. 	
7	<p>Information and updates</p> <ul style="list-style-type: none"> • DWI joint Statement with EA and Natural England on A Catchment Approach was circulated for information. • Forward plan. Updates to the forward plan for CCG meetings were discussed. Additions to the agenda included: <ul style="list-style-type: none"> ○ Discussion on the implications and response to Ofwat consultation on Setting Price Control 2014 (consultation released 28 Jan 2013) to be added to agenda for 13 March ○ Drinking Water Quality proposals and other regulatory driven outputs to be discussed following review with business to be added to agenda for July/September depending on progress ○ WTP timetable and opportunities for CCG involvement. 	
8	<p>Next meeting 13 March 2013</p> <p>Agenda items to include: Progress on consultation on Draft Water Resources Plan The provision of independent assurance to CCG</p> <p>The meeting closed at 15:00hrs</p>	

Minutes of 3rd CCG meeting held on 23 January 2013

Approved by



Date

13 March 2013

Affinity Water Customer Challenge Group

Date: 13 March 2013
 Location: Hub, Tamblin Way, Hatfield, AL10 9EZ
 Meeting Room: Board Room, first floor

Timing	Content	Presenter
9:30 – 10:00	Arrive and coffee	
10:00	<p> Introductions, apologies Housekeeping Approval of minutes from 23 January 2013 Chairman's report Objectives for meeting </p> <ul style="list-style-type: none"> • Support and assure actions and interpretation of findings arising from engagement activity. • Understand and contribute to the process for developing Outcomes measures to support Customer Expectations. <p>The day will be broadly split in two sessions.</p> <p>Morning.</p> <p> Consultation on draft Water resources Management Plan Evaluation of findings from PR14 research and next steps Workshop on development of outcome measures </p> <p>Afternoon</p> <p> Response to Ofwat consultation on Price Setting SDS – progress and timetable Assurance and the role of the reporter </p> <p>Updates to challenges</p> <ul style="list-style-type: none"> • Leakage • Debt 	
10:15	<p>Receive a reports and discuss :</p> <ol style="list-style-type: none"> 1. Consultation on draft water Resources Management Plan 2. Evaluation of findings from engagement activity – to shape future research 	<p>Mike Pocock</p> <p>Liz Allen</p>
11.00	<p>Workshop</p> <ol style="list-style-type: none"> 3. The development of the framework to define outcome measures 	Chris Offer
13.00	<p>Lunch</p> <p>Room 1.3 (next door but one to Board Room)</p>	

13.45	<p>Updates and Information</p> <p>4. Response to Ofwat consultation on Price Setting</p> <p>5. SDS – progress and timetable</p> <p>6. Assurance and the role of the reporter</p>	Chris Offer
14.30	<p>Updates to Challenges</p> <p>7. Debt</p> <p>8. Leakage</p>	<p>Pauline Wilson</p> <p>Mike Pocock</p>
15:00	<p>AOB not advised to Chair</p> <p>Report structure</p>	
15:30	Finish	

Customer Challenge Group

Purpose of Meeting:	Customer Challenge Group planned meeting Number 4	
Location:	Hub	
Date of Meeting:	13 March 2013	
Present:	Chair Robin Dahlberg	
	Jacky Atkinson DWI Jim Barker, EA Karen Gibbs, CCWater Allan Johnson, Tendring Council Mark Kibble, Dacorum Council Lucy Lee, BluePrint for Water Jill Thomas, CCWater	
Observers	Andy McAlinden, AW (part) Tim Monod, AW (part)	Presenters Mike Pocock AW Chris Offer, AW Liz Allen, AW
Apologies:	Allyson Broadhurst, Charis Grants Keith Cane, East Kent Housing Tim Hutchings Hazel Smith, GlaxoSmithKline Mark Tomkins, Heathrow Airport Ltd	
Distribution:	As above and web site	
Originator:	Liz Allen	

No	Notes of Meeting	Action
	<p>Introductions and apologies</p> <p>Actions arising from the previous meeting were discussed and the minutes from the meeting 23 January 2013 were approved and signed by the Chair. These will be published on the public web site.</p> <p>The attendees introduced themselves for the benefit of new members.</p> <p>The Chair presented his report on key meetings and actions since January including a meeting with other CCG chairs and with Ofwat.</p> <p>At the meeting with Ofwat concerns were raised about the timetable and additional requirements for reporting by the CCG. The CCG Chairs stressed the importance of having fixed dates so that they can plan, with their companies, when reports will be written.</p> <p>The Ofwat Consultation document - Setting Price Controls, identified two further reporting requirements from CCG's during 2014. The CCG noted that the limited time between the response from Ofwat, on the notification of the baseline, and a resubmission would make scoping, delivering and reviewing any additional research difficult.</p> <p>Comments were also raised around the assumptions companies would have to make on costs and the impact that has on investment priorities (and customer support) before Ofwat issued their cost assumptions. The CCG suggested that Affinity Water ensure that the cost assumptions they make are 'reasonable' and consistent with their understanding of Ofwat's expectations.</p> <p>The Chair introduced a draft framework and content list for the CCG report to Ofwat. The Chair plans to progressively construct a report in modules and work to the same timetable as the</p>	

Customer Challenge Group

	<p>Company Business Plan submission to Ofwat. The Chair anticipated that the CCG would approve the final report at the planned meeting in November so that it could be available for the Affinity Water Board the same month. This would still allow for minor changes to be made before final submission in either December 2013 or January 2014.</p> <p>Members suggested some additions to the content list including a section on acceptability of the plan. The Chair made it clear that the report would be comprehensive and would include areas where the CCG felt it did not have the competence to comment – such as on the assumptions of interest rates etc.</p> <p>Monthly review meetings have been arranged between the Chair and AW. These will increase in frequency when needed.</p> <p>Objectives for the meeting</p> <ul style="list-style-type: none"> • Review the timetable and process for the development of the Water Resources Management Plan • To understand and support the development of processes to: <ul style="list-style-type: none"> ◦ evaluate and consolidate findings from research ◦ develop Outcome Measures • To receive updates and information about: <ul style="list-style-type: none"> ◦ the company response to the Ofwat consultation, ◦ the progress with the SDS and ◦ Challenges raised. 	
1	<p>Receive a report and discuss the progress on the development of the draft Water Resources Management Plan dWRMP,(agenda paper 1) Mike Pocock, Physical Asset Strategy Manager.</p> <p>The presentation and discussion provided an update to the process, a reminder of the reporting requirements and an explanation of how the feedback from the pre-consultation has been reviewed and reflected in the draft Plan.</p> <p>The requirements for reporting and consultation are published in two core documents: the Water Resource Management Plan Regulations and the Water Resource Planning Guidelines. The Planning Guidelines are jointly published by the Environment Agency, Defra and Ofwat. The WRMP is approved by Defra and funding is secured through the Business Plan approved by Ofwat.</p> <p>The extent of consultation undertaken in the pre-consultation phase was more than required in the regulations. Over 1000 stakeholders were personally contacted and invited to comment. The responses were reviewed and 5 themes emerged from the analysis, these are being carried forward into the draft WRMP.</p> <p>The plan will be submitted 31 March. Subject to security and commercial confidentiality checks the plan will be published to the public in May. Supporting technical reports will be available on request.</p> <p>The consultation will be open for 15 weeks and a response, taking account of the feedback, made to the Secretary of State by the end of October.</p> <p>Questions were raised about targets and the approaches to water efficiency and leakage and whether these were stretching enough. Assurances were provided that both issues will be covered in the plan and all responses will be considered.</p> <p>Further suggestions were made about metering and testing for acceptability of sustainability reductions. It was confirmed that these issues are included in the consultation and will be</p>	

Customer Challenge Group

	<p>considered as part of the wider engagement.</p> <p>After the presentation and discussion the CCG:</p> <ul style="list-style-type: none"> • Understood the sequence of events that are being followed • Supported the approach being taken • Were assured that information and feedback from the pre-consultation was being used to inform the draft plan. 	
2	<p>Change to order of the agenda: item 3 was taken next Workshop on the development of the framework to define outcome measures, Chris Offer, Head of Regulation.</p> <p>The CCG were invited to challenge and comment on the framework and initial suggestions for outcomes and measures of success.</p> <p>The approach adopted by Affinity Water to develop outcome measures is consistent with the best practice principles issued by UKWIR and Frontier Economics. Reference was made to the definitions from Ofwat stating that outcomes are 'the higher level objectives that company actions, activities and achievements are intended to help deliver. They represent what customers and society really value'.</p> <p>The process Ofwat is establishing is to develop a series of incentives and penalties for performance aligned to the customer outcomes. In summary the stages are:</p> <ul style="list-style-type: none"> • Agree customer outcomes with customers • Develop a framework of outcome measures • Set and commit to defined levels of performance • Establish incentives or penalties – based on performance with Ofwat. <p>The CCG were taken through a simple assessment matrix which aimed to evaluate the measures against six criteria. This workshop is one of a number being held across the company to develop the thinking and the approach to developing robust measures of success which will be used to help assess the effectiveness of the Business Plan.</p> <p>Following the session and discussions the CCG:</p> <ul style="list-style-type: none"> • Understood the process and criteria being developed to challenge the appropriateness of different indicators • Offered their comments, provided feedback and identified gaps • Were aware of the difference between outputs and outcomes and the complexity of identifying representative measures. <p>A commitment was made to share further iterations of the outcome measures of success with the CCG.</p>	
3	<p>Agenda item 2 (paper item 2) receive a paper and lead a discussion of the process of evaluating findings from engagement activity and how that will be used to inform the scope and subjects of future research, Liz Allen, Stakeholder Engagement Manager.</p> <p>The presentation and discussion provided an update of findings from the first phase of the engagement programme showing how they were being reviewed in order to provide a consolidated list of issues. The structured approach takes account of findings from targeted research and on-going customer contact. Consideration is given to the level of representation, of the findings, across the whole customer population.</p> <p>The CCG requested a paper at the next meeting showing how the process for consolidation had been applied along with the supporting evaluation that determined the type of action that is</p>	LA 5/13

Customer Challenge Group

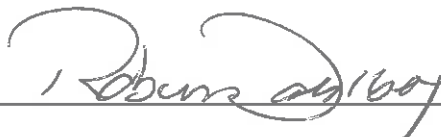
	<p>to be taken for each issue. The CCG want to be assured about the approach and to have the opportunity to identify any gaps or areas of weakness.</p> <p>Following the presentation and discussion the CCG:</p> <ul style="list-style-type: none"> • Understood and supported the process being followed to evaluate and consolidate the findings from the research • Was assured that the process was appropriate for this stage of the engagement programme • Identified further information they wished to see. 	
4	<p>Updates and information Agenda item 4 (paper item 4) receive a paper and lead a discussion on the response to the Ofwat consultation on future price control, Chris Offer, Head of Regulation</p> <p>The presentation provided an overview of the key components of the methodology consultation and highlighted the areas where Affinity Water is in agreement with Ofwat and where there are concerns. The role of the CCG is not directly affected by the consultation, other than the proposed additional reporting in 2014.</p> <p>The formal response from Affinity Water will be broadly supportive of the consultation and will raise some concerns over the need to have more clarity around some of the key financial changes including Ofwat's approach to 'totex', baseline setting, efficiency assessment and associated measures.</p> <p>Following the discussion the CCG:</p> <ul style="list-style-type: none"> • Was aware of the scope of the consultation and the key issues for Affinity Water 	
5	<p>Information and update Strategic Direction Statement (SDS)</p> <p>The consultation on the draft SDS showed that most of the respondents were supportive of the four outcomes as they were presented. There was some feedback, including from special interest groups, questioning whether 'environmental issues' had enough prominence.</p> <p>A question was raised as to whether there had been any specific consultation on broader environmental drivers as part of the activity to date. It was reported that the scope of the consultation so far had been to gather information about all issues that customers felt were important and the responses received indicated that broader environmental issues did not appear to be a priority for them. This issue can be re-visited as part of further research.</p> <p>Much of the feedback, received in written responses, was directly related to levels of abstraction in specific chalk stream habitats.</p> <p>The regulatory framework, under which the company operates, ensures that significant environmental impacts are considered as part of the day to day management of the business. The debate is whether this needs to be made more obvious, by having an additional outcome or whether assurances can be provided by showing how environmental impacts, including management of the water environment can be reflected within the outcome measures.</p> <p>The CCG were advised that the preference for Affinity Water was for four outcome measures with a clear commitment to carry out more work to ensure the wider environmental issues were appropriately reflected.</p> <p>Further work is taking place to clarify this so that clear statements can be included in the SDS.</p> <p>BluePrint for Water will shortly be holding a review of their involvement and finding of the</p>	LL 5/13

Customer Challenge Group

	CCG's. The outcomes will be shared.	
6	Information and update Assurance and the role of the Reporter The CCG were advised that Affinity Water is using an independent Reporter to review and challenge their Water Resource Management Plan and Business Plan. Copies of the Reporters reports to the Affinity Water Board will be made available to the CCG and they will have access to the Reporter as needed.	
7	Updates to Challenges Debt An update to the Debt Challenge was tabled. This provided an update on company awareness of some significant issues facing customers and the business. Affinity Water is still developing its policy on social tariffs and debt and will keep the CCG informed.	
8	Updates to Challenges Leakage A formal update to the challenge on leakage, discussed at the last meeting was not available. Affinity Water apologised and explained resources had been focused on the draft Water Resources Management Plan and an update would be presented at the next meeting.	
9	AOB The Chair extended an invitation to the non-executive Directors of Affinity Water to attend a CCG meeting to discuss: <ul style="list-style-type: none"> • Board level engagement and support of the programme of activity • Non-executives' views on the investment strategy In addition the CCG would like to receive a paper from Affinity Water about the governance of the Business Planning process and the role of the different groups.	LA 5/13

Minutes of 4th CCG meeting held on 13 March 2013

Approved by



Date

22 May 2013

Affinity Water Customer Challenge Group

Date: 22 May 2013
 Location: Hub, Tamblin Way, Hatfield, AL10 9EZ
 Meeting Room: Board Room, first floor

Timing	Content	Presenter
9:30 – 10:00	Arrive and coffee	
10:00	Introductions, apologies Housekeeping Approval of minutes from 13 March 2013 Chairman's report Regulator updates – Jim Barker, EA verbal update Objectives for meeting <ul style="list-style-type: none"> • Close off phase 1 of engagement • Review plans for stage two of engagement programme 	Robin Dahlberg
	1 CCG Report <ul style="list-style-type: none"> • Review, planning and approach <i>Affinity Water staff to leave the meeting for the discussion</i>	
11.00	2 Sign off Engagement phase 1 <ul style="list-style-type: none"> • Summary of action, findings and next steps including OPM report of process and interpretation of findings 	
	3 Plan for phase 2 <ul style="list-style-type: none"> • Process, approach and timetable of activity 	Liz Allen
11.30	4 WTP <ul style="list-style-type: none"> • Summary of timetable and approach to WTP • Introduction to Acceptability Testing 	External Presentation from ICS
12.45	LUNCH	
13.30	5 Governance and decision making, including forward plan and revised timetable.	Tim Monod

14.15	6 Updates <ul style="list-style-type: none"> • Business plan expectations – Pioneer (baseline plan) • Audit activity – outline of actions and stages 	Tim Yearsley
15.00	<ul style="list-style-type: none"> • AOB 	
15:30	Finish	

Customer Challenge Group

Purpose of Meeting: Customer Challenge Group planned meeting Number 5 Location: Hub Date of Meeting: 22 May 2013 Present: Chair Robin Dahlberg Jim Barker, EA Allyson Broadhurst, Charis Grants Karen Gibbs, CCWater Tim Hutchings Lucy Lee, BluePrint for Water Hazel Smith, GlaxoSmithKline Jill Thomas, CCWater Mark Tomkins, Heathrow Airport Ltd	
Observers	Richard Bienfait, CEO, AW (part) <div> Presenters Tim Monod AW Tim Yearsley AW Joseph Sanders, AW David Barlow, AW Liz Allen, AW Lisa Gahan, ICS </div>
Apologies:	Jacky Atkinson DWI Keith Cane, East Kent Housing Mark Kibble, Dacorum Council Allan Johnson, Tendring Council
Distribution:	As above and web site
Originator:	Liz Allen

No	Notes of Meeting	Action
	<p>Introductions and apologies</p> <p>Actions arising from the previous meeting were discussed and the minutes from the meeting 13 March 2013 were approved and signed by the Chair. These will be published on the public web site.</p> <p>The Chair invited statutory members to provide an update of their activity.</p> <p>Jim Barker, Environment Agency explained that draft Water Resource Management Plans (dWRMP) were out for consultation and the EA would be undertaking a strategic review. He said he would make the EA report on AWL available, in confidence, to CCG members.</p> <p>In addition JB passed comments about the way Affinity Water had submitted their dWRMP and expressed some concerns around the delivery of correct information in a timely manner. He said that Affinity Water were the only company to have had difficulty submitting the correct information on time.</p> <p>The Chair commented that he was looking to the EA to comment on the dWRMP and to provide assurance to the other members of the CCG.</p> <p>Karen Gibbs, CCWater reminded the CCG about an information paper that CCWater had produced on engagement and a newly published paper on expectations when testing customer views on acceptability of business plans. The proposals included a number of principles to allow a degree of comparability across companies.</p>	

Customer Challenge Group

	<p>The Chair asked how that would fit with the localism agenda being promoted by Ofwat. KG pointed out that many customers have two service providers (separate water and waste water services) and that a means to provide comparability and assurance on the way prices were determined would be useful.</p> <p>The Chair presented his report on key meetings and actions since March, including recent meetings with other Southern CCG chairs, attending an Ofwat Workshop and meetings with the Affinity Water Board.</p> <p>The Chair reported that the Chief Executive of Ofwat, Regina Finn had resigned but she would remain in post until November. This raised some concerns about potential changes to expectations and delivery dates (latest date for Business Plan submission in 2 December). Following discussions with the other Southern CCG Chairs and AW, it was concluded that it was unlikely that submission dates would change; however, all parties would have to monitor developments and be prepared to act.</p> <p>The Chair attended the AW Board meeting 21 May and informed members about the make up of the Board and their commitment to fulfil their requirements in relation to PR14. Non-Executive and Independent Directors have been invited to attend the CCG meeting on 18 September.</p> <p>In response to the change of submission dates announced by Ofwat, the Chair stated that he would attend the AWL Board in October to provide them with a draft of the CCG report, prior to the final sign off by CCG in November.</p> <p>The newly appointed Chair to the AWL Board, Dr Phil Nolan, will meet with the CCG Chair separately.</p> <p>Objectives for the meeting</p> <ul style="list-style-type: none"> • Close of Phase one of the Engagement Programme • Review plans for Stage two of the Engagement Programme 	
1	<p>CCG report</p> <p>Affinity Water employees were asked to excuse themselves while the CCG members reviewed the drafts of parts of their report on Affinity Water's Business Plan.</p> <p>The CCG Chair provided the minute for this part of the meeting.</p> <p>The Chair noted that the two representatives from CCWater had reviewed all five versions of chapter four, and he thanked them for their contributions.</p> <p>The members decided that "Stages" was not the best name for chapter four. The members agreed to propose alternative titles by Friday 7 June 2013.</p> <p>Action: CCG members to propose alternative titles for chapter four by Friday 7 June 2013.</p> <p>The members decided that when the report includes an opinion or view expressed by the CCG, this should be put in a separate paragraph and highlighted either by italics or bold.</p> <p>Action: CCG Chair to amend the drafts.</p> <p>The members decided that the opinions expressed in the draft of part of chapter four represented the collegiate view of the CCG.</p> <p>The members decided that a précis or abstract should be added to the beginning of each module in the report.</p>	

Customer Challenge Group

	<p>The members decided to add a new section to chapter four on acceptability testing.</p> <p>The CCG reviewed in detail the following paragraphs of chapter four, and agreed amendments: 4.1, 4.5, 4.12, 4.14, 4.15, 4.19, 4.20, 4.38, 4.39, 4.50, 4.58, 4.62, 4.66 and 4.67.</p> <p>Action: CCG Chair to make the necessary amendments.</p> <p>The CCG members challenged the accuracy of paragraph 4.15 in chapter four.</p> <p>Action: Affinity Water to advise under what circumstances do the company refund overpayments. For example, do customers have to ask for a repayment?</p> <p>The CCG considered the diverse styles used in the biographies / autobiographies appendix. The members decided to retain the diversity. Hazel Smith noted that her contribution had not been updated to incorporate the latest material she submitted. The CCG Chair said that members were free to make further amendments, but the version agreed at the September CCG meeting should be the final version.</p> <p>Action: CCG Chair to update Hazel Smith's autobiography.</p> <p>Action: Affinity Water should send CCG members a reminder in August 2013 that they should make any further amendments in good time for the September CCG meeting.</p> <p>The CCG Chair advised that he expected to provide drafts of additional material at all the remaining CCG meetings in 2013. For each paper, the Chair would provide a version control document highlighting the new material.</p>	
2	<p>Agenda item 2 (paper item 2) The completion of phase one of the Engagement Programme, Liz Allen, Stakeholder Engagement Manager.</p> <p>Much of the content of the paper had been discussed during item one and members commented that the findings had not revealed any surprises.</p> <p>CCG</p> <ul style="list-style-type: none"> • Agreed that the activity undertaken in phase one was appropriate to meet the objectives of listening and learning about customer attitudes and opinions • Supported that the summary findings were the most significant issues to be taken forward <p>To provide further assurance CCG members requested a summary for 3 issues to show where issues arose and how these will be taken forward.</p> <p>Action AW to produce a detailed information flow showing how the following issues were identified and validated.</p> <ul style="list-style-type: none"> • Support for metering • Value for money • Abstraction <p>In addition two contextual issues were discussed and members requested addition information on.</p> <ul style="list-style-type: none"> • Comparative increases in water bills over time • Affinity Waters' view of the broader political situation and whether they felt there was any political pressure on bill levels 	LA 7/13

3	<p>Agenda was re-arranged to accommodate an external speaker Agenda Item 4 Background and approach to Willingness to Pay Research, Lisa Gahan, ICS Consulting.</p> <p>The purpose of the presentation was to inform members of the purpose of Willingness to Pay Research, how it was used and applied. A presentation was given showing how a value for services could be assessed in financial terms. This financial value could then be used to provide a measure of 'benefit' within a cost benefit assessment.</p> <p>As part of the context for the WTP work interviewees are asked a number of questions these include:</p> <ul style="list-style-type: none"> • How they feel about the amount paid for the water supply services received from Affinity Water • Commenting on the service areas and on those that need improvement or not • Whether they feel bills should go up, stay the same or go down in the future <p>As part of the choices there is range of questions to capture the range of bill impacts which customers seem to think is appropriate. Sewerage bill charges are introduced – to see whether this influences views on what should be delivered in terms of water service.</p> <p>After questioning about choices, questions are asked about motivations – to give respondents the opportunity to say what they think companies should pay for improvements, whether the company is inefficient, whether they trust the company to deliver the improvements etc.</p> <p>An analysis of customers' views on current services and bill levels will be included in the WTP survey responses. The acceptability testing will be designed to make this explicit and will include the sewerage element.</p> <p>Members raised a number of questions and the answers provided helped to increase understanding. Questions raised included:</p> <p>Q: Customers affected by a single attribute – such as low pressure would place a higher value on improving that service, than someone who had no experience. How was this taken into account to ensure bias was minimised?</p> <p>A: The sample size of the stated preference survey would address this bias. However, if it was found that there was 'over' sampling for any attribute – this could be addressed through weighting results but this would be unlikely.</p> <p>A: ICS set the sample size to be quite large – this should ensure that issues that do occur occasionally in the population are captured. The sample selection is random to avoid bias. ICS generally avoid oversampling customers with known issues on the grounds that their WTP will pull the average up. If we were to find a large portion of the sample experienced issues not experienced in general across the population we could address this bias through weighting. But this is not expected.</p> <p>Q: How big is the sample size? And who is excluded?</p> <p>A: The number of interviews planned will be sufficient to give a statistically robust response. A high level of confidence is required and this will influence the numbers surveyed. Additional, the more analysis performed on the results, ie by region, Socio-Economic Group, age etc, the higher the response rate required. Final numbers are being agreed and these will significantly exceed the minimum.</p> <p>A: All respondents are screened to ensure they meet basic requirements – such as being responsible for paying the Affinity Water bill; no one will be excluded for non payment. (They are not asked whether they have paid their bill.)</p> <p>Q: Do the choices include a reduction in bills – with a potential reduction in service?</p> <p>A: Yes, the blocks of choices will always include the current situation and two alternatives. These are generated at random and will include reductions both in service level and bill.</p>	
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Customer Challenge Group

	<p>Q: How is the total bill tested? A: A separate piece of research is being undertaken to assess total bill acceptability as it is understood that customers will want to trade off different services if they each have an impact on bills.</p> <p>Q: The research is assuming that customers already place a value on the service they are receiving. Customers may be dissatisfied with the service but cannot choose to go somewhere else, how will this WTP make a difference? A: The purpose of WTP research is to gain a monetary 'value' of change in service, not whether the absolute level of service and the bill is worth what is being paid. However we do include questions to find out the customer view on this important issue. The acceptability testing, that considers the whole bill impact, is more closely aligned to answering the type of question raised. The design of the survey questionnaire will include a range of questions on current bill levels and service levels and seeks to understand customer's views of the existing service before considering the impact of future changes. A: In the absence of direct competition, it is the role of Ofwat to ensure that the charges made to customers reflect the cost to deliver those services. If companies are less efficient than the level of performance assumed by Ofwat when it sets prices then it is the company shareholders and not the customers who pay for this inefficiency.</p> <p>Q: Are domestic and commercial customers surveyed with the same information? A: The same choices will be given to commercial and domestic customers, however, some of the language will be changed to ensure it is appropriate for the audience. The surveys are performed separately and the responses aggregated. The numbers of domestic customer surveyed is higher than commercial customers.</p> <p>Q: The illustration provided shows a linear progression for the marginal benefit. Is that realistic? A: There are many interdependencies on each of the attributes and it would not be possible to show and use multiple variables. The survey results are only valid in the range set, so there is a level of the service and price change that is implicit in the estimated WTP and set the boundary for the validity of the numbers used.</p> <p>Q: How are the surveys undertaken? A: A variety of methods are used. Face to face is considered the most robust, but all methods have pros and cons so we are including on-line. The testing and pilot stages identify opportunities to improve the language and the approaches taken so that the issues are explained in clear way enabling respondents to provide valuable responses. Most interviews are carried out in the presence of an interviewer. A: The experts who undertake this work are aware of the challenges, such as people skipping through pages etc and build in checks, such as the amount of time spent on page, to ensure the quality of the data.</p> <p>Affinity Water has chosen to undertake a two stage survey. The scope of stage one will be for the whole of the business plan and will be aligned with the Customer Outcomes. The stage two work will focus on Water Resources.</p> <p>The draft surveys are under construction and are open for review until 24 June. CCG members will be given the opportunity to see and test the questions.</p>	
4	<p>Agenda Item 5 (paper item 5) Business Plan Governance, Tim Monod, Director of Legal and Regulation Richard Bienfait, CEO Affinity Water joined for the presentation</p> <p>The presentation started with a reminder of the changes in ownership of the business and the impact that is having, and will continue to have on the governance arrangements.</p>	

Customer Challenge Group

	<p>The role of the Board, in relation to its responsibilities for PR14, was discussed and it was noted that a significant proportion of Board time was being spent on the subject.</p> <p>Members raised some questions about the defined roles and membership of the Board, including their involvement with customer issues and terms of office. The members were assured that the Independent Directors took an active interest in customer issues including challenging the business on SIM scores. The existing Independent Directors had a wealth of water industry experience, having held board positions under the previous ownership. The Board worked within the guidance of best practice for membership, terms of office etc. and these would be considered as part of the general review of corporate governance.</p> <p>A revised timetable of activity for the Board, in relation to PR14 was shared. This reflected the change in submission date.</p> <p>The Board have recently reviewed the proposed structure for the business plan and this will be shared with the CCG in July.</p> <p>While the CEO was present members used the opportunity to ask some questions. These included:</p> <p>Q: Is Affinity Water expecting to standardised ways of working and produce a business plan covering all three regions?</p> <p>A: Standardisation will be progressively introduced where it is appropriate – such as IT systems, consistent processes etc. Operationally, each region has different characteristics and challenges and there is no intention to loose the benefits of local skills and knowledge. As far as possible the business plan development process will be standardised to deliver priorities which will be tailored to respond to the local needs.</p> <p>Q: When committing to four outcome measures how will Affinity Water demonstrate that environmental concerns are appropriately reflected?</p> <p>A: The Outcome Measure Framework is still under consultation and development. Once the metrics and measures have been defined, they will be shared with the CCG. This should provide assurance of the importance of environmental measures. The performance levels will also be identified with an indication of where each measure will contribute to either a financial or reputational driver.</p> <p>Members asked to see the outcome measures framework and the supporting metrics and performance measures.</p>	CO 7/13
5	<p>Agenda Item 6 Updates. Capital Investment Portfolio Optimiser, Tim Yearsley, Asset Delivery Manager, Joe Sanders, senior Asset Engineer, David Barlow, Head of Asset Delivery</p> <p>The presentation explained how the use of dedicated software will help to optimise capital investment in physical assets. Asset and maintenance costs will be balanced with the preferred service levels for customers in order to identify the investment options that deliver best value.</p> <p>The tool will be run periodically to re-optimize investment in light of changes in performance or need and incorporate revised customer preferences.</p> <p>The first output is due shortly and will provide the baseline for the business plan. Customer views from Willingness To Pay studies will then be applied to demonstrate the impact of customer preferred service levels.</p>	
6	<p>Agenda was re-arranged to accommodate an external speaker</p> <p>Agenda Item 4 part 2 Acceptability Testing, Lisa Gahan, ICS Consulting.</p>	

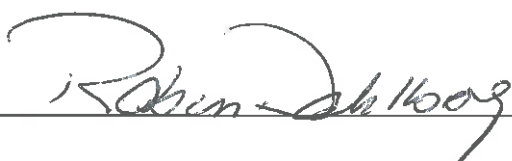
Customer Challenge Group

	<p>Customer Acceptability Research complements Willingness to Pay (WTP) and Cost Benefit Assessment activity. WTP research allows for a value to be determined for a service or a change in service, which are then proposed within a plan(s). Customer Acceptability is assessing the plan(s) to determine which is most acceptable. This means wider influences on bills such as customer affordability and mandatory investment can be considered.</p> <p>The options include testing acceptability for a preferred plan or testing a number of plans. Affinity Water have not finalised the approach they will be taking.</p> <p>The methodology ensures a robust statistically significant sample of customers is questioned in order to provide evidence of acceptability.</p> <p>Q: How will any efficiencies gains (from unification) or previous inefficiencies etc be managed so that customers are not paying for past poor decisions? A: Customers in the current regulatory period are not paying for inefficiencies. Ofwat assume a level of efficiency for all companies. Any divergence, from that level of efficiency, results in a cost carried by the shareholder.</p> <p>Q: When will a preferred plan be available for consultation? A: Consultation on a preferred plan will run in parallel with the Willingness to Pay work. The two pieces of work do not have to be sequential.</p> <p>ACTION The CCG would like to see a timetable of the different activities which ICS are carrying out identifying when and where they may be able to comment.</p>	CO 6/13
7	<p>Agenda was rearranged. Agenda Item 3 Plan for Phase 2, Process and timetable overview, Liz Allen, Stakeholder Engagement Manager.</p> <p>The phase two programme for engagement 'Testing and Valuing' was shared with the members. This showed how action was planned to build on the findings from Phase One. Members were reminded of the process followed. A summary of the objectives, success factors, including proposed indicators, were shared.</p> <p>Members were advised that Affinity Water proposed segmenting stakeholders into three tiers and that they were developing a range of activities for each tier in order to show that 'sufficient engagement' was planned.</p> <p>A timetable of activity was shared and members will be advised of dates and locations for events so that they can observe or attend.</p> <p>The CCG</p> <ul style="list-style-type: none"> • Supported the approach • Were provided with information about the outline programme and content, showing how gaps, identified in phase one, were to be addressed • Confirmed that they would like to be involved throughout the campaign 	
8	<p>Agenda item 6 Audit activity The item will be carried over until the next meeting when AWL will be sharing the approach and timetable to auditing.</p>	
9	<p>AOB Discussions about additional meetings either in person or by telephone conference in October were discussed. It was suggested that one of the meeting dates booked with the Chair might be suitable. Dates to be confirmed once AWL confirmed the date for the completion of the second version of the</p>	

Customer Challenge Group

	Business Plan.	
	The meeting closed at 16:00hrs	

Minutes of 5th CCG meeting held on 22 May 2013

Approved by 

Date 24 July 2013

Affinity Water Customer Challenge Group

Date: 24 July 2013
 Location: Hub, Tamblin Way, Hatfield, AL10 9EZ
 Meeting Room: Board Room, first floor

Timing	Content	Presenter
9:30 – 10:00	Arrive and coffee	
10:00	Introductions, apologies Housekeeping Approval of minutes from 22 May 2013 Chairman's report Regulator updates Objectives for meeting <ul style="list-style-type: none"> • Build understanding of the components of business plan • Confirm and close off the processes that will be used to deliver the outcomes under each of the challenge records. 	
10.30	CCG report planning time and discussion	
11.00	Components of the business plan <ul style="list-style-type: none"> • Description of each element • Contribution to the final business plan • Assurance Consultation version of plan <ul style="list-style-type: none"> • Update on action • Comments on style, language and format 	Chris Offer
	Information paper to be circulated in advance on Quality programme. A member of the Affinity Water Quality team will be available to respond to issues raised as needed.	
12.45	LUNCH	
13:30	Challenge updates <ul style="list-style-type: none"> • Social Tariff • Leakage • Willingness to Pay and Bill Acceptability 	Vince Muldoon Tbc Chris Offer
15.00	AOB	
16:00	Finish	

Customer Challenge Group

Purpose of Meeting:	Customer Challenge Group planned meeting Number 6		
Location:	Hub		
Date of Meeting:	24 July 2013		
Present:	Chair Robin Dahlberg		
	Jacky Atkinson DWI Keith Cane, East Kent Housing (until 12:45) Karen Gibbs, CCWater David Howarth, EA Tim Hutchings Mark Kibble, Dacorum Council Jill Thomas, CCWater		
Observers		Presenters Chris Offer Patrick Campbell	
Apologies:	Jim Barker, EA Allyson Broadhurst, Charis Grants Allan Johnson, Tendring Council Lucy Lee, BluePrint for Water Hazel Smith, GlaxoSmithKline Mark Tomkins, Heathrow Airport Ltd		
Distribution:	As above and web site		
Originator:	Liz Allen		

No	Notes of Meeting	Action
	<p>Introductions and apologies</p> <p>Actions arising from the previous meeting were discussed and the minutes from the meeting 22 May 2013 were approved and signed by the Chair. These will be published on the public web site.</p> <p>Actions arising from the minutes were all completed or were to be addressed in the meeting.</p> <p>In his report the Chair highlighted a meeting with the recently appointed Chair of Affinity Water Limited (AWL), Dr Phil Nolan. They discussed the role of the CCG and the relationship with the Board. The AWL Chair was open to suggestions from the CCG about improving customer satisfaction. The CCG Chair said the Board needed to ensure that the future plans provided a balance between customers and shareholders. Dr Nolan and two other non-executive directors are planning to attend a future CCG meeting.</p> <p>A detailed timetable of Business Plan iterations is to be agreed with the company to ensure the CCG have sufficient time and information to allow them to complete their report.</p> <p>The Chair repeated the advice and direction from Ofwat that the CCG are not expected to review the detailed financing models in the business plan. However, should the CCG have concerns in these areas, they should direct Ofwat toward areas of concern.</p>	
1	<p>Minute of CCG review of draft report</p> <p>Affinity Water employees excused themselves from the meeting during the CCG's review of the latest drafts of their report to Ofwat. The Chair drafted this part of the minute.</p> <p>The following amendments were agreed.</p>	

	<p>Throughout – correct misspelling of "Foreword"</p> <p>Foreword</p> <p>Add material on ToR</p> <p>Under "Governance arrangements," second paragraph, add sentence that the administrative arrangements did not compromise our independence.</p> <p>Under "Preparation of our report," add sentence that Affinity Water employees were absent when the CCG reviewed drafts; add sentence on version control.</p> <p>Executive Summary</p> <p>Add sections of achievement of regulatory objectives for DWI and EA</p> <p>Add section on Affinity Water's overriding aim</p> <p>Add section on the impact of the acquisition and the merger</p> <p>Under "Financial assumption" add gearing changed from 45% to 77%</p> <p>Affinity Water's engagement with its customers</p> <p>Add section on CCG's assessments</p> <p>Stages</p> <p>Change title to "Narrative"</p> <p>CCG agreed the amendments as drafted</p> <p>In para 3.95, Chair to ask Affinity Water to email statement advising which comments were incorporated into the final version; Chair to add to this information.</p> <p>Themes</p> <p>Change title to "Challenge Records and Affinity Water's Responses"</p> <p>Chair to create a new Challenge on metering, which will be sent for review by Karen Gibbs and Jill Thomas (both of CCWater); Affinity Water will be asked to reply in time for the September CCG meeting.</p>	
2	<p>Agenda Item 2 The Components of the Business Plan, Chris Offer, Head of Regulation</p> <p>A presentation covering the core components of the business plan, their contribution to the business plan and a summary of the investment proposals was given.</p> <p>This was followed by a review of the current consultation including the testing of outcome measures, language and style of the report in preparation for the production of the final business plan in December.</p> <p>The CCG</p> <ul style="list-style-type: none"> • Gained an understanding of the key components of the proposed plan and the relative contributions to the overall plan • Were provided with a summary of the assurance process which was in place for each of the components and for the balancing of the whole business plan • Were updated on the business plan consultation activity • Reviewed the approach to and definitions of the outcome measures and the structure of the final submission <p>Discussion points were raised throughout the presentations and the key points are noted below.</p> <p>The Business plan is made up from 10 core components. The finance element has a number of significant sub components. These were described and an assessment of the relative contribution, the degree of discretion that AW can apply to reflect customer feedback and the relative impact on the final bill was discussed. It was pointed out that the findings from the engagement activity will be particularly relevant to a number of components of the business</p>	

plan including capital maintenance and water resource management planning. On this basis engagement was not assessed as being a key contribution to the investment plan. It was noted that this distinction was important for presentational reasons.

Points were raised about Opex efficiency and how this was assessed. The current approach, as used by Ofwat, establishes a year on year operational efficiency target. These assumptions were used going forward and CO explained that the business plan consultation includes an on-going efficiency target of around 1.5% per year. The change in Ofwat accounting to using Totex may change this for PR14, and it is expected that the final price setting methodology will help clarify this

Capital maintenance accounts for around c60% of the total investment plan. The prioritisation of programmes will be influenced through the use of optimisation, which makes use of the cost benefit assessments which in turn have been developed from the findings of the willingness research. Points were raised about the basis of the assessment for capital maintenance and the impact on customer bills. CO explained that, in general terms, capital investment expenditure is paid for over the life of the constructed asset (through depreciation charges). This means that the impact on bills, for a single year or even a five-year period, is less than might be expected given the level of investment proposed. CO explained that in comparison to capital expenditure, operating expenditure has a high impact on customer bills. This expenditure is met by customer bills in the year in which it spent. This was shown in the business plan component assessment.

