

27 April 2018

James Veaney
Ofgem
9 Millbank
London
SW1P 3GE

Dear James

Response: RIIO-2 Framework Consultation – Workforce Resilience

Thank you for the opportunity to provide feedback into the Ofgem approach for the new RIIO-2 framework.

Our key consultation response points are immediately below, supported with appendices to provide supporting commentary on the RIIO-2 principles and a snapshot of the evidence for the labour market tensions being outlined. I would be pleased to meet with your team to discuss any aspects of this submission in more detail:

Workforce Resilience for the GB Energy sector

The RIIO-2 framework consultation currently makes no reference at all, to ensuring that the GB energy sector retains a resilient, skilled and sustainable workforce. Ofgem must address this critical resilience omission, to make explicit the value of skilled human capital in ensuring a reliable, safe and secure energy system delivering optimum value to customers.

The UK labour market is at its tightest point since records began in 1975, with the Office of National Statistics reporting record high employment; record low unemployment; EU nationals working in the UK down; EU nationals emigrating up; and the general costs of employment rising. We have been keeping the Ofgem CEO and Chief Engineer closely briefed on these UK trends through the dashboard '*tracking the labour market towards BREXIT*'. This is all in addition to the well-known and recorded workforce challenges already existing in gas and power.

With this tightening general labour market has come greatly increased UK-wide competition for the available talent. Currently, every major business sector in the UK is publicly reporting difficulty in accessing the skilled workers they need at a price they can afford. This is inevitably driving up

employment costs, forcing efficient and competitive businesses to aggressively protect their human capital.

The energy sector must be able to compete effectively and win the battle for talent if it is to deliver its strategies, achieve the desired productivity, affordability and secure the levels of innovation and customer service needed.

RIIO-2 must embed long-term resilience thinking ‘in the round’ for the whole regulated energy sector, to drive efficiencies and enable the attraction and retention of vital talent.

This principle of sustainability for the energy workforce applies to the critical regulated businesses, and also to the vital supply chain that operates significant parts of the energy system, and to ensuring maintenance of skilled energy policy makers, regulators and the other mission-critical stakeholders.

We see no current evidence that Ofgem can rely on other existing government policy frameworks to protect the sector’s efficiency, productivity, workforce resilience and sustainably. Specific resilience action is needed through the RIIO-2 framework.

Policy support and activity

There is currently no central guiding mind in the UK government that is thinking for the labour needs of the sectors of critical strategic value to the UK, or any form of coordinated workforce renewal and skills strategy for GB or the UK. Skills policy has been increasingly devolved to nations, local institutions and cities, and is primarily education based.

Utility employers’ experience of the devolved system has shown that the four nations’ policy makers are currently working in independent and often opposing directions, with no shared focus or joint ambitions to ensure that GB’s energy or wider utility sector is protected. Whilst the new Industrial Strategy initially offered thinking in the round and stated clearly the priorities of sustainable ‘infrastructure’ and ‘people’, the sector’s experience is that none of the proposed activity is targeted to enable, consider or deliver RIIO-2, and the solutions proposed are primarily focused in England.

As an example, the energy and utility sector has welcomed the strategic aim of the UK government’s apprenticeship levy to stimulate more talent into the labour market. Those companies committed from the inception to make the policy succeed, and were the first to secure Ministerial sign off of a Trailblazer apprenticeship, the first to graduate an apprenticeship and at the time of writing are delivering one in five of every apprentice graduated under the new English system.

However the workforce resilience needs and skills gaps faced by GB energy and utility employers are much broader, with the majority of their labour needs coming from upskilling, rather than apprenticeships. Simply put, the clear labour market challenges faced as we move to a post-European environment don't pause at the English borders, and workforce resilience and sector sustainability needs 'thinking in the round' which could never be addressed by English apprenticeships and technical education alone.

