



Your views

Supporting evidence for: *Your water. Your choices.*



About this document

Over the last year (2012-13), we have consulted extensively with our customers and stakeholders about the future of our water and waste water services.

This document summarises the main insight we have drawn from this consultation. We have used this information to help us develop our next consultation: *Your water. Your choices*. It explains the general emerging trends rather than presenting definitive conclusions.

Whilst this document has been scrutinised and challenged by the Customer Engagement Working Group, a sub-group of the Severn Trent Water Forum, the information in it has not been audited. The views given are not necessarily those of either Severn Trent Water or the Customer Engagement Working Group. Some excisions of sensitive information have been made.

You can view the full consultation document *Your water. Your choices* at:

www.severntrent.com/yourchoices

You can find out more about the Water Forum at: www.severntrent.com/waterforum

How this document is structured

In *Your water. Your choices* we set out 10 long term objectives. In this document, we have structured the insight we have gathered through consultation under each of these objectives.

We go on to explain:

Where are we starting from?	Our initial position at the start of our current business planning period for 2010-15 (AMP 5). Information has been drawn from our business plan for that period, or our 2007 Strategic Direction Statement.
Where have we taken information from?	Our principal sources of information. They have been: <ul style="list-style-type: none">• Our latest Willingness to Pay (WTP) customer research• Our quarterly customer satisfaction survey (tracker)• Bespoke customer research undertaken as part of this consultation.• Our historic catalogue of 20 years of research.• Stakeholder responses to our April 2012 consultation <i>Making the right choices</i> (MTRC).• Stakeholder views given at five workshops held in 2012 to support MTRC.• The policy or regulatory positions of Defra and our regulators.• Relevant customer research undertaken by other stakeholders, for example, CCWater.
What have we learned?	The main insight we have drawn.
In summary	The key points summarised.

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1. We will provide water that is good to drink

Where are we starting from?

We began AMP5 (our 2010-15 business planning period) stating that a reliable, safe water supply is the top priority for our customers.

Our plans for 2010-15 are designed to ensure that we maintain our high water quality standards. We are not investing to improve the taste and odour or hardness of our water. This is because the value our customers placed on making further improvements at the time we built our plan (2008/09) was lower than it would have cost to make them. Furthermore, research following our 2009 draft business plan, showed that taste and odour had lower support from customers than other improvements. We proposed at that time that the scale of our future programme should depend on the extent to which benefits exceed costs.

During this AMP, and following guidance from the Drinking Water Inspectorate (DWI), we implemented the holistic risk assessment approach referred to as Drinking Water Safety Plans (DWSPs). This has helped us identify new and emerging risks.

Water quality is assessed in accordance with Water Quality Regulations by taking samples at the customer's tap. In 2011-12 we achieved 99.97% compliance with the drinking water standards for all our regulatory samples. However, we have had an increase in single non-repeating coliform (bacteriological) detections at water treatment works and distribution service reservoirs since 2010. In response we have implemented detailed action plans. This includes increased investment and greater sampling at most risk sites and which was funded from an extra £150m investment package announced by Severn Trent in response to strong financial performance.

Where have we taken information from?

We have taken stakeholder views principally from the DWI and relevant legislation and guidance. Our customer evidence comes from a range of sources including willingness to pay (WTP) research and our quarterly customer satisfaction survey (tracker).

What have we learned?

The following section summarises the key insights we have drawn from this information.

Safety of drinking water remains the highest priority for our customers and stakeholders

Our customer research continues to show that customers place the highest value on receiving a safe supply of water. It is their top priority.

We believe stakeholders share this view. The DWI has reiterated to us that its priority is to ensure that public health is protected through safe drinking water quality (First meeting of the Severn Trent Water Forum, March 2012). It has expressed concerns about deteriorating trends in our distribution

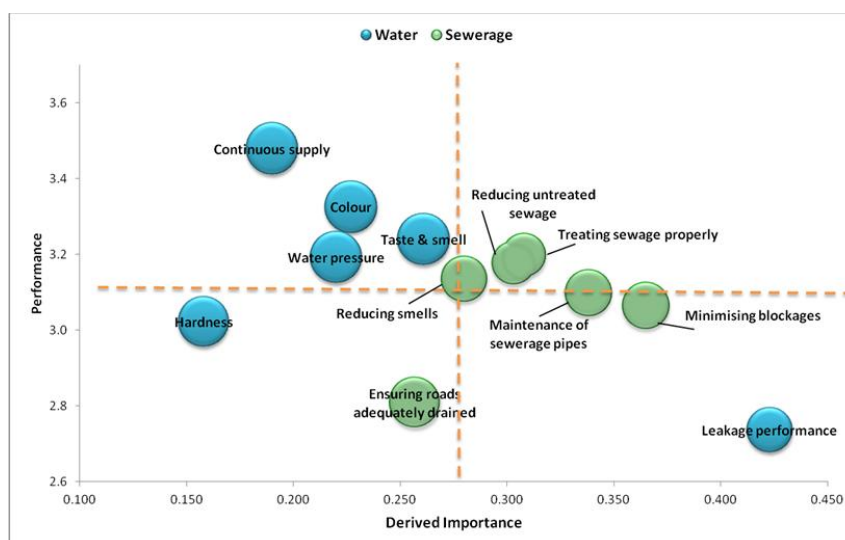
maintenance index. It has also stated that the industry lacks the skills and resources necessary for effective management of water quality (DWI Central Region report and letter to the Minister, June 2012).

We need to understand more about customer and stakeholder preferences about the pace at which we mitigate these risks.

Customers want a water supply with consistent taste, odour and hardness levels.

We believe our customers are broadly satisfied with the current taste, odour and hardness levels of their water. Our quarterly satisfaction survey suggests that taste, smell, odour and hardness all have low unstated preferences for our customers ie an improvement would not necessarily drive an improvement in satisfaction.

Revealed relationship between overall satisfaction and delivery of key services



2012 Q1 STW Customer Satisfaction survey

We do have incidental evidence, however, that changes in water taste or hardness, can cause dissatisfaction for our customers. For example, when we changed the source supply of water in Oswestry in 2007 this caused concern for residents. It suggests customers like consistency in their supply.

We have previously invested in improvements to hardness, taste and odour (2005 – 2010).

Between 2006-10 we carried out a programme of research into taste and odour. Research was conducted in four geographical areas. In three of these areas treatment works were fitted with low pH coagulation systems designed to improve the taste and odour of the water. One area received no such treatment and was used as a control. In all cases, customers were surveyed before and after the treatments had started. They were not told of the purpose of the research other than to assess taste and odour.

Irrespective of the treatment, all the areas surveyed showed more customers saying that their water was acceptable or very acceptable in terms of taste and odour. The proportion of customers with water considered to be acceptable rose by between 7% and 16% depending on the areas surveyed.

In all instances, these effects could not be attributed to the low pH coagulation applied. This suggests that investment specifically designed to improve taste and odour (as opposed to maintenance which might bring indirect benefits) did not directly improve customer satisfaction.

Hardness research was undertaken between 2007 and 2010. In two locations reverse osmosis treatments were installed to determine if they had any effect on customer perceptions. In addition, there were control areas in which no treatment was applied.

Between 2007 and 2010 the proportion of customers surveyed that said their water had an acceptable or very acceptable taste rose by 11% - 17%. This was true of all the areas surveyed, irrespective of whether reverse osmosis systems had been used to change water hardness.

Overall, we do not believe there is strong customer support to make widespread improvements in this area.

Discolouration is not acceptable

Our Willingness to Pay (WTP) survey suggests that customers are concerned about discolouration, particularly where this is associated with whether water is safe to drink. For the water supply attributes, discolouration has the highest value. The business customer survey shows that customers value discolouration above all other attributes.

Our quarterly customer satisfaction survey, however, suggests that customers are broadly satisfied with their current service. On the Q2 tracker 2012, 'colour' is 71% 'as expected', 12% slightly better than expected', 13% much better than expected. In fact, in terms of below expectations only 5% say this.

The evidence indicates that discolouration is a problem only experienced by a minority of customers, but that customers generally are prepared to pay to resolve these problems. Therefore, on balance, we believe there is some customer support for further investment to address discolouration.

We all need to address the use of metaldehydes

The DWI has stated that it wishes companies to consider the removal of traces of metaldehydes from drinking water sources (First meeting of the Severn Trent Water Forum. March 2012). The National Health Authority has confirmed that there is no risk to human health from the current levels being found. They are nonetheless above the level allowed for pesticides in European and UK drinking water quality standards. Water UK has contended:

“Although the levels being detected are above the standard for drinking water, the standard for individual pesticides is not set on a health basis, but as a near-zero value reflecting European Union legislation that pesticides should not be present in drinking water. This is really a technical and political issue about meeting a technical standard set on a “one size fits all” basis.”

Water UK, Briefing paper, October 2012

Water UK has further noted that the cost of removing metaldehyde through traditional treatment processes may be prohibitively expensive. It has suggested that the prevention of the pesticide entering raw water sources in the first place would be a better solution.

“It is therefore a very difficult compound to remove even using existing advanced water treatment processes. Further research is being carried out into other treatment methods but early indications are that even if they work they would be prohibitively expensive and energy consuming to implement.

The most sustainable solution is to control the pesticide at source to prevent metaldehyde getting into watercourses and rivers in the first instance. This is best achieved by changing the way metaldehyde is used in the catchment.”

Water UK Briefing Paper, October 2012

The DWI too has asked companies to consider what role catchment management could play in tackling metaldehyde (First meeting of the Severn Trent Water Forum, March 2012). Our discussions with stakeholders indicated that they would be supportive of us working in partnership.

We should work in partnership

At our water workshop on 12 June 2012, we raised the question as to the extent to which we should work in partnership with other organisations to protect our raw water supplies. There was widespread support for greater partnership working:

A council officer said ultimately STW benefits from better quality water. S/he added ‘if working together can improve water then surely it is in everyone’s interest’

A conservation group representative pointed out that farmers in the past were unaware that some of their actions were harming the water supply. S/he stated that since farmers have been made aware of this, they are ‘now working with agencies to help improve the water supply’ and farmers have been informed that different practices can pollute water.

A conservation group representative said that certain chemicals are ‘incredibly difficult to remove from the system, but there are very good reasons why farmers use them. Perhaps they have to be incentivised not to use them, as they have been done in some areas’

Stakeholder comments from the water workshop, 12 June 2012

This was echoed by some written responses to *Making the right choices*. Coventry Citizens Advice Bureau noted a catchment based approach could be taken. The Birmingham and Black Country Wildlife Trust supported further investment in catchment management.

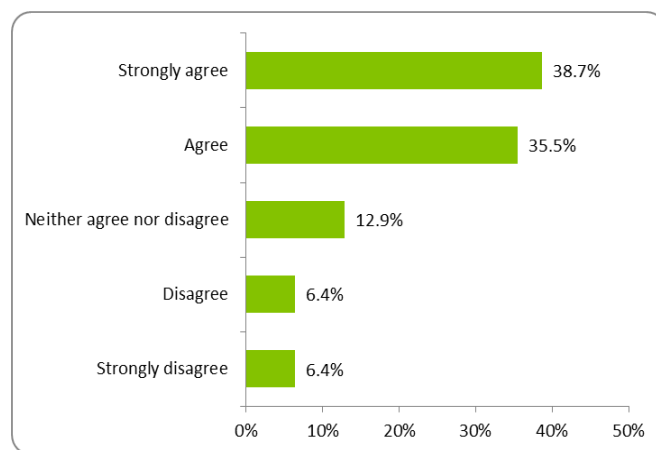
“In order for STW to increase its capability and effectiveness in partnership working it will need to prioritise engagement and increase investment in staff, skill and project resources. This increased ability to work in partnership with a range of stakeholders and partnerships would have the return of enhanced and effective catchment management and a higher positive profile for STW, being part of active partnerships and projects achieving better outcomes for the water and natural environment and also for STW as a public company in the public eye.”

Stakeholder written response to MTRC

Workshop attendees also supported us incentivising other parties to change their practices.

Water workshop, 12 June 2012

To what extent do you agree with the following statement? “STW should incentivise land owners to change their land use practices if it protects raw water supplies”



Although, as the discussions at the workshop highlighted, not all attendees agreed with this. One attendee believed that the agricultural sector was already sufficiently incentivised, through, for example, the Common Agricultural Policy.

“A business group representative disagreed with the idea of more money added bills as s/he felt the ‘extra costs are paid through tax’. S/he said customers will need an explanation for the extra cost and the benefits the customer will receive”

“A council officer said the focus should be on education and collaborative approaches, not cash incentives”

Stakeholder comments from the water workshop, 12 June 2012

In its written response to *Making the right choices*, CCWater suggested it would support such approaches where the benefits to customers could be demonstrated.

“However, these schemes can be more risky since they are delivered over a longer time frame and there may be less certainty about the outcomes. In the past, we have taken a pragmatic line towards such schemes where it was clear that these would reduce costs to water customers in the long-term. For example, we supported Wessex Water’s choice to pay land managers to change their practices...Where customers money is paying for these schemes, it is vital that there is clarity about benefits and costs to them.”

CCWater written response to MTRC

On balance, we believe there is a good level of support for working with other parties to protect our raw water sources. In many cases, this support extends as far as incentivising others to change their behaviour. This support for partnership working is further reflected in comments relating to the use of catchment management to improve river water quality in our region (see objective: we will protect our water environment). We note, however, that there must be demonstrable benefits to customers from this approach.

We need to further understand the desired pace of change on lead

The requirement to comply with a standard for lead has been in place for some time. Lead is commonly found in drinking water as a consequence of lead pipes. We have been undertaking a programme of lead replacement in 2010-15. The DWI would like us to consider the pace and scale of this programme for 2015-20.

Lead is usually measured at the customer’s tap, meaning that both we and the customers (who are responsible for the supply pipes on their properties) need to work together to achieved the standard. We need to further understand customers’ views on the scale and pace of further replacement activity.

In summary, what have we learned so far?

We have learned from the evidence we have gathered to date:

- Maintaining standards should be a priority.
- Given the importance that customers attach to this issue, there may be support for some further investment to address certain issues. We need to further test views on: the pace at which risks are reduced; who is best placed to deal with metaldehydes; our approach to lead; and whether we could bring discolouration benefits, for example, through maintenance activity.
- We believe that there is limited support for further improvement in taste and odour and hardness. We therefore consider that the benefits to customers are unlikely to exceed the costs involved. There may, however, be localised issues that we need to consider further.
- There is strong support for greater catchment management and partnership working to protect our raw water sources.

- Customers like consistency in their water supply. In building our plan, we need to be aware of how changes in approach elsewhere (for example water trading, abstraction changes and the expansion of the strategic grid) could affect this consistency.



2. We will ensure water is always there when you need it

Where are we starting from?

We set out our long term aspiration in our Strategic Direction Statement to provide a continuous supply of quality drinking water to our customers, noting the key challenges facing us in the future such as increasing population, climate change, environmental pressures to reduce abstraction and increasing customer expectations. We noted that there was strong customer and stakeholder support for reducing leakage. We stated that our long term objective was for all customers to be metered (where it is practicable to do so), and our research showed that the majority of customers agreed this to be the fairest method of charging.

In our 2010-2015 business plan, we recognised that ensuring a reliable, safe water supply is the top priority for our customers. Our plans were designed to ensure that we increased the resilience of our assets to reduce the risk of supply failures, reduce interruptions to supply, and balance supply and demand through reducing leakage and promoting water efficiency.

In our water resources management plan we explained in more detail our overall aim of achieving and maintaining the level of headroom necessary to ensure we can deliver our target levels of service at 'least cost' to customers, whilst minimizing the impact on the environment. We explained we plan to do this in part by reducing leakage and managing the demand for water, and partly by developing new resources. Our longer term strategy is to make better use of our existing resources by maximising their sustainable use and further integrating our network. We further discuss the impact of our abstractions on the environment under our objective: 'We will protect our water environment'.

A major resilience programme was planned for AMP5, although our isolated communities programme was not accepted at the 2009 price review (PR09). We were also supportive of growing our strategic grid.

At the end of 2011-2012 we have a good track record in terms of SOSI index (a measure of whether our supply capacity is sufficient to meet demand) and our leakage performance is on track. During AMP5 we carried out a selective metering trial, metering some properties when there is a change in occupier. Our AMP5 interruptions performance needs improvement and there are plans in place to achieve this. We have good performance in terms of low pressure.

In 2011 our per capita consumption (pcc) was 133 litres/head/day for unmeasured households and 112 litres/head/day for measured households. In the previous five years, since 2007, our measured pcc has declined from 117 litres/head/day and was the lowest in the industry. Our metering penetration has increased over the past five years from 28.6% in 2008 to 34.7% in 2012.

In November 2012, the Environment Agency published a consultation on a proposed new classification for water stressed areas. Under this new classification the Severn Trent region would be classified as water stressed. We noted in our response, however, that whilst there were water stressed catchments in our region, this was not the case for the entire region.

Where have we taken information from?

We have taken stakeholder views from a range of sources, but principally from our workshop on 12 June 2012 and written responses to *Making the right choices*. Around 32 individuals representing 28 separate organisations attended our water workshop.

The views of customers have been taken from a range of sources including: our willingness to pay research; our historic catalogue of research (spanning 20 years); the views of CCWater and relevant research carried out by CCWater and Ofwat.

What have we learned?

The following summarise the key insights we have drawn from this information.

Our approach to supply demand should represent a shift to a best value solution (rather than least cost) which balances environmental impact and affordability

Guidance from the Government and the Environment Agency, and the views of our stakeholders, suggest that we should select the 'best value' option to balance supply and demand rather than the options which have the lowest financial cost. A 'best value' approach would include seeking solutions that would deliver longer term environmental benefits. This should also take into account customer views on what is acceptable and affordable.

To manage future supply and demand and reduce the pressure on the environment from the water we abstract from rivers and other water sources, we need to be smarter in using the supplies we have, develop new ways of capturing, storing and sharing water, and reduce the amount of water we waste. We also need to take action where too much water is being abstracted from catchments and damaging water ecosystems, and reform our approach to abstraction to reduce the risk that these problems become worse in the future.