A request was made to have a clearer view of the capital maintenance programme. It was explained that AW would need to consider how best to provide this as this was dependent on the level of detail sought.

A summary assurance map was shared identifying that work packages were being peer reviewed and externally validated as necessary. Third party assurance was being supplied by a number of agencies covering specific technical aspects.

At the CCG Chairman's request the external process auditors, Atkins will provide a report for the CCG. The scope will be confirmed and is likely to include:

- Assurance that the process used to compile the business plan was sound and that the contributing information has been used appropriately – this will be consistent with any report produced for the AWL Board
- Appropriate use of customer and stakeholder responses from engagement activities and how this has affected choices
- Changes to the final business plan after the CCG have completed their report

Investment proposals

Capital maintenance and water-resource planning are the major contributors to the capital programme – 60% and 25% respectively. Levels of service associated with these activities are being tested as part of the outcomes/expectations 'having enough water' and 'minimising disruption to you and your community'.

It was noted that in overall terms capital maintenance expenditure, (combining both maintenance infrastructure and maintenance non-infrastructure), is proposed at a level consistent with that funded by Ofwat for the AMP period 2005-2010. The proposed business plan does however include large increases in water quality (Q) expenditure and water resources (SD) expenditure to meet expected future obligations.

The overall proposed capital investment programme was shown both in terms of regulatory categorisation and by outcome.

A CCG member raised the issue of pressure in response to an explanation of Enhanced Service Level (ESL) capital expenditure. [post meeting response – the number of properties

Customer Challenge Group

<p>affected by low pressure are recorded. This performance is not shown separately in the annual report to Ofwat. It is a component of serviceability. The current register for properties affected by low pressure is 96 properties for Affinity Water]</p> <p>Consultation</p> <p>The proposed plan is out for consultation on the web site and forms the basis for the large scale deliberative forum events. All CCG members had been invited to observe events. A suggestion was made to video the final session. AW agreed to investigate as to whether videoing would be possible. [post meeting note – it was not possible to arrange at short notice]</p> <p>A range of qualitative and quantitative pieces of research are being undertaken during July and August. The findings from these will inform the final business plan.</p> <p>Outcome measures</p> <p>Testing is taking place on nine outcome measures which relate to the four customer expectations/outcomes. CCG members were invited to consider the full suite of measures which sit beneath the top nine.</p> <p>Comments made by members included:</p> <ul style="list-style-type: none"> • The number of water quality complaints should be reported alongside the compliance performance • Where are the environmental measures given that the 'environment' was not identified as a separate outcome? <p>It was explained, in response to these specific comments, that the outcome measures were designed to be a high level package of measures that align closely to the outcomes. Additionally, the outcome measures should be considered alongside a range of company KPI's that may form the basis of future regulatory performance reporting.</p> <p>The overall performance measurement framework specifically includes water quality customer contacts as a supporting KPI. On the issue of the environment it was explained that within the performance framework there are a range of key environmental measures that compliment the overall outcome of 'having enough water'. CO stressed that the 'enough water' outcome was in itself a water environment outcome as it was focussed on meeting the key challenge of leaving more water in the environment. Furthermore, it was explained that the approach to the outcome measures for 'enough water' was intended to support customer communication by enabling the business to give the following message:</p> <ul style="list-style-type: none"> • We (AWL) will play our part – by reducing leakage; • You (customers) will play your part – by reducing consumption; so that • Together we can improve the efficiency and use of water resources and leave more water in the environment <p>Specific KPI's, addressing the other significant environmental impacts of the operations, are included to demonstrated an integrated approach.</p> <p>A request was made to see the 'long unconstrained list' of measures before the final list was agreed.</p> <p>CCG members were invited to inform AW about gaps or missing measures in the outcome measures and the supporting metrics by 5th August. Members requested seeing earlier iterations of measures [post meeting note – copies of iterations showing the development of outcome measure Affinity water and Ofwat KPI's circulated]</p> <p>ACTION</p> <p>CCG members to advise Affinity Water of any gaps or omissions in the outcomes measures framework (see slide 36) by 5 August.</p>	<p>CCG 5/8/13</p>
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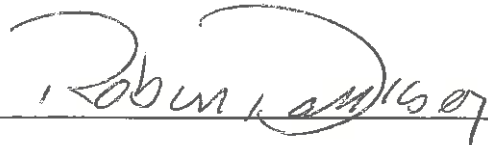
	<p>Incentive mechanisms</p> <p>Ofwat's approach to outcome incentives is designed to encourage companies to define levels of future performance associated with outcomes and make commitments around their delivery that could have financial and non-financial rewards and penalties.</p> <p>The concepts have been challenging for customers to understand. The 'penalty' approach is understood – i.e. if a company fails to achieve the performance it commits to then the shareholder takes the hit and customers' bills potentially go down. Customer's are much less supportive of the opposite position, i.e. that they could pay more for the company doing well.</p> <p>It was recognised that this approach was already used – as SIM, but that it was not very transparent.</p> <p>AW is committed to developing a suitable set of incentives which can be understood by customers. The intention is to 'test' these with the on-line panel. There was some discussion as to whether performance targets would be set at different levels in different communities to reflect local circumstances. Whilst it is an aspiration for AW to localise investment to meet needs, there was no expectation that different incentive /penalty arrangements would operate at community level for the AMP6 period even if performance data is available.</p> <p>Levels of detail</p> <p>Several discussions took place regarding levels of detail of information. The consultation, taking place with customers, is focusing on outcomes and services they value. In order to achieve those, AW needs to consider which combination of inputs and outputs will deliver the best balance. The detailed make up of the inputs and outputs can only be finalised once all the findings from the willingness to pay have been considered, included in the CBA and optimisation work.</p> <p>Keith Cane left the meeting at 12:45.</p>	
3	<p>Information paper on Water Quality</p> <p>No issues were arising from the information paper. A member of the Water Quality team was available for informal discussions at lunchtime and to clarify any points raised by members.</p>	
4	<p>Review of Challenges</p> <p>Updates on three challenges were discussed.</p> <p>1 Leakage</p> <p>A copy of the updated challenge had been circulated to the CCG. Points for clarification were raised. This included:</p> <p>Q What was the company approach to supply pipe leakage?</p> <p>A - In addition to the existing policy, where in some circumstances the repair is free of charge, further action will be considered as part of a metering programme. In addition, customers are being asked, as part of an on-line panel, whether the subsidised scheme should be extended.</p> <p>Q Clarification of use of SELL (sustainable economic level of leakage) and ELL? (Economic level of leakage).</p> <p>A - ELL was the optimum level for financial efficiency in the business however, SELL was the 'societal' value. The level at which AW operate varies with location and water resource availability. This can mean that leakage activity is above the unit cost of water saved and does not pay for the cost of detecting and repairing.</p> <p>Q Are customers prepared to pay to operate below SELL?</p> <p>A – Currently operating at 5-7% below ELL. Further work is being carried out to determine customer preferences in the stage two work on Willingness to Pay which is focused on water</p>	

Customer Challenge Group

	<p>resource management.</p> <p>ACTION Circulate the leakage questionnaire and update response to leakage challenge.</p> <p>Social Tariff</p> <p>ACTION Email Alyson Broadhurst to collect additional comments.</p> <p>The CCG supported the approach that Affinity Water is taking to a Social Tariff, in particular the need to keep it simple. Some constructive and helpful observations were made.</p> <ul style="list-style-type: none"> • When selecting the criteria it was suggested that this could be any means tested benefit. • AW need to consider how to continue to check eligibility for the tariff. • Suggest that it would be reasonable to expect recipient to pay fortnightly or monthly by direct debit, in part to reduce bad debts. • Introduce a capped volume, above which the customer should pay the normal metered rate. <p>Willingness to Pay, Investment and Bill Acceptability</p> <p>The CCG confirmed that the revised scope of the challenge met their requirements and that the level of detail presented in the response was appropriate.</p> <p>The CCG highlighted that the methodology defined in this response to the challenge, along with the framework for weighting findings from research, were the two pieces of reference that they needed.</p> <p>The full response to the challenge would be drafted and circulated before the September CCG meeting.</p>	<p>PC 8/13</p> <p>LA 8/13</p>
5	<p>AOB The timetable for the different editions of the Business Plan to be confirmed Additional performance information is being requested from AW in order to place some context around the CCG report. Scope of audit report from Atkins to be confirmed.</p>	

Minutes of 6th CCG meeting held on 24 July 2013

Approved by



Date

18 September 2013

Affinity Water Customer Challenge Group

Date: 18 September 2013
 Location: Hub, Tamblin Way, Hatfield, AL10 9EZ
 Meeting Room: Board Room, first floor

Timing	Content	Presenter
9:30 – 10:00	Arrive and coffee	
10:00	Introductions, apologies - including 3 Directors from AWL Housekeeping Chairman's report Regulator updates Objectives for meeting <ul style="list-style-type: none"> Review impact of customer feedback on the baseline plan 	
10.30	Address any issues arising from the CCG challenge – Investment options, willingness to pay and bill acceptability (exec summary circulated in advance) WTP and Bill Acceptability findings and application to next iteration of the business (including how different pieces of research yield findings which weighted are used differently) Discussion with the Directors, including how the Board intend to balance the competing needs of customers, shareholders and regulators	
12.30	Lunch	
13.15	Approval of minutes from 24 July 2013 CCG review report	
14.45	Coffee	
15.00	Clarification of issues arising Timetable – iterations of business plan Findings evaluation, process and future dates	
16.00	Finish	

Customer Challenge Group

Purpose of Meeting:	Customer Challenge Group planned meeting Number 7	
Location:	Hub	
Date of Meeting:	18 September 2013	
Present:	Chair Robin Dahlberg Jacky Atkinson DWI Allyson Broadhurst, Charis Grants Keith Cane, East Kent Housing (by video link from 13:30) Karen Gibbs, CCWater David Howarth, EA Allan Johnson, Harlow Council Lucy Lee, BluePrint for Water Hazel Smith, GlaxoSmithKline Jill Thomas, CCWater Dr Phil Nolan, Executive Chairman, AWL (morning) Kenton Bradbury, Shareholder Director, AWL (morning) Fiona Woolf, Independent Director, AWL (morning)	
Observers		Presenters Christopher Offer
Apologies:	Jim Barker, EA Tim Hutchings Mark Kibble, Dacorum Council Mark Tomkins, Heathrow Airport Ltd	
Distribution:	As above and web site	
Originator:	Liz Allen	

No	Notes of Meeting	Action
	<p>Introductions and apologies The Chair welcomed the Affinity Water Limited Directors (AWL) to the meeting. The AWL Chair thanked the CCG for the opportunity to meet with them and looked forward to having an open discussion.</p> <p>Chairs report In addition to items summarised, the Chair commented on discussions at the last CCG Chairs meeting when concerns were raised about the potential implications of the Thames Water Interim Determination of K (IDoK) on total bill acceptability research. The timing of the response from Ofwat to the IDoK, will not allow for further testing to be completed before submission of Business Plans. No other water companies have applied for an IDoK and the impression the Chair gained was that Ofwat are likely to push back on the application.</p> <p>The chair proposed changes to the running order in the agenda to maximise the time allocated to discussions with the Directors.</p> <p>Regulator comments David Howarth, Environment Agency. The EA have started a round of meetings with all water companies to review business plans. A standard set of questions have been sent to companies in advance. The EA are seeking to gain replies to assure the Minister that all companies are meeting their obligations. The meeting with Affinity Water is taking place on 19 September.</p> <p>This nationally consistent process will be completed in October after which Paul Leinster will</p>	

Customer Challenge Group

write to the Minister, and the EA will write back to companies to share their views.

The EA will write to each of the CCG Chairs at the end of November with a statement which can be included in CCG reports.

DH reported that Affinity had responded to requests for information on time and as a result the Agency had identified the issues they wish to explore. These included:

- The company's approach to emergency drought orders of 1:50 years, whereas most of the industry is working to 1:200 years or never
- Levels of investigation for some water resource options to provide assurance of compliance with Water Framework Directive requirements of no deterioration
- Definitions of emergencies when the company can retain licence to abstract from sources subject to sustainability reductions

PN (Chair AWL) responded that the company were committed to meeting all statutory obligations and that the board were aware of the issues raised. The investment needed to meet a 1:200 year or 1:50 emergency drought order has significant financial implications for the company operating in a water stressed area.

DH confirmed that there was no Government or political acceptance for standpipes.

All issues raised by the EA will be addressed in the formal statement of response to the Secretary of State.

Regulator comment

Jackie Atkinson, Drinking Water Inspectorate

The DWI had received all the proposals which were now under review. They had raised a number of issues, which were being dealt with by the business.

Some issues, such as Metaldehyde, were common across companies in the South East and DWI is working with Water UK (Meeting 11 October) to review benefits of catchment management.

Issues DWI are progressing with Affinity Water include:

- Clarification of benefits to Affinity Water customer to the proposal for additional activity at Ardleigh reservoir to manage/mitigate by-products from disinfection when a majority of the water treated is supplied to Anglian Water.
- Greater visibility of the activity to maintain assets to assure continual improvement to Water Quality

JA also confirmed that the DWI regard the maintenance of base assets as a key component in ensuring compliance with drinking water standards.

Assessment of proposals, by DWI, is undertaken by 3 staff to ensure consistency. DWI will provide formal responses by 31 October.

Regulator comment

Karen Gibbs and Jill Thomas, CCWater

CCWater have developed some high level principles for undertaking acceptability testing. In addition they commissioned some focus group research to gain an understanding of what customers would spontaneously feel was a minimum level of acceptance of proposed business plans, as a % of people asked.

The research indicated that customers felt comfortable with a 70 – 75% acceptability.

CCWater have a role in responding to dWRMP and have fed back comments to Affinity Water and have not raised any new issues.

CCWater do not intend to issue a specific response to the Business Plan, they will feed their comments through the CCG.

Issues of concern include:

Customer Challenge Group

	<ul style="list-style-type: none"> • Size of increase in sewerage service bills for Thames Water customers • Made reference to recent Ofwat speech by Sonia Brown on the potential downward pressures that exist currently going into this price review. • Made reference to speech from Sonia Brown signalled that 4.1% might be an appropriate cost of capital. <p>The AWL Board members were asked if they were aware of this comments, and the AWL Chair said they were.</p>	
1	<p>Impact of Customer Feedback on the Business Plan, Christopher Offer, Head of Regulation</p> <p>The presentation started by summarising the stated preference, <i>willingness to pay</i>, research to remind members of the process which had been presented at earlier meetings. The purpose of the research is to generate monetary values for the benefit (dis-benefit) customers place on changes in services. The statistically robust data is then used within cost benefit assessments to support optimisation assessment used to determine investment options. Questions were taken throughout the presentation to clarify and expand on issues, These are summarised at the end of this section.</p> <p>The key findings showed that customers:</p> <ul style="list-style-type: none"> • Do not want to see service deterioration, even if that means lower bills • Value no deterioration in service, more than an improvement in service • Value improvement in tackling leakage, property flooding from bursts and issuing of boil notices the most • Identify hardness as an issue; however, customers do not value it in the same way as other water quality attributes. This means we cannot be confident that there is positive value to reducing hardness.' <p>The package of services that customers' value is formally reviewed and validated, as it is accepted that customers value individual components differently to the sum of the parts. The 'package valuations' can be used to constrain the scale of the service changes and cross referenced to the results from the acceptability testing.</p> <p>The <i>Bill Acceptability</i> research was designed to test acceptability of 3 different versions of the plan. 1200 surveys were conducted with defined quotas of domestic and non-domestic customers. The output was weighted to reflect the customer base.</p> <p>The results recorded 91% acceptability for the proposed plan and for the slower plan - showing a high level of acceptance for a plan that would increase bills (in real terms) by around £3.70 or less by the end of the five years.</p> <p>Key findings included:</p> <ul style="list-style-type: none"> • Support to improve leakage rates • Maintain water quality standards • There is no statistical difference between the slower pace plan and proposed plan for household customers. • Acceptability is not driven by SEG, gender or age • A modest annual increase is enough to have a notable impact on acceptability <p>Additional quantitative research from the on-line panel provided findings that were consistent and included:</p> <ul style="list-style-type: none"> • Leakage – over 80% concerned about water wasted through leakage • Metering – 50:50 split on getting a meter fitted. • Metering seen as 'fairest way to pay' by 70% of non-metred customers • Environment – 88% agreed with reducing water taken to leave more in the 	

Customer Challenge Group

environment

- Water Quality – hardness an issue but majority agreed they rarely think about it or only notice when they see limescale

Headline findings from qualitative research, such as large scale deliberative forums reinforced the messages. The large scale Lets Talk water campaign received 3600 responses; the results were consistent with all other work.

By taking into account the customer feedback AWL presented the likely options for change to the Proposed Plan that was consulted upon. AWL confirmed that it would be recommending to its Board, subject to the finalisation of the Water Resources Management Plan (WRMP) that it should:

- Adopt a slower pace of investment for “Minimise disruption” outcome to keep service levels as they are;
- Have a slower pace of investment in terms of the metering programme so that the number of water resource zones metered in AMP6 is reduced pushing more into AMP7. This would increase the risk of not achieving water efficiency gains to balance supply and demand in the short term; and so
- Consider placing greater incentives on achieving or exceeding proposed leakage reductions, where this is supported by customers, opposed to increasing the level of performance commitment;
- Looking at how to advise our customers on addressing hard water; and
- Ensuring Ofwat is aware of our customer feedback on sewerage charges for its review of Thames Water business plan

Summary of comments and clarifications from questions raised:

- Colleagues who had attended the engagement events agreed that the findings were consistent with what they had heard and seen
- Customer experience of disruption was low which is reflected in the low value placed on service improvements
- Customers will raise water hardness as an issue, however, compared to other quality attributes it is not valued as highly
- Bill acceptability research and the business plan consultation activity have used figures excluding inflation. Comments were made to ensure customers were aware that the unknown future RPI would be added to any increase
- Customers value water supply and sewerage services equally
- Sewerage charges are determined through a separate mechanism, over which Affinity Water has no influence and there is no balancing across service providers. The CCG wanted further assurance that Affinity Water were mindful of the potential increases and that the impact was considered in future plans. AWL confirmed it would need to demonstrate in the Business Plan that it had given consideration to the implications of the sewerage bill on water customers.
- A suggestion was raised to test whether customers would prefer to have separate bills for the separate services
- Note that non-domestic customers had a higher preference for the slow plan
- Request for the segmentation and quotas of non-domestic customers surveyed
- Key challenge to ensure that there is enough water in the central region, for customers and the environment and the need to take an integrated approach – joining up services for metering with social tariffs and education to reducing demand

Customer Challenge Group

	<p>The CCG accepted the conclusions drawn from the research and noted the proposals that would be taken to the Board. The company made a commitment to present a full report, summarising all the engagement reports that the CCG have received, to show how findings have been developed into themes to influence the business plan.</p>	
2	<p>Discussion with Directors</p> <p>Questions from the CCG had been circulated to the Board in advance a wide ranging discussion took place. A summary of points is given below.</p> <p>Q. How will the Board balance the competing issues of customers, regulators and shareholders?</p> <p>A. Given the need to ensure compliance with all regulatory requirements the Board seeks to collect views, produce plans, consider the findings from research and outputs from cost benefit model to make decisions that achieve a balance given the limited discretion available. This includes consideration of risk, particularly longer term risk with availability of water. The 25 year Water Resource Management Plan shows that the lower cost demand side measures may not be sufficient to continue to meet demand, based on predicted population growth and increasingly unpredictable weather patterns. By working with the other water companies, in the South East of England, longer term regional options can be being considered when balancing potential short term savings, against potential future financial burdens.</p> <p>A specific area for consideration by the Board is the speed of the metering programme. Metering helps to manage demand, manage leakage and enable customers to have more control on their bills. We know, from our research, that a significant majority of customers accept that metering is the fairest way to pay for the water used, however, a proportion is still reluctant to switch to a metered charge. The experiences gained through the metering programme in the southeast region, and elsewhere in the industry, will be used to shape the delivery programme to increase successes and allay concerns. In addition, there is an option to slow the pace of metering and spread the learning and costs over a longer period.</p> <p>Q. Why should customers support the proposed plan instead of the low cost, slow investment plan?</p> <p>A. The proposed plan and the slower plan are equally acceptable to household customers: business customers had a slight preference for the slower plan. The Board will need to take account of the views of the other stakeholders be they regulators, shareholders and or the environment, when making the final decision about what is best for the business in the long run. Reference was made to and exchange of views between AWL and CCG Chair on the same question. The correspondence was made available to all CCG members prior to the meeting.</p> <p>The board is mindful of the wider economic situation and aware that average incomes may not have kept pace with inflation. Similarly direct costs to the business including materials, chemicals and energy have increased and all businesses are facing real upward cost pressure.</p> <p>Q. Affordability for low income households under universal metering. Transitional arrangements.</p> <p>A. Affordability is an issue for all low income households, including those already on a metered charge. We are developing a social tariff which, along with a comprehensive education and awareness programme, will be made available to all customers moving to a metered charges. We seek to 'pull' customers toward metering by showing the benefits and provide advice on water efficiency to minimise the number of customers that are compulsorily switched to a metered charge.</p> <p>Further research is planned to test acceptability of the transitional arrangements. CCWater have offered support.</p>	

Customer Challenge Group

Q. Debt – efforts to control the impact on households who pay their bills.

A. We are developing our debt management systems to minimise overall debt levels that end up impacting on the bills of all customers.

We are taking the long term view, seeking to implement the least cost, demand side management options first. Through carefully monitoring and measuring we will be able to see whether we are achieving the savings before committing to expensive investment in supply side measures.

Q. How does the maintenance programme ensure continual improvement in water quality?

A. The capital maintenance programme will always include measures to continually improve water quality. This type of investment delivers multiple benefits, not just improved reliability. The use of outcome measures and indicators of performance will allow us make this more visible.

The EA raised some points – which had been covered in earlier discussions.

The Chair of the CCG ask the Board members whether they felt there were any points the CCG should be addressing?

A. The AWL Board members felt that there was a common understanding with the CCG of the key issues and that the CCG had not raised any matters they were not aware of. One area of agreement was about the opportunity to increase customer's awareness and understanding of the challenges faced.

The AWL Board Chair responded by asking the CCG whether they felt they had enough access to and debate with the company.

Observations made by members included:

CCWater

- Very good access to the company
- The CCG for Affinity Water started later than other companies, which meant research and engagement work had to start very quickly, and it would have better to have been more involved in developing the strategy
- Important to be involved in the closing stages to assure that the interpretation of findings is accurate

Chair CCG

- Can see a process of cultural change over the last 18 months and that there is an on-going challenge for the AWL Board to continue to distil the issues down
- Company should consider how to continue the dialogue with customers and should consider checking with focus groups or panels before implementing changes affecting the service
- From attendance at various events it was seen that customers value AWL as a local company employing local people who were knowledgeable about the area
- In all forums customers have been universally positive about the company and that the challenge is to continue to maintain that trust and legitimacy

Allan Johnson

- Suggested not putting too much weight on customer feedback on some issues and this was based on perception, not an actual reality

The AWL Directors left the meeting.

3	<p>Executive Summary of CCG Challenge Response on Investment Options, Willingness to pay and Acceptability of Proposed Bill Levels, Christopher Offer, Head of Regulation.</p> <p>The presentation summarised the response to the Challenge. CCG members had been provided with the full response and supporting appendices. The presentation and discussion ensured that members understood:</p> <ul style="list-style-type: none"> • How Affinity Water have consulted with customers • How Affinity Water have determined their preferences and acceptability • How Affinity Water have assessed acceptability in light of the overall sewerage bill. <p>Earlier discussions at the meeting provided the opportunity to review the findings and members accepted that the process was complete and robust and the use of findings was appropriate.</p> <p>The challenge response was accepted.</p> <p>Further Bill Acceptability research is being planned and the members requested that the scope should include reference to:</p> <ul style="list-style-type: none"> • Phasing of any increases over the 5 year period • The additional increase from RPI • Total bill impact, where sewerage charges are considered <p>It was agreed that the findings from that research would form an additional appendix to the Challenge and would be reported in the summary report on all engagement activity.</p>	
4	<p>Minutes from previous meeting</p> <p>Minutes of the meeting 24 July were accepted. All actions identified had been completed.</p>	
5	<p>CCG report review Minute provided by Chair.</p> <p>The AWL employees left the meeting.</p> <p>The Chair advised that Tim Hutchings had provided comments by email as he was unable to attend the meeting due to illness.</p> <p>The statutory bodies said that would provide brief text summarizing their views to be incorporated into the Executive Summary. Where they provided a separate letter to the CCG, this could be included as an appendix to the report.</p> <p>The CCG noted that a copywriter had been engaged to improve the quality of the report. They noted that the copywriter would not modify any of the opinions expressed by the CCG. The CCG considered whether the report should be shortened, and there was a strong view that the Report should not be shortened. One colleague said that the report seemed very similar to a majority of other CCG draft reports that she had sight of. The CCG resolved to continue with the current approach to writing the report.</p> <p>The CCG agreed the proposed changes to the draft CCG Report, except where noted below.</p> <p>The CCG decided that <i>Chapter 2 - Affinity Water's engagement with its customers</i> needed to be rewritten. The CCG decided it was not appropriate to include tables extracted from the various engagement reports, in part because the tables would then be out of context, in part because it for AWL (and not the CCG) to make the case for the Business Plan. The CCG should refer to the engagement reports where they provided evidence of concerns the CCG wished to highlight. The CCG agreed a number of conclusions that they would like to be incorporated into the chapter. On a point of detail, the CCG noted that paragraph 2.27 was internally inconsistent. It was agreed that the Chair would rewrite the chapter and circulate a</p>	

Customer Challenge Group

	<p>new draft by 25 September. CCG members could provide additional comments by email.</p> <p>In <i>Chapter 4 – Themes</i> the CCG agreed the approach used to write the section on “Debt.” The CCG asked the Chair to incorporate agreed conclusions at the end of the section.</p> <p>The CCG agreed that they would not like to see any interim drafts before the papers are distributed for next CCG meeting (except for chapter 2, as noted above).</p> <p>The Chair thanked the CCG members for their contributions and their continuing efforts.</p>	

Minutes of 7th CCG meeting held on 18 September 2013

Approved by Robin Dalby

Date 4 November 2013

Affinity Water Customer Challenge Group

Date: 4 November 2013
 Location: Hub, Tamblin Way, Hatfield, AL10 9EZ
 Meeting Room: Board Room, first floor

Timing	Content	Presenter
9:30 – 10:00	Arrive and coffee	
10:00	Introductions, apologies Housekeeping Approval of minutes from 18 September 2013 Chairman's report Regulator updates Objectives for meeting <ul style="list-style-type: none"> Gain an overview of the business plan to understand how priorities have been addressed 	
10.30	Presentation of Business Plan, including headline figures, outcome measures etc.	Chris Offer
12.30	Lunch	
13.15	CCG report review and finalisation	
16.00	Finish	

Customer Challenge Group

Purpose of Meeting:	Customer Challenge Group planned meeting Number 8	
Location:	Hub	
Date of Meeting:	4 November 2013	
	Chair Robin Dahlberg	
Present:	Jim Barker, EA Keith Cane, East Kent Housing (by video link) Karen Gibbs, CCWater Tim Hutchings Allan Johnson, Harlow Council Hazel Smith, GlaxoSmithKline Jill Thomas, CCWater	
Observers	Richard Moriarty, Affinity Water (morning only)	Presenters Christopher Offer
Apologies:	Jacky Atkinson DWI Allyson Broadhurst, Charis Grants John Fox, Tendring Council Mark Kibble, Dacorum Council Lucy Lee, Blueprint for Water Mark Tomkins, Heathrow Airport Ltd Damian Williams, Tendring Council	
Distribution:	As above and web site	
Originator:	Liz Allen	

No	Notes of Meeting	Action
1	<p>Introductions and apologies The Chair welcomed Richard Moriarty, newly appoint Regulations Director, Affinity Water to the meeting. The Chair advised of developments with membership including: Lucy Lee would be leaving WWF shortly and is seeking a replacement so that Blueprint for Water can maintain their representation on the CCG, post report submission. John Fox and Damian Williams have joined the CCG and will represent Tendring Council. Allan Johnson will step down after CCG report submission.</p> <p>Amendments to minutes The Chair took amendments to the minutes from 18 September 2013. These were revised, approved and signed by the end of the meeting.</p> <p>Chairs report In addition to points raised in his report the Chair updated the group on his meeting with the Board 23 October. There were 4 concerns raised, these were: the cost of capital, proposed price increase above inflation, the qualification criteria for the social tariff and issues raised by the Environment Agency.</p> <p>The Chair had a long conversation with the Board covering each point.</p> <p>Subsequent discussions with Affinity Water on social tariff have addressed concerns. CCWater advised that they had been consulted and the Chair advised that Allyson, from Charis Grants was supportive. It was noted that Affinity Water was very keen to launch the service as soon as possible.</p>	

Customer Challenge Group

	<p>The CCG recommended that Affinity Water should consider undertaking a pilot launch of the social tariff as an opportunity test the administration and management systems.</p> <p>Regulator comments Jacky Atkinson, DWI, has sent a letter to Affinity Water and the CCG commenting on compliance for inclusion in the CCG report. All concerns had been addressed and there were no outstanding matters.</p> <p>Regulator comment Jim Barker, EA, has sent a draft letter of compliance to Affinity Water and CCG raising some concerns. Further meetings have been planned to discuss matters prior to a final letter being issued. The EA will draft a paragraph for inclusion in the CCG report and the compliance letter being added to the appendix.</p> <p>Regulator comment CCWater confirmed that they will not be sending a separate letter.</p>	
2	<p>Final Business Plan, presentation by Chris Offer, Head of Regulation</p> <p>The presentation covered a summary of the Outcome Delivery Incentive (ODI) framework including the proposed rewards and penalties, a summary of customer feedback and how the final plan had been developed to take into account this feedback, a summary of investment proposals, Bill Acceptability testing phase 2 and projected bill impacts for the final plan.</p> <p>The outcome measures framework includes 4 customer outcomes and 13 performance measures, 2 of which are mandatory Ofwat measures (SIM and AIM, although the AIM assessment mechanism is to be confirmed and SIM is currently under consultation). The performance commitments in the final business plan reflect customer preferences with a majority of the improvement targets linked to the outcome of having enough water.</p> <p>Discussions covered the evolution of the changes, from consultation to current position, and comments were raised about the leakage reduction and the revised PCC measure.</p> <p>Q What does a 14% reduction in leakage relate to as a % of total leakage? Q How does the reduction of PCC from a proposed 7% to 2% reflect customer priorities? Q A strong message coming from the research (especially the on-line panels and the Lets Talk Water campaign) that customers feel that the standard time of five days to fix a visible leak is too long. Is Affinity water going to change this standard?</p> <p>These issues will be clarified for the CCG.</p> <p>Responses were given to comments about housing growth, confirming that future housing growth and development had been taken into account as part of the water resource planning and was therefore built into the final business plan and investment proposals.</p> <p>Design and use of ODI's Ofwat defined a set of criteria to be taken into account when designing ODI's. Affinity Water has developed their framework, in conjunction with Frontier Economics, to meet these criteria.</p> <p>The incentive types are financial or non-financial. Affinity Water is proposing a number of financial penalty only measures, where customers do not value improvements in performance and one reward / penalty measure for leakage.</p> <p>The maximum positive incentive achievable is 1.56% of total revenue for out performance in leakage reduction and SIM. The potential penalty for poor performance against the 4 applicable measures is 3.96% of total revenue.</p>	

Members made reference to the 'Daily Mail' test – would customers accept that their bills could be increased if Affinity Water outperformed their leakage reduction target?

Summary of customer Feedback

The CCG were reminded of the findings from the research that Affinity Water had undertaken and how these were summarised into a series of 14 customer themes that were used to influence the business plan.

Based on the priorities identified by customers, the investment plan was revised and a set of investment proposals presented.

Those investment proposals generated a programme of planned capital investment of £506m over 5 years. This investment was compared to the current investment plan for AMP5 (2010-2015). Significant changes are required to meet future obligations for supply and demand management and a range of water quality schemes.

Compared to the current AMP, investment to meet new obligations for supply and demand will increase by around 330% and an increase of around 90% to meet quality obligations. These obligations account for an additional £123m (compared to investment in AMP5)

Bill Acceptability Testing stage 2

The current research is testing acceptability of a bill increase of £1.80. This reflects customer priorities but does not take account of shareholder and financeability requirements.

The projected impact on the customer bill, to be presented to the Board for approval, is likely to be no more than zero over the five years, (before inflation, after the financial considerations have been taken into account).

The group held a wide ranging discussion about some of the presentational challenges of the ODI rewards and penalties.

The CCG challenged that Affinity Water had not asked the direct question to customers on their views on rewards for increased performance in leakage. In response they were advised that the detailed *Willingness to Pay* research, undertaken in controlled conditions where multiple integrated impacts were considered, showed that customers did value an increase in leakage activity more than maintaining the current performance. This provides evidence that customer's support and value further leakage reduction..

In addition, the stage 1 Bill Acceptability Research showed a very high acceptance for an increase of up to £3.70. It was therefore the case that, providing service levels were achieved, customers were prepared to accept some increase in bills for outperformance on leakage reduction.

The CCG explicitly commented that they did not think customers would like a potential reward to outperformance in leakage reduction. In particular the issue of bill stability was raised as a concern. It was argued that customers preferred bill stability and predictability and therefore the approach to outcomes and incentives was objected to as a matter of principle.

Further discussion around the issue of balancing rewards and penalties considered the extent to which it was possible to ensure rewards from outperformance could be accommodated within a flat real bill profile (that is flat bills excluding inflation). Affinity Water responded that they were grateful for the feedback and reflected that whatever approach was taken it needed to be simple to explain to customers and that the final outcome delivery incentive design would need to be reviewed and approved by the Board alongside the final expected level and profile of bills for AMP6 .

Customer Challenge Group

3	<p>The CCG Chair provided the minute of the time when the CCG members reviewed the draft report.</p> <p>No Affinity Water employees were present.</p> <p>CCG members first considered the report as a whole and confirmed that they did not wish to make any substantive changes in approach.</p> <p>The Chair circulated a nine page document he prepared in advance showing all the changes he thought the CCG should consider making to the draft report.</p> <p>CCG members then reviewed each page of the entire report, proposing changes.</p> <p>CCG members confirmed every opinion contained in the report was correct (subject to amendments being incorporated).</p> <p>Several CCG members offered to email proposed text to the Chair for incorporation into the next version.</p> <p>The Chair said he would circulate a revised draft by Friday 8 November 2013.</p> <p>CCG members noted that they were still awaiting several important documents, including the following:</p> <ul style="list-style-type: none"> • 2 x challenge records • Report on Bill Acceptability, phase 2 • Final draft of the Business Plan • Assurance from Doug Hunt of WS Atkins Ltd. <p>The Chair thanked the members for their continuing efforts.</p>	
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Minutes of 8th CCG meeting held on 4 November 2013

Approved by Robin [Signature]

Date 18 November 2013

Affinity Water Customer Challenge Group

Date: 18 November 2013
 Location: Hub, Tamblin Way, Hatfield, AL10 9EZ
 Meeting Room: Board Room, first floor

Timing	Content	Presenter
9:30 – 10:00	Arrive and coffee	
10:00	Introductions, apologies Housekeeping Approval of minutes from 4 November 2013 Chairman's report Regulator updates Objectives for meeting <ul style="list-style-type: none"> Review final CCG report taking account of updates on business plan 	
10.30	Updates on business plan since 4 November.	Chris Offer
12.30	Lunch	
13.15	CCG report review and finalisation	
16.00	Finish	

Customer Challenge Group

Purpose of Meeting: Customer Challenge Group planned meeting Number 9 Location: Hub Date of Meeting: 18 November 2013 Chair Robin Dahlberg Present: Keith Cane, East Kent Housing (by video link) Tim Hutchings Allan Johnson, Harlow Council Mark Kibble, Dacorum Council Lucy Lee, BluePrint for Water Hazel Smith, GlaxoSmithKline Jill Thomas, CCWater Mark Tomkins, Heathrow Airport Ltd Observers Apologies: Jacky Atkinson DWI Jim Barker, EA Allyson Broadhurst, Charis Grants John Fox, Tendring Council Karen Gibbs, CCWater Damian Williams, Tendring Council Distribution: As above and web site Originator: Liz Allen			Presenters Christopher Offer
No	Notes of Meeting	Action	
1	<p>Introductions and apologies The Chair thanked Lucy Lee for maintaining her role on the CCG representing BluePrint, for water, after changing roles.</p> <p>The minutes were reviewed and an amendment made. The minutes were approved and signed.</p> <p>Three questions were posed in the minutes 4/11/13 and replies provided:</p> <p>1 What does 14% reduction in leakage look like as a % total leakage?</p> <p>If the starting Distribution Input (DI) is 946.51 MI/d in 2014/2015 and our leakage target is 196 MI/d that is 20.7% of DI.</p> <p>If DI is 952.78 MI/d in 2019/2020 and leakage is reduced by 27 MI/d to a target of 170 MI/d that is 17.8% of DI</p> <p>NB – if we calculate against a forecast reduction in DI of 901.35 MI/d at same level of leakage (170 MI/d) this would be 18.9% of DI.</p> <p>Therefore care needs to be taken when comparing % of leakage to DI over time when significant reductions in DI are planned.</p> <p>2 How does a reduction of PCC from a proposed 7% to 2% reflect customer priorities?</p>		

Customer Challenge Group

	<p>The CCG were advised that the figure had been revised. The proposed reduction in PCC is 7%.</p> <p>3 A strong message coming from research is that the standard time of five days to fix a visible leak is too long. Is Affinity Water going to change this standard?</p> <p>This standard is based on working within statutory notice period requirements (before working on highways) enforced by the Highways Authorities (County Councils, London Boroughs and Unitary Authorities). For most jobs we work to a 3 day notice period. Agencies can request a 30 day notice for non-emergency situations.</p> <p>Emergencies are generally restricted to leaks and burst that are 'causing damage' to property. In these situations we aim to fix the leak/burst immediately.</p> <p>We work cooperatively with Local Authorities and do not call all work 'emergencies'. In drought situations we do treat visible leaks as emergencies which the authorities tolerate.</p> <p>If we want to change the standard to 24hours it relies on the cooperation of all the Local Authorities. We have no plans to change the standard, other than in drought situations and recognise customers need more information about operational constraints.</p> <p>The Chair advised that Affinity Water had committed to a bill increase that would be equal to or lower than zero in real terms. The final numbers were being processed for recommendation to the Board on 20 November.</p> <p>Regulator Updates There were no regulator members available to provide an update.</p>	
2	<p>Updates on the Business Plan since 4 November 2013, presentation by Chris Offer, Head of Regulation</p> <p>Updates were provided on the outcome measurement framework; customer feedback; acceptability testing; projected bill impacts; and comparative average bills to disposable household incomes.</p> <p>The outcome measurement framework was updated to show 7% reduction in demand (PCC) and 5% improvement in Water Available For Use (WAFU).</p> <p>Confirmation was given that Affinity Water has designed a penalty/reward framework that reflects customer priorities. There are two potential reward/penalty measures, four penalty measures and the remainder have non-financial incentives. The two measures with potential rewards/penalties are for SIM (currently under review by Ofwat) and leakage.</p> <p>There will be a lag effect in the application of any rewards. That means that if performance exceeds the target in year one, the reward could not be applied before year 3 and for SIM (under current arrangements) the adjustment is made at the end of five years.</p> <p>The profiling of the final bill level will take account of any potential rewards.</p> <p>Customer feedback had been summarised and validated into a set of 14 themes. A summary table showing how these aligned to customer outcomes was shared.</p> <p>The stage two Bill Acceptability summary report was circulated to members. Headlines were</p>	

Customer Challenge Group

	<p>drawn out comparing stage one and two. This showed a high acceptability for the proposed plan reflecting customer priorities. This provided reassurance that the plan being put forward is acceptable to a large percentage of customers.</p> <p>The changes in performance, for a range of the services, were accepted. This gives assurances that customer support the planned activity.</p> <p>It was repeated that the investment plans, and associated changes in service, had been finalised and the scale and scope of the investment programme agreed.</p> <p>The last stage is to make recommendations to the Board that will take account of the overall financeability of the plan.</p> <p>It was confirmed that the cost of capital being applied was lower than the assumed figure set out in the draft business plan consultation.</p> <p>A summary showing average household bills, mapped against real disposable household income was shared. This used an indicative bill level (equal to or less than zero). The trend shows a decline in water bills relative to an increase in household disposable income based on OBR forecasts for the period from 2010 to 2020.</p> <p>The CCG raised some questions. Q What notified items were Affinity water including in the business plan? A: We have not finalised our position and are considering this in the broader context of future uncertainty and how we balance risks across the full range of regulatory mechanisms available.</p> <p>Q Is Affinity Water considering using a performance measure associated with “fair profit”? Where company gains were shared with customers? A: The current debate and the decisions to share gains are pertinent to the financeability of the plan. No explicit performance measure is being considered. The annual customer survey, to test the outcome ‘providing a value for money service’ is being developed and there is an opportunity to cover this issue.</p>	
3	<p>CCG report</p> <p>The CCG Chair provided the minutes for this section.</p> <p>Affinity Water employees were asked to excuse themselves from the room while the CCG reviewed their draft report.</p> <p>The Chair asked colleagues whether they were broadly content with the report or whether they wished to raise any major concern. No major concerns were raised, so the CCG reviewed the amendments that each member suggested. The amendments were mainly to the Foreword and chapters 1 and 2. The representatives from CCW and WWF committed to providing new text to cover issues they raised. The CCG asked the Chair to speak to Jim Barker to confirm that the EA were still content with the wording of 1.21. The Chair promised to amend the report and circulate the new version by the end of the week.</p>	
4	<p>AOB</p> <p>The Chair and the CCG offered their congratulations to Fiona Woolf (Independent AWL Director who attended CCG meeting in September) on her appointment as Lord Mayor of London.</p>	

Customer Challenge Group

	<p>The Chair expressed his thanks to the CCG for their commitment and involvement in challenging the business on its delivery and use of customer and stakeholder engagement over the last 18 months.</p> <p>The CCG expressed their thanks to the Executives and staff from Affinity Water for their accessibility and willingness to provide information and share experience.</p>	
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Minutes of 9th CCG meeting held on 18 November 2013

Approved by_____

Date _____.

