

Ofwat
Centre City Tower
7 Hill Street
Birmingham B5 4UA

28th August 2024

By email - PR24consultation@ofwat.gov.uk

Dear Sir.

Response to PR24 Draft Determinations

Thank you for the opportunity to comment on your PR24 Draft Determinations for the water companies in England and Wales and your explanatory letter covering the headline points for the NHH Market.

As the representative body for the water retailer community, our response is focused solely on the specific factors that will impact and/or benefit the Water Retail Market and NHH customers. We see these as:

1. Smart metering.
2. Smart meter data.
3. Water efficiency.
4. Wholesaler alignment with the Market and incentivisation.
5. Wholesale charge increase and transparency.

We appreciate the proposed investment is the largest the sector has seen since privatisation and is vital to ensuring water security and environmental improvements for our future. We believe Retailers and the NHH Market have a key role to play in helping deliver the improvements in service to customers and the environment. We set this out below under our five themes.

1. Smart metering.

Smart metering is key for both achieving the reduction in demand set out in the Environment Act, i.e. 9% by 2038, and for the development of value-added services for customers and future success of the Market.

UKWRC members therefore welcomed Ofwat's stance in their PR24 methodology that all new meters should by default be smart. We therefore support the Wholesalers' commitment to roll out smart metering.

However we note that the Draft Determination funding is 13% lower than the £1.8Bn requested by the water companies. We also note that whilst six companies have an increased allowance for smart metering, eleven have a reduced allowance ranging from 12% down to 59%. Further, the two wholesalers with the most experience of smart meter rollout have their allowances reduced by 30% and 32%. We do not follow the basis of this, given that i) their experience in smart meter installation, ii) the costs are presumably based on competitively sourced contract rates and iii) the assumption that they have completed most of the easier installations and will be moving onto the more difficult, and by definition, more expensive installations.

We would be very concerned if the potential impact of these funding reductions, combined with the use of an average unit rate, incentivised Wholesalers to focus on replacing the cheapest and smallest meters, rather than those that could give greater benefit to customers and the environment. We explain this further below.

The Draft Determinations do not specify the split in numbers between household and non-household smart metering. However, they do expect companies to achieve a 7.5% reduction in NHH consumption in England by 2029-30, of the 2029-20 baseline.

Of the total consumption in the NHH Market, 72% is accounted for by the 13% of higher users with large and medium size meters. It will be critical for achieving the reduction target that these customers and their medium and large size meters are included in the smart meter rollout. However, Wholesalers will be incentivised to deliver as many smart meters as they can for their reduced allocation. This means they will focus on the easier to install and cheaper household meters at the expense of larger NHH and/or the harder-to-read or more remote NHH meters, potentially leaving those to the next AMP. UKWRC members see this as a significant issue that needs to be addressed in the Final Determinations by a separate unit rate for medium and large NHH meters and the 'long unread' and the more difficult to reach meters. This should be backed up with a target and separate PCD for the rollout of medium and large meters¹.

Rollout of smart meters.

Whilst not directly a Draft Determination issue, we also wish to comment on the rollout of smart metering and the planning process and communications with customers.

We firmly believe there is a need for a consistent strategy across the Market for the rollout of smart metering in Water - to avoid the problems encountered in the Energy sector. That strategy should include at least: planning which meters are replaced, and for NHH customers,

¹ National Metering Strategy defines medium size meter as 25-65mm and large meters as 80mm and above.

Wholesalers working with Retailers - to include setting priorities and identifying those NHH customers most likely to be interested in smart metering; communications with customers and with Retailers and keeping both informed; and providing access to smart meter data. We cover these further below.

Once developed, all Wholesalers should be obliged to comply with the strategy for rolling out smart meters.

Customer communications.

Wholesalers and Retailers need to consider the customer smart metering journey and the processes to support this. Customers should therefore be provided with clear, informative and consistent communications – from the high level and reasons for smart metering in Water to the basic administration of when their smart meter will be installed, including potential access arrangements. There needs to be agreement on who – Wholesaler or Retailer – is responsible for each stage. We are therefore suggesting the communications process and responsibilities should be developed and agreed through an RWG subgroup. However, to ensure compliance with such a strategy will need support from Ofwat.

We believe Ofwat is considering some form of more centrally controlled and coordinated approach to rollout, potentially taking on board the lessons from Energy. However we are unsighted on this. We would value hearing further information on this and potentially working with you to develop a coordinated and consistent approach for NHH customers.

2. Smart meter data.

There is little reference in the Draft Determinations to the significant data volumes that will be generated from smart meters installation, who owns that data, how it will be made available and how and who will use it to benefit customers and the environment.

Whilst the National Metering Strategy sets out some principles around data sharing and governance and the provision of 'data-related service to customers' and charges for the provision of data, this work is incomplete and it seems subject to different interpretation by some trading parties, with e.g. some Wholesalers now offering a service free of charge to NHH customers, based on smart meter data.