It is also critical to the success of the current GB energy delivery model that the main delivery partners and supply chain bodies are retained in the energy and utility sector, and have the confidence and financial sustainability they need not to seek to move to other markets. As highly competitive and multi-national businesses, that are operating many of the operational day-to-day aspects of energy infrastructure, they have no choice other than to work in the most sustainable and stable commercial environments.

We recommend that Ofgem and RIIO-2 explicitly take into account energy supply chain stakeholders' confidence in the market, and their sustainability, in the same way that Ofgem and RIIO-2 will do for investors.

Both are critical audiences that underpin and enable the very delivery model of energy at present. They are not obliged to operate in utility markets, and are at liberty to leave or adjust their risk premia, should other sectors or countries prove to offer lower risk, better returns or be more viable in the long-term.

Other sectors are indeed acting, and are formidable competitors for the available workforce and skills available. In transport in England, where significant and sustained infrastructure investment is already attracting away skilled workers from energy businesses and their vital supply chain, the Department for Transport centrally operates a Directorate for Infrastructure Skills that is mandated for its partners, and the Department has also brought about a Strategic Transport Apprenticeship Taskforce and collective strategy to maximise the sector's resilience. Energy has no such institutional strategic thinking, no central stewardship and no protection for its resilience. HS2, Crossrail2 and other major projects will impact energy workforce sustainability and costs.

Regulatory approaches

It is vital that RIIO-2 builds in the necessary resilience thinking and assurances to protect the sector. Ofgem has a duty to promote economy and efficiency, contribute to the achievement of sustainable development and makes clear its commitment to secure long term resilience in the energy sector. To secure change, we recommend that Ofgem consider available best practice from other comparable regulatory bodies.

We note the regular references in this consultation to the work of the water regulator Ofwat. Their final methodology for the PR19 price review (2020 to 2025) has enshrined workforce resilience as a major component of its approach to ‘resilience in the round’ and offers valuable precedent.

The Ofwat approach requires regulated company business plan submissions to consider the internal and extraneous challenges of the 5 year review period on their business, plus long-term projections for another ten years beyond”. The Ofwat PR19 Final Methodology advises that *“In order to be corporately resilient, companies must ensure that they have the capability within their workforce to provide the services their customers expect not only today but over the longer term, in the face of potentially significant changes in how they do this and in the wider employment landscape”....“Companies therefore need to ensure that they have the plans in place to secure access to the workforce they need, including transferring knowledge and increasing diversity”.*

We recommend that Ofgem reviews the Ofwat approach to ‘resilience in the round’ and adopts an equivalent approach for workforce resilience in RIIO-2. A copy of our policy analysis for the Ofwat Final Methodology is attached as an appendix to assist Ofgem.

In addition to securing the success of the next energy price review and settlement, it is important that RIIO-2 also looks to enable wider responsibilities, such as its part in helping UK government deliver the £0.5 trillion National Infrastructure Plan. The utility sector is currently the single biggest contributor to that plan, with energy forming a significant part.

That National Infrastructure Plan recognised from the outset that labour market conditions, and the availability of skilled labour, would be critical to its delivery and affordability.

Enshrining workforce resilience in RIIO-2 will provide direct policy read-across and productivity benefits to the National Infrastructure Plan.

Ofgem ultimately regulates companies that extensively operate in, draw from and drive significant investment through regional and national communities right across Great Britain.

The sustainability, resilience, capacity and capability of the GB energy workforce performs extensive social and environmental good for the country, and provides wide-ranging additional value for the whole UK. The employment and ‘whole-life’ career investments provided by the many companies that are covered by the scope of RIIO-2 positively impact huge numbers of businesses, families and individuals. The contribution made by energy supports UK government aims in public health, social mobility, diversity, taxation, social order and many more.

Embedding workforce resilience and sustainability in RIIO-2 directly supports Ofgem’s Social and Environmental Obligations. It provides Ofgem with robust evidence to demonstrate how it meets these obligations, when submitting its annual letter to the Secretary of State for Energy.