Note 25 November. Minutes circulated to CCG. Not formally approved as next meeting is after submission date.

Appendix 6

Challenge Records and Responses

Debt

Leakage

Investment

Metering

Customer Challenge Group

Number/reference: 0001	Date: 13 November
Raised by: CCG 13 September 2012	Subject area: Debt
Due by date: 21 November	

The challenge: Debt

Challenge:

To clarify how current levels of debt impact on customers' bills and how forecast debt levels are likely to impact customers' bills, if current debt recovery practices are continued; and what additional actions Affinity Water plan to take to reduce these levels of debt and associated recovery costs and how these will potentially impact customers' bills?

To understand what, if any, plans the company has to introduce social tariffs or any other measures designed to address affordability issues and some customers' inability to pay.

Expectations:

The CCG would like to understand the current costs associated with debt and how these are redistributed amongst the customer base.

The CCG has formed a tentative view that in considering the potential introduction of social tariffs, the current and forecast debt position, and associated cross subsidies, needs to be understood. If the company plans to consult its customers on social tariffs, the debt issue will need to be discussed in order to provide customers with some context.

The CCG would therefore like to receive a paper on these topics to support a further discussion at the CCG meeting in November 2012

Specific points to be addressed:

- A general explanation of the company's tariffs (household and business) and the components of a metered and unmetered bill.
- How debt and recovery costs are redistributed amongst different classes of customers; the range of the cross subsidy, as well as the average figures. We are particularly interested in how domestic and commercial tariffs account for debt. Does one group of customers subsidise more than the others?
- The CCG would like graphs of the trends in debt over the last five years and a forecast of the future debt levels through to 2020. We would like to see how this has impacted customers' bills and the range of cross-subsidies not just an average figure.
- Are there any differences in the debt levels in Central, East and Southeast? What are the lessons that Affinity Water has learned from the different regional experiences, and how will these be applied?

- During the consultation process, how does Affinity Water propose to advise customers' of the debt issues?
- In looking at water metering proposals, is Affinity Water considering affordability, and in doing so taking the opportunity to provide practical help and encouragement to customers to be more water efficient?

Company challenge response

Prepared by:

Martin Hall, Senior Regulatory Economist
 Nick Carney, Debt Collection Manager
 Pauline Wilson, Head of Customer Relationships (Affinity Southeast)
 Christopher Offer, Head of Regulation

1. Introduction

This CCG challenge response has been prepared in two parts. The first part focuses on the principal issue of customer debt and how debt costs are redistributed across customers. The second part focuses on the broader related issue of affordability and social tariffs.

This response has been prepared by a number of contributors across the Affinity Water business which reflects the extent to which customer debt impacts a range of important issues in addition to debt recovery practices.

We have set out our current views in relation to the issue of affordability, social tariffs and the impact of potential future water metering proposals.

2. Current levels of debt and redistribution of costs across customers

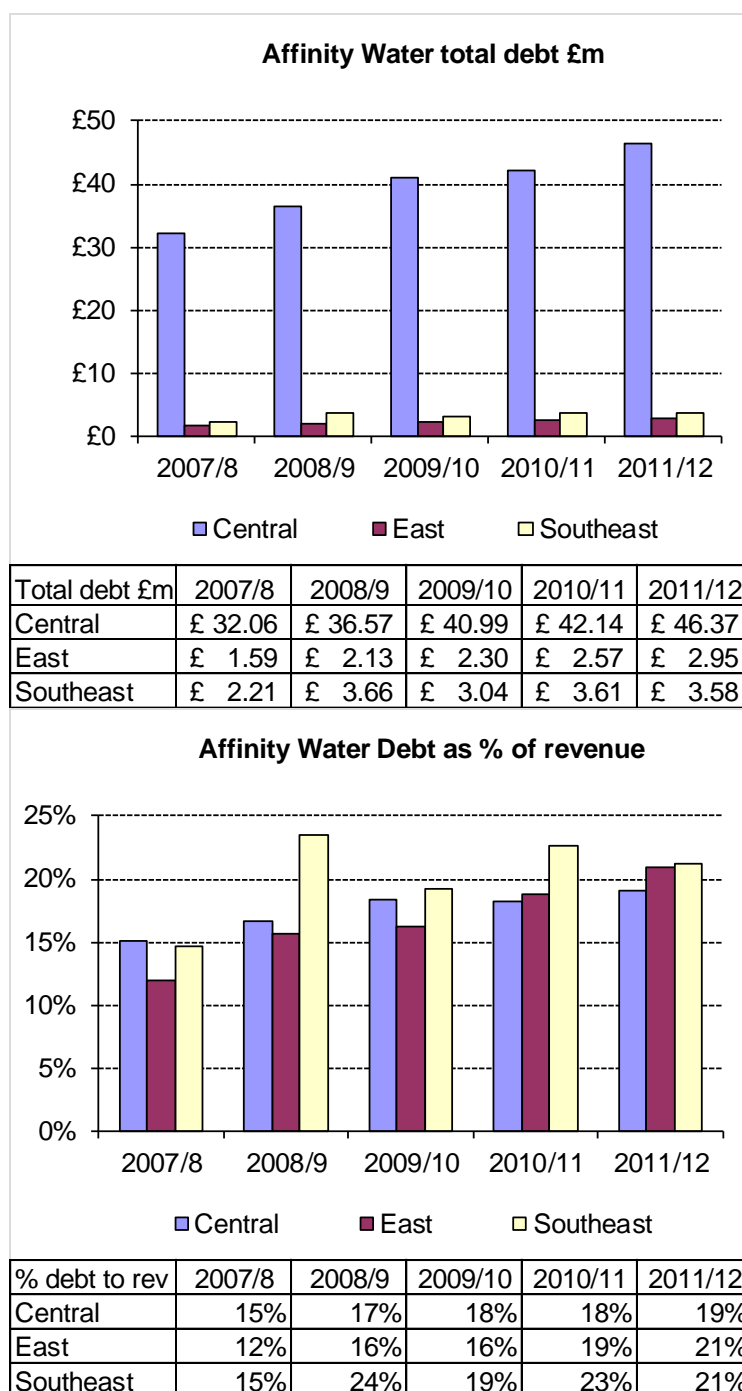
Current levels of debt

We start by presenting information on recent trends in debt over the last five years.

The figure on the next page show the total levels of debt (£m) and debt as a percentage of revenue for each of the Affinity Water regions for the period 2007/08 to 2011/12.

For all three regions the level of debt as a percentage of revenue has grown over the period. For the central region debt as a percentage of revenue has grown from 15% in 2007/08 to 19% in 2011/12. A similar rate of growth has occurred in the southeast region while the highest rate of growth has occurred in the east region which has almost doubled during the period from 12% in 2007/08 to 21% in 2011/12. We do not explicitly forecast future levels of debt through to 2020 but we will need to make an assessment of these costs as part of our overall business plan for PR14.

Figure1: Summary of debt and debt as a percentage of billing for Affinity Water 2007/08 to 2011/12



Source: Affinity Water 2012-13

How debt impacts customer bills

The mechanism by which debt impacts customer bills is through 'bad debt'. It is not possible at the end of a single year to know how much debt will be collected in the end. This is because we will continue trying to collect unpaid bills for many years. We therefore make a charge at the end of the year in our accounts called 'Bad debt'. Bad Debt is essentially an estimate of the amount of debt that we will eventually write off, in other words debt that we accept is no longer worth trying to collect).

Because bad debt charge in our accounts appears on the profit and loss statement it is an item of operating expenditure. When Ofwat are calculating price limits at a periodic review, they forecast future operating expenditure, amongst other things, and calculate the future 'revenue requirement' of the company. The forecast of future operating expenditure is not very sophisticated. Ofwat basically pick a year, which they call the 'base year' and assume that future expenditure will be the same as it was in that year with some adjustments for known changes and efficiencies. We expect 2012-13 will be the base year for PR14, with some possible use of the 2013-14 figures. The revenue requirement is effectively the amount of money that the company will need in order to finance itself during the next five years. The revenue requirement is converted into a k factor at the periodic review and the k factors are converted into tariffs, which are the bills which customers pay.

Generally speaking, therefore, a higher level of debt will lead to a higher bad debt charge, which will lead to a higher operating expenditure in the base year, which will lead to a higher revenue requirement, which will lead to a higher k and higher tariffs in the next five year period. It is worth noting that higher debt levels will have no effect on customers' bills within the period.

Regional lessons in debt management

There has been much learning from each region's method and systems for debt collection. Indicated below are some of the changes we have implemented or are in the process of implementing to improve overall debt recovery rates.

- Adoption of consistent best practice recovery paths and actions
- Adoption of consistent best practice letters across all three regions
- Recovery of costs of debt collection agencies (i.e. £50 charge when accounts are placed with debt collection agencies)
- Use of the same debt collection agencies
- Expansion of the use of Debt Recovery Officer for household property visits
- Increased promotion of direct debit as the preferred method of future payment

Looking further ahead

- Improved scheduling and running of recovery to ensure accounts move from one step to the next on recovery paths
- Use of High Court enforcement actions for higher value debt
- Implementation of a Debt Management System during late 2013

We have been sharing and implementing good practice on billing and collection of debt for many years. The limited tools that companies can use to recover debt, following the ban on disconnection in 1999, and the strong regulatory incentives for companies to manage debt effectively, mean that individual companies are continually seeking ways to improve their performance through learning from others.

Initially, sharing of good practice took place in a relatively informal way. To provide a greater focus, in 2007 a dedicated "Water UK Debt Good Practice Network" was established.

This network is open to debt practitioners from all companies - members of the network are typically operational managers with responsibility for debt and collection and is chaired by the Affinity Water Debt Collection Manager.

The network operates as a way for companies to identify and share good practice, and to benchmark their activities in billing and collection of debt. It meets at least twice a year in person, and operates as a virtual network between meetings. This allows any company to request information on a topic of interest at any time, and outputs are shared with all companies.

Information on a wide range of subjects have been shared by the network (c200), for example approaches to social tariffs and debt restart schemes, information sharing with local authorities or credit reference agencies, use of internal and external debt collection agencies, Water Direct and how companies handle changes of occupation.

The network is now in its sixth year and continues to generate a regular flow of requests for benchmarking information, as individual companies respond to the incentives provided by regulation to become more effective at managing debt.

Throughout the life of the network Affinity Water has been a regular attendee at meetings and a key contributor of information and data.

Forecasting future levels of debt has been the subject of research undertaken by Water UK Industry Research (UKWIR) which is due to present its findings to water companies and associated stakeholders in November.

Debt cost redistribution and issues of cross-subsidy between customers

In the short term, less than 5 years, increases in bad debt charges are met by investors not customers. This is because the prices we charge are fixed by the price control formula, so they are not allowed to rise even if bad debt charges rise. Investors carry the risk of higher bad debt charges.

Every five years, at price reviews, the regulator can re-align the price control formula to reflect actual costs. At this point, customers, begin to meet any increases in bad debt charges arising in the prior five year regulatory period.

We operate a simple measured tariff structure and we supply the majority of customers, in the same region, at the same standard tariff rates (a general explanation of our household and business tariffs and the components of a metered and unmetered bill are set out in Appendix A). As a result we have a uniform distribution of recovery of costs of bad debt. This applies whether customers are business customers or domestic, rural or urban, single or multiple occupiers. As a result it is not possible to say, with certainty, that one group of customers subsidise more than any other.

There is no strong correlation between water consumption and rateable value. However, it can be argued that within the unmeasured rateable value system of charging, customers occupying high rateable value, larger properties pay more than customers in smaller properties. Therefore it is technically correct to conclude there is a general cross-subsidy from occupiers of large properties towards those in smaller homes, which includes all the costs of supply, not just those relating to bad debts.

There are also certain differences between our charging policies for commercial and domestic customers that are not currently reflected in tariffs. Firstly we are not allowed to disconnect domestic customers for non-payment, but we may, as a last resort, disconnect business customers. We are also allowed to request security deposits from business customers with high risks of non-payment as surety against future bills, although in our company this is not commonplace. Finally we tend to bill business customers more frequently than domestic customers and this helps us detect cases of unpaid bills more quickly than with half-yearly billed household customers. In general these differences, along with other factors, mean that the incidence and severity of bad debt is generally lower amongst business customers than with households. This leads us to conclude there is a tendency for business customers to cross subsidise the bad debt costs of households.

In setting large user and mid user tariffs, we reflect differences in network costs, but make no specific differentiation for bad debt costs.

Overall, our assessment is that in bad debt costs, there is generally a cross subsidy from commercial customers to domestic customers and from unmeasured customers in large properties to other unmeasured domestic customers although it is not possible for us to be specific about the size and scale of any cross subsidy.

3. Affordability, social tariffs and the impact of potential future water metering proposals.

Consultation on debt issues

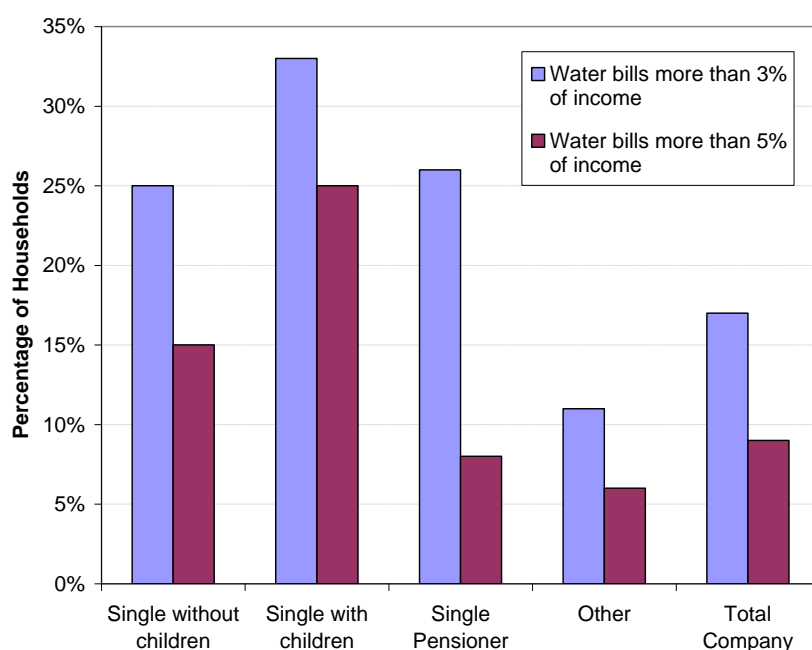
As part of our business planning process we will consult with customers about the possible future paths of water prices. We will expose the key drivers of prices, including bad debt charges, and the effects of our plans to improve management of bad debts.

Affordability

Ofwat promote a measure of risk of being unable to afford water bills as being households where the water and sewerage bill accounts for more than 3% of income after housing costs. In our area, 1 in 6 households or 17% of households are within this category. This is lower than the national average, reflecting higher average incomes in our area and that the sewerage bill from Thames Water is currently the lowest in England and Wales.

Affordability risks are concentrated amongst households with a single adult, whether that adult has children (1 in 3), is without children (1 in 4) or is a single pensioner (1 in 4). This is shown on the diagram below. Amongst single adults without children, water bills are more than 5% of income for 1 in 6, rising to 1 in 4 for those with children.

Figure 2: Affordability Indicators Affinity Water Ltd Central Area



Social tariffs

We are considering introducing a social tariff to alleviate affordability risks. A likely future scheme would offer reduced charges for customers able to demonstrate receipt of certain means tested state benefits. Periodically customers would have to demonstrate continued eligibility or be transferred out of the scheme. The reduced charges would be funded by charging more, say up to 1.5% more (as per the recent Defra guidance), to all other household customers.

We need to discover whether a social tariff would have support from customers, and also to what extent customers would be willing to pay more for water to fund concessions for other customers. We specifically raised this issue in our consultation 'Investing for your community' by asking respondents "In principle, do you think we should implement social tariffs? Why?" We also need to know whether customers support the receipt of means tested state benefits as qualification for social tariff assistance. This is key element of our future customer engagement.

There may be advantages in working with Thames Water as if there were a common approach covering water and wastewater; it would be simpler for customers to understand and for us in our billing operations.

More generally, we could, with customer and regulatory support, alter the general balance of our tariffs towards reducing standing charges. This would help because in general, standing charges have greater incidence effects on single adult households. Similar to single occupier discounts for Council Tax, charges will be less reflective of the cost because the standing charges are per property driven rather than occupancy driven.

Impact of potential future water metering proposals

In looking at water metering proposals, we will take into account the issue of affordability as well as the opportunity to provide practical help and encouragement to customers to be more water efficient.

Education is the key to encouraging customers to change their use and become more water efficient and we take every opportunity to provide practical help and advice on how customers can save water, through various media. We offer simple practical devices such as Hippo Bags, shower restrictors and water butts but a level of apathy from consumers means we need to take a more innovative approach.

Recent tariff trials in the Southeast region offered a number of customers the option to pay a lower rate per cubic metre (1000 litres) for the first 80m³ (80,000 litres) used which then increased to a higher than standard tariff rate if more than 80m³ was used. This two year trial had little to no impact in getting customers to reduce their average daily consumption leading us to believe that there needs to be a significant difference in the cost before this option would be effective. In future new technology will allow customers the option to measure their water consumption every 15 minutes through a device located within their home.

Experience has shown that providing customers with detailed information about their own consumption using simple graphs on bills can be helpful. An option would be to consider using this information to highlight to customers through their bills the comparable cost of a cubic metre of water to other everyday commodities to promote improved awareness.

Overall, our customers trust us; so we must build on that trust by offering practical help. We must also work with local authorities and parish councils who are well placed to offer support.

4. Conclusions

- Levels of customer debt have continued to increase across the Affinity Water regions during the period 2007/08 to 2011/12
- We have been sharing and implementing good practice on billing and collection of debt for many years.
- The limited tools that companies can use to recover debt, following the ban on disconnection in 1999, and the strong regulatory incentives for companies to manage debt effectively, mean that individual companies are continuously seeking ways to improve their performance through learning from others.
- We have a uniform distribution of recovery of costs of bad debt. This applies whether customers are business customers or domestic, rural or urban, single or multiple occupiers. As a result it is not possible to say, with certainty, that one group of customers subsidise more than any other.
- As part of our business planning process we will consult with customers about the possible future paths of water prices that will expose the key drivers of prices, including bad debt charges, and the effects of our plans to improve management of bad debts.

- Ofwat promote a measure of risk of being unable to afford water bills as being households where the water and sewerage bill accounts for more than 3% of income after housing costs.
 - In our area, 1 in 6 households or 17% of households are within this category
 - Affordability risks are concentrated amongst households with a single adult, whether that adult has children (1 in 3), is without children (1 in 4) or is a single pensioner (1 in 4).
- We are considering introducing a social tariff to help the least well off. We need to discover whether a social tariff would have support from customers, and also to what extent customers would be willing to pay more for water to subsidise other customers.
- In looking at water metering proposals, we will take into account the issue of affordability as well as the opportunity to provide practical help and encouragement to customers to be more water efficient.
- Education is the key to encouraging customers to use less water and become more efficient and we take every opportunity to provide practical help and advice on how customers can save water.

Appendix A: Background information on company tariffs

Regulatory process

In January each year, and after consultation with CC Water, we propose our tariff plans to Ofwat in our Charges Scheme. Our Board certify the Scheme as being consistent with our price control; Ofwat's published charging guidelines and all other legal and regulatory rules relevant to water charging. We may not commence charging at the new rates until Ofwat have approved our charges.

Ofwat takes a risk based approach to approval, for example, using a straightforward and simple approval for low risk cases, but subjecting company's charging plans to greater scrutiny if its Board have not been able to certify fully compliance or have otherwise highlighted compliance risks. This is an evolution from the previous system where Ofwat thoroughly scrutinised each company's proposals, regardless of its views on compliance risk. Ofwat provides its approval in a formal letter, usually at the end of January.

Tariff setting

Tariffs for customers using less than 50,000m³/year are subject to a price control formula which limits the rate of change in tariffs to the inflation rate (RPI) plus or minus an adjustment factor, K per cent. Last year for example, the inflation rate was 5.16% and the K factor in Affinity Water's Central area was minus 2.8%, so the average price increase was 2.36%. K factors are fixed for the 5 years ahead, by Ofwat at its five-yearly price reviews.

To demonstrate compliance with the price control formula, we prepare and submit the Principal Statement in January each year. The Principal Statement is an Ofwat spread sheet which we complete with each of the water supply tariffs we offer. It calculates the weighted average percentage increase in tariffs between the current year and those proposed for next year. The weighted average charge increase must not exceed the increase fixed by the price control formula and the Principal Statement demonstrates that this is the case.

Whilst meeting the charges limit, we do not have to increase each tariff uniformly, for example we could increase tariffs for business customers faster than the formula, provided we offset this by not raising domestic tariffs as quickly. What matters for regulatory compliance is the overall average increase.

In addition to the price control formula, tariffs have to be set so that there is no undue discrimination or preference. This is usually interpreted as meaning that tariffs must broadly reflect the costs of supply. This feature of tariff setting is most in evidence in the balance between measured and unmeasured tariffs where we set tariffs to meet the tariff differential rule. This says that we should set measured and unmeasured tariffs such that a measured customer who happens to use the same volume of water as the average unmeasured customer, will have a bill that exceeds the average unmeasured bill only by the annualised costs of providing and operating the meter.

- Measured tariffs comprise a £/year standing charge which covers the "per customer" costs of supply, and a volumetric rate per cubic metre of consumption recorded on the meter.
- Unmeasured tariffs comprise a £/year standing charge, and a rate poundage charge, which is payable per £ of rateable value (RV) set for the property. Rateable values originate in the local government taxation system used prior to

1990 and are notional rental values attaching to each property. Other things being equal, larger properties have higher RVs than smaller. Whilst local authorities discontinued RV based taxation in 1990 and the system is anachronistic, our preference is for metering and unmeasured customers are welcomed to be metered instead, free of charge.

Most commercial customers are metered and pay the same tariffs as domestic customers. The remaining small numbers of unmeasured commercial customers pay the same tariffs as domestic customers.

Our largest commercial customers using more than 50,000m³/year can choose to be supplied at our large user tariff. This is lower than the standard rate as large users are connected at 150mm pipe diameters and above. They do not make use of the smaller diameter network assets so the tariff excludes the costs of maintaining and operating those assets. Similarly, mid-users, using more than 3,000m³/year do not make use of the sub 25mm network assets and pay a slightly lower rate than standard.

The table below shows the main tariffs offered by the three predecessor companies to Affinity Water in 2012/13. Differences in the tariff structure reflect the charging priorities and policies of the predecessor companies prior to creation of Affinity Water. Prices differ mainly because of differences in the size of the charging base of the predecessor companies – for example, water consumption is lowest in the East area, so the costs of providing services have to be shared out over a smaller total volume billed. The unit price is therefore higher.

Table: Summary of tariffs offered by Affinity Water Ltd

	Central	East	Southeast
Household measured standing charge (£/year)	30.00	26.40	35.28
Household volumetric rate (£/m ³)	0.9763	1.6442	1.5703
Household unmeasured standing charge (£/year)	41.64	38.64	65.40
Household rateable value (£/£RV)	0.5581	1.0110	1.4496
Standard commercial volumetric rate (£/m ³)	0.9763	1.6442	1.5703
Mid-user rate (£/m ³)	0.9008	1.6442*	1.5703
Large user surcharge (£/year)	15305	31272	-
Large user volumetric rate (£/m ³)	0.5947	0.8985*	1.1535
<i>* Time weighted average of winter and summer rates on seasonal tariff</i>			
<i>Source : Company Charges Schemes 2012-13</i>			

Version No:	Draft 131112 v2	Final	
Date:	13 November 2012	15 November 2012	
Submitted to:	PR14 Board	PR14 Board	
Prepared by:	Chris Offer	Chris Offer	
Approved by:	PR14 Board	PR14 Board	
Reference:	0001	0001	
Date to Chair CCG		16 November 2012	
Accepted by CCG		16 November 2012	

Challenge Record

Number/reference: 0002	Date: 03 December 2012
Raised by: CCG	Subject area: Leakage
Due by date: not set	

The challenge: Leakage

Challenge:

Ofwat has asked water and sewage companies to make a step-change in their approach to leakage. Ofwat is motivated, in part, by consumers' belief that the current rate of leakage is unacceptable and acts as a barrier to customers adopting more water efficient behaviours. (It needs to be noted that this has not yet been evidenced in Affinity Water's focus groups on WRMP) Further, anecdotal evidence suggests that consumers cannot accept the economic cost of leakage rationale.

Ofwat is also clearly looking to individual companies to devise strategies, appropriate for their specific context that can be demonstrated to have their customers' support. Taking the opportunity for a complete rethink of the issue of leakage, how should Affinity Water address these expectations?

Expectations:

Affinity Water will propose a strategy for addressing leakage that is acceptable to its customers and to the statutory bodies.

Customer research findings and consultation responses should be used to confirm customers' views on leakage and the priority given to this issue. AFW should address this in the development of the demand management strategy contained in its WRMP (which will be released for public consultation next spring).

Specific points to be addressed:

How will Affinity Water :

- engage with customers on the topic of leakage
- articulate the current basis for setting the level of investment in this area and potential costs to customers if a lower level of leakage was proposed (given that many customers may assume that the costs of reducing leakage should be financed by the value of the water saved, or funded by the company by reprioritising other potential investments)

- proceed if the outcome to willingness to pay research suggests further funding will not be forthcoming what alternatives might the company consider (alternative funding or possibly alternative leakage strategies)?
- raise customer awareness to the leakage issues including the current target and company performance against this; current leakage policy and activity more generally?
- help customers with supply pipe leakage?

RESPONSE from Affinity Water

1. Introduction and context

We see the CCG having a key role in judging if we are promoting an appropriate approach for leakage reduction.

Leakage reduction is an integral component of our strategy for meeting the outcome of making sure our customers have enough water. As such, we are not proposing a separate strategy for leakage reduction. While we recognise that customers may see current levels of leakage as unacceptable, we believe that our strategy must be to take a balanced approach because relying solely on high levels of leakage reduction presents significant risks to customers if these cannot be achieved in a sustainable and cost beneficial manner.

We have set out for consultation in our draft Water Resources Management Plan (dWRMP) how we plan to meet the outcome of making sure our customers have enough water over the next 25 years. Our Preferred Plan includes a balanced range of options to:

- **Reduce leakage** across most of our water resource zones;
- Assist customers to **reduce domestic consumption** by minimising waste and using water wisely;
- Continue to **extend household metering** as a fair means of charging and to reduce demand;
- Make **best use of our existing water supplies**;
- Continue to **work with our neighbouring water companies** in providing cross-border water transfers.

Our Preferred Plan will result in substantial changes to our operations and carries additional risk which means it is essential we work in partnership with our customers to reduce water consumption through leakage reduction, compulsory metering of most households by 2020 and water efficiency initiatives. In the five years from 2015 to 2020 we expect our Preferred Plan will achieve:

- A saving of **20MI/d** in leakage at a cost of £11.3 million.
- Over **36MI/d** of demand reductions from compulsory metering by automated meter reading in five of our six water resource zones in the Central region; the total cost for metering in all of our regions is £95 million.
- Around **4MI/d** from water efficiency, in addition to the benefits of the combined domestic metering and water efficiency programme; this will cost £5.1 million.
- An extra **1MI/d** from our existing licences, by increasing the amount we abstract without causing damage to the environment. These options also give us an extra 8MI/d during peak conditions at a cost of £2.2 million.

- An additional **21Ml/d** of water that we will buy from our neighbouring water companies to make sure we have enough to meet the needs of our customers, rising to 31Ml/d during peak conditions. This will cost £12.9 million.

2. Engagement with Customers and Stakeholders

We recognise that customers see current rates of leakage as unacceptable and this may act as a barrier to customers using less water. We have therefore ensured in all our communications with customers we make a clear commitment to reducing leakage as the first plank in our strategy. We understand that we need to communicate effectively how we plan to balance leakage reduction with other measures so we can:

- ensure our customers continue to have enough water
- provide value for money for customers and
- prevent the inefficient use of resources and so reduce the impact of abstraction on our local environment.

We are seeking customer views on leakage reduction through a range of consultation processes including:

- publication of our demand management strategy in our dWRMP on our website and advertising through the media (consultation period between 17 May and 12 August 2013)
- writing to and meeting key stakeholders
- focus groups
- deliberative forums including environment groups
- on-line panels
- willingness to pay survey
- service measure cost benefit survey
- our draft Business Plan consultation (July 2013)

We will take account of stakeholder views on our approach to leakage reduction in our Statement of Response to the Secretary of State on our dWRMP stating how our Final WRMP has been informed by those responses.

Our objective is to demonstrate customer support for our strategy and priorities, CCG endorsement and regulator approval of our plans. Feedback from each of these stakeholders during the dWRMP and Business Plan consultation process is therefore a key element in refining our strategy.

In the following sections, we set out the factors influencing our approach to leakage reduction, how we are selecting future targets for leakage and how we will communicate our plans and take into account their views.

3. Impact of sustainability reductions, climate change & population growth

Our dWRMP, which supports one of the outcomes for our Business Plan of making sure our customers have enough water, is strongly influenced by the need to support the policy objectives of DEFRA and the Environment Agency for restoring sustainable abstraction.

Following extensive dialogue with the Environment Agency, we have agreed a

reduction of 77 Ml/d (6% of our resource base) to be included in our baseline supply demand balance. This requirement:

- generates a substantial water resources deficit; and
- strengthens the economic case for demand side measures including leakage reduction and compulsory metering coupled with water efficiency.

4. How we have modelled the options for leakage reduction

The leakage options considered during our econometric modelling work were constrained:

- to those within a reasonable range of confidence of the current cost of leakage reductions and
- to ensure a balanced combination of demand management and supply side options in our Preferred Plan.

The costs of reducing and maintaining leakage at far lower levels than we are now, become more and more uncertain as the target level of leakage reduces. When modelled (compared) against metering and water efficiency, leakage is always selected and we know this to be unrealistic and a weakness in our modelling approach. We therefore think the above is the correct balanced and sustainable approach. This approach also meets Government aspirations and our objective of working with our customers to reduce consumption and so reduce the impact of abstraction on our local environment. Although we use UK Water Industry Research (UKWIR) best practise approaches when forecasting leakage costs we are committed to improving our understanding of true costs when we operate at lower levels of leakage

As our Preferred Plan includes leakage reductions that are constrained, we will be closely monitoring the actual cost of reducing leakage during 2015 and 2020 and we have put in place new systems to do this. This will ensure any decision to reduce leakage beyond 20 Ml/d is based on a clear comparison of cost compared to other supply or demand side options.

Our plan will therefore remain flexible in accordance with DEFRA requirements. We will review our investment programme on a progressive basis, so that if further leakage reduction beyond 2020 is the least cost option to balance supply and demand, compared with other investments, we will implement these as a priority at that time.

5. How we are setting our targets for leakage

We have taken account of sustainability reductions, climate change and population growth in our work with other companies under the Water Resources in the South East (WRSE) project and in our own econometric modelling. Both WRSE and our own assessments have selected leakage reductions options based on costs derived from Economic Level of Leakage (ELL) and Sustainable Economic Level of Leakage (SELL) assessments.

SELL is the level of leakage at which our costs and other external costs, are the lowest. The SELL calculation includes all costs and benefits associated with different

levels of leakage, **including environmental and social ones**. Operating at SELL means the total cost to the company, customer and society of supplying water is minimised and that we are operating efficiently.

We are planning to set targets for leakage levels over the next 15 years which are lower than SELL.

The CCG challenge suggests customers may not accept an ELL or SELL but also that customers may assume the cost of reducing leakage should be financed by the value of water saved - which is in itself an economic position. In normal operational terms the cost of reducing leakage together with the cost of producing water is minimised.

In order to remain below an upper limit for leakage in all conditions, we will need to control leakage to much lower levels during benign weather periods. Equally, we may need to reduce leakage in drought conditions to meet the expectations of our customers. Under both of these transient conditions, leakage operations may be sub-economic. Having a flexible approach to leakage may also conflict with DEFRA's aspiration that leakage should not rise; however, we consider this will be necessary at times to be able to adapt to seasonal and annual weather conditions, whilst seeking to be as efficient as we can in our operations.

We will ensure a continually reducing leakage level through the careful monitoring and response to leakage outbreaks and the natural rate of rise of leakage encountered together with controlled implementation of leakage reduction measures from one leakage level to another.

The CCG also suggested customers would expect further leakage reduction to be achieved or funded by the company by reprioritising other potential investments. As indicated above this could be done but in the short term (2015 to 2020) this would impact on the need for metering and water efficiency measures and this would not meet broader government objectives of reduced consumption. In the longer term (post 2020), we recognise there is a place for prioritising further leakage reduction and we will review our plans and commit to that when we are able to be confident that this is the least cost approach compared to other supply side measures.

6. Our consultation with customers about leakage reduction

The starting point for our consultation with customers about leakage reduction between 2015 and 2020 will be to set the wider context of the challenges we face over the next 25 years from sustainability reductions, climate change and population growth. We are explaining how our approach to leakage fits within a balanced set of measures which will allow us to:

- ensure customers continue to have enough water
- provide a value for money service and
- support the policy objectives of DEFRA and the Environment Agency for lower per capita consumption and restoring sustainable abstraction

We are explaining to customers and stakeholders that for the five year period 2010 to 2015, we have planned our investment for leakage control to ensure we achieve the targets set by our economic regulator. We will explain how we have performed against those targets.

We are indicating through our dWRMP and Business Plan consultation that our Preferred Plan includes a reduction in leakage of 20 MI/d between 2015 and 2020. This will mean that we are proposing to spend more on repairing pipes to reduce leakage beyond the level which is the most cost effective to achieve and maintain.

We will set out for customers the indicative impact on bills for three different leakage reduction scenarios (including our Preferred Plan) so that customers can indicate their preferences.

As indicated above, we have a range of activities in hand and are consulting with customers over their views on leakage and other investments in our Preferred Plan for the dWRMP.

We also recognise there is an “emotional level of leakage” for customers, in particular in drought. We are therefore seeking customers’ and stakeholders’ views on how flexible we should be in setting our leakage target and if this should take account of weather conditions such that lower levels of leakage would be reached should drought restrictions be implemented in future or higher leakage would be allowed when there is a surfeit of local resources. We will also explore the appetite for alternative leakage performance measures such as ‘repair 95% of all visible leaks within 24 hours’ as customers may be more satisfied with an operational measure of leakage performance.

In particular we are carrying out a quantitative survey on leakage in July using our on-line customer panel. We are consulting on a range of leakage issues including:

- the specific proposals in our Preferred Plan
- options for higher and lower leakage targets linked to levels of service options and
- the effect on bills from the alternative investment plans

This issue is explored in our sensitivity tests in Figures 28 and 29 (page 100) of our dWRMP.

7. Willingness to pay

The CCG have asked us to consider alternative plans and funding if customers indicate they are not willing to pay for leakage reductions. If there is no customer support for leakage reductions then we would only pursue leakage reductions where this is least cost. If some stakeholders such as regulators or the CCG consider further leakage reductions are warranted in the absence of wider customer support then we would seek to verify and agree the wider cost-benefit case for these reductions in order to justify such a strategy to our wider customer base.

In terms of funding, at this stage we do not envisage any alternative sources if costs are not included in the charges customers pay. We recognise there is a perception with customers that ‘shareholders should pay for leakage’. However, whilst it may be possible to secure shareholder investment for leakage reductions this investment will be repaid at some future point and thus in overall terms this is not ‘free money’. We seek CCG support and challenge as to the best way of explaining this issue to our customers to minimise any misconceptions over funding and the charges they pay.

8. Helping customers with supply pipe leakage

We have also recognised the need to support customers over supply pipe leakage. In particular we are considering what support we should offer to customers when installing meters. Our experience in our Southeast Region is that customers value support for supply pipe repairs at the time of meter installation. We expect to confirm our proposals in our Business Plan submission to Ofwat and our Final WRMP and are mindful of the recent consultation by DEFRA on possible legislative changes providing for the adoption of supply pipes by water companies.

9. Provision of Information

We agree it is important in future to make our performance on leakage more visible to customers. We are exploring how to do this in a number of ways - for example through our Service Delivery Map project which is developing new tools to monitor operational and asset performance at both company and zonal (community) level. This could be reported monthly on our website in future. We are also proposing to include leakage as one of our core measures of success of meeting the outcome of making sure our customers have enough water.

In light of the challenge by the CCG we will publish additional information specifically on our approach to leakage reduction and we will also publish operational information on our current target and leakage performance and activity.

