

Ms Sonia Brown
Ofwat
Centre City Tower
7 Hill Street
Birmingham
B5 4AY

01 April 2014

Dear Sonia,

We wrote to you on 14 March 2104 providing our observations on Affinity Water's bid for enhanced status. Our views were based on the company's work in progress at that date. Subsequently, in response to discussions with Ofwat, the company refined their Outcome Delivery Incentives (ODI). As the CCG, we are writing again to you to comment on the company's latest proposals.

Affinity Water provided us with a four-page memorandum comparing the ODIs included in their bid dated 17 March 2014 against their latest proposals. The memorandum included the following summary of the changes:

- No change to performance commitments
- Revised calculations align to Ofwat's July 2013 methodology and send strong signal to customers that rewards can only be earned when targets are exceeded by delivering exceptional performance
- Penalties for failure to achieve performance equal to a little more than 2% of our Return on Regulatory Equity (RoRE).
- Rewards for outperformance will be around 0.5% RoRE.
- Previously both rewards and penalties were in balance at around +/- 1.5% RoRE.
- Increased number of performance commitments that attract penalty to 7 ODI's (previously discussed: leakage, restoring sustainable abstraction, supply interruptions more than 12 hours and new: average water use, water available for use, water quality standard and customer contact on discoloration).
- Overall, there will be less bill impact from rewards for outperformance and greater prospect of reductions in bills if we fail to perform.

The CCG considered these changes by email and telephone exchanges.¹

¹ The following CCG members participated in the discussions: Robin Dahlberg (Chair), Jim Barker (EA), Allyson Broadhurst, Keith Cane, John Fox, Karen Gibbs (CCWater), Kathy Hughes (WWF), Tim Hutchings, Mark Kibble, Hazel Smith, Jill Thomas (CCWater) and Damian Williams.

The 2012-2013 customer research showed that customers were reluctant to reward the company for over performance, but keen to extract penalties when they under performed. As the latest package of ODIs reduces the potential rewards and increases the potential penalties, the CCG believe this ODI package will be more acceptable to customers than the package in the first bid for enhanced status.

We note that Affinity Water's March 2014 customer research showed that 94% of customers either supported or did not object to the proposed future water bills that were implied by the company's first bid for enhanced status. These bills would always be lower than they were in 2015 in real terms (before inflation). As the latest changes to ODIs mean that bills can only be even lower, the CCG believe it is reasonable to extrapolate from this March 2014 research and conclude that customers will support the new changes to Affinity Water's ODI package.

Yours sincerely,

A handwritten signature in black ink that reads "Robin Dahlberg". The signature is written in a cursive style with a large, looped initial 'R'.

Robin Dahlberg

CC Georgina Mills