

**Thames Water**  
**PR09 Business Plan Challenge Team**  
**Final Report**

## Executive Summary

In November 2009, Ofwat will determine the price that customers will pay for the water and sewerage services they receive over the following five years. Price limits for Thames Water's customers will be set on the basis of an agreed final Business Plan. This will set out in detail the levels of service and improvements that the company will commit to deliver over that period. The business plan submission, therefore, is the key company submission for the periodic review.

Thames Water have prepared their draft business plan using quality assured processes, based on the principles contained in the company's regulatory information governance framework developed in 2006 and used with great effect on both the 2007 and 2008 June Returns to Ofwat.

The business plan has been challenged by the company's Regulatory Committee (a formal Board committee including non-executive directors, with delegated authority from the Board) and the PR09 Steering Group (attended by members of the Executive Management Team and established to supervise the companies preparations for PR09). It has been underpinned by Thames Water's largest ever programme of qualitative and quantitative research designed to ensure their plans are cost-beneficial and that customers' and stakeholders' priorities are understood and reflected in planned outcomes.

To provide external challenge and augment internal processes for the development of the business plan Thames Water established The PR09 Challenge Team. The Challenge Team had the objectives of providing a thorough independent review of Thames Water's draft Business Plan. The principle of the Challenge Team has been discussed with the company Reporter who supported the approach taken.

✂ [Redacted]

The Challenge Team played a major role in the processes that resulted in Thames reducing the scale of its proposed AMP5 investment programme from approximately £8 billion to £6.5 billion. The review process prompted Thames to reassess and further challenge significant elements of its Business Plan proposals, make a number of substantial changes to investment plans, and to re-visit and update the evidence presented in support of its investment cases. In addition Thames appointed an external consultant ✂ [Redacted] to undertake a technical author review of all of its investment cases.

There was acknowledgement by the Challenge Team that Thames had exposed its plan to significant internal challenge in order to develop its constrained business plan whilst managing associated risks. The Challenge Team therefore saw it as essential that the submission clearly conveyed this level of challenge, and highlight the consequences for customer outcomes, regulatory requirements, and statutory obligations if Ofwat were to cut back on Thames' proposed programme.

In certain instances the Challenge Team's examination of Thames' proposals has led to further analysis that will provide evidence in time to inform the final Business Plan submission – resulting in Thames' inclusion of some reserve positions in its draft submission.

## The purpose of this document

This document is the final report from the Challenge Team's scrutiny of Thames Water's draft Business Plan. It sets out the role of the group, the way in which the Challenge Team review sessions operated, and the impact they have had on the development of Thames' draft Business Plan submission.

The report is structured under the following sections:

1. Role of the Challenge Team
2. Scope of the Challenge Team
3. Summary of Challenge Team Scrutiny Sessions
4. Impact on Thames draft Business Plan
5. Challenge Team Endorsement

## 1. Role of Challenge Team

The Challenge Team was established to provide a comprehensive independent review of Thames Water's approach to the development of its draft Business Plan and to provide reassurance to the Thames Water Board and Executive Management Team (EMT) that the preparations for PR09 are robust, stand up to commercial scrutiny and have been vetted for stakeholder acceptability.

The Challenge Team process was designed and run in the format of a scrutiny panel so that it would provide demonstrable evidence to the Reporter and Ofwat that every effort has been made to challenge the robustness of the business plan and that Thames Water's processes, up to Board level, are robust.

The Challenge Team panel was chaired by David Owens. Its members ✂ [Redacted] were drawn from the external business environment and Thames Water's senior management team. Members were selected and invited to join the Challenge Team on the basis of their significant experience and expertise in the water industry, economic regulation, and other utility sectors in the UK.

✂ [Redacted]

## 2. Scope of Challenge Team

✂ [Redacted]

The Challenge team operated in the manner of a “scrutiny panel”. The coverage of the case review topics were constructed to ensure that Thames Water’s draft Business Plan and processes were subject to comprehensive examination.