In terms of recognising the significant workforce resilience challenge being faced, Ofgem deserve great credit, and have been a valuable and important partner in the cross-utility work of the Energy & Utilities Skills Partnership as it seeks to tackle the main challenges of labour quantity, quality and transferability. Specifically, the pro-active and enthusiastic support of the Chief Executive, Chief Engineer and company Directors has been appreciated.

This knowledge and insight should now be transposed into the RIIO-2 price review process.

In RIIO-1, Ofgem primarily sought to protect existing skills and the required volumes of operational staff. The framework for RIIO-2 offers Ofgem and the regulated energy sector a chance to start to build a resilient, skilled and sustainable workforce, that will help ensure a reliable, safe and secure energy system delivering optimum value to its customers.

Ultimately, Great Britain cannot have a resilient or a sustainable energy sector without a skilled workforce. Unless you have the volume and quality of people needed to deliver the desired energy transition and then maintain robust levels of consumer trust and resilience, the point is arbitrary.

Yours sincerely



Nick Ellins
Chief Executive

Appendix 1: Areas of support for statements within the RIIO-2 Framework consultation

Energy & Utility Skills supports the Ofgem statements:

“Our overall aim is to ensure a regulatory framework that drives innovation, supports the transformation to a low carbon energy system **and delivers the sustainable, resilient, and affordable services** that all consumers need.”

“....the regulatory framework will need to evolve over time, and **we will need to respond to unforeseen challenges as they arise. A key part of our approach will be to build resilience and flexibility into the framework.** We will also continuously monitor developments, seeking to learn from what has worked (including from trials, where appropriate) and responding in an agile way to changes.”

- a) The RIIO model has worked well. The networks are more reliable and consumers appear highly satisfied with the service provided by local network operators.
- b) Deliver a sustainable energy network for existing and future consumers with a stable and predictable regulatory framework
- c) The energy system is in transition to a lower carbon, more decentralised, flexible, dynamic and responsive system, and the scale and pace of the change is causing traditional boundaries to break down between network and system operators and other market participants; even between consumers, producers and suppliers of energy
- d) The transition creates new possibilities, but it makes it even more challenging for Ofgem to deliver its commitments to resilience and sustainable development in forecasting longer-term outputs and the business environment around regulated energy companies
- e) All companies should be directed to act in a way that benefits the whole system, and not just their own network. To support this, the framework used to regulate the parties that operate

the system must be appropriate to their shifting roles and best incentivise them to deliver the required services

- f) Network companies should be directed to focus on the long-term when considering what outputs they should deliver and how they should deliver them. This reflects the challenge of delivering a sustainable energy sector, the long-lived nature of network assets, and the uncertainty of how to meet the needs of existing and future consumers
- g) Uncertainty surrounding network activity in the future, and even within the next 5-10 years, means it is extremely difficult to predict the allowances necessary for a range of different activities
- h) The energy transition will necessitate changes in how the system operates, how the network is developed, and how users interact with energy. It is also likely to shift where investment is needed on the network and, additionally, blur the boundaries between traditionally distinct sectors (eg transmission and distribution networks). Given we expect this transition to require significant network development and ongoing investment, it will be important to ensure that the energy system as a whole is effectively coordinated to deliver best value for consumers ('whole system outcomes')
- i) The current framework incentivises companies to focus on optimising their own network, but this may not lead to more fully optimised coordination
- j) Ofgem cannot be sure on the timing and extent of changes associated with the energy transition and a whole range of future scenarios could be plausible. Ofgem do need to take steps within RIIO-2 to help minimise the negative impacts on consumers of this demand uncertainty
- k) The world the energy sector operates in is changing rapidly. The scale, nature and complexity of new and emerging challenges will require careful planning and innovative responses to deliver the levels of resilience customers want and can afford now and in the long term
- l) Design RIIO-2 so that companies develop their networks to respond to the changes happening across the energy system.....Regulating to ensure resilience is about identifying and managing the risks to the delivery of the vital public services on which customers and society depend
- m) The energy system is evolving, especially with regard to the services and flexibility that network and non-network companies can provide and offer one another and the system. There are also major changes expected on the demand side, with increasing uptake of technologies such as electric vehicles and smart meters. The boundaries between transmission and distribution, network and non-network and even producers and consumers,

including beyond the consumers' meters, are blurring. Going forward, Ofgem need to ensure that the critical infrastructure and right regulatory framework is in place to facilitate this transition

