

## **Issues Paper Customer Engagement, Insight and Service June 2015**

*Topic:*

Customer engagement, insight and service

*Scope:*

This paper discusses how continuous engagement will enable a deeper understanding of customers' priorities over the short, medium and long term. The paper examines how continuous customer engagement will assist companies in identifying changing customer priorities whether that be through social, technological, economic or financial factors. It assesses the use of customer panels to test themes, issues, priorities and programmes over the life of a business plan's development. The work also considers the range of customer research techniques and data available to companies including the potential cognitive challenges when engaging with customers on key areas of activity e.g. willingness-to-pay. Consideration is given to good practice from other sectors, the perceived best practice from the PR14 process and recent developments in research methodologies and techniques.

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## *Background*

It is well documented that the water industry faces a number of long term challenges, from population growth and rising customer expectations, to addressing issues of climate change<sup>1</sup>. Coupled with this are the more established challenges around customer affordability, water scarcity and diminishing efficiencies. In the immediate future, the sector also needs to develop the opportunities created through retail competition as well as the other reforms put forward in the Water Act. Therefore, it has never been more important for the water industry to enhance its ability to protect the environment and continue to increase value for its customers and stakeholders.

## *Introduction*

Since privatisation in 1989, the water industry has invested significantly in protecting the environment, whilst greatly enhancing levels of service to customers and stakeholders. Typically, levels of investment have been reflective of the relative success of each price review and the economic arguments put forward in business cases. For the 2014 price review (PR14) Ofwat introduced a step change in how companies approached the development of their business plans. This change placed customers at the heart of the price setting process and ensured customer views informed each stage of the business planning process. Unlike previous price reviews, water companies consulted its customers to ensure business plans reflected the outcomes they and wider society wanted at every stage of the water cycle, from improved water quality to protecting and improving the environment. This process was challenged and endorsed by the newly established Customer Challenge Groups (CCG).

## *Context for PR19*

Customer engagement will need to play an even greater role in the run up to the next price review in 2019. Ofwat has already stated that companies will be expected to achieve '*dynamic upper quartile standard that moves during the period*'<sup>2</sup>, which is a further development to the fixed benchmarks set out in the PR14 final determinations. This change in approach will require the sector to reconsider how it approaches customer engagement and the provision of consistent market data in preparation for PR19. It is also expected that a number of reviews being undertaken by UKWIR<sup>3</sup>, Consumer Council for Water<sup>4</sup> and individual consultants will feed in to this thinking during 2015.

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<sup>1</sup> Ofwat's Forward Programme, Ofwat, 2015

<sup>2</sup> 'Cox warns of 'dynamic' PR19', Utility Week, March 2015

<sup>3</sup> The Future Role of Customer and Stakeholder Engagement in the Water Sector, UKWIR, Due November 2015

<sup>4</sup> The Customer Voice and Price Setting, Consumer Council for Water, June 2015

## *Defining customer and stakeholder engagement and the role of the regulator*

### **Exploration of customer needs**

To ensure customers receive services they truly value, the industry needs to understand customers attitudes and behaviours towards the established and long term challenges facing the water industry. Whilst activity during PR14 aimed to achieve this, the period in which activity was undertaken did not allow the industry to observe or monitor the changing attitudes of its customers as well as it could have done. The UK also experienced the worst recession in recent history in the run up to PR14 which put the issue of customer affordability at the top of the political agenda, which limited the level of investment companies could plan for. For companies embarking on a price review, it is important for them to understand upfront what services customers want or could have, at a price that is affordable<sup>5</sup>.

### **The role of Customer Challenge Groups**

It is essential that the sector continues to create value for customers and stakeholders. The part in which CCGs play must become more strategic in its thinking to ensure company plans are deemed 'dynamic' and continue to reflect customers and stakeholders views. CCGs and companies must understand customers attitudes and behaviours towards the established and long term challenges if they are to agree future service levels at a price customers can afford. Companies and CCGs should work together to identify what big issues face the region and set out a programme of customer engagement to address these e.g. resilience, drought, catchment management, customer service, bill profiling etc.

