

1. REGULATORY UPDATE

The purpose of this paper is to update the Water Forum on the latest regulatory developments in terms of messages from Ofwat and legislation relating to drinking water quality and environmental management and associated guidance. This summary highlights guidance from Ofwat and signposts the level of engagement that NWG achieves with the Drinking Water Inspectorate (DWI) and the Environment Agency (EA) as part of our regulatory approach. It provides insight into areas that need to be addressed within our business plan for PR19.

2. OFWAT

Ofwat are currently in preparation mode for the publication of their methodology consultation document on 11 July. We understand the document will be detailed and will include draft tables and a financial model. This should put Ofwat and the industry in a much better position than for the 2014 Periodic Review, with early clarity over business plan requirements.

The various Ofwat working groups on cost assessment, bioresources and water resources have completed, and the final consultative workshops have been run. With this in mind, Ofwat publications have been limited, with conference presentations by David Black (Ofwat Water 2020 Director) and Cathryn Ross as the recent highlights.

The opening of the non-household retail market on 1 April 2017 appears to have gone smoothly and has been highlighted by Ofwat as being successfully delivered by the market participants.

2.1 David Black's presentation at Water Industry Asset Management Conference, 10 May 2017

<http://www.ofwat.gov.uk/wp-content/uploads/2017/05/David-Black-presentation-Water-2020-Wholesale-markets-and-PR19-Water-Industry-Asset-Management-Conference.pdf>

Covered Ofwat's four key themes of **Innovation, Resilience, Customer Service and Affordability**.

Extract: Although we will be consulting on our detailed methodology from 11 July, last year in our May Water 2020 policy document we set out key aspects of the policy framework that will govern the next review to give you the visibility and certainty you need. That includes:

Strengthening our approach to customer engagement and outcomes. Companies should incorporate learning from their daily engagement with customers as well as a wider range of evidence such as pilots, rather than rely on traditional willingness to pay research. Co-creation and co-delivery recognises that customer lie at the centre of the water and wastewater value chains.

2.2 Towards the regulation of markets in water - speech by Cathryn Ross, The Future of Utilities 29 March 2017

<http://www.ofwat.gov.uk/wp-content/uploads/2017/04/Towards-the-regulation-of-markets-in-water-speech-by-Cathryn-Ross-The-Future-of-Utilities.pdf>

Mainly focused the opening of the non-household retail market, but there were other references to the new markets for water resources and bioresources.

Extract: After decades during which not much changed in the sector, we ushered in some big changes to the way we regulate in PR14. Difficult for companies and for investors to get their heads around initially. Not perhaps initially best handled by us either. We definitely had a collective wobble. But we came together, we ultimately agreed this was the right way to go. And I think everyone agrees that the 2014 review brought valuable additional flexibility for companies, better enabling efficiencies and provided better incentives for companies to do more of what their customers need and want.

After PR14 we said we wanted to build on that success to go further in the same direction. I wouldn't have been surprised if companies had said 'enough!' But they didn't. And in fact through the marketplace for ideas, they have helped co-create the Water2020 policy framework. And they have

engaged in a genuinely constructive way to agree the licence reforms we need to implement that policy through PR19.

2.3 Ofwat Guidance on the Economic Asset Valuation for the Bioresources Regulatory Capital Value (RCV) Allocation

<http://www.ofwat.gov.uk/publication/economic-asset-valuation-bioresources-rcv-allocation-pr19/>

This document sets out the approach for water and sewerage companies (WaSCs) to value their bioresources assets, following their consultation on this topic in March 2017. It sets out the information Ofwat require from Water and Sewerage Companies in **September 2017**.

3. DRINKING WATER

- 3.1 The Drinking Water Directive (DWD) is currently being revised after extensive negotiation across member states. The key change in the revised DWD will be the move towards a risk-based monitoring approach for drinking water parameters, although the formal issue of the new regulations is not due to be available until October 2017. It is anticipated that the impact from these legislative changes will be low for NWG and will not specifically influence PR19 outcomes.

The benchmarking of company performance data has also been under revision by DWI since August 2016 and a new water quality measure entitled the Compliance Risk Index (CRI) is being promoted to supersede the statistical measure used for the last twelve years - Mean Zonal Compliance. The drive for change is to allow greater focus on risk management, the types of breach and the possible number of people affected, as opposed to the current tool which simply focuses on compliance. The new measure is currently in draft form and NWG has provided thought-leadership to the proposed change by coordinating industry opinion and feedback through strategic liaison.

- 3.2 NWG is supportive of the new water quality index as it aligns with the expected changes to DWD whilst providing more focus on health-based breaches and the needs of the customer. We believe additional advantages of the new measure are the ability to assess company behaviours in relation to failure investigation, consumer advice, asset management and the timely delivery of operational or capital interventions; these elements are all captured within NWG's leading strategy to deliver clean, clear water that tastes good.
- 3.3 Once the components of the new CRI are confirmed, discussion will be required on how this can be translated into an ODI for the PR19 process. CRI is not directly comparable to Mean Zonal Compliance as it has a number of subjective elements factored into it as opposed to being a simple pass/fail calculation. NWG is currently working with the Water UK network to develop suggestions on how CRI can be taken forward into 2020-25 as a robust ODI and comparator measure for water quality.
- 3.4 As part of risk management, DWI is keen for companies to understand their single points of failure at water treatment works to help make assets more resilient and so protect consumers from events related to loss of supply or quality deterioration. Under the 'Too Critical to Fail' banner, the DWI are encouraging companies to mitigate such risks by having processes and/or procedures in place to manage a potential outage at a treatment works without impact being seen outside of the site boundary. Its direction of travel by DWI is very much aligned with Ofwat's focus on resilience. Shared learning industry workshops are currently being run to help identify good resilience practice in the water service and indicate common failure modes. For NWG, we understand the sites which carry the most significant risk and we will look to develop strategies for resilience based around the areas of process control, containment and recovery; for PR19, this will include further enhancements to water treatment disinfection regimes, filter management, and process run to waste options.

4. ENVIRONMENT

- 4.1 The EA is also currently looking at resilience, although from the perspective of treatment capacity. All waste water treatment works (WWTW) have limits to the amount of flow they can receive into them before treatment capability (and hence discharge quality) is affected; at this point inflows or partially treated sewage are commonly diverted to storm tanks for treatment at a later time. The trigger point

is known as Flow to Full Treatment (FFT) and is often influenced by weather conditions such as heavy rainfall. There is currently a desire by EA for improved monitoring and increased scrutiny in this area of compliance due to concerns that the settings for flow diversion are too low or incorrect at some sites across the industry.

- 4.2** The EA is currently carrying out a campaign of detailed assessment into FFT across the industry which in turn will result in a number of PR19 drivers for inclusion in draft business plans. These are likely to include say additional flow monitoring on WWTWs or increased storm tank capacity where current provisions are deemed inadequate. However, it is recognised by EA that any work-stream to improve FFT across the water industry needs to be proportionate and so any environmental programmes will be risk-based and spread over a 10-15 year depending on environmental impact, design requirements and planning, and costs at any given works. It is likely that some NWG sites will be included within this work and we are intending to support EA with a Task & Finish group to help set criteria and expectation around FFT improvements.

5. NEXT STEPS

The remainder of 2017 will see resolution and clarity being achieved on DWD, performance measures and impacts on our business plan from new regulatory priorities. The ability to influence regulatory change is seen as an opportunity within NWG and as a company, we continue have significant representation across various industry working groups. We will continue to constructively engage with regulators and offer a collaborative approach to consultations and outcomes.

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