To ensure a positive experience for customers, there must be a clear and consistent approach nationally to the availability and costs of providing their smart meter data.

UKWRC members believe a framework covering the ownership, access, use of smart meter data and the interface with customers must be developed as a matter of urgency. Such a framework should not be just a good practice guide, but must be an expectation, monitored and enforced by Ofwat.

The costs of providing smart meter data were questioned at the recent MOSL-facilitated PR24 Draft Determination NHH workshop (14th August 2024). Ofwat's response then was – 'is not the Thames Undertaking good enough?'. However this was challenged by a Wholesaler representative suggesting this was not a requirement on other companies and depended on the costs incurred.

Such difference in views and lack of clarity clearly suggests the need for a proper and informed discussion on the process and costs for the provision of smart meter data and the development of a common and enforceable framework.

3. Water efficiency

UKWRC members are acutely aware of the predicted 4000Ml/d gap in public water supply by 2050 and the need to meet this gap, half through increased supply and half by demand reduction, noting that at the same time meeting the needs of new development to deliver the Government's growth agenda.

Retailers therefore accept the challenge of working in collaboration with Wholesalers to help deliver the target of 7.5% reduction in NHH demand by 2030, cf the 2019-20 baseline, and the 9% reduction by 2038. We do though note the regional variation in NHH demand reduction targets from 14% for Northumbrian to zero for Affinity.

However, we have concerns that the Draft Determinations and recent Ofwat 'PR24 Common Performance Commitments' paper, whilst clarifying some points, will encourage Wholesalers to deliver water efficiency interventions themselves, rather than involve and work with others, including Retailers - who can bring additional value. We believe the incentive for Wholesalers to collaborate is not sufficiently strong.

Retailers' added value

We understand that water security is one of the key priorities to deliver the Government's growth agenda. Improving water efficiency is a key component of water security, as are more innovative options including alternative sources to potable supplies, where appropriate for industrial or process use.

We believe Retailers' involvement in promoting and delivery water efficiency will both add value and deliver better outcomes.

1. Retailers are by their nature sales organisations. They know their customer base and have the relationship with their customers; especially so with those customers who have switched. Retailers have conversations with their customers and therefore understand their wants, needs and expectations. They are well placed to inform and engage those customers, not just on saving water but on the wider implications of impacts to their business from a potential shortfall in their supply needs.

2. Retailers can reach, promote consistent messaging and directly engage multi-site, multi-region customers - something not possible for Wholesalers.
3. Retailers have the capability to share learning and experience from one NHH customer's site in one region with all their NHH customers across the country.
4. Retailers have, because of the competitive market and desire to retain valued customers, pressure to deliver more innovative service offerings, including for water efficiency, rather than the conventional 'quick-fix' approaches more suited to household properties pursued by Wholesalers.

Retailers can therefore be the key to a step-change approach in delivering water efficiency savings, enabling better outcomes for both customers and the environment. In contrast, in the current climate, water companies (i.e. Wholesalers) are no longer seen as trusted parties, so are unlikely to get the same level of engagement with customers that Retailers can achieve.

In addition, the current financial arrangements set out in the Draft Determinations incentivise the conventional Wholesaler short-term approach to deliver a target number, rather than more innovative and sustainable approaches to deliver the right outcomes for customers and the environment.

We would also refer you to the Strategic Panel's Open Letter on Water Efficiency² that sets out the case for the Market-led approach:

'The benefits of a market-led approach include a dedicated focus on customers; a better understanding of diverse non-household requirements; and the ability to take a national perspective with customers who may have sites in different regions. Retailers are in a strong position to engage with customers, and it is widely acknowledged that customer engagement – or rather the lack of it – is a critical challenge that needs to be overcome to achieve greater water efficiency.'

We believe Wholesalers working in collaboration with Retailers to deliver water efficiency promotions and intervention could bring a step change in NHH customer response, where saving water has generally been of low importance because of the low potential cost savings compared with energy reduction and the poor return on investment. Retailer input is therefore key to ensure the water efficiency and, more appropriately, the water security agenda is received and acted on by NHH customers.

Retailers should therefore be seen as the valuable and trusted 'salesforce' for the Wholesalers, who together can deliver so much more than separately.

² <https://mosl.co.uk/documents-publications/8367-strategic-panel-open-letter-on-water-efficiency/file>

Collaboration

We welcome Ofwat's update in July to the Business Demand PC paper, but we do not believe this goes far enough in incentivising the potential for collaboration.

The paper suggests three examples of collaboration. We believe this should be extended to encompass all the five menus set out within the RWG 'Menu for Wholesaler and Retailer collaboration on NHH water efficiency'³ i.e.:

1. Retailer promotion of wholesaler lead interventions.
2. Wholesaler funding for retailer lead interventions.
3. Outputs based general funding scheme.
4. Inputs based general funding scheme.
5. Wholesaler issued alerts and notices.

