

Bristol Water Business Plan 2020-2025

Assurance Report
September 2018

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Foreword

In April 2016, I was appointed the Independent Chair of the Bristol Water Challenge Panel, a vital component of the assurance regime required by the water sector regulator Ofwat. Our role is to act as a champion for the customers of Bristol Water and to make sure that the company understands what customers expect from their water company. Given that water is essential for life and that customers have little choice in which company provides their water supply, the views of Bristol Water's customers will guide the decisions made by the Board of Bristol Water regarding issues such as the cost of bills for the customer, the resilience of the water storage and distribution network, where innovation can drive improvements and lower costs as well as how the natural environment of the water catchment should be stewarded.



Every water company in England and Wales has a similar committee set up to carry out three roles:

- To assure Ofwat of the quality of the customer engagement with Bristol Water customers
- To scrutinise and challenge the extent to which the views, priorities and preferences of customers is reflected in the 5-year business plan by Bristol Water for the asset management period from 2020 to 2025
- To scrutinise the performance of Bristol Water on the performance commitments and promises it made in its 2015 to 2020 business plan.

The Bristol Water Challenge Panel is independent from both Bristol Water and Ofwat, although we enjoy excellent working relationships with both organisations. This report sets out the evidence of how the Challenge Panel has carried out its role. In order to assist the Challenge Panel in carrying out its function, we have adhered to the duties and responsibilities set out by Ofwat in its various documents. Additionally, either the Independent Chair or the Deputy Chair have attended meetings, workshops or conferences organised by Ofwat and the Consumer Council for Water to assist us in the execution of our roles.

Challenge Panel members exhibit a range of the strengths, skills and expertise relevant to the roles it carries out. Members of the Challenge Panel are drawn from business, public health, university academics, farmers, local councillors and more. Additionally, the detailed knowledge of water regulation is provided by members representing The Environment Agency, Natural England and the Consumer Council for Water.

The Challenge Panel is pleased to report the excellent working relationships with the company. Bristol Water kept the Challenge Panel informed of their progress with the customer engagement framework and sought our views at an early stage in the process of writing its business plan.

Supporting the work of the Challenge Panel were a number of executives and managers from Bristol Water, including, the Director of Strategy & Regulation, Chief Customer Officer, and Head of Customer Service. Specialists such as the Head of Water Resource & Environment, Regulatory Policy Advisor, Head of Economic Regulation, among others, enabled the Challenge Panel to probe deeply on behalf of the customer the range of strategic plans, policies and reports in development during the asset management period.

The agenda conferences for each Challenge Panel meetings was attended by the Independent Chair, Deputy Chair, Report Writer and relevant executives from Bristol Water. Full Challenge Panel meetings and sub-group meetings were attended by relevant Bristol Water executives and, at times, the Chief Executive and Bristol Water stakeholder board members.

The scrutiny and requests for information arising from discussions in the Challenge Panel meetings, sub-groups and consultations are set out in the Panel's Challenge Log. As Bristol Water responded satisfactorily to each challenge, it was removed from the active log and archived. The summary of the

archive provides the evidence the Challenge Panel provides to Ofwat in carrying out our role. The Challenge Panel raised more than 600 challenges. One in four of our challenges has resulted in a change in the way that Bristol Water conducts its business that benefits the customer.

This report sets out the evidence on customer preferences and priorities gathered by the company's customer engagement strategy and vulnerability, valuation and acceptability research which involved more than 37,000 customers of Bristol Water.

In general terms, the Challenge Panel is pleased to assure Ofwat of the high quality of customer engagement evident in the Bristol Water business plan; a plan that focuses on building trust, being transparent in its undertakings and inspiring confidence among its customers. The reduction in the cost of the bill will be welcomed by its customers. Customers will also be pleased with the environmentally-focused performance commitments that respond to customer expectations as identified in the customer engagement research activities. Also in the report are two areas where the Challenge Panel raises a lack of consensus regarding the performance commitments proposed by Bristol Water in its business plan. However, the impact on the customer is not material in the context of the overall business plan.

The publication of this report is the culmination of work carried out by the Challenge Panel from 2015 to September 2018. With Bristol Water designated by Ofwat as 'prescribed', it was important that the Challenge Panel ensured that Bristol Water built its customer engagement strategy from first principles, taking nothing for granted regarding the breadth of its knowledge of customer preferences. Implementing the business plan will be challenging, as many of the performance commitments are stretching while others rely on changes in customer behaviour in order to be achieved.

I wish to express my enormous gratitude to the members of the Challenge Panel for their insight, dedication, incisive analysis and commitment support in carrying out our work over this period. The Challenge Panel as a whole took very seriously our responsibility to obtain and represent the views and priorities of customers fully and comprehensively. The Deputy Chairperson and Report Writer have worked tirelessly over the period to challenge, record and report the work of the Challenge Panel and deserve particular thanks for their sterling efforts.

I now await the response from Ofwat regarding the assurances provided by the Challenge Panel in this report and in connection with the quality of customer engagement with customers of Bristol Water. Ofwat's feedback and further scrutiny will be reported to the customers of Bristol Water in due course.

Mrs Peaches Golding OBE

Independent Chair

Bristol Water Challenge Panel

Executive Summary

The role of the Bristol Water Challenge Panel is defined by Ofwat, the water regulator, and is three-fold in nature; firstly to provide an independent assurance to Ofwat of the quality of customer engagement undertaken by Bristol Water, secondly, to provide evidence of the extent to which the findings from its customer engagement is reflected in the company's business plan for the period of 2020 to 2025 and lastly to scrutinise the performance of the company on the commitments and promises it made for its 2015 to 2020 Asset Management Plan (AMP).

The Challenge Panel is independent from Ofwat and Bristol Water, yet works with each one to obtain the best outcomes for customers of the water company.

As Bristol Water is in the prescribed category by Ofwat, the Challenge Panel was acutely aware that the company would be receiving greater scrutiny than most water companies regarding the quality of its customer strategy, its analysis and translation into its business plan. As a Challenge Panel, our ambition is to assist Bristol Water to become the best performing company in the water sector, and possibly the utilities sector as a whole. In order to do so, the Challenge Panel comprises a range of skilled independent contributors drawn from diverse backgrounds as well as a selection of stakeholders such as the environment regulators (Natural England and Environment Agency) and the Consumer Council for Water.

This report sets out the evidence of how the Challenge Panel has carried out its role. In order to assist the Challenge Panel in carrying out its function, we have adhered to the duties and responsibilities set out by Ofwat in its "Customer engagement policy statement and expectations for PR19" published in May 2016, its publication "Delivering Water 2020: Our final methodology for the 2019 price review" from December 2017 and the Ofwat "Aide Memoire for Customer Challenge Groups" from March 2018. The extent of challenge made by the Challenge Panel exceeded the issues in the above documents as the strengths, skills and expertise of Challenge Panel members broadened, augmented and enriched its discussions and deliberations.

The Challenge Panel was keen to ensure that the customer engagement strategy was rooted in the realities facing customers in the short and longer term and presents evidence to this effect. Among these key issues facing the local area are the impact of austerity measures on certain customers, the expectation of a resilient water supply and service as well as the longer-term potential for climate change to affect water supplies, the scarcity of water as a natural resource and the importance of stewardship of the water catchment.

The Challenge Panel wishes to highlight that 25% of its challenges and scrutiny have resulted in changes in how the company carries out its business. The Challenge Panel has had real influence over the creation and implementation of the customer engagement strategy and how it has been translated into the Bristol Water business plan.

Throughout the period from 2015 to 2019, the Challenge Panel has worked closely with executive directors and senior managers of Bristol Water to:

- establish a customer engagement framework that used a wide range of research techniques to understand customer priorities and preferences
- scrutinise the findings revealed in customer research
- challenge Bristol Water on its triangulation of the research and the valuation data obtained
- examine and ensure that customer preferences were driving company decisions regarding its business planning process
- assess whether the final business plan met customer expectations and priorities.

The Challenge Panel has tested Bristol Water to ensure that the voice of the customer is heard in all its diversity and that their needs and priorities are reflected throughout the business plan. The customer engagement plan included several notable innovations, including the use of an interactive game to engage customers. Importantly, bespoke research aimed at understanding the needs and

priorities of vulnerable customers has resulted in a step change of support targeted at these individuals. Comparisons between vulnerable customers and control groups on particular pieces of research ensured that Bristol Water could compare and contrast priorities across its entire customer base.

The Challenge Panel is pleased to report that the Director of Strategy & Regulation, Chief Customer Officer, and Head of Customer Service attended Challenge Panel agenda conferences, meetings and sub-group meetings, keeping the Panel informed of their progress with the customer engagement framework and seeking its views at an early stage in the business planning process. Specialists such as the Head of Water Resource & Environment, Regulatory Policy Advisor, Head of Economic Regulation, among others supported the Challenge Panel in probing deeply on behalf of the customer the range of strategies, policies and reports in development during the asset management period.

Throughout 2016, an Independent Non-Executive Director of the Bristol Water Board attended several Challenge Panel meetings as both observer and contributor. The executive director and senior managers supporting the Challenge Panel responded well to the scrutiny posed by the Challenge Panel and were supportive of our requests for, say additional information, greater clarity wider considerations or clearer communication, in a timely and transparent manner and as thoroughly as practicable. There were times when the Challenge Panel found that the executives had advanced quicker in the development of the business plan than the Challenge Panel was informed or that business planning concepts were developed before the Challenge Panel had an opportunity to scrutinise them thoroughly. However, the Challenge Panel felt it had contributed to the formulation of strategies through its influence on the executive team and in reports to the Bristol Water Board, the latter by presentation of the yearly Annual Report written by the Challenge Panel.

Members of the Challenge Panel participated in a number of consultation and research initiatives, either as observers or in the role of an independent, 'honest broker' chairperson in bringing together company, local council, community leaders and customers. Bristol Water develop a broad-ranging customer engagement strategy involving 50 pieces of research and that obtained responses from 37,000 customers.

As part of the customer engagement strategy, Bristol Water defined its customer base and created segments to understand the impact of its operations and activities on customers of differing ages, income and other characteristics. As a result, the Challenge Panel has seen clear evidence that the bespoke performance commitments set out in its business plan reach into new areas of activity (such as the measuring of community satisfaction with investments in co-created community activities).

The Challenge Panel has seen evidence that Bristol Water also is proposing to assist customers with the affordability of their water bill and provide support for vulnerable customers.

Bristol Water is meeting its statutory obligations regarding the environment, although there is little in the plan that it is doing anything outstanding or above and beyond. The Business Plan includes some key projects in WINEP that will help to address diffuse pollution threats to lake SSSIs under the company's ownership, together with important strategic work to develop its future direction on Biodiversity and Natural Capital enhancement. The Panel has evidence that the business plan meets the value for money expectations of its customers.

The Challenge Panel notes that changes in the Bristol Water Corporate Board and company shareholders have resulted in the lack of an independent designated non-executive director focused on customer engagement for a period of some two years. The Director of Strategy and Regulation and the Chief Customer Officer, both Directors of Bristol Water, attended Challenge Panel meetings and provided a tangible link with the Board. The hiatus in independent Board-level involvement with the Challenge Panel may not necessarily have changed the outcome of the business plan submitted, however it does impact on the Board's ability to observe the quality of discussion, debate and challenge carried out by the Challenge Panel on behalf of the customer. Since this matter was raised by the Chair of the Bristol Water Challenge Panel during a recent Board meeting, a number of Board Independent Non-Executive Directors and shareholder Directors have attended subgroup and

Challenge Panel meetings. The Challenge Panel is pleased with this improvement in corporate governance.

In developing its long-term strategy and business plan 2020-2025, Bristol Water has stressed that its aims are to provide greater transparency, increase levels of trust from its customers and improve confidence in services provided by the company. The Challenge Panel has evidence that the company has increased the level and quality of communication with its customers on a range of topics, from supply interruptions to environmental and educational messages. Use by the company of social media has increased exponentially and has provided a useful platform for communications of all types. From a standing start, Bristol Water has in excess of 3,600 followers on Twitter and 2,600 followers on Facebook. The local BBC and ITV television stations and other broadcast media cover incidents and provide updates and information presented by the Chief Customer Officer.

Bristol Water has established new performance commitments that are in line with customer expectations and that address customer priorities. In line with its history of being a local privately-owned water company that provides services for all the residents in its area, performance commitments by Bristol Water, such as its satisfaction with its local community investments, underline this local, community-focus.

Bristol Water has adopted the methodology set out by Ofwat in setting incentives in most cases. The Challenge Panel has questioned the cases where the methodology is not followed and it understands and accepts the reasons put forward by Bristol Water.

The Challenge Panel notes that Bristol Water has committed to upper quartile performance in many areas, especially where customers have expressed a preference in the setting of this aim. Targets such as supply interruptions and leakage are particularly stretching and will be monitored closely by the Challenge Panel.

The Challenge Panel, however, brings to the attention of customers, Ofwat and the Bristol Water Board that there is a lack of consensus on two performance commitments. These are the level of ambition regarding the Biodiversity Index and the imposition of a deadband on waste disposal compliance. A programme of work is planned by the Company to ensure that performance commitments in PR24 linked to biodiversity protection and enhancement are fully informed by a thorough assessment of what is feasible alongside the limitations of operational constraints.

The Challenge Panel notes with concern the on-going arbitration with the Canals & Rivers Trust regarding its £10m demand for the abstraction of water from the Sharpness Canal and the potential impact on customer bills when this matter is resolved.

On balance the Challenge Panel supports the business plan set out by Bristol Water. Customers are likely to welcome both the reduction of water bills across the period and the bill profile set out in the business plan. The service commitments align with Bristol Water's strategic objectives at a cost that is affordable. Customers can be assured that their bills will become increasingly affordable and that customers in vulnerable circumstances have extensive and ambitious levels of support targeted to them.

The Challenge Panel is clear about the areas where the Challenge Panel it will need to monitor the performance of Bristol Water against its targets, particularly those that are particularly innovative, through our on-going performance assurance role. The Panel has also asked that in 2020 the Bristol Water Board sets out a clear corporate responsibility statement and policy that enshrines the company and its shareholders responsible attitude towards, for example the communities where they operate, how their investment strategy affects customers and their policy on shareholder dividends and the performance related element of executive pay.

In summary, the Challenge Panel considers the evidence that the Bristol Water Business Plan 2020-2025 is grounded in a sound, extensive customer engagement strategy and research; the views,

priorities, preferences and valuations of customers are reflected throughout. Performance commitments meet the regulatory and statutory requirements set out by Ofwat and other regulators and the incentives reflect what customers value and prefer.

1. Introduction

The Bristol Water Challenge Panel (the 'Challenge Panel') is the independent Customer Challenge Group for Bristol Water. The Challenge Panel's role is to monitor, scrutinise, challenge and report on Bristol Water's performance against the commitments set out in the final report of the Competition and Markets Authority dated 6th October 2015 and the Ofwat Price Review 2014 (PR14) Final Determination of December 2014. The Challenge Panel reports to Ofwat and to Bristol Water's Board.

The Challenge Panel is also required to review and challenge Bristol Water on its customer engagement policies and procedures and to examine how customer preferences and priorities have driven decision making and business planning for Ofwat's current price review for the period 2020-25, and the company's longer-term strategy.

The Challenge Panel has adhered to the duties and responsibilities set out by Ofwat in its "Customer engagement policy statement and expectations for PR19" published in May 2016, its publication "Delivering Water 2020: Our final methodology for the 2019 price review" from December 2017 and the Ofwat "Aide Memoire for Customer Challenge Groups" from March 2018.

The Bristol Water Director of Strategy & Regulation, Chief Customer Officer, and Head of Customer Service attended Challenge Panel agenda conferences, meetings and sub-group meetings, keeping the Panel informed of their progress with the customer engagement framework and seeking the Panel's views at an early stage in the business planning process. Specialists such as the Head of Water Resource & Environment, Regulatory Policy Advisor, Head of Economic Regulation, among others supported the Challenge Panel in probing deeply on behalf of the customer the range of strategies, policies and reports in development.

This report provides Ofwat, the Bristol Water's Board and customers with the Challenge Panel's opinion on the Bristol Water's Price Review 2019 (PR19) business plan, in particular:

- The extent and quality of the customer engagement undertaken by Bristol Water in developing its business plan and the extent to which customer and stakeholder engagement is embedded in its business.
- How Bristol Water has established customers' needs and priorities, including those in circumstances that make them vulnerable, and their willingness to pay for them.
- How the results of its engagement have driven Bristol Water's business planning decisions and are reflected in its business plan.
- How customers are driving change and improvement in service and how Bristol Water is performing in terms of innovation and sustainability.
- Customers' views on the acceptability and affordability of Bristol Water's business plan.

A glossary of terms used in this report is provided in Appendix 1.

The Environment Agency (EA), as a member of the Panel, supports the views expressed in this report. However, these views will not necessarily influence any subsequent position the EA takes as part of its ongoing statutory and regulatory duties associated with Bristol Water's environmental obligations.

2. Panel's Membership and Governance

2.1 Membership and Skills

2.1.1 Members

The Challenge Panel was established in November 2015 and is composed of an independent chair, deputy chair and report writer, together with the environmental regulators, wider stakeholders and individuals drawn from several backgrounds, as shown in the diagram below.

The Challenge Panel's Terms of Reference is given in Appendix 2.

Since its establishment, the membership of the Challenge Panel has changed in small part in response to members having to resign due to other work commitments or in response to the evolution of the Ofwat PR19 methodology requiring the Panel to have additional skill sets. The Challenge Panel has been fortunate to be able to replace members who have had to resign with others with similar skill sets. This has proved invaluable in ensuring continuity of focus throughout the process.

A full listing of the Challenge Panel members who have reviewed and challenged the preparation and content of Bristol Water's business plan is given in Appendix 3.

The Drinking Water Inspectorate (DWI) attended one meeting at the Challenge Panel's request and provided an overview of its expectations on Bristol Water's drinking water quality proposals for PR19. Its statement on these proposals is given in Appendix 4.

The Challenge Panel has met 14 times since its formation in November 2015. A list of the Challenge Panel's meetings and the topics discussed at each is provided in Appendix 5.

2.1.2 Skills Audit

A full audit of the skills of all Challenge Panel members was undertaken in 2016/17 and was reported in the Challenge Panel's Annual Report for that period. There was no requirement to repeat the Skills Audit as new members were recruited to have the same skills set as the members they replaced.

2.2 Sub-Groups

The Challenge Panel established sub-groups to assist it with its review and challenge of the detail of Bristol Water's business planning process and the resulting plan. These sub-groups were:

- A Customer Engagement Sub-Group (CESG) to review and challenge the customer engagement activities, results and Bristol Water's use of these. The CESG also reviewed Bristol Water's affordability and vulnerability plans. The CESG met 12 times between January 2017 and July 2018.
- A Performance Commitment and Outcome Delivery Incentive Sub-Group to review and challenge Bristol Water's Performance Commitments (PCs), service targets and Outcome Delivery Incentives (ODIs) and how these linked to customers' needs and priorities. This sub-group met three times between January and June 2018
- An Assurance Sub-Group to review and monitor Bristol Water's PR19 assurance regime. This sub-group met three times between November 2016 and June 2018
- An Environment Sub-Group (part of Bristol Water's regular environment tripartite meetings with EA and Natural England (NE)). This sub-group met five times between December 2016 and June 2018.

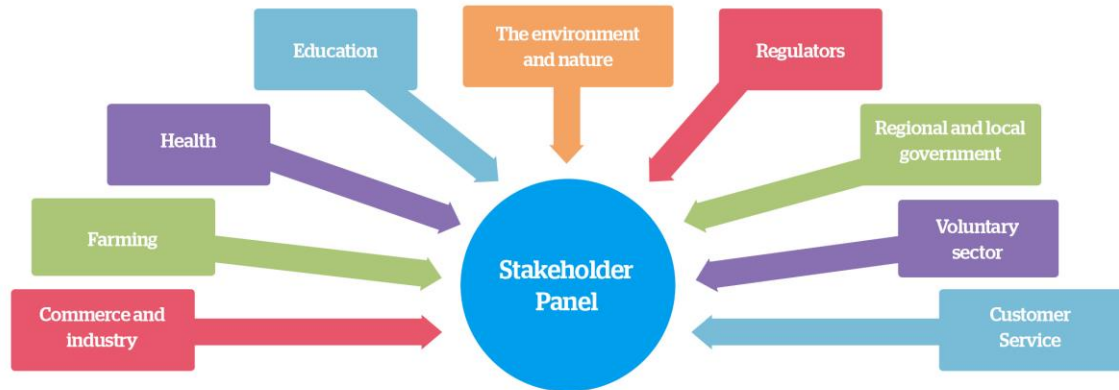
A list of the sub-group meetings and the topics discussed at each is provided in Appendix 5.

2.3 Governance

The Challenge Panel's role, membership, governance, terms of reference, minutes of its meetings and its annual reports can be found at: www.bristolwater.co.uk/challengepanel

Results and impact of our work with the Bristol Water Challenge Panel

The Bristol Water Challenge Panel represents...



Their work with us includes...

✓ 635 challenges	✓ 37 meetings	✓ 25% of challenges had an impact on the business
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On a variety of topics...

Vulnerability Engagement Framework Drought Plan
Triangulation **Information Assurance**
Research Results Affordability Resilience
PR19 Methodology Water Resources Environment Strategy BW Performance Tariffs
Customer Engagement

The Challenge Panel is independent of Bristol Water and reports to Ofwat and the Bristol Water Board.

The Chair and Deputy Chair are each paid a stipend by Bristol Water. The Report Writer is paid by Bristol Water for his time and expenses. Certain members are paid by their respective organisations to contribute to the Challenge Panel's work. Council representatives have their time authorised which counts towards their set hours as councillors. Charity representatives on the Challenge Panel receive a fixed payment from Bristol Water for attending meetings. The independent members provide their time voluntarily, but can claim their expenses from Bristol Water.

The Chair of the Challenge Panel attended selected meetings of the Board as part of the PR19 process.

She also attended meetings with Ofwat and the Chairs of other companies' CCGs. She reported to the Challenge Panel members the topics discussed at these meetings and the outcomes.

Bristol Water has fully understood and accommodated the role and objectives of the Challenge Panel.

The Bristol Water Director of Strategy & Regulation, Chief Customer Officer, and Head of Customer Service attended Challenge Panel agenda conferences, meetings and sub-group meetings, keeping the Panel informed of their progress with the customer engagement framework and seeking the Panel's views at an early stage in the business planning process. Specialists such as the Head of Water Resource & Environment, Regulatory Policy Advisor, Head of Economic Regulation, among others supported the Challenge Panel in probing deeply on behalf of the customer the range of strategies, policies and reports in development.

Throughout the process the Challenge Panel has been able to work constructively and collaboratively with Bristol Water in order to achieve its objectives. The Challenge Panel's information requests and challenges have been addressed in full and in a timely manner by Bristol Water.

Meeting processes and protocols were agreed with Bristol Water. These included private in-camera sessions at the start and end of each meeting to enable Challenge Panel members to discuss issues without Bristol Water being present.

Bristol Water provided meeting venues, issued agreed agendas and produced presentational material. Notes and minutes of the all the meetings of the Challenge Panel and its sub-groups were produced by the Report Writer. The minutes of the main Challenge Panel meetings are published on the website given above.

The Chair, Deputy Chair and Report Writer agreed the agendas of each Challenge Panel and sub-group meeting in advance with Bristol Water in advance. Typically, the meetings consisted of presentations given by Bristol Water (or its consultants) on the customer engagement and future performance commitments and incentives associated with the business plan. Bristol Water's planning methodologies and assumptions and its interpretation of Ofwat's PR19 methodology were also presented.

The Challenge Panel and its sub-groups have had the opportunity to challenge Bristol Water robustly on its business plan in the meetings and through email correspondence.

Challenge Panel members have not attended operational meetings held between the company and its economic, water quality or environmental regulators. However, as mentioned above, members of the Challenge Panel's Environment Sub-Group attended the meetings of Bristol Water's Environment Tripartite Group (which also included EA and NE) at which PR19 related environmental issues, the Water Resources Management Plan (WRMP) and current environmental performance were discussed.

The Challenge Panel relied on its representatives from the EA and NE to confirm the requirements of the statutory environmental elements of the Bristol Water's business plan.

The Drinking Water Inspectorate (DWI) attended one meeting at the Challenge Panel's request and provided an overview of its expectations on Bristol Water's drinking water quality proposals for PR19. Its statement on these proposals is given in Appendix 4. The Challenge Panel's comment on these expectations is given in Section 11.5 of this report.

The Challenge Panel challenged both DWI and EA on their views and decisions and required both regulators to confirm the statutory justification for their requirements and expectations of Bristol Water and its business plan.

All meetings of the Challenge Panel and its sub-groups were attended by executive directors and senior managers of Bristol Water.

Whilst the Chair of the Challenge Panel attended a number of meetings of the Bristol Water Board to inform it of the Panel's work and its findings, she considered part way through the process that the Board's engagement with the Challenge Panel should be extended to increase its ability to observe the quality of discussion, debate and challenge carried out by the Challenge Panel on behalf of the customer. The Board responded positively to these challenges and Bristol Water's CEO and Board directors from its major shareholder attended the Challenge Panel's meetings during the period when the draft and final business plans were being presented and discussed. The Challenge Panel welcomed this response and were satisfied with it.

The Challenge Panel wishes to thank Bristol Water for its assistance in organising and facilitating its meetings, in fulfilling its requests for information and in responding both openly and effectively to its challenges.

The Challenge Panel considers it has been given adequate opportunity to scrutinise and challenge Bristol Water's policies and plans as presented to it and it considers the process to have been very open, transparent and constructive.

3. The Review and Challenge Process

Ofwat’s methodology for PR19 for the water and wastewater monopoly service providers in England and Wales was published in December 2017 in its document “Delivering Water 2020: Our final methodology for the 2019 price review”. The methodology sets out Ofwat’s expectations and requirements for companies preparing their business plans to meet the needs of their customers from 2020 to 2025 and beyond. It also describes how these expectations form the basis for the tests Ofwat will use to assess companies’ business plans (its initial assessment of business plans (IAP)). Prior to this, Ofwat’s customer engagement expectations had been set out in its “Customer engagement policy statement and expectations for PR19” published in May 2016.