This approach brings the opportunity for local level engagement. Previous price reviews have tended to address industry or regional wide issues only. Given the increased need for investment to address big issues, such as resilience, companies and the regulator would need to consider how to evaluate the legitimacy of local level engagement for specific investment in future business plans.

### **The role of Ofwat**

This approach may require a wholesale shift in the way the industry approaches future price reviews. For example, the one size fits all regulatory framework may need to change to allow companies the flexibility to submit and agree business plans with the regulator, requiring CCGs to become more strategic and able to effectively challenge company thinking. The companies themselves must also consider

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<sup>5</sup> Affordability is addressed in a separate paper as part of wider Water2020 review

approaching customer engagement on a more frequent basis. The recent review undertaken by UKWIR<sup>6</sup> highlighted that many companies' customer research activity was more aligned to the regulatory process, rather than '*meaningful {customer} engagement*'. If the industry is to develop more innovative approaches to customer engagement, the regulator needs to be less prescriptive in how it expects companies to undertake customer engagement at the next price review.

The introduction of a dynamic approach to the price review process would require the regulator to have the confidence to step back and allow companies the flexibility and autonomy to own the relationship with their customers. One example of where this is in place is Scotland, where Scottish Water has recently negotiated its plans directly with the independent Scottish Customer Forum. During this process, the Scottish regulator facilitated the dialogue between the two parties, rather than setting the agenda. By providing companies with the responsibility to own its relationship with customers, this should encourage more continuous customer engagement rather than the regulatory process dictating the dialogue.

### **Continuous customer and stakeholder engagement**

Across other sectors, customer engagement is seen as a continuous activity, not just undertaken to develop business plans. For example, in the financial services sector, companies undertake longitudinal studies to monitor customer attitudes towards company brands; perception of value for money to highlight changing social and economic trends; and have structured engagement programmes to ensure companies support the priorities of their customers and key stakeholders. The development of social media channels has also provided financial services companies with an opportunity to measure real-time customer sentiment or feeling.

Continuous research such as this would provide the industry with a more customer centric approach to the price review and give further opportunity to explore any customer and/or industry issues which may have not been addressed previously. Through CCG assurance, the regulator can be confident that customers have been consulted on a regular basis to ensure development of the plan is representative of their views (both at a strategic and tactical level). This ongoing activity will benefit CCGs by helping them understand what customers and stakeholders truly value, as well as allow them to get fully involved in the research.

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<sup>6</sup> Post PR14 Customer Engagement, Communication and Education, UKWIR, 2015