Defra, strategic policy statement to Ofwat (draft for consultation)

“A preferred solution will have to be decided on the basis of it being the best value for water company customers and the environment. The final preferred solution may not necessarily be the least cost option”

Defra / Welsh Government / Ofwat / EA Water resources planning guidelines

“We would like to see options selected which give the best value (not necessarily the lowest cost). Options should be selected which also cause the least environmental impact”

EA MTRC written response

“We consider that all decisions should be driven by customer’s views on what they think is acceptable and affordable”

CCWater MTRC written response

Supply/demand balance

There is a political and regulatory expectation that we will reduce demand.

Guidance from the Government expects companies to deliver demand reductions over the long term, and in the next five years where demand is high or water resources are over-used.

“Where companies are in designated water stressed areas, or where they have demand that is significantly above the national average, we expect companies to produce a plan that will deliver overall demand reductions in the first five years. Looking further ahead we will expect all WRMPs to demonstrate that the demand trend is significantly downward”

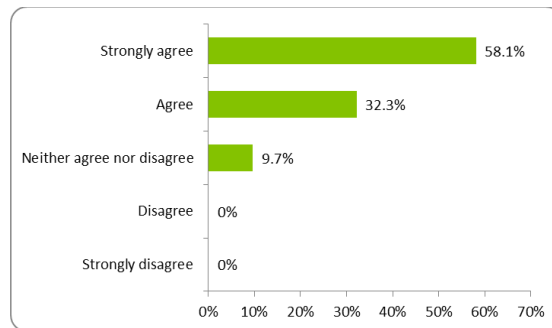
Defra White Paper, Water for Life, December 2011

Stakeholders emphasise demand management options, although there is no consensus on which. On the supply side stakeholders believe we need to make the best of what we have got. However there is some qualitative evidence of customer support for new supply options.

Stakeholders at our water workshop supported demand reduction options over new source development. This was further reflected in written responses to *Making the right choices*.

Water workshop, June 2012

To what extent do you agree with this statement: “STW should prioritise demand reduction options over new source development”



“A mixed package of options, emphasis on reducing demand through education”

Stakeholder MTRC written response

“We support an approach which makes best use of the water resource you currently have access to before the development of new supplies”

EA MTRC written response

“Priority must be given to managing / ensuring the efficiency of the existing water supply before new options are considered”

Stakeholder MTRC written response

“STW should seek to secure the supply of water whilst reducing the environmental impact...In order to achieve this, priority should be given to improving water efficiency, reducing leaks, and accelerating the roll out of water meters. STW should also seek to invest in expansion of the grid...these measures should take priority over investment in new assets and sources of supply”

Stakeholder MTRC written response

“English Heritage considers that the more efficient use of existing supplies be prioritised, as for example through reducing leakage, the introduction of demand management measures and wider catchment management measures. The increase in supply through the exploitation of new sources and or greater extraction could potentially impact the historic environment”

Stakeholder MTRC written response

Stakeholders also recognised the potential future impact of climate change on the supply demand problem and agreed it was our responsibility to encourage customers to be more carbon efficient in their water usage.

“Reducing leakage and increasing water efficiency will become increasingly important and should be given equal priority. The predicted impacts of climate will inevitably lead to a change of services offered by ST, including more regular hosepipe bans”

Stakeholder MTRC written response

“It is clear from the Met Office rainfall deficit maps that part of the STW region will be impacted by future water shortages...Whilst it is recognised that reducing leakages or moving water around the region can help to address concerns over the water supply, it is considered that STW should address supply issues as part of a holistic approach”

Stakeholder MTRC written response

Comments in our quarterly tracker research show some customers express an interest in more reservoirs being built. The logic underpinning this is that they feel they are paying their bills and “doing their bit”, but water companies should spend money to ensure we have more supplies. Research carried out by CCWater in 2012 also shows some people believe companies should build more reservoirs to avoid hose pipe bans in the future.

In our Q3 2012 customer satisfaction survey most customers see meeting the supply/demand balance as a joint responsibility between them and the water companies. There is a slight emphasis for some towards this being more a water company responsibility:

- 11% responsibility lies more with customers
- 23% more with companies
- 67% combination of the two.

Water efficiency and education

Customers do believe it is acceptable to be asked to reduce demand. Education has a key role going forward.

Our stakeholder research shows 99% of those surveyed believe that helping customers to be more water efficient should be a priority for us. Stakeholders at our water workshop felt that incentives ought to be offered to customers to save water. Practical initiatives such as subsidising water butts so homes did not use drinking water to water their gardens or wash their cars were suggested by a number of stakeholders.

Research carried out by CCWater in 2012 showed that nine out of ten customers feel it is acceptable to be asked to reduce demand during a drought or hose pipe ban. However two out of five customers feel it is unacceptable to be asked to reduce usage all of the time, or when there is not a hose pipe ban.

“Greater education is needed so that customers understand the value of their water and the consequences of wasteful use”

Stakeholder MTRC written response

Research carried out by CCWater in 2012 showed that a third of customers feel their water company should provide them with more information about how to use less water.

Our customer tracker research shows that creating “water awareness” changes behaviours and perhaps, paradoxically, increases satisfaction.

Although our customers say they want to reduce demand there is little evidence that they take active steps to do so, and we use more than we think.

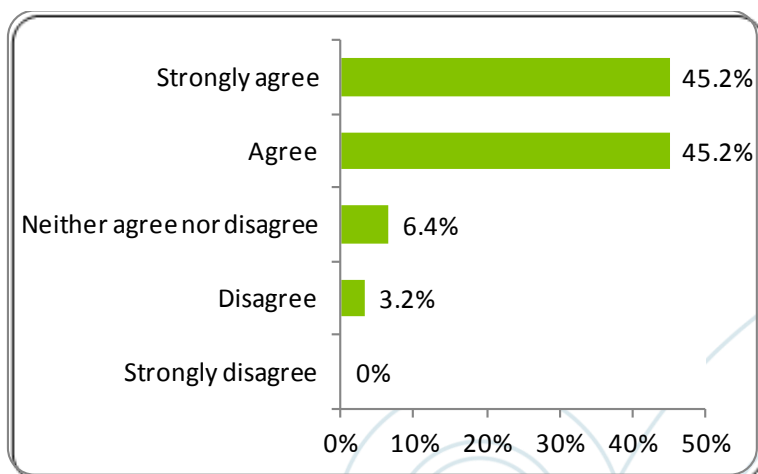
Our customers think it is acceptable to be asked to reduce water consumption; however few are doing anything radical to save water aside from showering rather than bathing. 33% of customer claim to have bought or installed something specifically to save water.

In 2011/12 we did some research into grey water recycling. We found there is a lot of interest in this area, especially for use in toilet flushing and the garden. However customers are not prepared to pay very much for it (circa £90 for a retrofit rain water harvesting system for the toilet).

Unilever research on customer awareness on water usage shows misaligned understanding of actual use. Findings reveal that the average shower is 8 minutes long and uses nearly as much energy and water as a bath, and that the average power shower could use nearly twice as much

Water workshop, June 2012

To what extent do you agree with this statement: “STW should retain its current focus on water resource efficiency (keeping the input per customer low)”



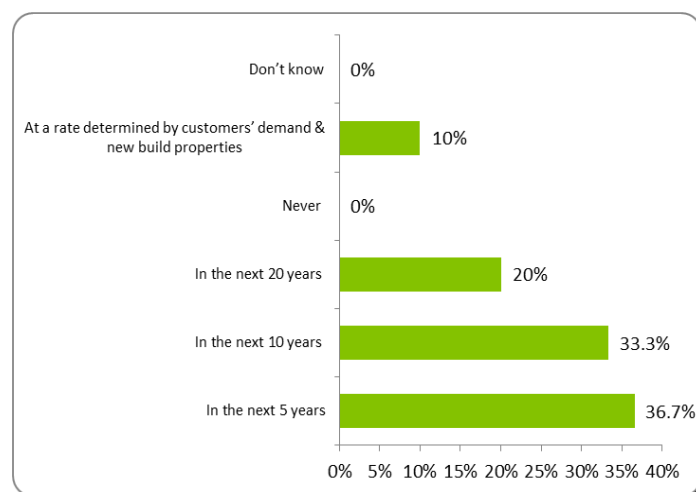
Metering

Stakeholders show clear support for metering as the fairest method of paying for water and sewerage services. However there is no consensus on the pace and the affordability impact on vulnerable customers must be addressed. We also need to bear in mind we cannot universally meter unless our area is designated as “water stressed” by Defra / EA (it is not currently designated but may be in future).

Stakeholders at our water workshop supported metering. Some felt this must also be supported by education to show people have to save and reduce usage. This was further reflected in written responses to *Making the right choices*.

Water workshop, June 2012

All customers should have a meter...



Some further views expressed at our stakeholder workshop were:

“A council officer stated that people are resistant because it’s a change, ‘but if people don’t attach a value to something it’s often wasted’”

“A council officer said that STW had an ‘incredibly conservative target for metering, you pay for what you use in every other walk of life, why not water?’”

“An environmental group representative said there is some research that suggests at the start, having a meter causes consumption to reduce but then it ‘creeps back up.’”

“A council officer highlighted that there is an environmental benefit with a reduced carbon footprint”

“The company must try and meter more houses. The best way to do this would seem to be by making it compulsory to install a meter on change of occupier. Increasing connectivity and water trading must also make sense”

Stakeholder MTRC written response

“We believe that metering is the fairest basis of charging for water and sewerage services, but STW first need to take into consideration the impact of more metering on the vulnerable and low income customers”

CCWater MTRC written response

“Educate customers on potential benefits to them and increase progress on roll-out of water meters where possible. Consider mandatory metering in some circumstances”

Stakeholder MTRC written response

“We support...that the future charging system should in general be based on a metered system...we recognise that affordability is an issue for some customers and this needs to be developed alongside any proposals to apply metering more widely”

EA MTRC written response

“Until customers actually pay for the amount they use, as with gas and electricity, then that appreciation (of the value of water) will not come, our belief is that this is best achieved through a rolling programme of, socially responsible, metering”

Stakeholder MTRC written response

The Defra White Paper also states that *“we believe water companies are best placed to find the appropriate local solution in discussion with their customers. Government is interested in the potential of smart water meters to improve water company network management and encourage more sustainable water use by consumers. Government wants water companies to do more to actively promote metering to those who would benefit and to make switching as simple as possible for those who chose to do so”*.

Customers also support metering, and research shows metered customers are more satisfied with value for money and affordability.

Our quarterly customer tracker research also shows that 55% of customers think everyone should be on a meter and pay for just what they use. 61% would prefer to pay based on a meter reading / what they use as opposed to a fixed charge irrespective of their use.

Our tracker research also shows that metered customers are generally happier with us in almost every way. Customers with meters rate us better on almost all measures including value for money. 45% of metered customers agree we represent value for money compared to 40% of unmetered

customers, and 44% agree we are affordable compared to 33% of unmetered customers. CCWater's tracker research in 2011-2012 also supports the view that metered customers are generally more likely to think their bill is affordable, more satisfied with aspects of their water service, more aware of company services such as compensation for failing to meet standards, different tariffs such as WaterSure, or services for the elderly, and more likely to take actions to reduce their water usage.

Studies also show the impact of metering on driving down demand.

Our tracker research suggests that water metering has quite an effect in reducing the amount of toilet flushing and also the way in which gardens are watered. 38% of metered customers don't flush the toilet every time it is used compared to 21% of unmetered customers.

There is however very little evidence that metering has much effect on purchasing or installing specific devices.

We need to review our AMP5 selective metering trial

Our AMP5 selective metering trial has shown that we do have the ability to selectively meter customers. However it also showed that there are high unit costs for selective metering compared to a metering optant, the process of warrant of entry/enforcement needs reviewing to ensure a consistent approach, and that the process was not popular with customers, leading to lower scores in Ofwat's Service Incentive Mechanism, measuring customer satisfaction.

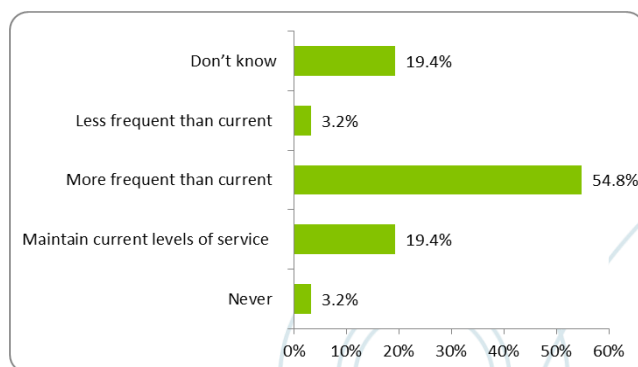
Hose pipe bans

Our stakeholders show a clear consensus that more frequent hose pipe bans are acceptable in the event of low rainfall.

Stakeholders who attended our water workshop believe that more frequent hose pipe bans would be acceptable. Bans might also help highlight the issues of water scarcity.

Water workshop, June 2012

What is an acceptable frequency of hosepipe bans?



Some stakeholders at our water workshop expressed different views:

Water workshop, June 2012

“A conservation group representative stated that hose pipe bans are needed. S/he commented that the target of having a hose pipe bans ‘3 times every 100 years in grossly inadequate’.”

“A conservation group representative commented that STW needs to avoid hose pipe bans when water levels are low.”

“An environmental group representative made the point that drinking water is used on gardens and it is expensive. S/he said the use of hose pipes should be seen as an added benefit not a standard requirement that STW needs to provide”

“A conservation group representative stated that ‘farmers worry about hosepipe bans because of the possible effects it could have animals’ and that they also worry about the possibility their water supply could be cut off”

“A council officer commented that it ‘focuses the public’s mind if we have hosepipe bans, and encourages people to think ahead. It is a good public awareness exercise”

“A council officer speculated that if there are extreme environmental conditions then hosepipe bans are acceptable but STW has to update it targets to reflect what is ‘happening in the wider environment”

“An environmental group representative pointed out that some people think that if they are paying then they can use what they want”

“A council officer said that bans are always dependent on supply-side restrictions. S/he opined that the ‘odd hosepipe ban is not necessarily a bad thing’. S/he thought bans would help people understand that water is a finite resource and serves to connect people to the environment”

“A business group representative said that, ‘as a customer s/he would not expect a ban but if STW hasn’t got the resources then s/he would be more understanding. There are not many ways to restrict water uses. Customers have to realise that there is not a limited supply- this is the first point of limiting supply.”

Our willingness to pay research shows customers place a low priority on hose pipe bans.

Our customer willingness to pay research shows customers place a low priority on hose pipe bans, and this is backed up by CCWater research which suggests a large number of customers (78%) would be unwilling to pay anything more to avoid hose pipe bans.

Our historic tracker research shows that in the event of low rainfall, 68% of customers are in favour of a hose pipe ban. 44% of customers would be in favour of imposing a ban earlier, to prevent harsher restrictions in the future.

However we must not use hose pipe bans for failures in our service delivery.

Our historic tracker research shows customers think hosepipe bans need to occur because (in decreasing order) of lack of rainfall (77%), water companies not dealing with leaks (59%) and households wasting water (45%).

"More frequent hose pipe bans could delay or even reduce the need for new water sources or provide a surplus which could be used as a transfer to a company. It is an option that should be fully considered"

EA MTRC written response

"The level of service that customers receive will be impacted by the implementation of measures necessary to meet the WFD and should not be dictated by an arbitrary target; therefore customers may have to face an increase in the number and frequency of hose pipe bans..."

Stakeholder MTRC written response

Leakage

There is a political and regulatory expectation that we will reduce leakage.

We want to see the downward trend for leakage to continue. If a water company is unable to reduce leakage further during the planning period it must clearly justify its position.

Defra / Welsh Government / Ofwat / EA Water resources planning guideline

Leakage needs to be maintained at the point where the environmental, economic and social cost of water saved by reducing leakage is lower than, or equal to the cost of getting water from other sources. As ELL us developed it is likely that companies will undertake more wholesale mains replacement than simply patching up small sections of mains. In the longer term this is likely to be a more effective and efficient method of cutting losses from the network.

CCWater Policy Position, November 2010

Visible leakage is a key area of customer dissatisfaction, and tackling it is key to getting customers to reduce demand. We also need to respond to leakage better, including when it is reported to use. Tacking leakage is a customer priority equal to safe water.

For stakeholders, the second most important thing they want to hear about from us is how we are tackling leakage. Around 98% of them consider this to be a priority - the same extent to which they consider delivering safe drinking water. Research carried out by CCWater in 2012 showed that customers identified both lack of rain and leaks from pipes as equally important causes of drought.

Our own customer tracker research shows that customers rate our leakage performance as the number one area of dissatisfaction, and top area for improvement and have done so consistently for

years. 53% of customers think we should do more in this area, compared to 26% who think we are doing the right amount.

Almost all our qualitative research underpins this, suggesting that customers find being charged for something that they see us as wasting is fundamentally unfair, especially when they are being asked to conserve water or are subject to a hose pipe ban.

“Leakage continues to be a key issue for customers and can be a barrier to them doing more to save water. We, therefore, believe that customers would support the company’s current work to reduce leakage”

CCWater MTRC written response

“Our experience shows that when our residents report a leak to STW there is no consistency in the response they receive, sometimes the sewers will be checked and there is no follow up to check the mains”

Stakeholder MTRC written response

“We endorse continuing to reduce leaks from the network and to increase the number of customers with metered water”

Stakeholder MTRC written response

“My impression is that there isn’t a shortage of water, it is just in the wrong place and there is an issue with leakage”

Council officer, Water workshop

Some of the comments at our water workshop were:

“A council officer said that STW doesn’t do enough to publicise what it does to prevent leaks, and that perhaps local information on leakage prevention could be provided to customers”

“A council officer expressed the view that there should be a focus on leaks on highways as these can cause accidents. S/he said ‘in the past I have discussed leaks on highways with STW who have initially denied the leaks were their responsibility, but I have then been proved right”

“An environmental group representative said that a cost-effective approach needs to be taken by looking at whether it costs more to repair a leak than let it continue”

“A council officer said people wouldn’t mind paying more to ensure major and important leaks are repaired”

“A conservation group representative agreed with the earlier cost-effectiveness point. ‘I don’t want to see water wasted, but cost has to be taken into account, it has to be a realistic and practical approach’.”