Ofwat’s methodology states that Customer Challenge Groups (CCGs) will provide independent assurance to Ofwat on the quality of a company’s engagement with its customers to develop its business plan.

Ofwat’s detailed expectations on CCGs at PR19 are set out in its publication “Aide Memoire for Customer Challenge Groups” of March 2018. This document can be found at:

<https://www.ofwat.gov.uk/publication/aide-memoire-customer-challenge-groups/>

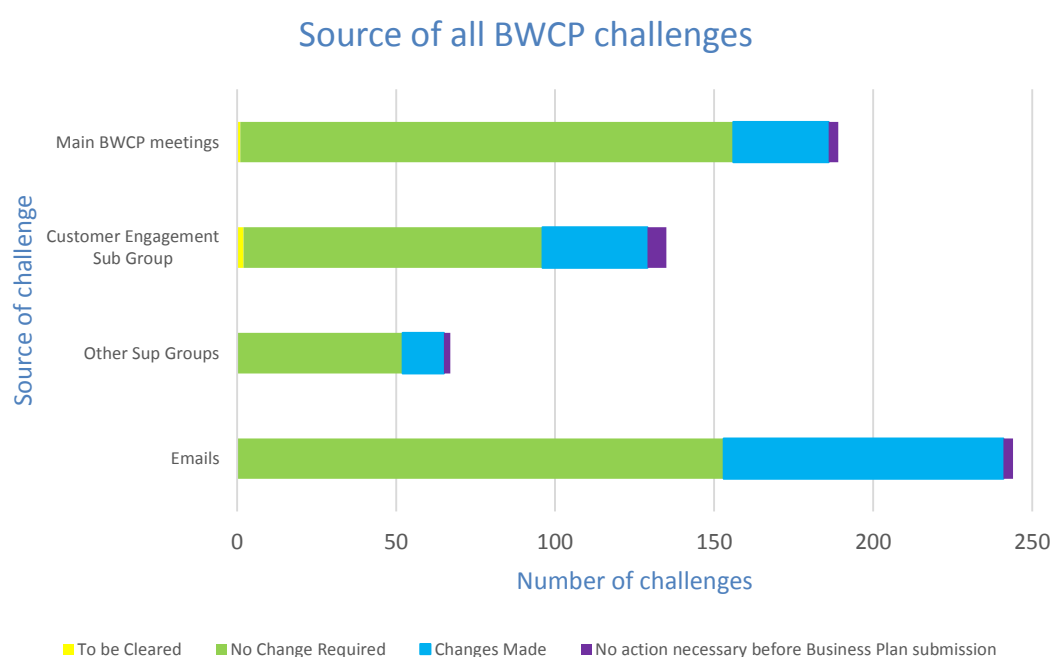
The relationship between Ofwat’s IAP tests and its Aide Memoire requirements on CCGs is shown in Appendix 6.

The Challenge Panel has followed Ofwat’s guidance and has addressed the specific questions Ofwat has asked CCGs to address. Appendix 7 provides a guide to where Ofwat’s Aide Memoire questions have been addressed by the Challenge Panel in this report.

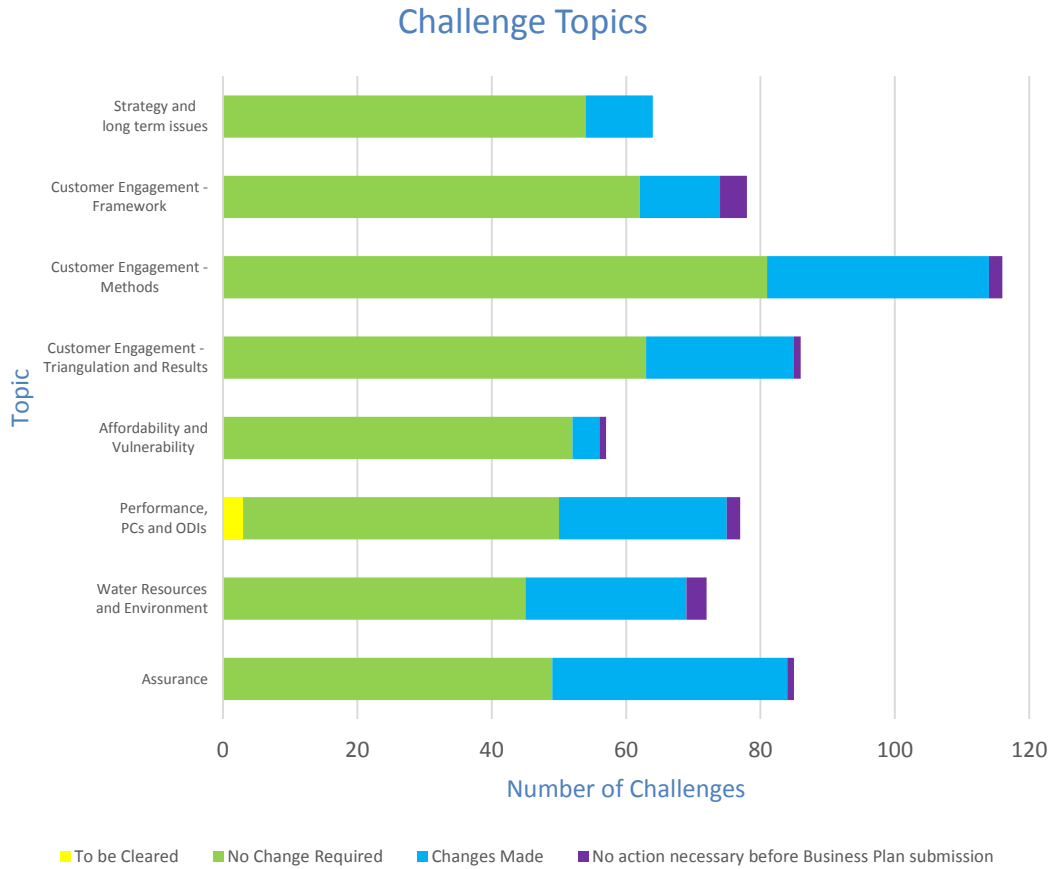
In order to provide evidence of its independent challenge of the business plan, the Challenge Panel maintained a comprehensive Challenge Log through the process. 635 challenges were logged in total.

For information on how to inspect the Challenge Log, please see the Challenge Panel’s webpage at www.bristolwater.co.uk/challengepanel. An example extract from the Challenge Log is provided in Appendix 8.

Challenges arose mainly from the meetings of the Challenge Panel and its sub-groups but a significant number were also raised via email. The sources of the challenges were as follows:

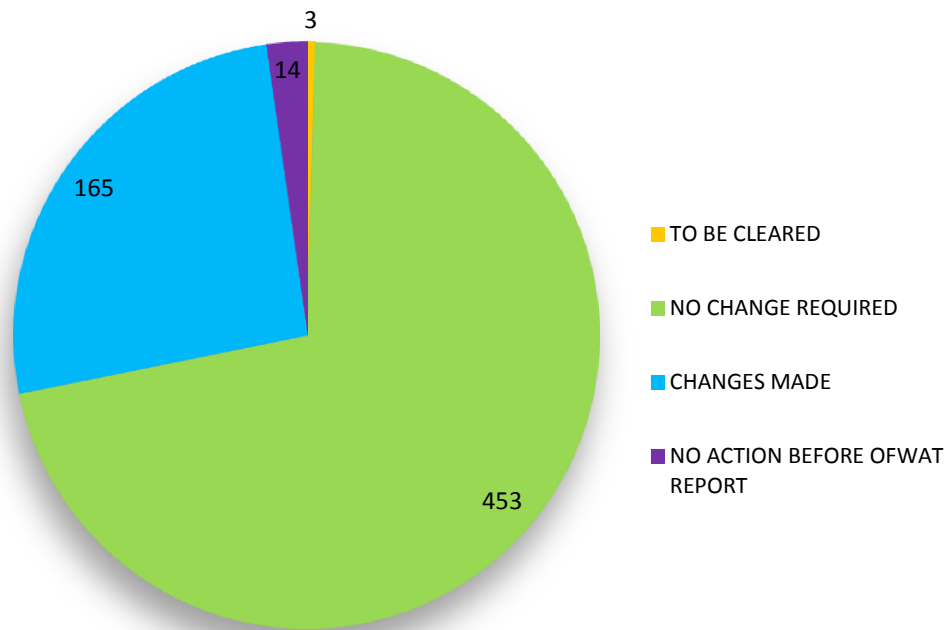


The challenges covered all aspects of the Challenge Panel’s areas of focus (as set out in Ofwat’s Aide Memoire and relating to customers’ priorities) as follows:



Considerable work was undertaken by the Deputy Chair, Report Writer and Bristol Water staff to review documentation to ensure that the challenges were addressed and so cleared, either with changes made or agreeing that no changes were required. This work continued up to the submission of this report.

The following chart illustrates the status of the challenges at the end of the process.



The Challenge Panel is pleased to report that all the challenges relevant to process up to submission of the business plan to Ofwat have been addressed by Bristol Water. Around 25% of the Challenge Panel's challenges resulted in a change to Bristol Water's plans, business planning and engagement processes or outcomes. The Challenge Panel regards this as strong evidence of the influence it has had on Bristol Water's business plan. There are three challenges that weren't resolved. These relate to points of detail on three PCs and are described in Sections 8.5, 8.6 and 9.2 of this report.

4. Assurance

Bristol Water's assurance regime for its PR19 business plan submission to Ofwat consisted of:

- An assurance framework
- Internal checking and governance
- Third party assurance
- Board assurance statements

The Challenge Panel placed great importance on, and took a close interest in, the design, effectiveness and output of the assurance regime. This gave the Panel confidence in the business planning methodologies employed (including customer engagement), the results obtained the use of the results in developing the business plan. It also provided strong evidence of Bristol Water Board's involvement in the development of the business plan and its ownership and endorsement of it.

A particular challenge from the Challenge Panel early in the process was what appeared to be a lack of independent assurance to the business plan and that Bristol Water was relying on the Challenge Panel to provide this assurance. The Challenge Panel sought reassurance of the PR19 assurance regime in detail and the role of Bristol Water's PR19 assurance partner in this. It also wanted reassurance that Bristol Water was on track to meet each of the nine business plan assessment areas identified by Ofwat in its PR19 methodology.

The Challenge Panel was also mindful of Ofwat's Company Monitoring Framework assessment of Bristol Water's information reporting and governance regime as 'Prescribed', ie the category that warrants the closest scrutiny from Ofwat. The Challenge Panel is aware that Ofwat's concerns arose primarily from Bristol Water's PR14 submissions, and its subsequent Appeal to the Competition and Markets Authority (CMA).

The Challenge Panel requested and received presentations on the PR19 assurance regime and its findings at various stages throughout the process. It particularly wished to obtain ongoing comfort that the independent assurance regime was being followed and was being effective. The Challenge Panel relied heavily on this expert opinion to be able to accept at face value much of the customer engagement and business plan information provided to it.

Bristol Water informed the Challenge Panel that it received third party assurance on the following aspects of its business plan (areas that were relevant to the Panel's work):

- Customer engagement
- Cost adjustment claims
- Investment planning

In addition, Bristol Water used specialist consultants to help it with:

- Customer engagement
- Willingness to pay (including triangulation)
- Cost benefit analysis
- Incentive rate calculations

Whilst the Challenge Panel accepts that the use of specialists to assist with activities cannot assure their quality, it takes some comfort from knowing that this expertise has been employed.

As well as providing updates on the findings of the assurance regime (as presented to its Board), Bristol Water provided the opportunity for the Challenge Panel to review the findings of its external assurers' reviews.

Based upon the evidence provided to it, the Challenge Panel considers Bristol Water's PR19 assurance regime to have been robust and effective.

5. Customer Engagement

5.1 Review by the Challenge Panel

Throughout its review and challenge of Bristol Water's customer engagement, the Challenge Panel has been fully aware of Ofwat's expectations on it to provide an independent view on the quality of the engagement and the way that the results have driven Bristol Water's decision making and are reflected in their business plan, thus effectively placing the customer at the centre of the process.

In order to do this effectively, the Challenge Panel established a Customer Engagement Sub-Group in January 2017 to review in detail Bristol Water's engagement processes, the results obtained and their use in the development of the business plan. The Customer Engagement Sub-Group's review and challenge also included Bristol Water's customer engagement on its draft Drought Plan and draft Water Resources Management Plan.

The Customer Engagement Sub-Group has met twelve times and has reported its findings to the Challenge Panel throughout the process. Bristol Water and its customer research consultants responded positively to all challenges relating to customer engagement posed by the Challenge Panel and the Customer Engagement Sub-Group. In many cases the challenges resulted in changes to proposed research methodologies and materials. The Challenge Panel welcomed this constructive relationship.

To provide an overview of the process, members of the Challenge Panel were given the opportunity to review and comment on the Strategic Policy Framework that Bristol Water intended to use in driving its customer engagement and in recruiting partners (the Customer Engagement Framework). The Challenge Panel questioned and challenged the processes and research intentions being put in place. This provided the Challenge Panel and Bristol Water with a shared understanding of the engagement task. It has also provided the framework for monitoring the progress of engagement via the company's Quarterly Progress Reports which were presented and discussed at the meetings of the Customer Engagement Sub Group. This gave the Challenge Panel the opportunity to challenge and suggest changes to the detail of the customer engagement plan as it progressed. The quarterly reports also ensured the Challenge Panel was able to indicate which upcoming parts of the engagement they wished to consider in more depth before their use with customers.

The Challenge Panel members have received all relevant documents and have been able to attend meetings of the Customer Engagement Sub-Group depending upon their interest in the agenda topics.

Bristol Water provided the opportunity for Panel members to attend key customer engagement events over the last eighteen months. Members have attended a number of deliberative workshops, focus groups and meetings of the Bristol Water Customer Forum.

The Challenge Panel would like to thank Bristol Water for the time they took to ensure it had the opportunity to discuss and challenge the Customer Engagement programme and on the way Bristol Water took into consideration the Challenge Panel's comments both before and during the research.

5.2 Overview of Customer Engagement

5.2.1 Research Techniques

Bristol Water's Customer Engagement Framework has made use of a wide range of qualitative and quantitative research tools, using a mix of tried and tested methods and more innovative approaches particularly in assessing willingness to pay. Bristol Water used specialist consultants to assist with the design and implementation of the majority of its engagement activities.

The research activities have included:

- Customer segmentation
- Online scenario game
- Customer affordability assessment
- Stated preference research - Part 1

- Review of customer experience by attribute
- Benefits transfer review
- Macroeconomic analysis and qualitative study of resilience costs
- Customer dashboard
- Customer Panel
- Customer Forum group
- Youth Board
- Stakeholder engagement
- Deliberative scenario workshops with quantitative valuation
- Stated preference research - Part 2
- Staff roadshow
- Staff online panel
- Drought Plan consultation
- ODI research
- Revealed preference research
- Customers in vulnerable circumstances research
- Company financing and bill impact research
- Long term strategy engagement
- A co-creation event involving other utilities, community groups and service providers to align strategies and identify areas for future joint working
- Affordability assessment
- Special Cost Factor/Small Company Premium research
- Deliberative testing before draft plan
- Focus groups with vulnerable customers
- WRMP deliberative events
- Draft business Plan acceptability testing
- Final business Plan acceptability testing

The key research techniques used were:

Deliberative workshops: these comprised random groups of typically around 30 customers spending time learning about a particular element of the Bristol Water business and discussing it together. This approach is used to understand customer views on complex issues like how Bristol Water meet water supply needs in the long term.

Focus groups and interviews: these were often smaller groups of customers or individuals to understand their views on a very specific topic, or to hear from a particular group of customers like those who are struggling with their bills.

Surveys: a wide range of surveys were undertaken to ask large numbers of customers what they think, for example the customer panel where up to 1,000 customers let Bristol Water know their views.

Economic valuation tools: Bristol Water used six diverse types of valuation tools to determine customer attitudes to the value placed on Bristol Water's service which were used in setting Bristol Water's bill options. Bristol Water have been innovative in using new techniques like revealed preference surveys that investigate the actual costs customers face when supply is interrupted and integrated valuation studies into the deliberative workshops.

Customer forum: this comprises a forum of about 40 informed customers that meets four a times a year to feed in to Bristol Water's business planning.

Bristol Water's Customer Engagement Framework was based on strategic outcomes defined from previous research and the objective of researching customers' needs and priorities on these and other issues in order to develop the business plan. The Customer Engagement Framework was adapted during the process as a result of clarification and changes in regulatory requirements, challenges from the Challenge Panel and the need to explore certain issues in more detail. The Challenge Panel considers that the research activities undertaken were appropriate and remained

focused on the overall objective of informing the business plan and the need to adapt and extend the original Engagement Framework was essential to improve the outcome.

The Challenge Panel noted that feedback from the early research activities showed that participants wanted to know why they were being consulted and that their responses and recommendations were more robust and meaningful once they became better informed. The Challenge Panel was very keen to ensure customers were provided with sufficient, appropriate and clear information on Bristol Water's current and historic performance to help them engage fully and effectively in the research. From the opportunities it had to review and influence research material in advance and from the events it attended, the Challenge Panel is satisfied that this was the case. A particular example related to the deliberative research on environmental issues, where the Challenge Panel had significant input into helping Bristol Water with the design of information boards.

Challenge Panel members attended a number of research events which enabled it to confirm that the engagement process was two-way and transparent. Participants were given sufficient and objective information on the company's comparative performance relative to its peers and on its plans and options on these performance measures where appropriate. It also observed that participants were encouraged to provide their own thoughts as well as their answers to specific questions.

Overall the Challenge Panel has been impressed with the wide range of customer engagement methods adopted by Bristol Water and the rigour with which they were used and the results analysed. The methods used, both traditional and innovative, have enabled Bristol Water to engage with a wide range of customers in order to understand the needs and requirements of different groups including age, gender, ethnicity, household size, wealth and location (urban or rural).

Case Study – Environmental Research

In early 2017 the Challenge Panel noted that an environmental dimension was missing from the preliminary PR19 customer priority list. Bristol Water acknowledged that the environment may need more attention in the forthcoming research.

A discussion then ensued on how best to include the various aspects of the environment into research. This resulted in Bristol Water producing a report 'Customer Engagement on the Environment' which became part of its engagement strategy.

After further discussion the Challenge Panel considered the paper contained gaps in Bristol Water's strategy, for example its ambitions around biodiversity and habitats and linkage of these with the results of its customer engagement. As a result a meeting was setup between the environmental regulators from the Challenge Panel and Bristol Water responsible officers during the Challenge Panel's 2018 Away Day at Purton Treatment Works.

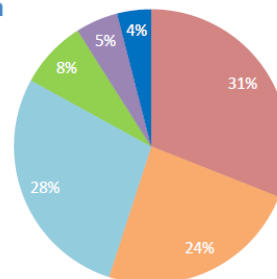
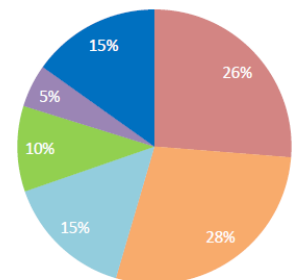
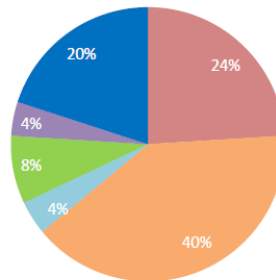
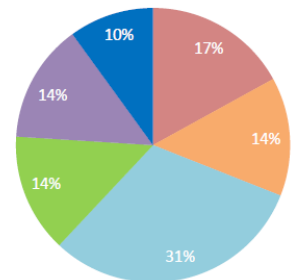
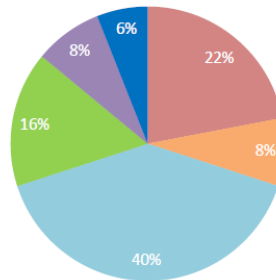
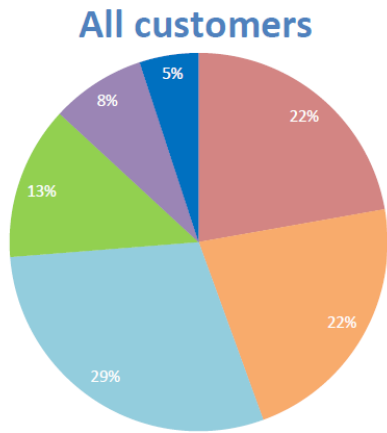
The re-issued 'Customer Engagement on the Environment' outlined Bristol Water's environmental objectives and targets as well as including a plan of the customer research to achieve the objectives. Bristol Water undertook to continue to report to the Challenge Panel on how they are exploring environmental issues with customers and revisit the research questions regularly to ensure they reflect the latest thinking of the Bristol Water team, the Challenge Panel and their customers. This document was also updated as the research progressed.

5.2.2 Customer Segmentation

As part of the Customer Engagement Framework, Bristol Water conducted a segmentation exercise, using their customer data to better understand who their customers are and their individual needs. This took some time to complete and involved the Challenge Panel at various stages.

The segmentation exercise took longer than originally expected as Bristol Water wished to move away from the conventional methods and provide something that more closely matched its customer base. Customer segmentation runs right through the whole of the research programme as it is the mechanism by which a single piece of research can be matched to the wider Bristol Water customer base and thus become relevant to ongoing work.

Understanding our customers



- Young Urban Renters
- Mature and Measured
- Comfortable Families
- Social Renters
- Thirsty Empty Nesters
- Safely Affluent

A list of some 60 possible variables was presented to the Challenge Panel who queried several apparently missing variables stretching from race through ethnicity and religion to health issues and pension credit.

The results were used to align the results of research to the Bristol Water customer base, the intention being that these customer personas provide a framework within which all future research can explore the variation in views among different customers.



Safely Affluent 5%

The average age of this group of customers is 58. They have an average income of £71,000 and very few are in debt or struggling. 98% own their own home and most live in a detached house. Nearly half have children at home. Only 36% use a water meter but most are interested in saving water.

Thirsty Empty Nesters 8%

The average age of this group of customers is 63. They have an average income of £36,000 and over half are struggling or in debt. The majority live in their own home – mostly in semidetached or terraced houses. This group pays the most for their water –



but most do not have children at home and live by themselves or with one other person. Only 6% have a water meter.



Mature & Measured 23%

This group of customers has an average age of 73 and an average income of £39,000. Only 33% are employed, but only a few are running into debt. Most of these customers own their own homes and live with only one other person. All are interested in making efforts to cut down their water usage and most are on a water meter.

Young Urban Renters 22%

This group of customers has an average age of 36, and an average income of £38,000. Most of them are employed, and a small majority rent the property they live in. Most are only just managing to make ends meet and could be running into debt. A small majority have a water meter, this group demonstrates the least interest in cutting down their water usage.



Social Renters 13%

This group of customers has an average age of 59 and an average income of £19,000. Most are in debt or struggling, and only 33% are employed. Most of this group are in social housing, and the majority live alone or with one other person.

Comfortable Families 29%

This group of customers are middle aged, with an average age of 46. Most have children at home – with three or more people living in the property. This segment are fairly affluent, with an average income of £51k, but with discretionary incomes that are only slightly higher than average due to larger families. This is reflected in the fact that just over half do not hold any savings despite their high incomes. They have larger than average water bills which correlate with their household sizes and the percentage that have children at home.



The numbers of customers consulted for PR19 was high (around 37,000), significantly more than the 3,000 consulted for PR14.

As a result of its challenges, the Panel is satisfied that the research was representative of Bristol Water's customer base and that the engagement was robust, balanced and proportionate.

Vulnerable, Hard to Reach and Seldom Heard Customers

As well as using information from its ongoing customer engagement, Bristol Water undertook specific and bespoke pieces of research to understand the situations and needs of customers in vulnerable circumstances and customers who are hard to reach and seldom heard, for example rural customers.

This research was strongly encouraged and welcomed by the Challenge Panel. It paid particular attention to the segmentation and geographical location of the participants used in the research and whether it included the genuinely hard to reach. It was pleased to see it included customers who are experiencing financial worries, have negative attitudes towards organisations or mental health issues.

The Challenge Panel was impressed with Bristol Water's efforts in these research areas. It considers that the engagement was effective in informing its affordability and vulnerability strategies and the Challenge Panel was very pleased to have contributed to them. The strategies are described in more detail in sections 6 and 7 of this report, together with the Challenge Panel's opinion on them.

Business Retailers

Bristol Water has undertaken some limited PR19-specific engagement with business retailers as it relies primarily upon market mechanisms to obtain feedback from this group.

The Challenge Panel requested information from Bristol Water on the scope of this feedback and the outcomes. It established that there are regular face to face meetings with retailers covering Bristol Water’s performance, new initiatives, feedback from operational incidents, discussions around water resource, drought plans, industry consultations, water efficiency and more recently its PR19 plans.

Bristol Water also obtains feedback from surveying retailers on a quarterly basis and the most recent survey covered its draft business plan, specifically whether the plan would help Bristol Water serve its retailers. While the responses were generally positive, they were limited. Bristol Water told the Challenge Panel that the engagement with business retailers on the business plan had not been easy as retailers had been asked by every company for comment. However the business retailers that did participate said that they believed Bristol Water to be performing above other retailers.