### **Customer and stakeholder engagement to support the price review process**

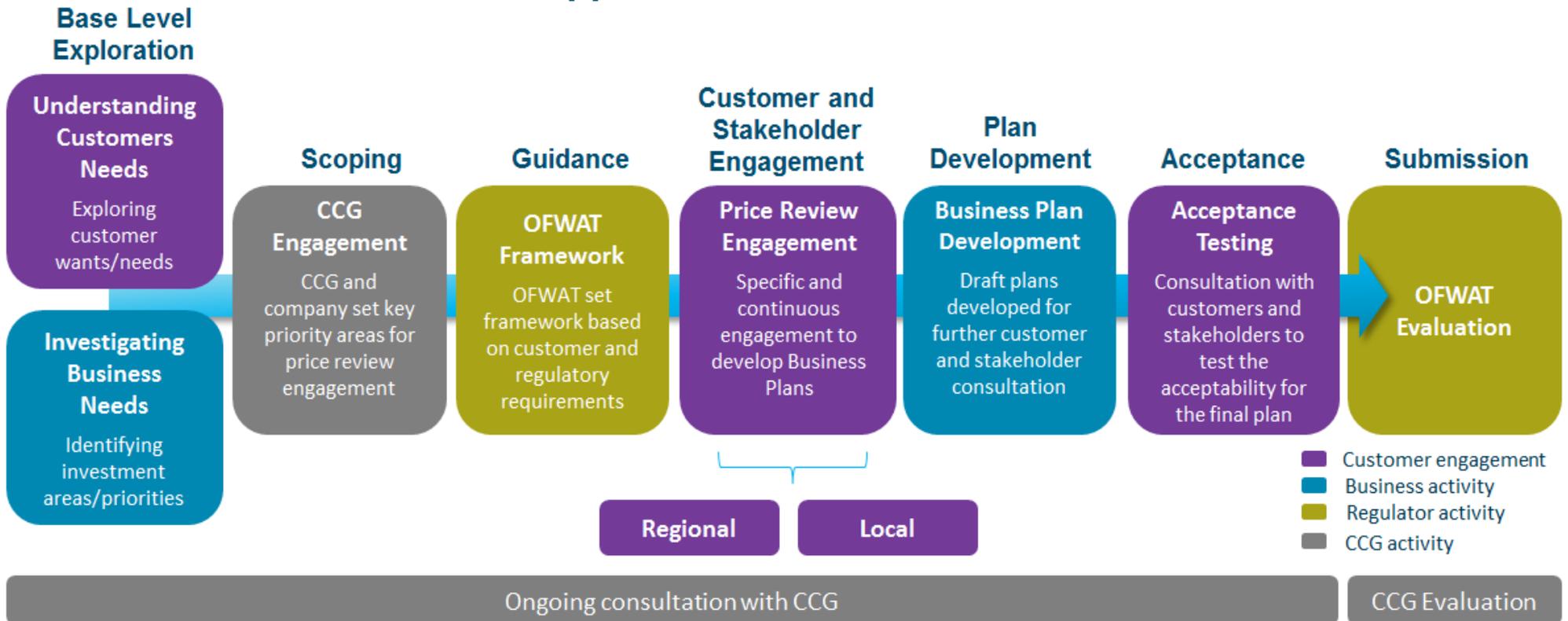
Coupled with continuous research is the specific activity industry undertakes to engage with customers and stakeholders to develop business plans. The process in PR14 was iterative and at times disjointed e.g. conducting Willingness to Pay prior to undertaking Outcomes research. Whilst the final outcome was supported and agreed by customers and stakeholders, the overall approach could have been seen as inefficient and at times unnecessarily time consuming.

The aspects of service which were tested throughout the Willingness to Pay (WtP) process were quite granular and cognitively challenging for customers (and stakeholders), therefore questioning the long-term validity of WtP. This was born from the UKWIR study which identified concerns about the reliability of the WtP methodology adopted by the industry. The review challenges the industry to develop a new approach to WtP that conveys choices in a way customers fully understand and can accurately value. The industry therefore needs to rethink at what level to engage its customers e.g. how to define services for PR19 moving beyond wholesale to, for example, water resources, water treatment, sludge etc.

Combined with the specific price review research, the insights drawn from the continuous engagement activity would provide further evidence (and confidence) that the business plans developed fully represent customer views. This would be further tested through final customer and stakeholder acceptability testing.

The diagram overleaf illustrates how engagement activity could support future price reviews as part of company 'business as usual' customer and stakeholder engagement. For CCG's the diagram highlights how they can influence further the future investment needs based on legitimate and robust customer and stakeholder engagement.

## Customer and Stakeholder Engagement to support the next Price Review



### *In Summary*

- Strong drivers for change exist in the water industry and it must consider introducing ways of engaging with its customers and stakeholders on a more regular basis to continually drive both physical and financial value
- To ensure the industry provides customers with services they truly value, the industry needs to adopt a continuous approach to understanding and evaluating customers attitudes and behaviours towards the established and long term challenges, as well as identifying whether companies need to define services beyond wholesale e.g. test the big issues over a longer period of time
- The regulatory one size fits all model appears to have a limited shelf life, industry must adapt to changing customers' needs and be willing to deliver against these, even at a local level
- CCGs must develop its industry knowledge and become strategic in its thinking in order to provide confidence to the regulator that they have robustly challenged and endorsed companies plans through effective consultation
- The regulator must adapt its approach from setting the price review agenda, to facilitating dialogue between the companies and CCGs, with a clear brief as to what it expects from the outset

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