Customers expect large leaks to be dealt with quickly. More noticeable or visible leaks are the priority.

On the question of expectations for response times, our Q3 2012 customer satisfaction tracker found that:

- Noticeable large leaks are expected to be dealt with within 1 day by most customers.
- Similarly, large leaks that are less noticeable are expected to be dealt with in around 2 days.
- For small leaks, differences between expectations of visible versus non-visible is less pronounced. Typically the expectation here is 3-4 days.

On the question of priorities, as with response expectations, there was a slight preference for visible leakage. However, most customers regard these of equal priority, if not response speed:

- 9% say non-visible leaks are a priority
- 13% say visible leaks are a priority; and
- 77% say treat both the same.

The concept of unaccounted for water needs to be explained more widely.

At our water workshop a significant proportion of attendees were not aware of the issue of 'accounted for' and 'unaccounted for' water. The feeling across the group was that STW does not currently do enough to address unaccounted for water.

Resilience

There is a clear need for resilient assets and service

Defra's White Paper highlights the need to make sure our existing infrastructure can continue working efficiently. It recognises that a changing climate is not just a threat to the amount of water available but that it also threatens our supply systems, for example through increased flood risk.

In their responses to our consultation *Making the right choices* our stakeholders also support the need for a resilient water supply and to include projects that deliver an adaptation benefit in our plan at a low additional cost.

"It is essential that a supply of water is maintained for our residents and this should be achieved by ensuring the supply is resilient through growing the grid and maintaining current assets"

Stakeholder MTRC written response

"We believe it is important for STW to continue to strengthen its network and carry out work to better understand risks and vulnerability to its assets...we believe that resilience should be delivered with minimal additional financial impact"

CCWater MTRC written response

In our workshop some stakeholders disagreed – a business group representative thought STW is spending too much on resilience instead of the basics such as pipes etc...They saw this as “*saving the world without thinking about day to day upkeep*”. However the majority (64%) support the inclusion in our plan of projects that deliver an adaptation benefit at a low additional cost, with 36% supporting the inclusion of projects solely driven by adaptation.

Our approach needs to be incremental, risk based and over the medium term. Customers do not want to see drastic increases in bills.

“We feel you should tackle them [issues] in a systematic way in the medium term where risks are greatest and there are no regrets...And we support your current approach which is evidence led, flexible, takes action where there are multiple benefits...”

Prioritisation should be based on the likelihood and consequences of failure – for your business continuity, for your customers and for the environment...we feel the option you should chose should be the best value option taking a medium/long term view”

EA MTRC written response

“We believe a sensible approach be to reduce risks by tackling them in a planned way over the next 20 years”

CCWater MTRC written response

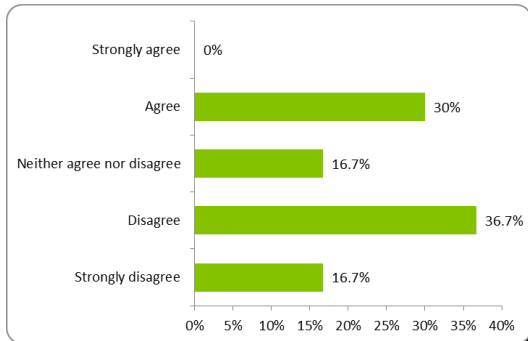
Customer research conducted by Ofwat in 2011 found that customers were willing to start to pay smaller amounts now in order for water companies to be able to begin to put measures in place and avoid the need for more drastic increases in bills in the future.

Stakeholders accept that some customers may have a different level of service

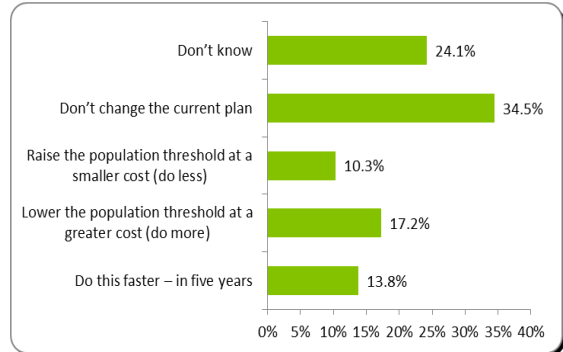
Stakeholders who attended our workshop disagreed that all our customers should benefit from the same level of resilience. Some felt that the reliability of other utilities, such as electricity or the internet, is dependent on the geographic area and that it was a fact of life that the demand in rural communities would be different from that in urban ones. There was little support to change our current plan to increase the resilience of populations greater than 20,000 that rely on a single source of supply over the next 10 years.

Water workshop, June 2012

To what extent do you agree with this statement:
All our customers should benefit from the same
level of resilience?



STW plan to increase the resilience of
populations > than 20,000 that rely on a single
source of supply over 10 years. Should we?

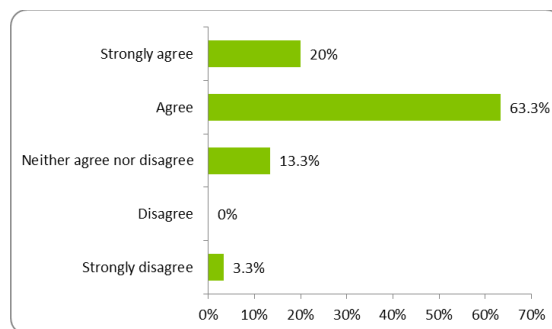


There is clear support for the concept of the strategic grid

Stakeholders who attended our workshop agreed that we should increase resilience through growing the strategic grid. Working effectively with neighbouring water companies was widely viewed as a good way of helping STW's resilience in the future. Support for the strategic grid was further reflected in written responses to *Making the right choices*.

Water workshop, June 2012

To what extent do you agree with this statement: "STW should increase the resilience of their customers' water services through growing the grid"



"We support an approach which builds resilience by increasing greater connectivity of your strategic supply network"

EA MTRC written response

"Investing in the strategic grid to the north east of the region which is most vulnerable to water scarcity is fundamental to that going forward"

Stakeholder MTRC written response

Some assets, such as our major aqueducts, are too critical to fail

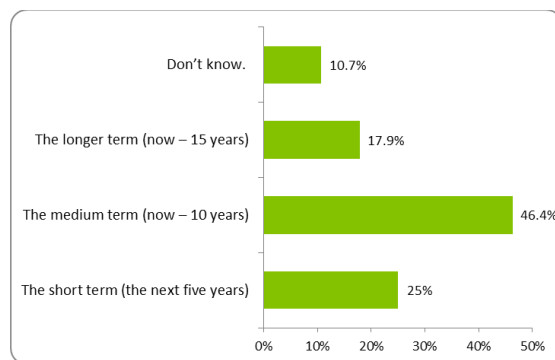
Stakeholders who attended our workshop felt that the risk of aqueduct failure should be mitigated over the short – medium term.

77% of stakeholders were in agreement that certain assets are too important to be allowed to fail and that maintenance of these assets was of paramount importance. There was consensus that STW should not adopt an approach whereby it simply fixes certain assets after they have failed. Instead, it was felt that STW should be more proactive in its approach. Most stakeholders felt that STW should work quickly in order to have the capacity in place to allow for long-term controlled shutdowns of its aqueducts.

Stakeholders who attended our workshop felt that the risk of aqueduct failure should be mitigated over the short – medium term.

Water workshop, June 2012

“How quickly should we aim to mitigate the risk of disruption to water services presented by an aqueducts failure?”



Some of the other views expressed at the water workshop were:

“A business group representative highlighted that if the problem can be predicted then it should be prevented and that ‘if it happens it should never happen again’

“An environmental group representative believed that lack of maintenance is unacceptable, STW should be on top of it as it is such a big part of the service”

“A conservation group representative thought there must be a degree of control over the asset; if STW hasn't invested enough in an asset it is unacceptable. S/he added, terrorism is more forgivable as it is a variable you can't control”

“A council officer made the point that aqueducts are not built to last forever, ‘they will fail at some time in the future, they will crack up at some point’”

Customer research, conducted by CCWater after the 2007 Mythe incident, shows customers felt that such an incident should never happen again, anywhere. Participants in the research wanted to see action based on the belief that in the future, with the predicted increases in extreme weather; flood levels are likely to be significantly higher.

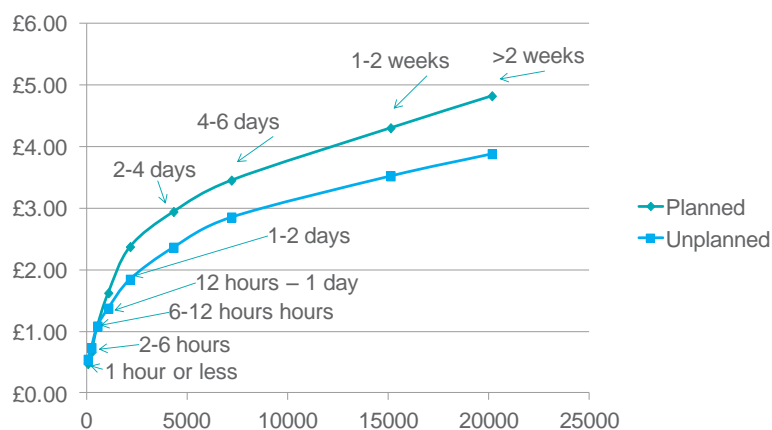
Interruptions to supply and low pressure

Customers continue to support investment to maintain a reliable service by reducing interruptions to supply

Our willingness to pay customer research shows that preventing interruptions remains a priority for our customers. A noticeable finding is that planned interruptions are valued more highly than unplanned interruptions.

When tested in our Q3 2012 customer satisfaction tracker, customers similarly valued reducing planned interruptions higher than unplanned.

How much extra, if anything, would you be prepared to pay on top of your current annual water bill to reduce the chances of a unplanned interruption to your water supply for each of the following situations?



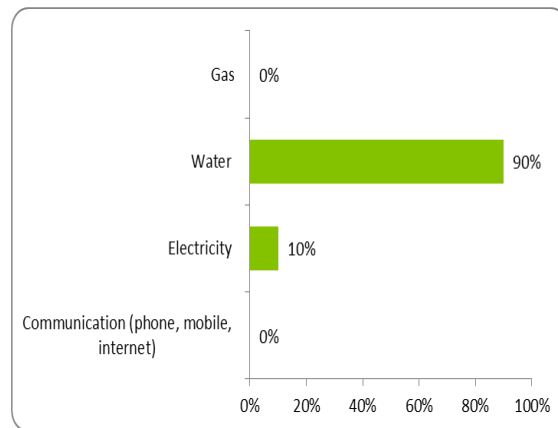
However, when faced with a 'forced choice' customers chose unplanned interruptions as the type that STW should invest most to avoid – 80% say invest more in unplanned interruptions, 20% say invest more in planned interruptions.

And when there is a supply failure, most customers (90%) expect it to be fixed within 12 hours. 99% expect it to be fixed within 2 days. Few customers regard discoloured water after a interruption as inconvenient (14%). The key issue is getting water back on.

In our water workshop stakeholders ranked water as the utility they would least want to lose for a week.

Water workshop, June 2012

“If you were going to lose one of your utilities for one week which one would you least like to lose?”



Water workshop, June 2012

“A council officer said that 5,000 customers without water for 12 hours in the STW region is a very low percentage, so resilience didn’t seem bad”

“An environmental group representative commented that it depends if you are one of the customers who has lost their supply whether you think the current level of expenditure on resilience is good value”

“A council officer said ‘you can’t plan perfectly for these things.’ S/he added: you can’t eliminate risk. Sometimes it is actually better to provide compensation for people after an event”.

“A business group representative pointed out that 17 days without water for a hospital is different to 17 days for a house”

Our customer research also found that, although many customers has experienced low pressure, they were generally unperturbed by this disruption to their water supply. Both the domestic and business customer willingness to pay values are lower than our previous research at PR09.

Our stakeholder research showed that they rated us most highly for a reliable service, followed by responding well to emergencies.

In summary, what have we learned so far?

We have learned from the evidence we have gathered to date:

- There is support for moving to a best value approach rather than least cost in our approach to water resource management planning. Stakeholders strongly support demand management, however we need to explore the balance between demand management options and pace. We could also test the appetite for more supply options.
- There is wide ranging support for metering. Although we cannot universally meter we can explore attitudes to compulsory metering. However we need to explain how vulnerable customers would be protected and promote innovation in terms of technology and tariffs.
- Leakage is acknowledged to be a priority for customers and stakeholders. We should focus not just on the economic level of leakage (ELL) but also on exploring attitudes and response times to visible leaks.
- There is support for more frequent hose pipe bans, however we need to explain what increased frequency we mean.
- There is a strong support for greater customer education and water efficiency initiatives. We should take this opportunity to explain the value of water, the ELL, unaccounted for water.
- There is strong support for the strategic grid and growing our network.
- Our approach to the resilience of our assets needs to be risk based and over the medium term. Some of our assets are too critical to allow to fail, we need to develop our risk and consequence evidence to develop our programme.

3. We will safely take your waste water away

Where are we starting from?

We began AMP 5 with the view that sewer flooding is unacceptable. We set out our long term aspiration in our Strategic Direction Statement to eliminate it. We noted that there was stronger customer support for reducing internal sewer flooding than external sewer flooding.

At the end of 2011-2012 we had reached our forecast historic risk register position. We are increasingly finding that problems which we are now addressing require increasingly complex and expensive solutions.

We also recognised that the statutory framework regarding the management of flood risk was changing. We explained our commitment to work with other stakeholders, including lead local flood authorities (LLFAs), under the provisions of the Flood and Water Management Act 2010.

Where have we taken information from?

We have taken stakeholder views from a range of sources, but principally from our workshop on 12 June 2012 and written responses to *Making the right choices*. Around 40 individuals and 29 separate organisations attended our waste water workshop. Over 50% of attendees were from local authorities. The remaining attendees represented environmental groups or customers. We held a further dedicated workshop with LLFAs and the Environment Agency on 25 September 2012.

The views of customers have been taken from a range of sources including: our willingness to pay research; our historic catalogue of research (spanning 20 years); the views of CCWater and relevant research carried out by CCWater and Ofwat.

What have we learned?

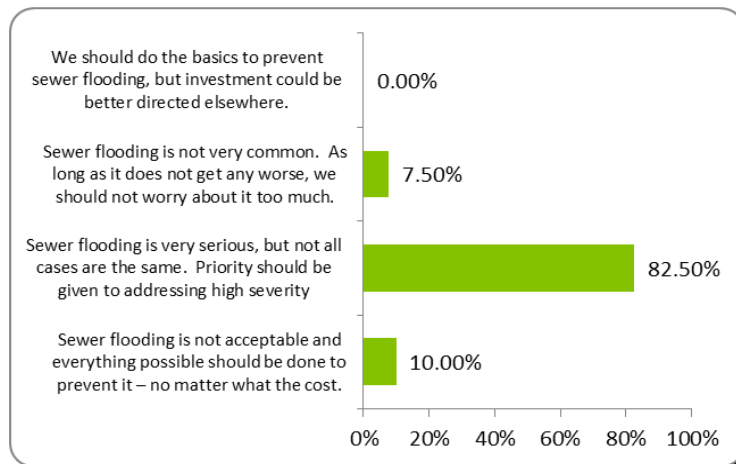
The following summarise the key insights we have drawn from this information.

Sewer flooding is serious and must be tackled quickly, but not at any cost

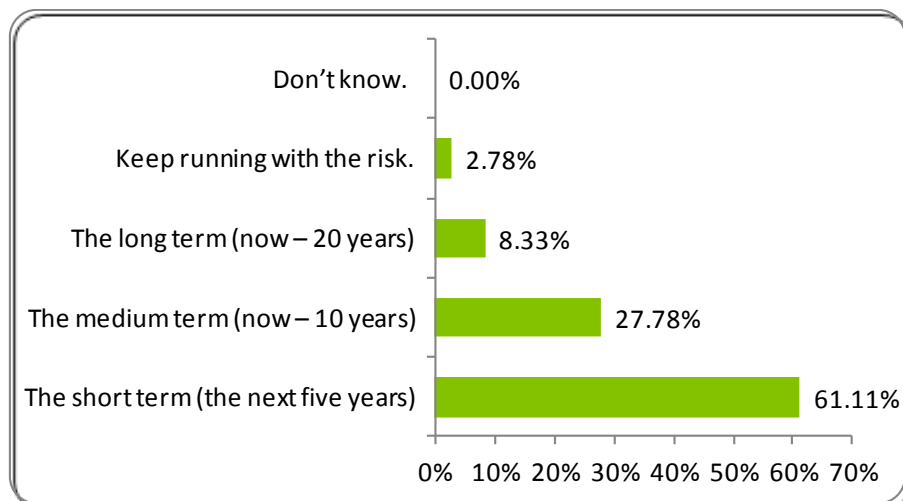
Stakeholders who attended our workshop believe that sewer flooding is very serious, and that the most severe cases should be dealt with in the short term.

Waste water workshop, June 2012

Which of the following best describes your views on sewer flooding?



How quickly should we aim to resolve the most severe sewer flooding?



Values from our willingness to pay research indicate that reductions in sewer flooding are likely to be a high priority for customers. The value attached by our customers was much higher than at PR09. The gap in valuations between internal and external sewer flooding has also narrowed.

Results from other customer research also indicate there may be modest support for an increase in investment in sewer flooding. Our 2011 Q4 STW Customer Satisfaction survey indicated that 66% of customers wish to maintain investment levels, 29% wished to see more and 5% wanted to see less (within an envelope of £2).

CCWater's response to *Making the right choices* agreed that sewer flooding is unacceptable to customers and should be a key priority. It did not agree, however, that it was a case of "no matter what the cost".

We therefore believe that both our customers and stakeholders regard tackling sewer flooding a priority. There is support for an increase in investment for sewer flooding, but possibly only by a modest amount. We need to seek further views on by how much.

A risk based approach should be taken

Our current approach to managing sewer flooding is pre-dominantly reactive. We maintain a register of houses and offices that have suffered sewer flooding in the past. We then aim to take these properties off the register. The work is prioritised based on whether a house has flooded inside or whether only the outside has flooding, and on how often the flooding has happened and does not take into account the impact or consequence of the flooding incident.