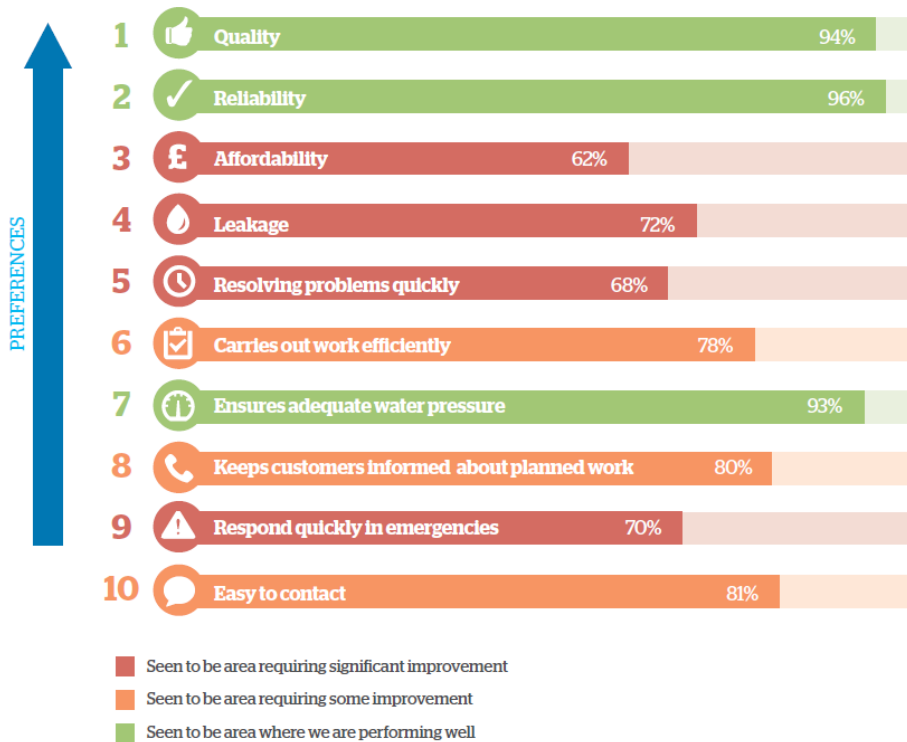
Future Customers

The Challenge Panel has seen that Bristol Water-engaged with future customers through the use of its Youth Board, its Customer Summits and a focus group testing the acceptability of the final business plan.

The Youth Board was established in January 2018 as part of the PR19 Customer Engagement Framework. It comprises 19 A-Level students from across Bristol Water’s supply area. The Youth Board has focused on primarily on water efficiency and related behavioural change and also their preferences for the draft business plan. The Youth Board suggested ideas for promoting greater water efficiency, including greater use of mobile and digital technology, which Bristol says it will explore further. Bristol Water intends to continue the Youth Board for the foreseeable future, meeting annually.

The Bristol Water Customer Summit also included a small number of younger customers.

5.3 Customer Preferences and Willingness to Pay



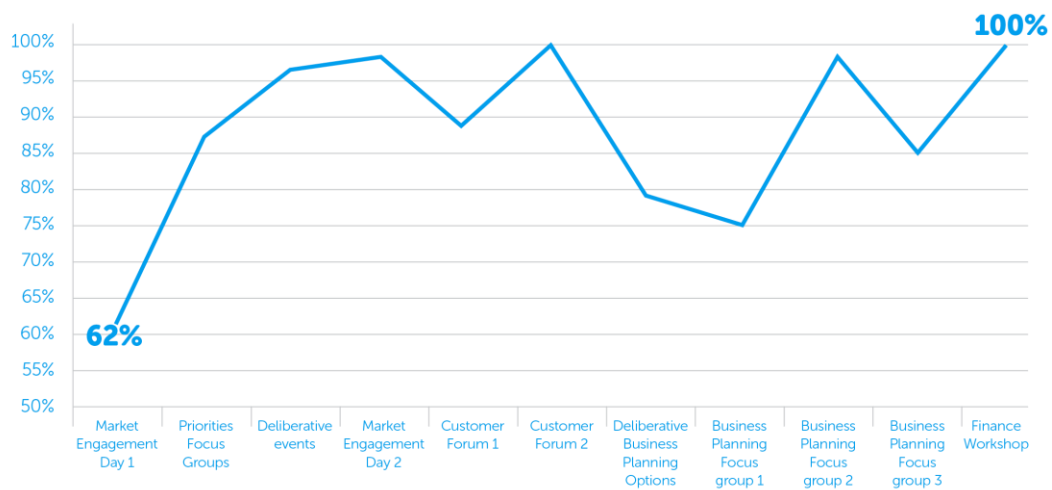
Bristol Water undertook a range of research on customer priorities available both from the last price review, and from ongoing customer research. Bristol Water refreshed its understanding of customer priorities by conducting three research events with different customer groups, designed to better understand some of the reasons behind the priorities customers choose and to understand the views of different customer groups. This has been supplemented by the annual survey.

The research showed that the top priorities of Bristol Water’s customers have remained largely unchanged over the years, with reliability, water quality, and affordability consistently prominent across most of the research. Most customers considered Bristol Water is doing well across the range of priorities, but some areas still have room for improvement.

When implementing the Framework, the Challenge Panel needed to ensure that when customers discussed their priorities, preferences and responsibilities regarding the level of service they wanted from Bristol Water they:

- Knew enough about the water they drink, clean with and use every day;
- Could ask about the things they lacked knowledge on; and
- Could identify areas where they could take on responsibilities.

“I understand how the output from the event will be used by Bristol Water”



After every workshop, focus group or interview, Bristol Water carried out a set of evaluations to gauge customer views. Bristol Water needed to ensure the customer insights were fed into the business plan, however, the lowest evaluation score was for ‘knowing how the output from the event will be used by Bristol Water’. An evaluation approach that tracks the influence of the customer research more systematically was implemented as well as more information being provided to customers; resulting in a very positive improvement in evaluation scores as shown on the chart.

During the process the Challenge Panel became concerned about the way environmental protection and enhancement were being treated in the research. After some work with the Challenge Panel Bristol Water developed its understanding of and research into environmental issues. This resulted in Bristol Water treating these attributes with the same rigour as other attributes of their customer service.

The Customer Engagement Sub Group quarterly review meeting made clear that Bristol Water were supporting the PR19 internal working groups to ensure that decision makers were making the most of the research outputs. This resulted in the development of an evaluation before and after the use of the research. As well as embedding customer research into the organisation it produced a shared understanding that engaging customers on certain topics is difficult and takes time and that customer engagement is needed earlier in the process. In this way the use of customer views and priorities was becoming enshrined throughout the company right from the PR19 Executive meetings downwards.

The Challenge Panel welcomed the addition of research on the financing of the company into the Framework programme. As well as being enjoyable for the attendees it had provided an interesting insight into customer's views on company debt and profit.

Bristol Water derived customer valuations for various service outcomes and commitments and has used these to inform service targets and incentives. Valuations for most performance commitments were obtained but some have been derived from research at service outcome level.

One of the highlights of the Customer Engagement Framework was identifying and challenging the innovation that Bristol Water had built into the programme. One of the first major innovations was the use of 'Max Diff' methodology within the Willingness to Pay (WTP) work; this was rightly praised by the reviewer during the independent Peer Review.

The Challenge Panel was initially concerned with the identification of some methodological limitations in the WTP stage 1 research which was carried out jointly with Wessex Water. The Challenge Panel was assured by the peer-reviewer that the limitation only applied to the Wessex Water results, not Bristol Water's.

A methodology to triangulate its various sources of valuation (WTP) information for each service area consulted on was developed by Bristol Water. This was based upon a combination of systematic judgement and cost benefit analysis. Bristol Water presented the triangulation methodology to the Challenge Panel who welcomed this and found it to be very informative. The Challenge Panel could immediately see the advantages of the method in bringing together diverse research results to provide a range of attribute values for Bristol Water to use in its cost benefit analysis and the allocation of future incentive targets and rates.

The Challenge Panel was particularly interested in the triangulation methodology as it was innovative and formed a key component of the target setting process and it highlighted the strengths and weaknesses of each valuation approach. The key challenges included:

- The geographical segmentation of the valuation results, eg by urban or rural respondents.
- The understanding of which valuation and triangulation methods have been applied to each attribute.
- Compatibility with Ofwat's and CCWater's guidance and expectations
- The possible need for peer review to provide confidence to third parties that the methodology is robust.
- Additional explanation and clarity on the assumptions and judgement used to review each valuation data point and the decision and justification to include or exclude data points in the triangulation.
- The inclusion of learning points from the process if results are excluded.
- The provision of confidence levels on the valuation data points and the resulting triangulation outcomes and the justification for these levels.
- Clarity on the choice of one willingness to pay value over another for each service attribute to be able to assess the robustness of the methodology.

Bristol Water responded to these challenges to the Challenge Panel's satisfaction although the disappointingly low confidence levels attributed to the initial Triangulation outputs was of concern. The Challenge Panel suggested the triangulation methodology be peer reviewed.

Bristol Water's response to the Challenge Panel's concerns was to commission further valuation research at the draft business plan stage. Participants were presented three plans each containing the same package of services but implemented at different rates. These resulted in 'Expected' willingness to pay (WTP) values for the various service outcomes and these have been used for most cost benefit analysis with the exception of leakage. Further comment on leakage is given in section 8.7 of this report. The 'Expected' WTP values are not necessarily of higher confidence but Bristol Water assured the Challenge Panel that they are relevant for the context of the draft Business Plan.

At the Challenge Panel's request, Bristol Water documented the linkage between customer and stakeholder priorities and willingness to pay and its business plans outcomes, performance commitments and associated incentives. Bristol Water was also asked to clearly justify areas of the business plan where this linkage was not strong or where it had made management decisions to

overrule the results. Examples included issues on which customers had not been consulted directly, where the company has statutory and regulatory obligations to meet or where there was a clear and justifiable strategic, economic or operational case.

Case Study: Where Bristol Water's plans differ from customers' preferences

Early in 2018 Bristol Water tested the acceptability of 11 of its proposed PCs in a survey that grouped packages of PCs together and offered three distinct rates of improvement for each PC; 'Slower', 'Suggested' and 'Faster'. The results were variable, particularly between the slower and suggested plans; in eight of the PCs most of the customers who expressed a preference indicated that they would prefer a slower improvement than Bristol Water were intending with their 'Suggested' plan, in the remaining three PCs most of the customers preferred the 'Suggested' rate of improvement.

This concerned the Challenge Panel who challenged Bristol Water to understand why and what action it would take to ensure the majority of customers preferred their final plan. Coupled with this the Challenge Panel challenged Bristol Water not only to seek new and innovative ways to develop its plan but also to consider what the results meant for its on-going corporate governance.

Some of the PCs had targets mandated by Ofwat so it was not possible to go at the 'Slower' rate. Some PCs could not be at the 'Slower' rate as they are linked to PCs that the customer wished to see proceed at the 'Suggested' rate.

Bristol Water undertook further research where it became clear that customers were opting to receive a lower bill than the 'Suggested' plan would provide. This was demonstrated in the results for several attributes that were either the customers' high priority or an important goal, that only achieved a 'Slower' rate.

When testing the affordability of its proposals with customers, the research showed that customers were more likely to choose the 'Suggested' or 'Faster' plans when the base bill is lower. This effect was particularly pronounced for customers with lower incomes, eg the Social Renters segment. Lowering the cost of the overall bill is thus likely to make the cost of improvements acceptable to more customers.

The Bristol Water Board considered these survey results and was able to find additional cost efficiencies to allow it to offer the 'Suggested' plan at a lower cost. This combined with offering some of the customers' high priority attributes at a lower cost enabled Bristol Water's final acceptance research to return acceptance rates of over 70% for all PCs.

5.4 Resilience and Other Longer-Term Issues

Bristol Water's long-term strategy is set out in its 'Bristol Water, Clearly' document published in Spring 2018. This strategic document has been informed by customer research. Bristol Water invited comments from the Challenge Panel on drafts of this document and the Challenge Panel had influence over its final form.

While the Challenge Panel considers that 'Bristol Water, Clearly' is a good long-term strategy, it felt that the document should have been published much earlier in the business planning process. The long-term strategy was presented to the Challenge Panel at the same time as it was reviewing the PR19 PCs and ODIs and during the WRMP consultation. The Challenge Panel also considers the long-term targets could have been made clearer in this document. Bristol Water noted these observations. It would have preferred to have published this strategic document earlier but had been focused on the change of ownership early in the PR19 process and the resulting major reorganisation of its business.

The Challenge Panel reviewed the particular resilience challenges being faced by Bristol Water noting that it has made significant investment in resilience over successive price review periods in order to improve the reliability of the network, provide greater inter-connectivity and increase the robustness of the business.

The Challenge Panel observed that Bristol Water engaged with its customers on resilience and other longer-term strategic issues in a number of ways.

Qualitative research on operational resilience, using deliberative techniques, was undertaken covering both the demand and supply sides of the business. Some of this research contributed to the production of the draft WRMP. The qualitative research covered issues such as drought, flooding, security of supply and associated asset management but did not cover wider resilience issues such as IT systems. The deliberative research attempted to determine what resilience means to customers and their expectations of Bristol Water's response to such events. The Challenge Panel considers the engagement on operational resilience was effective and meaningful. It noted that customers are generally happy with Bristol Water's current approach to planning for and dealing with such resilience issues and wish it to further reduce the risk and impact of supply interruptions and supply outages, encourage greater water efficiency and reduce leakage, both in the short and longer terms.

Bristol Water engaged with customers in late 2017 on financing issues such as gearing, Pay As You Go (PAYG) and Regulatory Capital Value (RCV) run off rates, that is paying for investment now or spreading the cost and what proportion of bills should be financing costs. Whilst the Challenge Panel didn't have the opportunity to comment on the research materials in advance, it did note that the current bill was presented in the context of its primary components (including interest and profit) to obtain opinions on the cost of finance and the level of profit both before and after a game was completed. The outcome was that all participants preferred to borrow more to keep bill as low as possible but didn't want financing costs to become a dominant part of the bill. In response to a challenge from the Challenge Panel, Bristol Water said there was not much discussion on profit and it didn't influence the outcomes from the game. The Challenge Panel notes that Bristol Water plans to broadly maintain current borrowing levels.

The Challenge Panel has taken a keen interest in Bristol Water's corporate resilience, particularly the definition of its corporate responsibility and how this links to customers. Bristol Water is currently strengthening its corporate responsibility policies. The Challenge Panel welcomes this and would like to see greater clarity on the link with customer-focused strategic outcomes such as the community programmes and that Bristol Water's Board continues to maintain contact with its customers and its customers representatives. It would also welcome greater and continued understanding of other stakeholders needs and priorities, particularly over the long term. The Challenge Panel will be discussing these issues further with Bristol Water over the coming months.

5.5 Options and Trade-Offs

The Challenge Panel noted that various service level and bills options were presented to customers during the PR19 engagement process, particularly during the deliberative research stages, (including the online game and other valuation and affordability studies) and the acceptability testing of the draft and final business plans. Participants were presented with sets of options which allowed them to make high-level trade-offs between different levels of service improvements and changes in the level of the bill. The key options used included the level of leakage reduction, environmental improvement, the timing of investment and provision of assistance to customers in vulnerable circumstances. Trade-offs were explored both before and after participants received information on the nature of services or the company's current performance.

In addition, customers were provided with water resource planning options in the consultation on the draft Water Resources Management Plan (WRMP). These included options on leakage and demand reduction and new resource development.

Case Study: Environment 'Top Trumps' Cards

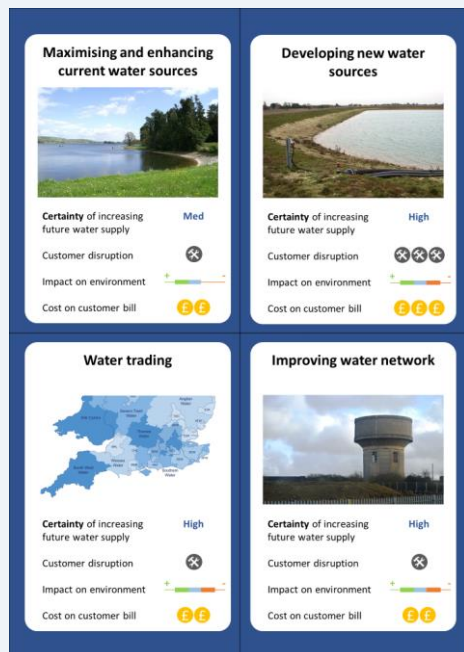
In early June 2017 Bristol Water wished to hold a series of one day workshops to better understand its customers' views on a series of topics of concern to their customers. Bristol Water provided the Challenge Panel with copies of the various posters and 'Top Trumps' cards that were to be used during the workshop.

The Challenge Panel was concerned about how the environment had been referenced in the research material, particularly reminding the participants that water is a natural, precious, scarce and finite resource and that water abstraction impacts the environment by having the potential to cause dried habitats, less oxygen and algal blooms. Bristol Water responded by adding information to the facilitators pack and a new poster with quiz questions.

The Challenge Panel reminded Bristol Water of the environmentally useful work it is doing with its catchment management work particularly the importance of land management to recreate a more natural hydrology and increase resilience. This resulted in a further environment poster, 'Top Trumps' handout cards for use during the workshop and improved facilitators notes written by a member of the Challenge Panel.

Finally, the Challenge Panel noted that the trade-off between the effects on new resources supply restrictions and environmental damage was not clear. This resulted in further updates to the workshop material partially provided by the Challenge Panel.

A Challenge Panel member attended one of the workshops and reported that the environmental information provided by Bristol Water was well received by the participants and contributed to a successful event.



From its review and challenge of the research methodologies employed, including attendance at some events, the Challenge Panel is happy that the service level and bills options presented were realistic and understandable to customers and allowed them to make appropriate trade-offs.

Bristol Water has had to explore and make a number of trade-offs in formulating its business plan. It has used the results of its customer engagement where possible but has also in some cases had to be mindful of its regulatory and statutory obligations, challenges and comments from the Challenge Panel, macro-economic considerations and financing constraints on its business. Bristol Water has documented and shared its decision making with the Challenge Panel.

Leakage reduction is a particular example where the government expectation of a minimum 15% reduction was traded off against initial customer willingness to pay for a lower level. However the

company has since obtained good customer support for its proposed 15% leakage reduction at a lower cost.

One particular area where trade-offs have been made between different groups of customers is in relation to social tariffs. The research has shown that customers who are not in vulnerable circumstance are willing to pay more for Bristol Water to provide support to those who are. The Challenge Panel welcomes this outcome.

Another example relates to future bills where current customers generally want to protect future customers from significant bill increases. The Challenge Panel did note that future customers were less concerned about bill rises in future.

5.6 Co-Creation and Co-Delivery

Bristol Water has used a number of co-creation methods to develop its business plan and is proposing to co-deliver some of them with customers and stakeholders.

The Challenge Panel saw that Bristol Water's Customer Forum was the main channel for co-creation. A Challenge Panel member attended one session of the Customer Forum and observed that participants were given the opportunity to comment on and shape elements of the business plan by providing their acceptability and preferences for various performance level options and the resulting bill impacts. The results were used in finalising the draft business plan.

The Bristol Water Youth Board established in January 2018 was used to develop future thinking on water efficiency. Bristol Water is proposing to continue with its Youth Board for the foreseeable future.

Other examples of co-creation included:

- Bristol Water's new website was tested with nine customers in face to face meetings before going live. This helped with the design of the website, particularly, its clarity, ease of use, preferred contact channels and options.
- Customers were consulted on Bristol Water's special cost factors before its Cost Adjustment Claims were submitted to Ofwat. The consultation was on which special cost factors should be submitted to Ofwat. Some customers supported factors that were not submitted as they did not meet Ofwat's materiality criteria. See section 10 of this report for more comment and opinion on this.
- Customers were consulted on a new bespoke performance commitment for customers in vulnerable circumstances to understand what they considered might be best measured. See section 7 of this report for more comment on this.
- Bristol Water's primary ongoing method of using customer feedback to effect change and service improvement is its customer dashboard. This captures ongoing customer insight from complaints, monthly and annual surveys. There are quarterly customer research meetings which review the findings and generate actions that feed into day to day business activity. In the future Bristol Water also intends to review the insight and how it is being used with the Challenge Panel.
- Bristol Water held a co-creation event entitled 'Resource West' involving other utilities, community groups and service providers (e.g. Bristol Waste) to align strategies and identify up to six areas for future joint working. As a result of this event Bristol Water has committed to sharing good practice and to look for opportunities to better co-ordinate and co-deliver existing initiatives, and to build commitment to take forward some innovative ideas for joint-working. Bristol Water has committed to a number of actions to deliver co-ordinated messages on water, waste and energy efficiency. It has also agreed a pilot scheme to work jointly with Bristol Waste in a Bristol neighbourhood and to produce a video in conjunction with Knowle West Media Centre to encourage people to reduce water usage. The Challenge Panel welcomes these innovations.

5.7 Acceptability Testing

The Challenge Panel had the opportunity to review and challenge Bristol Water's approach to testing the acceptability of its draft business plan in April and May 2018, the results it obtained and the use of these in finalising the plan.

The acceptability testing of the draft plan included:

- Reconvening customers who had participated in earlier research
- Engaging and recruiting uninformed customers
- Mass participation (roadshows, water talks, social media and a freepost survey)

The testing including obtaining opinion on three levels of service improvement (slower, preferred and faster) and bill impact and was designed primarily to inform the final Plan. The Challenge Panel noted that the acceptability research on the draft Business Plan focused on the Bristol Water's strategic outcomes and the resulting bill impacts, rather than the detail of individual Performance Commitments (PCs) within them. The Challenge Panel confirmed that customers' actual bills, rather than averages, were used where possible. The acceptability research also sought views on the overall level of ambition in the draft plan, overall bill levels and the level of vulnerability assistance.

Reaching out to new customers involved representative surveys (online and face to face), focus groups and the online panel. Customers in vulnerable circumstances were included in the face to face surveys.

The Challenge Panel noted that the preferred plan was marginally more acceptable than the slower plan. It did observe there were some anomalies and differences at service package level, for example interruptions to supply and water usage, but accepted the Bristol Water Board's view that a plan with a lower bill level with the suggested (preferred) service levels is more likely to be acceptable overall to customers.

The Challenge Panel also noted that the 'Social Renters' customer segment felt unable to support the preferred plan. It challenged Bristol Water on its intentions to help this customer group. Bristol Water assured the Challenge Panel that its affordability strategy will increase the number of customers on social tariffs and introduce more flexible payment plans. It will also consider how to use its segmentation information more effectively. The Challenge Panel stressed the importance of the learning gained from communicating with customers more effectively and getting the message across on issues such as social tariffs and behavioural change on water efficiency and improving service. Communicating using different terminology for different customer segments will be needed to achieve sustained behavioural change.

The Challenge Panel was pleased to see that Bristol Water took on board customers' recommendations that it should add water quality explicitly into its ambitions, clarify its community ambitions and reference the environment more in the final business plan.

Acceptability testing of the final business plan using took place in June and July 2018 using a mix of telephone surveys, focus groups and the Customer Forum. Challenge Panel members attended the Customer Forum and two focus groups.

The acceptability of the final plan was high across all the research activities the results obtained followed the patterns of the previous research. The level of unacceptability was very low at around 5% and also consistent across the research activities. The Challenge Panel was interested to know Bristol Water's intentions to engage with this minority group in future. Bristol Water considers that, whilst a minority of customers will always have an unacceptable view of its service and plans, it hopes its new customer segmentation data and improved data processes will aid access to and understanding of this group.

Bristol Water also researched customers' views on the principle of Outcome Delivery Incentives (ODIs) using focus groups in late 2017. It also undertook research covering the overall bill impact of its proposed incentives. The Challenge Panel notes customers' acceptance of the principle of incentives and overall impacts on bills. More comment on this is provided in section 9 of this report.

6. Affordability

Bristol Water's proposed affordability strategy for the next five years is based upon:

- A one-off bill reduction in 2020 of around 5% followed by inflationary increases until 2025.
- A commitment to keep bills low thereafter
- Reducing the number of customers in water poverty from 1.9% currently to zero by 2025
- Improved processes, use of customer segmentation data and automation to reduce bad debt
- Earlier engagement, motivation and rehabilitation of specific debtor groups
- Increased promotion of social tariffs
- Increased help for customers to save water
- Efficiency improvements in customer service through better use of digital channels and new technologies

Bristol Water has set out its affordability strategy in Section C2 of its business plan.

The Challenge Panel has reviewed and challenged the strategy as well as the customer engagement that informed it.

Bristol Water has used a number of qualitative and quantitative engagement approaches to assess affordability including:

- Customers in Vulnerable Circumstances Report
- Customer Affordability Assessment (Social tariff eligibility modelling)
- Annual survey of customer perceptions and priorities
- Customer Forum business plan options research
- Business plan options research
- Ongoing analysis and insight

The Challenge Panel received assurance that the research covered a representative sample of the customer base and was pleased to see the segmentation work described in Section 5 of this report informed this.

The Challenge Panel noted that customers in financial difficulty consider water bills a lower priority than energy, rent or council tax bills because the consequences of not paying are less severe.

The Challenge Panel was pleased to learn that Bristol Water's plans to increase customers' knowledge and awareness of its financial assistance measures extended across its supply area, not just within the city of Bristol, recognising the issue of rural poverty.

The Challenge Panel also challenged points of detail on:

- The creation of a charity trust fund to gift amounts to help repay debts between 2020-25.
- Water Direct
- The Assist fund
- Targeting areas of high deprivation

The Challenge Panel discussed and received assurance on Bristol Water's plans to increase awareness of help for those in debt, addressing the challenge of reaching the debt deniers and pro-actively targeting financial assistance.

Case Study – Affordability and Vulnerability

During the customer engagement quarterly review meetings, the Challenge Panel became aware that the then current Bristol Water policies and practices on Affordability and Vulnerability did not go as far as the Challenge Panel members would like. The Challenge Panel Chair challenged Bristol Water to make the vulnerability research more encompassing of wider affordability issues, as well as understanding the more specific issues around social tariffs and priority services.

The Challenge Panel members took a strong interest in the vulnerability research as it progressed and in the subsequent creation of the Affordability and Vulnerability policy. The Challenge Panel has encouraged Bristol Water to think widely around vulnerability, to be ambitious with its use of technology and to consider which additional partners it could work with beyond those with which it currently liaises.

The Challenge Panel is pleased to note that the Bristol Water Affordability and Vulnerability policy now warrants its own section (C2) within the Bristol Water Business Plan. The Challenge Panel believes that this policy is far in advance of where Bristol Water was two years ago and notes that the views developed in producing the policy have now percolated throughout the company. The Challenge Panel looks forward to working with Bristol Water in the execution of this policy.

If the Panel has a regret it is that, due to time restraints, Bristol Water was not able to involve rural customers as much as other hard to reach sections of the community. This was due to the lack of existing support structures. However, the Panel notes the intention to develop these contacts during the plan period.

Two affordability related PCs have been proposed and are described in more detail in section 8 of this report.