- n) The framework should support companies in proactively managing and shaping the significant changes that are occurring across the energy system in the long-term interests of consumers

Appendix 2: About the Energy & Utility Skills Group

Energy & Utility Skills Group is the leading workforce resilience and skills body for the power, gas, water and waste management sectors. We work across the UK with governments, policy makers, economic, health & safety and quality regulators, unions, regulated businesses and their vital delivery and supply chain partners to bring about a resilient, skilled and sustainable workforce for the UK utility sector.

Our operations manage 1.1 million skills records for the UK utility sector, and currently deliver 20% of all apprentices graduated under the new UK Apprenticeship Levy.

We operate the Energy & Utilities Skills Partnership, a voluntary partnership of 29 utility-based Chief Executives and Managing Directors. The Partnership works closely with the key UK utility stakeholders and interest groups to secure the quantity, quality and transferability of workforce needed by the entire sector, in delivering the safe, secure, reliable and adaptable services demanded by consumers now and in the future.

This Partnership and its Workforce Renewal & Skills Strategy has been progressed in full cooperation and collaboration with Ofgem.

Dermot Nolan, Chief Executive, Ofgem

“The clean, reliable and affordable supply of energy is vital to customers and communities across the land. The development of a smarter, more flexible energy system and increasing use of smart technologies will transform the way our industry operates in the decades to come.

“Delivering this future vision will be very challenging, particularly as many skilled people in the energy industry will soon retire. Not only do they need replacing, but more advanced skills are required to deliver the technological changes that are central to the future of the industry.

“Success is dependent on attracting talented people into the sector from diverse backgrounds and developing the advanced skills that are needed. The Energy & Utilities Skills Partnership and their comprehensive workforce renewal and skills strategy offers a blueprint to achieve this challenging objective.”

Appendix 3: Labour market trends and issues

Tracking the UK Labour Market towards BREXIT

EU Nationals Seeking Work in the UK



EU nationals working in the UK down by **200,000***

EU nationals migrating to the UK down by **180,000***

EU nationals emigrating from the UK up by **24,000***

Unemployment Levels



Unemployment levels are the lowest since 1975 at **4.4%**

Less than **1%** of job seekers allowance claimants are pursuing work in the occupations of the UK's shortage lists (3000 of 514,000)

20,000 annual shortfall of engineering graduates (conservative estimate)

Employment Levels and Labour Costs



Highest level of employment since records began (1971) at **75.3%**

Hourly wage costs have increased by **1.4%*** (private sector)

Total weekly pay increased by **2.4%***

Graduate Market



University applications fell by **4%*** in the UK

Only **1%** of higher education leavers choose to work in the energy and utilities sector

All major UK business sectors reporting labour risks

UK firms from engineers to banks struggle to fill skills shortage



Business

Skills shortages at 'critical levels' risking UK growth, research claims



The Telegraph

By Anne Swan, ECONOMICS CORRESPONDENT

10 November 2016 - 12:00pm

News » UK » Skills shortages reach record high » continued 22 Jan 2016

Skills shortages reach record high

Employers are struggling to hire 'from cleaner to accountant' as Brexit skills shortage bites



LONDON - The number of suitable job candidates has fallen to its lowest level in 10 years, according to a new survey.

