
8 JUNE 2018

ANNUAL PERFORMANCE MEETING

NWL OFFICES, BOLDON HOUSE

MEETING NOTES

PRESENT:

Chair: Jim Dixon
Vice Chair: Melanie Laws

For Customer Council for Water (CCW): Bernard Crump, Robert Light
For Environment Agency: John Giles
For the Environment theme: Chris Barnard (Ouseburn Trust)
For the Customer theme: Mark McElvanney (StepChange), Graham Dale and Bhupendra Mistry (CCW)
For the Communities theme: Mary Coyle (Independent), Jo Curry (Changing Lives)
For Economic Impact theme: Steve Grebby (CCW), Sarah Glendinning (CBI)

Water Forums Independent Author: Sarah Young

For NWL Board: Margaret Fay (Independent Non-executive Director)

For the Company: Heidi Mottram, Ceri Jones, Louise Hunter, Richard Warneford, Elaine Erskine, Jim Strange and Chris Johns (part)

Ros Shedden (Water Forum Secretary)

NOTES AND ACTIONS

1. Welcome and apologies

Jim Dixon (JD) and Melanie Laws (MJL) shared the chairing of the meeting. MJL opened the meeting and welcomed everyone. She said the aims of the meeting were to look at the Company's two 2017 – 18 performance reports (Our Contribution and Annual Performance Report) and then later agree their positions statements. As PR19 was in full swing it was efficient to include the Company's progress on its Drainage Wastewater Management Plan and its Business Plan finances.

2. Our Contribution – Northumbrian Water Group's Environment, Social and Economic Impact Report

Members were given an early draft of the Company's Our Contribution Report at this meeting (8 June 2018).

Louise Hunter (LH) gave the context of the Our Contribution Report. In 2017 the Company had decided to start formal Capitals reporting. The Report forms part of the Company's formal reporting. It is not a regulatory obligation.

LH took members through the Report, describing the context behind the development the Report structure and content. LH said that the Company was in the process of embedding the Capitals into the normal business activity.

Members noted that, overall, the report was very good and they liked that the Company was doing this and was seeking to be leading. They made a couple of specific points – the Company should:

- check technical language and reduce or explain where needed (eg Capex, BI);
- in commentary, to give balance, flag areas of concern and state what it is doing to improve those areas; and
- in 'Highlights' - by changing this heading from 'key data' the company had inadvertently got some low lights, ie Leakage – also the Company should improve language/perspective to reflect the benefits for customers ie X awards - so what?

MJL said members would endeavour to give the Company further timely feedback on the concept and the document.

3. Drainage Wastewater Management Plans

Members had been supplied with a background paper before the meeting (3.0 Drainage Wastewater Management Plans (DWMP)).

Richard Warneford (RW) presented an overview of DWMPs and where the Company was in transitioning to the new framework. RW said that industry water resource management planning was really robust, this was the start of creating a robust and consistent approach to drainage and wastewater planning. However, drainage and wastewater planning was entirely different; it is not as controlled as water resource planning.

RW described the requirement for the water industry to demonstrate a consistent and transparent approach to long-term resilient drainage and wastewater planning. It supported:

- UK Government's draft Strategic Policy Statement to Ofwat and Welsh Strategy for Wales;
- Ofwat's PR19 Methodology; and
- EA's WISER.

The 21st Century Drainage Programme worked as a 'whole sector' partnership approach towards developing and enhancing integrated long-term planning for drainage and wastewater, and improved service to customers and the environment by addressing sewer misuse. It was starting from a good place as it built on existing frameworks and metrics.

The Company was actively supporting the programme in technical areas and providing the following experts:

- Richard Warneford – Programme Board
- Martin Huttly – DWMPs, Resilience Metrics and Capacity Assessment
- James MacLean – Storm Overflow Assessment Framework

RW showed the timeline for developing and publishing DWMPs and how they fit well with the Company's approach. He said one of the outcomes would be National Capacity Maps which would be published.

For PR19 the Company's plan included:

- developing its narrative and approach using gap analysis;
- working up additional costs under enhancements with supply chain;
- continuing to support DWMP steering group and contribute in trialling new elements
- DWMP dissemination event(s) in September 2018; and
- briefing Water Forum, Northumbria Integrated Drainage Partnership and other partners.