As a result of its challenges, the Challenge Panel considers the company's approach to assessing affordability, both through its bespoke PR19 research and its ongoing engagement with customers, have been both efficient and effective. As a result Bristol Water has obtained a good understanding of what affordability looks like for its customers.

Bristol Water's plans to address affordability represent a step change increase over its current activities and the Challenge Panel welcomes these. These plans coupled with steady bills in real terms following a reduction in 2020 are designed to increase affordability for current customers, future customers, and those struggling, or at risk of struggling, to pay. The plans should also increase the accessibility to Bristol Water's social tariffs and assistance schemes.

The Challenge Panel considers the proposed affordability-related PCs include stretching targets and ambition which should provide a good mechanism for monitoring progress. The Challenge Panel is pleased to see that Bristol Water is already making plans to ensure delivery of the proposed strategy.

7. Vulnerability

The key components of Bristol Water's vulnerability strategy for 2020 to 2025 include using data wisely, increasing awareness and improving the customer journey. It also includes a significant increase in the help provided to customers in vulnerable circumstances and an ongoing Affordability Action Plan implemented in conjunction with Wessex Water.

In its business plan Bristol Water outlines the activities underpinning its vulnerability strategy as including:

- Improving customer segmentation, analysis and modelling capability to identify customers at risk.
- Scenario-mapping customer needs and priority levels for different types of incident.
- Sharing data with utilities and third parties
- Working towards introducing a single point of registration of vulnerability for customers across all utilities.
- Establishing partnerships with a range of local community groups, including: local councils and housing associations, charities, Bristol Old People Forum, Royal Blind Society and health professionals.
- Offering tailored channels and communications to target these customers.
- Improving the Priority Services Register to map customer to need and nominee details.
- Introducing a joined-up approach to enable increased sign-up in the field.

The Challenge Panel recognises that the key strands of the vulnerability strategy align with Ofwat's principles as set out in its Vulnerability Focus report published in February 2016. The Challenge Panel is also satisfied that Bristol Water strives to provide excellent service to all its customers, including those who find themselves in vulnerable circumstances.

Bristol Water kept the Challenge Panel informed during the research and development of its vulnerability strategy. This enabled the Challenge Panel to review and challenge the emerging proposals and to test whether there was adequate and appropriate customer support for them. In addition, being present at research events assured the Challenge Panel that participants weren't led to a particular result by the questions posed to them.

The customer research into vulnerability included; surveys, panels, focus groups, social media, ongoing data gathering and face-to-face interactions. The Challenge Panel reviewed and challenged the research methodologies and the results obtained.

The Challenge Panel's key area of focus and challenge included:

- The segmentation and geographical location of the participants used in the vulnerability research, whether there was any skew, and the selection being on the basis of vulnerability risk factors rather than demographics. As a result of the challenge Bristol Water agreed to 'retrofit' the profiles of participants into the company's customer segments adopted in other research so comparisons could be made.
- The vulnerability research didn't include rural customers. Rural poverty wasn't assessed because these are difficult groups to reach as there are often fewer social structures in place. Bristol Water recognises that this issue should be addressed and has agreed to do so in the future.
- Why there is a low understanding of Bristol Water amongst certain groups, eg the Centre for the Deaf and the Eye Clinic (social services). In most cases it is because the Bristol Water hasn't had a direct relationship with these groups to date, but it recognises there are opportunities to improve this in future.
- Whether the research had included people that may not consider themselves to be vulnerable even though they are, and confirmation that the research had been guided by the definition of vulnerability rather than the perception of it.
- Some common themes that emerged from the research included financial worries, negative attitudes towards organisations, mental health issues, the importance of informal networks, getting help and support and resilience to crises over time. The Challenge Panel agrees these are important issues and that organisations should adopt behaviours that

help people who are experiencing them. Bristol Water accepted that more empowerment of staff to make decisions to help such people may be required.

- Customers' ability to choose a channel of communication with the company will depend on the data the company has collected. The company has longer term plans to better link data and intelligence on network performance.
- The risk of vulnerability-related performance measures driving the wrong behaviour. The key to this is using data to know customers well enough to identify they are vulnerable and that other parties' data will be key to this but accepting that some is outside the company's control. Equally customers could be asked directly to provide relevant information.
- The limited success Bristol Water had in attempting to obtain data on vulnerability from third parties despite its efforts and suggestions from the Challenge Panel.

As a result of its challenges, and Bristol Water's responses to them, the Challenge Panel is satisfied that there has been effective and targeted ongoing and bespoke engagement on vulnerability.

One bespoke PC related to vulnerability has been proposed and is described in more detail in section 8 of this report.

Bristol Water engaged with customers during the development of this PC to better understand what should be measured. The Bristol Water used its online panel and focus groups for this. Mixed views were obtained over whether the satisfaction of vulnerable customers or the number of customers on the Priority Services Register (PSR) should be measured. The Challenge Panel questioned how the satisfaction of those customers on PSR would be measured if numbers were rising, as is expected across the industry. Bristol Water settled on a commitment related to how it satisfies those as registered on the PSR as this would ensure employees are kept trained to deliver the intended high-quality service and experience. This will be backed up by a key performance indicator (KPI) aimed at increasing the number of customers on the PSR. The Challenge Panel accepted this.

Bristol Water's plans to help customers in vulnerable circumstances represent a significant increase over its current activities and the Challenge Panel welcomes this. The plans are designed to be targeted and efficient and the Challenge Panel agrees if well implemented they should be effective. They should also increase the accessibility to Bristol Water's assistance schemes.

The Challenge Panel considers Bristol Water's plans to establish partnerships with third party organisations are commendable but will require considerable effort. The Challenge Panel has seen that Bristol Water is already making plans to ensure the delivery of its vulnerability plans.

The Challenge Panel considers the proposed vulnerability-related PC includes a stretching target and should provide a good mechanism for monitoring progress.

8. Performance Commitments and Service Targets

8.1 Review by the Challenge Panel

The Challenge Panel has scrutinised the 26 PCs proposed by Bristol Water. For each PC this scrutiny covered:

- the clarity of definition
- the initial service levels
- the performance target for 2024-25 and the degree of stretch or ambition involved in achieving it
- the performance profile to 2024-25
- the investment or operational activity required to achieve the performance
- the degree of customer support for the PC and the proposed performance to 2024-25 and where possible beyond this
- industry comparative performance where available

In order to assist and support the Challenge Panel in its review and challenge of Bristol Water's PCs and Outcome Delivery Incentives (ODIs), the Challenge Panel established a Performance Commitment and Outcome Delivery Incentive (PC & ODI) Sub-Group.

The PC & ODI Sub-Group reported its findings and opinions to the Challenge Panel and followed-up any queries it raised. Some members of the PC & ODI Sub-Group also attended the Challenge Panel's Customer Engagement Sub-Group so there was good linkage and continuity across these topic areas. This was very useful in assessing Bristol Water's customer research on its PCs and ODIs and the way it used the results to develop them.

The level of access to documentation and personnel (both Bristol Water and its research consultants) given to the Challenge Panel and its Sub-Groups was sufficient for it to carry out its work.

The Challenge Panel's comments on the company's ODIs are given in Section 9 of this report.

The Challenge Panel recorded all its challenges associated with the various PCs and performance targets. Its key areas of focus and challenge included:

- The clarity of definition of the PCs, the associated metrics, service levels, targets and incentives. This was to ensure that they would be understandable to customers and stakeholders and that performance reporting on them would be clear and unambiguous
- The justification for discontinuing PCs from the current period (PR14), particularly to ensure there would be no resulting detriment to customer service or in meeting statutory or regulatory obligations
- The use of customer and stakeholder information and research results to develop and define the proposed new PCs and service targets
- Evidence and strength of customer support and willingness to pay for the PCs and service targets
- The categorisation of PCs as existing, common, mandatory or bespoke (in line with Ofwat's requirements)
- Any exemptions included in the definitions of bespoke performance commitments and the justification and customer support for these
- The reasons for selecting certain asset health PCs from the list suggested by Ofwat and discounting others
- The basis of the service level at the end of the current period (2019/20), the target for 2024/25 and the performance profile to achieve it
- The justification for adopting single year, five-year or cumulative targets
- The degree of stretch or ambition involved in meeting the service targets
- The justification for not striving to meet future industry upper quartile performance for a number of PCs
- The operational activity or capital and operational investment required to meet each target

The Challenge Panel strongly encouraged Bristol Water to document its PCs, service targets and ODIs in line with the challenges and requirements listed above. This was primarily to assist the Challenge Panel in fulfilling the requirements of Ofwat's Aide Memoire but, in agreeing to do this, Bristol Water also recognised that it would also be very useful evidence to include in its business plan submission to Ofwat. The Challenge Panel aided Bristol Water with the format and content of the documentation. The result is Section C3 of Bristol Water's business plan which the Challenge Panel considers to be a very comprehensive reference document.

8.2 Customer Engagement on PCs and Service Targets

Bristol Water has proposed 26 performance commitments (PCs) for the period 2020-2025, grouped under three of its the four PR19 outcomes as follows:

- Safe and reliable supply: eleven PCs
- Excellent customer experiences: six PCs
- Local community and environmental resilience: nine PCs

Bristol Water is not proposing any PCs for its fourth PR19 outcome (corporate and financial resilience) as it considers this outcome supports delivery of all other PCs and can be monitored using financial and corporate metrics.

The PCs fall into the following categories:

- **Nine common measures**, all required by Ofwat and including two asset health metrics,
- **Eleven mandatory bespoke measures**, all required or suggested by Ofwat and including seven existing measures,
- **Six optional bespoke measures**, including four existing measures, one required by Ofwat and one new company-defined bespoke measure.

Bristol Water's customer engagement on its PCs commenced in 2016 with research based on information from the development of PR14 combined with ongoing feedback from customers. The results of this phase of the engagement were used to develop Bristol Water's preliminary high level outcomes for PR19.

Between March 2017 and February 2018 further research was undertaken into specific service areas including resilience, water efficiency, demand reduction, affordability and vulnerability, and company-specific issues such as cost adjustments and financing costs. The results were used to refine the outcomes and to develop the PCs.

Business plan options were tested between March and April 2018 and this work enabled the development of some indicative service targets. Bristol Water informed Ofwat of its proposed PCs for PR19 in May 2018.

The service targets were finalised during acceptability testing of a draft and final business plan between June and August 2018.

The Challenge Panel, primarily through its Customer Engagement Sub-Group, has reviewed in detail Bristol Water's customer engagement processes, the results obtained and their use in the development of the PCs and service targets. It notes however that the majority of the PCs are either specified or suggested by Ofwat and several also cover statutory water quality and environmental obligations.

Throughout the research the Challenge Panel saw that customers continued to place high priority and value on service areas including supply reliability, adequacy of water pressure, the aesthetics of water, affordability, reducing leakage and, later in the research, protecting and enhancing the natural environment. Bristol Water is proposing several common and mandatory PCs covering these areas. The Challenge Panel is pleased to see that optional bespoke PCs are being proposed relating to value for money, affordability, vulnerability and community satisfaction, some of which are carried over from PR14.

In response to requests and pressure from the Challenge Panel, Bristol Water documented the development of the proposed PCs that are not mandatory or existing, including where these were co-

created with customers and/or stakeholders. Not only did the Challenge Panel want to see that the PCs were based on customer and stakeholder priorities where possible, rather than priorities identified wholly by the company, it also wanted it made clear where Bristol Water had decided to override customers views where it felt long term business or economic considerations were more relevant and applicable.

The Challenge Panel is satisfied that Bristol Water has defined its bespoke PCs using the outcomes from the results of customer engagement either at outcome level or, in some cases, PC level, either directly or by using reasonable judgment or sound strategic thinking on issues where customers had not been consulted or where customers' views have been overridden.

The Challenge Panel raised a number of queries on early drafts of the PC definitions including:

- The rationale for removing the Security of Supply Index (a PR14 PC) and ensuring nothing is missing from Drought Risk.
- The need for sufficient background information on Drought Risk and the Compliance Risk Index
- How the proposed PCs enable Bristol Water to achieve a role beyond water.
- The learning that can be gained from other industries in the delivery of excellent customer service and whether the Customer Measure of Experience (C-Mex) is sufficient and innovative enough to cover this.
- The need for PCs covering mandatory environmental obligations
- The significance and long-term challenge associated with the vulnerability-related PC and that it will be developed in conjunction with other organisations.
- The clarity of the proposed Biodiversity metric and the associated ambition (see Section 8.5 for more information on this)
- The ambition associated with improving raw water quality
- The need for a briefing to the Panel on the DWI Compliance Risk Index
- The benefit to Bristol Water's customers of the proposed Abstraction Incentive Regime (AIM)-related PC
- Understanding the meaning of void properties and the impact of them on customers
- Whether the proposed resilience-related PCs reflect the particular resilience challenges being faced by Bristol Water and customers' priorities

Further details on specific challenges posed by the Challenge Panel are given in sections 8.4 to 8.8 of this report.

As a result of its challenges the Challenge Panel is happy that the 26 proposed PCs are clearly defined and are based on the needs and priorities of customers or Bristol Water's statutory and regulatory obligations or judgement where necessary and appropriate. The Challenge Panel's comments on the service targets associated with the proposed PCs, the associated level of stretch and ambition and the customer engagement on them are given in Section 8.3 of this report.

At the Challenge Panel's request, Bristol Water has documented the source and strength of customer support for each PC and to highlight where customers have co-created the measures or where other information has been used in isolation or in combination with customers' preferences to define them.

Bristol Water has tested the acceptability of its Business Plan with customers in a number of qualitative and quantitative ways. Acceptability for the company's proposed outcomes was tested together with different options for investment across a number of service areas.

The strength of support for eleven PCs and the service targets associated with them was tested as part of the acceptability research. Testing of the remaining fifteen PCs was undertaken indirectly by researching at outcome, rather than PC level. The Challenge Panel notes that, based on this research, customers find Bristol Water's outcomes and performance commitments (where tested) to be acceptable, although further research was undertaken in July 2018 on bill options associated with the proposed local community PC to determine the preferred level of community investment.

8.3 Initial Service Levels and Service Targets

8.3.1 Initial Service Levels

The Challenge Panel reviewed and challenged the initial service levels (for 2019/20) for each of the 26 PCs and the proposed service target to 2024/25. The basis upon which the service level and targets had been set and the level of stretch involved with each was scrutinised. The Challenge Panel also reviewed the evidence and strength of customer or other stakeholder support for the proposed service levels.

Historical performance information for each PC, both company and industry, was reviewed where available.

The Challenge Panel also requested information from Bristol Water on how it intends to achieve its targets, particularly if its approach will be different in future and whether additional resources, investment or new and innovative ways of working will be required.

Bristol Water was asked to document how it had assessed its service levels and targets for each PC, in particular the use of:

- cost-benefit analysis,
- comparative information,
- historical information,
- minimum improvement,
- maximum level attainable and
- expert knowledge

Bristol Water has done this in Section C3 of its business plan.

It is noted that some of the proposed PCs are new and the industry is waiting further information from Ofwat on targets for them. Examples include the Customer Measure of Experience (C-Mex) and the Developer Services Measure of Experience (D-MeX). Other measures are new or company-specific and no reliable comparative industry historical information exists, for example 'Void properties' and 'Local community satisfaction'. In these cases, the Challenge Panel is satisfied that Bristol Water has referred to other appropriate sources of information or use reasonable judgement to set its initial service levels and targets.

In most other cases the Challenge Panel confirmed that Bristol Water had based the initial service levels on:

- a continuation of current performance trends or average of performance in recent years
- the best level of performance achieved in recent years
- forecasts set out in related company plans, eg WRMP
- statutory obligations, for example water quality and WINEP

As a result of its review and challenge, the Challenge Panel considers Bristol Water's initial service levels are reasonable.

8.3.2 Service Targets to 2024/25

The Challenge Panel reviewed and challenged the service targets for the five-year period to 2024/25 for each PC.

Bristol Water did not consult its customers on the acceptability of individual PC service targets and the level of stretch associated with them. This means the Challenge Panel is unable to confirm the validity of the individual service targets and level of stretch from a customer perspective.

However, Bristol Water has tested the customer acceptability of its draft plans and rate of service improvement at service outcome and related package level (covering 11 PCs) including:

- Customer experience (two PCs)
- Vulnerability assistance
- Leakage

- Water use
- Environmental enhancement
- Community satisfaction
- Water quality
- Interruptions to supply
- Drinking water aesthetics (appearance, taste and smell)
- Protection against a major water supply event

For each of these packages, three rates of improvement were tested (slower plan, suggested plan, and faster plan) by presenting the bill impacts of each.

Overall the results show that, despite some variability across the packages, customers generally preferred the suggested draft plan and as a result Bristol Water decided to proceed with these suggested plan levels albeit at a lower cost, although Bristol Water also decided to conduct more research into local community satisfaction to be sure on this particular package.

The Challenge Panel has assessed the individual PC service targets and the level of stretch associated with them. It did this by asking Bristol Water to document the basis of the service targets and any assumptions it made. It also asked Bristol Water to justify the degree of stretch and ambition associated with them. The Challenge Panel reviewed all the information provided to it.

In many cases Bristol Water is targeting to achieve industry upper quartile performance by 2024/25. The Challenge Panel welcomes this. Of particular interest to the Challenge Panel were those PCs where Bristol Water is not targeting to achieve this level of performance. The Challenge Panel wished to understand the reasons for this and to assess whether they were justified. The reasons included:

- The PC measure, whilst common to all companies, is new to the industry and no historic industry performance data exist. Example PCs include C-Mex and D-Mex
- The level of performance is mandated by Ofwat through the PR19 Methodology or by other regulators, for example DWI and EA. Example PCs include water quality compliance, WINEP, supply interruptions, turbidity and leakage
- The PC is bespoke to Bristol Water and no other company performance data exist. Example PCs include unplanned outage, properties at risk of low pressure, population at risk from asset failure, percentage of satisfied vulnerable customers, raw water quality of sources, the Abstraction Incentive Mechanism (AIM), the Biodiversity Index and local community satisfaction
- Where current performance is significantly below industry upper quartile performance and where Bristol Water considers the cost of achieving future upper quartile performance is high and uneconomic and, in some cases, there is insufficient customer willingness to pay for this. Example PCs include mains bursts, water quality contacts, meter penetration and per capita consumption

As a result of its review and challenges, the Challenge Panel considers the initial service levels and service targets for all of the proposed PCs except the Biodiversity Index (see section 8.5 of this report) to be based upon robust information and/or sound judgement, to be in line with its statutory and regulatory obligations and to be stretching. The Challenge Panel agrees with Bristol Water that the proposed service targets relating to supply interruptions and leakage reduction are particularly stretching.

The Challenge Panel raised a number of challenges on Bristol Water's proposed PC relating to biodiversity. These are described in detail in section 8.5 of this report.

Bristol Water researched and derived customer valuations for various service packages for its proposed outcomes. It used these in whole or in conjunction with other information to set service targets and incentives.

A methodology to triangulate its various sources of valuation (willingness to pay) information for each service package it consulted on was developed with the assistance of National Economics Research Associates (NERA). The triangulation applied weightings to each information source based upon a combination of systematic judgement and cost benefit analysis.

The Challenge Panel paid close attention to the triangulation methodology and its opinion on this is provided in Section 5.3 of this report.

As a result of challenges from the Challenge Panel on the level of confidence in the initial WTP results, Bristol Water commissioned further valuation research at the draft business plan stage. Participants were presented three plans each containing the same package of services but implemented at different rates. These resulted in 'Expected' WTP values for the various service outcomes and these have been used for most cost benefit analysis with the exception of leakage. Further comment on leakage is given in section 8.7. The Expected WTP values are not necessarily of higher confidence but Bristol Water assured the Challenge Panel that they are relevant for the context of the draft Business Plan.

During its review of the PC service targets, the Challenge Panel raised queries and challenges relating to the basis, the level of ambition and stretch and the degree of customer support for them.

Bristol Water provided additional clarity or information which was sufficient to satisfy the Challenge Panel that the service targets for the PCs are reasonably stretching, some particularly so, and in line where possible and appropriate with broad customer preferences and willingness to pay.

The Challenge Panel is satisfied that the majority of the company's proposed PCs and service targets are well defined, transparent and should be meaningful to customers and stakeholders. It notes however that customers haven't been consulted on the individual definitions.

As mentioned above the Challenge Panel considered the Biodiversity Index PC to be poorly defined in the first instance which would have meant it would not have been clear to customers and stakeholders what commitments Bristol Water was making and how ambitious its plans were. As a result of the challenges posed Bristol Water significantly improved the definition of the PC and the associated performance targets.

Bristol Water describes in its business plan how it intends to report its performance in AMP7. It will be building on its recent work on annual reporting, that is the use of a single interactive page on the website supplemented by a written report.

The Challenge Panel considers the new reporting format to be good but that the information provided should be transparent. Bristol Water agrees with this but wants the reporting to be engaging and a one size fits all.

8.4 Common Performance Commitments

Bristol Water is proposing nine common measures, all required by Ofwat and including two asset health metrics. The common performance commitments are:

- Customer measure of experience (C-Mex)
- Developer services measure of experience (D-Mex)
- Compliance Risk Index (CRI)
- Water supply interruptions
- Risk of severe restrictions in a drought
- Asset health: mains bursts
- Asset health: unplanned outage
- Leakage
- Per capita consumption

Each of the common PCs has been reviewed in detail by the Challenge Panel. It sought clarity and posed specific challenges on four of them:

- Risk of severe restrictions in a drought - the rationale for removing the Security of Supply Index (a PR14 PC) and ensuring nothing is missing from the drought risk
- Compliance Risk Index – the Challenge Panel received a briefing from DWI on this Index in order to aid its understanding of it
- C-Mex - The learning that can be gained from other industries in the delivery of excellent customer service and whether C-Mex is sufficient and innovative enough to cover this.

- Leakage – the degree of customer support for the proposed 15% reduction on leakage by 2024/25

The Challenge Panel’s comments on the setting of PC service targets for PCs are given in section 8.3.2 of this report.

Bristol Water provided further information and clarity in response to the Challenge Panel’s challenges.

Case Study – Mains Bursts

The Challenge Panel asked why there is no improving performance planned for mains bursts in AMP7. Bristol Water replied that the Ofwat methodology doesn’t permit a glidepath as this is an Asset Health measure. Also, Bristol Water considers an improvement in performance would not be in customers’ interest as it would cost a lot of money. The Challenge Panel wondered therefore what the Bristol Water’s long-term aim for bursts is. Bristol Water replied that there is no long-term target for this measure because service improvements for customers will come from other measures that matter more to them, eg leakage, water quality.

The Challenge Panel needed to consider carefully the proposed target and deadband for this PC as the industry upper quartile performance is forecast to improve but Bristol Water’s performance isn’t. At first sight there appeared to be no long-term vision for asset health. The Challenge Panel said Bristol Water should inform customers about the health of its assets and how it will be managing them. In response Bristol Water set out its asset management strategy to inform the Challenge Panel on what is being replaced, spent and in place generally on asset management. It also included a related narrative in its business plan to make it clear it has plans in place to look after and improve its mains.

As a result of its work the Challenge Panel is satisfied that the common performance commitments and their associated service levels and targets are:

- Clearly defined in a way that should be understandable to customers when performance is reported to them
- Aligned to the results of customer engagement at outcome and service package level
- Stretching in performance terms, with initial service levels and targets based upon robust information and judgement, but which have not been tested explicitly with customers

8.5 Bespoke Performance Commitments

The company is proposing 17 bespoke performance commitments, 13 mandatory (required by Ofwat’s PR19 methodology) and four optional as follows:

Mandatory Bespoke PCs

- Water quality contacts – appearance
- Water quality contacts – taste and odour
- Properties at risk of receiving low pressure
- Turbidity performance at water treatment works
- Unplanned non-infrastructure maintenance
- Population at risk from asset failure
- Percentage of satisfied vulnerable customers
- Void properties

Meter penetration
Raw water quality of sources
Biodiversity Index
Waste disposal compliance
Abstraction Incentive Mechanism (AIM)

Optional Bespoke PCs

Percentage of customers in water poverty
Value for money
WINEP compliance
Local community satisfaction

The Challenge Panel has reviewed and challenged each of the bespoke PCs in detail. It sought clarity and posed challenges on all of them. Bristol Water responded on all the challenges raised. Particular issues covered included:

- The need for PCs covering mandatory environmental obligations and the avoidance of double-counting of incentives
- The significance and long-term challenge associated with the vulnerability-related PC and the need for it to be developed in conjunction with other organisations.
- The clarity of the proposed Biodiversity metric and the associated ambition (see below for more information on this)
- The ambition associated with improving raw water quality
- The appropriateness of an incentive deadband for waste disposal compliance given that performance against this measure is a statutory requirement
- The benefit to Bristol Water's customers of the proposed AIM-related PC (see section 8.6)
- The clarity of definition of the void properties-related PC

The Challenge Panel's comments on the setting of PC service targets for PCs are given in section 8.3.2 of this report.

Case Study – Raw Water Quality

The Challenge Panel raised two concerns with Bristol Water's proposed PC for raw water quality of sources. These were:

- There should be no overlap between the work included in this PC and any similar in the WINEP
- The level of ambition in setting the target and the amount of stretching in setting the incentive levels

After discussions, and provision of further information, the Challenge Panel formed the view that the proposed PC is reasonable. Whilst the proposed phosphorous reduction target appears to be modest, the proposal is considered to be appropriate when a number of factors are considered, for example the size of the catchments, the small number of landowners involved, the uncertainty over whether uptake of advice/grants will increase going forward, together with the significant penalty proposed.

Case study - Biodiversity Index

The Challenge Panel had difficulty in assessing the basis of and the ambition associated with Bristol Water's proposed PC relating to biodiversity, in particular:

- The proposed target improvement of 50 Biodiversity Index (BI) units in relation to current performance
- The work involved in achieving the target and the constraints associated with this
- The distinction between business as usual biodiversity-related work and genuinely new activity
- The potential for overlap with work to meet statutory obligations relating to biodiversity
- The appropriateness of the proposed BI incentive to drive behaviour. See Section 9 for more comment on this.