Brexit blamed as employers struggle to fill staff vacancies



Business

'Pervasive' skill shortages across UK economy to drive up wages

By Tim Wallace

9 January 2016 - 12:00pm

Appendix 4: UK Industrial Strategy and National Infrastructure Plan for Skills

Industrial Strategy



*".....it epitomises my belief in a strong and strategic state that intervenes decisively wherever it can make a difference. It is rooted in the conviction that a successful free-market economy must be built on firm foundations: **the skills of its workers, the quality of the infrastructure**, and a fair and predictable business environment. And where these are missing it takes energy and partnership between government and the private sector to address the problems."*

The Prime Minister



National Infrastructure Plan

The National Infrastructure Plan and its subsequent National Infrastructure Plan for Skills, recognised that utility-based infrastructure businesses are the single largest contributor to its half a trillion pound ambition.

Workforce resilience is recognised as an explicit threat to the productivity and cost ambitions of that plan.



"Investment in infrastructure is a vital element of improving the UK's productivity. With infrastructure output in the UK predicted to continue to grow, government and industry need to work together to ensure we have the right people with the right skills to deliver the ambitious pipeline of £411 billion of planned public and private investment to 2020 and beyond. This growth is happening in an increasingly competitive global infrastructure market."

POLICY BRIEFING:

2019 Price Review for the Water Industry in England & Wales

Resilience and Workforce Resilience



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Registered Office: Friars Gate, 1011 Stratford Road, Shirley, Solihull, B90 4BN

Registered no: 3812163

W: www.euskills.co.uk

T: 0845 077 99 22

E: communications@euskills.co.uk

A: Friars Gate, 1011 Stratford Road, Shirley, Solihull, B90 4BN

Policy Briefing: 2019 Price Review, Resilience and Workforce Resilience

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Introduction

Ofwat has duties to promote economy and efficiency, contribute to the achievement of sustainable development and secure long-term resilience. The economic regulator's strategy of 'Trust in Water' describes a shared vision for the water sector in England and Wales whereby customers and society have confidence and trust in the water and wastewater services provided in the UK. The next price review, known as PR19, deploys the Ofwat duties and seeks to address those priorities.



PR19 aims to empower and incentivise companies to address the future challenges facing the sector, including:

- Resilient companies and services
- Environmental challenges
- Customer expectations
- Affordability for all customers

It will set price controls for the period between 2020 and 2025, and has been developed following a full consultation, which took place in July 2017. The final methodology is underpinned by four key focusses: customer service, affordability, innovation and resilience.

Resilience in the round is about considering all aspects of resilience, including – operational, corporate and financial resilience. Resilience is not just about outcomes and expenditure. It means making sure the right people, leadership, infrastructure, systems and processes, are all in place and working effectively.

Ofwat PR19

This Policy Briefing focusses primarily on resilience, and specifically the new price control focus on ensuring the sector's workforce resilience within the approach to corporate and operational sustainability.

Resilience is a key focus of PR19. Ofwat has stated regularly and publicly over recent years that regulated water companies in England and Wales will be assessed on how well they have considered and planned for resilience, how well they have foreseen and mitigated risks and how they consider the holistic picture of resilience throughout their business.

Companies are expected to undertake longer-term thinking, providing long-term projections for at least ten years beyond the five-year price setting period. They are required to collaborate with stakeholders and other companies, employing innovation and taking a

wholesale view of their business in relation to the benefits of innovation and effective risk management to society and the economy.

The subject of workforce resilience is a new feature of the price control approach, featuring heavily in PR19. The economic regulator's views on the vital nature of human capital to company and sector's performance were set out well in advance, through their 'Resilience in the Round' document and the draft PR19 methodology. Quality regulators such as the Drinking Water Inspectorate have also been explicit in setting out their expectations for companies to have the workforce competence and behaviours necessary to protect public health and deliver a continuous supply of safe, wholesome drinking water.

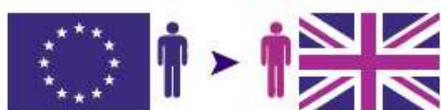
The general need for a resilient, skilled and sustainable workforce has increasingly been recognised by central and devolved governments, as a key challenge for all the main UK business sectors in a post European-exit economy. The UK government Industrial Strategy explicitly recognised 'people' as one of its five key pillars for action, but also the vital nature of 'infrastructure' as another pillar that is key to the future of the UK economy and society.