We welcome the introduction of the requirement to complete the proforma to confirm evidence of collaboration, including the sign-off by the collaborating partner. We assume the intention was that 3rd parties would mean a consultant or contractor working directly for the customer. However, in its current format the water company could evidence 'collaboration' as working with one of their pre-existing contractors, without discussion or engagement with any Retailer operating in their region. This requirement for collaboration with third parties should therefore be clarified to avoid exclusion of Retailers in an update to the PC paper.

Further, we have reservations that the financial incentive associated with the requirement to collaborate is linked only to out-performance payments. So where a wholesaler faces a tough target and is unlikely to be able to achieve any upside, any incentive to collaborate is lost.

As set out above, to achieve the challenging demand reduction targets will, we believe, require Wholesalers, Retailers and third parties working together through a mix of collaboration, coordination and partnerships between Wholesalers and other parties who can add value. This would include Wholesalers providing incentives and making funds available to Retailers and/or genuine 3rd parties to provide their customers with water efficiency support.

Our final point on funding is the link back to smart metering and the significant reductions in funding for smart meter rollout, despite expectations on number of meters installed remaining unchanged. As we pointed out in our comment on smart metering (1) this is likely to drive Wholesalers to focus on easier and cheaper household and small NHH installations at the expense of the medium and larger meters supplying the 13% of customers who account for 72% of NHH demand.

³ <https://mosl.co.uk/document/groups-and-committees/retailer-wholesaler-group/rwg-water-efficiency-guidance/8363-rwg-guidance-document-collaboration-on-nhh-water-efficiency-final-draft-120624-1/file>

Wholesalers who adopt such an approach are therefore unlikely to be able to deliver on their PC for Business Demand reduction. There is therefore a potential discontent in the Draft Determinations between funding for smart metering, essential for identifying and prioritising the opportunities for water saving and the ambition for delivering demand reductions.

4. Wholesaler alignment with the Market and incentivisation.

UKWRC strongly supports the introduction of the BR-MeX incentive and looks forward to this driving Wholesalers to deliver the right outcomes for NHH customers and the Market.

In our response to the draft Methodology we noted that Ofwat proposed to make outperformance and underperformance payments for BR-MeX proportionate to those for C-MeX, based on revenue collected.

We welcome therefore the increase in incentive from the +0.05% to -0.1% to the more proportionate +/-0.2% RORE. We believe Ofwat was previously considering a review of the C-MeX incentive. If this should change then the BR-MeX incentive should move accordingly and keep pace with the C-MeX incentive.

Members welcomed the inclusion of MPF data within the BR-MeX measure, as the latter provides a significantly greater scale of incentive. However there is a concern that MPF development is behind schedule and key components around data quality, particularly around premises and meter asset data, may not be available in time, resulting in their omission from BR-MeX from 1st April 2025.

Retailers are concerned that BR-MeX focuses on the right metrics, including those from the MPF. If MPF data is not available for inclusion by April 2025, then there needs to be a mechanism to include this from April 2026, rather than delay further until the next AMP.

5. Wholesale charge increase and transparency.

Ofwat has suggested that the average bill increase for households (excluding inflation) will be 21% by 2029-30, yet the wholesale charge for business customers has been advised as 27%. We have yet to hear a clear explanation of why the non-household wholesale increase will be almost 30% above the charge increase for households, which includes the retail costs.

At the recent PR24 DD Workshop, Retailers present questioned the disparity. Ofwat responded that this was an estimate based on companies split of cost allocation between HHs and NHHs, based on Ofwat's Charging Guidance. However we are unsighted on how costs are being allocated by Wholesalers or whether they are doing it on the same basis.

This 'anomaly' has already been remarked on by the Federation of Small Businesses in their Press Release of 11th July 2024 – *'Rise in water bills hard to swallow for small firms'*. It starts

with 'Businesses' water bills are estimated to be set to rise by 27% on average, almost a third higher than the 21% average rise estimated for households'.

Consequently, Retailers have already been asked for an explanation of this difference, but they are currently unable to provide one.

Retailers therefore need a clear and rational response that customers will understand. It would also be helpful if Ofwat could set out how Wholesalers are expected to allocate costs between HH and NHH customers and how the Guidance ensures that the cost allocations between NHH and HH customers are proportionate and truly cost reflective.

Retailers require this information preferably before, but at the latest, with the Final Determinations.

We trust you find these comments pertaining to the Draft Determinations on the Water Retail Market helpful and constructive.

We would be happy to discuss any of these points further at our next Ofwat-UKWRC meeting.

Yours faithfully.

A handwritten signature in black ink, appearing to read 'P Mills', with a long horizontal line extending from the end of the signature.

Phillip Mills
Chair
UK Water Retailer Council