The Challenge Panel regards the BI performance commitment and associated incentive as potentially a good driver for changing company behaviour. However, the Challenge Panel had difficulty in assessing whether the PC proposed by the Company for the BI was sufficiently stretching, in particular due to an insufficient evidence base to support it. The Challenge Panel considered the PC lacked transparency and found it inherently difficult to judge how challenging the proposals are without a great deal of contextual information, some of which was not initially made available by Bristol Water.

The Challenge Panel considered that the BI PC definition needed to be tightened to give it the assurance it needed and to satisfy Ofwat's feedback on this PC. It also suggested a linked condition in the BI PC that by end of the AMP7 period a report should be produced by Bristol Water in readiness for PR24 discussions which clearly sets out the scope for enhancing BI scores across each landholding including a thorough assessment of operational constraints – the idea is that this would remove the possibility of this uncertainty (which appeared to have led in part to a lack of ambition) continuing.

Clarity on measurement was also required to bring the commitment to life and to help assess the level of ambition.

At present Bristol Water doesn't appear to have management plans to enhance biodiversity across its landholders, hence it is difficult for it to set targets because of concerns around possible operational constraints. This is understandable, but the Challenge Panel is aware that some companies do have biodiversity plans across their non-SSSI landholdings that they implement as part of their core business. The WINEP investigation on the Biodiversity Index will help Bristol Water get on the 'right track' with this, and this is positive for the future. Bristol Water's performance on biodiversity to date has been reasonable but not outstanding. The Biodiversity Index may be a novel accounting tool, and Bristol Water is arguably leading the way in this regard, but the level of 'stretch' depends on the targets set against this tool.

To its credit Bristol Water responded positively to these challenges and significantly improved the presentation of this PC in its business plan. It also committed to producing a detailed BI action plan and agreed that an example BI case should be presented to the Panel and other stakeholders for review after the Business Plan is submitted.

It was also agreed that there is a need to design and implement a BI AMP7 performance monitoring mechanism that involves the Challenge Panel.

The Challenge Panel remains committed to this innovative BI PC being in place for AMP 7, as currently included in the Bristol Water business plan as the Bristol Water customer engagement research rates environmental improvements to Bristol Water land holdings as important. In successive Challenge Panel meetings, the environmental regulators have expressed concerns about whether the proposed BI PC reward threshold is sufficiently stretching, and the Challenge Panel members have not disputed the issues raised. However, whilst there may be a limited amount of data to robustly defend the proposed reward target, all agree that an acceptable process, based on the BI PC, can be found that would benefit both the customer and the environment. The Challenge Panel believes that by working with Bristol Water after the plan submission an acceptable process with stretching targets can be found that would benefit both the customer and the environment; if this requires a future change to the BI PC targets and/or incentive targets and rates this will be submitted by Bristol Water to Ofwat for consideration.

As a result of its work the Challenge Panel is satisfied that, with the exception of the Biodiversity Index PC, the bespoke performance commitments and their associated service levels and targets are:

- Clearly defined in a way that should be understandable to customers when performance is reported to them
- Aligned to the results of customer engagement at outcome and service package level
- Stretching in performance terms, with initial service levels and targets based upon robust information and judgement, but which have not been tested explicitly with customers

The Challenge Panel notes that six of the bespoke performance commitments contain exemptions:

- Customer contacts about water quality (appearance) - This performance commitment excludes: contacts relating to taste and smell and any water complaints associated with reportable events that are notified to the Drinking Water Inspectorate (DWI), in line with DWI reporting guidelines.
- Customer contacts about water quality (taste/smell) - This definition excludes: contacts relating to appearance, and any water complaints associated with events are notified to the Drinking Water Inspectorate (DWI), in line with DWI reporting guidelines.
- Properties at risk of receiving low pressure - Various exemptions are included in the definition in line with Ofwat's definition.
- Turbidity - Only routine regulatory samples taken at the final water compliance taps at water treatment works (WTWs) and that are reported in the regulatory returns to the DWI are used in the calculation of this metric. This is aligned to Ofwat's June Return guidance from 2011.
- Voids – This excludes properties which are temporarily recorded as void when they enter into the change of occupancy metering programme (and do not receive a bill until the date the meter is fitted). This is consistent with the definition used to report void numbers within Bristol Water's Annual Return.
- Meter penetration - This includes household properties only. Non-household, void properties and multiple properties served by a single meter are excluded.

The Challenge Panel notes that Bristol Water has not consulted customers on these exclusions. The Challenge Panel accepts consulting customers at this level of detail would not have been appropriate and proportionate. However, the Challenge Panel has reviewed and challenged the exemptions and considers them to be reasonable.

8.6 Abstraction Incentive Mechanism commitments

Bristol Water is proposing a single AIM-related PCs at its Shipton Moyne source. This groundwater source is located outside Bristol Water's supply area.

The Challenge Panel notes this is a mandatory PC specified by Ofwat. Bristol Water does not have any AIM sites under the strict Ofwat definition but has identified its abstraction at Shipton Moyne in Wessex Water's area as a possible candidate. The commitment aligns with customers' general preferences for environmental protection and sustainable and secure resources.

The Challenge Panel recognises that the benefit from this performance commitment is to the water catchment around the source and not to Bristol Water's customers directly. However it accepts that this type of commitment is appropriate as long as the environmental benefits are clear.

The Challenge Panel notes that Bristol Water has discussed its AIM proposal with EA. EA has concluded that there would be environmental benefits from the proposed AIM commitment. However the Challenge Panel has concerns that the environmental benefits will be felt by non-Bristol Water customers. The issue of whether Bristol Water's customers should be paying for this commitment remains outstanding and the Challenge Panel looks to Ofwat to determine whether it should be funded. Bristol Water has told the Challenge Panel that it would be happy to exclude the commitment from its plans if deemed necessary by Ofwat.

8.7 Leakage

The Challenge Panel notes that leakage reduction is an existing PC but that Ofwat requires that leakage should be reported in AMP7 based on a new shadow definition and on a three-year rolling average basis.

Bristol Water's service target for its leakage-related PC is to achieve a 15% reduction in leakage by 2024/25 against the forecast performance in 2019-20. The percentage reduction is reported on a three-year average basis in line with Ofwat's requirements. The target reduction of 15% is in line with Ofwat's minimum industry expectation. It is also in line with Bristol Water's draft WRMP.

The Challenge Panel has challenged the proposed PC and service target and the level of customer support for these. Its challenges, combined with further study by Bristol Water, altered the company's initial plan for a 15% reduction in leakage within the WRMP planning period (25 years), to achieving this by 2024/25.

The Challenge Panel noted that the customer research on leakage for the draft business plan suggested leakage reduction is a high priority for customers. Whilst there was a preference for a slower level of reduction (ie less than the 15% Ofwat expectation) from Social Renters and a higher level of reduction from Safely Affluent customers, there was overall customer support for the suggested plan for a 15% reduction by 2024/25. The acceptability testing of the final business plan showed over 80% support for the 15% reduction.

The Challenge Panel is pleased that Bristol Water is aiming to achieve a significant reduction in leakage and it recognises that this will be a stretching target to achieve as Bristol Water is already a frontier company and that aims to remain an industry upper quartile performer by 2024/25.

8.8 Scheme Specific Commitments

The Challenge Panel notes that Bristol Water is not proposing any scheme-specific commitments.

9. Outcome Delivery Incentives (ODIs)

9.1 Review by the Challenge Panel

The Challenge Panel has reviewed the proposed Outcome Delivery Incentives (ODIs) for Bristol Water's 26 proposed PCs. The detailed review was undertaken primarily by the PC and ODI Sub-Group. The Challenge Panel also reviewed the ODIs at a higher level.

The PC and ODI Sub-Group's review and challenge of the ODIs focused on:

- The methodologies, assumptions and source information used to calculate the ODIs
- The consistency of application of the methodologies and assumption
- The categorisation of ODIs into financial or reputational and the justification for these
- The proposed timing of incentive payments, for example in period or end of period
- The extent and quality of the customer engagement on ODIs
- The evidence and strength of customer support for incentives both in principle and for individual ODIs
- Bristol Water's proposals for the use of any out-performance payments it receives
- Ensuring incentives were not being double counted across PCs, for example with penalties arising from breaches of statutory obligations

The Challenge Panel's scrutiny included:

- The methodology and assumptions used for cost benefit analysis, particularly the clarity of presentation of the results, the triangulation of valuations and the selection of values to calculate incentive rates
- The justification for any skewed incentives, dead-bands and end of period payments, in particular whether there was an appropriate balance of risk and reward
- The appropriateness of outperformance payments for apparent business as usual activities or for meeting statutory obligations

Bristol Water provided further clarity or additional information in response to the challenges and questions raised. As a result, the Challenge Panel understands the basis of each ODI and the degree of customer support for each.

9.2 Customer Engagement on ODIs

Bristol Water undertook qualitative customer engagement in late 2017 using focus groups to explore perceptions on:

- The concepts of incentives around service delivery
- Whether incentives should be financial or reputational – most participants favoured financial incentives
- Whether financial incentives should be penalty only or penalty and reward – most participants preferred penalty and reward incentives
- Whether incentive payments should be in-period (annually), at the end of five years or for a longer period of time – participants selected a mix of in-period and end-of-period.

The Challenge Panel notes that the engagement on incentives didn't cover:

- The incentive amounts proposed for each financial ODI,
- The basis of the calculation of incentives,
- Whether future customers should pay for or benefit from incentives related to the service performance affecting current customers.
- The size of the proposed asset health underperformance penalties (and any outperformance payments), and how these relate to past performance and the asset health challenges the company is facing.

The engagement showed that participants were generally comfortable with the principle of incentives. Customers supported incentives at overall plan level due to the proposed smoothing of bills.

Acceptability testing on the draft business plan showed an 80% preference for in-period incentives. This acceptability research also included the scale of annual ODIs (including C-Mex) and associated bill impact. Participants preferred a package including total ODI of plus or minus £2m per annum, equivalent to plus or minus £4 on bills, because it was felt it would encourage innovation both to keep bills low and to meet obligations.

The Challenge Panel noted that participants preferred reputational incentives to several PCs which is at variance with Bristol Water's proposals. These included customer contacts about water quality (taste and smell), raw water quality of sources and the Biodiversity Index. Bristol Water has set out in Section C3 of its business plan why it has chosen financial incentives for these measures.

The Challenge Panel considers that the research into incentives, whilst broad in nature and involving a small number of participants, was appropriate given its objectives.

Bristol Water's proposed sharing mechanism on outperformance payments has been presented to the Challenge Panel. The acceptability of the sharing mechanism has been tested with customers together with options for how it is structured. Customers are willing to accept up to £4 per year on bills for Bristol Water to invest a proportion of any outperformance payments in local community projects.

Case study - Waste Disposal Permit Compliance

Bristol Water has proposed an underperformance penalty deadband on the waste disposal PC. Although Bristol Water's target is to achieve 100%, its baseline has been forecast to achieve 96% compliance due to a new discharge consent now in place for the fisheries at Blagdon.

The EA advised the Challenge Panel that Bristol Water has to achieve 100% compliance on waste disposal and so EA can't support the deadband because legally it could be acting on any compliance less than 100%.

The Challenge Panel can understand the positions of both Bristol Water and the EA. It has been unable to reach a consensus over the deadband and so refers the issue to Ofwat for consideration and decision.

Whilst the details of the mechanism are not fully defined at present, the Challenge Panel supports it in principle as long as it is involved as an independent body monitoring its implementation throughout the period. Bristol Water has agreed that the Challenge Panel will have this role.

As a result of its work, the Challenge Panel is satisfied that all Bristol Water's proposed ODIs:

- Are appropriately categorised as financial or reputational incentives
- Have appropriate reward and penalty or penalty-only incentives
- With the exception of waste disposal compliance, contain dead-bands and caps and collars where appropriate.
- Are aligned and consistent with the results of customer research
- Have incentives values calculated using appropriate WTP values (where available) or sound judgement

Bristol Water is proposing outperformance payment caps and underperformance penalty collars for all its financial ODIs except:

- C-Mex – because the incentive design has yet to be finalised by Ofwat
- D-Mex – as for C-Mex
- WINEP compliance – because a cap and collar mechanism would not be appropriate as this is a statutory obligation

The Challenge Panel notes there has been no direct customer engagement on the caps and collars, neither in principle nor on individual ODIs so it is not possible to gauge customer support for them. However, there was some quantitative research on caps and collars at a general level. Customers supported a balanced incentive package, including the use of a general collar on the overall package. In addition, all customers who participated in the Customer Forum event in July 2018 supported the proposals to include caps and collars on the incentive package as a whole.

After having reviewed the individual caps and collars and their justifications, the Challenge Panel is comfortable with their inclusion in the proposed incentive regime.

Bristol Water is proposing reputational-only ODIs for:

- Risk of severe restrictions in a drought – Ofwat’s recommendation is that this ODI should be reputational
- Percentage of customers in water poverty – a continuation of the existing PC which incorporates a reputational incentive. Customers did not support financial incentives relating to affordability. CCWater also favoured a reputational incentive.
- Value for money – a revision to an existing PC which incorporates a reputational incentive. Customers did not support a financial incentive associated with value for money. CCWater also favoured a reputational incentive.
- Percentage of satisfied vulnerable customers - a new incentive for PR19. Customers did not support financial incentives relating to vulnerability. CCWater also favoured a reputational incentive.

Based on the above evidence, the Challenge Panel is satisfied that the reputational ODIs proposed by Bristol Water are appropriate.

All the financial ODIs proposed by Bristol Water are in-period (revenue-based). The Challenge Panel notes this is in line with Ofwat’s requirements.

As a result of the initial customer engagement on incentives, the Challenge Panel notes that participants opted for a mix of in-period and end-of-period revenue adjustments. Acceptability testing on the draft business plan showed an 80% preference for in-period incentives.

The Challenge Panel notes there was no research into why future customers should pay for/benefit from incentives related to the service performance affecting current customers. This was because all the proposed incentives are in-period.

Bristol Water has set out the rationale it has used to set incentive rates in Section C3 of its business plan. The Challenge Panel has reviewed this.

In general the ODIs have been developed using customer Willingness to Pay (WTP) information and costs allocated to outcomes from Bristol Water’s investment programme. The Challenge Panel has reviewed the WTP information but not the costs. Where Bristol Water has WTP data for a given PC it has calculated the ODI using the formula set out in Ofwat’s PR19 methodology. Where WTP data for a specific PC doesn’t exist, a broader base of evidence has been used to develop an overall incentive package including:

- Customer research on the draft business plan
- Crosschecks against Bristol Water and other companies’ ODIs from PR14;
- Cost and WTP data for proxy measures where available; and
- Information on Bristol Water’s customers’ relative priorities.

The Challenge Panel notes that in some cases Bristol Water has set additional reward levels based on the higher ranges of customer WTP, and that the penalty ranges are based on forecast costs and WTP. The updated triangulated ‘Expected’ WTP values have been used in most cases in the WTP design. The exception was leakage, where Bristol Water considered the strength of customer priority meant that WTP outweighed actual costs by a large margin, and did not reflect views that tackling leakage should reduce bills. Therefore the lower range of WTP was used and targeted where marginal cost and benefit were balanced at the point where the investment plan as a whole saw bill reductions and long-term stability. Bristol Water therefore proposes to revisit the long-term ambition for

leakage with innovation, which is appropriate given Bristol Water's position in the current industry upper quartile.

The Challenge Panel notes that, whilst in-period incentives are proposed, Bristol Water intends capping the application symmetrically at £2.5m (2017/18 prices) in any one year, with the balance rolled forward to subsequent years (or to RCV at 2025). Bristol Water considers this reflects customer views on risk and bill profiles.

In summary Bristol Water has generally used the standard formulae if it has both marginal benefits and costs or modified formulae where it doesn't have quantifiable marginal benefit figures.

The Challenge Panel notes there are no proposed enhanced incentive rates applied to common measures.

Some PCs have two tier incentives rates. These include supply interruptions and customer contacts about water quality (appearance, taste and smell). A second tier outperformance payment regime for these PCs, based on upper WTP values, is intended to provide additional incentive if performance beyond the forecast industry upper quartile or industry frontier is delivered.

The Panel hasn't reviewed the calculation of individual incentive rates as these have been assured for the company by a third party.

Bristol Water hasn't consulted customers on changes to the standard formulae of calculating ODI outperformance and underperformance payment rates.

Bristol Water sets out the range of possible bill impacts from each of its proposed ODIs (the Return on Regulated Equity (RoRE) ranges) in Section C3 of its business plan.

Information has been provided to the Panel on the overall range of ODIs and the impact on bills.

Bristol Water's proposed sharing mechanism on outperformance payments has been presented to the Challenge Panel. The acceptability of the sharing mechanism has been tested with customers together with options for how it is structured. Customers are willing to accept up to £2 per year on bills for Bristol Water to invest a proportion of any outperformance payments in local community projects.

Bristol Water's proposed bespoke resilience performance commitment is 'Population at risk from asset failure' (which looks at population centres over 10,000). This has a financial incentive (reward and penalty) with an associated cap and collar.

The Challenge Panel questioned the particular resilience challenges being faced by Bristol Water given that it has made significant investment in resilience over successive price review periods in order to improve the reliability of the network, provide greater inter-connectivity and increase the robustness of the business.

The Challenge Panel has seen that reliability of water supply is a top priority for Bristol Water's customers. This outcome came from various customer engagement and research on reliability and interruptions to supply. During the acceptability testing of the draft business plan most participants commented on protecting against interruptions to supply rather than major water supply events, with the latter appearing to be not a priority and the current level of risk to be acceptable. Bristol Water considers this was because most customers had not experienced severe interruptions, and those that had were happy with the customer services response. However, overall participants did prefer the suggested plan which includes investment in increased resilience as long as it could be delivered at a lower cost.

The Challenge Panel is satisfied that Bristol Water's proposed investment in critical mains resilience, comprising network reinforcement and increased inter-connectivity, associated with its population at risk of asset failure PC reasonably reflects the operational resilience challenges it is facing and aligns with the wishes of customers to maintain and improve water supplies.

Caps and collars have been included for the PC relating to population at risk of asset failure. A cap is justified to help ensure bill smoothing. A collar is justified on the grounds that Bristol Water already has reputational consequences from poor performance and that it ensures that the maximum penalty rate is incurred for a smaller level of underperformance.

Bristol Water has assured the Panel that the potential over performance payments on this PC do not overlap with funding received from the cost allowances.

Bristol Water's proposed asset health metrics are:

- Water quality contacts – appearance
- Water quality contacts – taste and odour
- Properties at risk of receiving low pressure
- Turbidity performance at water treatment works
- Unplanned non-infrastructure maintenance

There is evidence of customer support for these asset health metrics from current customers. Some metrics are more supported than others, for example water aesthetics and low pressure are of more obvious concern to customers than unplanned non-infrastructure maintenance.

Through attending one of Bristol Water's environmental resilience workshops the Challenge Panel saw that three resilience scenarios were used to explore how customers view the impacts of disruptive events on the community, the economy and the environment as well as the potential measures and challenges to improve resilience. An exercise was also used to investigate customers views on the trade-offs between short and long-term water resource options such as improving the water network and reducing leakage.

In its financing and bill impacts Bristol Water sought customers views on paying for things upfront (PAYG) versus spreading the cost over a long period of time. A game was used to ask customers to take on the role of a water company and as a group make finance decisions about water supply investments. The activities promoted discussion about uncertainty and risk and leaving a legacy and debt for future generations.

The five proposed asset health measure include the following financial incentives:

- Water quality contacts (appearance) – out and under-performance
- Water quality contacts (taste and odour) - out and under-performance
- Properties at risk of receiving low pressure - out and under-performance
- Turbidity performance at water treatment works - under-performance only
- Unplanned non-infrastructure maintenance - under-performance only

Bristol Water's customer engagement on incentives included explanation of the total amount of incentive payments, not on individual PCs. Therefore it hasn't explained directly to its customers the size of its individual asset health underperformance penalties (and any outperformance payments), and how they relate to past performance and the asset health challenges it is facing.

Bristol Water has set out the basis of its financial incentives for its asset health metrics in Section C3 of the business plan. This includes the linkage to customer engagement and the asset health challenges it is facing. It also sets out the size of its individual asset health incentive payments.

Whilst consideration of historic performance was used by Bristol Water in many cases to set future service targets, it was not used to set incentive rates. Incentives were set using WTP, investment costs and cost benefit analysis.

The Challenge Panel notes there are no proposed enhanced incentive rates applied to the proposed common PCs.

In summary, the Challenge Panel has rigorously examined the proposed ODIs and their impact on customers and investors. There is a fair sharing of risk for capital expenditure between the customer and the company. The balance between penalties and rewards in service performance ensures that the targets set by Bristol Water are stretching and ambitious.

10. Cost Adjustment Claims

Bristol Water submitted five cost adjustment claims for consideration by Ofwat in May 2018:

- Purchase of Water from the Canals and River Trust
- Water Treatment Complexity
- Prevailing Wages in the Bristol Water Supply Area
- Network age and materials
- Congestion in the city of Bristol

Bristol Water explained the background to each claim to the Challenge Panel and that it will find out whether its claims have been accepted by Ofwat after submission of its business plan.

Ofwat seeks assurance on project-related cost adjustment claims in terms of:

- The evidence of customer support for projects
- Whether the proposals relating to the claims deliver outcomes that reflect customers' priorities, identified through customer engagement.
- Evidence that proposals relating to the claims represent the best value for customers in the long term

The Challenge Panel notes that Bristol Water's cost adjustment claims relate to costs associated with the nature of its asset base or its operating environment. None are associated with specific projects.

Bristol Water engaged with its Customer Forum on local company-specific challenges including congestion in Bristol city, the age of its network, the complexity of its treatment works and local wages.

The purpose of the event was to understand customers' views on specific aspects of Bristol Water's operations that differentiate it from other water companies and how this can affect costs. 10 potential claim areas were explored. Bristol Water presented the results to the Challenge Panel.

The consultation was on which special cost factors should be submitted to Ofwat. The Challenge Panel noted that some customers supported factors that were not submitted as they did not meet Ofwat's materiality criteria.

Customers were generally agreed that some allowance in their bills should be made for traffic congestion, network age, treatment works complexity and local wages. Views were more mixed that the issues are outside management's control and should be included in cost allowances as follows:

- Water Treatment Complexity – limited agreement
- Prevailing Wages in the Bristol Water Supply Area – limited agreement
- Network age and materials – limited agreement
- Congestion in the city of Bristol – limited agreement

Bristol Water did not consult customers on whether its claims deliver outcomes that reflect customers' priorities or represent value for money in the long term as it considered its claims relate to underlying cost factors rather than specific projects. The Challenge Panel agreed with this approach.

Bristol Water has explained to the Challenge Panel that it is negotiating future abstraction charges from the Gloucester-Sharpness Canal with the Canal and Rivers Trust. The current uncertainty around these charges poses a significant financial risk to Bristol Water and potentially to customers' bills. The future abstraction charges will not be agreed until after the business plan is submitted and potentially the Final Determination made by Ofwat.

The Challenge Panel notes that Bristol Water has not built any cost increase into its business plan to reflect this risk as negotiations are ongoing and that arbitration may ultimately determine the future abstraction cost. Bristol Water proposes to use the Ofwat Notified Item process, including the associated scrutiny from Ofwat, to deal with and recover any significant additional future costs and their impact on bills.

The Challenge Panel notes that the congestion case from the early submission to Ofwat was withdrawn for the final business plan because it proved to be immaterial. The remaining four claims are included in the final business plan.

11. Other Areas

11.1 Corporate and Financial Structures

Bristol Water has consulted its customers indirectly on its corporate structure as part of its PR19 planning. Research into Bristol Water's current privately-financed ownership arrangements was undertaken in the context of a nationalisation of the industry. Customers expressed support for the current arrangements. The Challenge Panel is aware that some water companies have received criticism of their financial structures and levels of gearing. During attendance at the Customer Forum, the Challenge Panel was aware of some anti-private, anti-profit and dividend sentiment but these views were very much in the minority and there does not appear to be evidence of significant unease around Bristol Water's governance structure.

Bristol Water engaged with customers on financing issues such as gearing, Pay As You Go (PAYG) and Regulatory Capital Value (RCV) run off rates, that is paying for investment now or spreading the cost and how much of the bill should be financing costs. Whilst the Challenge Panel didn't have the opportunity to comment on the research materials in advance, it did note that the current bill was presented in the context of its primary building blocks (including interest and profit) to obtain opinions on the cost of finance and level of profit both before and after a game was held. The outcome was that all participants preferred to borrow more to keep bill as low as possible but didn't want financing costs to become a dominant part of the bill.

The Challenge Panel enquired about Bristol Water's current and proposed future gearing level and notes that it is planned to stay broadly static at around 62.5% from now until 2024/25. The Challenge Panel notes that in the Ofwat early view assessment (as at 31 March 2017) of gearing levels for the cost of capital at PR19, Bristol Water has the lowest level of gearing of all the water only companies. Consequently, the sharing of outperformance associated with high gearing does not arise currently for Bristol Water. Gearing may rise slightly after 2024/25 but decisions on this will be taken by the Bristol Water Board nearer the time.

The Challenge Panel also discussed Bristol Water's sharing proposal to reinvest up to 50% of the small company premium, particularly the selection of the proposed performance triggers. The Challenge Panel is content that the performance triggers reflect Bristol Water's business priorities as well as customers' interests. The Challenge Panel notes that 50% of the small company premium equates to £1.50 on bills or a £750,000 investment. It has suggested to Bristol Water that should ask customers at the time about the reinvestment areas they would favour.

11.2 Financeability

No financeability constraints have been identified by Bristol Water.

11.3 Bill Profiles

Bristol Water has sought customer opinion on bills and bill profiles at various points during the engagement for PR19.

The Challenge Panel notes that a common theme throughout the engagement is that customers require bills that are steady and affordable.

During the testing of business plan options Bristol Water presented different service areas with customers, different options for investment in those service areas (including the speed of investment), and the resulting impact on customer bills. Scenario games were used to see whether customers' opinions on the investment options changed with different bill profiles.

The Challenge Panel was pleased to see that participants were provided with information on Bristol Water's bills in relation to other water companies as part of this engagement. It was also keen to ensure bill information was presented in an understandable way and in real terms.