From 2018 until the start of AMP7 – the Company would be:

- preparing and starting DWMPs in collaboration with its partners;
- looking how the Company was structured with its Intelligent Asset Management team; and
- setting up an internal DWMP Implementation Group.

RW said the Company was in a good place to start this process. It was heavily involved in the developing the framework and knew what was coming.

Members noted the following:

- One problem was getting Local Authorities involved – members suggested could companies could consider asking the national body - Association of Directors of Environment and Planning (ADEPT).
- With regard to National Capacity Maps – these will show the integrated plan of the live risk and the future plan identifying:
 - problem areas; and
 - where large schemes are underway.

RW said the Company was really proud of its reputation with regard to working in partnership on sustainable urban drainage. MJL said members had visited Killingworth - as a resident she had not been aware of what the Company had done. Members said the Company should engage more widely on this type of work - distil the information on wider benefits to downstream customers and say what the scheme has done for the community. This had been is a theme in the recent CCWater Conference about letting customer know about the good work going on around them (**Challenge**).

RW said the DWMP note which had been provided (Item 3) said 'possible work for AMP6' - this programme had been confirmed so the word 'possible' should be removed. Jim Dixon (JD) said the note had helped members understanding of what was to be done, but the Company could be clearer on how much of this was in the PR19 Business Plan. RW said there was about £18m of work to be done, about £3m to be done in this AMP.

Graham Dale (GD) said the Company could use its experience of working in partnerships to set best practice models for DWMP.

Steve Grebby (SG) said he sat on the Programme Board and he agreed that the Company was ahead of the rest. He urged the Company to stand up and lead because other companies and organisations were struggling. Margaret Fay (MF) said this could go hand in hand with involving partners RW said yes, the Company should work as a partnership.

MJL said this was a tremendous piece of work, working in partnerships, education campaigns, and customer participation.

4. Annual Performance Report

Members had been supplied with a background paper before the meeting (4.0 Annual Performance Report).

Jim Strange (JS) said the Company would be publishing its Annual Performance Report on or before 15 July. He said the Report wasn't finalised and some numbers were still draft.

JS brought members attention to the more notable performance outcomes:

- **Service Incentives Measure (SIM)** - the Company had dropped from first to third – this was a natural variation in the numbers, position tended to be volatile as the gap between companies, and the bottom and the top score was very small. Heidi Mottram (HM) said this is hugely disappointing for the Company. Members said this was actually good to hear, because it showed healthy competition. HM said first position is important because you would know that you are giving customers really great service.
- **Leakage** – the Company's leakage levels were a little higher than the Performance Commitments (PCs) in both operating areas (in mega litres per day E&S 66 vs 66.17 and NWL 137 vs 137.15). This had been on target but the February weather (Beast from the East) had increased the leakage level to just above the PCs. The Company planned to renew its efforts and the work it had done in 2017 – 18 meant it was in a healthy position in the new reporting year.
- **Overall drinking water quality compliance** – 99.938% compliance from 45 failures out of 70,341 samples was slightly better performance than in 2017. This was a high level of compliance and none of the failures gave any risk to health. However, this performance placed the Company behind others. The Company was committed to improving.
- **Taste and odour** - targets had been set wrongly by Ofwat; this had now been corrected. The Company was now in a good place and was meeting its performance commitments.
- **Sewer flooding** – the Company was ahead of its PC; however there was no room for complacency on sewer flooding, it would continue to push on.
- **Interruptions to supply** – the Company's performance had deteriorated due to a small number of longer interruptions – it was still beating its PC and continued to compare well to the rest of the industry.
- **Pollution:**
 - Category 3 – this had been a real area of focus for the Company – it was really proud to maybe be leading - also had gone 12 months without a serious pollution.
 - Category 1 and 2 – performance on these has also improved.
- **Implementing billing system** – the live by date was delayed (30 days late) as the Company was concentrating on getting the system right. CCWater members said this was the right thing to do and it seemed to have gone well. HM said it was operating well

Members noted:

- **On leakage:**
 - Difficult to manage because it is measured in March, which means winter impacts needed to be assumed and to over compensate by expecting the worst would give a high cost to customers - Ofwat had recognised and change this measure for 2020 – 2025 when leakage would be measure on a three-year average.
 - The Company was using innovative ways with lots going on, however the trends were not demonstrating improvement; HM said the Company shared the frustration. However, she was certain that improvement would be evident in coming years.
 - There was a 1 mega litre difference between the paper and this meeting. Leakage measurement was a hugely complex process, it was not usual for this to happen. There was an external auditor going through this number at the time of this meeting (7 June 2018).
- **On The Beast from the East** (27 February to 10 March 2018):
 - Resilience to incidents was really important to customers and the Forums should take a view on this; from what the Forums have seen. Companies were more resilient when their incident management was part of their DNA rather than a dusty book on a shelf.
 - In the past the Company had been good at managing normal and extreme events, the Beast was a particularly good example of resilience planning - people empowerment was as important as a company's assets.
 - Ofwat had requested information on how the water industry had fared (19 March 2018) – members had been supplied with the Company's response.

- CCWater had taken part in Ofwat's review – but its views were embargoed until after Ofwat's Report was published.
- Organisations should expect that extreme events are the norm.
- Communications matter - the Company's communications had been really low key; HM said if you scare people they will fill baths; it is the wrong thing to do.
- **On penalties and rewards** – the Company was forecasting a net reward for the 2015-2020 period of £23 million, this was largely earned on excellent performance on interruptions in supply and sewer flooding, offset by two small penalties for leakage performance in Essex & Suffolk Water.
- **On maintaining transparency of reporting** – the Company was:
 - awarded "Self Assured" status by Ofwat in November 2017;
 - continuing to publish two versions of its Annual Performance Report;
 - continuing to be a strong supporter of the Discover Water website;
 - continuing to conduct an extensive customer engagement programme which, where appropriate, it will share its actual and comparative performance; and
 - consult annually on its Draft Assurance Plan – this will include gap analysis.
- **On the 2019 Business Plan:**
 - **Sewer flooding challenge** – the Company was not reconsidering its response to their challenge to improve on external sewer flooding – it was committed to zero internal sewer flooding and did not want to overstretch at this time.

Members said this paper (4.0) was excellent, it was great to read – and had good level of detail.

5. Business Plan Finances

Members had been supplied with a background paper before the meeting (5.0 Business Plan Finances). JD said it was important that members take an interest in this.

Chris Johns (CJ) gave a recap of Ofwat's Aide Memoire and which financial aspects Ofwat required CCGs to explicitly comment, challenge or ask companies to provide evidence on customers' views – they were:

- Corporate and Financial structures (8b) – where Ofwat was looking for high levels of transparency and engagement with customers on issues such as corporate and financial structures.
- Securing cost efficiency and need for investment (10) – where with regard to cost adjustment claims – Ofwat needed assurance of support from customers and CCG.
- Financeability (11) – Ofwat need assurance that customer support where companies take steps to address financeability constraints.
- Bill profiles (12) – regarding the impact of PAYG and run-off rates – assurance that customer views on the bill profile over time had been addressed.
- Accounting for past delivery (13) – regarding reconciliation items to 'rulebook methodology' – assurance of customer support for anything the Company was choosing to do.

CJ then summarised the Company's position on each of these areas, he said none were "contentious".

Members noted:

- **Corporate and financial structures** – the Company:
 - doesn't have a complex corporate or financial structure;
 - publishes a copy of our organisation chart on its website, in Our Finances Explained; (OFE) publication, in its Annual Accounts and Annual Performance Report (APR), so is fully transparent.
 - is not a highly geared company (not above Ofwat's 70% level);
 - does not have 'whole business securitisation' financing structure or Cayman companies;