We will update the CCG further on completion of our July online panel survey.

Mike Pocock, Physical Assets Manager

Date: 12 July 2013

Passed to / date: Robin Dahlberg 12 July	Clarifications:
Accepted by / date:	

Response

All responses will be clearly identifiable and traceable and will append the following table.

Version No:	1 draft	2 Final	3 Final post CCG meeting 24 July
Date:	19 June	12 July 2013	1 August 2013
Submitted to:	PR14 Board	CCG	CCG
Prepared by:	Mike Pocock	Mike Pocock	Patrick Campbell
Approved by:	Stephen Martin	PR14 Board	PR 14 Board

Reference:	Draft	Final	Final, revised
Date to Chair CCG		12 July 2013	1 August 2013
Accepted by CCG			

Challenge Record 0003

Number/reference: 003 / 004	Date: 9 April 2013 Superseded: 8 July 2013
Raised by: CCG	Subject area: Investment options, willingness to pay and bill level acceptability
Due by date: to be agreed	Date: 18 September 2013

The challenge: Investment Options / Willingness to pay / Acceptability of proposed bill levels

Challenge:

How will Affinity Water (AW) consult with domestic and commercial customers to determine their preferences and willingness to pay for alternative investment options and/or possible service enhancements? How will Affinity Water determine their customer's acceptability of proposed bill levels including their overall water and sewage bill in the period 2015 - 2020?

Expectations:

- a) AW should demonstrate that its research includes representative samples of both domestic and commercial customers.
- b) AW should demonstrate how the value it places on the outcome from investments has arrived at and has been validated.
- c) AW should demonstrate that the investment options do not result in any undue cross-subsidies between commercial customers and domestic customers.
- d) AW should demonstrate that it has explored all investment possibilities including those that could result in reduced or static bills for customers. These may be the preferred options in the current economic climate.
- e) AW should demonstrate how they have consulted with customers in a transparent manner, showing how a water bill consists of various components including not only the cost of supplying clean water and the proposed investments/service enhancements but also debt financing, tax, profits, avoided costs and efficiencies.

Specific points to be addressed:

- f) AW should demonstrate that it has engaged with customers both commercial and domestic who are reliant on a constant/consistent source of water
- g) AW should test the assumption that its current customers are willing to pay to secure resources for future customers.
- h) AW should be transparent about the assumptions it makes on variables such as cost of capital which Ofwat will determine and is likely to advise after this research has been undertaken.

- i) AW should keep in mind and inform the CCG about the implications of such assumptions being significantly off target/not materialising.
- j) AW should consider whether it is prudent to test for more than one 'Ofwat scenario' and explain its decision on how to deal with this issue to the CCG.
- k) AW should validate any monetised value they place on costs or benefits when assessing investment options.
- l) AW should demonstrate how it has they offered customers competing choices to establish customers' preferences.
- m) AW should demonstrate that any proposed price adjustments to customers in the east (Brett) and south-east (Dour) communities have taken into account and returned to customers the cost savings/efficiencies resulting from unification.
- n) AW should inform the CCG on how it intends to communicate these savings/efficiencies to the customers in Brett and Dour.
- o) AW should demonstrate how the consultation processes were applied to both domestic and commercial customers and all representative organisations and stakeholders.
- p) AW should demonstrate how the research has been put in context for customers in respect of the expected increases in sewage charges by Thames and possibly Anglian.
- q) AW should consult with Anglian and Thames and inform the CCG as to what the sewage charges are likely to be in the period 2015-2020.
- r) AW should demonstrate that respondents to this research have been reminded that their water bill and sewage bill should be regarded in the context of other household expenses and expectations of financial security.

RESPONSE from Affinity Water

Executive Summary

In developing our draft Business Plan consultation and moving towards our final Business Plan, we have undertaken a significant amount of customer research with both household (domestic) and non-household (commercial) customers to determine;

- their preferences and Willingness to Pay for alternative investment options
- their preference for possible service enhancements
- the level of customer acceptability for future bill levels; and
- if customer acceptability for future bill levels is influenced by considering the overall water and sewerage bill in the period 2015-2020.

Representation has been given from all customer groups and stakeholders and both qualitative and quantitative activities have been undertaken, including;

- **‘Have Your Say’ discussion forum** hosted on our website to capture both qualitative and quantitative feedback on our plans plus an interactive questionnaire to gain specific feedback on primary documents, including Investing for Your Community and our Strategic Environmental Assessment scoping report.
- **Postal consultation** with stakeholders. Almost 1000 letters to statutory consultees, regulators and representative bodies, inviting feedback on our Investment for Your Community consultation.
- **Drop-in events.** Ten drop in events across our communities to offer customers the opportunity to ‘drop in’ and discuss any aspects of our plans.
- **Focus groups.** Ten independently run focus groups seeking feedback on our plans that included both household and non-household customers as well as environmental stakeholders.
- **Online panels.** An independently operated panel of 2,000 customers across our communities, reflecting our customer profile that is used to explore key issues arising from all sources of consultation.
- **Environmental forums.** Giving voice to the views of environmental groups representative of customers and government bodies impacted by our operations.
- **‘Lets Talk Water’ large scale multimedia campaigns** with the aim of reaching as many customers as possible. The output provides high volume snap shot views from customers. A large scale communication campaign called ‘lets talk water’ ran from April to September 2013 which involved getting customers to complete a standard questionnaire.
- **Deliberative forums.** Independently facilitated events providing opportunities to explore issues in more depth with large groups of customers. The qualitative output is supported by individual voting, on specific issues providing indicative, quantitative feedback of the preferences of the audience.
- **Quantitative Willingness to Pay and Acceptability Testing research.** To understand customer preferences, estimate customer benefit valuation and customer acceptability of potential changes to bill levels and levels of service.

The information and insight received from these activities has helped us to develop and support consultation on our draft Business Plan, which set out our Proposed Plan for 2015 to

2020, alongside two alternative plans – showing a slower pace of investment and a faster pace of investment. This enabled customers to decide if our Proposed Plan will achieve the right balance between the service we provide, the price we charge and the pace of our investment.

We have undertaken extensive Willingness to Pay and Acceptability Testing research carried out by a specialist third party, using industry ‘best practice’ guidance. The output from the Willingness to Pay work has enabled us to assess the value that customers place on each water service attribute. This information is then used to inform our Cost Benefit Analysis (CBA) so that investment decisions include the assessment of customer benefit valuation.

We are using CBA to allow us to compare the pros and cons of making investment decisions so that we can develop the combination of investment solutions that will give the largest overall net benefit including customer benefit valuation. We are using an investment optimisation software tool called PIONEER to implement CBA at an investment programme level. We are also using Acceptability Testing as an overall test of our investment proposals.

This research has allowed us to develop our first draft final plan demonstrating how customer engagement and research has been used to challenge and influence the balance and content of the Proposed Plan upon which we consulted.

This response provides further detail on the process that has been followed to date and addresses all aspects of the challenge raised by the CCG in addition to the principal expectations set out immediately below:

Expectation 1: Representative Samples of Customers

The WTP study included both household (no. 1,209) and non-household customers (no. 508), with quotas set for both. Household quotas are set by age, gender and SEG (based on 2011 Census data). Non-household quotas were set by the industrial classification based on ONS data. All participants were randomly selected. The Acceptability study also covered both household and non-household customers (no. 1,200 per phase).

Expectation 2: Deriving the Values Placed on Outcomes

In order to value the outcome from investments we asked customers, as part of our early stated preference research, about aspects of service that they regard as important. This drove the selection of a number of water service attributes that formed the basis of the WTP study and the service measure framework. This approach enabled all investment options to be articulated in performance terms and in terms of value to customers. We have also carried out acceptability research to understand how much customers want service (and therefore bills) to change. This makes sure that the business plan does not contain service improvements that customers either do not value, or value but either cannot afford or do not find acceptable.

Expectation 3: Demonstrating no Undue Cross-Subsidies

The investment options we have considered in developing our proposed plan, and which form the basis of our dWRMP, are investments that will ensure we deliver the four high level customer expectations we set out in our SDS. These customer expectations do not differentiate between non-household (commercial) and household (domestic) customers and so will not lead to any undue cross subsidy between these two groups of customers.

Expectation 4: Exploring all Investment Possibilities

In developing our draft Business Plan consultation, we have set out our Proposed Plan for 2015 to 2020. Alongside this, we present alternative levels of future investment so customers can decide if our Proposed Plan will achieve the right balance between the service we provide, the price we charge and the pace we of our investment. The alternative levels of investment consider a range of investment possibilities that could result in static, higher or reduced bills. The WTP survey includes increases in service/bill and decreases in service/bill.

Expectation 5: Ensuring Transparency

We have ensured that all expected costs for each investment plan are included in the bill presented to customers. The bill impact is the revenue required from each customer for the proposed changes and thus includes debt finance, profits, tax and avoided costs and efficiencies. We have presented this information to customers in our deliberative forums and Strategic Direction Statement by showing where each pound of a customer bill is spent on average. We have not explicitly listed out these components of the bill for the purposes of WTP or acceptability testing. Customers are only asked to consider total changes in bill and associated levels of service.

Efficiencies are explicit in the survey. Cost of finance efficiency is included in this. The approach we have adopted is in line with Ofwat Acceptability testing of the draft business plan in PR09 and also meets the CC Water expectations as set out in the paper “CCWater’s expectations on water companies’ testing of customer views on acceptability of their Business Plan for the 2014 Price Review”.

1. Introduction and context

We are clear about the importance of the CCG's role in challenging us around the development of our business plan and investment proposals. We understand it is essential that we are able to show clearly how we have consulted with household (domestic) and non-household (commercial) customers to determine:

- their preferences and willingness to pay (WTP) for alternative investment options;
- their preference for possible service enhancements;
- the level of customer acceptability for future bill levels; and
- if customer acceptability for future bill levels is influenced by considering the overall water and sewerage bill.

Related issues

In order to address each aspect of this challenge we will need to cover a range of issues that have been presented and discussed at earlier CCG meetings. These include:

- explaining the difference between stated preference research and acceptability testing
- explaining the application of cost benefit analysis (CBA) and the implementation of investment optimisation, which we are doing through the use of a modelling tool called 'PIONEER', and
- describing the full range of engagement activities we are undertaking that will inform the development of our final plan.

We will also describe the process we have followed in developing our 'Proposed Plan' that we are using for consultation with customers. We also explain the process we are following to show how customer engagement and research has been used to challenge and influence the balance and content of the draft final plan.

The remainder of this challenge response is structured in the following way:

2. customer research
3. implementation of CBA and investment optimisation
4. stated preference research (otherwise known as WTP research)
5. acceptability testing
6. engagement activities
7. business plan consultation
8. first draft final plan
9. Next steps

Where possible we have referenced materials previously presented to the CCG and included these as appendices to this challenge response. We have also included technical supporting information as additional appendices as necessary.

2. Customer research

Qualitative research

The majority of our customer engagement activities, previously shared with the CCG and set out in more detail later in this challenge response, are qualitative. This is where we seek customer views and opinions from individuals and groups of customers. This feedback is representative of customers' views, as quotas are set for targeted research, but it will not be statistically robust. This type of research is used to understand customer perceptions and priorities.

Quantitative research

Our quantitative customer research is designed to produce statistically robust data that is representative of our customer base. This research is carried out across large numbers of customers and covers both stated preference research, known as willingness to pay research, and acceptability testing. These quantitative customer research methods are described in more detail below. In addition we have also established an independently operated online panel of 2,000 customers across our three supply regions with a sample group that reflects our customer profile so we can generate statistically significant quantitative responses to questions we post.

At the January CCG meeting we gave a presentation covering WTP. The presentation explained that the term 'Willingness to Pay' is often used to describe two distinct approaches to assessing customer support for investment proposals. The two approaches are:

- 'stated preference research' used to understand what customers find important and to value the benefit of investments by assessing customers views; and
- 'acceptability testing' of overall bill levels and/or changes in bill levels from a range of investment proposals. The January CCG presentation is attached as Appendix A.

The distinction between quantitative and qualitative customer research is important because of how they will be used to influence the development of our final business plan. The qualitative research will be used to benchmark and cross reference the results of the quantitative work.

How we balance the range of research results will be a key challenge for us. We are developing a framework to allow us to take multiple stakeholders and customer views and synthesise them into a set of findings that can be used to influence, inform and provide insight for the development of our final business plan. The framework we have developed has been reviewed and challenged by third party advisors to ensure that it is fit for purpose and is able to accommodate stakeholder and customer views as described.

The quantitative research will help determine both the relative preferences of customers between different investment options and possible service enhancements as well as the overall level of customer acceptability for future bill levels. The relative preference of customers, expressed through stated preference research, is a key input to our approach to CBA and investment optimisation.

3. Implementation of CBA and investment optimisation

Cost benefit analysis (CBA)

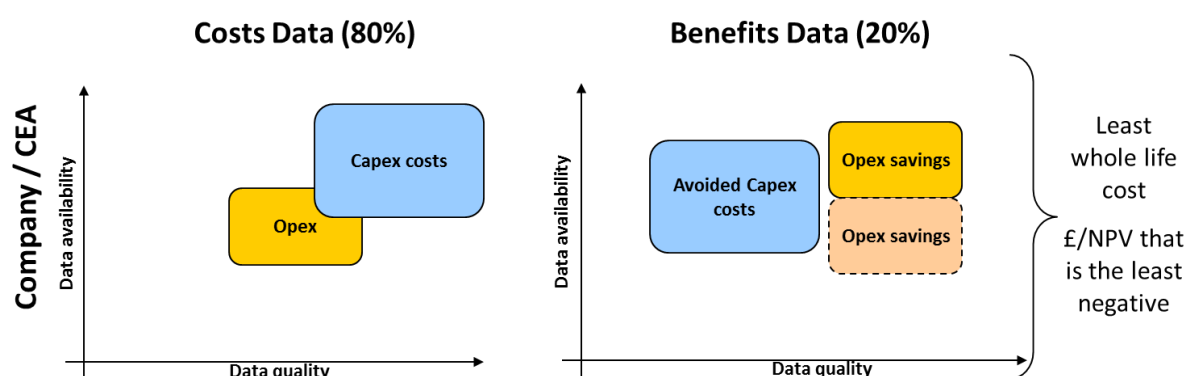
CBA is a structured way to compare the pros and cons of making an investment decision. The principal objective of CBA is to facilitate the comparison of the pros and cons of an investment decision using a common measure, which is money.

Traditional financial appraisal of an investment decision considers the costs of an investment, understood and measured in terms of operating expenditure and capital expenditure, while benefits might take the form of additional revenue or avoided costs. The case for investment is clear where the benefits are greater than the costs or where there is a net benefit in monetary terms. This type of appraisal is known as cost effective analysis.

CBA applies the same decision rule as the traditional financial appraisal, i.e. the case for investment is clear where the benefits are greater than the costs. However, CBA is informed by the monetisation of all impacts on the economic welfare of those affected by an investment decision. In other words, the investment decision takes account of a much wider range of pros and cons than traditional financial appraisal. For example, CBA is likely to consider the environmental factors such as carbon and green house gases, or importantly customer valuation of benefits such as the taste and smell of water, leakage or supply interruptions. It is this explicit consideration of customer valuation of different water service attributes that places customer preference at the heart of investment decision making. The service attributes we use are described later in this challenge response under the service measure framework and are illustrated in Diagram 3 in the section 'How we have implemented CBA'.

The difference between cost effective analysis and CBA is illustrated in the diagrams below. Diagram 1 illustrates the approach taken and the data used under cost effective analysis. This type of analysis does not capture the wider benefits of an investment that CBA does include. When this type of appraisal is applied to water investments it is rare that the result is a positive net benefit as only a limited range of quantified benefits are included in the assessment. In the past the chosen investment option was the one that was assessed as being the least cost over the whole life of the project.

Diagram 1: Cost effective analysis



Note to Diagram 1 and 2:

- It is standard practice when undertaking financial and economic appraisal to assess current and future costs in terms of net present value (NPV). This approach discounts future costs and benefits to allow for the time value of money so all costs and benefits can be compared on a consistent basis.
- Cost data is shown on the left hand side of the diagram and benefit data is shown on the right hand side. We have

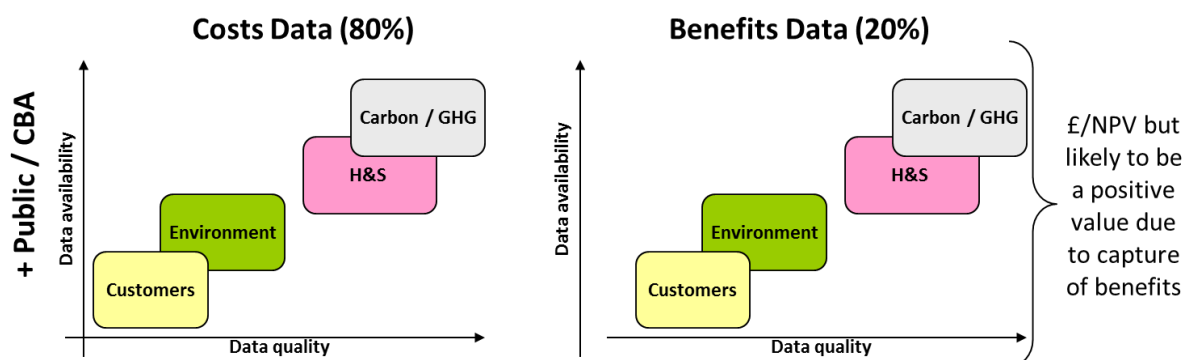
made an assessment of the balance between cost and benefit data 80:20 to illustrate the relative influence of the data on the overall assessment

- The diagram illustrates the relative quality and availability of data. Information to the top right hand side indicates this is high quality data and easy to come by.

An example of cost effective analysis could be water treatment to tackle a water quality issue. There will be a range of investment solutions to tackle the water quality issue each with different investment costs made up of capital and operating expenditure. Under cost effective analysis the chosen investment solution would be the one with the lowest overall investment cost, assessed over the whole life of the assets constructed to tackle the water quality issue. The benefit, to end customers, of tackling the underlying water quality issue is not considered in the choice of investment solution. The wider environmental costs and benefits of different investment solutions would also not be part of the decision making process.

When the full economic benefits of the investment options are considered, illustrated in Diagram 2, in addition to the existing cost and benefit data from the cost effective analysis it is possible to prioritise investment options on the basis of those that do provide the biggest net economic benefit.

Diagram 2: CBA



We can use the results of CBA to select and schedule projects so we can maximise the value of every pound of investment. CBA can be used to demonstrate whether the total benefits provided by an investment programme or a single project justify the cost of delivering those benefits. It is therefore possible that uneconomic projects may be components of an overall programme considered to be cost beneficial. This type of analysis, at a programme level, allows us to optimise the programme. We have implemented an investment optimisation software tool (Pioneer) which enables us to do this for the majority of our capital maintenance investment expenditure.

It is important to note that CBA is only one part of the business case and that it needs to be used alongside other evidence to inform the decision making process. It is not a decision making tool that is used in isolation. For example, an investment may be required to meet a legal requirement or obligation and would be included in the investment programme on these grounds.

Assessing investment costs and benefits

The process of assessing investment costs and benefits used in a CBA is very important. Clearly, better information results in a better assessment. The CCG, as part of this challenge have asked two specific questions in this regard:

k) Affinity Water should validate any monetised value they place on costs or benefits when assessing investment options (cost); and

b) Affinity Water should demonstrate how the value it places on the outcome from investments has been arrived at and has been validated (benefits)

Costs

Understanding cost information has always been a critical business process. Challenging the cost of investment solutions was a main point of emphasis for Ofwat at past price reviews through the use of comparative efficiency assessments. Cost assessment remains a key regulatory challenge and the price setting framework for PR14 contains several strong incentives to ensure companies provide realistic, challenging and efficient cost assessments. One of Ofwat's four key areas of its risk based review of company business plan is cost.

Our approach to validating cost information is embedded into our approach to asset management and delivery. We record cost information from completed schemes and projects and use industry benchmark data so that we have unit cost models that provide valid actual historical costs that can be used to price future investment schemes.

Benefits

Benefits are either expressed as cost savings, as explained above under the cost effective analysis, or are assessed through a robust WTP stated preference exercise that aligns with best practice and is subject to robust peer review by leading academics. The WTP study also provides indications of the maximum level of bill increase for customers and therefore within which the WTP is valid.

In order to value the outcome from investments we asked customers, as part of our early stated preference research, about aspects of service that they regard as important. This drove the selection of a number of water service attributes that formed the basis of the WTP study and the service measure framework. This approach enabled all investment options to be articulated in performance terms and in terms of value to customers. We have also carried out acceptability research to understand how much customers want service (and therefore bills) to change. This makes sure that the business plan does not contain service improvements that customers either do not value, or value but either cannot afford or do not find acceptable.

We provide more information on the service measure framework and our approach to WTP research and acceptability testing below.

How we have implemented CBA

For the last price review in 2009, we developed our approach to investment planning so that we were able to carry out CBA on our investment plan. This approach was consistent with other water companies and Ofwat's expectations. Before that price review Ofwat published a Regulation Director letter (RD 04/06) in which they stated;

"We want to see companies providing consistent best value in the service they deliver to consumers and the environment. This means that companies need to take account of both the costs and benefits and to consider both capital and operating expenditure, across base service and enhancements, in an integrated and coherent manner."

Since 2009 we have worked to develop our approach to CBA to ensure consistency with best practice guidance issued by United Kingdom Water Industry Research (UKWIR). In particular, we have refined and developed the measures of our service that we use to

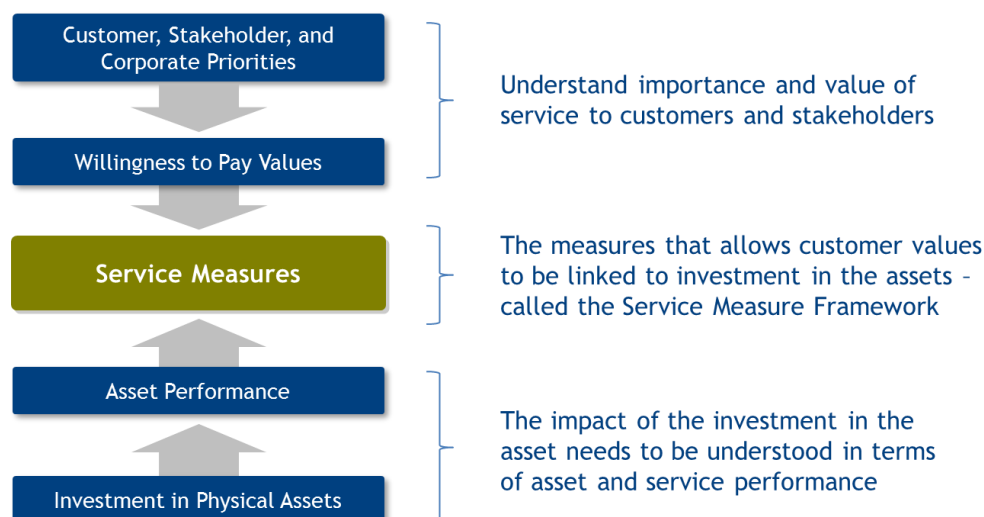
assess customer priorities that can be linked to assets and investment decisions. This process was explained to the CCG in May by Lisa Gahan from ICS consulting. The May CCG presentation is attached as Appendix B.

The diagram below shows the key relationship between customer priorities and investment decisions and the role of the service measures. The service measure framework we have adopted is how customer valuation for each water service attribute is taken into account in investment decision making.

The set of measures has been established through engagement with customers and stakeholders, our prior experience and lessons from the PR09 price review, regulatory requirements and through industry guidance issued by UKWIR. Critically the service measures reflect a range of attributes of the current service, including those for which it is important to maintain existing service levels. It is not simply a list of attributes which may need to be improved.

Further information on the development of our service measure framework is contained in Appendix B and covered in work we have carried out prior to undertaking our stated preference research.

Diagram 3: Service Measures Framework



We have applied CBA to all future potential investments. Our dWRMP, covering all water resource investment options, is based on extensive analysis and modelling using CBA. The modelling is known as EBSD, otherwise known as Economic Balance of Supply and Demand. Our water quality investments, as set out in our submission to the Drinking Water Inspectorate (DWI) on 31 July, are also based on scheme by scheme CBA assessment. Finally the approach outlined above is used to assess the majority of the remaining capital maintenance programme.

Investment optimisation

As discussed earlier, we can use CBA at a programme level to optimise an overall investment programme. We have implemented an investment optimisation software tool called 'PIONEER' to do this. An overview of PIONEER was presented to the CCG in May by Tim Yearsley and Joe Sanders. The May CCG presentation is attached as Appendix C.

PIONEER assists our analysis by informing us about the combination of investment solutions that will give the largest overall net benefit, subject to a series of constraints that can be applied. These constraints themselves can reflect customer priorities. For example, a key constraint may be the overall impact on bill levels. If we find that a certain change in bill level is a key conclusion from our acceptability testing then we can use PIONEER to inform us about the likely programme of investments that would deliver the largest net economic benefit for the level of bill. Other constraints may be targeted levels of performance. For example, we may constrain the optimisation to ensure that levels of water quality compliance targets are achieved.

Investment optimisation is particularly valuable where we seek to apply more than one constraint. So using the examples above, we may choose to constrain the optimisation to ensure that the levels of water quality compliance targets are achieved and that there is no change in bill level. PIONEER will inform us about the expected programme of investments that will deliver the largest net economic benefit subject to both of these constraints.

At some point, as more constraints are applied, the optimisation becomes more and more difficult to achieve until eventually a solution cannot be found. This is the nature of the constraints that we are likely to want to apply. For example, it is logical that improving service levels, minimising environmental impact, reducing bill levels, reducing delivery and operational risk and maintaining investor returns will be impossible to achieve at the same time.

The key point about the investment optimisation is that this translates both customer preferences, expressed through service measures and CBA, and customer acceptability into an overall investment programme.

Investment options

One final part of investment optimisation is the actual investment options themselves. The CCG, as part of this challenge has asked two specific questions in this regard:

- c) Affinity Water should demonstrate that the investment options do not result in any undue cross-subsidies between commercial customers and domestic customers; and*
- d) Affinity Water should demonstrate that it has explored all investment possibilities including those that could result in reduced or static bills for customers. These may be preferred options in the current economic climate.*

Cross-subsidy

The investment options we have considered in developing our proposed plan, and which form the basis of our draft Water Resources Management Plan (dWRMP), are investments that will ensure we deliver the four high level customer expectations we set out in our Strategic Direction Statement (SDS). These customer expectations do not differentiate between non-household (commercial) and household (domestic) customers and so will not lead to any undue cross subsidy between these two groups of customers.

Static or reduced bill levels

In developing our Business Plan consultation, we have set out our Proposed Plan for 2015 to 2020. Alongside this, we present alternative levels of future investment so customers can decide if our Proposed Plan will achieve the right balance between the service we provide, the price we charge and the pace we of our investment. The alternative levels of investment consider a range on investments possibilities that could result in in static or reduced bills.

The WTP survey includes increases in service/bill and decreases in service/bill. When combined with cost in a CBA assessment, this gives information on whether customers want

static bills or reductions. From customer research to date, customers state they are against bill reductions if they are at the expense of service levels.

Further information is set out in section 7 below. We also set out in section 5 how we have tested the acceptability of potential future changes in bill levels. We now turn to the question of stated preference research that underpins CBA.

4. Stated preference research

Stated preference research is the principal method of carrying out willingness to pay research. Willingness to pay is a measure of value and represents the value of services to customers. We use willingness to pay to provide an estimate of the benefit of changes to service. We express the benefit in £ and treat it, for the purposes of CBA, as money.

Approach to research

The methods we are using are well established. This type of research is a form of market research questionnaire with several stages. These include:

- understanding customer preference and selecting water service attributes to test;
- undertaking stated preference exercises (known as Choice Experiments); and
- modelling the relationship between customers' preferred service levels and their willingness to pay in monetary terms

The stages of the research, the techniques and methods have been subject to considerable academic rigour over the years and take into account industry guidance (UKWIR study). The approach to our research is set out in Diagram 4 below and includes the following key stages:

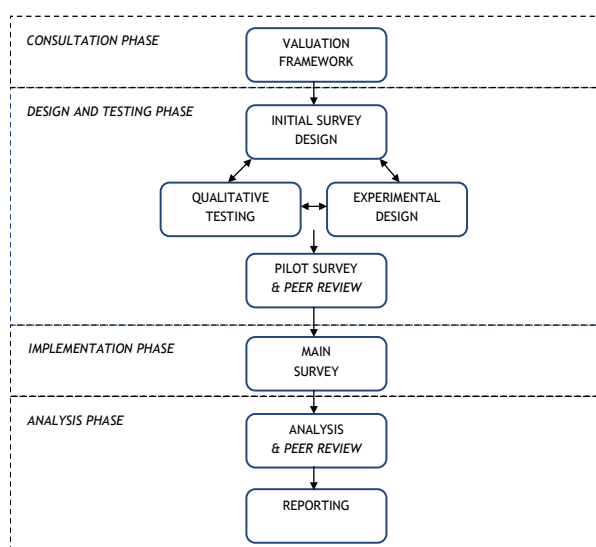
Valuation Framework and Scoping

Initial consultation was carried out to confirm the issues to cover in the WTP study and the range of service areas that may be of interest. The output of this phase of work was the Valuation Framework, which outlines the service measures needed for CBA assessment, and the valuation technique to be applied.

Survey design and qualitative testing

This detailed phase of qualitative testing has been undertaken, including focus groups and cognitive interviews with household (domestic) customers and in-depth telephone interviews with non-household (commercial) customers. These have focused on respondent understanding of the survey material, such as the definitions of water related service attributes presented to respondents, and the framing and phrasing of questions.

Diagram 4: Approach to stated preference research



Experimental design

In parallel to the qualitative testing the specification of the design and implementation of the choice tasks has been undertaken. This provides the range of alternatives that respondents are presented with. The experimental design fixes the number of service attributes to be included in a choice experiment and the number of choice tasks to be administered to respondents. Both these elements are important with respect to the cognitive burden (level of understanding) imposed by the survey on respondents. An example choice card is illustrated below.

Diagram 5: Example Choice Card

EXAMPLE

To derive £ need to include bill or money impacts

CHOICE CARD 1			
	Alternative O Current position	Alternative A	Alternative B
Properties with unplanned interruptions to water lasting more than 12 hours	8 in every 10,000 properties (=3,000 per year)	16 in every 10,000 properties (=6,000 per year)	2 in every 10,000 properties (=750 per year)
Hosepipe bans lasting more than 3 months	1 in 16 years	1 in 25 years	1 in 16 years
Properties affected by low pressure of water	4 in every 10,000 properties (=1,500 in total)	4 in every 10,000 properties (=1,500 in total)	1 in every 10,000 properties (=375 in total)
Change to annual bill	No Change	No Change	Increase by £15
Please tick ONE box			

Pilot survey

This involves drawing together the outcomes from the qualitative testing and then testing in a pilot study. This allows the assessment of the cognitive burden (understanding) imposed on respondents by the format of the choice tasks in a basic field test of the questionnaire. Results of the pilot testing phase of the research are attached as Appendix D.

Peer review

This involves collating feedback from the Pilot Study, comments from the academic Peer Reviewer and other stakeholders to develop the final questionnaire.

Main survey

The main survey sample covers both household (domestic) and non-household (commercial) customers across all three regions. A key feature of the household survey is the split sample survey implementation of using face to face interviews and online techniques. For non-household (commercial) customers, the telephone recruitment to an online survey was used. The numbers surveyed are sufficient to yield a statistically robust response rate, as noted in the minute of CCG meeting in May 2013.

The CCG, as part of this challenge has asked three specific questions regarding the representativeness of the main survey:

a) Affinity Water should demonstrate that its research includes representative samples of both domestic and commercial customers;

f) Affinity Water should demonstrate that it has engaged with customers both commercial and domestic who are reliant on a constant/consistent source of water; and

o) Affinity Water should demonstrate how the consultation processes were applied to both domestic and commercial customers and all representative organisations and stakeholders

Representative samples

The WTP study covers both household (domestic) and non-household (commercial) customers. The survey numbers are substantially above the minimum levels for all research, namely 1,717 for WTP (508 non-households and 1209 household). Quotas have been set for households and businesses. Household quotas are set by age, gender, and Socio-Economic Group (SEG) based on 2011 Census. Business quotas were set by the industrial classification based on Office for National Statistics (ONS) data. All respondents have been randomly selected.

Customers reliant on constant/consistent source of water

The research includes CAPI (face to face), which improves access to hard to reach and vulnerable customers. However, all customers are randomly selected, so that there is a mix of customers that are highly and less dependent on a constant/consistent source of water.

Domestic and commercial customers

The WTP survey included household (domestic) and non-household (commercial) customers. Both groups of customers were engaged in the survey development and testing process – in the cognitive testing and in the pilot study

We have carried out two stated preference research studies. A main generic study covering a range of water service attributes and a separate water resources study to inform the dWRMP consultation. The attributes are set out below

Diagram 5: Attributes in the Main and Water Resources studies

Main Study

- Tap water quality
 - Discoloured water
 - Taste and smell of water
 - Drinking water restrictions
 - Water hardness
- Reliability of your water supply
 - Low water pressure
 - Unexpected interruptions to water supply
 - River pollution
 - Burst Mains Flooding to Properties
- Environment
 - Hosepipe bans (NEUB for business)
 - Low water levels and flow in rivers
 - Leakage

Water Resources Study

- Water Use Restrictions
 - Hosepipe Bans - duration and frequency
 - NEUB: Non Essential Use Bans - duration and frequency
- Water Options
 - Water efficiency in homes
 - Fix leaks in water supply pipes
 - Install water meters
 - Transfer from other regions
 - Taking water from rivers
 - Taking water from the ground
 - Take water from the sea

The attributes in the main study align with our customer expectations of ‘Supplying high quality water you can trust’ and ‘Minimising disruption to you and your community’ and ‘Making sure our customers have enough water’. The water resources study is also aligned with our third customer expectation of ‘Making sure our customers have enough water’. Our fourth customer expectation of ‘Providing a value for money service’ is more closely aligned to the acceptability testing described in section 5 below.

Research output

The research output will enable us to assess the value customers place on each water service attribute and we can then use this information in our CBA so that decisions about investment choices explicitly include the assessment of customer benefit valuation.

5. Acceptability testing

Customer acceptability testing complements willingness to pay and CBA as it acts as an overall test of investment proposals. Not all investment options are covered by willingness to pay and it does not capture the overall limit on what customers can afford and therefore what is an acceptable level of bill and/or change in bill level. Customer acceptability is not just about testing if our plan is acceptable. It is also seeking to indicate if our plan is likely to be the most acceptable to customers. The approach to acceptability testing was explained to the CCG in May by Lisa Gahan from ICS consulting. The May CCG presentation is attached as Appendix E.

We have developed a Proposed Plan around which we have a range of options. We have specifically taken this approach so that the quantitative acceptability testing we carry out is consistent with the qualitative research we are carrying out on our business plan consultation. In other words we are testing multiple plans.

We are testing our plans with customers to find out:

- % of respondents that think each plan is acceptable and very acceptable
- % of respondents that think each plan is unacceptable and completely unacceptable
- Why the plan is acceptable or not
- Which is the most preferred plan from the options presented

We expect this will allow us to understand:

- what changes in our plans customers support and which they do not
- customers' views on current levels of service, value for money and key areas for improvement and
- what changes to the most preferred plan would make it more acceptable.

These factors will be a key input in shaping the first draft final plan. We are also planning to carry out some final acceptability testing of the final plan prior to its completion and submission.

The CCG, as part of this challenge have also asked a number of additional questions regarding the acceptability testing survey:

a) Affinity Water should demonstrate that its research includes representative samples of both domestic and commercial customers;

f) Affinity Water should demonstrate that it has engaged with customers both commercial and domestic who are reliant on a constant/consistent source of water;

l) Affinity Water should demonstrate how it has offered customers competing choices to establish customers' preferences; and

o) Affinity Water should demonstrate how the consultation processes were applied to both domestic and commercial customers and all representative organisations and stakeholders.

Representative samples

The acceptability study covers both household (domestic) and non-household (commercial) customers. The survey numbers are substantially above the minimum levels for all research, namely 1200 for each phase of acceptability, giving 2400 in total. Quotas have been set for households and businesses. Household quotas are set by age, gender, and SEG based on 2011 Census. Business quotas were set by the industrial classification based on ONS data. All customers have been randomly selected.

Customers reliant on constant/consistent source of water

The research includes CAPI (face to face), which allows hard to reach customers to be included. All customers are randomly selected, so that there is a mix of customers that are highly and less dependent on a constant/consistent source of water. We are planning that the Phase 2 acceptability testing will have questions on whether the customers are vulnerable or have a particular reliance on water so that these are expressly considered in the research.

Competing choices

The acceptability research has allowed multiple options to be tested in the first phase. One option has a slight reduction, one a small increase, and one a more moderate increase in bills and service, so that customers' attitudes to future bills can be explored. This is described at the start of this section and explained further in section 7. The acceptability survey also includes a specific question to ask if customers want bills and service to increase, decrease or remain static.

Domestic and commercial customers

The WTP survey has included household (domestic) and non-household (commercial) customers. Both groups of customers were engaged in the survey development and testing process – in the cognitive testing and in the pilot study. Stakeholders have been engaged through the process of the CCG.

Finally the CCG as part of this challenge have asked a number of additional questions regarding the combined water and sewerage bill. Specifically the questions were:

p) Affinity Water should demonstrate how the research has been put in context for customers in respect of the expected increases in sewerage charges by Thames and possibly Anglian;

q) Affinity Water should consult with Anglian and Thames and inform the CCG as to what the sewerage charges are likely to be in the period 2015-2020; and

r) Affinity Water should demonstrate that respondents to this research have been reminded that their water bill and sewerage bill should be regarded in the context of other household expenses and expectations of financial security.

Combined bill

The acceptability and WTP study make explicit reference to the associated sewerage bill. As both Thames and Anglian are likely to develop and change their plans we have carried out surveys using a range of potential sewerage bill impacts to cover a range of potential outcomes.

We have consulted with Anglian and Thames on their potential sewerage charges for the period 2015-2020. Both companies have published their draft plans online.

The stage one acceptability testing has not explicitly reminded customers that their water bill and sewerage bill should be regarded in the context of other household expenses and expectations of financial security. This will be included in the phase two testing.

6. Engagement activities

In 2012, we instigated a customer consultation programme to gain a clear picture of the current and future expectations of our customers for their water service. We are consulting on our PR14 proposals in a variety of ways.

Investing for Your Community

In autumn 2012, we published Investing for Your Community – a Consultation, which initiated our community engagement programme and asked for customer views on expectations for future water supply services. The document asked for feedback to inform preparation of our SDS (subsequently published in the summer of 2013). The publication invited comment by post, by email or via the online discussion board on our website.

We also used Investing for Your Community to structure the workshops we held in the community.

Have your say

We have set up a discussion forum on our website to capture both qualitative and quantitative feedback on our plans. An interactive questionnaire was available to gain specific feedback on key topics and on a number of the primary documents including Investing for your Community and our Strategic Environmental Assessment Scoping Report, both of which are available to read on our website.

Postal consultation with stakeholders

In October 2012 we wrote to our statutory consultees and regulators to consult them on our plans. We also wanted to extend the consultation more widely so we sent a further 900

letters to representative bodies. These included local environmental interest groups, MPs, MEPs, parish councils, local and district councils, social welfare bodies, commercial organisations and other public representative bodies. For some groups we enclosed the Investing for your Community consultation document and in all cases we included our postal, email and online feedback channels.