Bristol Water also used additional deliberative research to understand whether and how customer priorities changed to different bill levels that were not linked to service changes, as well as the cost of

packages of service improvements. This research was used to test the triangulation of the range of WTP studies and used to develop the packages of plan options for the consultation.

The Challenge Panel noted that a similar number of participants chose the proposed slower plan as the suggested plan. However it agreed with Bristol Water's conclusions from its research that future bills should be no higher than in the suggested plan and that a plan with a lower bill levels (but containing the suggested service levels) would be most likely to be accepted by customers.

11.4 Accounting for Past Delivery

Bristol Water highlighted two pieces of customer research to the Challenge Panel that it considers provide evidence for its proposed reconciliations for the 2015-20 period and how well it has followed the PR14 reconciliation rulebook methodology. These are:

- The financial modelling used for the bill levels in the acceptability testing takes account of the impact of the PR14 reconciliations, so customers are taking these into account in their assessment; and
- The PAYG bill profile research that expressed a preference for smooth bills, which is how the PR14 adjustments are being applied in 2020-25.

Bristol Water informed the Challenge Panel that the combined effect of the adjustments is £1.8m a year in customer's favour (a bill reduction of approx. £2.64 per household customer per year).

11.5 DWI support

The DWI's statement on Bristol Water's drinking water quality proposals for PR19 is given in Appendix 4. The DWI has supported four schemes in its statement. The Challenge Panel understanding is that two schemes may not proceed as expected in the DWI statement.

The Challenge Panel understands that the DWI supported Cheddar Water Treatment Works scheme is unlikely to go ahead in AMP7, unless there is a significant increase in the number of complaints, as Bristol Water are continuing with its trials to determine the correct solution. The Challenge Panel understands that Bristol Water is considering a less expensive solution of undertaking the scheme at the same time as its wider maintenance scheme due at Cheddar after 2025. Bristol Water continues its discussion with the DWI.

The Challenge Panel understands that the Bristol Water Metadehyde catchment work at Purton will continue. The revision that the DWI refer to requires a change to the ministerial guidance which would take some time to implement.

The Challenge Panel is satisfied that Bristol Water is currently taking the most appropriate course of action as regards to its customers.

11.6 The Initial Assessment of Business Plans (IAP)

These are primarily Ofwat's Business Plan tests. The Panel's overall opinion on Bristol Water's business plan is provided in Section 12 of this report.

12. Conclusions

12.1 The Challenge Panel's Review

The Challenge Panel has a diverse membership representing various customer and stakeholder groups. It is independent of Bristol Water.

The Challenge Panel has been reviewing and challenging Bristol Water's 2020-2025 business plan since late 2016. It established a number specialist sub-groups to review aspects of the plan in detail, including customer engagement, PCs and ODIs and assurance. The Challenge Panel has followed Ofwat's guidance and has addressed the specific questions Ofwat has asked CCGs to address.

There has been a positive, professional and transparent relationship and interaction between Bristol Water and the Challenge Panel throughout the process. An excellent working relationship with the Challenge Panel has existed at executive director and senior manager level. In addition, Bristol Water's Board responded well to challenges on its engagement with the Panel and on its corporate responsibilities.

All the Challenge Panel's challenges have been logged and the responses from Bristol Water reviewed. Many challenges resulted in Bristol Water changing its engagement methodologies and materials and the presentation of information to its customers. All the Challenge Panel's information requests have been satisfied and there are no material issues outstanding.

The Challenge Panel has had real influence over the plan as a result of its work. In particular the Panel has ensured the customers' voice has been well tested and heard and that customers' needs and priorities are reflected throughout the business plan.

12.2 Customer Engagement

Bristol Water's Customer Engagement Framework was well planned and incorporated both ongoing and bespoke research activities. The Framework was adapted and supplemented by additional research activities in response to clarification of Ofwat's PR19 requirements, challenge from the Challenge Panel and other stakeholders and the need to further explore and refine outcomes from the initial research.

Engagement has been two-way and transparent and participants were provided with accurate and sufficient information on Bristol Water's current performance relative to its peers.

The Customer Engagement Framework incorporated some innovative and ground-breaking research activities including innovative willingness to pay study methodologies, the use of web-based tools including an online game, and the establishment of a Customer Forum and a Young Persons Forum.

An appropriate range of customers has been consulted in order to understand the needs and requirements of different groups. This was informed by effective customer segmentation to ensure as many different customer groups as possible could be involved. The number of customers engaged with at PR19 is an order of magnitude greater than at PR14.

Bristol Water made considerable effort to contact hard to reach customers and those in vulnerable circumstances and it was successful in doing so.

There has been effective engagement with future customers both in shaping and testing the business plan.

Long-term issues such as operational resilience and bill levels and profiles have been researched.

There is evidence of the use of co-creation of plans and policies and of methods of co-delivery of solutions with customers and stakeholders. Particularly good examples of this included Bristol Water's Youth Board, engagement on special cost factors, engagement on the proposed vulnerability-related PC and commitments to work jointly with environmental stakeholders to deliver co-ordinated messages on water, waste and energy efficiency.

Throughout the research the Challenge Panel saw that customers placed high priority and value on service areas including supply reliability, adequacy of water pressure, the aesthetics of water,

affordability, reducing leakage and, later in the research, protecting and enhancing the natural environment. Bristol Water engaged its customers on all of these areas and that related levels of service options presented were soundly based, realistic and relevant to the customer base. Appropriate trade-offs between different levels of service improvements and changes in the level of the bill were also presented. The key options included the level of leakage reduction, environmental improvement, the timing of investment and provision of assistance to customers in vulnerable circumstances.

Customer willingness to pay valuations have been obtained for various service areas using a range of techniques, some of which were innovative and independently peer-reviewed. Valuations for the highest customer priority Performance Commitments have been obtained and others have been derived from the research at a higher, service package level.

A methodology to triangulate the various sources of valuation information for each service area consulted on was developed and applied. The initial results were deemed to have low confidence in some cases so further WTP research was undertaken to generate values suitable for cost benefit analysis and to calculate incentive rates for the 26 proposed Performance Commitments.

The process for deriving service targets and incentives from the valuations obtained for the majority of the Performance Commitments has been made clear to the Challenge Panel.

The acceptability research on the draft business plan obtained opinion on three levels of service (slower, preferred and faster) and associated bills and was designed primarily to inform the final Plan. It focused on the Bristol Water's strategic outcomes and the resulting bill impacts, rather than the detail of individual PCs within them. It also sought views on the overall level of ambition in the draft plan, overall bill levels and the level of vulnerability assistance.

The Challenge Panel noted that the preferred plan was marginally more acceptable than the slower plan. It did observe there were some anomalies and differences at service package level, for example interruptions to supply and water use, but accepted the Bristol Water Board's view that a plan with a lower bill level with the suggested (preferred) service levels is more likely to be acceptable overall to customers.

A high level of acceptability of the final business plan has been obtained across all components of the research, both quantitative and qualitative. The Plan was also deemed to be affordable by the vast majority of participants.

12.3 Affordability and Vulnerability

Bristol Water's proposed affordability strategy for the next five years is based upon a number of initiatives, the most noticeable of which include a one-off bill reduction in 2020 of around 5% followed by inflationary increases until 2025 and a commitment to keep bills low thereafter. It also includes commitments to further reduce the number of customers in water poverty and to improve the use of data and processes to reduce debt and increase promotion of social tariffs.

The Challenge Panel reviewed and challenged the strategy as well as the customer engagement that informed it. It considers the company's approach to assessing affordability, both through its bespoke PR19 research and its ongoing engagement with customers, has been both efficient and effective.

As a result of its challenges, the Challenge Panel considers the company's approach to assessing affordability have been both efficient and effective and a good understanding of what affordability looks like for customers has been obtained.

Bristol Water's plans to address affordability represents a step increase over its current activities and the Challenge Panel welcomes these.

The Challenge Panel considers the proposed affordability-related PCs include stretching targets and should provide a good mechanism for monitoring progress. The proposed affordability strategy represents a step change improvement to its current approach and the Challenge Panel is pleased to see that Bristol Water is already making plans to ensure its delivery.

The key components of Bristol Water's vulnerability strategy for 2020 to 2025 includes using data wisely, increasing awareness and improving the customer journey. It also includes a significant increase in the help provided to customers in vulnerable circumstances and an ongoing Affordability Action Plan implemented in conjunction with Wessex Water.

The Challenge Panel recognises that the key strands of the vulnerability strategy align with Ofwat's principles as set out in its Vulnerability Focus report published in February 2016. The Challenge Panel is also satisfied that Bristol Water strives to provide excellent service to all its customers, including those who find themselves in vulnerable circumstances.

The Challenge Panel reviewed and challenged the proposals to address customer vulnerability and to test whether there was adequate and appropriate customer support for them. It is satisfied that there has been effective and targeted ongoing and bespoke engagement on vulnerability.

Bristol Water's plans to help customers in vulnerable circumstances represents a significant increase over its current activities and the Challenge Panel welcomes this. The plans are designed to be targeted and efficient and the Challenge Panel agrees if well implemented they should be effective. They should also increase the accessibility to Bristol Water's assistance schemes.

Bristol Water's intentions to establish partnerships with third party organisations are commendable but will require considerable effort. The Challenge Panel has seen that Bristol Water is already making plans to ensure the delivery of its vulnerability plans.

The Challenge Panel considers the proposed vulnerability-related PC includes a stretching target and should provide a good mechanism for monitoring progress.

12.4 Performance Commitments and Service Targets

26 PCs and associated service targets for 2020-2025 are proposed by Bristol Water and all have been reviewed and challenged by the Challenge Panel.

Most of the PCs and some service targets have been specified or suggested by Ofwat and several relate to statutory water quality and environmental obligations.

Bristol Water's customer engagement on its PCs commenced with research based on information from the development of PR14 combined with ongoing feedback from customers. Further research was undertaken into specific service areas including resilience, water efficiency, demand reduction, affordability and vulnerability, and company-specific issues such as cost adjustments and financing costs. The results were used to refine the strategic outcomes and to develop the PCs. Business plan options were then tested and this work enabled the development of some indicative service targets.

Bristol Water is proposing PCs covering the service areas most important to its customers. These include supply reliability, adequacy of water pressure, the aesthetics of water, affordability, reducing leakage and protecting and enhancing the natural environment. Bespoke PCs, some mandated by Ofwat, are included and Bristol Water has used the results of its customer engagement to define these and the associated service targets, either directly or by using reasonable judgement on issues where customers had not been consulted.

Four of the bespoke PCs are specific to Bristol Water. The Challenge Panel is pleased to see that these are concerned with value for money, affordability, vulnerability and community satisfaction - areas that are relevant to and aligned with customers' priorities and Bristol Water's aim of being a local, community-focused company.

Bristol Water did not consult its customers on the acceptability of individual PC service targets and the level of stretch associated with them. However, it tested the customer acceptability of its draft plans and rate of service improvement at service outcome and related package level (covering 11 PCs).

The Challenge Panel has assessed the individual PC service targets and the level of stretch associated with them.

In many cases Bristol Water is targeting to achieve industry upper quartile performance by 2024/25 and there is evidence of push from customers in setting this aim. The Challenge Panel has reviewed

where upper quartile performance isn't targeted and understands and accepts the reasons for this. It is satisfied that customers should not lose out as a result.

As a result of its review and challenges, the Challenge Panel considers the initial service levels and service targets for all but one of the proposed PCs to be based upon robust information and/or sound judgement, to be in line with its statutory and regulatory obligations and to be stretching. The proposed service targets relating to supply interruptions and leakage reduction are particularly stretching.

The ambition associated with the Biodiversity Index (BI) service target and proposed outperformance threshold has proved difficult for the Challenge Panel to judge due to limited information provided by Bristol Water. However, Bristol Water has committed to producing a detailed BI action plan and agreed with that an example BI case should be presented to the Panel and other stakeholders for review after the Business Plan is submitted. It was also agreed that there is a need to design and implement a BI AMP7 performance monitoring mechanism that involves the Challenge Panel.

The Challenge Panel remains committed to having a BI PC in AMP7 as the Bristol Water customer engagement research rates environmental improvements to Bristol Water land holdings as important. In successive Challenge Panel meetings, the environmental regulators have expressed concerns about whether the proposed BI PC reward threshold is sufficiently stretching, and the Challenge Panel members have not disputed the issues raised. However, whilst there may be a limited amount of data to robustly defend the proposed reward target, all agree that an acceptable process, based on the BI PC, can be found that would benefit both the customer and the environment.

12.5 Outcome Delivery Incentives

Bristol Water's 26 proposed PCs each have an associated Outcome Delivery Incentive (ODI), either financial or reputational.

The Challenge Panel has reviewed and challenged the basis of each ODI including the justification for its categorisation as financial or reputational, the level of incentive, any associated performance dead-bands, caps and collars and the degree of customer support for each ODI where available.

Bristol Water has determined its ODIs in accordance with Ofwat's methodology in most cases. WTP values have been used to calculate incentive rates where possible. The Challenge Panel has challenged where the Ofwat methodology hasn't been followed and is satisfied and comfortable with Bristol Water's approach in these cases.

Bristol Water undertook qualitative customer engagement to explore perceptions on the concept of incentives for service delivery. The engagement explored whether incentives should be financial or reputational, penalty only or reward and penalty, the timing of incentive payments, the overall scale of incentives and their impact on bills. It didn't cover the incentive amounts proposed for each financial ODI.

The engagement showed that participants were generally comfortable with the principle of incentives. Financial incentives were generally preferred. Acceptability testing on the draft business plan showed strong preference for in-period rather than end-of-period incentives and a limit on the scale of annual incentives.

The Challenge Panel considers that the research into incentives, whilst broad in nature and involving a small number of participants, was appropriate given its objectives.

There is a lack of consensus between the Panel and Bristol Water on the level of ambition regarding the Biodiversity Index and the imposition of a deadband on waste disposal compliance. A programme of work is planned by the Company to ensure that performance commitments in PR24 linked to biodiversity protection and enhancement are fully informed by a thorough assessment of what is feasible alongside the limitations of operational constraints. Both commitments, however, have a limited material impact on customers in the context of the overall business plan.

As a result of its work, the Challenge Panel is satisfied in material terms that Bristol Water's proposed ODIs:

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- Are appropriately categorised as financial or reputational incentives
 - Have appropriate reward and penalty or penalty-only incentives
 - Contain dead-bands and caps and collars where appropriate.
 - Are aligned and consistent with the results of customer research
 - Have incentives values calculated using appropriate WTP values (where available) or sound judgement

Bristol Water's proposed sharing mechanism on outperformance payments has been presented to the Challenge Panel. The Challenge Panel considers it to be appropriate and aligned with Bristol Water's local and community-focused objectives. The acceptability of the sharing mechanism has been tested with customers together with options for how it is structured. Customers are willing to accept up to £2 per year on bills for Bristol Water to invest a proportion of any outperformance payments in local community projects.

12.6 Cost Adjustment Claims

Bristol Water submitted five cost adjustment claims to Ofwat for consideration in May 2018 and it also presented these to the Challenge Panel.

The Challenge Panel notes that the claims relate to costs associated with the nature of its asset base or its operating environment. None are associated with specific projects.

Bristol Water engaged with its Customer Forum on several local and company-specific challenges relating to its cost adjustment claims. Customers were generally agreed that some allowance in their bills should be made for these issues but views were more mixed that the issues are outside management's control and should be included in cost allowances.

Bristol Water did not consult customers on whether its claims deliver outcomes that reflect customers' priorities or that they represent value for money in the long term as it considered its claims relate to underlying cost factors rather than specific projects. The Challenge Panel agreed with this approach.

The Challenge Panel is aware of Bristol Water's ongoing negotiation of future abstraction charges from the Gloucester-Sharpness Canal with the Canal and Rivers Trust. The current uncertainty around these charges poses a significant financial risk to Bristol Water and potentially to customers' bills. The future abstraction charges will not be agreed until after the business plan is submitted and potentially the Final Determination is made by Ofwat. The Challenge Panel notes that Bristol Water has not built any cost increase into its business plan to reflect this risk and proposes to use the Ofwat Notified Item process, including the associated scrutiny from Ofwat, to deal with and recover any significant additional future costs and their impact on bills.

12.7 Other Areas

Bristol Water hasn't consulted its customers directly on its corporate structure as part of its PR19 planning. However it did engage with customers on its current privately-financed ownership arrangements and financing issues such as gearing, Pay As You Go (PAYG) and Regulatory Capital Value (RCV) run off rates, that is paying for investment now or spreading the cost and how much of the bill should be financing costs. The Challenge Panel noted the outcome was that participants supported the current financing arrangements, preferred to borrow more to keep bill as low as possible but didn't want financing costs to become a dominant part of the bill.

The Challenge Panel discussed Bristol Water's sharing proposal to reinvest up to 50% of the small company premium, particularly the selection of the proposed performance triggers. The Challenge Panel is content that the performance triggers reflect Bristol Water's business priorities as well as customers' interests and has suggested to Bristol Water that should ask customers at the time about the reinvestment areas they would favour.

Bristol Water sought customer opinion on bills and bill profiles at various points during the engagement for PR19.

The Challenge Panel noted that a common theme throughout the engagement was that customers require bills that are steady and affordable. It considers that the proposed bill reduction 2020/21, followed by flat bills in real terms to 2024/25, go a long way to meeting these needs and is a good outcome for customers.

12.8 Overall Assessment of the Business Plan

As a result of its review and challenge, the Challenge Panel considers that Bristol Water's business plan is grounded in very sound customer engagement, the results of which can be seen throughout the plan and in particular in the proposed outcomes, promises, service commitments and targets.

Bristol Water has gained a good understanding of its customers' priorities, needs and valuations through its customer research. The business plan includes commitments in areas of service that customers have said they value and prioritise and at a price they find affordable. It also includes commitments to meet all statutory and regulatory obligations.

The proposed service commitments are aligned with Bristol Water's strategic objectives which are to provide excellent customer service, safe and reliable water supplies and local and community resilience. Performance targets are particularly stretching in areas where customers priorities lie. In other areas Bristol Water has struck a reasonable balance between cost and benefit.

Bristol Water's plans to ensure its services remain and become increasingly affordable and to further support customers in vulnerable circumstances are more ambitious and extensive than current activity in these areas. The Challenge Panel welcomes these initiatives.

Appendices

Appendix 1

Glossary

AIM	Abstraction Incentive Mechanism
AM	Aide Memoire
AMP	Asset Management Plan
AMP6	Asset Management Plan 6 (2015-2020)
AMP7	Asset Management Plan 7 (2020-2025)
BI	Biodiversity Index
BW	Bristol Water
BWCP	The Bristol Water Challenge Panel
Caps and Collars	Upper and lower limits of performance beyond which no financial incentive applies
CCG	Customer Challenge Group
CCWater	The Consumer Council for Water
CEO	Chief Executive Officer
CESG	Customer Engagement Sub-Group
CMA	Competition and Markets Authority
C-Mex	Customer Measure of Experience
CRI	Compliance Risk Index
Deadband	A range either side of the performance target within which no financial incentive applies
Defra	Department for Environment, Food and Rural Affairs
D-Mex	Developer Measure of Experience
DWI	Drinking Water Inspectorate
EA	Environment Agency
FD	Final Determination (Ofwat December 2014)
IAP	Initial Assessment of Plans
NE	Natural England
NERA	National Economic Research Associates
ODI	Outcome Delivery Incentive.
Ofwat	Water Services Regulation Authority - The economic regulator of the water sector in England and Wales
PAYG	Pay As You Go

PC	Performance Commitment.
PR14	Price Review 2014
PR19	Price Review 2019
PR24	Price Review 2019
RCV	Regulatory Capital Value
RoRE	Return on Regulated Equity
SSSI	Site of Special Scientific Interest
WRMP	Water Resources Management Plan
WINEP	Water Industry National Environment Programme
WISER	Water Industry Strategic Environmental Requirements
WTP	Willingness to pay
WTW	Water treatment works

For information on the economic regulation of the water industry in England and Wales including the setting of prices and Ofwat's expectations of CCGs, the reader is directed to the regulator's website www.ofwat.gov.uk.

Appendix 2

Challenge Panel Terms of Reference

Approved at the meeting of the Challenge Panel on 21 September 2016

1. Role

- 1.1. The Bristol Water Challenge Panel is an independent body that scrutinises and reports to Ofwat, the Bristol Water Board and its customers, on Bristol Water's wider engagement strategy with its customers and how this drives decision making in company performance and its future company business plans.
- 1.2. Ofwat defines the role of Customer Challenge Groups (CCGs) to "provide independent challenge to companies and provide independent assurance to us on: the quality of a company's customer engagement; and the degree to which this is reflected in its business plan"
- 1.3. As interested and expert stakeholders, the membership of the Challenge Panel will be well placed to consider the evidence of customers' views and the company's response. Wider consultation directly with customers will be achieved through representative pieces of customer research and open consultations. In carrying out its role, the Challenge Panel will compare the performance and plans of Bristol Water with that of other water companies and provide challenge to the company by using local, regional, national and international benchmarks in customer engagement.

2. Purpose

- 2.1 The primary purpose of the Challenge Panel is to act as an independent body to ensure that the customer voice remains at the heart of Bristol Water's decision making.
- 2.2. Ofwat states that "CCGs should focus on those issues that customer engagement is most likely to genuinely influence. We have provided more guidance on the issues that CCG reports should include and made it clear we do not expect CCGs to endorse a company's overall plan."
- 2.3. The Challenge Panel will provide independent reporting to Ofwat, the Bristol Water Board and the public on the performance of Bristol Water against its 2015-2020 Business Plans. It will do this by facilitating inclusive discussion in an open and transparent manner.
- 2.4. The Challenge Panel will challenge, comment and advise the company on its plans to educate, inform and consult its customers on the development of Bristol Water's 2020-2025 Business Plan. The panel's work will ensure that the outcomes and service levels customers expect from their water services are reflected in the company's plans as well as any incentives around delivering higher levels of service.

3. Activities

The work of the Challenge Panel falls into several main functions:

3.1. Delivery of the 2015-2020 Bristol Water Business Plan

- Monitor and challenge Bristol Water’s delivery of its performance commitments (and any associated penalties and rewards set by Ofwat), charges to customers and data assurance processes to ensure a proportionate and transparent approach that involves customers in service delivery. The performance commitments are compared with others in the water sector.
- Understand and challenge the recovery of any underperformance and the use of any ‘out performance’ revenue from such mechanisms as incentives, outcome return on regulatory equity, etc.
- Challenge, monitor and input into how Bristol Water communicates with its customers on performance, how it interprets the responses from customers, and how this is reflected in its long term strategy.
- Provide an independent annual report to Ofwat, the Board of Bristol Water and the public on how Bristol Water has delivered against its performance commitments for the benefit of its customers.

3.2. Production of the 2020-2025 Bristol Water Business Plan

- Review, challenge and comment on the development of 2020-25 Business Plan in terms of representing the needs of both customers and the environment.
- Monitor, challenge and input into Bristol Water’s customer policies, its ongoing research/engagement programme with customers to provide a robust, balanced and proportionate evidence base across its diverse customer base.
- Advise and challenge on the phasing of delivery of outcomes to maximise the affordability and acceptability of the overall business plan.
- Engage and challenge longer-term views around risk and resilience.
- Challenge regulatory compliance with regard to the environment from a customer perspective.
- Challenge Bristol Water to work with other water companies in areas of overlap for the wider interest of the customers, the environment and water resources in the Bristol Water area.
- Consider the trade-off between different levels of service and bill profiles; specific major schemes to improve service; to ensure the views of Bristol Water’s customers are reflected in the business plan.

3.3. Business and Domestic retail markets

- Review and comment on the proposals for the possible Domestic retail market as they become available.
- Review the communication with customers.
- Respond to Ofwat (and other) consultations as appropriate.
- Monitor Bristol Water risk assessment programme where it imposes on customer priorities and preferences.

4. Membership

4.1. A Chair and Deputy Chair have been appointed to the group following a selection process. The Chair and Deputy Chair will each be paid a stipend.

4.2. Ofwat requires that CCG membership should reflect local circumstances and challenges and include a representative from the Consumer Council for Water (CCWater). Chairs should not represent particular organisations or groups of customers. The environmental and drinking water quality regulators should play a significant role informing CCG discussions and CCG reports should highlight any concerns raised about

the ability of the proposed plan to meet statutory obligations.

4.3. The Challenge Panel will represent both Bristol Water's domestic and retail customers, with members invited from:

- CCWater
- Local Authorities elected representatives
- Natural England
- Avon Wildlife Trust and/or other environmental charities.
- Citizens Advice Bureau and/or other similar bodies dealing with vulnerable customers.
- Environment Agency
- Local Academia
- Local Businesses
- Other local customer representatives as appropriate

Independent members and charity organisations will be paid a day rate for attendance at meetings. All members will be reimbursed for reasonable expenses incurred in relation to their membership of the Challenge Panel.

The Environment Agency is a member of the Challenge Panel and is represented by Jeremy Bailey, National River Basin Management Service, National Operations. As a contributor to the Panel and its overall aims and outcomes the function of the Environment Agency as the statutory regulator and enforcing authority in respect of Bristol Water Company remains unaffected and it will continue to take all regulatory measures, as appropriate, under any circumstances, in accordance with its published guidance and policies.

4.4. The Challenge Panel will ensure that Bristol Water consults all sections of the company's customer base, including minority Ethnic groups, vulnerable and hard to reach customers.

4.5. Challenge Panel Members are responsible for fully participating in delivering the work of the challenge panel. Members are expected to attend all the meetings or send an appropriate substitute or provide input in advance if unable to attend. All members are welcome to attend any sub-group meeting. Topic specialists will be invited to attend meetings at the discretion of the Chair to aid the members in their understanding of that topic.

4.6. Independent non-executive members of the Bristol Water Board are welcome to attend any meeting of the Challenge Panel or its sub group.

5. Meetings

5.1. Frequency

- Meetings of the Challenge Panel with Bristol Water will be held at approximately three monthly intervals, with a minimum of four meetings per calendar year. Additional Challenge Panel meetings will be arranged as appropriate depending upon the workload.
- Private meetings of the Challenge Panel without Bristol Water will be held at the beginning and end of each regular meeting. Additional private meetings of the Challenge Panel will be arranged as required.