- pays tax; and
- and is not the target of Ofwat's focus on highly leveraged companies.
- **Corporate and financial structures** – customers:
 - have said the Company tell them everything they want to know;
 - tell the Company they trust us;
 - through Customer Focus Groups, have told the Company they didn't want to read long report on "Finance" – they were really switched off by "Thames" approach; and
 - told the Company they just wanted to know where their money goes – this is all covered in OFE publication in very clear and simple terms with graphic information also now included in customer bills to show the cost per day and where that money goes in very simple language – giving simple and clear customer communications, giving customers the level of information they want.
- **Securing cost efficiency and need for investment** - customer:
 - acceptability of size of 2020-25 investment programme and priorities had been tested; and there was
 - support for base plan, resilience and enhancement schemes.
- **Securing cost efficiency and need for investment** - Company:
 - Total PR19 capex could be c.£1.4bn (17/18 prices) (c.£0.7bn Water/c.£0.7bn Waste Water).
 - Capex split c.£0.7bn 'base' and c.£0.7bn 'enhancements'.
 - Net opex could be c.£1.6bn (17/18 prices) for 2020-25 (c.£0.95bn Water/£0.45bn Waste Water/£0.2bn Retail).
 - c.£3bn Totex (17/18 prices) for 2020-25.
- **Securing cost efficiency and need for investment** - Company:
 - was an efficient operator;
 - was outperforming AMP6 totex by c.15%;
 - had strong operational and financial performance that has supported over dividend yield and RoRE in 2015-2017;
 - had not had any large ODI windfalls like SVT – all ODIs go to RCV in 2020 currently;
 - believed its cost profiles were upper quartile (UQ) based on Ofwat's latest models and its own assessments;
 - was aiming to position its business plan costs at where it believed Upper Quartile would be for PR19;
 - had shifted the efficiency frontier for costs down in AMP6 which benefits all customers;
 - would share the AMP6 cost outperformance broadly 50/50 with customers at 2020;
 - would lower cost allowances set from Upper Quartile position for AMP7 which again would benefit customers through lower bills;
 - had not made any cost adjustment claims for "special factors"; and
 - had addressed customer engagement requirements for all the discretionary enhancement schemes (which had already been shared with the Water Forum).
- **Financeability** – the Company:
 - had tried to keep PAYG/RCV run-off rates close to the natural rate as possible for PR19, just like the Company did for PR14; and
 - had not made changes to customer bills to address any financeability constraints.
- **Bill Profiles:**
 - the reduction in WACC (3.6% to c.2.3%), lower totex cost allowances, fall away in AMP5 revenue correction mechanism all mean that NWL (and ESW) customer bills would all reduce significantly;
 - bill reductions were expected in spite of WINEP and enhancement programme;
 - revenue for NWL could fall by c.£80m pa;
 - bills could for NWL (and ESW) customers fall by c.10%;

- the Company was continuing to look at bill profiles to smooth any YOY effects across 2020-25 bill profiles and link back to Financeability;
 - with revenue reduction of c.£80m pa anticipated from 2020 the Board taken decisive action now to preserve its strong investment grade credit ratings;
 - the revenue reduction flows down to bottom line profit and cash availability;
 - the Company was keen not to “play around” with PAYG/run off rates etc to “prop up” revenue;
 - its flexible dividend policy was being used decisively by the Board to preserve its ratings commitment, well ahead of 2020;
 - cash dividend paid in 2017/18 for NWL reduced by c.50%;
 - Dividend forecast for following years through to 2020 significantly reduced again to ensure not over-levered at 2020; and
 - financial capacity was being created to absorb the challenges that PR19 would bring.
- **Accounting for Past Delivery:**
 - it was difficult to talk about regulatory accounting reconciliations with customers – Ofwat recognised this;
 - the Company had demonstrated clearly how it shared our efficiency outperformance with customers (50/50) – its customer research confirms customers support this sharing of gains/losses;
 - the Company had applied all reconciliation adjustments in-line with PR14 rulebook and used Ofwat’s models
 - its work has been assured; and
 - Ofwat’s new Financial Flows would give greater clarity of this and the Company was aiming to publish the new information alongside our 2017/18 APR even though no requirement yet.

CJ said he would spend time with Bernard Crump to go through more detailed financial matters.

Members noted that the Company was to donate a 1% contribution to communities - this was a commitment the Company had always made; it had no intentions of changing this.

JD said the financial stuff was the responsibility of the Board - however this would be an area that would feature more on the Forum agenda - because of the political agenda.

SG said this was a really good paper, this should also be translated onto plain language on the web site for customers (the current financial information was very good).

Members noted that there would be a one-off adjustment to the 2021 bill – for Water Trading and there were various things in the Ofwat rule-book which encouraged companies to be as efficient as possible - so companies gain a benefit which is shared with customers (it would however be a low sum - pence). The Company said it would summarise the outcome of any adjustments and bring them back to the Forums (**Action Company**).

6. Finally a message from Heidi

HM said the Company had been really pleased to receive the members support in the review of the Business Plan. Many adjustments have been made. The Company is now going to take these out to customers. Members said the Company was usually really good at listening.