Market studies and data from the Office of National Statistics show clearly that labour availability in the UK is tightening, and the costs of general employment are steadily rising.

More detailed sector studies by the Energy & Utilities Skills Partnership and Energy & Utility Skills has made clear the impact of such risk on the utilities sector and also set out the vital role that delivery partners and the supply chain play in the overall sustainability of the main asset operators.

Labour Market Analysis Towards Brexit

EU Nationals Seeking Work in the UK



EU nationals migrating to the UK down by

47,000*

EU nationals emigrating from the UK up by

28,000*

Unemployment Levels



Unemployment levels are the lowest since 1975 at

4.2%

Less than **1%** people claiming Job Seeker's Allowance were seeking work in the energy-related occupations on the UK's Shortage Occupation List (545 of 475,000)

*Year on year figure.
For full list of sources [click here](#).

Employment Levels and Labour Costs



Highest level of employment since records began (1971) at

75.4%

Gross weekly full-time earnings have increased by

2.2%*

Graduate Market



University applications fell by **2%*** in the UK

Only **1%** of higher education leavers choose to work in the energy and utilities sector

The Details of the 2019 Price Control Process: Resilience

Resilience: What is it?

The 'Task and Finish Group' defined resilience as: the ability to cope with, and recover from, disruption, and anticipate trends and variability in order to maintain services for people and protect the natural environment, now and in the future.

Ofwat expects companies to prove that they have the necessary systems, processes and capability to deliver the services customers expect not only today, but in the long term.

Resilience is different from simply managing risk exposure. It requires a much broader range of options, often systems-based ones, which not only reduce risk, but enhance the ability to cope with, and recover from, pressures and shocks. This extends not only to service delivery but also to financial and workforce resilience, ensuring the right people and leadership is in place as well as the right systems, processes and infrastructure.

Companies must look at innovative ways to consider resilience in the long term. If the way services are delivered today affect or increase the risk to the service delivery in the future, the company is not securing long-term resilience.

Resilience in the Round

Ofwat has defined 'resilience in the round' as achieving strong operational, corporate and financial resilience and robust infrastructure. Each element of it reinforces overall resilience.

Within the definitions of achieving successful corporate and operational resilience, Ofwat sets out the need for a resilient and sustainable workforce.



In planning for effective resilience, water companies must consider their business as a whole, taking into account not only external factors, but also how different aspects relate to one another internally. This should now also explicitly consider their relationships with the vital suppliers in the context of resilience in the round. The component parts are:

Operational Resilience: focussing on the day-to-day operation of the business, water resource management, asset health and a total expenditure approach.

Corporate Resilience: focussing on the leadership teams and the processes and infrastructure in place in the company as well as transparency and company monitoring framework.

Financial Resilience: ensuring financial sustainability through innovation, monitoring and long-term financial viability statements.

The approach is underpinned by water companies ensuring that they have the right skills, the right people, the right leadership and the right systems. Workforce resilience is now a stated element of a sustainable and balanced business plan.

Workforce Resilience

Resilience is not just about expenditure and outcomes. It is also about making sure that companies have the right people, leadership, infrastructure, systems and processes in place and that all of these are working efficiently and effectively.

Ofwat is clear that human assets are in the spotlight for its approach to business plan assessments, and states that in order for a company to be corporately resilient, *“companies must ensure that they have the capability within their workforce to provide the services their customers expect not only today but over the long-term, in the face of potentially significant changes in how they do this and the wider employment landscape.”*



In order to be corporately resilient, companies must ensure that they have the capability within their workforce to provide the services their customers expect not only today but over the long term, in the face of potentially significant changes in how they do this and in the wider employment landscape. A focus on long-term resilience should therefore also include companies identifying and addressing possible skills gaps in the future. The Energy and Utilities Skills Partnership ‘workforce renewal and skills strategy’ (2017), which includes the water and wastewater sector, estimates that a third of vacancies are “hard to fill”. It also suggests that over 220,000 new recruits will be required by 2027. Companies therefore need to ensure that they have plans in place to secure access to the workforce they need, including transferring knowledge and increasing diversity.