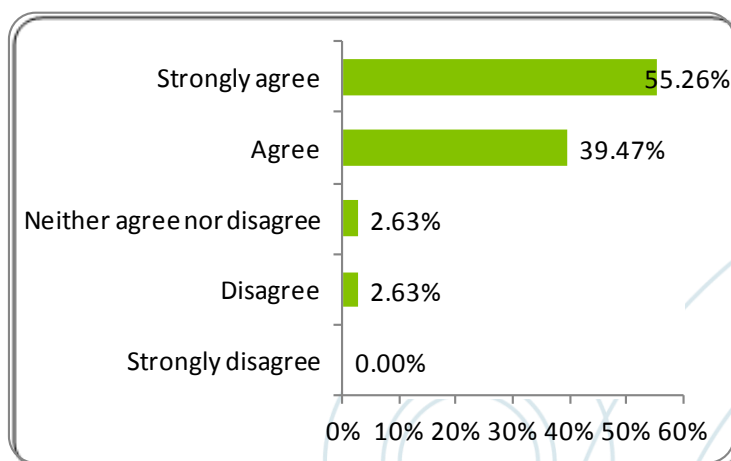
A risk-based approach would include moving away from our current historic risk register towards targeting properties most at risk (taking into account likelihood and consequence) and varying the level of protection with the risk. It would enable us to protect a larger number of customers from flooding by using a wide range of options. This could, at times involve the use of mitigation measures, which reduce the likelihood and/or consequence of flooding. Therefore properties would be protected based on the risk of flooding and not to a fixed design standard for the sewer system. This would also enable us to offer protection to customers affected by a fairly low of risk of flooding.

Attendees at our workshop on 19 June were supportive of taking a risk based approach to tackling sewer flooding. This support was further reflected in written responses to *Making the right choices*.

Waste water workshop, June 2012

To what extent do you agree with the following statement:

"STW should adopt a risk based approach to sewer flooding"



"In the short term we would advocate an approach that addresses those identified as being most at risk or alternatively can deliver quick wins. In the long to medium term we would recommend that STW explore opportunities for collaborative working."

Stakeholder MTRC written response

"We support your proactive approach to take action based on risk and likely consequence to your customer"

EA MTRC written response

But, some stakeholders were concerned to ensure that taking a risk based approach did not come at the cost of not addressing lower frequency/lower consequence properties.

"Whilst it is recognised we cannot prevent all sewer flooding it is essential that properties that flood on lower return periods aren't ignored."

Stakeholder MTRC written response

Attendees at the 25 September 2012 workshop also expressed a concern that a risk based approach could mean that smaller scale historic problems were not solved. Stakeholders at all events urged us to ensure that it has a sufficiently robust methodology and information to identify those most at risk.

"The proposed approach to sewer flooding is potentially less transparent than the DG5 approach. There still appears to be some level of 'number juggling' similar to the current DG5 approach"

Attendee at 25 September 2012 workshop

We believe that there is broad support for us taking a risk based approach to addressing sewer flooding in the future. We recognise the need, however, to give our stakeholders confidence in our approach, and work with them as it develops.

There needs to be proactive maintenance

A number of our stakeholders believe adequate maintenance of our assets is crucial.

"We believe that achieving fewer pollution and sewer flooding incidents related to sewerage infrastructure will be dependent on the adequate operational maintenance activities as well as timely asset renewal and rehabilitation."

EA MTRC written response

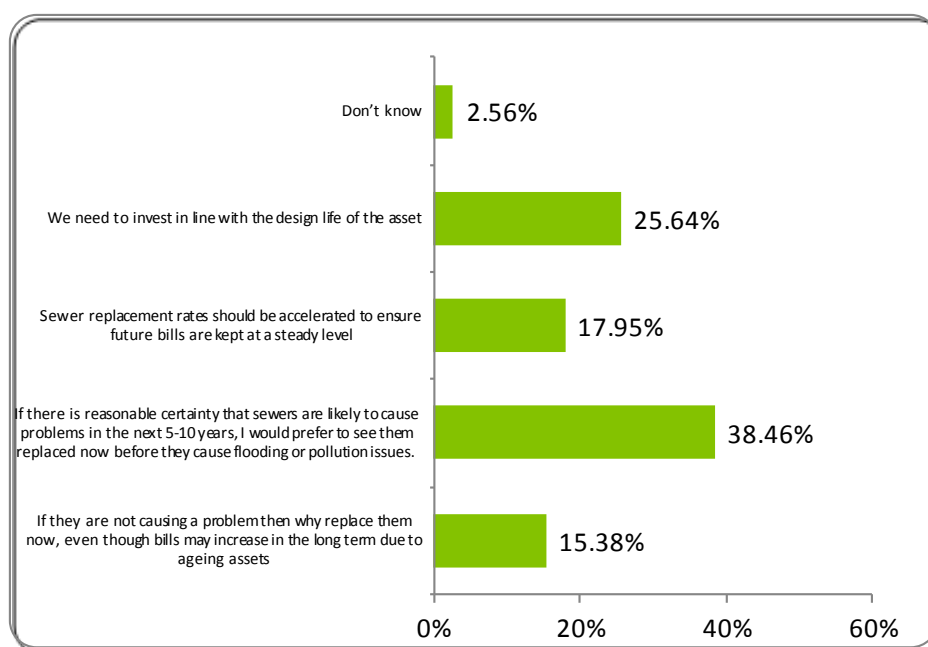
"The pace of asset renewal is a crucial aspect in relation to future sewer performance and therefore flooding. This should be addressed substantially"

Attendee at 25 September 2012 workshop

Most attendees at the 19 June workshop supported taking a proactive approach to maintenance (to varying degrees) in order to spread the cost over future bills (as opposed to 'fixing on failure').

Waste water workshop, June 2012

On the basis that over 70% of our sewers are older than 50 years, which of the following best represents your views



Some respondents also asked us to look further into the future and take an approach to maintenance that would help us to tackle future issues.

“Separation of systems should be carried out as part of any structural repair.... This is particularly important now with the impacts of climate change and environmental benefits promoting separation”.

EA MTRC written response

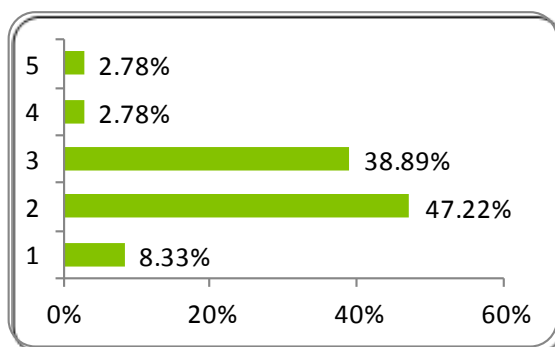
STW should invest, but customers should also play their part

Stakeholders at our workshops advocated STW investing further to prevent sewer flooding. They demonstrated a preference for this approach, over relying on educating our customers to use sewers more responsibly. They recognised however, that future investment could be negated if customers were better educated to prevent blockages, and that this should have a role in STW's approach.

Waste water workshop, June 2012

What do you think is the right balance between Severn Trent investing in its assets and all stakeholders making changes to control issues at source?

1 = STW led, 4 = behavioural change, 5= don't know.



"We would support an expanded programme of public education to help reduce blockages in the sewer system, and to discourage impermeable surfacing of driveways and garden areas."

Stakeholder MTRC written response

There appears to already be a high level of awareness from household customers about what they should not flush down the toilet or sink. CCWater's 2011 tracker research found that only 2% of customers in England and Wales think it is acceptable to put fats, oils and greases down the toilet. Awareness, however, does not always translate into behavioural change.

Greased lightening trial, Birmingham, 2009

Where we have previously trialled ways of encouraging our customers to reduce the fats, oils and greases they put down drains, we have seen positive results. In 2009 we ran Grease Lightening a partnership with the charity Community Service Volunteers Environment (CSV) to reduce sewer flooding caused by fats, oils and grease in a high incident area of Birmingham.

The pilot showed significantly positive results. By November 2009 (6 months into the project) there were 601 active community members from whom 1,719 litres of oil had been collected and used as biodiesel, thereby diverting it from sewers or landfill. There was also a significant reduction in sewer flooding incidents in the area; 17 incidents between 1 April and 30 November 2009 compared to 54 in the same period in 2008.

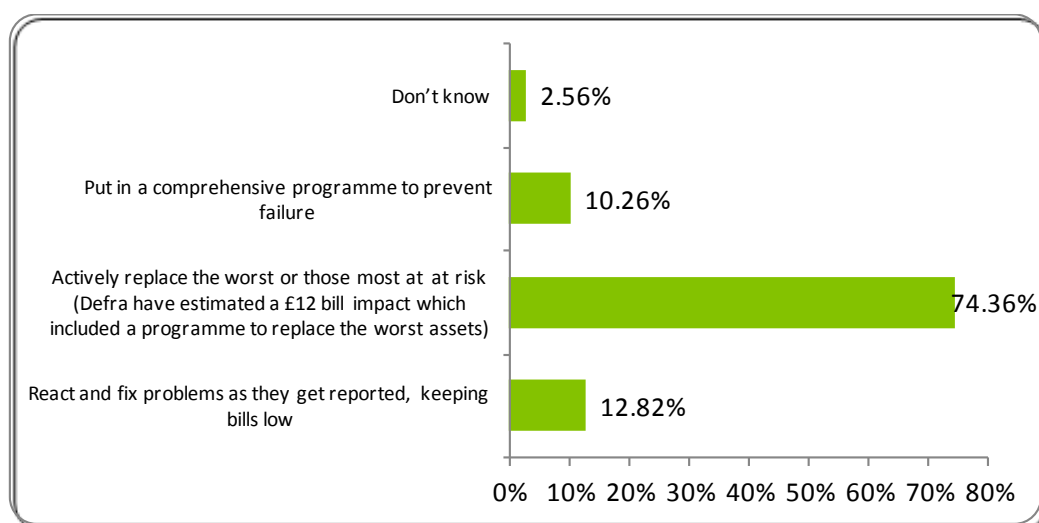
We believe, therefore that there is a positive role further education can play in our future plans. The focus of our approach should move our customers (both households and businesses) from being aware of the issues, to actually changing their behaviours.

Actively replace or repair those transferred sewers that are most at risk

We asked stakeholders how we should treat previously privately owned sewers that had transferred into our ownership (PDaS). There was a general view that we should actively repair and replace these assets as we would any other area of our asset base. There was limited support to carry out a comprehensive programme to bring all sewers up to the same standard at once.

Waste water workshop, June 2012

How should we bring our recently transferred sewers up to standard?



From the evidence we have from research, customers too appear to prefer prudent, risk based approach over a comprehensive replacement programme.

"In terms of spreading the costs, 66% of domestic customers and 57% of business customers prefer bill increases to happen sooner rather than later to avoid potentially steeper increases later. This suggests the second option of reacting to problems and completing the improvement work needed is the preferred option for customers."

CCWater MTRC written response

Our existing research suggests customer views on PDaS are polarised. When asked in our December 2011 tracker: *"From October 2011 the government has made Severn Trent responsible for parts of drains and sewers that were once privately owned or where ownership was unclear. How acceptable is the £10 bill increase?"*. 36% felt this was unacceptable or completely unacceptable, 39% felt this was acceptable or completely acceptable, the remainder opted for "neither" or "don't know".

Work in partnership

There was a strong view from our stakeholders that we should work in partnership with local authorities, LLFA and developers more in future to help tackle flooding and the possible impacts of climate change. This theme of partnership working more generally was common through all the workshops we held.

“STW should seek opportunities to work closely with the development industry and supply chain to encourage the uptake of investment...and should look to the example of other water companies such as Anglian who have produced guidance on the use and implementation of SUDS.”

Stakeholder MTRC written response

“Where SuDs technologies are appropriate but responsibility of build and maintenance costs have been an obstacle in the past, we would support you in working with others (LPAs, LLFAs , developers, communities and ourselves) in resolving any obstacles”

EA MTRC written response

“The proposed approach to sewer flooding for AMP6 offers multiple benefits and funding streams. The move away from the DG5 register towards a proactive risk based approach will allow Risk Management Authorities under the Flood and Water Management Act (which includes Severn Trent) to work together to plan strategically for challenges and work together to manage flood risk at a catchment scale. In summary, the proposed sewer flooding approach fro AMP6 will provide a better service for the public.”

“The proposed approach could be more aspirational and bold. The approach could go further to promote more collaboration (e.g. joint strategies where Surface Water Management Plans show integrated flooding problems) and could promote the use of predictive tools to get more value out of capital schemes.”

“Opportunities to link surface water management and water resources should be pursued. For example, where surface water is stored, this should be harnessed to replenish water resources to reduce the risk of drought.”

Attendees at 25 September 2012 workshop

But some stakeholders also said there could be challenges that would need to be overcome.

“There is concern that Defra, CLG and Ofwat are not talking to one another on flooding issues. This may lead to a lack of ability to collaborate at grass roots level. The proposed approach to sewer flooding provides a potential future opportunity for all Risk Management Authorities to be working to one flood risk register, rather than a ‘silo’ approach. This would need to be endorsed by Defra, CLG, Ofwat.”

Attendee at 25 September 2012 workshop

“Population growth will impact on many of your sewers as they have finite capacity.....developers may propose non-mains drainage systems within sewered areas. We consider that a proliferation of non mains systems could lead to water quality deterioration.”

EA MTRC written response

Furthermore, whilst further cooperation and collaboration was encouraged it was noted that Government guidance (Defra/Environment Agency guidance on requesting information and co-operation (pursuant to the Flood and Water Management Act 2010)) was that cooperation should take place in a “reasonable way”. There was limited discussion about what would constitute “reasonable”.

In summary, what have we learned so far?

We have learned from the evidence we have gathered to date:

- Tackling sewer flooding remains a top priority for both our customers and stakeholders. They would like to see us tackle the most severe cases quickly. But it is not a case of “no matter what the cost”. We need to gather more evidence on this, and in turn, the pace at which improvements are made.
- There is wide ranging support for adopting a risk based approach. This will not, however, be without its difficulties. We must ensure we have sufficiently robust information to target properties, and that those properties which are considered lower risk are not neglected.
- We should be proactive in our approach to maintenance, but again, we must consider the cost implications.
- We should not focus on investment alone. We should continue to encourage more responsible sewer use by our customers.
- There is a strong desire for us to work in partnership more but we need to gain a better understanding of what further collaboration and joint working stakeholders would like to see, and how this can be achieved.

4. We will provide excellent customer service

Where are we starting from?

In our 2007 Strategic Direction Statement we undertook to:

- Reduce the need for our customers to contact us by providing an even better quality product with even fewer interruptions to supply.
- Make it easy for customers to contact us via multiple communication channels.
- Provide a speedy and efficient response to customers by dealing with issues at the first contact point.

So far, we have made a good start to the AMP5 regulatory period, having acted on our promises and realised the benefits of efficiency improvement programmes. Our customers can choose to call, write, email, or take care of the vast majority of their account management needs via web self-service. Automated payment systems mean that customers can quickly pay their bills via telephone without waiting to speak to us. The real-time incident map on our website provides customers with up to date information on any incidents in their local area.

We recognise, however, that there is still scope to improve our performance. In response to our 2011 performance on the qualitative components of Ofwat's Service Incentive Mechanism (SIM) we created our 'Customer Experience Programme'. This programme is dedicated to improving the experience of our customers who have cause to contact us and in particular, how we leave them feeling. Over the last year our SIM scores have improved, however there is still considerable work to be done. In the latest SIM wave we scored 4.32 out of 5, putting us 7th overall against all the other water and waste water companies in England and Wales.

Where have we taken information from?

The insights we have summarised are drawn from: our review of 20 years of customer research; our quarterly domestic customer tracker; research conducted on our customer experience programme in 2011 and a series of customer focus groups held in August and September 2012 to discuss customer service issues.

What have we learned?

Help customers to make an informed choice about their tariffs

Our Q3 2012 customer satisfaction tracker found that the majority of customers (55%) think that people should be charged based upon the amount they use. However, 58% of those surveyed did not have a water meter fitted.

We explored reasons and beliefs behind this. The main barrier to meter uptake is the fear of irreversible bill increases (41%). Those surveyed were told that in fact this is untrue and they were then asked if they would be likely to consider having a meter. More of these customers would

consider it, but there is still some reluctance. Residual cost concerns or inconvenience factors were often cited here.

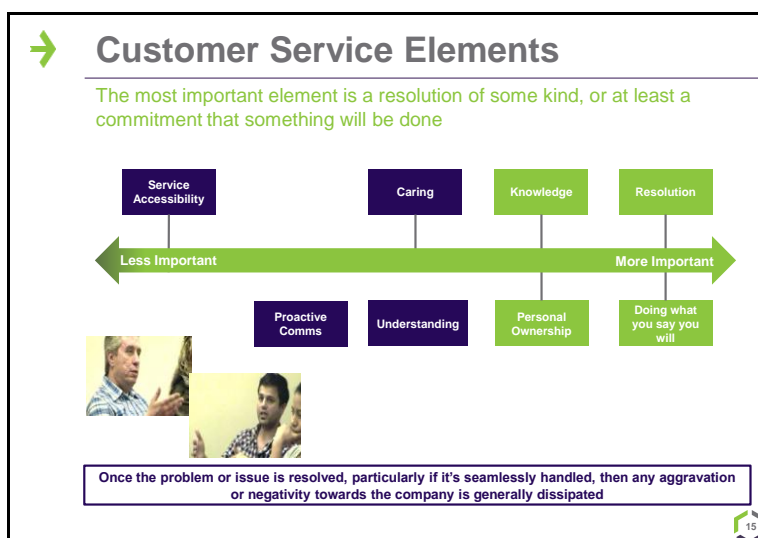
In our most recent customer tracker research we further investigated the barriers to metering. Our research revealed that there is uncertainty amongst those not metered about whether there is a fitting charge, that the majority of unmetered customers believe they will end up paying more and that there is a lack of knowledge about being able to revert to rateable value charging within a year.