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- Between meetings, the Challenge Panel will be provided with information updates and/or asked for input by email.
 - Bristol Water will provide telephone conference facilities for the use by members between the routine meetings to discuss urgent items as required.

5.2. Sub Groups

- The Challenge Panel may establish ad hoc sub-groups or task and finish groups to consider specific topics where it is considered by the membership to be beneficial to fulfilling the purpose of the panel.
- Each sub-group will usually be chaired by the Deputy Chair, its terms of reference will be set by the main Challenge Panel and meeting dates agreed with the Chair.
- Sub-groups will provide feedback to the next Challenge Panel meeting, including their recommendation for discussion by the main Challenge Panel. Decision making authority remains with the Challenge Panel.

5.3. Support and Administration

- Secretariat services will be provided to the Challenge Panel to enable the Challenge Panel to fulfil its role and functions in an independent manner.
- The agenda and papers (including the written results of actions from the previous meeting) for each meeting will be uploaded to a website hosted by Bristol Water, not less than five working days before each meeting. Members of the group will be provided with access to the website, and will be expected to have read all papers before the meeting.
- Minutes of the meeting will be taken and a draft checked by the Chair before being distributed no later than two weeks after each meeting.
- Confidential items will be duly marked in the Minutes for member's information and redaction.
- Bristol Water will provide a regular update on matters concerning the Challenge Panel work areas.
- Challenge Panel welcomes Bristol Water informing us about specific topics with a wider set of 'interested' third parties in preparation for our deliberations.

5.4. Agendas

The Chair, in consultation with Bristol Water, will determine meeting agendas. Standard items will normally include:

- Private sessions
- Minutes and matters arising from previous meetings
- Review of the Challenge Log outstanding items
- Quarterly update on the delivery of performance commitments
- Update of ongoing customer research and engagement
- Feedback from sub-groups

5.5. Meeting Evaluation

In its presentations to the Challenge Panel, the members would expect Bristol Water to report against the following four criteria:

- How it is customer led
- Impact on customers
- How it relates to Best Practice and Innovation within the industry
- Ethical Issues, eg differing 'willingness to pay' methods, intergenerational concerns, etc.

Informal scoring of Bristol Water's presentations will be carried out as well as of the Challenge Panel's own performance at the meeting.

6. Outputs

6.1. The principal published output will be the Challenge Panel's Independent report to Ofwat and the public to accompany Bristol Water's 2020 Business Plan. This report is expected to be published in September 2018.

6.2. Other published outputs of the Challenge Panel will be:

- Minutes of all main and sub group meetings.
- Annual report on the delivery of Bristol Water's commitments to its customers.
- Annual report on the operation of the Challenge Panel during the previous year.
- The Challenge Panel will submit a second independent report if Bristol Water does not achieve 'enhanced' status as a result of Ofwat's Risk Based Review of PR19 Business Plans.

7. Review of Terms of Reference

The Terms of Reference for the Challenge Panel shall be reviewed and agreed by the membership from time to time, including a formal review in light of any further information published in the Ofwat Methodology due to be published in December 2017.

Appendix 1: Non-exhaustive list of issues for CCG reports to include:

- Has the company developed a genuine understanding of its customers' priorities, needs and requirements – and where appropriate customer valuations – drawing on a robust, balanced and proportionate evidence base? Has the company engaged with customers on the issues that really matter to them?
- Where appropriate, has the company engaged with its customers on a genuine and realistic range of options? For example, in relation to a need to rebalance supply and demand, this might include increasing its own capacity, purchasing water from another company or demand management options. Where appropriate, has the company considered how customers could help co-create and co-deliver solutions to underlying challenges?
- Has customer engagement been an on-going, two-way and transparent process, where companies are informing their customers as well as soliciting feedback from them?
- Has the company effectively engaged with and understood the needs and requirements of different customers, including those in circumstances that make them vulnerable? Has the company considered the most effective methods for engaging different customers, including those that are hard to reach?
- Has the company effectively engaged with its customers on longer term issues, including resilience, impacts on future bills and longer-term affordability? Does the business plan adequately consider and appropriately reflect the potential needs and requirements of future customers? Wherever appropriate, has the company engaged with its customers on the long-term resilience of its systems and services to customers?
- Has the company effectively informed and engaged with customers on its current levels of performance and how does this compare to other companies in a way customers could be expected to understand?
- Has the evidence and information obtained from customers (including through the company's day-to-day contacts with customers) genuinely driven and informed the development of the

business plan to benefit current and future customers? What trade-offs (for example between different customers) have been identified and how has the company proposed to deal with these?

Appendix 2: Governance

Ofwat states that “To build trust and legitimacy we would like to see an increased focus – by companies and the CCGs themselves – on CCG governance and funding process transparency.”

Chair and Deputy Chair

- The Chair and Deputy Chair have been appointed following an open interview process.
- The role of the Chair and Deputy Chair is to encourage full, frank and inclusive debate, identify areas of consensus, summarise differences and distil possible solutions emerging or needing to be investigated further.
- The roles will be sufficiently independent from Bristol Water to be able to ensure they can challenge effectively, to give proportionate assurance to both Ofwat and Bristol Water customers.
- The Chair and Deputy Chair should ensure that they act independently of any affiliations with other bodies, such as parent organisations, and oversee the group in an objective manner.
- The Chair will have regular meetings with an independent non-executive member of the Bristol Water Board to provide feedback and assurance.

Members

- Members will be required to formally approve the Challenge Panel Terms of Reference.
- A work programme and protocol will be agreed with members of the group.

Independence

The governance that enables the independence of the Challenge Panel consists of:

- An independent Chair and Deputy, appointed through a rigorous and robust process involving a representative concerned with vulnerable customers, CCWater and regulator Environment Agency.
- The maintenance of good relationships with the regulators of Bristol Water, Bristol Water (including with an independent non-executive director, chief executive officer, chairperson and executive staff), interested stakeholder bodies (including Water UK, CCWater) and the chairpersons of customer challenge groups across England and Wales.
- A broadly based panel capable of challenging customer engagement through its representation of customers drawn from, or composed of urban and rural businesses, young people, vulnerable people, people of minority ethnicity, local government authorities, environmental concerns, and more.
- The panel itself is inducted and informed on issues affecting the business, its performance and its business planning and can:
 - * Represent and provide challenge from the range of views among the customer-base.
 - * Challenge and inform customer research proposals and interpretations.
 - * Scrutinise performance, proposals and innovations proposed by Bristol Water.
- The panel will maintain a Challenge Log of issues it has raised and the resolution of such issues. This will be published with our final report.
- The panel evaluates its performance, and that of Bristol Water, based on whether it is customer focused, the interests and concerns of the customer lead the items on the agenda, ethical issues (such as willingness to pay, inter-generational costs) feature during the meetings, reference to best practice and other comparative data.

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- Reports of the Challenge Panel are available through the website of Bristol Water, signposted through Ofwat and accessible through internet search engines.

Role of Ofwat

Ofwat has stated that:

- “We will enable, inform and incentivise good quality customer engagement that puts customers at the heart of decision making. In keeping with our statutory duties and strategy, we will step in if required.”
- “We will continue to provide clarity on our expectations regarding good quality customer engagement at PR19, including the roles that we, companies and CCGs have in delivering this.”
- “We will host regular workshops with CCG chairs to facilitate the sharing of information, knowledge and good practice and help foster more CCG collaboration.”
- “We confirm our commitment to publish early indications on the weighted average cost of capital and outcome return on regulatory equity”

Appendix 3

Challenge Panel members who have contributed to the Business Plan assurance review

Peaches Golding OBE	Chair
Tony Denham	Deputy Chair
Jeremy Hawkins (Report Writer)	Creoda Consulting
Michael Barnes	CCWater
Mike Bell	CCWater
Jeremy Bailey	Environment Agency
Dr Mark Taylor	Natural England
Prof. Chad Staddon	University of the West of England
Dr Danielle Wain	University of Bath
Cllr. Robert Cleland	North Somerset DC
Cllr. Terry Napper	Mendip DC
Cllr. Mhairi Threlfall	Bristol City Council
Susan Evans	Citizens Advice
Alison Sleightholm	Western Power Distribution
Dr. Tabinda Rashid-Fadel	NHS
Luke Hasell	The Story Group
Daniel Woodhead	Step Change
David Wilson	Duchy Home Farms
Alex Hastings	Independent

Appendix 4

DWI statement

Drinking Water Inspectorate statement

PR19 Drinking Water Inspectorate statement for Bristol Water plc Water Challenge Panel 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 PR19, 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 in the long-term. Ministers summarised these requirements in “The government’s strategic priorities and objectives for Ofwat¹ (Sept 2017)”.
- 1.4 In addition, the Inspectorate set out in our “Guidance Note: Long term planning for the quality of drinking water supplies (September 2017)²”. This includes 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.
- 1.5 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.
- 1.6 The Inspectorate have supported the Company’s CCG process throughout the PR19 process being available to discuss any matters relating to drinking water quality.

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.

¹ https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/661803/sps-Ofwat-2017.pdf

² <http://www.dwi.gov.uk/stakeholders/guidance-and-codes-of-practice/ltpg.pdf>

Drinking Water Inspectorate statement

- 2.2 Bristol Water plc submitted 4 formal proposals for drinking water quality to the Inspectorate, listed in the table in Annex A.
- 2.3 The Company submitted its proposals to the Inspectorate by the published deadline of 31 December 2017. Some further follow up information was requested from the Company and responses received as required.
- 2.4 The Inspectorate has formally supported 3 of the Company's proposals and we will put legal instruments in place to make the proposals legally binding programmes of work. The Company also submitted proposals building on current catchment management options to facilitate compliance with metaldehyde. With regard to metaldehyde, we are currently awaiting Ministerial guidance about future use restriction for metaldehyde and will look to revise the existing undertakings once this guidance has been received. Our final decision letter was sent to the Company on 30 May 2018.
- 2.5 Two of the Company's proposals relate to facilitating compliance with the lead standard. The Inspectorate expects that the Company will have a strategy in place for managing lead in drinking water that should form part of a risk-based programme of work that includes a range of measures to address lead in identified high risk areas, and target high risk properties and vulnerable consumers. In AMP7 the Company proposes to install phosphate dosing equipment at the Alderley works and to continue to implement their lead strategy with an extensive programme of lead pipe replacement/refurbishment targeting vulnerable groups and engagement with stakeholders.
- 2.6 The Inspectorate also supports a programme of treatment modifications at the Cheddar site to improve customer acceptability and reduce taste and odour complaints in the area.
- 2.7 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.
- 2.8 The summary of improvement schemes above reflects the position at the time of writing this note. Further discussions are needed with the Company to finalise details. We will advise the Water Challenge Panel of any material changes.
- 2.9 This note will be copied to Mr Graham Williams of Bristol Water plc. Any queries arising should be directed to Sue Pennison, Principal Inspector, Drinking Water Inspectorate, at Sue.Pennison@defra.gsi.gov.uk.

Drinking Water Inspectorate statement

Milo Purcell.

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Drinking Water Inspectorate
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29 June 2018

Drinking Water Inspectorate statement

Annex A: Drinking Water Quality schemes and DWI decisions

PR19 DWI ref	Scheme Name	Quality parameter	Scheme type	Preferred option	DWI final decision
BRL 1	Alderley WTW	Lead	Treatment	Phosphate dosing	Support - Regulation 28 notice
BRL 2	Cheddar WTW	Taste and Odour	Treatment	Treatment modifications	Support - Regulation 28 notice
BRL 3	Lead strategy	Lead	Treatment/Distribution	Implement lead strategy	Support - Regulation 28 notice
BRL 4	Purton and Littleton WTW	Pesticides (Metaldehyde)	Catchment	Various catchment management activities /implementation of use ban as appropriate	Support - current undertaking to be revised

Appendix 5

List of Challenge Panel and Sub-Group meetings

Challenge Panel Meeting 1	17 November 2015	Easy to contact Sufficient Water Supply Affordable Bills Efficient use of water Satisfied Customers
General Sub Group	25 November 2015	Efficient use of water Affordable Bills Satisfied Customers
Challenge Panel Meeting 2	1 March 2016	Resilient Supply Affordable Bills Satisfied Customers Efficient use of water
Away Day	10 May 2016	Achieving our Ambition Performance Reporting Independence and Membership Evaluations
Challenge Panel Meeting 3	9 June 2016	Ongoing Performance Water 2020 Ongoing Customer Engagement Household retail competition
Challenge Panel Meeting 4	21 Sept 2016	Customer Satisfaction Approach to PR19 Resources Management Drought Planning Customer Charges Customer Assurance
Assurance Sub-Group 1	30 Nov 2016	Approach to Assurance Assurance Assessment Assurance Status PR19 Assurance Framework
Challenge Panel Meeting 5	7 Dec 2016	Mid-Year Performance Update Assurance Update PR19 Customer Engagement Strategy Willingness to Pay Research
Environment Tripartite Meeting 1	7 Dec 2016	Bristol Water approach to PR19 Group Terms of Reference Drought Plan Water Resources Management Plan National Environment Plan Environment Performance Measures
Customer Engagement Sub-Group 1	9 January 2017	Customer Engagement Framework Update Working Together

Challenge Panel Meeting 6	25 Jan 2017	PR19 Customer Engagement Drought Plan Engagement Environment Update Ofwat Consultations
Environment Tripartite Meeting 2	1 March 2017	Bristol Water approach to PR19 Group Terms of Reference Drought Plan Water Resources Management Plan National Environment Plan Environment Performance Measures
Customer Engagement Sub-Group 2	4 April 2017	Customer Engagement Resilience Vulnerability
Challenge Panel Meeting 7	17 May 2017	BW Performance Triangulation Customer Engagement
Customer Engagement Phone-in or Customer Engagement Sub Group 3	17 May 2017	Asset Health PCs Water Resources Environment Triangulation Customer Engagement
Environment Tripartite Meeting 3	1 June 2017	Periodic Review 2019 Drought Plan Water Resources Management Plan Environmental Performance Resilience
Customer Engagement Phone-in	7 June 2017	Environment Resilience Water Resources Customer Engagement
Customer Engagement 4 Sub-Group	6 July 2017	Customer Engagement Triangulation Water Resources
Challenge Panel Meeting 8	12 July 2017	Customer Engagement Environment Information Assurance Triangulation Vulnerability BW Performance Water Resources
Assurance Sub-Group 2	21 July 2017	Information Assurance
Environment Tripartite Meeting 4	6 September 2017	Periodic Review 2019 Drought Plan Water Resources Management Plan Environmental Performance Resilience

Customer Engagement Sub-Group 5	22 September 2017	Customer Engagement Drought Plan Engagement Triangulation Vulnerability Strategy
Customer Engagement Sub Group 6	19 October 2017	Vulnerability Strategy
Customer Engagement Sub Group 7	31 October 2017	Triangulation
Challenge Panel Meeting 9	24 November 2017	BW Performance Tariffs Triangulation Customer Engagement Water Resources
Environment Tripartite Meeting 5	4 December 2017	Periodic Review 2019 Drought Plan Water Resources Management Plan Environmental Performance Resilience
Customer Engagement Sub Group 8	8 January 2018	Triangulation Information Assurance Customer Engagement
PC & ODI Sub Group 1	8 January 2018	Outcome Delivery Incentives
Challenge Panel Meeting 10	24 January 2018	Outcome Delivery Incentives Information Assurance Strategy
PC & ODI Sub Group 2	26 February 2018	Outcomes Framework Business Plan Assurance Performance Commitments Information Assurance
Customer Engagement Sub Group 9	7 March 2018	Vulnerability Customer Engagement
Environment Tripartite Meeting 6	14 March 2018	Periodic Review 2019 Drought Plan Water Resources Management Plan Environmental Performance Resilience
Customer Engagement Sub Group 10	20 April 2018	Water Resources Research Acceptability Testing Draft Business Plan Customer Summit Communication Plan
Challenge Panel Meeting 11	25 April 2018	CCG Aide Memoire Draft Business Plan ODI Early Submission Special Cost Factors Early Submission Drinking Water Quality Voids

Challenge Panel Meeting 12	25 May 2018	Consultation Responses Vulnerability and Vulnerability PC Targets, Penalties and Rewards Delivering Outcomes for Customers
PC & ODI Sub Group 3	7 June 2018	All 26 PCs were individually reviewed in detail.
Environment Tripartite Meeting 7	7 June 2018	Drought Plan Water Resources Management Plan National Environment Programme Measuring Environmental Performance Resilience
Assurance Sub-Group 3	13 June 2018	BW 2017/18 Performance Assurance of all Performance data
Customer Engagement Sub Group 11	26 June 2018	Draft Business Plan Vulnerability Assistance Customer Strategy Retailers Research Acceptability Testing
Challenge Panel Meeting 13	9 July 2018	Bristol Water Board Final Business Plan Transparency on PC Targets and Incentives Community PC Customer Priorities
Customer Engagement Sub Group 12	17 July 2018	Outstanding Challenges PC and ODI Update Triangulation Bill Profiles ODI Deadbands
Challenge Panel Meeting 14	9 August 2018	Customer Support for PCs Acceptability Testing Results Affordability Update Water Poverty Target Values for Money target Update Final Business Plan PR19 Assurance

Appendix 6

IAP to Aide Memoire Linkage

Ref	Subject Area	Ofwat's Description	Ref	Subject Area	Ofwat's Description	CCG to explicitly comment	CCG to challenge	Customer evidence needed
EC1	Engaging Customers	EC1 What is the quality of the Company's customer engagement and participation and how well is it incorporated into the Company's business plan and ongoing business operations?	1	CCG Role	Customer challenge groups (CCGs) will provide independent challenge to companies and provide independent assurance to us on the quality of a company's customer engagement; and the degree to which this is reflected in its business plan	n/a	n/a	n/a
			2	Customer engagement	Customer engagement will be a central part of the initial assessment of business plans. Customer engagement also provides essential evidence for companies' proposals in their plans. In assessing the customer engagement test, we will take into account evidence including, not limited to, evidence from its CCG	✓	✓	✓
			3	Engagement with business retailers	We consider wholesale should engage with business retailers as part of the customer engagement process to learn about their views and the views of their customers.			✓
								☐
AV1	Addressing Affordability and Vulnerability	AV1 How well has the company demonstrated that its bills are affordable and value for money for the 2020-25 period?	4	Affordability	Companies are required to provide robust evidence in their business plans on how their approaches, have, and will, deliver affordability for current customers, future customers, and those struggling, or at risk of struggling, to pay. This includes evidence on the customer engagement they have carried out on their approaches, how well the company understands what affordability looks like for their customers, and the customer support for the approach they have taken. Our assessment on affordability will be supported by evidence provided by companies, the independent reports from CCGs, and evidence from other expert organisations	✓	✓	✓
AV2		AV2 How well has the company demonstrated that its bills will be affordable and value for money beyond 2025?	5	Vulnerability	In our February 2016 Vulnerability focus report we said that we would encourage CCGs to use the report as a base on which to challenge companies and their business plans when considering both customer service excellence and their companies' approaches to addressing vulnerability. In assessing the vulnerability test, we will take into account evidence that the company's approach to vulnerability is targeted, efficient and effective, including evidence from the independent CCG report.	✓	✓	✓
AV3		AV3 To what extent has the company demonstrated that it has appropriate assistance options in place for those struggling, or at risk of struggling, to pay?						
AV4		AV4 To what extent does the company identify and provide accessible support for customers in circumstances that make them vulnerable, including proposing a bespoke performance commitment related to vulnerability?						
						☐	☐	☐
OC1	Delivering Outcomes for	OC1 How appropriate, well evidenced and stretching are the company's proposed performance commitments and service levels?	6	Performance commitments		☐	☐	☐

Ref	Subject Area	Ofwat's Description	Ref	Subject Area	Ofwat's Description	CCG to explicitly comment	CCG to challenge	Customer evidence needed
OC2	Customers	OC2 How appropriate and well evidenced is the company's package of outcome delivery incentives?	6a	General approach to performance commitments	CCGs will challenge companies on their approaches to setting performance commitments including how well they reflect customers' views and how stretching they are. Our assessment will include focussing on the CCG report.	✓	✓	✓
OC3			OC3 How appropriate is the Company's focus on service performance in its risk/return package?	6b	Setting stretching performance commitments	Our approach to setting stretching performance commitment levels for PR19 is that companies should: engage with their customers on their performance commitment levels; and challenge the level of stretch in their performance commitments with the customers, CCGs and other stakeholders	✓	✓
		6c		Using multiple data sources for performance commitment levels ("triangulation")	Companies will need to engage with their customers on the factors they take into account and will need to explain how they have balanced these factors when setting their performance commitment levels using multiple data sources. The role of CCGs will be important in assuring how companies have engaged with their customers on this issue.	✓	✓	✓
		6d		Setting initial service levels (2019-20) for performance commitments	At PR19 we expect companies to forecast appropriate levels of 2019-20, and for these to influence the level of their performance commitments. CCGs will challenge companies on their forecasts for 2019-20, as well as their performance commitment levels		✓	✓
		6e		Common performance commitments	We expect companies to have four common performance commitments on asset health; mains bursts, unplanned outages [sewer collapses and treatment works compliance for WASCs]. This will enable customers, CCGs and us to compare performance and challenge companies about their proposed levels for these commitments		✓	✓
		6f		Bespoke performance commitments	Companies have the freedom to engage widely with their customers and local stakeholders, to propose performance commitments that reflect their customers' particular preferences. There should be no, or very few, exemptions included in the definitions of bespoke performance commitments and any exemptions need to be well justified and supported by customers.			✓
		6g		Abstraction Incentive Mechanism (AIM)	It is for companies to propose their AIM incentives following engagement with their local stakeholders, and assurance from the CCG. Companies should identify suitable sites in liaison with the Environment Agency [or Natural Resources Wales] and provide evidence of their engagement	✓	✓	✓
		6h		Leakage performance commitments	We expect companies to explain how their five-year performance commitment levels and long-term projections for leakage take into account the views of their customers (with CCG assurance on how those views have been taken into account) and local stakeholders. Companies can make the case for leakage reductions that do not achieve our challenges above where they can provide robust evidence and a strong rationale for this. For example, that a company is already a frontier performer or has strong customers support not to reduce leakage to this extent.		✓	✓
		6i		Transparency of performance commitments	We require companies to explain in their business plans, how they will disseminate their performance information during 2020-2025 period to customers, CCGs and other stakeholders		✓	✓

Ref	Subject Area	Ofwat's Description	Ref	Subject Area	Ofwat's Description	CCG to explicitly comment	CCG to challenge	Customer evidence needed
			6j	Scheme-specific performance commitments	A company should engage with its customers and CCGs on any scheme-specific performance commitments, as part of its engagement process on all its performance commitments		✓	✓
			7	Outcome delivery incentives				
			7a	Consulting customers on ODIs	We expect companies to develop their ODIs in consultation with their customers. CCGs will challenge companies on how well their proposed ODI outperformance and underperformance payment rates reflect a suitably wide range of evidence on their customers' preferences. Companies can propose outperformance payment caps and underperformance penalty collars on their individual ODIs, if supported by their customer engagement. Our approach allows for a company to propose a reputational-only ODI, if a company provides convincing evidence that this is appropriate. This includes evidence from its customer engagement or that a performance commitment is not well suited to a financial ODI	✓	✓	✓
			7b	In-period ODIs	Companies would need to justify, with evidence why in-period ODIs are not in customers' interests, including why future customers should pay for/benefit from incentives related to the service performance affecting current customers. The evidence should include customer research and view of the CCG		✓	✓
			7c	Setting ODI rates	CCGs will challenge companies on how well their proposed ODI outperformance and underperformance payment rates reflect a suitably wide range of evidence on their customers' preference. Companies can base their ODI outperformance and underperformance payment rates on the existing formulas, but amended, so that companies can use alternative customer valuations instead of only marginal stated preference WTP		✓	✓
			7d	The overall size of a company's ODIs (the RoRE range)	We expect companies to develop their ODIs in consultation with their customers, and obtain customer support for the overall RORE range proposed in their business plan. We expect companies to propose approaches to protecting customers in case their ODI payments turn out to be much higher than their expected RoRE ranges for ODIs		✓	✓
			7e	ODIs for resilience performance commitments	Companies should only propose financial ODIs related to resilience performance commitments if they reflect the particular resilience challenges facing them, are supported by evidence and by their customers and do not involve ODI outperformance payments that overlap with funding received through the cost allowances.			✓
			7f	ODIs for asset health performance commitments	Companies should engage with their customers and CCGs on how their asset health metrics protect current and future customers and the environment. Companies should explain to their customers, CCGs and Ofwat the size of their asset health underperformance penalties (and any outperformance payments) and how they relate to their past performance and the asset health challenges they face, Companies can only propose outperformance payments for asset health performance commitments if they can show there are benefits for customers and their proposals reflect evidence of customer preferences -as above		✓	✓
			7g	Enhanced ODI outperformance payments and underperformance penalties	The enhance outperformance and underperformance payments are only appropriate for the common performance commitments, which are based on comparable data. This is so that customers, CCGs and Ofwat can be more certain that the enhanced outperformance threshold truly represents frontier-shifting performance.		✓	✓
							☐	☐

Ref	Subject Area	Ofwat's Description	Ref	Subject Area	Ofwat's Description	CCG to explicitly comment	CCG to challenge	Customer evidence needed
CA1	Securing Confidence and Assurance	CA1 To what extent has the company's full Board provided comprehensive assurance to demonstrate that all the elements add up to a business plan that is high quality and deliverable, and that it has challenged management to ensure this is the case?	8	Securing confidence and assurance	This section repeats CCGs main role; it is also important that CCG reports highlight areas of challenge and disagreement, including how the company has responded to challenges and any areas of outstanding disagreement. The Environment Agency, Natural England and Natural Resources Wales have also set out wider expectations for companies, as have the UK and Welsh Governments through their strategic policy statements. We expect companies to take these into account when developing their business plans and outcomes, and to implement them when they are in customers' interests and have customer support.	✓	✓	✓
CA2		CA2 To what extent has the company's full Board been able to demonstrate that its governance and assurance processes provide operational, financial and corporate resilience over the next control period and long term?	8b	Corporate and financial structures	We have introduced a new IAP test to require assurance from company Boards that their business plan will enable customers' trust and confidence through high levels of transparency and engagement with customers on issues such as its corporate and financial structures.	☐	☐	✓
CA3		CA3 To what extent has the Company's full Board provided assurance that the Company's business plan will enable customer's trust and confidence through high levels of transparency and engagement with customers, on issues that matter to customers (which extends to their ability to understand the Company's corporate and financial structures and how they relate to its long term resilience)?						
CA4		CA4 To what extent has the company's full Board provided assurance that the company's business plan will enable customers' trust and confidence, through appropriate measures to provide a fair balance between customers and investors (which include outperformance sharing, dividend policies and any performance related element of executive pay) and high levels of transparency and engagement, on issues that matter to customers (which extends to their ability to understand corporate and financial structures and how they relate to its long-term resilience)?						
CA5		CA5 To what extent does the company have a good track record of producing high quality data, taking into account the company's data submission, assurance process and statement of high quality, and our 2018 assessment of the company under the company monitoring framework?						
CA6		CA6 How consistent, accurate and assured are the company's PR19 business plan tables, including the allocation of costs between business units, information on corporation tax, and the assurance and commentary provided?						