Drop in events

We arranged ten drop in events between October and December 2012 in our local communities across our regions to offer customers the opportunity to 'drop in' and talk to us about any aspects of our plans. Drop in events were promoted widely through local press advertising, news events and our website.

Focus groups

Between October and December 2012, we conducted ten independently run customer focus groups seeking feedback on our plans. In one group we consulted small and medium sized enterprises in the sports and leisure sector, reflecting concerns raised by the group during the 2012 drought, and, in another, we consulted environmental stakeholders. The remaining eight groups were for our household (domestic) customers, covering a demographic and geographic range of our customer profile.

Online panel

We have set up an independently operated online panel of 2,000 customers across our three supply regions. The sample group reflects our customer profile, and provides us with a statistically significant number of quantitative responses to questions we pose. We plan a regular programme of consultation with the panel to explore key issues arising from all sources of consultation. We have so far carried out surveys on the following issues:

- 'Investing in you community' pre-consultation;
- Draft water resource management plan issues;
- Environmental reporting;
- Lets Talk Water; and
- Leakage

Environmental forum

During November 2012, we launched an environmental forum to give voice to the views of environmental groups representative of customers and government bodies impacted by our operations. The second meeting took place in February 2013, and the third in July 2013. As the forum develops, we intend to debate key issues and options with delegates at these events to gain input to our plans.

Deliberative forums

These events involve large, purposefully sampled groups of customers. They are independently facilitated events providing opportunities to explore issues in more depth and are a valuable addition to focus groups and on-line surveys. The qualitative output is supported by individual voting, on specific issues. This provides indicative, quantitative feedback of the preferences of the audience. During July 2013, four events took place across the company regions. The focus was on the consultation version of the Business Plan.

Affinity Water managed on-line consultation

Each consultation document is made available on the company web site. Accompanying these is a response form which can be used to register comments and provide feedback on the relevant document. This means of gathering feedback is in addition to other direct engagement and communication activity. This has included:

- The consultation on the Strategic Direction Statement / pre-consultation of the draft Water Resource Management Plan and (October 2012 to January 2013)
- Draft water Resources Management Plan (April to August 2013)
- Consultation Business Plan (July – August 2013)

Agency managed communication campaigns

Large scale multimedia campaigns with the aim of reaching as many customers as possible. The output provides high volume snap shot views from customers. The output, which may be a combination of qualitative and quantitative data, can be used to provide a valuable insight into views and opinions. A large scale communication campaign called 'lets talk water' ran from April to September 2013 which involved getting customers to complete a standard questionnaire.

Our PR14 Business plan consultation

As set out earlier, in July 2013, we launched our Business Plan Consultation for the upcoming five years from 2015. As part of that consultation, we have shared our proposals to achieve each of our four outcomes for customers (customer expectations).

7. Business plan consultation

In our Business Plan consultation, we have set out our Proposed Plan for 2015 to 2020. Alongside this, we present alternative levels of future investment so customers can decide if our Proposed Plan will achieve the right balance between the service we provide, the price we charge and the pace of our investment. The overall plan, in terms of customer expectations, measures of success and indicative performance commitments are illustrated in the diagram on the following page.

Our Proposed Plan seeks some improvement in the service customers currently receive and tackles our water resources challenge of leaving more water in the environment. We plan to reduce our current abstraction whilst ensuring our customers have enough water both during 2015 to 2020 and beyond.

The CCG, as part of this challenge, have asked a number of questions about how we have consulted with our customers, specifically:


g) Affinity Water should test the assumption that its current customers are willing to pay to secure resources for future customers;

h) Affinity Water should be transparent about the assumptions it makes on variables such as cost of capital which Ofwat will determine and is likely to advise after this research has been undertaken;

i) Affinity Water should keep in mind and inform the CCG about the implications of such assumptions being significantly off target/ not materialising;

j) Affinity Water should consider whether it is prudent to test for more than one 'Ofwat scenario' and explain its decision on how to deal with this issue to the CCG.

Diagram 6: Proposed Plan for consultation

 Affinity Water OUR PROPOSED PLAN	
2014/15 average household bill	£165
Making sure our customers have enough water	+ £4.60
Supplying high quality water you can trust	+ £2.00
Minimising disruption to you and your community	+ £2.60
Providing a value for money Service	- £5.50
2019/20 average household bill	£168.70

Customer expectation	Measure of success	Our Proposed Plan <i>Proposed 2020 performance compared to our current target / performance</i>
Making sure our customers have enough water	Leakage	10% reduction
	Average water use	7% reduction
	Water available for use	6% improvement
Supplying high quality water you can trust	Compliance with water quality standards	No change
Minimising disruption to you and your community	Unplanned interruptions to supply over 12 hours	5% reduction
	Number of burst mains	15% reduction
	Affected customers not notified of planned interruptions	15% reduction
	Planned work taking longer to complete than planned	10% reduction
Providing a value for money service	Community survey	

Future generations

We have not explicitly tested the assumption that current customers are willing to pay to secure resources for the future. However, as part of our research we surveyed customers to ask whether they were willing to pay more for water today to avoid significant bill increases for future generations. Given that resolving future water resource issues will drive investment and increase bills we have implicitly asked this intergenerational question. Half the customers disagreed with this statement, with half of these (or a quarter of the responses) strongly disagreed. There was not much variation between metered and unmetered customers. This suggests to us that there is limited appetite to move much beyond on

Proposed Plan.

Alongside our Proposed Plan we have consulted on alternative levels of future investment. This is consistent with our dWRMP. The alternative levels of future investment will mean:

- Investing at a slower pace - This would maintain the service customers currently receive and would go some way to tackling our water resources challenge. Beyond 2020 this pace of investment could lead to a less reliable service, would leave less water in the environment and will increase costs for future generations.
- Investing at a faster pace – This will seek to improve the service customers currently receive and would tackle more quickly our water resources challenge. Beyond 2020, this pace of investment would lead to a more reliable service, would leave more water in the environment and will reduce costs for future generations.

The approach we have taken is consistent with the information we have used for the quantitative acceptability testing and allows us to test if customers are willing to pay to support investment at a faster pace. Our Business Plan consultation is central to our 'lets talk water' campaign that we have undertaken to engage with our customers and stakeholders.

Cost of capital

In our Business Plan Consultation document we have been explicit about the assumptions we have used on the cost of capital. We have modelled bill impacts using a pre tax debt and post tax equity 'vanilla' cost of capital of 4.5%. At PR09 the equivalent cost of capital was 5.3%. In the final PR14 price setting methodology publication Ofwat has confirmed that it will set an industry wide cost of capital based upon a notional company structure with a level of gearing in the range of 60 – 70%.

We will inform the CCG of the cost of capital assumptions that we use for the preparation of our final business plan. This will be important given the potential impact a small change could have on overall bill impacts. Nevertheless the final cost of capital will be determined by Ofwat.

Ofwat scenarios

We anticipate that we will model several scenarios as set out by Ofwat in the final PR14 price setting methodology publication. At this stage we have not determined the number and scenarios but we aim to keep the CCG informed of our decision and any implication this may have for overall customer bill levels.

The CCG as part of this challenge, also asked a number of additional questions:

c) Affinity Water should demonstrate how they have consulted with customers in a transparent manner, showing how a water bill consists of various components including not only the cost of supplying clean water and the proposed investments/service enhancements but also debt financing, tax, profits, avoided costs and efficiencies;

m) Affinity Water should demonstrate that any proposed price adjustments to customers in the east (Brett) and south-east (Dour) communities have taken into account and returned to customers the cost savings/efficiencies resulting from unification; and

n) Affinity Water should inform the CCG on how it intends to communicate these savings/efficiencies to the customers in Brett and Dour.

Bill transparency

All costs are included in the bill presented to customers. The bill impact is the revenue required from each customer for the proposed changes and thus includes debt finance, profits, tax and avoided costs and efficiencies. These components of the bill are not explicitly listed out for the purposes of WTP or acceptability testing but are included in the overall bill. Customers are only asked to consider total changes in bill and associated levels of service.

Efficiencies are explicit in the survey. Cost of finance efficiency is included in this. The approach we have adopted is in line with Ofwat Acceptability testing of the draft business plan in PR09 and also meets the CC Water expectations as set out in the paper “CCWater’s expectations on water companies’ testing of customer views on acceptability of their Business Plan for the 2014 Price Review”.

Cost savings and efficiencies resulting from unification will be returned to customers in the East (Brett) and Southeast (Dour) communities through the adoption of the average cost to serve price control. As a single unified business the retail costs per customer will be lower in the East and Southeast regions than would have been the case as three separate companies. The lower unified cost to serve will more than offset the efficiencies of £900k identified at the time of unification.

8. First draft final plan

Our first draft final plan will show how customer engagement and research has been used to challenge and change the balance and content of the Proposed Plan we consulted upon. The quantitative research described above will help determine both the relative preferences of customers between different investment options and possible service enhancements as well as the overall level of customer acceptability for future bill levels.

9. Conclusions

We are clear about the importance of the CCG’s role in challenging us around the development of our business plan and investment proposals. Through all of our engagement work, including our draft Business Plan consultation, we are able to demonstrate that we have consulted with both household (domestic) and non-household (commercial) customers to determine;

- their preferences and Willingness to Pay for alternative investment options
- their preference for possible service enhancements
- the level of customer acceptability for future bill levels; and
- if customer acceptability for future bill levels is influenced by considering the overall water and sewerage bill in the period 2015-2020.

Expectation 1: Representative Samples of Customers

The WTP study included both household (no. 1,209) and non-household customers (no. 508), with quotas set for both. Household quotas are set by age, gender and SEG (based on 2011 Census data). Non-household quotas were set by the industrial classification based on ONS data. All participants were randomly selected. The Acceptability study also covered both household and non-household customers (no. 1,200 per phase).

Expectation 2: Deriving the Values Placed on Outcomes

In order to value the outcome from investments we asked customers, as part of our early stated preference research, about aspects of service that they regard as important. This drove the selection of a number of water service attributes that formed the basis of the WTP study and the service measure framework. This approach enables all investment options to be articulated in performance terms and in terms of value to customers. We have also carried out acceptability research to understand how much customers want service (and therefore bills) to change. This makes sure that the business plan does not contain service improvements that customers either do not value, or value but either cannot afford or do not find acceptable.

Expectation 3: Demonstrating no Undue Cross-Subsidies

The investment options we have considered in developing our proposed plan, and which form the basis of our dWRMP, are investments that will ensure we deliver the four high level customer expectations we set out in our SDS. These customer expectations do not differentiate between non-household (commercial) and household (domestic) customers and so will not lead to any undue cross subsidy between these two groups of customers.

Expectation 4: Exploring all Investment Possibilities

In developing our draft Business Plan consultation, we have set out our Proposed Plan for 2015 to 2020. Alongside this, we present alternative levels of future investment so customers can decide if our Proposed Plan will achieve the right balance between the service we provide, the price we charge and the pace we of our investment. The alternative levels of investment consider a range on investments possibilities that could result in static or reduced bills. The WTP survey includes increases in service/bill and decreases in service/bill.

Expectation 5: Ensuring Transparency

We have ensured that all expected costs for each investment plan are included in the bill presented to customers. The bill impact is the revenue required from each customer for the proposed changes and thus includes debt finance, profits, tax and avoided costs and efficiencies. We have presented this information to customers in our deliberative forums and Strategic Direction Statement by showing where each pound of a customer bill is spent on average. We have not explicitly listed out these components of the bill for the purposes of WTP or acceptability testing. Customers are only asked to consider total changes in bill and associated levels of service.

Efficiencies are explicit in the survey. Cost of finance efficiency is included in this. The approach we have adopted is in line with Ofwat Acceptability testing of the draft business plan in PR09 and also meets the CC Water expectations as set out in the paper "CCWater's expectations on water companies' testing of customer views on acceptability of their Business Plan for the 2014 Price Review".

Appendices

- Appendix A: CCG Meeting 23/01/13 – Willingness to Pay, Affinity Water
- Appendix B: CCG Meeting 22/05/13 – Willingness to Pay (WTP) and its role in putting together business plans, ICS Consulting
- Appendix C: CCG Meeting 22/05/13 – Capital Investment Portfolio Optimiser, Affinity Water
- Appendix D: PR14 Willingness to Pay Survey: Pilot Study, ICS Consulting

Appendix E: CCG Meeting 22/05/13 - Acceptability Testing – and its role in putting together business plans, ICS Consulting

Passed to / date:	Clarifications:
Accepted by / date:	18 September 2013

Response

All responses will be clearly identifiable and traceable and will append the following table.

Version No:	Draft	Final	
Date:	17 July	09 September	
Submitted to:	CCG for comment	CCG	
Prepared by:	Chris Offer	Chris Offer	
Approved by:		Tim Monod	
Reference:		0003	
Date to Chair CCG		11 September	
Accepted by CCG		18 September 2013	

Meeting date	23 January 2013
Subject/agenda item	Agenda item 4, Willingness to Pay
Prepared by	Christopher Offer
Purpose (inform, discuss, approve etc)	For information and discussion

Summary of content/ finding

- A vital component of our approach to engagement is 'Willingness to Pay' (WTP).
- WTP is a single term that is often used to describe two distinct approaches to assessing customer support for investment proposals.
- The paper provides a summary of each of these approaches and sets out how we will use the information we get from our research.

Action for CCG

For Information / action etc (define requirements and any questions)

- For information and to provide the CCG with an opportunity to:
 1. Understand the difference between willingness to pay in terms of bill level acceptability versus a technique to value non-market benefits of investments that can be used as a key input to cost benefit analysis
 2. Familiarise themselves with a cost benefit analysis planning objective (plus related terms and language as set out in glossary)
 3. Understand when we are planning to undertake research in order that they can contribute to the work and challenge our plans

Affinity Water Limited:

Willingness to Pay

23rd January 2013



Contents

- **Introduction**
- **Stated preference research**
 - Cost Benefit Analysis
 - Choice experiments
 - Contingent valuation
 - How this information will be used
- **Willingness to Pay**
 - Bill levels
 - Investment options
 - How this information will be used
- **Next Steps**
 - Timetable
 - Glossary

Introduction

Introduction

- A vital component of our approach to engagement is 'Willingness to Pay' (WTP).
- WTP is a single term that is often used to describe two distinct approaches to assessing customer support for investment proposals.
- These approaches are quite different, WTP is both:
 - A technique to value non-market benefits of investments that can be used as a key input to cost benefit analysis (CBA); and
 - A means to assess the acceptability of overall bill levels and/or changes in bill levels from a range of investment proposals
- The remainder of this paper provides a summary of each of these approaches and sets out how we will use the information we get from our research.

Stated Preference Research

Stated Preference Research

Cost Benefit Analysis (CBA) – overview

- CBA represents a structured comparison of the pros and cons of making an investment decision that uses scarce economic resources.
- The principle objective is to facilitate comparison in terms of a common metric; money
- Financial appraisal expresses the concept of ‘net benefit’ in monetary values. Costs are understood and measured in terms of Opex and Capex, while benefits might take the form of revenue or avoided costs
- CBA applies the same decision rule as financial appraisal, but is informed by a monetisation of all impacts on the economic welfare of those affected by an investment decision

Stated Preference Research

Cost Benefit Analysis (CBA) – using the results

- CBA results can be used to prioritise and schedule projects in order to maximise the value of every pound of investment. CBA can be used to demonstrate
 - Whether total benefits provided by an investment programme justify the cost of delivering those benefits.
 - Whether the benefits of an individual project justify the costs of that project.
 - Whether the benefit to customers of planned investment is being maximised.
- Uneconomic projects may be components of an overall programme considered to be cost beneficial
- Our approach to PR14 is to use CBA and optimisation tool called 'Pioneer'

Stated Preference Research

Cost Benefit Analysis (CBA) – welfare measures

- Economics defines benefits by looking at measures of individual satisfaction referred to as welfare or utility.
 - Economic theory assumes individuals can maintain the same level of utility while trading off different goods, services and money.
 - The willingness to trade off compensation for goods or services can be measured either as willingness to pay (WTP) or as a willingness to accept compensation (WTA). WTP and WTA are generally expressed in monetary terms.
 - It is important to note that WTP does not necessarily equal WTA.
 - This distinction is important in terms of AMP planning and base service vs. service enhancement.

Stated Preference Research

Choice experiments (CE)

- Economic value is revealed through questionnaires based on constructed or hypothetical markets.
 - Water services have many “attributes”, each has their own “value”
- Stated preference methods include CE and these are needed to
 - Value of attributes not revealed by purchasing decisions of customers
- CE questionnaire is the approach we used at the last price review which contains choice sets rather than individual questions.
 - CE is able to identify ‘implicit’ prices and can better explore WTP and WTA.
 - Encourages more stakeholder participation.
 - Suited to scenarios of competing options.

Stated Preference Research

Choice experiments (CE) – examples

- During the research survey the basic choice task is explained.
 - Depending on the 'block' that is randomly allocated to the respondent, relevant attributes, and the associated bill changes, are explained.
 - Respondents are then asked to go through the twelve choice cards allocated to them. The order in which the cards appear is randomised across respondents.
 - This is repeated many times over generating a substantial set of data points

CHOICE CARD 1			
	<i>Alternative O</i> Current position	<i>Alternative A</i>	<i>Alternative B</i>
Properties with <u>unplanned interruptions</u> to water lasting more than 12 hours	8 in every 10,000 properties (=3,000 per year in total)	16 in every 10,000 properties (=6,000 per year in total)	2 in every 10,000 properties (=750 per year in total)
<u>Hosepipe bans</u> lasting more than 3 months	1 in 16 years	1 in 25 years	1 in 16 years
Properties affected by <u>low pressure</u> of water	4 in every 10,000 properties (=1,500 in total)	4 in every 10,000 properties (=1,500 in total)	1 in every 10,000 properties (=375 in total)
Change to <u>annual bill</u>	No Change	No Change	Increase by £15
Please tick ONE and ONLY ONE box			

Stated Preference Research

Contingent valuation (CV)

- Stated preference methods also include CV
 - CV questionnaires contain several well defined elements and is similar to a series of referendum style questions.
 - CV is well understood by respondents but can be costly to use, provides limited information on preferences and can be prone to bias.
- At PR09 we followed our CE with a CV question that was framed similarly to the CE tasks.
 - WTP from this CV question can be tested to for consistency with the derived WTP from the CE exercise for the same improvement scenario.
 - Indeed consistency between the two WTPs is a test for the validity of the CE stated values.

Stated Preference Research

How this information will be used

- Stated preference research is a key input to any investment appraisal
 - It helps us value non-market benefits of investments
 - These values are used as a key input to cost benefit analysis alongside a range of other costs and benefits
- *Ofwat RD 04/06 prior to PR09*

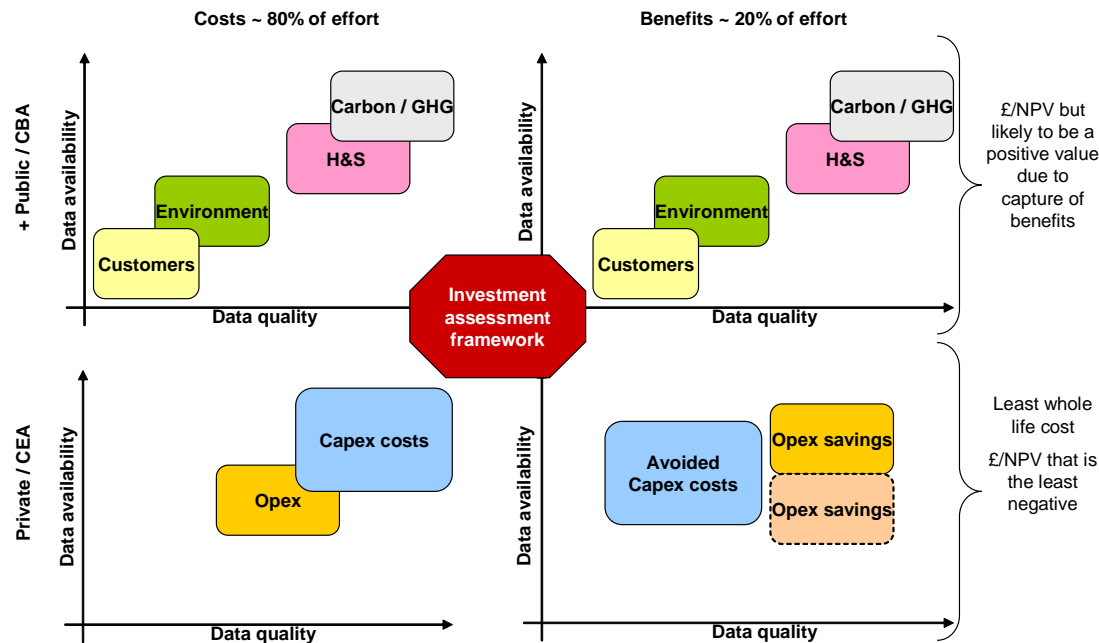
“We want to see companies providing consistent best value in the service they deliver to consumers and the environment. This means that companies need to take account of both costs and benefits and to consider both capital and operating expenditure, across base service and enhancements, in an integrated and coherent manner.”

Stated Preference Research

How this information will be used

- Implementation of a cost benefit analysis planning objective opposed cost effective analysis planning objective

Cost effective & cost benefit analysis



Willingness to Pay

Willingness to Pay

Bill levels

- This approach to WTP is as a means to assess the acceptability of overall bill levels and/or changes in bill levels from a prospective range of investment proposals
 - Our approach here is iterative and guided by our developing investment proposals but also by our understanding of customer priorities and bill impacts
 - We will be carrying out a range of surveys covering many elements of our developing business plan
 - It is vital that any WTP questionnaire is coherent, well designed and is able to provide robust sound results

Willingness to Pay

Investment options

- Throughout the remainder of this year we will be establishing and refining our business plan and will be seeking customer feedback on our proposals and their impact on bills.
- With the remaining uncertainty surrounding elements of Ofwat's future price setting methodology we may need to conduct WTP survey work using less than definitive bill impact numbers.
 - We do not anticipate this causing difficulty at a investment plan component level
 - However, this may impact upon our ability to present overall investment plan / total bill impact estimates with the level of certainty we would like.

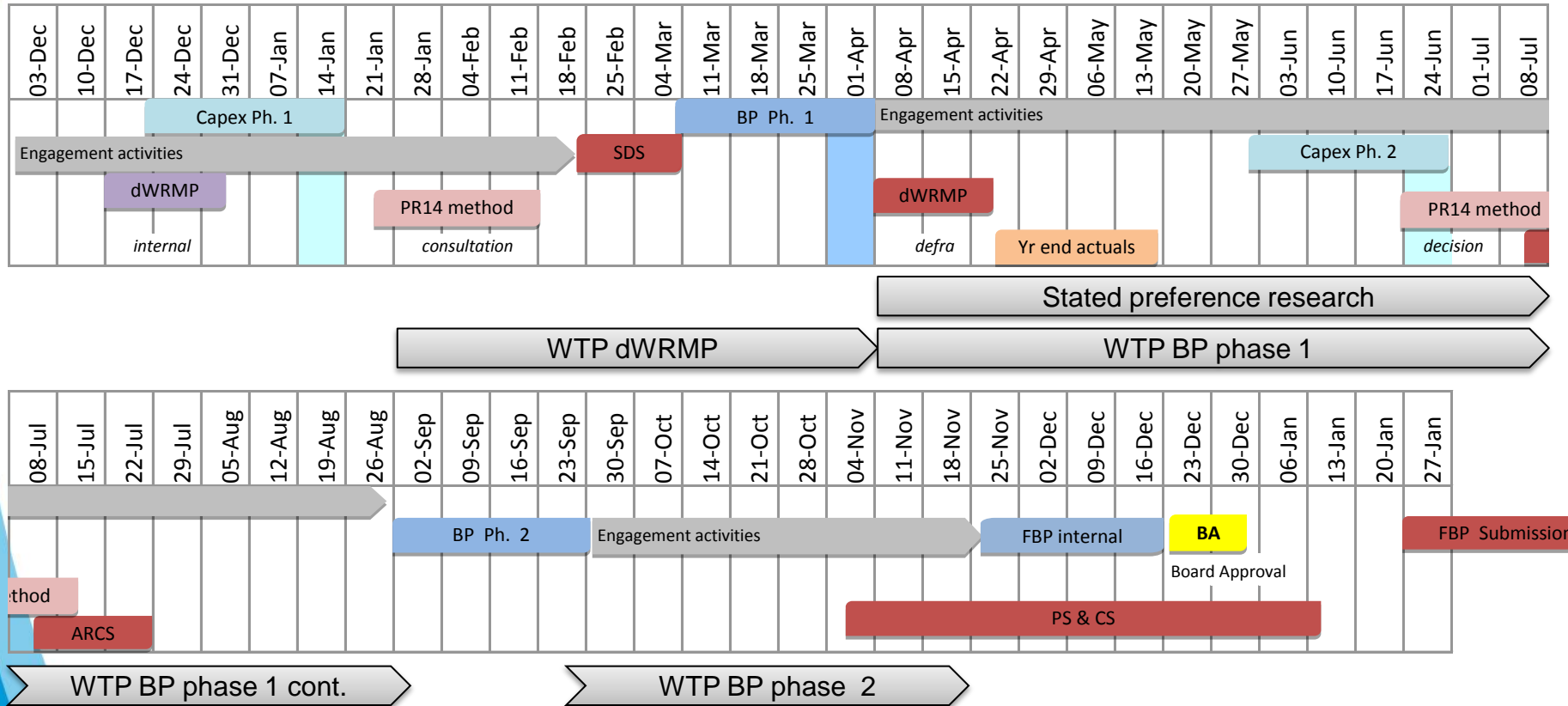
Willingness to Pay

How the information will be used

- The information from these surveys will help us to refine and develop subsequent iterations of our business plan during the year.
- The information will also be critical in understanding overall acceptance of potential changes in bill levels
 - We expect to be able to conduct surveys to help us understand what ‘trade – offs’ may be required between components of our business plan while achieving an overall bill level that customers are willing to pay.
 - We are planning to make regular use of our on-line panel to generate statistically robust data on which we can make decisions influencing the development of our business plan

Next steps

Timetable



Glossary

Annuity is the value from a project that is paid in a series of regular payments.

Benefits transfer (BT) involves taking the results from one or more primary economic studies with estimated values for similar environmental impacts, and modifying and transferring them to the project being evaluated.

Bequest value the value of leaving something behind for the next generation.

Cost Benefit Analysis (CBA) is a technique used to compare alternative projects by assigning monetary values to all outlay and outcomes. The procedure involves weighting the total expected costs vs. the total expected benefits of one, including social costs and benefits, or more actions in order to choose the most net beneficial option.

Cost effectiveness is the achievement of a particular objective at the least cost. A cost effectiveness approach is most applicable where outcomes cannot be quantified in monetary terms though costs can be monetised

Direct use value is the economic value derived from direct use or interaction with a biological resource or resource system

Discount rate is used to convert all costs and benefits to 'present values'. While the interest rate incorporates an individual's 'time preference' the social time preference discount rate incorporates society's preference for benefits now and costs deferred to future generations for calculating the present value of expected future benefits and costs

Existence value is a concept used to refer to the intrinsic value of some asset, normally natural/environmental. It is the value of benefits people place on just knowing a species or ecosystem exists, even if they will never see it or use it

Financial appraisal is the comparison of cash flow costs and benefits for different project options over the same time period. It should include a consideration of intangibles. Costs will include both revenue and capital, initial capital costs, costs of replacing assets, operating costs including staffing. Benefits will include income generated and savings in costs. Appraisal is usually carried out on the basis of fixed cost date, i.e. the price fixed at a date, excluding the effects of inflation

Hedonic prices is a service demand that may be reflected in the prices that people are willing to pay for associated goods

Indirect use value is the value attributed to indirect utilisation of ecosystem services, through positive benefits that ecosystems provide

Internal rate of return is the discount rate or interest rate at which the NPV of an investment is equal to zero; when cash inflows equal cash outflows

Non-use / passive values is an economic value attached to an environmental or natural resource that is not based on the tangible human use of the resource. Non-use values may include existence values, bequest values. Altruistic values and options values

Net present value (NPV) for a CBA is the net benefit of the project, allowing for the value of the costs and benefits to be worth less in the future than at the present

Option value is the value to keep open the possibility of (direct or indirect) use in the future; the difference between the intrinsic value of an option and its actual value

Social time preference rate (STPR) is used for discounting future benefits and costs based on the value society attaches to present consumption. It is based on comparisons of utility across different points in time or different generations

Time horizon / planning period the time period over which the project is relevant

Total economic use is the sum of use and non-use values with due consideration of any trade-offs or mutually exclusive uses or functions of the resource habitat in question

Use value is an economic value based on the tangible human use of some environmental or natural resource; includes direct and indirect use values

Willingness to accept (WTA) is the minimum amount of compensation consumers would be willing to accept for foregoing units of consumption

Willingness to pay (WTP) is the largest amount of money that an individual or group could pay, along with a change in policy, without being made worse off

Affinity Water

Willingness to Pay (WTP) and its role in putting together business plans

May 2013

Agenda

- Willingness To Pay
 - What is it and how is it used?
 - How do you estimate Willingness To Pay?
 - What does a WTP survey look like?
 - How do we use WTP in cost benefit analyses?
- The WTP study at Affinity
- The project timeline
- Review of current Main study - demo of the online link

Willingness to Pay

What is it?

How is it used?

How do you estimate Willingness To Pay?

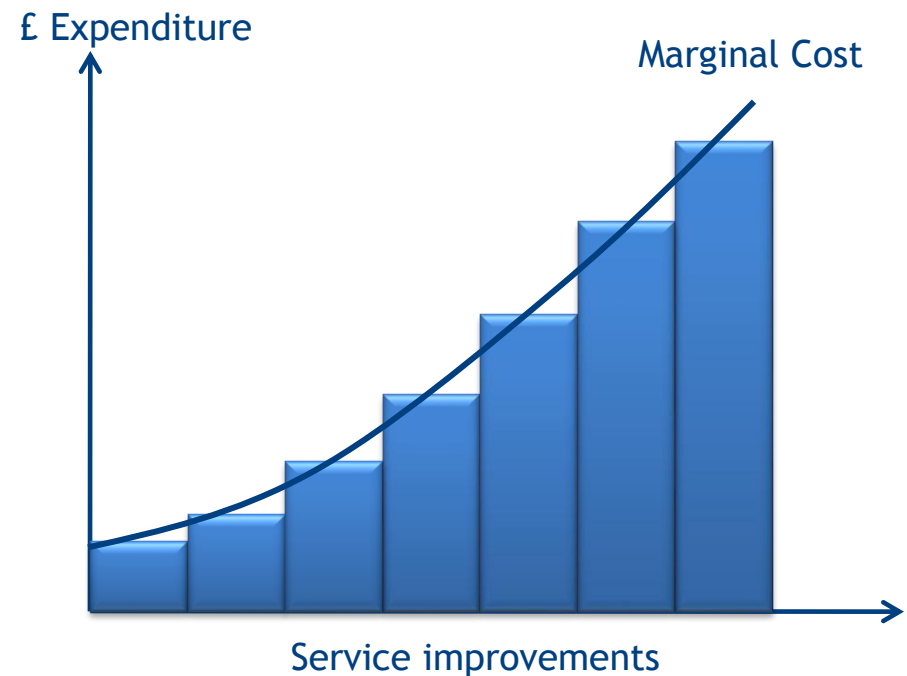
What does a WTP survey look like?

What is willingness to pay?

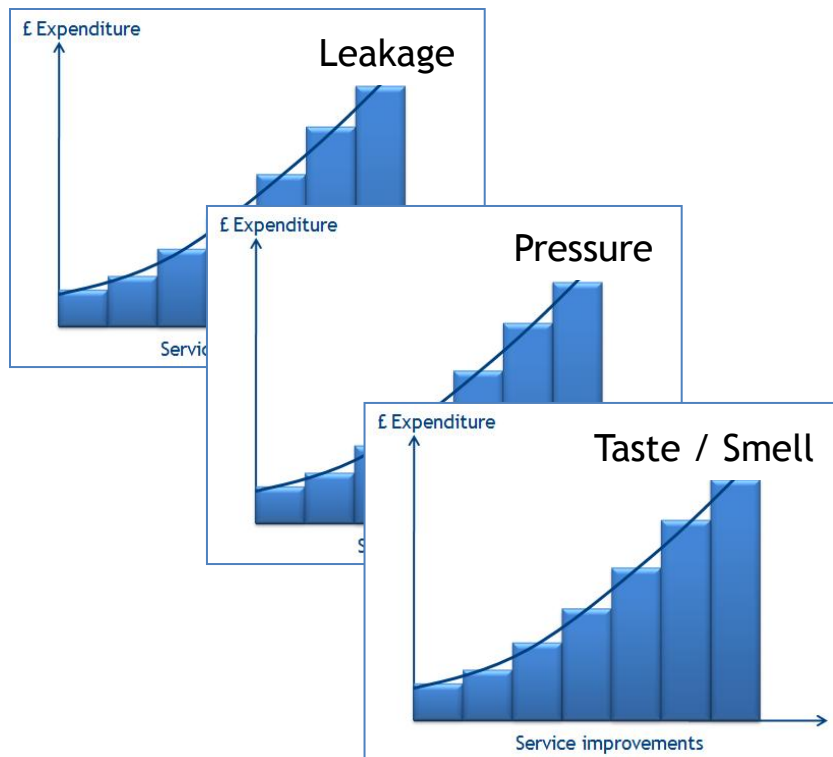
- Willingness to pay (WTP) is a measure of value:
 - Represents the value of services to customers
- WTP is the maximum amount a person would be willing to pay, sacrifice or exchange in order to receive a good or service
- We use WTP to provide an estimate of the ‘benefit’ of incremental changes to service
- **WTP is expressed in £ and treated as money**
- *Why do we need it and how do we use it?*

Water companies understand the costs of investment reasonably well

- **Marginal costs represent the cost of investment:**
 - The incremental cost of delivering incremental performance improvements
 - Shape denotes that it is more costly to continue to improve service
- How far up the MC curve should we invest?

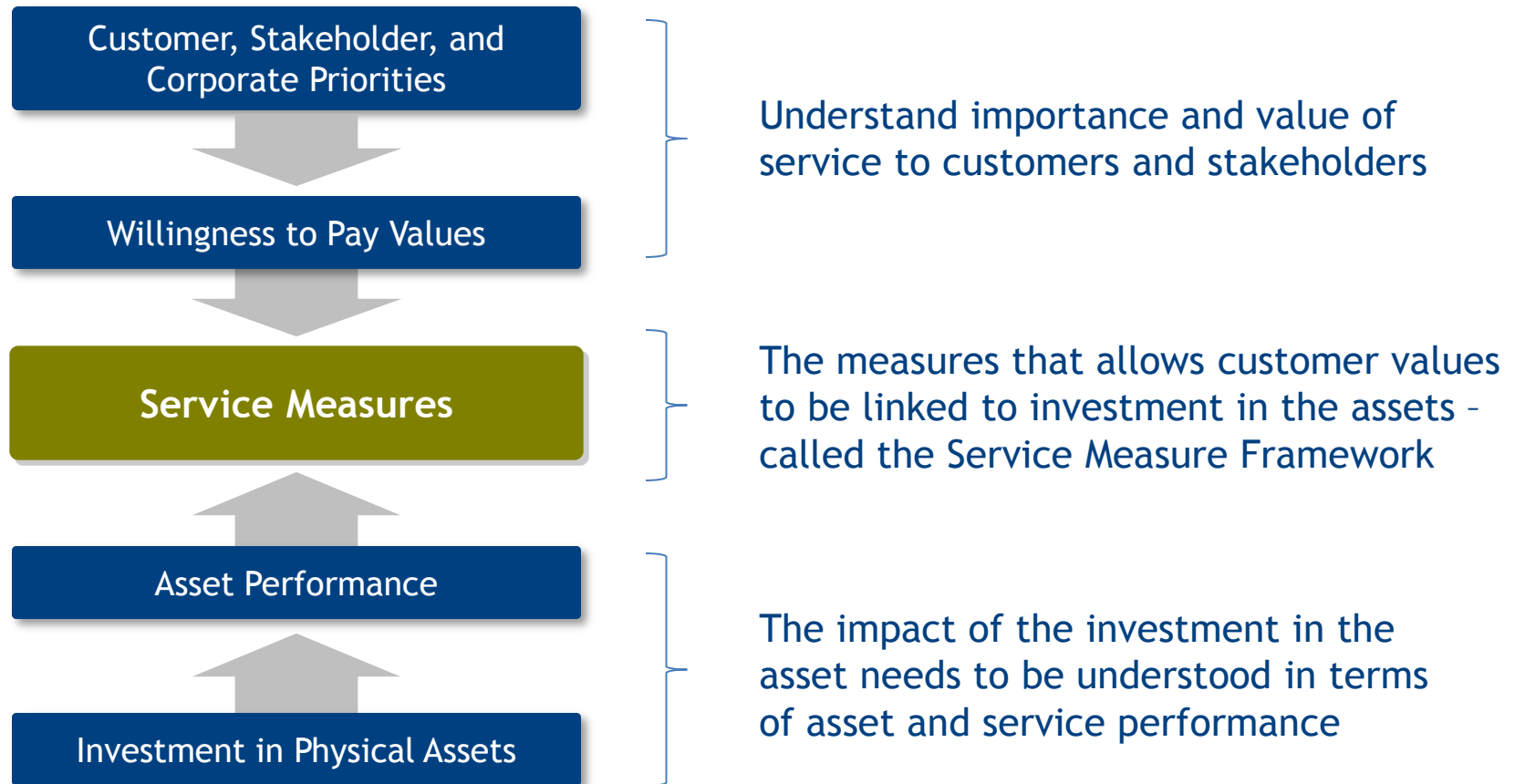


How do we decide what the right level of investment and performance is?



- We need to decide the cost and performance combination
 - For all performance areas
- How do we select the right level?
 - Are historic levels the right level?
 - Are current or improved levels robust?
 - What do customers want?

We first step is to define what service measures are important - to customers, stakeholders and the business



How do we agree the set of measures?

- Based on engagement with customers and stakeholders; prior experience and industry guidance
- Needs to reflect what service is important to maintain with customers
 - it is not just about what may need to be improved

Supply interruptions

Taste and smell of water

Discolouration

Drinking water notices

Pollution

Flooding to properties

Low pressure

Hosepipe bans

Low flow rivers

Leakage

Hardness

How do we determine willingness to pay for the service measures?