This suggests more information may help customers make better choices about the right tariff for them. A common thread throughout all of the research and engagement was that stakeholders and customers welcomed the idea of increased education and communication about the companies activities and responsibilities.

Resolve problems quickly

Our customer focus groups carried out in August 2012 highlighted that resolution of issues, or at least a commitment that something will be done, is the most important element of customer service.

Customer focus group, August 2012



This is further supported by our catalogue of research over 20 years. A key theme from this research is that when customers contact us their satisfaction increases with the speed of the company's response and the lower they perceive their own effort to be in getting the issue resolved.

Our 2011 research into customer satisfaction considered in more detail customer expectations of problem resolution, compared with their actual experience. The main reasons for claiming STW had not met expectations were: taking too long to resolve queries; unresolved queries; and lack of communication.

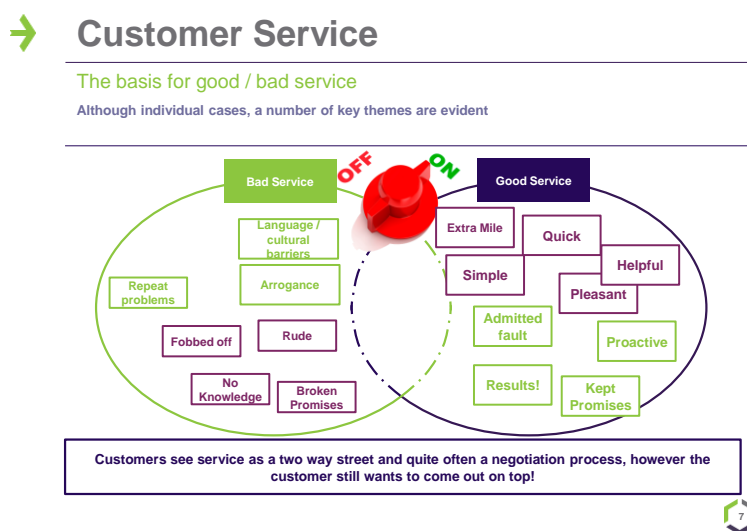
Keep our customers informed

Whilst fast resolution of issues is crucial, resolving issues quickly alone is not enough to drive satisfaction. Customer experience research carried out in 2011 showed that the 'softer' aspects of

service delivery are also critically important. They included: keep informed; provide time scales; and take responsibility (2011 STW Customer experience research).

These views were further supported by customer focus groups held in August 2012. Many expressed a view that even if STW could not immediately resolve an issue, being kept informed about what we are doing about it would go a long way to show that we cared about the customer and are taking responsibility for resolving their issue.

Customer service focus group (August 2012)



For customers who do not have cause to contact us (some 84% in 2012), their expectations for communication differ. Customers often have low top of mind awareness about their service, what they are paying for and how it compares to other services. For example, our Q4 2011 tracker revealed that 88% of our customers are not aware that we offer the lowest average combined household bill in England and Wales. Our customers will tend to only think about us, or want to think about us if: they need to contact us; they see us about in the community; or hear about us in the media.

One of our key ways of us proactively communicating with all our customers is through our bills. Our customer satisfaction tracker (Q2 2012) revealed that: 66% of our customers say it is clear how their bill was calculated and 81% of our customers know how much has to be paid and by when. However, a third of our customers are unsure how their bill was calculated.

Enable customers to choose how they contact us

Our customers have different preferences for how they contact us, and under what circumstances. For example, our stakeholder research shows that 62% prefer communicating with us electronically and 20% prefer to write us a letter. However, Ofwat industry research shows that customers still prefer to communicate by telephone, with customers seeking an excellent telephone contact service.

At our August 2012 focus groups some preferred the use of e-mail, particularly where an issue might be complicated, but others, for example in the case of a pressing operational issue, preferred telephone. One participant summarises that: *“Not everybody likes to do the same thing. Some like face-to-face, some like phone, some prefer e-mail. So, yes, it is important for Severn Trent to be quite versatile.”*

Many of the focus group participants were supportive of the use of on-line and social media, though there was a view that these should not be implemented at extra cost: *“If my bill goes up because they make an app that no-one ever uses I’ll be really irritated”*.

In summary, what have we learned so far?

We have learned from the evidence we have gathered to date:

- Our customers would like more and clearer information on tariffs to help inform their decision making, particularly relating to metering.
- Our customers would like us to keep bills simple and understand how they have been calculated.
- Our customers want us to resolve issues quickly.
- Where we can not resolve issues quickly, our customers value being kept informed.
- Not all customers have the same preferences for contacting us. They would like us to be flexible and offer a range of contact options.

5. We will have the lowest possible charges

Where are we starting from?

Severn Trent customers benefit from the lowest average combined water and sewerage bills in England and Wales. We recognise that household incomes have been substantially reduced in recent years and that our region has a high level of poverty. Therefore minimising bills is one way of helping our customers in water poverty and we constantly drive efficiency to keep bills as low as possible. In our current business planning period (2010-15) our efficiency improvements will save £14 from the average household bill.

Where have we taken information from?

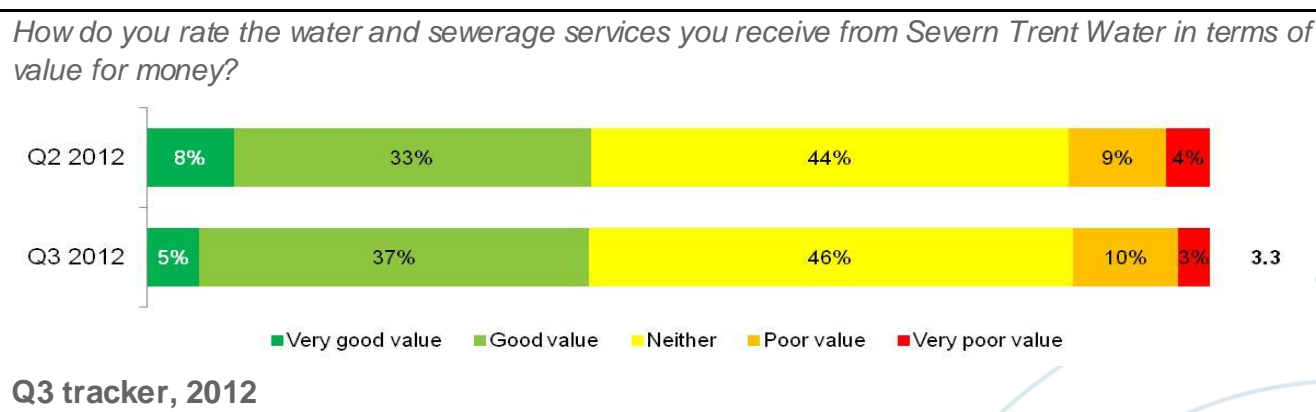
We have not specifically asked our customers about efficiency, but we know that they expect value for money and for their bills to be as low as possible. They do not expect to pay for wastage. We have taken evidence substantially from our quarterly household tracker.

What have we learned?

The following section summarises the key insights we have drawn from this information.

Our customers broadly think we are good value for money

Based on our most recent survey (Q3, 2012), 42% of our customers think we are good or very good value for money. Historical comparisons of value for money are problematic but our research suggests that perceptions of value for money have not changed appreciably over time.



The remainder of our customers think we are poor value, very poor value or don't know. One of the reasons for this is likely to be that customers are unlikely to know what other companies charge and therefore have no means of comparison.

Our Q1 2012 tracker showed that significantly more customers with water meters rate us as value for money compared to those who don't. This could be because they are more conscious of their water use.

Customers are unaware we offer the lowest average combined household bills

We believe our customers find it hard to understand as the concept of the average household bill rarely relates to them. 11% of customers (Q2) know we have the lowest average charges (13% in Q1 2012).

Severn Trent has one of the larger 'VfM gaps'

Research carried out by CCWater in 2012¹ considered why there was often a gap between customer satisfaction levels and their level of satisfaction with value for money. It found that when it comes to value for money (VfM), although a majority of customers are either 'very or fairly satisfied' with this, there is a gap of some 20 percentage points between overall satisfaction with the service and satisfaction with the VfM of water and sewerage services. Severn Trent Water, despite having one of the lowest bills in the country also has a larger than average 'VfM gap' (24% and 22%).

Perception of value for money can fluctuate from year to year

CCWater carries out an annual tracking survey, including satisfaction with value for money. As the table below shows, there are variations from year to year which probably do not reflect real change in service or bills. What is consistent from year to year is:

- Very low satisfaction with value for money in the South West area, reflecting high bills.
- High satisfaction in the Yorkshire area, possibly reflecting the efforts made to inform customers about services and bills, and possibly a greater sense of regional identity.

	2008	2009	2010	2011
Water				
Midlands	64% (9 th out of 10)	68% (8 th out of 10)	76% (2 nd out of 10)	70% (7 th out of 10)
National	70%	69%	72%	72%
Sewerage				
Midlands		70% (8 th out of 10)	74% (3 rd out of 10)	69% (9 th out of 10)
National		71%	73%	72%

¹ Value for Money: A report on Drivers of Satisfaction in the Water and Sewerage Industry, Report by Creative Research for CCWater, 2013

Research for the 2009 price review showed increased perception of value for money when more information is given to customers

National research carried out in 2008 showed Severn Trent customers rated their current water and sewerage service slightly lower in terms of value for money than the national average. However, when presented with information on current bills and services, the perception of value for money by Severn Trent customers increased, as shown below:

% of customers rating the service as fairly good or good value for money

	Initial view	After seeing current service and bill levels
Severn Trent	62%	67%
National	64%	61%

This demonstrates that if customers are given more information then the perception of Severn Trent value for money can increase.

Drivers of perception of value for money

The CCWater report referred to above identified that availability of choice and control over bills were significant factors in determining perception of value for money. This may explain why metered customers give a higher rating for value of money, and as metering increases this perception may improve.

The impact of the state of the economy

The state of the economy may affect perceptions of value for money. Any increases in bills may be less acceptable than in the past, and cause a deterioration in value for money assessments. Incomes have been falling in real terms, with wage increases not matching inflation, and welfare reforms will have an adverse impact on some customers. Our willingness to pay survey showed significantly lower willingness to pay higher bills than at PR09. A number of stakeholders at our Customer Stakeholder Workshop in September 2012 commented that welfare reforms would mean that paying water bills would fall down the list of priorities.

In summary

- Our customers broadly feel we offer good value for money, but a lack of understanding of what they pay for and the absence of comparators mean it is difficult for them to gauge.
- Providing further information improves perceptions of value for money.
- The state of the economy means that increases in water bills could adversely affect customers' views on value for money.

6. We will help you if you struggle

Where are we starting from?

We began AMP 5 with a strategy focussing on speaking to our customers, finding out their particular circumstances and tailoring our debt management approach. Through this approach we aimed to identify our most vulnerable customers and offer them a range of options including: Water Direct; Water Sure; Together scheme; single occupier assessment charge; support from the Severn Trent Trust Fund; and working with the Citizens Advice Bureau to provide debt counselling. For those customers we identify as being able to pay, but choose not to, we would take a harder approach including court action.

In 2012 we have also developed a new initiative with the Coventry Citizens Advice Bureau (CAB). The 'Big difference fund' provides funding for the CAB to target STW customers who struggle to pay and offer support and advice.

In 2008/09, 9% of customers spent more than 5% of their annual income on water charges, but only 2% did not pay their bills.

Where have we taken information from?

We have taken stakeholder views from a range of sources, but principally from our workshop on 6 September 2012 and written responses to *Making the right choices*. Around 31 individuals and 29 separate organisations attended this workshop.

The views of customers have been taken from a range of sources including: our historic catalogue of research (spanning 20 years); the views of CCWater and relevant research carried out by CCWater and Ofwat.

What have we learned?

The following summarise the key insights we have drawn from this information.

Welfare changes will bring further challenges

Our 6 September 2012 workshop revealed that our stakeholders are concerned about the impact of welfare reform on the ability of our customers to pay. This was the very first issue they raised at the beginning of the workshop.

A housing association representative stated it was important to understand what the effect of welfare reform will have on local economies. S/he added that STW will need to think about the problems their business customers will be facing as there will be less money in the local economy

A council representative explained that his/her local authority is already looking at the potential impact of welfare reform but local residents are still 'largely oblivious' to the scale of changes that are set to take place. S/he stated that 'we're getting customers to help tackle debt these by getting them to pay these off soon as their benefits come in'

Helping customers who struggle to pay workshop, September 2012

Stakeholders suggested that the nature of the reform could change not only how many customers may struggle, but also who may struggle.

A council representative felt that the table had not discussed 'vulnerability' enough; s/he referred to a report entitled 'In the Eye of the Storm' which was funded by Action for Children and compiled by the Institute of Fiscal Studies, which helps clarify those that are most at risk. S/he stated 'the most recent research I've read has suggested that pensioners have done well for themselves and will be okay following welfare reform, whereas families and children are set to suffer most from introduction of universal credit. STW need to identify people most in need, however this doesn't necessarily require a heavy use of resources'

A housing association representative said pensioners are being protected under the current round of welfare reforms.

Helping customers who struggle to pay workshop, September 2012

Stakeholders also suggested that, at times of austerity, payment of water bills could become a lower priority for customers.

A housing association representative stated that, due to the Welfare Reform Act, water debt gets lost in the other debts STW customers have. Again, there is no fear of being 'cut off' that customers have with other utilities.

A council representative added that it is important to be aware of other national issues such as the change in administration of the Social Fund from the Department of Work and Pensions. As it is dealing with crisis loans, water will not be included in that as the water supply will never be cut off. The stakeholder questioned how water can be embedded in debt queries.

Helping customers who struggle to pay workshop report, September 2012

We therefore believe that this could lead to an increase in the number and nature of our customers who struggle.

The challenge is to get customers onto the right tariff

Our willingness to pay focus groups found that customers are confused and concerned about what they are being charged. Primarily this relates to metering; whether they would be better off metered and the perception amongst many that this would be costly and irreversible and potentially detrimental to future house resale.

Stakeholders at our workshop expressed a view that it is important that customers are on the right tariff. A number commented that customers may be reluctant or fear switching to a meter as they are concerned it may be more expensive, and are unaware that they can switch back.

A housing association representative stated that STW should encourage tenants to go on to a meter. It was added that there is a fear among people about meters, particularly older people. The stakeholder suggested that there should be better education about meters and water usage to reduce fear. The stakeholder wondered if there is some way to highlight how useful a meter is for a household

An advisory service representative stated that there is a particular fear of leaks with water meters, causing an increase in charges

Helping customers who struggle to pay workshop, September 2012

A number of stakeholders commented that it was often difficult to ensure that customers were aware of the different tariffs, or range of support on offer. Stakeholders themselves were supportive of the range of support on offer, but were often not aware of it.

All agreed that STW's approach is a positive one and that the challenge is to get people to take advantage of the schemes available

An advisory service representative... was of the view that 'STW have a lot of options to allow them to do good but their methods of communication are a problem'. S/he said customers need to given/offered more options on how to pay their bills before they are hundreds and thousands of pounds in debt

An advisory service representative stated that current schemes that are available to STW customers are excellent but the customers are not aware of them. The stakeholder added that his / her organisation is not widely known about, and STW needs to think about how those customers are engaged

An advisory service representative added that 'one thing we've found is that people don't read their bills because they don't want to face it unless it gets really desperate'

An advisory service representative suggested that STW should 'send out information with bills'. County Courts send out information on advice agencies in his / her area and STW should be doing the same

A housing association representative deliberated over whether written information is the best way to communicate with his / her residents because they 'have an average reading age of 12'

Helping customers who struggle to pay workshop, September 2012

There is limited support from customers to help those on low incomes

Defra's guidance for the introduction of social tariffs to support those on low incomes, states that there must be broad support from our customer base.

The Government expects an undertaker's proposals for a company social tariff to be acceptable to their customer base. This includes broad acceptance from households that will benefit from the social tariff and those household customers that will be asked to contribute to the cost.

Defra, Company guidance on social tariffs, June 2012

Research carried out by CCWater (Research on cross-subsidies and social tariffs, June 2010) found that the majority of customers support the principle of having lower water bills for people on very low incomes.

In 2011 we surveyed our own customer base about their views on helping customers on low incomes with their water bills. 59% of customers supported lower water bills for customers on low incomes in principle. Of these customers, the average amount that they would be willing to pay extra on their water bill was around £4 (STW customer satisfaction survey, Q1 2012). At our current average bill at around £325, this would equate to £10 million of available support.

In our Q3 2012 customer satisfaction survey we asked more detailed questions about social tariffs. When asked about the principle of water companies being allowed to reduce water bills for some households with low incomes, on benefits and/or unusually high water usage we received mixed views: 39% agreed, 29% disagreed. However, when it was explained that the cost would be met by other bill payers, 24% agreed whilst 50% disagreed. This suggests there is some but nonetheless limited support for the introduction of a social tariff.

In 2013 we will be conducting further research into this area.

We need to target our help to customers that most need it

There was no consensus from stakeholders at our workshop about which customer groups would most need support. Some suggested specific groups but many believed that rather than allocate support on customer type (for example, pensioner, low income) they believe support should be allocated on the basis of need.