Ref	Subject Area	Ofwat's Description	Ref	Subject Area	Ofwat's Description	CCG to explicit comment	CCG to challenge	Customer evidence needed
LR1	Securing Long Term Resilience	LR1 How well has the company used the best available evidence to objectively assess and prioritise the diverse range of risks and consequences of disruptions to its systems and services and engaged effectively with customers on its assessment the risks and consequences?	9	Resilience planning principles	Principle 3: Customer engagement. Assessments of resilience should be informed by engagement with customers, to help companies understand their customers' expectations on levels of service. This will also help companies understand their customers' appetite for risk and how customer behaviour, in matters such as water efficiency, might influence approaches to resilience.	<input type="checkbox"/>	✓	✓
LR2		LR2 How well has the company objectively assessed the full range of mitigation options and selected the solutions that represent the best value for money over the long term and have support from customers?	9b	Operational resilience	The company will need to demonstrate the incremental improvement of the proposed investment, that it considered a range of options, and that the proposed solution delivers outcomes that reflect customers' priorities, identified through customer engagement.	-	-	✓
						-	-	<input type="checkbox"/>
CMI1	Targeted controls, markets and innovation	CMI1 How well does the company's business plan demonstrate that it has the right culture for innovation which enables it through its systems, processes and people, to deliver results for customers and the environment from innovation?	10	Securing cost efficiency - need for investment	In relation to cost adjustment claims: Where appropriate, is there evidence – assured by the customer challenge group (CCG) – that customers support the project? Best option for customers:• Does the proposal deliver outcomes that reflect customers' priorities, identified through customer engagement? Is there CCG assurance that the company has engaged with customers on the project and this engagement been taken account of?• Is there persuasive evidence that the proposed solution represents the best value for customers in the long term, including evidence from customer engagement?	✓	✓	✓
CMI2		CMI2 How well does the Company use and engage with markets to deliver greater efficiency and innovation and to enhance resilience in the provision of wholesale and retail water and waste-water services to secure value for customers, the environment and the wider economy; and to support ambitious performance for the 2020 - 2025 period and over the longer term?						
CMI3		CMI3 To what extent has the company set out a well evidenced long term strategy for securing resilient and sustainable water resources, considering a twin track approach of supply side and demand side options where appropriate, to meet the needs of customers and the environment in the 2020-25 period and over the longer term?						
CMI4		CMI4 To what extent does the company have a well evidenced long term strategy for delivering bio resources services, integrating an assessment of the value from the delivery of bio resources services by third parties for the 2020-25 period and over the longer term?						
CMI5		CMI5 How appropriate is the company's proposed pre-2020 RCV allocation between water resources and water network plus - and, if relevant, between bio resources and wastewater network plus - taking into account the guidance and /or feedback we have provided?						

Ref	Subject Area	Ofwat's Description	Ref	Subject Area	Ofwat's Description	CCG to explicit comment	CCG to challenge	Customer evidence needed
CMI6		CMI6 To what extent has the Company produced a Company Bid Assessment Framework for water resources, demand management and leakage services that demonstrates a clear commitment to the key procurement principles of transparency, equality / non-discrimination and proportionality and the best practice recommendations?						
CMI7		CMI7 To what extent has the Company clearly demonstrated that it has considered whether all relevant projects are technically suitable for direct procurement for customers? Where it has one or more such projects, to what extent has the Company provided a well reasoned and well evidenced value for money assessment supporting its decision on whether or not to take forward each technically suitable project using direct procurement for customers?						
CE1	Securing cost efficiency	CE1 How well evidenced, efficient and challenging are the company's forecasts of wholesale water expenditure including water resources costs?						
CE2		CE2 How well evidenced, efficient and challenging are the company's forecasts of wholesale wastewater expenditure including bio resources costs?						
CE3		CE3 How well evidenced, efficient and challenging are the company's forecasts of retail expenditure including bad debt costs?						
CE4		CE4 To what extent are cost adjustment claims used only where prudent and appropriate, and where they are used, are costs adjustments well evidenced, efficient and challenging?						
						<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
RR1	Aligning Risk and Return	RR1 Has the company based the separate costs of capital that underpin each of its wholesale price controls, and the net margin(s) that underpins its retail price control(s), on those we state in our early view? If not, has the company robustly justified, in terms of benefits for customers, its proposed costs of capital and retail margin(s) within the context of expected market conditions for 2020-25?	11	Financeability	We will look for evidence of customer support where companies take steps to address finance ability constraints.			✓
RR2		RR2 To what extent has the Company demonstrated a clear understanding and assessment of the potential risks in its RORE assessment including the effect of the risk management measures it will have in place across each of the price controls?						

Ref	Subject Area	Ofwat's Description		Ref	Subject Area	Ofwat's Description	CCG to explicitly comment	CCG to challenge	Customer evidence needed
RR3		RR3 Has the board provided a clear statement that its plan is financeable on both an actual and a notional basis? Is the statement appropriate and how robust is the supporting evidence?		12	Bill profiles	Companies should take into account customers' views on the profile of bills over time, which will enable companies to understand customers' implicit views on the impact of their PAYG and RCV run-off choices on bills, both in the short and long term. We acknowledge feedback from respondents to the consultation and we do not expect companies to directly ask their customers about their PAYG and RCV run-off rates.			✓
RR4		RR4 How appropriate are the company's PAYG and RCV run-off rates? How well evidenced are they, including that they are consistent with customers expectations both now and in the longer term?							
									☐
PD1	Accounting for Past Delivery	PD1 How well has the company given evidence of its proposed reconciliations for the 2015-20 period, and has it proposed adjustments by following the PR14 reconciliation rulebook methodology?		13	Accounting for past delivery	When testing how well the company has provided evidence for its proposed reconciliations for the 2015-20 period and how well it has followed the PR14 reconciliation rulebook methodologywe would expect to see.... evidence of customers' support, and the strength of that support, for its proposed adjustments to the 2020-25 price controls.			✓
PD2		PD2 How well has the company performed, and is forecast to perform, over the 2015-20 period and, taking into account this overall performance, how well has it put measures in place to ensure that it maintains confidence that it can successfully deliver its PR19 business plan?							
									☐
				14	The initial assessment of plans (IAP)	A high-quality business plan (the points most relevant to the CCG role): Is grounded in excellent customer engagement, with a wide range of evidence; Should include stretching outcomes and performance commitments that reflect what customers want, and their relative priorities, and clear line of sight from these through the plan. It should also include evidence of consideration of customer participation; Is affordable for all current and future customers, with appropriate assistance provided where needed; and Sets out the company's approach to effectively and efficiently identifying and providing support for customers in circumstances which make them vulnerable.			✓

Appendix 7

Ofwat Aide Memoire to CCGs - BWCP Assurance Report References

Ref	Subject Area	Ofwat's Requirement	CCG role	BWCP Assurance Report reference
1	CCG Role	Customer challenge groups (CCGs) will provide independent challenge to companies and provide independent assurance to us on the quality of a company's customer engagement; and the degree to which this is reflected in its business plan	Comment	All sections
2	Customer engagement	Customer engagement will be a central part of the initial assessment of business plans. Customer engagement also provides essential evidence for companies' proposals in their plans. In assessing the customer engagement test, we will take into account evidence including, not limited to, evidence from its CCG	Comment, challenge, & seek customer evidence	All sections
3	Engagement with business retailers	We consider wholesale should engage with business retailers as part of the customer engagement process to learn about their views and the views of their customers.	Seek customer evidence	Section 5.2
4	Affordability	Companies are required to provide robust evidence in their business plans on how their approaches, have, and will, deliver affordability for current customers, future customers, and those struggling, or at risk of struggling, to pay. This includes evidence on the customer engagement they have carried out on their approaches, how well the company understands what affordability looks like for their customers, and the customer support for the approach they have taken. Our assessment on affordability will be supported by evidence provided by companies, the independent reports from CCGs, and evidence from other expert organisations	Comment, challenge, & seek customer evidence	Section 6
5	Vulnerability	In our February 2016 Vulnerability focus report we said that we would encourage CCGs to use the report as a base on which to challenge companies and their business plans when considering both customer service excellence and their companies' approaches to addressing vulnerability. In assessing the vulnerability test, we will take into account evidence that the company's approach to vulnerability is targeted, efficient and effective, including evidence from the independent CCG report.	Comment, challenge, & seek customer evidence	Section 7
5b	Vulnerability: bespoke performance commitment	We are requiring companies to include at least one bespoke performance commitment for addressing vulnerability in their business plans, after engaging with customers and taking on board challenges from their CCGs	Comment, challenge, & seek customer evidence	Section 7

Ref	Subject Area	Ofwat's Requirement	CCG role	BWCP Assurance Report reference
6	Performance commitments			
6a	General approach to performance commitments	CCGs will challenge companies on their approaches to setting performance commitments including how well they reflect customers' views and how stretching they are. Our assessment will include focussing on the CCG report.	Comment, challenge, & seek customer evidence	Section 8.2
6b	Setting stretching performance commitments	Our approach to setting stretching performance commitment levels for PR19 is that companies should: engage with their customers on their performance commitment levels; and challenge the level of stretch in their performance commitments with the customers, CCGs and other stakeholders	Comment, challenge, & seek customer evidence	Section 8.3.2
6c	Using multiple data sources for performance commitment levels ("triangulation")	Companies will need to engage with their customers on the factors they take into account and will need to explain how they have balanced these factors when setting their performance commitment levels using multiple data sources. The role of CCGs will be important in assuring how companies have engaged with their customers on this issue	Comment, challenge, & seek customer evidence	Section 8.3.2
6d	Setting initial service levels (2019-20) for performance commitments	At PR19 we expect companies to forecast appropriate levels of 2019-20, and for these to influence the level of their performance commitments. CCGs will challenge companies on their forecasts for 2019-20, as well as their performance commitment levels	Challenge & seek customer evidence	Section 8.3
6e	Common performance commitments	We expect companies to have four common performance commitments on asset health; mains bursts, unplanned outages. This will enable customers, CCGs and us to compare performance and challenge companies about their proposed levels for these commitments.	Challenge & seek customer evidence	Section 8.4
6f	Bespoke performance commitments	Companies have the freedom to engage widely with their customers and local stakeholders, to propose performance commitments that reflect their customers' particular preferences. There should be no, or very few, exemptions included in the definitions of bespoke performance commitments and any exemptions need to be well justified and supported by customers.	Seek customer evidence	Section 8.5
6g	Abstraction Incentive Mechanism (AIM)	It is for companies to propose their AIM incentives following engagement with their local stakeholders, and assurance from the CCG. Companies should identify suitable sites in liaison with the Environment Agency [or Natural Resources Wales] and provide evidence of their engagement	Comment, challenge, & seek customer evidence	Section 8.6

Ref	Subject Area	Ofwat's Requirement	CCG role	BWCP Assurance Report reference
6h	Leakage performance commitments	We expect companies to explain how their five-year performance commitment levels and long-term projections for leakage take into account the views of their customers (with CCG assurance on how those views have been taken into account) and local stakeholders. Companies can make the case for leakage reductions that do not achieve our challenges above where they can provide robust evidence and a strong rationale for this. For example, that a company is already a frontier performer or has strong customers support not to reduce leakage to this extent.	Challenge & seek customer evidence	Section 8.7
6i	Transparency of performance commitments	We require companies to explain in their business plans, how they will disseminate their performance information during 2020-2025 period to customers, CCGs and other stakeholders	Challenge & seek customer evidence	Section 8.3.2
6j	Scheme-specific performance commitments	A company should engage with its customers and CCGs on any scheme-specific performance commitments, as part of its engagement process on all its performance commitments	Challenge & seek customer evidence	Section 8.8
7	Outcome delivery incentives			
7a	Consulting customers on ODIs	We expect companies to develop their ODIs in consultation with their customers. CCGs will challenge companies on how well their proposed ODI outperformance and underperformance payment rates reflect a suitably wide range of evidence on their customers' preferences. Companies can propose outperformance payment caps and underperformance penalty collars on their individual ODIs, if supported by their customer engagement. Our approach allows for a company to propose a reputational-only ODI, if a company provides convincing evidence that this is appropriate, This includes evidence from its customer engagement or that a performance commitment is not well suited to a financial ODI	Comment, challenge, & seek customer evidence	Section 9.2
7b	In-period ODIs	Companies would need to justify, with evidence why in-period ODIs are not in customers' interests, including why future customers should pay for/benefit from incentives related to the service performance affecting current customers. The evidence should include customer research and view of the CCG	Challenge & seek customer evidence	Section 9.2
7c	Setting ODI rates	CCGs will challenge companies on how well their proposed ODI outperformance and underperformance payment rates reflect a suitably wide range of evidence on their customers' preference. Companies can base their ODI outperformance and underperformance payment rates on the existing formulas, but amended, so that companies can use alternative customer valuations instead of only marginal stated preference WTP	Challenge & seek customer evidence	Section 9.2
7d	The overall size of a company's ODIs (the RoRE range)	We expect companies to develop their ODIs in consultation with their customers, and obtain customer support for the overall RORE range proposed in their business plan. We expect companies to propose approaches to protecting customers in case their ODI payments turn out to be much higher than their expected RoRE ranges for ODIs.	Challenge & seek customer evidence	Section 9.2

Ref	Subject Area	Ofwat's Requirement	CCG role	BWCP Assurance Report reference
7e	ODIs for resilience performance commitments	Companies should only propose financial ODIs related to resilience performance commitments if they reflect the particular resilience challenges facing them, are supported by evidence and by their customers and do not involve ODI outperformance payments that overlap with funding received through the cost allowances.	Seek customer evidence	Section 9.2
7f	ODIs for asset health performance commitments	Companies should engage with their customers and CCGs on how their asset health metrics protect current and future customers and the environment. Companies should explain to their customers, CCGs and Ofwat the size of their asset health underperformance penalties (and any outperformance payments) and how they relate to their past performance and the asset health challenges they face, Companies can only propose outperformance payments for asset health performance commitments if they can show there are benefits for customers and their proposals reflect evidence of customer preferences -as above	Challenge & seek customer evidence	Section 9.2
7g	Enhanced ODI outperformance payments and underperformance penalties	The enhance outperformance and underperformance payments are only appropriate for the common performance commitments, which are based on comparable data. This is so that customers, CCGs and Ofwat can be more certain that the enhanced outperformance threshold truly represents frontier-shifting performance. Have we got any?	Challenge & seek customer evidence	Section 9.2
8	Securing confidence and assurance	This section repeats CCGs main role; it is also important that CCG reports highlight areas of challenge and disagreement, including how the company has responded to challenges and any areas of outstanding disagreement. The Environment Agency, Natural England and Natural Resources Wales have also set out wider expectations for companies, as have the UK and Welsh Governments through their strategic policy statements. We expect companies to take these into account when developing their business plans and outcomes, and to implement them when they are in customers' interests and have customer support.	Comment, challenge, & seek customer evidence	Section 3
8b	Corporate and financial structures	We have introduced a new IAP test to require assurance from company Boards that their business plan will enable customers' trust and confidence through high levels of transparency and engagement with customers on issues such as its corporate and financial structures.	Seek customer evidence	Section 11.1
9	Resilience planning principles	Principle 3: Customer engagement. Assessments of resilience should be informed by engagement with customers, to help companies understand their customers' expectations on levels of service. This will also help companies understand their customers' appetite for risk and how customer behaviour, in matters such as water efficiency, might influence approaches to resilience.	Challenge & seek customer evidence	Section 5.4

Ref	Subject Area	Ofwat's Requirement	CCG role	BWCP Assurance Report reference
9b	Operational resilience	The company will need to demonstrate the incremental improvement of the proposed investment, that it considered a range of options, and that the proposed solution delivers outcomes that reflect customers' priorities, identified through customer engagement.	Seek customer evidence	Section 5.4
10	Securing cost efficiency - need for investment	In relation to cost adjustment claims: Where appropriate, is there evidence – assured by the customer challenge group (CCG) – that customers support the project? Best option for customers: • Does the proposal deliver outcomes that reflect customers' priorities, identified through customer engagement? Is there CCG assurance that the company has engaged with customers on the project and this engagement been taken account of? • Is there persuasive evidence that the proposed solution represents the best value for customers in the long term, including evidence from customer engagement?	Comment, challenge, & seek customer evidence	Section 10
11	Financeability	We will look for evidence of customer support where companies take steps to address financeability constraints.	Seek customer evidence	Section 11.2
12	Bill profiles	Companies should take into account customers' views on the profile of bills over time, which will enable companies to understand customers' implicit views on the impact of their PAYG and RCV run-off choices on bills, both in the short and long term. We acknowledge feedback from respondents to the consultation and we do not expect companies to directly ask their customers about their PAYG and RCV run-off rates.	Seek customer evidence	Section 11.3
13	Accounting for past delivery	When testing how well the company has provided evidence for its proposed reconciliations for the 2015-20 period and how well it has followed the PR14 reconciliation rulebook methodologywe would expect to see.... evidence of customers' support, and the strength of that support, for its proposed adjustments to the 2020-25 price controls.	Seek customer evidence	Section 11.4
14	The initial assessment of plans (IAP)	A high-quality business plan (the bullet points most relevant to the CCG role): Is grounded in excellent customer engagement, with a wide range of evidence; Should include stretching outcomes and performance commitments that reflect what customers want, and their relative priorities, and clear line of sight from these through the plan. It should also include evidence of consideration of customer participation; Is affordable for all current and future customers, with appropriate assistance provided where needed; and Sets out the company's approach to effectively and efficiently identifying and providing support for customers in circumstances which make them vulnerable.	Seek customer evidence	All sections

Appendix 8 - Extract from the Panel's Challenge Log

	Subject	Source	CHALLENGE DESCRIPTION	RESPONDENT	DATE CHALLENGE RAISED	OUTCOME, COMMENTS, RESPONSES	Date Completed	STATUS
240	Engagement Framework	Challenge Panel 6	The Chair observed that BW's priorities for engagement and the service attributes on which it intends to engage with customers (as presented in Appendix A of its Framework) were primarily its own list and didn't fully reference Ofwat's industry concerns such as resilience	BW	25/01/2017	DbD replied that resilience has been included but that resilience is considered to be a group of service attributes rather than a single one. BW added that its evidence review shows that customers' views on resilience are scattered and need to be brought together and built upon. BW also added that it has considered Ofwat's focus for PR19 but agreed it could be better mapped and presented in its Framework document. framework updated.	09/11/2017	Acknowledged. No change required.
241	Engagement Framework	Challenge Panel 6	The Chair said that customers' maturity in terms of their understanding of the service received also varies and the company should be considering the things customers know and those they don't know	BW	25/01/2017	This comment is noted	11/05/2017	Acknowledged. No action before Ofwat report
242	Environment	Challenge Panel 6	NE said that customers' environmental concerns should be opportunities and that questions concerning the environment should be framed to be more positive.	BW	25/01/2017	BW noted this. Focus group documents revised.	09/11/2017	Acknowledged. No change required.
243	Engagement Framework	Challenge Panel 6	EA asked how BW will be engaging with customers on resilience.	BW	25/01/2017	DbD replied that resilience has both operational and business dimensions. There will be stated preference (valuation) research followed by deliberative research to put additional context onto the valuations. All such research now completed.	09/11/2017	Acknowledged. No change required.
244	Resilience	Challenge Panel 6	EA said that there needs to be a common understanding on 'Resilience' as there is a risk of inconsistency in definition and perception.	BW	25/01/2017	BW agreed. It will be developing its valuation metrics for resilience shortly.	09/11/2017	Acknowledged. No change required.
245	Engagement Framework	Challenge Panel 6	The Deputy Chair, questioned the priorities included in the engagement framework	BW	25/01/2017	BW clarified that the current list of priorities included in the engagement framework are not the priorities for the Business Plan. The engagement process and outcomes will inform the Plan. Priorities will evolve over time	25/01/2017	Acknowledged. No change required.
246	Environment	Challenge Panel 6	NE asked why the environment doesn't appear in the list of priorities for engagement.	BW	25/01/2017	DBD replied that environmental issues will be covered as part of resilience. At present the environment is not a priority for our customers.	09/11/2017	Acknowledged. No change required.
247	Engagement Framework	Challenge Panel 6	The Chair said that cross cutting themes such as environment, climate change, biodiversity and affordability should be clearly identified in the deliberative research. BCC added that, whilst it considered the proposed framework to be comprehensive, such cross cutting themes need to be woven in.	BW	25/01/2017	DbD agreed this is a useful suggestion and BW will consider how best to do this.	26/04/2017	Acknowledged. Changes made.
248	Engagement Framework	Challenge Panel 6	NSC asked if BW was in touch with other companies on for PR19.	BW	25/01/2017	BW replied that not much sharing of information happens in the commercial environment. There is no common industry framework	25/01/2017	Acknowledged. No change required.
249	Engagement Framework	Challenge Panel 6	EA said that it is important how the outcomes are derived as well that what they are, particularly in respect of wider societal benefits such as recreation, wildlife, etc. The Chair added that engagement is a two way process with customer education an important aspect. The quality of engagement will depend on education, context and responsiveness of both by company and customers. The proposed interactive game is an exciting aspect and should provide an opportunity to include wider societal benefits into the engagement	BW	25/01/2017	BW replied that its framework incorporates a staged approach and includes programme contingency, review and sense checking of outcomes and the flexibility to evolve as necessary	25/01/2017	Acknowledged. No change required.
250	Strategy	Challenge Panel 6	There was discussion after the meeting between the Chair and BW over the timing of the sub-group meetings in relation to BW internal reviews and the benefits of engaging with the Panel before the BW review.	BW	25/01/2017	BW will consider this. Sub group meeting timing now agreed.	09/11/2017	Acknowledged. No change required.
251	Strategy	Challenge Panel 6	EA referred to BW's slide on Regulator Priorities pointing out these were Ofwat's priorities only, not EA, NE, DWI or CCW. BCC added that local council priorities should also be considered.	BW	25/01/2017	BW noted this and accepted EA's offer to help with the identification of environmental priorities	26/04/2017	Acknowledged. Changes made.
252	Engagement Framework	Challenge Panel 6	BW would welcome any comments from the Panel on its upcoming activities including customer segmentation, stated preference approach and the use of focus groups	BWCP Members	25/01/2017	Panel comments sent direct to BW by 31 January 2017, see challenges below for details	31/01/2017	Acknowledged. No change required.
253	Drought Plan	Challenge Panel 6	The Chair requested a list of consultees for the Drought Plan.	BW	25/01/2017	BW supplied a list of consultees	31/01/2017	Acknowledged. No change required.
254	Drought Plan	Challenge Panel 6	BW was questioned on its approach to the consultation exercise.	BW	25/01/2017	BW replied that it will be using various forms of communication such as adverts on buses, social media and through its billing process	25/01/2017	Acknowledged. No change required.
255	Drought Plan	Challenge Panel 6	BCC asked about the expected level of customer response. The customer response to the last Plan was very limited.	BW	25/01/2017	An online panel is out from 31st March and a survey online with a £200 prize draw. Aiming for a minimum of 30 responses.	25/01/2017	Acknowledged. Changes made.
256	Drought Plan	Challenge Panel 6	The Chair suggested that BW could extend reach through engaging with gardening clubs, health clubs, leisure centres, etc. There maybe scope for using the customer centre to help by using holding messages to promote the consultation. NSC added that allotment holders could also be consulted. CCW considers it important to tailor communication to individual consultees. UWE said that customers only respond when and if it's relevant to them. BW could put out a simple message to all customers saying that BW would really like to hear from them because the Drought Plan matters to them and to customers and here's how they can respond.	BW	25/01/2017	BW considered this but could not reach all of these with the resource they had.	26/04/2017	Acknowledged. No action before Ofwat report
257	Drought Plan	Challenge Panel 6	EA mentioned the proliferation of car washes, wondered what their impact on water supply was and whether BW was engaging with this industry.	BW	25/01/2017	BW noted this but said that car washes were a non-essential user of water and would be covered by temporary use bans if imposed	25/01/2017	Acknowledged. No change required.
258	Drought Plan	Challenge Panel 6	NE noted that BW's reservoir control curves and the resulting impact on the environment are not well defined.	BW	25/01/2017	BW agreed that the evidence base for the curves isn't good. There is scope to improve them but this is unlikely to be completed in time for the forthcoming WRMP update. It may include a commitment in the WRMP to review its control curves. WRMP19 will reference the need to update the existing control curve and it has been confirmed that review of these curves cannot be completed in time for WRMP19.	11/10/2017	Acknowledged. Changes made.
259	Drought Plan	Challenge Panel 6	BW invited feedback from the Panel on the non-technical summary of its Drought Plan	BWCP Members	25/01/2017	Panel comments sent direct to BW; see challenges below for details	07/02/2017	Acknowledged. No change required.
260	Environment	Challenge Panel 6	The Deputy Chair noted that DWI do not attend the group but meet separately with BW.	BW	25/01/2017	BW will let the Panel know how it will be engaging with DWI as part of the PR19 process and how it will keep the Panel informed of the outcomes. DWI attended the BWCP meeting on the 25 April.	08/06/2018	Acknowledged. No change required.



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