✂ [Redacted]

At the case review sessions the Challenge Team were presented with key elements of Thames’ draft Business Plan proposals, including the approach to case development, argumentation, evidence, and proposed outputs.

✂ [Redacted]

At each review session the Challenge Team were given the opportunity to cross examine Thames Water’s PR09 workstream leads and scrutinise the supporting evidence.

✂ [Redacted]

### **3. Summary of Challenge Team outcomes**

This section first sets out a summary of the generic support and challenge provided by the Challenge Team across the nine review topics. It then sets out, topic by topic, the specific areas of support and challenge and the actions / next steps arising for the PR09 team which required further work in advance of the draft submission in August 2008, and where indicated for the final submission in April 2009.

#### **SUPPORT**

Overall, the Challenge Team felt that Thames Water's draft Business Plan was very clear. The approach taken by Thames in developing its plan had ensured that a comprehensive assessment had been undertaken of the full range of issues facing the business post 2010 – including the difficult issues.

There was recognition from the Challenge Team that the evidence base and supporting analysis for the proposed package of activity contained in the business plan was comprehensive and credible.

The Challenge Team viewed Thames' stakeholder consultation exercise as extensive and rigorous. The outcomes of this analysis were seen as driving the development and refinement of the draft plan.

Thames' internal management systems and planning processes were recognised as being aligned with Ofwat and UKWIR best practice guidance. It was acknowledged that Thames had undertaken significant work in the early years of AMP4 to ensure that best practice asset planning was embedded in business as usual PR09 decision making – this had been demonstrably successful.

#### **CHALLENGE**

There was acknowledgement by the Challenge Team that Thames had exposed its plans to significant internal challenge in order to develop the constrained business plan whilst managing associated risks. The Challenge Team therefore saw it as essential that the submission clearly conveyed this level of challenge, and highlight the consequences for customer outcomes, regulatory requirements, and statutory obligations if Ofwat were to cut back Thames' proposed programme.

Overall the Challenge Team felt that the business plan needed to provide greater clarity in the following areas:

1. the internal processes and evidence based challenge which had been brought to bear on investment needs generated through operational assessments;
2. the impact of cost benefit analysis and willingness to pay research on the final package of solutions;
3. the level of development of alternative options that underpin the final proposals; and
4. the level of residual risk retained in the plan.

✂ [Redacted]

## 4. Impact on Thames' draft Strategic Business Plan

✂ [Redacted]

The Challenge Team scrutiny process resulted in the Thames Water's PR09 team undertaking an extensive review of its proposed investment plans and has led to many substantial changes to Thames' proposals including:

- further internal review of supporting evidence;
- additional analysis and external benchmarking;
- external independent peer review of our approach to Cost Benefit Analysis; and
- significant modification to the structure and presentation of investment cases.

As a result the Challenge Team played a major role in reducing the scale of Thames' proposed investment plan from approximately £8 billion to £6.5 billion.

In response to the Challenge Team's comments on the need for greater consistency and clarity in the presentation of required investment, ✂ [Redacted] an external consultant was appointed to undertake a technical author review of all Thames Water investment cases.

✂ [Redacted] The external consultant worked with Thames Water's PR09 investment case leads to develop a consistent case structure that they have subsequently applied across their draft business plan submission.

In addition, the external consultant undertook a thorough review of the strength of the supporting argumentation and evidence provided for each investment case – highlighting where they believed the level of evidence could be better presented and augmented reflecting the clear drivers for investment. In response investment workstream leads have reviewed the presentation of their cases and supplemented the level of supporting information and evidence where required.

The Challenge Team review has also set in train a number of important workstreams designed to deliver further evidence which will be used to influence the package of proposals in Thames Water's final submission

✂ [Redacted]

## 5. Challenge Team Endorsement

The Challenge Team confirm that this is an accurate description of the comprehensive examination that we undertook of Thames Water's draft business plan.

The information provided in this report provides an accurate description of the processes Thames Water followed, the information we were provided with and the comments and challenges that the Challenge Team levelled at the business plan cases brought forward to the review sessions.

✂ [Redacted]