A community association representative commented that STW needs to identify people in need rather than specific groups

An advisory service representative supported this view. S/he stated that need can be identified by organisations early on to prevent people from getting to that point of desperation

An advisory service representative stated 'there's not one group more needy than another'

A housing association representative commented that the main group should be 'large families'

An advisory service representative disagreed and stated it should be 'single without children not necessarily pensioners'

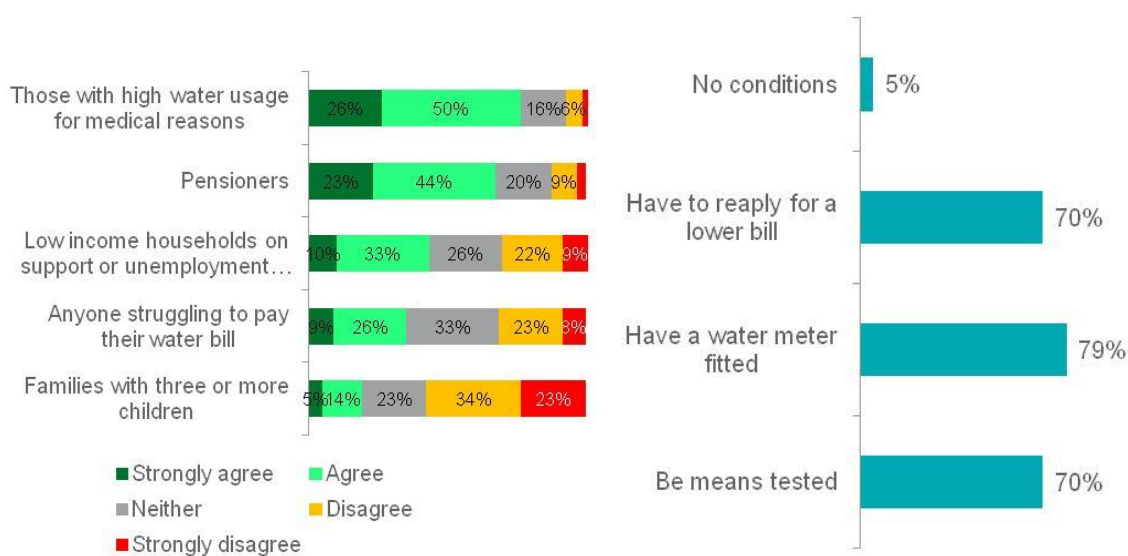
An advisory service representative was of the view the 'breakdown of groups needs to offer more detail'

A housing association representative said single males ages 25-40 are the most vulnerable as they 'don't know what to do' and there is 'no social help available'

Helping customers who struggle to pay workshop, September 2012

When we asked customers in our Q4 2012 customer satisfaction survey, there was most support for lower water bills towards those with medical needs and pensioners. Most believe those helped should follow certain conditions, such as metering or means testing.

STW Customer satisfaction survey Q4 2012



At our stakeholder workshop, we also posed the question about whether it was better to help a few people a lot, or a lot of people a little. Again, mixed views were expressed. The general consensus was that financial support should be targeted to the few that most need it, but advice should be available to all.

An advisory service representative was of the opinion that a 'few people should be helped a lot'

An advisory service representative was of the view that helping a lot of people 'a little will not be enough to help or make a difference'

An advisory service representative was of the opinion each individual's personal situation needs to be looked at when deciding how much help they receive

An advisory service representative commented that STW needed to be realistic and if it was to 'help too many people and you end up helping nobody'

A council representative stated that STW should be helping a few, but with a lot of advice. STW should also help those few with budgeting advice

An advisory service representative felt that STW should help all customers, but help should not necessarily mean financial help. STW could provide efficiency advice or budgeting advice, for example, and supply water-saving gadgets

A housing association representative agreed with this point, and added that there should be financial support for the few but advice for all.

Helping customers who struggle to pay workshop, September 2012

We contend that those on low incomes can be divided into two groups: those whose circumstances can be considered temporary and those whose circumstances can be considered if not permanent, then ongoing.... in our view, the latter 'grouping' requires automatic financial support whereas the former, however hard life is on a low income, do not.

Stakeholder MTRC written response

Social tariffs will not solve the issue – a range of options are needed

Stakeholders provided us with mixed views about social tariffs. Whilst some supported them, on balance most felt that a social tariffs would not be a panacea. A number agreed social tariffs should be a last resort, and some felt the expenditure could be better targeted through other approaches.

A housing association representative viewed the social tariff criteria as good as it covers a lot of areas but it 'may not work in practice'

The table agreed that it was the right decision that a social tariff should be a last resort and all agencies should be working closely with these customers before the need of a social tariff

A council representative commented S/he believes it would be better to encourage awareness among customers rather than concentrate on a social tariff

An advisory service representative commented that unless STW proactively identify people by finding out about their individual circumstances, it will not be able to identify whether people are eligible for social tariffs

There was a certain amount of support for a social tariff as one of a range of options that could help customers but some commented that this should be a last resort once other alternatives have been explored. Once again, it was noted that the real challenge was on identifying which customers should be eligible

An advisory service representative commented that social tariffs need to be used in addition to something else. S/he viewed the social as being 'good as stops the cycle'. S/he was of the opinion that the 'system is erroneous and needs to be looked at'

An advisory service representative pointed out a time comes when an advisory service has to say goodbye to a client and stop helping them after a certain amount of time. S/he was 'unsure of what is next but the social tariff is reassuring'

The table agreed that the consensus around the table was that once all other options are exhausted then a social tariff is suitable

A council representative suggested that STW would be 'better off giving funding to advice agencies in promoting them properly'

The general consensus on the table was that 'for the few or many' may be the wrong question. Tackling affordability issues is more about helping people and targeting them in a very different way

Helping customers who struggle to pay workshop, September 2012

We should work in partnership with relevant agencies/organisations

Virtually all stakeholders at our workshop believed there needs to be much greater partnership working between STW and their counterparts in order to: help target the right support to those who most need it; help proactively identify those who may be at risk of falling into debt and educate about the payment of water bills.

A community association representative stated that for him/her it was not merely a case of 'can't or won't'. S/he stated 'I appreciate that water suppliers are in a very tricky position because they can't just cut someone off, this is probably why water ends up at the bottom of their priority list. STW need to shift perceptions and teach people to view water as important as other utility bills. Everything's gone up apart from wages, with the best will in the world, even someone who wants to pay might struggle'. S/he explained that STW need to take a more 'holistic approach' and it was important to explore more diverse outlets to reach people in arenas where they are more likely to share information. S/he felt strongly that STW should make the most of the available community outlets

A community association representative was of the view that there was a need to 'take a step back' and firstly, consider how STW is actually perceived by people that are having trouble paying their bills. S/he explained that even doing something seemingly simple such as making a phone call, is a barrier for some. S/he explained that his/her association had found that 'if you want to engage with people you need to actually sit down with someone and provide them with an opportunity to do so'.

An advisory service representative felt that face to face verbal intervention is the best way to get people that were struggling to pay to face their water bill. S/he admitted that in practical terms this might be tricky to implement but in an ideal world this would be the most effective way to tackle the issue. S/he stated 'we find that people are very defensive if they think that STW is trying to get something out of them. However, if your approach is focused on helping people, they will be more willing to listen and learn'

An advisory service representative was of the view that the STW's greatest challenge was to trigger customers into taking advice and raising awareness of their schemes, rather than chasing up debts and s/he felt that STW need to be seen to want to help struggling customers

An advisory service representative stated that 'STW should engage with debt organisations, so we know about it, people aren't going to open their doors to the Citizens Advice Bureau – they need a buffer between STW and local authorities

An advisory service representative pointed out that STW has a good array of schemes that are well segmented, however their challenge was to encourage early access to the schemes for those having difficulties with payment

Helping customers who struggle to pay workshop, September 2012

In summary, what have we learned so far?

We have learned from the evidence we have gathered to date:

- Welfare reform risks changing the number, and type of customer who may struggle to pay in the future.
- Stakeholders support the range of support we already offer. They believe the most important thing is to improve and expand the information we make available to customers and other agencies, thus more effectively educating those who most need it, and the agencies who can help them, about the support available.
- There are mixed views about social tariffs. Some stakeholders support social tariffs, others believed focussing more on other approaches would be more effective. There is limited support from our customers to pay more to help support those who struggle to pay. 50% of our customers surveyed disagreed with this.
- Many stakeholders favoured helping a few customers a lot rather than many a little. There was no consensus of who to help and many believe eligibility should be focussed on need, rather than targeting specific customer groups.
- Given the complex nature of helping those who may struggle – identifying the who and the how – most stakeholders believed STW should focus its efforts on working in partnership with organisations who are in direct contact with customers who may struggle, or are likely to.

7. We will protect our water environment

Where are we starting from?

In our 2010-15 business plan, we recognised our responsibility to manage our impact on the local environment through our abstraction of water and discharge of waste water. We explained that abstraction of water risks affecting river flows and that the discharge of waste water risks affecting river water quality.

We recognised environmental pressures on abstraction and the need to meet the requirements of the Water Framework Directive (WFD). We set out our longer term strategy to maximise the sustainable use of our existing resources by using new technologies and a better integrated network rather than develop new water resources schemes.

We noted our support for the WFD and the provision of an exemption on the grounds of disproportionate costs. Over the current investment period, we have carried out a pilot project with the Environment Agency ('Balancing carbon and ecology') to further explore ways to meet the requirements of the WFD with a lower carbon impact.

We explained that as a significant land holder, we had a responsibility to improve the condition of Sites of Special Scientific Interest (SSSIs) on our land. There is a well defined statutory framework for SSSIs which is set out in the Wildlife and Countryside Act 1981, as amended by the Countryside and Rights of Way Act 2000 (CRoW). CRoW places a duty on public bodies (which includes water companies): to ensure that in exercising their functions we: *"take reasonable steps, consistent with the proper exercise of those functions, to further conservation and enhancement of the special features on a SSSI"*.

Where have we taken information from?

We have taken stakeholder views from our waste water services workshop on 19 June 2012, relevant government guidance and regulatory advice. Our customer evidence comes from a range of sources including willingness to pay research and our quarterly tracker.

What have we learned?

The following section summarises the key insights we have drawn from this information.

Take action to reduce unsustainable abstractions

Guidance from both the Government and the Environment Agency requires water companies to ensure that rivers and water bodies are not damaged through over abstraction.

“Many rivers and water bodies in the UK are being damaged when too much water is taken from them...We will develop an action programme for addressing unsustainable abstraction up to 2027 and beyond in the second cycle of RBMPs”

Defra White Paper, Water for life, December 2011

“The environmental impact of water company abstractions should be reduced where these impact upon sites within the scope of the EA’s RSA programme and where there is a need to reduce abstractions to meet the environmental objectives of the WFD.”

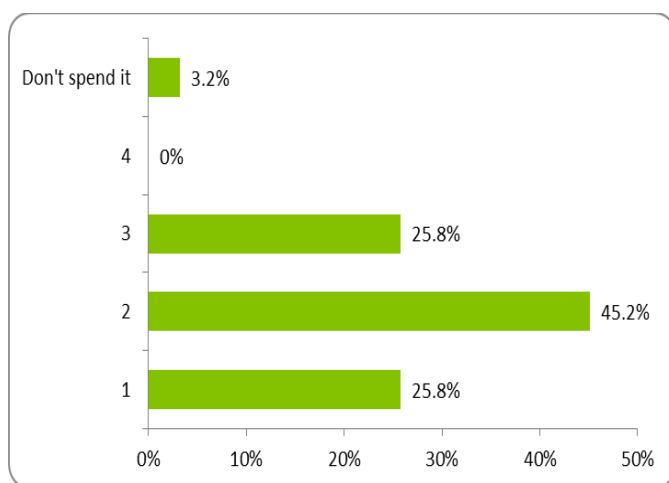
Environment Agency, written response to MTRC, July 2012

It is expected, however, that meeting required abstraction reductions could come at a cost for our customers. At our water workshop on 12 June, we asked our stakeholders how we should balance meeting environmental requirements with the needs of our customers.

Water workshop, 12 June 2012

“If we had £1 on bills available how should we spend it....” - Where on the following scale would you be (from 1 – 5)?

1 = All on environmental improvements; 4 = All on improvements to customers’ level of water service; 5 = Don’t spend it



Stakeholders recognised statutory requirements to take action. Many of those who commented believed it was appropriate to do so now, though some felt it too technical a question to comment on.

A conservation group representative made the point that environmental degradation is important, and water extraction under the Water Framework Directive should be observed, and there should be a cost / benefit analysis per abstraction. S/he said there was an importance in 'connecting the public with their water supply', adding 'we need to connect people to where their water comes from'

A business group representative commented STW needs to adopt a 'long term solution'

A conservation group representative agreed with this statement. S/he felt a long term strategic approach should be looked at. S/he stated STW should look at everything on a 'case by case basis and look at the fastest route available'

A business representative commented that STW should deal with the 'quick wins first' as it will put STW into a better position in the long-term

An environmental group representative said that there was a need to start planning now to meet the 2021 deadline around abstraction

A council officer worried that the question was too technical to answer well

A council officer said that if the cost isn't greatly increased then there isn't an incentive to get it done now

A business group representative claimed that from an environmental point of view it is the right thing to do to get it done quickly.

Water workshop, 12 June 2012

In general, attendees believed we should be taking action to ensure our abstractions are sustainable in the longer term. *However, there was no firm view expressed about pace and the potential cost to customers had not been quantified at the workshop.*

Our willingness to pay survey revealed that of all the water availability and environment attributes low flow is the highest valued attribute, and the value was significantly higher than in the 2007 survey. However, insight from our WTP focus groups (April 2012) suggests that river quality and low flows is not something that our customers have either considered relates to Severn Trent Water or indeed ever really thought about.

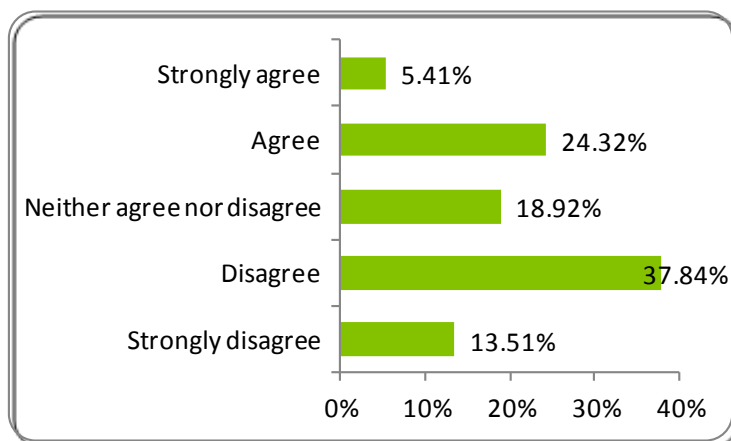
Overall, this suggests that there would be support for reducing our most unsustainable abstractions and that STW should take a long term view. We need to further understand, however, how much action should be taken and how quickly.

Take action to meet the requirements of the Water Framework Directive

We believe our stakeholders support us taking action to meet the requirements of the Water Framework Directive. Stakeholders at our 19 June workshop did not believe we were yet doing enough towards the WFD.

Waste water workshop, 19 June 2012

To what extent do you agree with the following statement? *"We are currently investing enough money to improve river water quality"*



Research suggests our customers support us taking some more action to protect the environment. The WTP value for bringing rivers up to good status (£8.32 per customer to improve 14% of rivers) was the highest of any service attribute. However, the key issue will be how this compares with the cost of improvements.

CCWater noted in its written response to *Making the right choices* that based on its research, improving river water quality is not a top priority when compared to other water and sewerage services, and suggested that Severn Trent needed to do more to educate customers about the benefits of improving rivers.

Our quarterly customer tracker shows customers give a high priority to river improvements – higher than improvements in any other aspect of service. This does not necessarily conflict with the CCWater evidence. Our research is in line with the view found in the CCWater research that safe, reliable water supplies are customers' highest priority. But customers are generally satisfied with current service in this area, so may not see improvement as a high priority.

STW customer satisfaction tracker Q2 2012

63% of customers say that the amount spent by us on river water quality is about right, 31% say we should spend more and 6% say we should spend less. The proportion of customers saying we should spend more on this issue was higher than for any other aspect of service.

What customers mean by this is varied. Of those who said we should spend more (31%), this is what they meant:

Comment	%
Cleaner rivers / improve water quality / waterways	17.7%
Prevent contamination from industries / reduce pollutants / chemicals	17.3%
Better environment for wildlife / plants that live in and around the water / plant more oxygenating plants	16.6%
Tighter control on untreated sewage entering rivers / ensure sewage properly treated	12.5%
Make it better for fish / fishing / restock with fish / too many dead fish	8.3%
Remove rubbish from rivers and banks / maintain on regular basis	7.2%
Control spillages / untreated leaks into rivers (unspecified mentions)	6.2%
Monitor continually / scientific tests	6.2%
Improve quality of drinking water / too hard / make it softer / install filters	5.5%
Improve water retention / stop leaks	5.5%
Clearer water / water looks too dirty	4.5%
Prosecute companies / heavy fines / stop people dumping	4.1%
Dredge more / help to reduce flooding	3.1%

As the table above shows, some of the improvements mentioned are not Severn Trent Water's responsibility. Whilst customers support further investment, they appear to have a lack of understanding about what benefits this would deliver. We need to do more to clarify what improvements they would/would not support.

The pace and extent of improvements

The pace with which we should make improvements, and the extent to which the requirements of the WFD could be met by 2027, are key issues.

This issue has been discussed by the House of Lords European Union Select Committee. In its evidence, Defra stated:

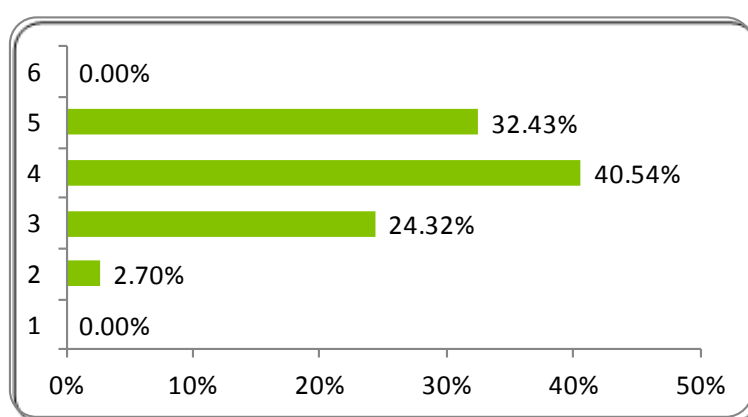
"To comply with the provisions to 100% would require some really quite impossible measures. Where we think we could see the benefits outweighing the costs, we would probably get to something like 75% good status by 2027".

At our stakeholder workshop on 19 June, attendees tended towards supporting us doing as much as feasibly possible, rather than nothing.

Waste water workshop, 19 June 2012

How much progress should Severn Trent make towards its share of achieving Good status between 2015 and 2020? Where on the following scale would you be?