Revealed Preference

Observing market data to derive £ (WTP)

e.g. how are house prices impacted by noise, proximity to sites, etc

More robust but limited application

Stated Preference

Asking passengers about hypothetical scenarios to determine preferences and £ (WTP)

Widespread application

Need to careful to get robust results

Benefits/Value Transfer

Take values from setting and apply to another

Need to ensure transferability - does not apply to all customer issues, but works for H&S and some environmental issues

Stated preference studies are the prime method

- Stated Preference methods are well established
- Essentially this is a form of market research questionnaire with several stages:
 1. Understand customer preferences and select attributes to test
 2. Undertake stated preference exercises (choice experiments)
 3. Model the relationship between customers' preferred service levels and their willingness-to-pay in monetary terms - £/ unit change
- These techniques and methods are subject to academic rigour
- Taking into account industry guidance (UKWIR study)
- Methods are continually developing

The studies involve presenting choices to customers....
these choices reveal preferences and trade-offs

EXAMPLE

To derive £
need to
include bill
or money
impacts

CHOICE CARD 1

	<i>Alternative O</i> Current position	<i>Alternative A</i>	<i>Alternative B</i>
Properties with <u>unplanned interruptions</u> to water lasting more than 12 hours	8 in every 10,000 properties (=3,000 per year)	16 in every 10,000 properties (=6,000 per year)	2 in every 10,000 properties (=750 per year)
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Change to <u>annual bill</u>	No Change	No Change	Increase by £15
Please tick ONE box			

In delivering these studies:

- Limited to circa 12 service measures per survey
- Need clearly defined attributes - rigorously tested with customers
- Survey customers as to their preferences for service-bill combinations
- Depending on issues to be explored more than one study maybe required
 - To cover all the attributes of interest
 - To deal with specific issues that may require a separate study

Stages of a stated preference study

Engagement with customers

What issues concern customers, what are priorities

How to phrase the questions with customers

To understand the set of service measures of relevance

Design of the survey questionnaire

Develop draft questionnaire

Pilot study to test

Revisions and amendments to produce final choice experiment questionnaire

Fieldwork

Survey completed by domestic and non-domestic customers

Analysis and conclusions

Assessment of priorities, WTP

Understanding of what factors drives WTP and thus breakdown by customer type and business sector

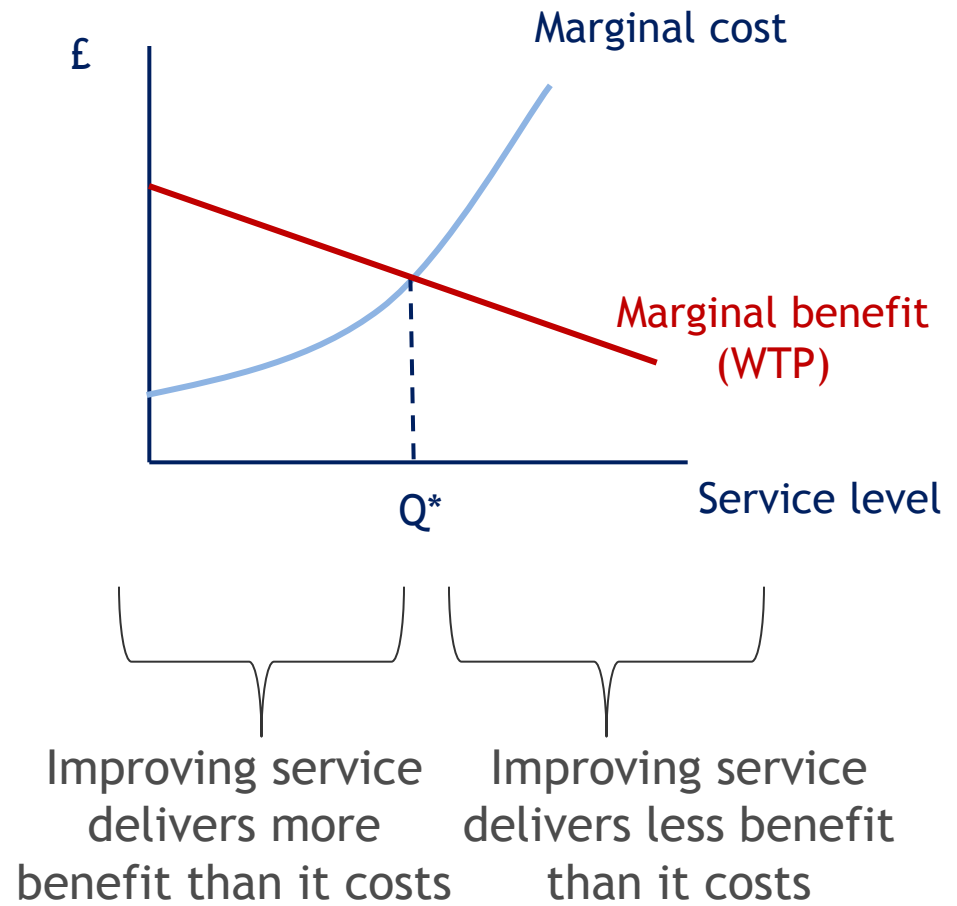
Assurance and accreditation:

Code of conduct of the Market Research Society, Data Protection Act

Academic rigour and peer review

We use WTP - together with investment costs - in a Cost Benefit Assessment

- CBA brings benefits and costs together in an assessment
- When $MB > MC$, investment is economic
- We need to measure the MB line - i.e., the WTP



How are the values used in CBA?

- The benefit of investment is applied to the change in service
- Probability of failure x Quantity Impacted x Consequence/Severity



WTP Applied to the
Consequence

- Example - each year there is a 10% chance of 100 customers suffering 6 hour interruption to supply. This reduces to 5% after investment. The WTP is £200 per interruption.
- Benefit of Investment = Pre Risk - Post Risk
$$= (10\% \times 100 \times £200) - (5\% \times 100 \times £200) = £2000 - £1000 = £1,000 \text{ per year}$$
- These values are used in a Net Present Value assessment

What is Net Present Value?

- Costs are discounted back to the present value of costs (PVC)
- Benefits are discounted back to the present value of benefits (PVB)
- The difference is the Net Present Value
- Example:
 - Benefits £2k per year for 40 years
 - Discounted at 3.5% is £44k in present value
 - Costs discounted to get PVC
 - If the PVC is less than this, investment is economic

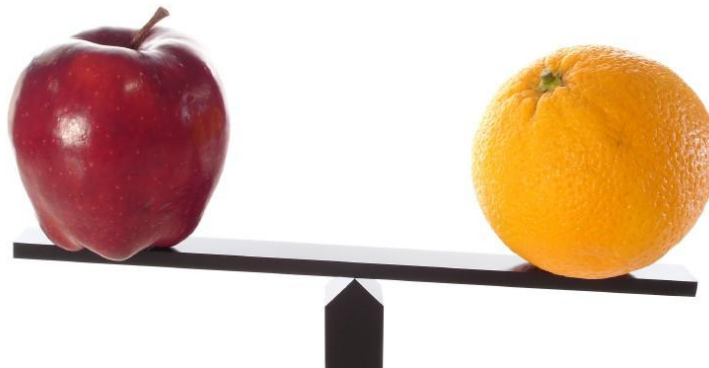
	Benefits	Discount Rate (5%)	PV Benefits
Year 1	2000	1	£2,000
Year 2	2000	0.97	£1,932
Year 3	2000	0.93	£1,867
Year 4	2000	0.90	£1,804
Year 5	2000	0.87	£1,743
Year 6	2000	0.84	£1,684
Year 7	2000	0.81	£1,627
Year 8	2000	0.79	£1,572
Year 9	2000	0.76	£1,519
Year 10	2000	0.73	£1,467
Year 11	2000	0.71	£1,418
Year 12	2000	0.68	£1,370
Year 13	2000	0.66	£1,324
Year 14	2000	0.64	£1,279
Year 15	2000	0.62	£1,236
Year 16	2000	0.60	£1,194
....
Year 39	2000	0.27	£541
Year 40	2000	0.26	£523
TOTAL			£44,205

Summary of WTP

- WTP Surveys have widespread application and are key part of assessing the value of non-monetary services
- But - there are typically gaps after the surveys are completed
- These gaps are filled value transfer from legitimate studies, e.g.:
 - HSE, Carbon, Congestion
- Key lessons learnt:
 - Peer review of valuations and application advisable
 - The valuations are subject to uncertainty and a range is appropriate
 - Some aspects of service are too difficult to value
 - Using WTP is only one part of the decision making process

Summary of Using WTP in CBA

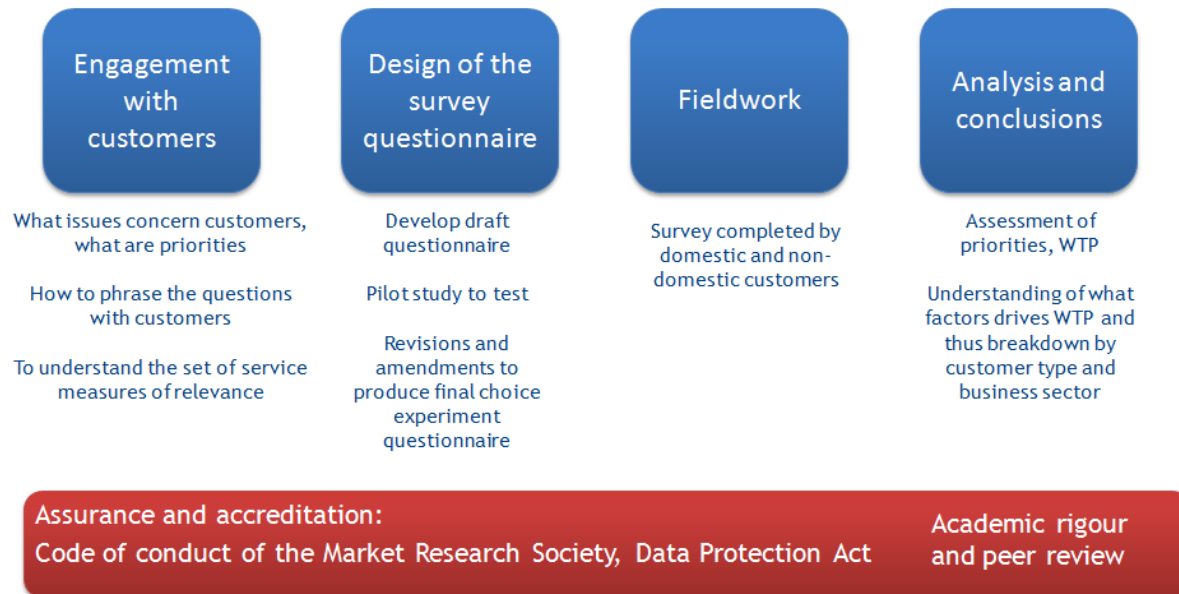
- Cost Benefit Analysis (CBA)
 - *What is the right level of investment given the economic value of services provided?*
 - *How much should we spend to improve service or reduce risks, if at all?*
- All benefits and all costs are expressed as monetary values and are discounted and summed in an NPV assessment
- Allows us to compare investments with different impacts



The WTP studies at Affinity

Affinity Water

- This process is being undertaken with Affinity Water for two studies



- Main Study - to give values for wide range of service impacts
- Water Resources - to provide specific input into the WRMP process

What attributes to include?

- Developed collaboratively with Affinity Water:
 - Engagement with customers - series of focus groups, building on work already undertaken by Affinity
 - Lessons learnt from PR09
 - Regulatory requirements (e.g., reporting indicators)
 - Consideration of what may be important for other stakeholders
 - UKWIR guidance

Attributes in the Main and the Water Resources Studies

- **Tap water quality**
 - Discoloured water
 - Taste and smell of water
 - Drinking water restrictions
 - Water hardness
- **Reliability of your water supply**
 - Low water pressure
 - Unexpected interruptions to water supply
 - River pollution
 - Burst Mains Flooding to Properties
- **Environment**
 - Hosepipe bans (NEUB for business)
 - Low water levels and flow in rivers
 - Leakage
- **Water Use Restrictions**
 - Hosepipe Bans - duration and frequency
 - NEUB: Non Essential Use Bans - duration and frequency
- **Water Options**
 - Water efficiency in homes
 - Fix leaks in water supply pipes
 - Install water meters
 - Transfer from other regions
 - Taking water from rivers
 - Taking water from the ground
 - Take water from the sea

Each survey has a similar structure

- Screening and quota questions
- Section A - Background (warm up, quota data)
- Section B - Service priorities (choice experiments)
- Section C - Follow up questions
- Section D - Socio economic questions (further quota data)

The Project Timeline

- Draft surveys developed and tested with customers
- Review by wider stakeholders welcomed and encouraged
- Currently developing pilot surveys
- Main study:
 - Pilot fieldwork about to commence
 - Main fieldwork commences on 1 July
 - Comments on survey due 24 June to be incorporated into final survey
- Water resources
 - Pilot and main fieldwork commence one week after the Main
 - Comments on survey due 1 July to be incorporated into final
- Results due end August/early September

Review of current version - online demo

Affinity Water

Willingness to Pay (WTP) and its role in putting together business plans

May 2013

Capital Investment Portfolio Optimiser

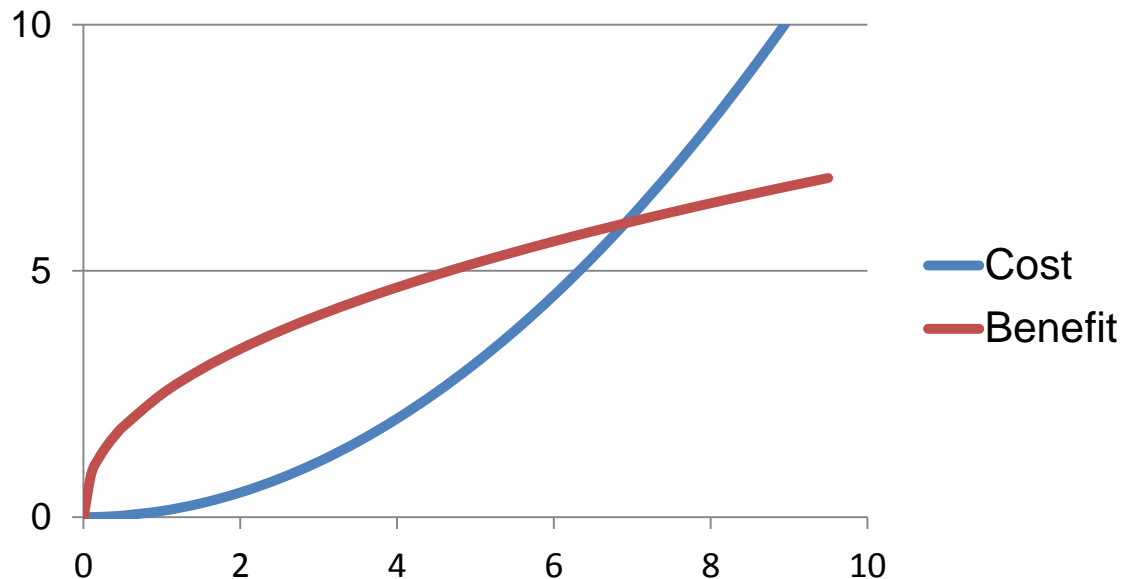


Tim Yearsley
Joe Sanders



PIONEER

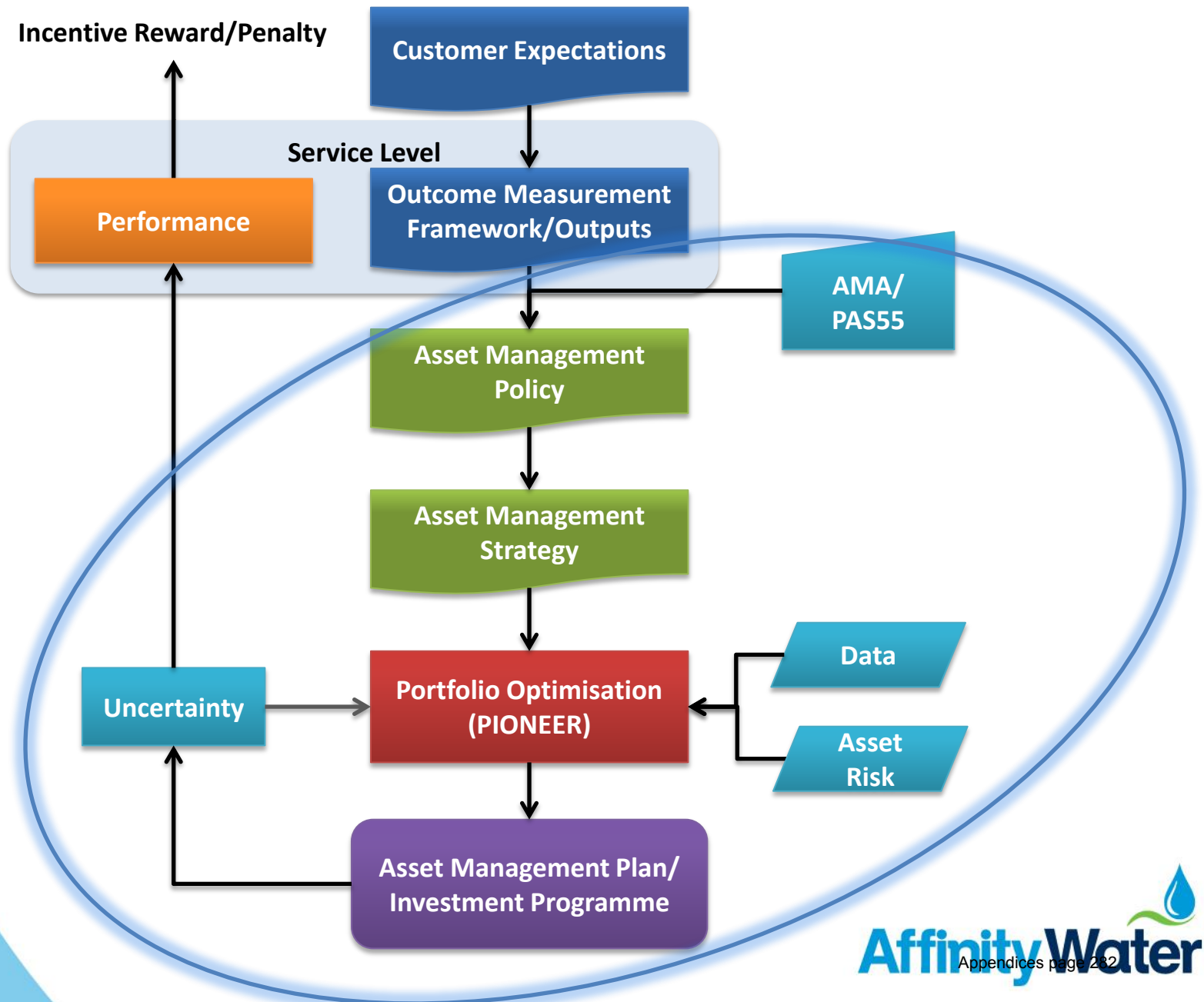
- Commercially available software tool
- Purpose
 - Optimisation of capital investment for business planning
- Objective
 - Optimise service level for the customer at least cost
 - Optimise within constraints



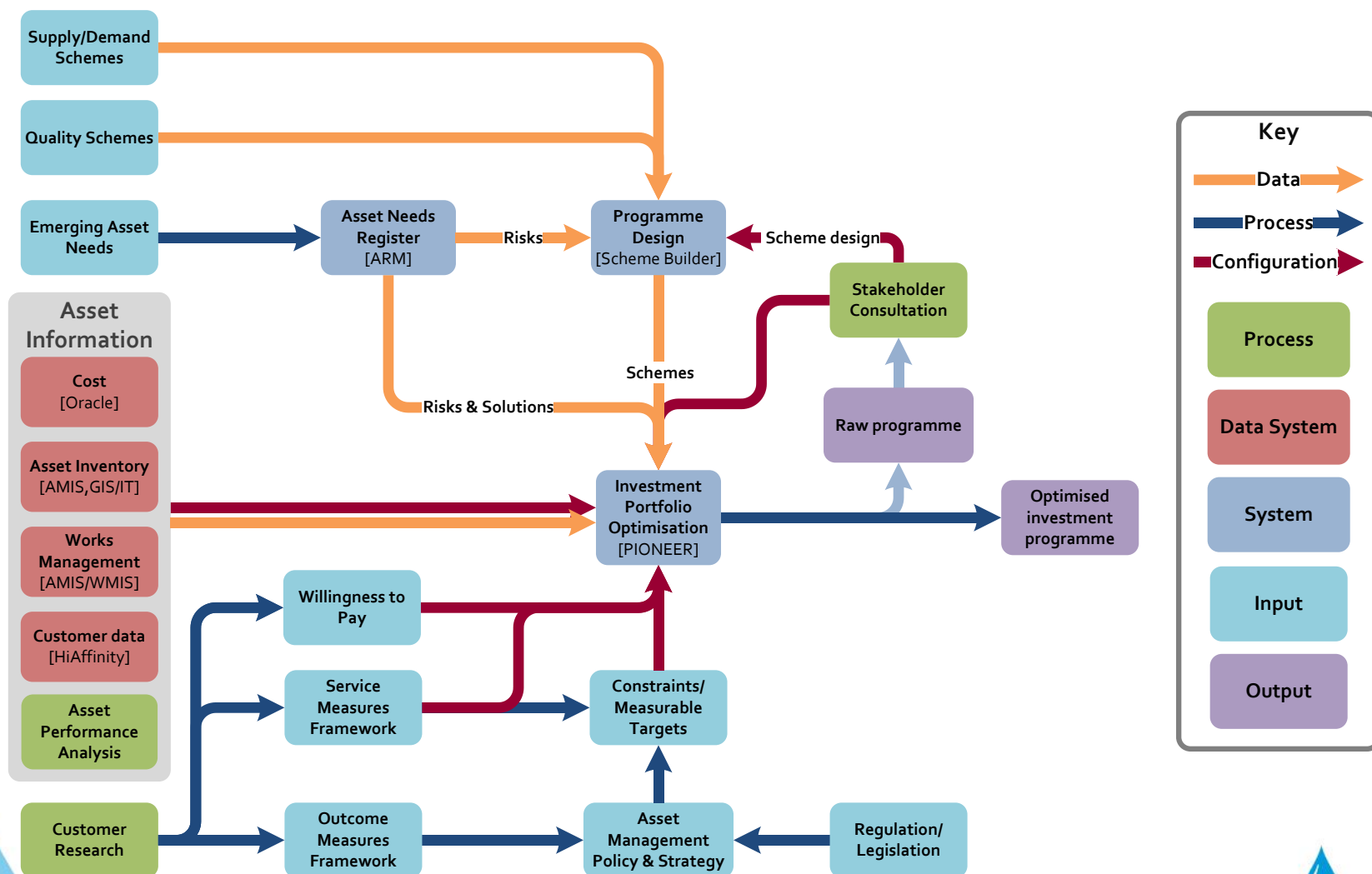
Benefits

- Portfolio and Programme views
 - Optimise investment in different business areas
 - Collectively
 - Separately
 - Optimise multiple intervention options / Schemes
- Reporting tools
- Audit trail
- Configurable
 - Forecasting future Service levels and costs
 - Impact of maintenance interventions



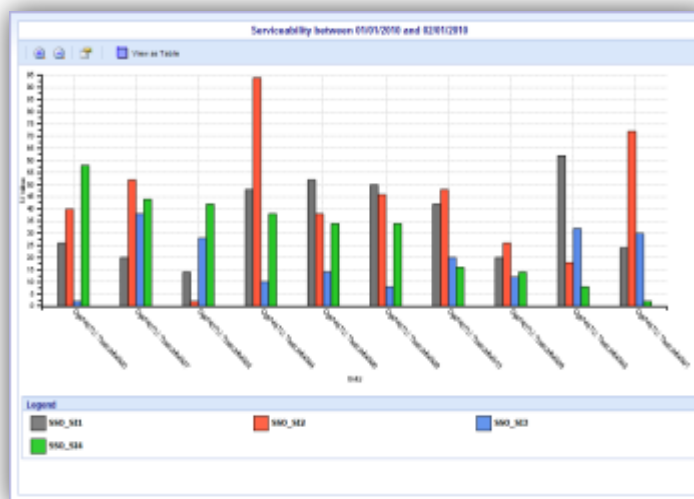


PIONEER Process



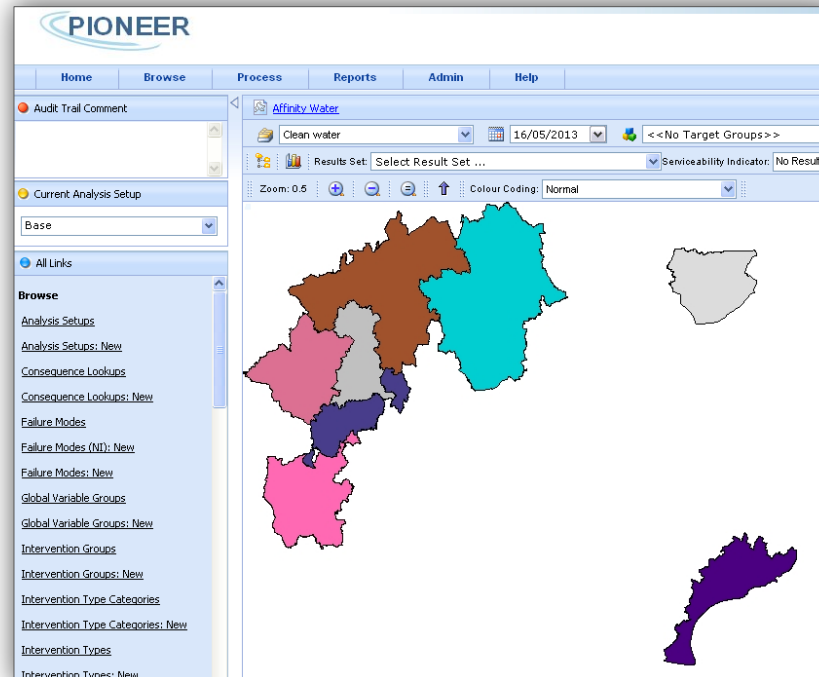
What are the outputs?

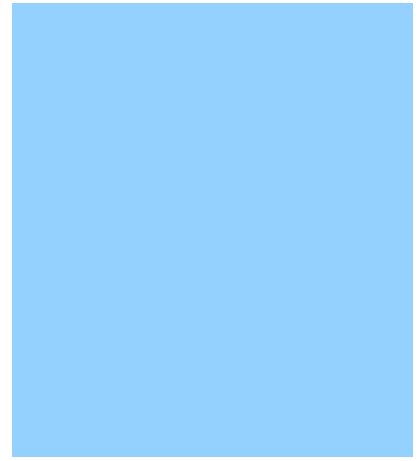
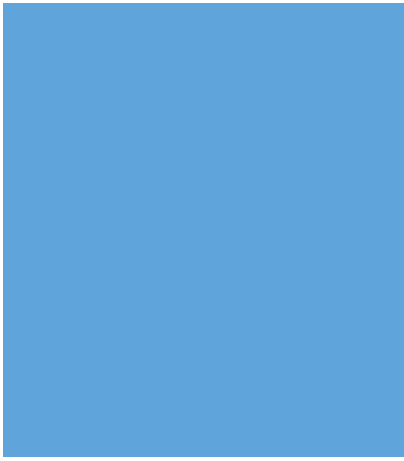
- PR14
 - Optimised Portfolio
 - Basis on which to build Business Plan
 - Reporting
 - Information for SDM
- Business as Usual
 - Re-prioritisation of investment
 - Optimisation of new needs



Schedule

- First full optimisation *Imminent*
- Iterations to support business plan *Jun-Oct 2013*





eftec
economics for the environment

ICS
consulting



*PR14 Willingness to Pay
Survey: Pilot Study*

*Report Submitted to
Affinity Water Limited*

June 2013

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CONTENTS

EXECUTIVE SUMMARY	5
BACKGROUND	5
STUDY FRAMEWORK	5
PILOT RESULTS	8
SURVEY IMPROVEMENTS	8
FEEDBACK	8
 1 OVERVIEW	 9
1.1 BACKGROUND	9
1.2 PROJECT OBJECTIVES	9
1.3 STUDY FRAMEWORK	10
 2 METHODOLOGICAL APPROACH	 12
2.1 VALUATION FRAMEWORK	12
2.2 QUALITATIVE RESEARCH - FOCUS GROUPS	13
2.3 QUALITATIVE RESEARCH - COGNITIVE TESTS	15
2.4 CONTENTS OF PILOT STUDY	17
2.5 EXPERIMENTAL DESIGN	19
 3 HOUSEHOLD RESULTS	 20
3.1 SAMPLE REPRESENTATIVENESS	20
3.2 SAMPLE PROFILE	21
3.3 PERCEPTIONS OF SERVICE LEVELS	24
3.4 AWARENESS OF SEWERAGE BILL	25
3.5 RESPONDENT FEEDBACK	26
3.6 ECONOMETRIC RESULTS	27
3.7 PACKAGE ANALYSIS	30
 4 BUSINESS RESULTS	 32
4.1 SAMPLE REPRESENTATIVENESS	32
4.2 PERCEPTIONS OF SERVICE LEVELS	34
4.3 AWARENESS OF SEWERAGE BILL	34
4.4 RESPONDENT FEEDBACK	36
4.5 ECONOMETRIC RESULTS	37
4.6 PACKAGE ANALYSIS	39

5	<u>NEXT STEPS AND CONCLUSIONS</u>	<u>40</u>
5.1	DEVELOPMENT OF MAIN STUDY	40
5.2	CONCLUSIONS	40
<u>DOCUMENT CONTROL</u>		<u>41</u>

Executive Summary

Background

For the 2014 Price Review (PR14) Affinity Water wants to ensure that the investments proposed in its Business Plan are worthwhile and represent value for money for customers. The development of Affinity Water's Business Plan will be supported by the use of cost-benefit analysis (CBA) to appraise all potential investments in water services. The use of CBA enables Affinity Water to directly compare the financial costs of investments - which, ultimately, are paid for by customers' bills - to the benefits of those investments, in terms of maintained or improved service levels to customers.

The objective of the Affinity Water PR14 Willingness to Pay Study is therefore to provide benefit estimates to input to the cost-benefit analysis (CBA) that will support Affinity Water's PR14 investment planning. The requirements for the study include:

- To estimate the societal value - in monetary terms - of the impact of changes in water quality, reliability of supplies, and water resources service levels;
- To build on work undertaken at PR09 and subsequently the outputs of recent UKWIR studies concerning the application of WTP studies and CBA; and
- To ensure that Affinity Water applies best practice in the water industry in the application of WTP studies and CBA.

Willingness to Pay studies are questionnaire-based stated preference techniques that involve asking survey respondents - a sample of domestic and non-domestic customers - to complete choice tasks that gather information on their preferences for changes in service levels.

Study Framework

The study framework is consistent with good practice for the implementation of stated preference surveys. The key stages of the study are as follows:

- **Valuation Framework and Scoping:** initial consultation has been carried out with Affinity Water to confirm the scope of the WTP study and the range of service areas that may be of interest. The output of this phase of work was the Valuation Framework, which outlines the service measures needed for CBA assessment, and the valuation technique to be applied. This underpins the application of CBA for PR14 investment planning.
- **Survey design and qualitative testing:** a detailed phase of qualitative testing has been undertaken, including focus groups and cognitive interviews with domestic customers and in-depth telephone interviews with non-domestic customers. These have focused on respondent understanding of the survey material, such as the definitions of water related service attributes presented to respondents, and the framing and phrasing of questions.
- **Experimental design:** in-parallel to the qualitative testing the specification of the design and implementation of the choice tasks has been undertaken. This provides the range of alternatives that respondents are presented with. The experimental design fixes the number of service attributes to be included in a choice task and the number of choice tasks to be administered to respondents. Both these elements are important with respect to the cognitive burden imposed by the survey on respondents.

- **Pilot survey:** this involves drawing together the outcomes from the qualitative testing and testing in a pilot study. This allows the assessment of the cognitive burden imposed on respondents by the format of the choice tasks in a basic field test of the questionnaire.
- **Peer review:** this involves collating feedback from the Pilot Study, comments from the Peer Reviewer and other stakeholders to develop the final questionnaire.
- **Main survey:** the main survey sampling covered both domestic and non-domestic customers across all three regions. A key feature of the domestic survey is the intention to split the sample survey implementation using face to face interviews and online techniques. For non-domestic customers, the telephone recruitment to an online survey is expected.

We are currently progressing through this process; this report summarises the output of the Pilot Survey stage.

The Main Survey will commence on 1 July, taking into account the feedback from the Pilot Study, the Peer Review and any stakeholder views.

Pilot Study Attributes

Based on a robust process of qualitative research with customers and the development of a Valuation Framework, the measures included in the first stage stated preference (SP) study were:

- Drinking water notices (combined boil and do not drink)
- Hardness
- Discolouration
- Taste & Odour
- Low pressure
- 6-12 hour supply interruption (plus ranking exercise for other severities)
- Water flooding to properties
- Hosepipe bans
- Low flow river
- Minor pollution
- Leakage

In order for choices across all these attributes to be 'manageable' from the perspective of respondent cognition, the service attributes were split into choice experiment 'blocks'.

The allocation of attributes to blocks for the pilot study was:

Table E.1: Choice experiment blocks

Block	WS1 (Tap Water Quality)	WS2 (Reliability of Water Supplies)	WS3 (Managing Water Supplies)
Attributes	Discolouration	Low pressure	Water Use restrictions
	Taste and smell	Unexpected SI	Low flow rivers
	Hardness	Burst Mains Flooding to Properties	Leakage
	Drinking water restrictions	-	-
	Water bill	Water bill	Water bill

There are three choice experiment blocks. One has four service attributes plus bill, and the other two have three service attributes plus bill:

- WS1 block - a set of attributes concerned with the quality of tap water (discolouration, taste and smell, hardness and drinking water restrictions)
- WS2 block - a set of attributes concerned with the reliability of water supply (water use restrictions, low flow rivers and leakage). Note for domestic customer the water use restriction is hosepipe bans, but is non-essential use bans for non domestic.
- WS3 block - a set of attributes concerned with managing water supplies (taste and odour, and discolouration) and inconvenience associated with restrictions on the use of tap water in the home ('boil water' notices).

Overall the design specified 60 choice cards for each choice experiment block. This was divided into 10 blocks of six choice cards each. Each respondent saw one of the 10 blocks allocated at random, and answered 6 choice cards on each of the three key areas.

Different performance levels for the attributes were presented to pilot survey respondents. The highest level for each attribute generally represents an 'aspirational level', seen as the highest service level that can be achieved within the current constraints of asset planning. The lowest level generally represents the maximum deterioration in service, but not below minimum standards required by water industry regulators.

The specification of attribute levels across improvements and deteriorations in services, along with two levels of improved service, implies that non-linear effects (gains-loss asymmetry and diminishing marginal benefits) should be achieved for most of the measures.

The bill attribute levels were defined in terms of the change in the current bill amount paid by the respondent. For domestic customers this was presented in terms of the annual water and sewerage bill as a £ amount. The bill levels were specified to be symmetrical around a 'no change' amount, following results from the pilot survey. For businesses this was presented as a percentage change in the bill from its current level.

Pilot Results

A sample of 100 household respondents and 88 business customers completed the pilot survey. The results were examined with the aim of developing the final survey. Despite no formal quotas being set on the respondents, there was a good mix of respondents in the samples.

The survey was administered successfully. The econometric analysis of the pilot choice experiment data shows the survey has worked well for both samples. The primary focus of the analysis was to determine whether the pilot experimental designs worked satisfactorily. That is, whether the estimated coefficients have the expected signs. The results of the pilot analysis are used to update and improve the efficiency of the experimental choice designs. This helps improve the precision of the resulting estimates of willingness to pay from the main fieldwork datasets.

The econometric results consisted of basic statistical (conditional logit) models. For the main fieldwork analysis we will report a wider range of models.

The survey was sent for Peer Review, with Professor Ken Willis. Professor Willis was very positive about the survey, making only minor suggestions for improvements to wording for the Main Fieldwork.

Survey Improvements

Both feedback from the survey respondents and the recorded interview duration suggested that the survey in its pilot form is a little too long. A survey that is too long can start to impact on the quality of responses if fatigue becomes an issue.

To address this we have updated the survey so that in the Main survey respondents will only complete two out of the three choice blocks. Each respondent will be randomly assigned any two of the three blocks, each block will consist of 8 choices and not 6 choices as per the pilot. Overall each respondent therefore sees less attributes and less choices. However, rotation of the blocks through the sample, together with the extra choices per block, will provide the information that is required for analyses.

We have also improved the routing to provide customer specific sewerage provider information. This will reduce the amount of reading required by the respondent helping to shorten the survey without compromising the information being provided or collected.

The final change of note relates to the wording of two attributes. We observed a very high number of respondents stating they had experienced drinking water restrictions. It is possible that the attribute descriptions are causing confusion, with drinking water restrictions prompting associations with water use restrictions. To address this we have changed the attribute descriptions to create a clearer division between them. Drinking water restrictions are renamed “boil water and other notices” and water use restrictions are renamed “hosepipe bans” for households, “non-essential use bans (hosepipe restrictions)” for businesses.

Feedback

The Main questionnaire fieldwork is due to commence on 1 July. Any peer review or stakeholder comments should be provided by 24 June so they are incorporated fully into the final survey.

1 Overview

1.1 Background

For the 2014 Price Review (PR14) Affinity Water wants to ensure that the investments proposed in its Business Plan are worthwhile and represent value for money for customers. In the policy statement '*Involving customers in price setting*' Ofwat (2011) established that water companies are directly responsible for customer engagement, with the underlying expectation that this engagement will play a significant role in shaping the PR14 Business Plans, both in terms of the investment priorities that are identified and the acceptability of service levels that are subsequently delivered.

The development of Affinity Water's Business Plan will be supported by the use of cost-benefit analysis (CBA) to appraise all potential investments in water services. The use of CBA enables Affinity Water to directly compare the financial costs of investments - which, ultimately, are paid for by customers' bills - to the benefits of those investments, in terms of maintained or improved service levels to customers.

To facilitate this process, Affinity Water has prepared a Valuation Framework that identifies the full set of service measures that are relevant to the application of CBA, and the valuation technique to be applied. Within this a subset of measures, such as interruptions to supply, low water pressure, discoloured tap water, and water use restrictions, relate directly to the benefits of water service that are experienced by customers.

1.2 Project Objectives

The objective of the Affinity Water PR14 Willingness to Pay Study is to provide benefit estimates to input to the cost-benefit analysis (CBA) that will support Affinity Water's PR14 investment planning.

The requirements for the study include:

- To estimate the societal value - in monetary terms - of the impact of changes in water quality, reliability of supplies, and water resources service levels;
- To build on work undertaken at PR09 and subsequently the outputs of recent UKWIR studies concerning the application of WTP studies and CBA; and
- To ensure that Affinity Water applies best practice in the water industry in the application of WTP studies and CBA.

Willingness to Pay studies are questionnaire-based stated preference techniques that involve asking survey respondents - a sample of domestic and non-domestic customers - to complete choice tasks that gather information on their preferences for changes in service levels.

These studies apply a combination of the 'choice experiment' (CE) and 'contingent valuation' (CV) methods. Respondents are presented with differing trade-offs between improvements and deterioration in different water-related service areas along with changes in bill levels. The trade-offs that respondents are willing to make between service levels and bill amounts reveals the benefits of investments that maintain or improve service. In particular the trade-offs measure in monetary terms what customers are prepared to 'give up' to secure a specified level of service. This trade-off is the 'willingness to pay' (WTP) measure of benefits and is the appropriate input to CBA.