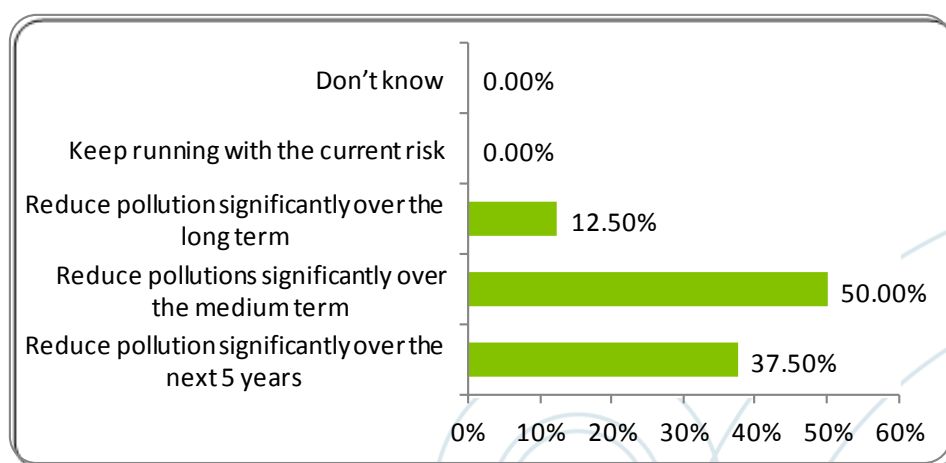
Nb. 1 = No progress and 5 = resolve as much as is technically feasible. 6 = Don't know



And where pollution is caused by failures in our own assets, stakeholders expressed a preference for us to do more, and quickly.

Waste water workshop, 19 June 2012

How quickly should we aim to address the risk of pollutions?

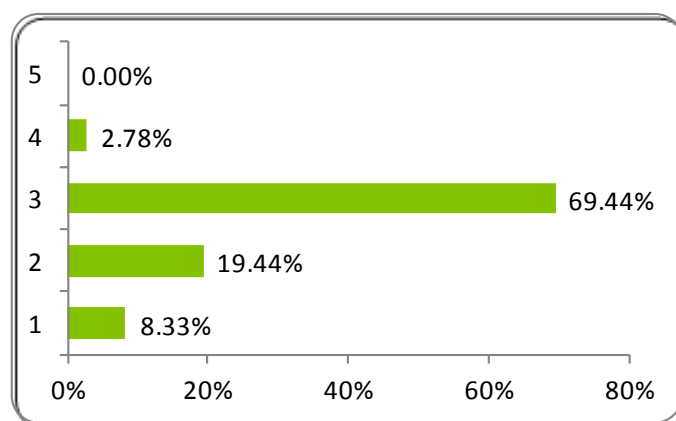


The issue of pace, however, is closely associated with cost. And whilst stakeholders supported action being taken quickly, there was less support for a significant increase in bills.

Waste water workshop, 19 June 2012

The 2010-15 river quality improvement programme added £9 to bills. What level of further addition to bills do you think is appropriate?

- 1 = Little or no change in river quality – less than a further £9 added to the bill
2 = Similar improvement in river quality – around £9 added to bills
3 = Significant improvement in river quality – around £18 added to bills
4 = The impact on the bill doesn't matter as long as we meet the standards
5 = Don't know



Discussion at the workshop further illustrates the range of views.

A council officer said future bills will need to 'increase significantly.' S/he would like to see the increase happening on a 'weekly/monthly basis.' and was of the opinion that there is too much 'emphasis on bills from OFWAT.' S/he feels OFWAT are being overly strict on prices

A customer warned that STW's customers will want to see an 'instant return' and won't want rising bills, so maybe STW should 'take more to begin, save that money and use it later so customers will complain less'

An environmental group representative was of the view that 'an increase in costs to secure outcomes that will result in improvements in our environment is a driver for us to bring out the improvements that we, as a nation, want to see'

A conservation group representative felt that it was important to communicate with consumers about what the benefits are for them

An environmental group representative responded 'we should comply with a directive where it will be beneficial for customers and cost beneficial

A domestic consumer representative asked about the cost implications of trialling innovative technologies. S/he went on to question whether the UK should be complying with an EU directive that is 'imposing' additional costs on UK customers

A council officer stated that a step change in investment is required in this area and that prices for water will have to go up

A domestic customer representative responded 'I think that this will be unacceptable to customers'

Waste water workshop, 19 June 2012

In areas where there are concerns about river water quality, there was a view that taking action should be a priority.

A majority of stakeholders supported making significant improvements, but there was a significant minority of stakeholders who were concerned about the costs.

Customer support improvements, but our Willingness to Pay research showed that customers are unwilling to see significant increases in the overall bill, which may constrain the extent of improvements. In addition, our initial analysis suggests that the costs of a significant proportion of the potential programme for the next five years will be greater than customers' willingness to pay for river quality improvements.

We therefore believe that, on balance, whilst there is support for us to make progress against the Water Framework Directive, there is no consensus on how quickly and at what cost. We need to provide further information, and test in more detail, views on this.

Play our part, not the part of others

Related to the issue of cost and pace is the extent to which we contribute to achievement of the WFD and the extent to which other parties play their part. Concerns have been expressed by both our stakeholders and customer representatives that we should not take action where it is not our responsibility to do so.

"In order for us all to move forward the EA need to fulfil their lead role and set out clearer objectives for each stakeholder so that this can be incorporated into future plans. It is pointless STW investing in actions when the EA could ultimately decide to enforce actions on other stakeholders that could result in water bodies achieving good ecological status without the need for STW investment"

Stakeholder MTRC written response.

"... where the cause is diffuse pollution from agriculture or urban run off then STW should not be seen as the default position for funding improvements".

CCWater, MTRC written response

An environmental group representative highlighted that STW is in danger of 'working in isolation' adding that 'everyone needs to do their fair share'

A conservation group representative said the answer to this questions 'depends on whether you put your consumer hat on or your commercial hat on'. S/he felt that STW should look for the most cost effective way of tackling issues alongside more sustainable ways of doing things to save money in the long-run

Waste water workshop, 19 June 2012

Although some stakeholders felt that we should take more of a leadership position and support other playing their part.

All council officers [at the table] said that STW is a key player and that the company should become better at working with its partners.

A council officer said that STW needs to play the role of 'big guy in town'. STW is a major corporation and it should have greater lobbying power as a result

An environmental group member stated that STW has to deal with issues anyway because they will affect the company's reputation. It was agreed that STW needs to 'be a leader and assume the responsibilities because it is a key part of your business'.

Waste water workshop, 19 June 2012

Explore collaboration opportunities and use catchment management

Our regulators (DWI, Environment Agency and Natural England) are supportive of the use of catchment management to meet both drinking water quality and river water quality objectives.

Our key priorities

Environmental standards and drinking water obligations are met:

- *The water environment and drinking water supplies comply with all legal standards and requirements.*
- *Water bodies are prevented from deteriorating and move towards good ecological status or potential.*
- *The environment improves so that protected areas and habitats move towards compliance. For example, Bathing Water and Shellfish Water quality improves, the need for treatment reduces in water abstracted from Drinking Water Protected Areas; and biodiversity is conserved in Natura 2000 sites, at Sites of Special Scientific Interest and in the wider environment.*

Our ambitions

Catchment solutions deliver the priorities listed above and provide a wide range of ecosystem services:

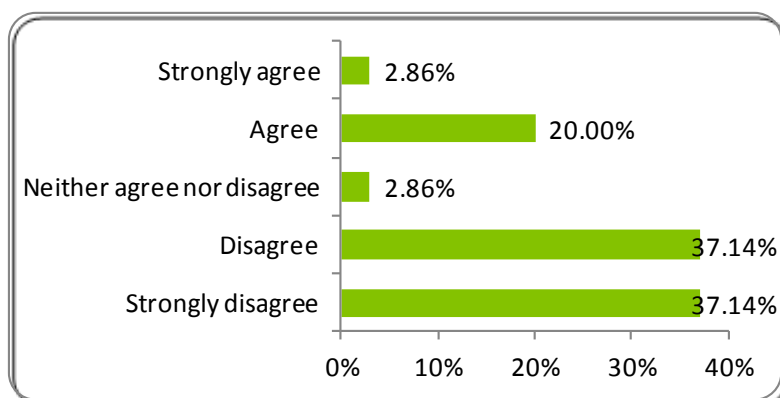
- *Novel and innovative catchment-based solutions that are sustainable and resilient to climate change become common place*
- *Joint funding and partnership opportunities are maximised*
- *Environmental improvements are secured that support and benefit communities*
- *Water companies continue to adopt a risk-based approach to managing the availability and quality of drinking water supplies that is evidence-based, and makes provision for managing emergencies and mitigating risks to consumers.*
- *Connectivity and resilience in public water supply and sewerage provision improve so that the impacts on the environment and people are minimised.*

A Catchment Approach for PR14 – A Joint Statement from the Drinking Water Inspectorate, Environment Agency and Natural England

As with the water workshop (12 June 2012), our stakeholders were supportive of us using catchment management to help us deliver outcomes. There was a strong consensus that we should rely less on traditional forms of treatment and more on changing the behaviours of others and addressing issues at source.

Waste water workshop, 19 June

To what extent do you agree with the following statement? *“STW should focus on its own assets rather than catchment solutions”*



Stakeholders would also like to see us use more innovative solutions with greater flexibility.

A customer representative was of the opinion that the demands of the WFD are so harsh it is financially crippling to meet them. S/he thought 'STW are shooting themselves in the foot by allowing phosphates in the water as the WFD is setting the bar so high that in the short-term it may be financially impossible for the company to meet targets'

An environmental representative commented that his / her agency had looked over the last few years at 'flexible ways of permitting' but with new technology, standards and EU directives in place, such as change in allowed phosphate levels, s/he 'need to revisit the work' as the ability to treat to tighter standards has 'moved forward'

A council officer felt that the current level of debt at STW is not sustainable and new approaches to investment need to be considered. S/he stated 'it's important to look at things differently and shift emphasis onto treatment solutions or flexible options rather than capital heavy investments'

A domestic customer representative added 'we're dealing with issues that are way beyond Severn Trent's control'. S/he felt that there were not yet adequate joined up catchment solutions to help resolve this issue

Waste water workshop, 19 June 2012

Use options that deliver multiple benefits

In addition to delivering improvements that are driven by the WFD, some options for further action could deliver broader benefits, particularly in relation to biodiversity and SSSIs. Natural England has stated it would like companies to consider options that deliver 'multiple benefits' (First meeting of the Severn Trent Water Forum, March 2012). Stakeholders at our 19 June workshop also encouraged us to look for wider benefits: *"A conservation group representative added that Water Framework Directive targets have to be met, and where SSSIs are under threat these should be tackled."*

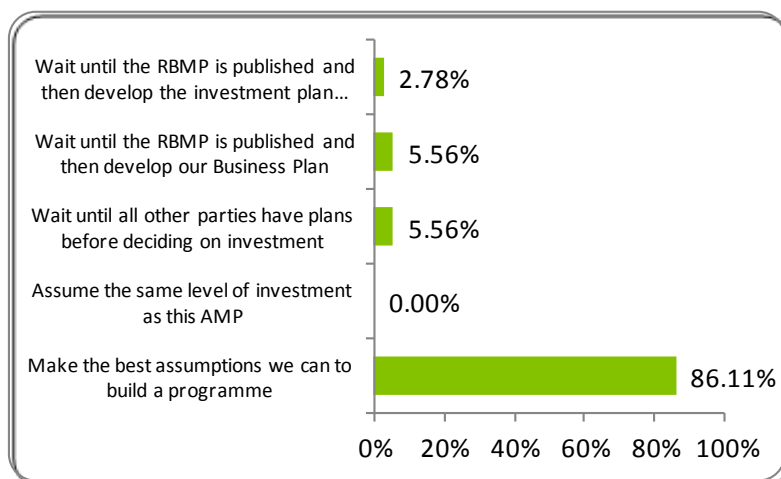
Make prudent planning assumptions

The extent of the environmental programme that we are required to deliver will not be fully confirmed until the publication of River Basin Management Plans in 2015. This is after our business plan will be submitted to Ofwat. At the 19 June waste water workshop, we asked stakeholders how we should deal this uncertainty.

Waste water workshop, 12 June

Our environmental programme will not be agreed until 2015. We need to consult on our business plan from April 2013.

Which of the following options would you recommend?



In its written response to *Making the right choices*, the Environment Agency broadly supported this approach. It noted, however, that there would be a risk that final requirements may be different to those assumed in our plan.

“We encourage you to be ambitious in PR14, however in doing so you will have to carefully consider risks associated with including an allowance for WFD in your business plans prior to certainty provided by Ministerial sign-off of the second river basin management plans in December 2015.”

EA written response to MTRC, July 2012

We discussed this issue and the risks associated at the second meeting of the Severn Trent Water Forum. It endorsed our proposed approach of making prudent planning assumptions.

Do more to explain these issues

Throughout our customer research, and stakeholder discussions, it was a common theme that both audiences did not have a full understanding of the role we play in protecting our region's water environment. This suggests there is more we can do to communicate to our stakeholders so that they can better understand the role they can play, and our customers to increase their appreciation of what they pay for.

In summary, what have we learned so far?

We have learned from the evidence we have gathered to date:

- There is both customer and stakeholder support to take action to protect the water environment through more sustainable abstraction and the water framework directive.
- There is no clear consensus, however, as to the extent of action we should take, and the pace at which we should progress. In the case of the WFD, a majority of stakeholders consulted favoured rapid action to make improvements but some were concerned about the impact of this on bills. Customer support for improvements is significant, but insufficient to support all of the potential programme.
- Stakeholders want us to play our part, there is some concern that we do not take on the responsibility of others.
- We should use catchment management and other innovative approaches to help make our contribution.
- We should seek out wider benefits for the water environment and biodiversity in the approaches we take.
- This is a difficult issue for our customers and some stakeholders to understand.



8. We will protect the wider environment

Where are we starting from?

We began AMP 5 with the aim of delivering a leading position in sustainable operations, and minimising our carbon footprint. We already led the sector in the use of digestion biogas in Combined Heat and Power engines to generate power. However, we acknowledged that this leading position must not compromise standards or increase customer bills beyond levels which our customers were willing to pay.

We have continued to increase our use of sewage sludge as a renewable energy source and maintained a leading position within the water sector on renewable production. As of 2011-12 we are on track to go beyond the commitment made in our business plan to deliver no net increase in emissions by 2015.

We started AMP 5 already recycling over 80% of our sludge production and set out to ensure that we continued to deal with this product and the other by-products of our business in a sustainable way, minimising and recycling where we could.

Where have we taken information from?

We have taken stakeholder views from a range of sources, but principally from our climate change workshop on 21 May 2012 and written responses to *Making the right choices*. Around 35 individuals and 29 separate organisations attended our climate change workshop. Over 50% of attendees were from local authorities. The remaining attendees represented environmental groups or customers.

What have we learned?

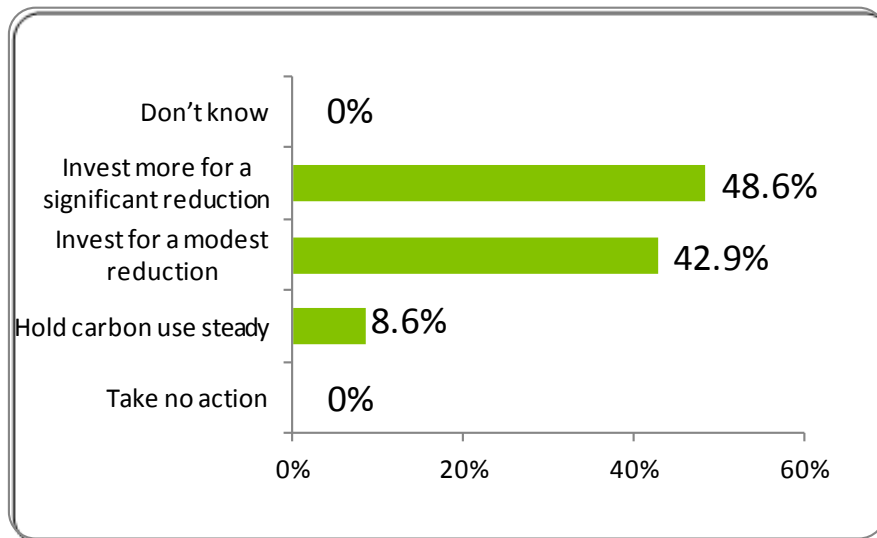
The following summarise the key insights we have drawn from this information.

We should invest to reduce our carbon footprint

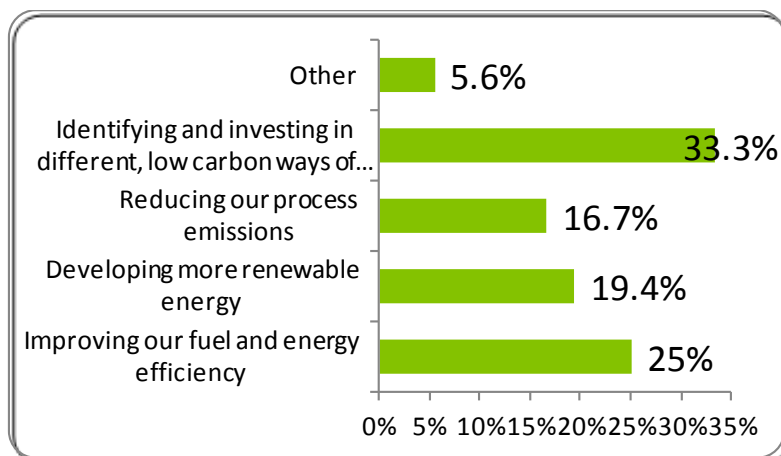
Stakeholders who attended our workshop believe that we should invest to achieve a *reduction* in our carbon footprint, with 49% supporting a significant reduction. The majority of support was to achieve this through investment in different, low carbon ways of designing and building infrastructure, followed by energy efficiency and developing renewables.

Climate change workshop, May 2012

Which of the following do you believe STW should adopt towards our carbon footprint?



STW could do some or all of the following but which would you like us to prioritise?



Stakeholders responding to our MTRC document also supported this view expressing support for energy efficiency and then renewable investment as a way to achieve a reduction in our carbon footprint.

"We would support further investment by STW in renewable energy particularly where this can improve the resilience of STW's infrastructure."

Stakeholder MTRC written response

"We would support increased investment in measures to reduce the carbon footprint of the business ... replacing equipment with more energy efficient equipment, more anaerobic digestion and fuel efficient vehicles."

Stakeholder MTRC written response

Reducing our carbon footprint should not be achieved at high cost to the customer

Results from other customer research also indicate there may be modest support for investing more in renewables. Our 2012 Q2 STW Customer Satisfaction survey indicated that 42% of customers believe we should do more, 16% thought we were doing the right amount and 38% didn't know.

CCWater's response to *Making the right choices* agreed that we should invest to see a "modest reduction" in our carbon footprint.

We therefore believe that both our customers and stakeholders support investment to reduce our carbon footprint by a modest amount.

We should encourage customers to be carbon efficient in the way they use water

Stakeholders responding to MTRC document expressed that we should work with customers to encourage them to use water efficiently, and therefore become more carbon efficient.

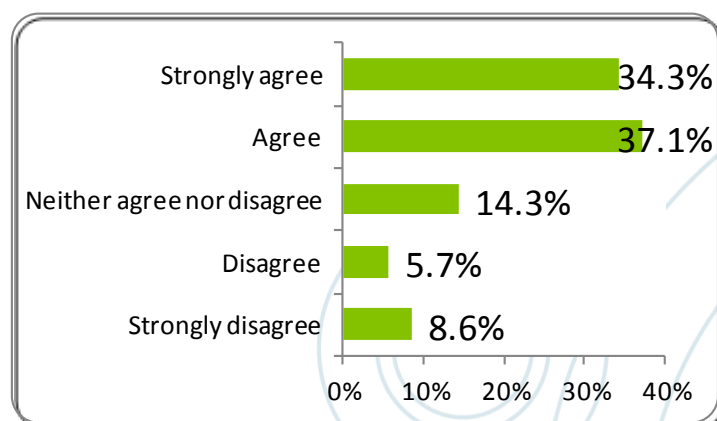
"We would recommend that customer incentive schemes should be looked at to encourage efficiency."

Stakeholder MTRC written response

Attendees at our workshop on 21 May were also supportive of this view. Over 60% of attendees believed that it was our responsibility to encourage customers to be more carbon efficient in the way they use water.

Climate change workshop, May 2012

To what extent do you agree with the following statement? It is STWs responsibility to encourage its customers to be more carbon efficient in the way they use water.



In summary, what have we learned so far?

We have learned from the evidence we have gathered to date:

- There is support for modest to significant investment to reduce our carbon footprint.
- However, that investment should not lead to significantly higher costs for customers.
- We should work with customers to increase water efficiency and therefore help them become more carbon efficient.



9. We will make a positive difference in the community

Where are we starting from?

In our Strategic Direction Statement, we made a commitment to enhance our involvement with local communities and our customers. We delivered this through the continued use of facilities such as education centres on our works and visitor experience sites.

We have a role in protecting and enhancing biodiversity at our sites or sites affected by our activities. We own or partly manage 37 Sites of Special Scientific Interest and work in partnership with our tenants and other partners to safeguard them. We have around 21 rangers who manage our 12 public access sites working with volunteers and organisations like the RSPB and Wildlife Trust. The sites provide the opportunity to engage with customers whilst enhancing and protecting the sites for nationally and internationally important species such as butterflies, water voles and tree sparrows.

We continued the programme of work started in AMP 4 on odour control at sewage treatment works and on sewerage systems. Research showed that customers supported our work to reduce the odour created by sewerage but not to the extent of very high-cost improvements.

Where have we taken information from?

Stakeholder views have been collected from the series of *Making the right choices* consultation and workshops held during the summer of 2012. The stakeholders included business customers, local authorities and council leaders, and journalists.

Customer focus groups took place in August 2012 in Nottingham and Birmingham to discuss the role of STW in the community. We have also drawn on evidence from our historic catalogue of customer and stakeholder research.

What have we learned?

The following summarise the key insights we have drawn from this information.

Customers expect good facilities at reservoir/visitor sites

Research carried out about our public access sites showed that although 99% of visitors enjoyed their visit to our sites at all locations, where facilities are sparse, or under-maintained, there is usually a negative reaction. Our public access sites can be very strong drivers of advocacy, particularly where we have invested in the facilities available for visitors. Carsington for example, is highly regarded by visitors. Sites where there were minimal or no facilities and had no obvious signs of investments were perceived in a negative way.

Stakeholders strongly believe STW should be doing more to educate

MORI stakeholder research conducted in 2011 demonstrated that the majority of stakeholders (and over 82% of constituency MPs) believe that it is important for STW to be active in the community with a focus on educating communities and schools about water efficiency, the environment and responsible waste water use. This was supported through our 2012 stakeholder workshops and focus groups where community education emerged as a strong theme.

Our 2012 focus groups showed that customers do not appreciate the full extent of the company's activities and responsibility, and there is a great need and opportunity to educate customers in this area.

An environmental group representative agreed with the view that individuals are misusing sewers but pointed out that 'STW shouldn't pass the blame to a third party'. Instead, STW should work with partners and customers to educate them about the effects of sewer misuse

A council officer agreed that education is key and educating children in schools is essential to ensure they know care of sewers is understood from a young age. 'STW needs to plant the seeds for the younger generation' s/he added

All agreed STW needs to engage with schools, Parish Councils and neighbourhood groups on this issue

Waste water workshop, 19 June 2012

A business group representative commented that public education is important. S/he felt it was important for 'STW to work in partnership' with others to educate the population in ways to be more efficient and save water

An environmental group representative said 'how about using hosepipe bans when it is just a dry summer, not waiting for a drought situation, and explain it's to protect the drinking water supply. There is a need to educate people'

Water workshop, 12 June 2012

A council officer mentioned that STW is managing expectations well. If people are aware of the problem they will understand if they spent hours or days without water. The key aspect is to educate people about the problems that STW is facing

A council officer said STW needs to educate customers of the benefits of using water butts

Another environmental group representative stated that STW should do more to educate consumers

Climate change workshop, 20 May 2012

Customers appreciate their role in responsible water and waste water use

Our customer focus groups show that customers generally understand their role in saving water and responsible sewer use, but wanted Severn Trent to tell them more about what they could do and the benefits.

In relation to STW working in communities, traffic impact is a key concern for customers

Our customer focus groups carried out in August demonstrated that the impact on traffic of our operations causes the most significant irritation to customers and is one of the most important drivers of the company's overall reputation.

One issue our focus groups highlighted is the affect of roadworks on the community. Road users are tolerant of the disruptions when we are more sympathetic to the inconvenience that is caused by providing as much notice and detail about planned works and keeping the community advised of updates. Our customers also would prefer that we work with other utility companies and align repair works in order to minimise disruptions, as frustrations grow when main roads are repeatedly dug up, re-opened and the closed again by another utility company for more repairs. Customer concern can be minimised as long as they are given sufficient notice and explanation of the need for the works.

Odour and other nuisance schemes are unlikely to win widespread public support

Nuisances such as noise and odour control were of lower interest and priority to customers as most are not impacted by them on a regular basis. Customers at our focus groups were unsympathetic to those who complain about odour control of our sites. They believe that by choosing to live near an established site then the odour is a factor that they would need to accept, and that it is not be an effective use of customer money to try and resolve.

We would need to consider this in the light of views of specific customers who suffer nuisance issues.

In summary, what have we learned so far?

We have learned from the evidence we have gathered to date:

- Our customers and stakeholders believe that education is extremely important and that there is a continued need to educate customers to enable them to contribute towards our key campaigns, such as water efficiency, the value of water and the disposal of fats, oils and greases.
- Customers who visit our public access sites are appreciative of the sites where we have invested money and provided facilities but are likely to perceive the less developed sites negatively.
- Our customers are more understanding about the repairs work we conduct when we communicate our plans and update on a regular basis, so they know what we are doing when,

why we are doing it and the potential duration for disruptions. They also expressed that they wished for utility companies to work and plan road works collaboratively in order to reduce the number of disruptions caused by road works.

- Customers have also expressed that they are happy for investments to be made on improvements where there is a true benefit and one that will affect the wider community as opposed to a small percentage. This was demonstrated in the view on investments to reduce odour control, where most of our customers would not be affected by the odour and are largely unsympathetic to those who 'choose' to live close to sewage treatment works.



10. We will finance our business sustainably

Where are we starting from?

We use a combination of revenue from customers' bills, debt and equity (shareholders) to finance our business. This helps us to sensibly phase the costs of investment and manage risks. We aim to ensure our investors receive a return that is commensurate with the risk they take on.

Around a third of the average household combined bill goes towards the costs of financing – interest on debt, profits paid on dividends and taxation.

In that year, due to efficiencies from our approach to finance we were able to make a special dividend payment of £150 million to our shareholders, we matched this with £150 million of additional investment to improve our services to our customers.

Where have we taken information from?

We have not asked our customers directly about this issue. This is because it is the role of our economic regulator, Ofwat to set a fair rate of return that allows us to sustainably finance our business.

We do know, however, from comments made in our quarterly tracker of customer satisfaction that this is an issue that is often at the forefront of customers' minds when they discuss water. In this survey, we ask customers to add a 'message to management'. These comments are summarised below.

We have also reviewed evidence from the national customer research carried out for the 2009 price review.

In 2011 we commissioned Makinson Cowell to interview 26 leading institutional investors (face-to-face and telephone interviews). The survey considered investors in the publicly-quoted utility companies – National Grid, Centrica, Northumbrian Water, Pennon, Severn Trent and United Utilities. Institutional investors hold 65% of the shares in these companies. We have included some of their comments below.

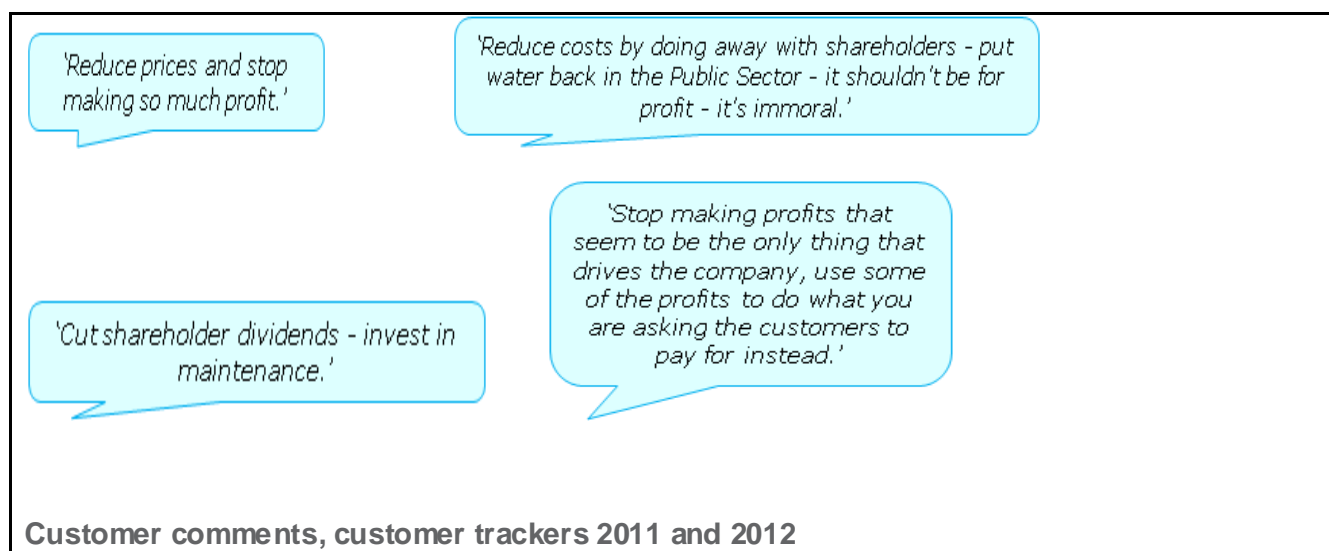
We have also looked at evidence from national reports and investor surveys and a report by Moody's, the credit rating agency.

What have we learned?

The following section summarises the key insights we have drawn from this information.

Our customers perceive our shareholders receive excessive dividends

Comments made by our customers in our quarterly tracker show that they perceive our shareholders receive excessive dividends or that we make excessive profits.



There were similar findings in the national research carried out for the 2009 price review²: "Respondents could see no justification for bill increases when they discovered the rises in salaries and dividends. Stories about profits resonated far beyond the geographical boundaries of the companies' areas and there was a great deal of suspicion. In many cases discussions about willingness to pay for improvements or maintenance of standards were moved decisively towards discussions of profit levels of water companies and proposals that a higher percentage of profits should be used to fund the companies requirements".

Investors generally have confidence in the sector but there is some concern about regulatory changes

Water UK commissioned investor surveys at the time of the price review, carried out by Indepen^{3,4}. Most respondents in the 2008 survey believed that the water sector was well placed to continue to finance its large capital programmes. respondents considered water to be more risky than UK energy transmission, on a par with UK energy distribution and less risky than electricity generation, UK energy supply and EU utilities generally. It was also seen as less risky than individual companies such as BT and BAA.

² Deliberative Research concerning Consumers' Priorities for PR09 for the Water Industry Stakeholder Steering Group, Corr Wilbourn, May 2008

³ 2008 Investor Survey, Indepen, March 2008

⁴ Investor Survey: Ofwat's PR09 Draft Determinations, Indepen, September 2009

Investors after the 2009 survey took a less favourable view. A substantial proportion of those interviewed, particularly equity holders, expressed concern that the regime was no longer transparent and trustworthy in the way it had been formerly. However, this was between Draft and Final Determinations, and after changes made by Ofwat in its Final Determinations investors may have taken a more favourable view.

Moody's, a credit rating agency, issued a report on the sector in October 2012⁵. This said that: "The fundamental business conditions for the UK water sector are stable, reflecting steady operating performance and price increases that have been sufficient to offset rising costs. Negative credit pressure will build for water companies in England and Wales over the medium to long term, due to a shifting regulatory landscape associated with Ofwat's ongoing review of regulation..."

We expect planned regulatory and legal reforms, and a desire to demonstrate the benefit to customers of competition, to lead to a tougher operating environment for companies and a potential deterioration in the overall credit quality of the water sector". Similarly, in February 2013, it referred to "a continuing low business risk profile for the UK water sector"⁶ but said that "In future, we may... see a wider spread of ratings and or more diverse ratios guidance for a given rating category to reflect company-specific strengths and weaknesses in adapting to the new framework" and that "Medium to long term credit risk for the sector may yet increase as Ofwat continues to work on introducing competition to other parts of the value chain, particularly in the upstream business, including water abstraction, resources and treatment".

Investors believe shareholders (equity) will have a continued role

Investors surveyed by Makinson Cowell were generally, though not universally of the view that the scale of future capital investment required by the industry, cash shortfalls, and the possible impact on customer bills, mean that equity should continue play an important role in financing.

"Generally the unlisted regulated utilities are very highly levered, so they tend not to have any flexibility at all. God help them if something goes wrong!"

"Debt has a part to play, but the sheer quantum is going to be difficult, plus the speed at which the capex is required to go in to certain projects may make it difficult, even in the short term."

"You can't run these things without equity, but whether you can do it without quoted equity is an interesting question. The main thing that quoted equity does is that it gives a good signal to the regulators as to how sensible or otherwise they are being with their allowed levels of returns, which actually supports all the non-quoted entities very well."

"It will be interesting to see how the equity market steps up to the sheer size of the investment that has to be done over the next 20 years because what I would observe is that over the last couple of years is that the rights issues by the utilities have not been particularly well received. Part of that is due to investors' perceptions that for that new incremental investment the returns are not quite as attractive as they need to be."

⁵ UK Water Sector, Moody's Investor Service, October 2012

⁶ Ofwat's Methodology for PR14 Likely to be Credit Neutral, Moody's Investor Service, February 2013

“Given the kind of capex we are talking about, it cannot be funded only by debt, so the equity component has to come in. The regulators need to realise that the cost of raising new equity is not the same as the cost of equity which they typically assume.”

“People look for utilities as dividend payers and that is one key yardstick which the market uses to value the sector. If you are paying a sub-standard dividend then it may be that your cost of capital is higher and therefore it may be that you are delivering poorer value at the end of the day to the customer.”

Makinson Cowell investor survey, 2011

Concern about shareholder returns

There has been significant media and political interest in recent months about:

- Tax avoidance by some water companies, e.g. “six of the water companies - Northumbrian, Yorkshire, Anglian, Thames, South Staffordshire and Sutton and East Surrey Water - are artificially adding to their debts by taking high interest loans from their owners through the Channel Islands stock exchange”⁷.
- The level of dividends paid by some highly-g geared companies e.g. “At the top end of the range, companies have been paying out close to 25% of their equity asset base (‘equity RAV’) to their holding companies... I would have hoped that companies would have shared gains that derive from external factors with their customers”⁸ (The Severn Trent figure was about 8%).

The limitations on the ability of companies with high levels of borrowing to raise additional finance e.g. “If they [Thames Water] had followed a more responsible corporate policy, they would now have the capital resources to support investment. The profligacy of the owners should be no excuse to let off Thames Water from its obligations and the company should be asked to make a substantial contribution to the [Thames Tideway] scheme. This will need to come through a rights issue”⁹. These concerns have generally been directed at companies with high gearing (a high proportion of their total finance raised from borrowing). Similarly, we have also raised concerns about the risks of high gearing and the need to attract additional finance from shareholders¹⁰. The concerns do, however, raise general issues about the right balance between investors and customers, and whether there should be more sharing of outperformance, which we will take into account in developing our plans.

⁷ Leaking away: The financial costs of water privatisation, Corporate Watch, February 2013

⁸ Observations on the regulation of the water sector, Lecture by Jonson Cox, Chairman of Ofwat, March 2013

⁹ Article in The Times, Sir Ian Byatt and Simon Hughes, MP, November 2012

¹⁰ Changing course through sustainable financing: Options to encourage equity financing in the water and energy sectors, Severn Trent and National Grid, September 2012

In summary

- Our customers are concerned about shareholders, particularly as they perceive they may receive excessive returns
- Investors believe shareholders will have a continued important role in the future financing of the industry.