1.3 Study Framework

The study framework is consistent with good practice for the implementation of stated preference surveys. The figure below documents the key stages of the study. These are summarised as follows:

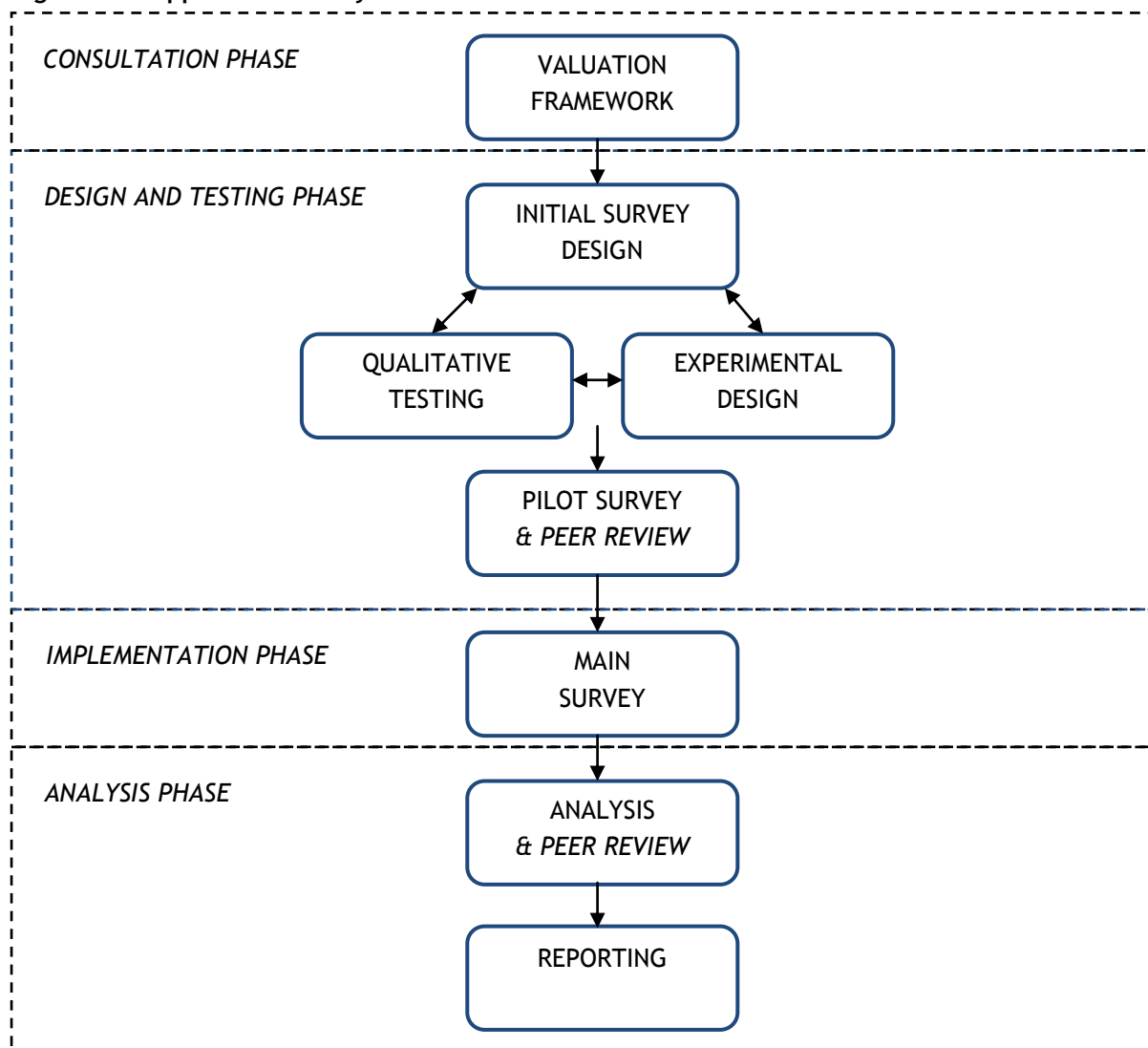
- **Valuation Framework and Scoping:** initial consultation has been carried out with Affinity Water to confirm the scope of the WTP study and the range of service areas that may be of interest. The output of this phase of work was the Valuation Framework, which outlines the service measures needed for CBA assessment, and the valuation technique to be applied. This underpins the application of CBA for PR14 investment planning.
- **Survey design and qualitative testing:** a detailed phase of qualitative testing has been undertaken, including focus groups and cognitive interviews with domestic customers and in-depth telephone interviews with non-domestic customers. These have focused on respondent understanding of the survey material, such as the definitions of water related service attributes presented to respondents, and the framing and phrasing of questions.
- **Experimental design:** in-parallel to the qualitative testing the specification of the design and implementation of the choice tasks has been undertaken. This provides the range of alternatives that respondents are presented with. The experimental design fixes the number of service attributes to be included in a choice task and the number of choice tasks to be administered to respondents. Both these elements are important with respect to the cognitive burden imposed by the survey on respondents.
- **Pilot survey:** this involves drawing together the outcomes from the qualitative testing and testing in a pilot study. This allows the assessment of the cognitive burden imposed on respondents by the format of the choice tasks in a basic field test of the questionnaire.
- **Peer review:** this involves collating feedback from the Pilot Study, comments from the Peer Reviewer and other stakeholders to develop the final questionnaire.
- **Main survey:** the main survey sampling covered both domestic and non-domestic customers across all three regions. A key feature of the domestic survey is the intention to split the sample survey implementation using face to face interviews and online techniques. For non-domestic customers, the telephone recruitment to an online survey is expected.

Analysis: a comprehensive analysis of the survey data, including estimation of the range of econometric models along with tests for non-linear effects in WTP, package effects and comparisons of results from the domestic face-to-face and online samples.

We are currently progressing through this process; this report summarises the output of the Pilot Survey stage.

The Main Survey will commence on 1 July, taking into account the feedback from the Pilot Study, the Peer Review and any stakeholder views.

Figure 1.1: Approach to study



2 Methodological Approach

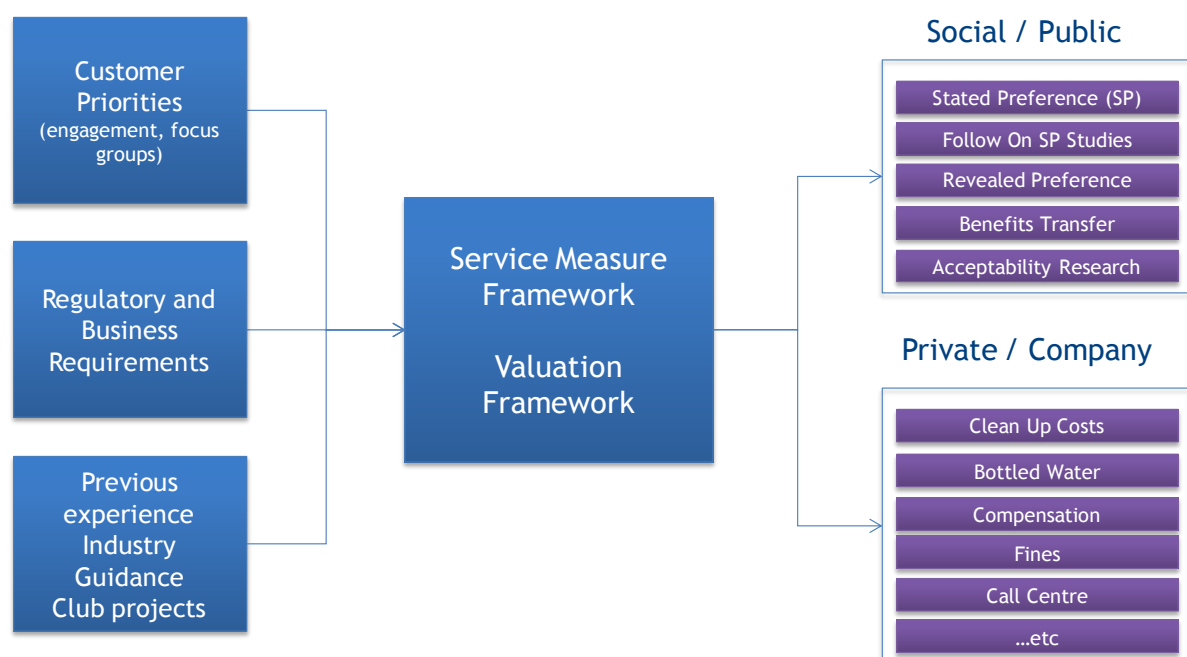
2.1 Valuation Framework

A key part of the WTP study was the development of the Valuation Framework. The Valuation Framework was the first step in the development of the customer willingness to pay surveys, and was developed collectively by Affinity Water and ICS Consulting.

At the heart of the approach to investment planning and cost benefit analysis within Affinity Water is the Service Measure Framework (SMF). This contains the full set of service measures that are of interest, either because they are valuable to customers or to Affinity Water; or because there is the need to report or constrain on them. The SMF includes a number of service measures such as different durations of supply interruptions, discoloured drinking water, water use restrictions, etc. Its development has taken into account customer priorities, lessons learnt from PR09, industry guidance, feedback from customer Focus Groups and the stakeholders, and regulatory and business requirements.

Affinity Water has spent considerable time updating the PR09 SMF and ensuring it is suitable for PR14. The findings from customer qualitative research, lessons learnt from PR09 and recent UKWIR studies around customer valuation were then used to finalise the SMF to ensure it meets customer requirements and can be aligned to customer valuation studies. This resulted in the Valuation Framework which formed the template for all of the customer research and development of estimates of private costs associated with service failures, as is shown in the figure below:

Figure 2.1: Development of Valuation Framework



There are multiple stages of valuation research that maybe appropriate - and were all considered in the development of the valuation framework:

- Main (first stage) study which gives wide coverage of a diverse range of service measures, such as supply interruptions, low pressure, water use restrictions, and taste and smell of water.

- Second stage studies which give the relative value of similar service impacts (such as different types of water use restrictions) or that consider different ways of delivering services (such as increasing leakage detection activity in order to reduce groundwater abstraction).

Valuation Framework Recommendation

The recommendation from the valuation framework was that the PR14 measures to be included in the first stage stated preference (SP) study should be:

- Drinking water notices (combined boil and do not drink)
- Hardness
- Discolouration
- Taste & Odour
- Low pressure
- 6-12 hour supply interruption (plus ranking exercise for other severities)
- Water flooding to properties
- Hosepipe bans
- Low flow river
- Minor pollution
- Leakage

It was also agreed that to complete the valuation framework would require additional research. These are as follows:

Second stage study:

- Water resources, to look at other forms of restrictions and water sources

Value transfer analyses

- Drinking water - illness values from HSE
- Carbon and renewable energy
- Congestion
- H&S

Consistent with PR09, there are other service measures for which a societal valuation is not recommended. This is either a result of the measures only having private costs, or the valuation being captured in other measures, and hence to avoid double counting.

2.2 Qualitative Research - Focus Groups

The valuation framework recommendation was tested in Focus Groups.

Focus groups are semi-structured discussion groups led by a moderator, in which participants are presented with topics pertaining to the design of the stated preference survey. Their use enables customer attitudes and perceptions concerning key issues to be reflected in the design of the

stated preference questionnaire, with an emphasis on ensuring credibility and that aspects such as the definition of attributes are meaningful and easily understood.

Six focus groups were undertaken in April 2013 with domestic customers in the Affinity Water region. Market Researcher Opinion Leader led the sessions. Ten participants were recruited to attend each focus group. Each focus group lasted 1½ hours.

Three locations were selected: Welwyn Garden City, Harwich and Dover. These locations were chosen to provide suitable coverage across the Affinity Water areas. Two groups were conducted in each location and based on Affinities main customer segments

Group 1

- A mixture of: own outright, owned with mortgage/ loan, private rented (min 2 of each per group)
- Household income £30k+

Group 2

- A mixture of: shared ownership, local authority rented, housing association rented (min of 2 of each per group)
- Household income under £30k

Affinity Water and its stakeholders viewed two focus groups in Welwyn Garden City.

The main role of the focus groups was to test and refine the descriptions of service attributes, particularly in terms of the show materials that would accompany the stated preference questionnaire. The set of attributes to test was developed in conjunction with input from Affinity Water, based on the content on the Valuation Framework. Initial attribute definitions were informed by Affinity Water's PR09 customer preference research and the template provided by the UKWIR (2011) *Carrying Out Willingness to Pay Surveys* report. Discussion areas in the groups included:

- Perceptions of utility services in general within the local area;
- Knowledge of water industry and the provision of water services;
- Perceptions of current levels of service received, including problems encountered in respect to the service attributes of interest;
- Understanding of attributes and descriptions, the extent of their relevance and the acceptability of such measures as criteria for delivery of service;
- The relative importance of different attributes and priorities for improvement;
- The perceived value of improvements to services, in terms of willingness to pay for changes in service levels; and
- Motivations towards the provision of services and improvements to them; i.e. whether willingness to pay was motivated by private values, public good values or altruistic (non-use) reasons.

A summary of headline findings from the focus groups is provided by Opinion Leader (2013) *'Willingness-To-Pay Qualitative Research Findings'*.

In general despite the essential nature of the services provided, customers felt these services were typically ‘taken for granted’. Participants typically said that they rarely if ever thought about the water services which were involved in delivering drinking water to their tap. Participants often had only a basic understanding and awareness of the water services that Affinity Water provides; for example supplying water to customers. This appears to stem from the fact that few participants had directly experience service failures and the view that the current level of service is high. This was coupled with the view that cost of the service (the annual water bill) was seen as relatively good value for money and inexpensive relative to other utilities.

The main priorities for service that were cited by participants (unprompted) included delivering a reliable supply of water, reducing hardness, fixing leaks, and ensuring a safe supply of drinking water.

Overall the findings from the groups reinforced the importance of the ‘content validity’ of the study and ensuring that respondents are able to effectively engage with the survey and that their responses reflect their genuine perceptions of service levels and the benefits of changes in these. The collective feedback from the groups has been used to modify individual attribute descriptions and showcards, as well as providing significant qualitative information on customers’ perceptions of service levels.

Specific changes made following the focus groups:

- Low water pressure - in the focus groups there was confusion about whether this was covered internal plumbing issues, with a number of respondents commenting on the impact of one appliance on another appliance or tap flow. The definition was amended to ensure that this is clear that this is the pressure into the property and not due to internal plumbing issues.
- Minor Pollution - this was changed to ‘River Pollution’ to clarify that it was not polluted tap water.
- ‘Water flooding to properties’ was changed to ‘Burst Mains Flooding to Properties’ to clarify that this is not river flooding.
- Drinking water notices - the expected duration of 2 to 3 days was added. Also that these are precautionary measures.
- Low water levels and flow in rivers - replace the term ‘visual amenity’ with ‘appearance’ as this term was not well understood.
- Water aesthetics - References to a week at a time of duration was confusing for both discolouration and taste/smell of water, so this is dropped.

In the focus groups the burst mains flooding, river pollution and protected wildlife were perceived to be lower priorities given the perceived high levels of performance in these areas. Despite this, all attributes were kept for the cognitive testing of the survey.

2.3 Qualitative Research - Cognitive Tests

A draft survey questionnaire was developed following the focus groups. All updates from the focus groups were taken into account in the survey development and were subsequently tested in the cognitive testing phase of the study.

Cognitive testing involves administering the draft stated preference questionnaire to a sample of respondents followed by a set of debriefing questions. The debriefing elicits qualitative feedback from respondents on questions and choice tasks in the main questionnaire. In general this permits the examination of a number of issues concerning the design of stated preference surveys, including respondent comprehension and retrieval of information (e.g. from attribute showcards), and respondent decision processes (e.g. mental effort, motivations behind choices, truth telling). Cognitive interviews are therefore highly useful in evaluating the validity of stated preference studies, especially when the topic area presented to respondents is complex.

In total fifteen cognitive testing interviews were undertaken in April 2013. Ten face-to-face interviews were conducted with domestic customers and five telephone interviews were conducted with non-domestic customers.

Key issues examined in the interviews included respondents’:

- Understanding of attribute descriptions and showcards;
- Understanding of the choice tasks (choice experiment and contingent valuation) and the clarity with which these were presented;
- Motivations for the choices made in the choice exercises;
- Perceptions of the credibility of the choice exercises; and
- Attitudes towards the payment vehicle in the choice exercises (the water bill).

The main findings from the interviews were similar across both domestic and non-domestic customers:

- Understanding of attribute descriptions and showcards is very high. All the respondents commented that the showcards were clear and made the attributes clear.
- Largely respondents reported no actual experience with most service failures and this appears to have been a key factor in their perceptions of the survey and choice tasks. The overwhelming feedback was that respondents were happy with current service levels.
- All respondents stated that the choice exercises were easy or relatively easy. The tap water quality block of choices was generally the easiest for respondents as they were more familiar with the attributes in this block. Some respondents commented that hardness was the key attribute of importance. Others attributes mentioned were low pressure, taste and smell of water, and environmental measures in general. For most respondents, the bill attribute was the most important factor in choices.
- Feedback from respondents on the motivations for their choice exercise responses suggests these were largely based on potential impacts to their household (i.e. they are currently satisfied with service levels and do not think that improvements in service that raise bills are necessary). Some respondents commented that any improvements would not impact on them and thus would be altruistic.
- All respondents were able to recall in the debriefing questions that bill increases would be from 2015 and would be on top of already determined improvements. The presentation of the separate sewerage bill was clear to all respondents.
- In general most respondents seemed reticent about service deteriorations with lower bills or service improvements with higher bills.
- No respondents commented that the survey was too long.

There was some challenge of the river pollution attribute on the grounds of whether it was an issue or not. This echoed the findings of the focus groups.

2.4 Contents of Pilot Study

Attributes and levels

The table below presents the set of service attributes and the definitions. Based on the feedback of the focus groups and cognitive tests, river pollution was dropped. This decision was also based on the fact that there are very few of these in reality (10 per year).

Table 2.1: Attributes and Levels

	-3	-2	-1	Current Level	1	2	3	4
Discolouration (nr properties)	-	48,000 (3.4%)	36,000 (2.6%)	24,000 (1.7%)	18,000 (1.3%)	12,000 (0.9%)	-	-
Taste and smell (nr properties)	-	48,000 (3.4%)	36,000 (2.6%)	24,000 (1.7%)	18,000 (1.3%)	12,000 (0.9%)	-	-
Hardness (nr properties)	-	-	-	1.4m (100%)	1.33m (95%)	1.26m (90%)	1.19m (85%)	1.12m (80%)
Drinking water restrictions (nr properties)	2000 (0.14%)	1000 (0.07%)	500 (0.01%)	<5	-	-	-	-
Unexpected SI (nr properties)	-	13,000 (0.9%)	10,000 (0.7%)	7,000 (0.5%)	4,000 (0.3%)	1,000 (0.1%)	-	-
Low pressure (nr properties)	-	1000 (0.07%)	500 (0.01%)	100 (0.01%)	0		-	-
Water Use restrictions (hosepipe ban) -frequency	-	25% (1 in 4)	15% (1 in 7)	10% (1 in 10)	5% (1 in 20)	3% (1 in 33)		
Water Use restrictions (NEUB) -frequency	-	15% (1 in 7)	10% (1 in 10)	5% (1 in 20)	3% (1 in 33)	2% (1 in 50)	-	-
Leakage (% water lost)	-	26%	22%	19%	15%	12%	-	-
Low flow rivers (% river lengths)	-	16%	12%	8%	4%	0%	-	-
Burst Mains Flooding to Properties (nr properties)	-	1000	500	250	0	-	-	-

Levels were specified on the basis of Affinity Water's asset planning data and historical service performance and generally incorporated Levels -2, -1, 0, 1 and 2:

- Level 2: the maximum improvement in service currently feasible for the period 2015-20
- Level 1: improved service from current level of service
- Level 0: the 'status quo'/current level of service, typically based on average performance levels over recent years
- Level -1: deteriorated service from current service level
- Level -2: the maximum deterioration in service, typically based on the 'worse' observed performance for an attribute.

Note:

- Hardness has nearly 100% of properties affected, so only has the current and improved levels. Four levels are presented.
- Drinking water restrictions is almost zero, so only has current and deteriorated levels. Four levels are presented
- Burst water mains flooding to properties is quite rare, so only has one improvement level, the current level, and two deteriorated levels.

The highest level for each attribute generally represents an 'aspirational level', seen as the highest service level that can be achieved within the current constraints of asset planning. The lowest level generally represents the maximum deterioration in service, but not below minimum standards required by water industry regulators.

The specification of attribute levels across improvements and deteriorations in services, along with two levels of improved service, implies that non-linear effects (gains-loss asymmetry and diminishing marginal benefits) should be achieved for most of the measures.

The bill attribute levels were defined in terms of the change in the current bill amount paid by the respondent. For domestic customers this was presented in terms of the annual water and sewerage bill as a £ amount. The bill levels were specified to be symmetrical around a 'no change' amount, following results from the pilot survey.

Bill levels for the domestic pilot:

- -£50
- -£30
- -£20
- -£10
- £0
- £5
- £10
- £15
- £20

For non-domestic customers the bill was presented as a percentage amount (%) to accommodate the much greater variation in bill amounts paid.

2.5 Experimental Design

One of the key features of choice experiments is the use of experimental design theory to optimise the amount of customer preference information that can be collected from a sample of a given size. In particular there are numerous ways in which service attribute levels can be combined into bundles of water services. In addition there are many more ways of combining these into sets from which respondents are asked to choose their preferred alternative. The purpose of the choice experiment design task is to ensure that the effects of interest - i.e. respondents' preferences for changes in attribute service levels - can be adequately and efficiently estimated from the available sample size. The design therefore specifies combinations of attribute levels for each choice task faced by a respondent; i.e. it determines which levels of attributes are presented on a given choice card in a choice experiment.

The typical practice in choice experiments of the type implemented in the study is to present two or three alternative options on each choice card. In this case three options were included with one specified as a fixed 'status quo' option where all attributes are specified at their current level ('Level 0') with no change in the current bill level. This allows respondents to select a 'no improvement/deterioration' option at no extra cost in a given choice task. With this approach it is also possible to directly control for the preference customers may have for maintaining current service levels, rather than 'forcing' them to opt for changes in service levels and bills.

In order for choices to be 'manageable' to respondents from the perspective of respondent cognition, the service attributes were split into choice experiment 'blocks'. The allocation of attributes to blocks for the pilot study was:

Table 2.2: Choice experiment blocks

Block	WS1 (Tap Water Quality)	WS2 (Reliability of Water Supplies)	WS3 (Managing Water Supplies)
Attributes	Discolouration	Low pressure	Water Use restrictions
	Taste and smell	Unexpected SI	Low flow rivers
	Hardness	Burst Mains Flooding to Properties	Leakage
	Drinking water restrictions	-	-
	Water bill	Water bill	Water bill

There are three choice experiment blocks. One has 4 service attributes plus bill, and the other two have 3 service attributes plus bill:

- WS1 block - a set of attributes concerned with the quality of tap water (discolouration, taste and smell, hardness and drinking water restrictions)
- WS2 block - a set of attributes concerned with the reliability of water supply (water use restrictions, low flow rivers and leakage). Note for domestic customer the water use restriction is hosepipe bans, but is non-essential use bans for non domestic.

- WS3 block - a set of attributes concerned with managing water supplies (taste and odour, and discolouration) and inconvenience associated with restrictions on the use of tap water in the home ('boil water' notices).

Overall the design specified 60 choice cards for each choice experiment block. This was divided into 10 blocks of six choice cards each. Each respondent saw one of the 10 blocks allocated at random, and answered 6 choice cards on each of the three key areas.

3 Household Results

A sample of 100 respondents completed the pilot survey and the following section examines the results with the aim of developing the final survey.

3.1 Sample representativeness

We would like to see a sample representative of Affinity's customer base. There is likely to be some variation driven by the relatively small sample size.

Table 3.1: Respondent gender

	Frequency	Percentage
Female	59	59
Male	41	41
Total	100	100

There appears to be a slight female bias within the sample but this does not hinder the testing process.

Table 3.2: Respondent age

	Frequency	Percentage
Age	Frequency	Percentage
18-29	12	12
30-44	21	21
45-64	40	40
65+	27	27
Total	100	100

Table 3.3: Respondent socio-economic group (SEG)

	Frequency	Percentage
AB	53	53
C1/C2	31	31
D	16	16
E	100	100
Total	53	53

Tables 3.2 and 3.3 show a spread of ages and incomes are represented within the sample.

Table 3.4: Respondent location

	Frequency	Percentage
Central region	91	91
East region	2	2
South East region	7	7
Total	100	100

The views of all regions served by Affinity Water are also represented. The East region has limited representation but is small in comparison to the other areas.

3.2 Sample profile

Table 3.5: Employment status

Occupation	Frequency	Percentage
Employed full-time (30+ hrs)	45	45
Employed part-time (up to 30 hrs)	6	6
Looking after the home / children full-time	4	4
Retired	33	33
Self-employed	7	7
Student	2	2
Unable to work due to sickness or disability	1	1
Other (please specify)	2	2
Total	100	100

Table 3.6: Level of education

	Frequency	Percentage
Professional qualifications (teacher, doctor, dentist, architect, engineer, lawyer, etc.)	20	20
Higher degree (e.g. MA, PhD, PGCE, post graduate certificates and diplomas)	19	19
First degree (e.g. BA, BSc)	25	25
NVQ (Level 1 and 2). Foundation / Intermediate / Advanced GNVQ / HNC / HND	3	3
A levels / AS level / higher school certificate	9	9
Other qualifications (e.g. City and Guilds, RSA/OCR, BTEC/Edexcel)	11	11
O levels / CSEs / GCSEs (any grades)	10	10
No qualifications	1	1
Prefer not to say	2	2
Total	100	100

The tables above show a diverse spread of employment with a high representation amongst the retired. We also see a high level of education within the sample with 64% of respondents having a degree or professional qualifications.

Table 3.7: Total gross household income

	Frequency	Percentage
Up to £539 per month (Up to £6,499)	2	2
£540 - £789 per month (£6,500 - £9,499 per year)	1	1
£790 - £1289 per month (£9,500 - £15,499 per year)	1	1
£1290 - £2079 per month (£15,500 - £24,999 per year)	7	7
£2080 - £3329 per month (£25,000 - £39,999 per year)	11	11
£3330 - £4999 per month (£40,000 - £59,999 per year)	25	25
£5000 - £7499 per month (£60,000 - £89,999 per year)	19	19
£7500 and over per month (£90,000 and over per year)	9	9
Don't know	2	2
Refused	23	23
Total	100	100

We see a greater representation of higher incomes within the sample. For example, there are more respondents with a household income of over £90,000 per year than those with less than £15,500 per year.

Table 3.8: Households with a water meter

	Frequency	Percentage
Yes	60	60
No	38	38
Don't know	2	2
Total	100	100

Over half of respondents surveyed were on a meter which will have implications for attitudes towards elements such as managing water supplies.

Table 3.9: Water only bill per year

	Frequency	Percentage
Less than £8 per month (Less than £100 per year)	8	8
£8 - £13 per month (£100 - £150 per year)	32	32
£13 - £16 per month (£151 - £200 per year)	21	21
£17 - £20 per month (£201 - £250 per year)	13	13
£21 - £24 per month (£251 - £300 per year)	4	4
£25 - £28 per month (£301 - £350 per year)	6	6
£29 - £32 per month (£351 - £400 per year)	6	6
£33 - £37 per month (£401 - £450 per year)	3	3
£38 - £41 per month (£451 - £500 per year)	3	3
£42 - £45 per month (£501 - £550 per year)	1	1
£46 - £50 per month (£551 - £600 per year)	0	0
Over £50 per month (Over £600 per year)	3	3
Total	100	100

The average water bills in the Central, East and South East regions are £174, £171 and £203 per year¹. It is reassuring to see a clustering of respondents paying similar bills whilst also having a spread of bill amounts represented.

Table 3.10: Experience of service failures

	Percentage				
	Within the last year	1-3 years ago	3+ years ago	Never	Don't know
Discoloured Water	10	8	13	60	9
Taste and smell of water	18	11	7	57	7
Drinking water restrictions	77	6	2	7	8
Water hardness	9	6	4	70	11
Low water pressure	21	15	7	46	11
Unexpected interruptions to supply	19	14	12	48	7
Burst Mains Flooding to Properties	3	10	3	72	12
Water Use Restrictions	38	30	3	21	8
Low water levels and flow in rivers	20	27	3	18	32
Leakage	21	25	11	28	15

77% of respondents stated that they had experienced drinking water restrictions such as boil water notices or do not drink notices. Given these restrictions are very rare this is an unexpected result.

It is possible that the attribute descriptions are causing confusion with drinking water restrictions prompting associations with water use restrictions. To address this we recommended to Affinity

¹ http://www.ofwat.gov.uk/mediacentre/pressnotices2008/prs_pn0313bills

Water changing the attribute descriptions to create a clearer division between them. Drinking water restrictions thus becomes “boil water and other notices”; and water use restrictions are renamed “hosepipe bans” for households, “non-essential use bans (hosepipe restrictions)” for businesses.

Besides this result the experience of respondents are not likely to cause issues and overall the sample appears to be reasonable for the pilot study.

3.3 Perceptions of Service Levels

Water hardness stands out as a priority for improvement which we would expect to see reflected within the modelling results. We also observe greater degrees of uncertainty around abstraction in particular, but also around the level of leakage.

Table 3.11: Perception of current water service levels

Service attribute	Percentage		
	Happy with current level of service	Needs improvement	Don't know
The taste and smell of tap water	67	29	4
The number of interruptions to supply due to burst pipes	78	10	12
The frequency of restrictions on water use during periods of drought (e.g. hosepipe bans)	53	42	5
The pressure of tap water	81	16	3
The hardness of tap water (e.g. scaling of kettles and other appliances)	17	82	1
Noise, disruption and inconvenience from water company repairs (e.g. traffic, dust, etc.)	73	10	17
The appearance and colour of tap water	87	10	3
Flooding from burst mains	60	20	20
The provision of information on water efficiency	54	23	23
The level of leakage	41	30	29
Low river water levels due to Affinity Water taking water from the environment	28	19	53
OTHER - SPECIFY	7	7	23

3.4 Awareness of sewerage bill

The pilot study included some questions on the sewerage bills customers pay.

First, customers were asked: *“As an Affinity Water customer a proportion of your bill that you pay to Affinity Water is paid to the provider of your sewerage services. The company providing your sewerage service is responsible for taking your waste water away, treating it and returning it to the environment. Affinity Water is only responsible for providing clean water at you tap. Are you aware of this?”*

This question was only presented to customers in Central and East Regions, where Affinity bill on behalf of Thames Water and Anglian Water. Customers in South East region receive separate sewerage bills from Southern Water

Table 3.12 Household customer awareness of Sewerage bills by Affinity Region

	No	Yes	Total
Central Region	37	51	88
East Region		2	2
South East Region	n/a	n/a	7
Total	37	53	100

This suggests awareness of current billing arrangements for sewerage services are mixed.

Second, we included a follow up question in the Package choices section of the pilot survey to help us understand how sensitive respondent choices may be to information about sewerage bill increases in the 2015-20 period.

Respondents who indicated they were prepared to pay for the maximum improvement package were then asked to re-state their choice after being provided with a randomly selected increase for sewerage bills. The sewerage bill increase was designed to be wide (for households £10, £25, £50, £75). The higher end of this range equates to the likely sewerage bill increase for the Thames Tideway project.

The table below summarises the responses. For both households and business customers a majority of respondents did not change their choice on water supply improvements. As expected respondents were more likely to change to a ‘No’ on water supply improvements when presented with a higher sewerage bill increases.

For the main survey the larger datasets should permit quantification of the sensitivity to sewerage bills in terms of its impact on the WTP for the water supply improvements.

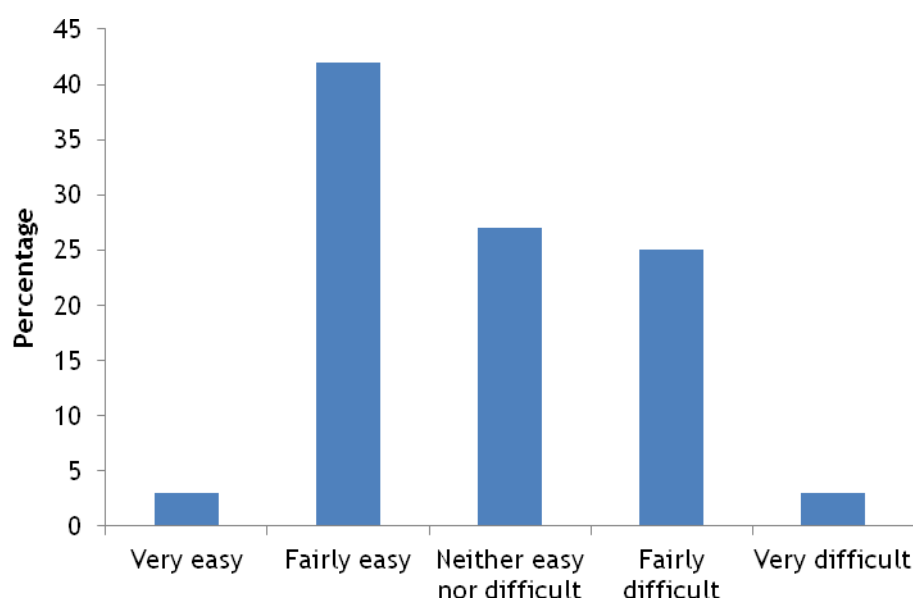
Table 3.13: Household customer responses to sewerage bill increase

	Sewerage Bill Increase £				
	£10	£25	£50	£75	Total
Still pay extra amount for water supply improvements	8	7	8	6	29
Pay different amount for water improvements	1	1	1	0	3
No increase in water bills / no water improvement	2	2	11	5	20
Don't know	2	1	1	1	5
Total	13	11	21	12	57

This shows that some respondents struggled to separate the services when participating in this service. It also shows the importance of the question on sewerage bills (Q.16) in understanding when respondents are accounting for other bill pressures and other impacts on their household budgets when expressing their WTP for improvements.

Reference is already made to potential increases in the sewerage bill ahead of the package question. It may be better therefore to use Q16 when interpreting the final WTP results making necessary adjustments.

3.5 Respondent feedback

Figure 3.14: Difficulty of choice questions

The majority of respondents did not struggle to answer the questions in the choice experiments. This suggests that the survey is working well and should provide robust results with respondents being able to trade-off the service levels presented to them.

This is further supported by responses below to Q.19: Did you find each of the levels of service we described realistic and easy to understand?

Table 3.15: Service levels realistic and easy to understand

	Frequency	Percentage
Yes	88	88
No	12	12
Total	100	100

Respondents who did not find service levels clear did not always state which areas were causing problems. However, two respondents cited “flooding”, “discolouration” and “water restrictions” as not being realistic or easy to understand. The latter has been amended for the next stage of the research.

The table below shows that 90% of respondents felt that they were able to make comparisons between the choices presented. Those who said no to this question most commonly stated the amount of detail was too much to process becoming confusing. This will always be the case for some respondents but the overall balance is positive.

Table 3.16: Able to make choices

	Frequency	Percentage
Yes	90	90
No	10	10
Total	100	100

The table below shows that over half of household respondents found the survey to be too long. This can impact on the reliability of results as respondents become fatigued. 58% of business respondents also stated that the survey was too long.

To address this issue each respondent will only be presented with choice experiments from two out of the three blocks in the main sample. The blocks will be rotated within the main sample to provide equivalent information, with each respondent completing 8 choices per block (this was 6 per block in the Pilot).

Table 3.17: Overall view of survey

	Frequency	Percentage
Interesting	31	31
Too long	51	51
Difficult to understand	15	15
Educational	6	6
Unrealistic/not credible	2	2

3.6 Econometric results

In this section we report on the econometric analysis of the pilot choice experiment data for households. The primary focus of this analysis is to determine whether the pilot experimental designs worked satisfactorily. That is, whether the estimated coefficients have the expected signs. The results of the pilot analysis are then used to update and improve the efficiency of the experimental choice designs. This helps improve the precision of the resulting estimates of willingness to pay from the main fieldwork datasets.

The econometric results are summarised below. We report basic conditional logit models for the pilot testing. For the main fieldwork analysis we will report a wider range of models.

Choice Block WS1 - Drinking Water Quality

In this choice block all coefficients had the correct signs and all attributes except hardness were statistically significant at the 95% level ($p < 0.05$). These are very encouraging results combined with the high model fit (Pseudo R2 = 0.1373). The finding on hardness is marginal and it is possible that statistical significance will be observed in a large sample.

With the exception again of hardness the willingness to pay estimates shown below are statistically significant at the 95% level.

Table 3.18: Household WS1 - Estimated utility coefficients

Attribute	Expected Sign	Estimated Sign	Statistical Significance?	P-value
Discolouration	-	-	✓	0.001
Taste and smell	-	-	✓	0.005
Hardness	-	-		0.144
Drinking water restrictions	-	-	✓	0.001
Water bill	-	-	✓	0.000
ASC Constant	-/+	+	✓	0.000

Pseudo R2 0.1373
Base - 100 respondents, 600 observations

Table 3.19: Household WS1 - Estimated willingness to pay

Attribute	Unit	per unit WTP (£/year)	P-value
Discolouration	1000 properties	1.42	0.011
Taste and smell	1000 properties	1.24	0.016
Hardness	100,000 properties	8.15	0.163
Drinking water restrictions	100 properties	2.60	0.009

Choice Block WS2 - Reliability of Water Supplies

Again, all signs are estimated correctly. Low pressure is the only attribute where statistical significance is not observed (this may reflect the relatively low priority attached to this service risk on average). The model fit for this choice block is very good, again an encouraging sign that the experimental design performed well.

Table 3.20: Household WS2 - Estimated utility coefficients

Attribute	Expected Sign	Estimated Sign	Statistical Significance?	P-value
Low pressure	-	-		0.262
Unexpected SI	-	-	✓	0.000
Burst Mains Flooding to Properties	-	-	✓	0.000
Water bill	-	-	✓	0.000
ASC Constant	-/+	+	✓	0.000

Pseudo R2 0.1491
Base - 100 respondents, 600 observations

Table 3.21: Household WS2 - Estimated willingness to pay

Attribute	Unit	per unit WTP (£/year)	P-value
Low pressure	100 properties	1.34	0.271
Unexpected SI	1000 properties	6.50	0.000
Burst Mains Flooding to Properties	100 properties	9.12	0.000

Choice Block WS3 - Managing Water Supplies

All coefficients are correctly signed and statistically significant.

Table 3.22: Household WS3 - Estimated utility coefficients

Attribute	Expected Sign	Estimated Sign	Statistical Significance?	P-value
Water Use restrictions	-	-	✓	0.000
Low flow rivers	-	-	✓	-0.037
Leakage	-	-	✓	0.000
Water bill	-	-	✓	0.000
ASC Constant	-/+	+	✓	0.000

Pseudo R2 0.0939

Base - 100 respondents, 600 observations

Table 3.23: Household WS3 - Estimated willingness to pay

Attribute	Unit	per unit WTP (£/year)	P-value
Water Use restrictions	1% change	3.35	0.000
Low flow rivers	1% change	1.50	0.051
Leakage	1% change	5.64	0.000

Overall, the household choice models are very encouraging and provide confidence that the main study will result in well determined and plausible estimates of willingness to pay.

3.7 Package analysis

The pilot survey includes a set of package choice questions. These questions are included in the survey to provide validity checks on the willingness to pay values derived from the discrete choice experiments. Specifically they help to test for part-whole bias where the valuation of a package of service change is different (typically lower) than the sum of the independent valuations.

The results of the package analysis are summarised in the tables below.

The estimated weights suggest household placed relatively more weight on the drinking water attributes in their package choices. This finding was marginally significant at the 90% level. The other weights were not statistically significant implying they would have a weight of unity.

The estimate of package willingness to pay for an across the board maximum improvement was around £10-15 per year on average. It is encouraging that the parametric estimate (based on the double bound responses) was statistically significant even with the pilot data.

Table 3.24: Household Package - estimated choice block weights

Choice Block	Estimated Utility Weight	P value
WS1 - Drinking Water Quality	2.03	0.082
WS2 - Reliability	0.76	0.42
WS3 - Managing Supplies	0.81	0.539

Table 3.25: Household Package - Estimated willingness to pay for maximum improvement

Package Estimate	£/hh/year	Statistical Significance
Parametric - Double Bound DCCV	15.71	✓
Non-Parametric - Turnbull	9.32	

Overall, the package exercise is working satisfactorily. We would anticipate based on these findings that scaled valuations will be lower than unscaled valuations due to the part-whole bias issue.

4 Business Results

4.1 Sample representativeness

88 businesses were surveyed as part of this pilot drawn from a range of industries as shown below.

Table 4.1: Respondent organisation

SIC	Frequency	Percentage
Construction	3	3
Manufacturing/Production	3	3
Other activities	49	56
Professional, scientific, technical and business administration/support	24	27
Public organisations, education, health and social work activities	4	5
Wholesale and retail trade	5	6
Total	88	100

The two tables below show small, medium and large businesses represented within the sample, both in terms of number of employees and the size of their water bills. There is a greater emphasis is on smaller businesses within the sample.

Table 4.2: Number of employees

	Frequency	Percentage
0 - 4	49	56
5 - 9	11	13
10 - 19	7	8
20 - 49	8	9
50 - 99	1	1
100-249	0	0
250 - 499	4	5
500 - 999	2	2
1,000 +	5	6
Don't know/not stated	1	1
Total	88	100

Table 4.3: Bill amount water and sewerage

	Frequency	Percentage
Less than £1,000 per year	59	67
£1,000 to £4,999 per year	9	10
£5,000 to £9,999 per year	2	2
£10,000 to £24,999 per year	2	2
£25,000 to £49,999 per year	4	5
£50,000 to £99,999 per year	2	2
£250,000 to £500,000	0	0
More than £500,000	0	0
Don't know	10	11
Total	88	100

In a repeat of the household sample we observe a very high number of respondents (63%) who have experienced drinking water restrictions. It is possible that the attribute descriptions are causing confusion with drinking water restrictions prompting associations with water use restrictions.

To address this we recommend changing the attribute descriptions to create a clearer division between them. Drinking water restrictions could become “boil water and other notices” and water use restrictions could be renamed “hosepipe bans” for households, “non-essential use bans” for businesses.

Table 4.4: Experience of service failures

	Percentage				
	Within the last year	1-3 years ago	3+ years ago	Never	Don't know
Discoloured Water	8	16	10	57	9
Taste and smell of water	20	10	6	56	8
Drinking water restrictions	63	6	6	19	7
Water hardness	5	10	8	70	7
Low water pressure	26	15	2	48	9
Unexpected interruptions to supply	13	19	15	42	11
Burst Mains Flooding to Properties	2	11	9	67	10
Water Use Restrictions	22	33	5	27	14
Low water levels and flow in rivers	13	20	2	35	30
Leakage	17	16	8	35	24

Overall the business sample appears reasonable for the pilot study.

4.2 Perceptions of Service Levels

As with household customers we see hard water as being an area where respondents would like to see improvements and the greatest uncertainty lies around abstraction. Leakage is another area where respondents may value improvements.

Table 4.5: Perception of current water service levels

Service attribute	Percentage		
	Happy with current level of service	Needs improvement	Don't know
The taste and smell of tap water	72	26	2
The number of interruptions to supply due to burst pipes	76	18	6
The frequency of restrictions on water use during periods of drought (e.g. hosepipe bans on homes and businesses)	55	40	6
The pressure of tap water	66	31	3
The hardness of tap water (e.g. scaling of kettles and other appliances)	25	72	3
Noise, disruption and inconvenience from water company repairs (e.g. traffic, dust, etc.)	69	23	8
The appearance and colour of tap water	86	11	2
Flooding from burst mains	58	30	13
The provision of information on water efficiency	50	32	18
The level of leakage	40	41	19
Low river water levels due to Affinity Water taking water from the environment	35	23	42
OTHER - SPECIFY	8	7	15

4.3 Awareness of sewerage bill

The pilot study included some questions on the sewerage bills customers pay.

First, customers were asked: *“As an Affinity Water customer a proportion of your bill that you pay to Affinity Water is paid to the provider of your sewerage services. The company providing your sewerage service is responsible for taking your waste water away, treating it and returning it to the environment. Affinity Water is only responsible for providing clean water at you tap. Are you aware of this?”*

This question was only presented to customers in Central and East Regions, where Affinity bill on behalf of Thames Water and Anglian Water. Customers in South East region receive separate sewerage bills from Southern Water

Table 4.6 Business customer awareness of Sewerage bills by Affinity Region

	No	Yes	Total
Central Region	39	42	81
East Region	1	0	1
South East Region	n/a	n/a	6
Total	40	42	88

This suggests awareness of current billing arrangements for sewerage services are mixed.

Second, we included a follow up question in the Package choices section of the pilot survey to help us understand how sensitive respondent choices may be to information about sewerage bill increases in the 2015-20 period.

Respondents who indicated they were prepared to pay for the maximum improvement package were then asked to re-state their choice after being provided with a randomly selected increase for sewerage bills. The sewerage bill increase was designed to be wide (for households £10, £25, £50, £75). The higher end of this range equates to the likely sewerage bill increase for the Thames Tideway project.

The table below summarises the responses. For both households and business customers a majority of respondents did not change their choice on water supply improvements. As expected respondents were more likely to change to a No on water supply improvements when presented with a higher sewerage bill increases.

For the main survey the larger datasets should permit quantification of the sensitivity to sewerage bills in terms of its impact on the WTP for the water supply improvements.

Table 4.7 Business customer responses to sewerage bill increase

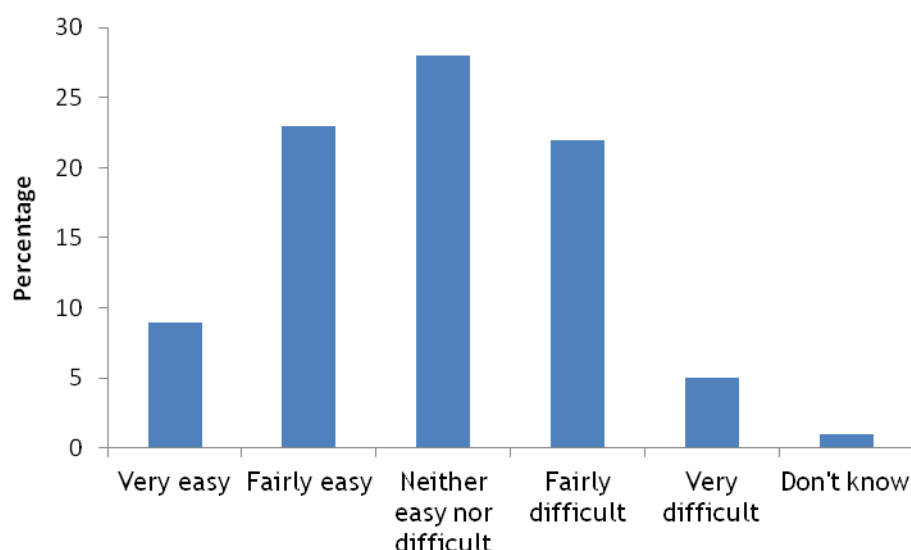
	Sewerage Bill Increase £					
	3%	5%	10%	15%	20%	Total
Still pay extra amount for water supply improvements	2	5	7	4	3	21
Pay different amount for water improvements	0	0	1	0	0	1
No increase in water bills / no water improvement	1	1	5	4	3	14
Don't know	1	0	0	1	0	2
Total	4	6	13	9	6	38

This shows that some respondents struggled to separate the services when participating in this service. It also shows the importance of the sewerage question (Q.16) in understanding when respondents are accounting for other bill pressures and impacts on their business budgets when expressing their WTP for improvements.

Reference is already made to potential increases in the sewerage bill ahead of the package question. It may be better therefore to use Q16 when interpreting the final WTP results making necessary adjustments.

4.4 Respondent feedback

Figure 4.8: Difficulty of choice questions



Similar to the household sample, the majority of respondents did not struggle to answer the questions in the choice experiments. This suggests that the survey is working well and should provide robust results with respondents being able to trade-off the service levels presented to them.

This is again further supported by responses below to Q.19: Did you find each of the levels of service we described realistic and easy to understand?

Table 4.9: Service levels realistic and easy to understand

	Frequency	Percentage
Yes	78	89
No	10	11
Total	100	100

Respondents who did not find service levels clear did not always state which areas were causing problems. Mainly protest responses were given in response to Q.20: Which levels did you find were not realistic or easy to understand?, rather than constructive feedback needed to refine the survey.

The table below shows that 85% of respondents felt that they were able to make comparisons between the choices presented. Those who said no to this question again commonly stated the amount of detail was too much to process becoming confusing. This will always be the case for some respondents but the overall balance is positive.

Table 4.10: Able to make choices

	Frequency	Percentage
Yes	75	85
No	13	15
Total	88	100

4.5 Econometric results

The business econometric results are summarised below. We report basic conditional logit models for the pilot testing. For the main fieldwork analysis we will report a wider range of models.

Choice Block WS1 - Drinking Water Quality

In this choice block all coefficients had the correct signs and all attributes except discolouration and hardness were statistically significant at the 95% level ($p < 0.05$). These are encouraging results combined with the high model fit (Pseudo $R^2 = 0.1314$). The non-significance of the hardness attribute is stronger than for households.

Table 4.11: Business WS1 - Estimated utility coefficients

Attribute	Expected Sign	Estimated Sign	Statistical Significance?	P-value
Discolouration	-	-		0.194
Taste and smell	-	-	✓	0.022
Hardness	-	-		0.830
Drinking water restrictions	-	-	✓	0.007
Water bill	-	-	✓	0.000
ASC Constant	-/+	+	✓	0.000

Pseudo R^2 0.1314

Base - 88 respondents, 528 observations

Table 4.12: Business WS1 - Estimated willingness to pay

Attribute	Unit	per unit WTP (%/year)	P-value
Discolouration	1000 properties	0.146	0.198
Taste and smell	1000 properties	0.256	0.021
Hardness	100,000 properties	0.301	0.21
Drinking water restrictions	100 properties	0.55	0.006

Choice Block WS2 - Reliability of Water Supplies

All signs are estimated correctly with the exception of low pressure. Low pressure is also the only attribute where statistical significance is not observed. Business respondents were mostly likely to ignore low pressure when making their choices and more so than households. So this finding if repeated in the main fieldwork is likely to reflect a relatively low priority being attached to this service risk on average. The model fit for this choice block is very good, again an encouraging sign that the experimental design performed well.

Table 4.13: Business WS2 - Estimated utility coefficients

Attribute	Expected Sign	Estimated Sign	Statistical Significance?	P-value
Low pressure	-	+		0.381
Unexpected SI	-	-	✓	0.005
Burst Mains Flooding to Properties	-	-	✓	0.001
Water bill	-	-	✓	0.000
ASC Constant	-/+	+	✓	0.000

Pseudo R2 0.1475

Base - 88 respondents, 528 observations

Table 4.14: Business WS2 - Estimated willingness to pay

Attribute	Unit	per unit WTP (£/year)	P-value
Low pressure	100 properties	-0.373	0.379
Unexpected SI	1000 properties	1.10	0.006
Burst Mains Flooding to Properties	100 properties	1.69	0.004

Choice Block WS3 - Managing Water Supplies

All coefficients are correctly signed in the third choice block. The low flow coefficient (and willingness to pay) was not statistically significant. Nearly half of business respondents said they ignored low flows when making their choices, whereas the same figure was 23% and 20% respectively for restrictions and leakage respectively. So this finding may genuinely reflect a lower business customer priority

Table 4.15: Business WS3 - Estimated utility coefficients

Attribute	Expected Sign	Estimated Sign	Statistical Significance?	P-value
Water Use restrictions	-	-	✓	0.000
Low flow rivers	-	-		0.383
Leakage	-	-	✓	0.000
Water bill	-	-	✓	0.000
ASC Constant	-/+	+	✓	0.000

Pseudo R2 0.1238

Base - 88 respondents, 524 observations

Table 4.16: Business WS3 - Estimated willingness to pay

Attribute	Unit	per unit WTP (£/year)	P-value
Water Use restrictions	1% change	0.768	0.000
Low flow rivers	1% change	0.217	0.384
Leakage	1% change	1.656	0.000

4.6 Package analysis

The results of the business package analysis are summarised in the tables below.

The estimated weights suggest businesses like households placed relatively more weight on the drinking water attributes in their package choices. However, all the coefficients were non-significant implying that all choice blocks would attract the base weight of unity (i.e. equal weight).

The estimate of package willingness to pay for an across the board maximum improvement was around 3.4 to 6.7% per year on average. The parametric estimate was not statistically significant even in the pilot data. The larger main study sample size combined with the reduction in survey length should result in more precise business package values.

Table 4.17: Business Package - estimated choice block weights

Choice Block	Estimated Utility Weight	P value
WS1 - Drinking Water Quality	1.1	0.66
WS2 - Reliability	0.7	0.16
WS3 - Managing Supplies	0.8	0.46

Table 4.18: Business Package - Estimated willingness to pay for maximum improvement

Package Estimate	%/hh/year	Statistical Significance
Parametric - Double Bound DCCV	3.36	X
Non-Parametric - Turnbull	6.68	

5 Next Steps and Conclusions

5.1 Development of Main Study

The Main questionnaire fieldwork is due to commence on 1 July. Any peer review or stakeholder comments should be provided by 24 June so they are incorporated fully into the final survey along with the findings below.

5.2 Conclusions

The implementation of the PR14 Willingness to Pay Study will involve a comprehensive design and testing phase of work for development of the stated preference survey, along with large scale sampling of domestic and non-domestic customers in the main survey implementation.

The pilot results from the household and business samples were broadly in line with expectations and on the whole encouraging. They are now being used to update the final design of the Main questionnaire.

Both feedback from the survey respondents and the recorded interview duration suggested that the survey in its pilot form is a little too long. This can start to impact on the quality of responses if fatigue becomes an issue.

To address this we recommend that in the Main survey respondents should complete two out of the three choice blocks. Rotation of the blocks through the sample will still provide the information required.

We have also improved the routing to provide customer specific sewerage provider information. This will reduce the amount of reading required by the respondent helping to shorten the survey without compromising the information being provided or collected.

The final change of note relates to the wording of two attributes. We observed a very high number of respondents stating they had experienced drinking water restrictions. It is possible that the attribute descriptions are causing confusion, with drinking water restrictions prompting associations with water use restrictions.

To address this we have changed the attribute descriptions to create a clearer division between them. Drinking water restrictions are renamed “boil water and other notices” and water use restrictions are renamed “hosepipe bans” for households, “non-essential use bans (i.e. hosepipe restrictions)” for businesses.

Document Control

Version History

Version	Date	Comments
1.0	20/06/13	Issued to Affinity Water

Distribution

Version	Owner	Proof read by	Issued to
1.0	Lisa Gahan	Scott Reid Martin Baker	Mike Robertson Chris Offer Elizabeth Allen

Affinity Water

Acceptability Testing

- and its role in putting together business plans

May 2013

Agenda

- What is expected from companies?
- Why is it needed?
- The options for acceptability testing
- Key steps and results

What is expected from companies?

- “Involving customers in price setting” - Ofwat’s customer engagement policy statement

Customer engagement will be an important factor in determining whether we will accept the companies’ business plans.
Customer acceptability is a key factor in our decisions.

Customers’ views will feed into the price-setting process in one of three ways.
*- Through direct local engagement between each company and its customers to understand customers’ views, **to inform development and test acceptability of the company’s plan***

- And more recently, the January 2013 Methodology document...

*Companies may commit up to a level of performance that represents the economic level of service (that is, where marginal benefits equal marginal costs), **within an acceptable and affordable overall plan***

What is expected from companies?

- CCWater paper on what it expects states testing needs to be:
 - “Valid i.e. a representative and accurate reflection of bill payers’ views;
 - Broadly comparable so that companies feel their research can be compared fairly with that of other companies.”

Representative sample ... include vulnerable or hard to reach

Include uniformed customers

Question preferred bill profile

Sample big enough to draw clear conclusions

Include bill impacts not covered by WTP

Question why plan is acceptable or not

Reference sewerage bills and inflation

Why don't we just use WTP?

- Customer Acceptability complements WTP and CBA
 - Not all areas are covered by WTP
 - WTP does not capture the limit on what customers can afford and therefore what is acceptable bill change
 - Mandatory investments (e.g. quality) and other cost pressures on bills can impact on what other investments are acceptable
- *Customer Acceptability is not just about testing if the plan is acceptable*
- *It should indicate the business plan that is likely to be the most acceptable to customers*

What are the options for testing the plan?

1: TEST OF THE PREFERRED PLAN

Akin to Ofwat Approach in PR09

Proposed business plan tested against current position (baseline)

Gives % of respondents that consider proposed plan to be acceptable

2: TEST OF MULTIPLE PLANS

Extension to testing dual plans

Test a few proposed business plans against current position (baseline)

Gives % of respondents that prefer each one

Gives plan that is most acceptable to customers

Includes qualitative questions to understand views on current level of service and rationale for the choices made

Should companies test one or more plans?

- Some companies are going straight for test of preferred plan
 - Need strong evidence for that
 - Difficult to justify if there is significant non discretionary spend
 - If part of a rolling iteration of plans, this is more robust
- More robust (and popular) to consider multiple plans
 - Means companies do not need one proposed plan
 - Deals with uncertainty as to level to propose
- Typically companies adopt two phases of research
 - Multiple to get general views, then the final test of preferred plan

What is involved?

- Agree the plan(s) to be tested
 - Service attributes and definitions, and groupings of attributes (linked to outcomes?)
 - Legal requirements and other areas not covered by WTP
- Plan has clear change in service and bill impact (and bill profile)
- Design of questionnaire and survey
- Pilot and Main Fieldwork and Analysis
- Applied to robust sample of customers
 - Representative of all customer types (age, SEG, vulnerable, etc).
 - Statistically significant (i.e. Large enough sample)

What are the results?

- We test with customers....
 - % respondents think each plan is acceptable and very acceptable
 - % respondents think each plan is unacceptable and completely unacceptable
 - Why the plan is acceptable or not
 - Which is the most preferred plan from the options presented
- Can understand what changes in the plan customers want and which they do not
- Understand customer views on current levels of service, value for money, key areas for improvement
- Understand changes to the most preferred plan that would make it 'more acceptable'

Which approach to apply?

- A useful approach is to use both types of research
 - Test multiple plans first
 - Then follow with the test of the preferred plan
- Both options can be delivered through a range of survey modes (online, face to face, telephone recruitment)
 - Some CAPI essential to ensure hard to reach customers are captured
- This is the approach we have recommended to Affinity Water
- The project timeline is currently being discussed

Affinity Water

Acceptability Testing

- and its role in putting together business plans

May 2013

Challenge Record

Number/reference: 0004	Date: 5 August update 21 August
Raised by: CCG	Subject area: Metering
Due by date: 11 September 2013	

The challenge: Metering

Challenge:

Affinity Water has a working hypothesis that customers support universal metering. This view is an outcome from the qualitative work in focus groups, environmental forums and deliberative workshops. It is not yet substantiated by robust quantitative research.

Expectations:

Affinity Water needs to demonstrate with robust quantitative research the extent to which customers support universal metering. The research should identify any implied qualifications, for example, whether customers believe metering is acceptable only if it is installed for free and/or will no bill impact. The research should also identify which customers groups do not support metering. Affinity Water should explain how it proposes to deal with those customers.

Affinity Water should also explain how it is preparing well in advance for universal metering and how it will help those customers with affordability issues. Affinity Water should also explain why the last water zone (2 – Colne) will be metered in the next AMP period ie after 2020.

The company demonstrate that it has taken account of increasing bills for customers / sub sets of customers that universal metering may bring.

What are the implications for the water demand-supply balance if universal metering is not introduced in 2015-20?

Specific points to be addressed:

There is some evidence from the qualitative engagement that customers support metering only if they do not have to pay for it. Is this correct? What are the implications for Affinity water?

Further, in the qualitative engagement, those unmetered customers who feel they will have to pay more appear not to support the introduction of metering. Is this correct? How will Affinity Water work with these customers to address their concerns?

Do customers in the East where metering is at 73% support and the demand-supply balance is healthy support universal metering.

RESPONSE from Affinity Water

1. Introduction and context

We understand that the context for this CCG challenge relates to our view that customers support universal metering. We have come to this view after considering qualitative work we carried out with focus groups, environmental forums and deliberative workshops. We are clear about the importance of the CCG's role in challenging us to show how this view has been substantiated by robust quantitative research.

It is important to clarify at the outset that we see metering as a key component within a range of measures to tackle underlying customer demand. The range of measures we intend to adopt are set out in our draft Water Resources Management Plan (dWRMP) and include activities to reduce leakage and develop our capacity to improve our ability to move water both into and within our areas of supply. Most importantly we are proposing a large scale programme of water efficiency activities alongside the roll out of metering that will be delivered to customers as a coherent single programme to target demand reduction.

In this challenge response we will show clearly how we have consulted with customers to address expectations from the CCG, as set out below:

- a) demonstrate with robust quantitative research the extent to which customers support universal metering;
- b) identify implied qualifications to universal metering support, for example whether customers only find metering acceptable if it is installed for free and/or will not impact on the level of customers bills;
- c) identify customer groups who do not support metering and how we will deal with this;
- d) how we are preparing for universal metering prior to the start of AMP6 (2015-2020);
- e) how we intend to help those customers who may have affordability issues;
- f) how we decided our delivery programme and the reason why two Central water resource zones will be metered in AMP7 (2020 – 2025);
- g) how we have taken account of increasing bills for some customers, that may be brought about by universal metering; and
- h) explain the implications for our water supply / demand balance if universal metering is not introduced in AMP6 (2015-2020)

2. Background

One of our key customer expectations is 'Making sure our customers have enough water, while leaving more water in the environment'. In order achieve this outcome we will improve the efficiency with which we use our resources and support our customers to reduce their consumption to leave more water in the local environment.

This will enable us to provide a sustainable water service and ensure that our customers have enough water both now and in the future to overcome the challenges we face.

The challenges we face

- We supply water to 3.5 million people within the southeast of England, an area of supply which is classified by the Environment Agency as subject to serious water stress
- Our key challenge is ensuring that our customers have enough water, now and in the future, whilst leaving more water in the environment to protect our chalk streams and local habitats
- The population of the communities we serve is forecast to grow by 15 per cent over the next 25 years
- Less predictable weather patterns, associated with climate change, have the potential to reduce the water resources available to us and increase the risk of droughts
- Our customers have one of the highest rates of water use in England and Wales
- Preserving our water sources for future generations

We need to use our water resources more efficiently and persuade our customers to recognise water as a precious and finite resource. This will allow us to secure our supply for future generations of customers and leave more water in the environment.

A key component in persuading customers to use water more efficiently will be to encourage our customers to pay for the water they use through metered charges. We have found that this reduces the level of individual consumption by at least 10 per cent, when we implemented universal metering within our Dour community (Southeast Region). In our WRMP we are proposing a saving of 13.6 per cent.

Universal metering programme summary

Our metering programme is focussed on delivery over seven years (2015-2022). This would mean overall metering penetration in our Central Region of around 70 per cent by 2020 and 90 per cent by 2022. During 2015 to 2020, our universal metering will be targeted at the four Central Region communities where we have greatest need from an imbalance between customer demand and water resource supply. To raise the level of metering to 90 per cent within these four communities we will install around 280,000 meters during the five years at a cost of £52.2 million to achieve a reduction in demand of 18.4Ml/d by 2020

3. Forming our initial views

Our initial view that customers support universal metering was based on qualitative work we carried out with focus groups, environmental forums and deliberative workshops but also quantitative work from establishing our online panel. The research activities we carried out formed Phase 1 'Listening and Learning' of our

engagement programme up to March 2013.

Phase 1 activities included

- Establishing customer and stakeholder baseline view
 - Corporate stakeholder mapping
 - Base customer focus groups
- Formal consultation
 - draft Strategic Direction Statement
 - pre-consultation on our draft Water Resources Management Plan
- On-line panel – establishment of panel
- On-going and regular customer engagement

The phase 1 engagement focussed on identifying issues, attitudes and opinions from our customers, specifically around their expectations of their water service provider. Research was conducted using independently run-workshops, face-to-face focus groups and online panels, members of which reflect the socio-economic groups in the communities we serve. A full report of the Phase 1 engagement activity has been shared with the CCG members¹.

Our customers told us that they judge their water service on the cleanliness of water, the consistency of supply, the price, the level of customer service and how we maintain the water infrastructure. Customers were broadly in agreement with the customer expectations we consulted upon.

In terms of water efficiency and metering, the focus group feedback showed that customers recognised their individual responsibility to save water and that there was support for metering and improving domestic water efficiency as well as tackling leakage. Much stronger support for metering, variable pricing and tariffs, education about water use and further leakage reduction came from the environmental forum.

We used our on-line panel 3 times to test views on aspects of water resource planning – including metering. Customers agreed that

- That having a meter installed would affect the amount of water they use (67%); (reference Panel Survey Findings PSF page 7)
- They consider meters as the fairest way to pay for water (75%); Reference PSF page 22
- A charging system that rewards customers according to their consumption (the concept of a volumetric stepped tariff) is supported (67%); Reference PSF page 27 and
- While opinion was divided on the likelihood of a meter saving them money, nonetheless 77% believe a metering programme should be universal rather than limited to areas of severe water scarcity only. Reference PSF page 26

4. CCG expectations

¹ Report on Engagement Activity – Phase one ‘Listening and Learning’, Activities undertaken during 2012, Affinity Water, 08 May 2013.

To address the specific expectations of the CCG we have grouped the issues under three headings; Customer support, Affordability and bills and Delivery as set out below.

Customer support

- a) demonstrate with robust quantitative research the extent to which customers support universal metering*

On completion of our Phase 1 engagement activities we identified a range of issues to be taken forward into Phase 2 of our engagement, from June to September 2013. The focus of our research was designed to 'test and value' the issues we had identified. In terms of metering and water efficiency we carried out activities to get robust quantitative evidence about customer views.

Our engagement took a number of forms including statutory and non-statutory consultations, quantitative research and qualitative research.

Phase 2 activities included

- Ongoing and enhanced communication
- Formal consultation
 - Draft Water Resources Management Plan Consultation
 - Draft Business Plan Consultation
- Deliberative forums
- Quantitative research
 - Stated preference research (known as willingness to pay)
 - Acceptability testing
 - Online panels

Research was conducted using independently run-workshops and customer surveys and choice experiments, face-to-face focus groups and online panels, members of which reflect the socio-economic groups in the communities we serve. A full report of the Phase 2 engagement activity has been shared with the CCG members².

The feedback from our quantitative research, carried out gave robust quantitative evidence about customer views, showed that customers prioritised demand management options over supply side options and favoured fixing more leaks and encouraging more customer water efficiency and metering³. Our acceptability testing, based upon the Proposed Plan we consulted upon in July 2013, showed customers had very strong support for a plan that increases bill by around £3.70 or less. This Proposed Plan included the proposal to reduce demand for water by installing 80,000 meters a year on a universal basis, community by community, so that customers only pay for the water they use. Our second round of acceptability testing gave us 77% support for increased metering, compared to 65% during the first round of testing

- b) identify implied qualifications to universal metering support, for example whether customers only find metering acceptable if it is installed for free and/or will not impact on the level of customers bills;*

Our research has not focussed on implied qualifications to universal metering

² Report on Engagement Activity – Phase 2 'Testing and Valuing', Activities undertaken March – September 2013, Affinity Water, October 2013.

³ Stated Preference Study: Water Resources WTP Study.

support. We know that proportion of unmeasured customers will benefit from moving to a measured charge and are likely to make the transition when they understand the potential for lower bills and that they will have a meter installed at no charge. We have instead focused on understanding those customers who do not support metering and this is considered further below.

c) identify customer groups who do not support metering and how we will deal with this;

Our research has identified a small proportion of customers who do not support metering. This group is largely made up of customers who are presently not on a measured charge. In order to address this we have carried out specific targeted research in Phase 3 of our engagement programme. Phase 3 is focussed on revisiting and assuring the engagement work and findings from the earlier phases. We have also focussed on carrying out specific targeted research where we felt we needed further evidence of customer views.

We carried out 2 independently hosted deliberative forums for customers in Harlow and Rickmansworth in October 2013. The Harlow event was attended by 36 participants and the Rickmansworth one by 35. Participants were selected to broadly reflect the population of the locations the events were held in. The sampling criteria used to inform the recruitment was: age; gender; ethnicity; income; and disability. Also all were Affinity water customers and responsible for paying the bill. The sample was weighted by a ratio of approx. 4:1 towards those who did not have a meter. Those who did have a meter were asked to consider that they didn't have a meter for the purposes of the discussion.

The purpose of these events was to discuss our community metering plans, looking at the 3 stages of the customer journey: pre-installation of a meter, installation and post-installation. Most participants were supportive of the principle of metering. They felt it was fair to pay for the water you use. See report Community Metering Consultation, deliberative forums, October 2013.

The key findings were:

- Customers became more supportive of metering, once they had the opportunity to discuss what was involved
- More customers would be prepared to have a meter fitted as a result of finding out more about metering
- Bill impact is the key issue to address for low and high users of water.
- There is an issue of trust about the metering programme some participants wanted reassurance that community metering was about reducing water usage
- Some participants found it difficult to talk about phases as they felt there were so many outstanding questions. They had a desire for much more information about the whole process

The research indicates three main areas of concern for customers; (i) where information will be needed to be provided for them around why we proposing metering, (ii) how will the metering journey look and (iii) how will it affect them.

The engagement work has reinforced the importance of the work we need to

undertake with customers to ensure we have a clear communication programme around the metering journey and the customer experience in advance of the installation programme. Our business plan will set out our plans to achieve this.

Affordability and bills

e) how we intend to help those customers who may have affordability issues;

Affordability is an issue for many households, including those that may already be on a metered charge. We are responding to this challenge by developing our social tariff proposals and intend to introduce this for 2014/15.

During the two-year post installation transition period (see below for more detail) we will target and support those customers most vulnerable to the change. CCW in their report 'The Customer Impact of Universal Metering Programmes' concluded that those customers who are families in low value properties are most likely to face bill increases. As well as receiving support for reducing consumption and spreading payments over affordable periods for the customer, we will have two alternative tariffs that customers may be eligible to receive.

WaterSure Vulnerable Tariff

WaterSure supports those customers who receive some form of welfare benefit, have 3 or more children on child benefit or may have a medical condition that may require water to be frequently used. The scheme has been in operation since 2000 and will continue and customers will be encouraged to apply throughout the metering programme. The benefits of the tariff are that water charges are capped at the average metered charge to ensure that those who need more water are not adversely impacted. In some cases the social tariff eligible may be of more value to a customer.

Social Tariff

We have gained customer support for a social tariff. Subject to Ofwat's approval (and potentially on a regional trial basis), we are planning to introduce for 2014/15 a tariff to support those customers who have a household income of less than £15,860 and/or have welfare support as a result. Eligible customers will receive a fixed flat rate bill currently £95.80 and reduction of approximately 40% of an average water bill. In addition they will be metered to ensure that excessive water is not used and we will also provide a water audit. The two-year transition period will enable us to identify customers who may eligible and encourage them to apply.

The alternative option available with the social tariff was to adopt a more specific and individual approach which would support fewer customers with a larger discount upon the bill. The proposal of the social tariff was finalised after discussion with CCW. Our proposal is to support a larger number of customers who are striving to pay, some who struggle but pay the existing bill and those who feel unable to pay the current bill at all. It is expected that the social tariff will support c 30,000 customers who are a mixture of current payers and non-payers. This will specifically help those customers who can currently afford the existing bill but may struggle to pay the new-metered bill if it is higher, subject to eligibility.

We are also considering the potential for a volumetric tariff that has no standing charge. This tariff would ensure that more of the customer bill reflects consumption.

- g) how we have taken account of increasing bills for some customers, that may be brought about by universal metering; and*

We are developing proposals to offer customers choice about when they switch to a measured tariff following meter installation. Our aim is to minimise the number of customers that are compulsorily switched to a measured charge. A transitional period will allow us to communicate and inform customers about water efficiency and the potential benefits and implications of moving onto a measured charge. We will also take into account the lessons of compulsory metering from others who are delivering it in this AMP (South East & Southern) and from our own programme in the Southeast region.

Delivery

- d) how we are preparing for universal metering prior to the start of AMP6 (2015-2020);*

Our preparations for universal metering are well advanced and we have focussed on defining and managing the 'The Customer Experience'. As discussed earlier, in early October we have held two deliberative forums in Rickmansworth and Harlow that have given us a clear view of customers' main concerns and how we can best address these; in particular:

- Customers do wish to be kept informed during the 'pre-installation phase' and we are planning to launch a communication plan between three to six months prior to installing a meter. We will utilise a third party to support our communication to ensure that customers have an independent view of the benefits of the programme throughout the journey. This will also assist the water efficiency work stream;
- Customers would like the ability to read the meter themselves and the utilisation of the web and/or an app to see 'real time' meter reads will assist.
- Customers liked the two-year transition period to adoption of the measured bill.

Proposed Customer Journey

We are planning a customer journey that gives customers 24 months to 'Opt' on to a measured charge before being compulsorily switched to a metered bill at the end of that period. In preparing for this customer journey we have been looking to the experience others have gained from delivering similar programmes. Universal metering programmes have been in place in the south east of England for a number of years. Folkestone and Dover completed compulsory metering in 2009 and more recently Southern Water and South East Water have undertaken metering programmes in AMP5.

The impacts upon the customer have been evidenced within Southern Water and South East Water through the service incentive mechanism, SIM. We have held meetings with both companies to understand what the customer concerns were, what went well and the negative impacts of their metering programme that drove complaints, a perceived reduction in service (SIM) and increased customer contact. We have also been taking into account the CCWater publication 'The Customer Impact of Universal Metering Programmes' in South East England. The findings of

the report together with earlier discussions with Southern Water and South East Water have helped shape our proposals. The key areas of our programme are outlined below.

Communication

Our own experience in Folkestone and Dover has made it clear that early, consistent and regular communications can help customers understand and be supportive of metering. Southern Water and South East Water both confirmed the value of communicating to key stakeholders in the community, individuals by leaflet/letter and complementary channels such as Facebook and websites. CCW's report emphasised that many customers did not appreciate that their bill could increase.

We will make the rationale for metering clear, the timing of the metering programme, providing greater information to customers closer to the point of installation. Explaining that metering may have a positive impact on some customers' bills, however other customers will pay higher bills. This is seen as being fair, as customers will pay for what they use, but we will support customers through a transition to a new tariff to ensure that customers have every opportunity to reduce their potential bill and budget for any increase.

We propose to adopt a two year transition from installation of a meter to address the specific concerns of customers over billing and how customers can influence the amount of water they use and manage their bill.

Transitional Period - Water Efficiency

We reviewed the transitional approach of both Southern Water and South East Water. We considered a transitional tariff but concluded an approach that encouraged customers to accept a meter would have a positive customer impact and build trust by engaging them in being involved in the solution of using less water.

Post meter installation- transition to a measured bill.

We have proposed a two-year transition from installation through to new-metered bill. Following installation of the meter the customer remains on their existing tariff unless they opt to switch to a measured tariff immediately or at any point over the two years. The meter will be read monthly for the first six months and the information made available to the customer together with advice regarding how to save water. At the end of the first 6 months a comparison letter will be sent to customers that have not switched showing the value of their existing bill compared to that of a metered bill.

The comparison letter will enable customers to understand whether they will gain by having a metered bill or that they will lose should they not alter their water usage sufficiently. At this point and at any point after installation, the customer can elect to be billed based upon the consumption read and the metered tariff, cancelling the existing bill and replacing it with the new-metered bill.

Customers who do not elect to have a metered bill will continue to be billed on the existing tariff and the process repeats every 6 months to show customers the progress they have made with their consumption and the comparison to their existing tariff.

We will continue to support those whose consumption results in a higher measured bill than their existing bill and intend to provide information to customers regarding

further support to those most vulnerable. This is likely to be families in properties with lower rateable value unmeasured bills. Whilst all customers will receive advice on how to use water wisely those customers whose potential metered bill is higher than their existing bill will receive additional support to reduce consumption such as free water saving devices and the offer of a water audit.

The two-year transition programme will support the customer to take control of their water consumption and manage their future bill preventing any bill shock and enabling them to become accustomed to the change. In addition it will reduce concerns over supply pipe leakage, metering supply errors etc. as these can be reconciled prior to change of tariff.

By placing all customers within the transitional period it allows customers to accept the meter and elect for the change, providing choice but also for those whose bill will increase allowing time to influence the bill increase by lowering consumption and budget for any future increase. It provides a regular touch point for us to target customers who use water more effectively and genuinely work with them to manage consumption and bill value.

Any customers who move into a property with a meter that has yet to be moved to the new tariff will be automatically billed on a metered tariff. At the end of the two-year period any customers who have yet to elect for a meter will be automatically transferred to the new tariff.

f) how we decided our delivery programme and the reason why two central water resource zones will be metered in AMP7 (2020 – 2025);

We have altered the delivery programme for universal metering. To ensure bill acceptability and ease affordability we are now proposing that the 90% target will be achieved in AMP7 with completion in 2021/22. The Service Delivery Map areas to be universally metered will be Water Supply Zone (WSZ) 1 – Stort; WSZ 2 - Misbourne; WSZ 2 – Colne and WSZ 3 – Lee.

WSZ 6 - Wey and WSZ 4 – Pinn will be completed in the next periodic review. These areas have the highest populations of customers who are likely to be impacted by the universal metering programme.

h) explain the implications for our water demand-supply balance if universal metering is not introduced in AMP6 (2015-2020)

Should a universal metering and water efficiency programme not be introduced, then we would be operating with a higher level of risk making it more difficult to ensure we leave enough water in the environment and meet our customers' expectations around having enough water. This risk will also arise if we find that the expected demand reductions from metering are not realised. This may require further investments that shareholders will initially finance.

Longer term, beyond AMP6, we may need to invest in more expensive supply side solutions and strategic options as set out in the dWRMP for AMP7 and beyond.

It is worth noting that because our supply areas have been designated by the Secretary of State as water stressed, we are required to consider all available options to manage demand, including metering, when preparing our WRMP. Following the statutory consultation we have carried out on our dWRMP and wider business plan consultation, we have chosen a universal metering programme to

FINAL 131113

achieve equity in service to customers while meeting our environmental obligations.

We have had regard to DEFRA's Guiding principles that companies with above the national average PCC should reduce that consumption to be at least at national average PCC by the end of AMP5. We expect to be at the national average level by the end of our compulsory metering programme.

Passed to / date: AW 5 August 2013

Clarifications:

Accepted by / date: RD 13/11/13

Response

All responses will be clearly identifiable and traceable and will append the following table.

Version No:	Draft	Final	
Date:	11/11/13	13/11/13	
Submitted to:	TM/AMcA	CCG Chair	
Prepared by:	CO	CO	
Approved by:	TM	CCG Chair	
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