Ofwat PR19

The Energy & Utilities Skills Partnership *Workforce Renewal and Skills Strategy* estimated that over 220,000 new recruits will be required in the whole utility sector by 2027.

Many of those labour needs are now common between water, gas, power and recycling utilities, creating useful synergies but also direct competition between the sectors for skilled workforce. In addition, and increasingly, the asset owners' chosen delivery partners and supply chain companies build and operate assets for multiple utility clients concurrently and work across infrastructure and wider disciplines. To achieve this, their workforce must be retained, dispersed and balanced across those industries and to meet the project timings required by their clients. Demand for the available skilled talent is therefore high and the cost of attracting and retaining human assets is identified by the Office of National Statistics as steadily rising.

Increasing competition for skilled talent is also now coming from other parts of the economy and specifically from non-water infrastructure businesses, such as energy generation, renewable energy, digital and a fast-growing rail sector that is expanding at record levels. Major projects such as HS2, Hinkley Point, Crossrail 2, expansions to southern airports, highways investment and the development of commercial infrastructure in Northern England, are all impacting the future resilience of the water industry workforce and challenging the ability of the water companies and their core delivery partners to retain the talent they need for meeting future service delivery. It is estimated that a third of skilled vacancies in the utility industry are now difficult to fill.

It is therefore important that water companies are thinking of 'resilience in the round' across their entire operational business, including their supply chain, and do not only consider the workforce they directly employ.

Under the final methodology, companies are required to focus on long-term resilience and demonstrate how they will ensure they have **the right quantity and quality of workforce**, with the right skills to meet their business and customer needs **for the price review period, plus long-term projections for at least ten years beyond**.

Ofwat is looking for regulated companies to show they have plans in place for securing access to the workforce they need in an increasingly competitive labour market, and can evidence how they will transfer knowledge and increase diversity within their workforce.

Business plans that deliver long-term resilience in the round should show how companies will make the best long-term decisions, on the basis of effectiveness and efficiency. Where collaboration with other water companies, stakeholders or partners can bring about a more efficient and effective outcome, this should be exploited.

Resilience and the Bigger Picture

In producing business plans that address long-term resilience risks, Ofwat expects companies to look outside their own geographical borders and have regard to the wider cost and benefit of their resilience to the industry, the economy and society as a whole.

Effective planning for resilience in the round will look for consideration of systems as a whole, taking into account the relationships between different segments of their business, as well as relevant external factors. This includes considering the resilience of the supply chain.

Companies (where able) should benchmark their performance against not only other water companies, but also against performance standards in other companies and industries.

How it will be assessed

Ofwat's outcomes framework, with its performance commitments and financial and reputational incentives encourages companies' management teams to identify and mitigate risks to operational resilience.

Ofwat will be assessing companies with the following two initial questions in mind:

1. How well has the company used the best available evidence, including engagement with its customers, to objectively assess and prioritise the diverse range of risks and consequences to its systems and services? Ofwat has clarified that 'risks' encompasses **all risks**.
2. How well has the company objectively assessed a comprehensive range of options to mitigate these risks? How well has the company selected the solutions that have support from its customers and also represent the best value for money for them?

Where investment is needed because of historical failures in a company's approach to resilience, Ofwat will consider whether these issues were as a result of evolving best practice or as a result of the company failing to do what they should have done. They also expect to see evidence that similar situations would be avoided in the future, whether these relate to processes, structure or governance.

Expectations for Business Plans

Ofwat expects business plans to be **based on cost efficiencies** that deliver value for money for its customers and secure trust and confidence, in accordance with Principle 5: Delivering best value solutions for customers.

operational resilience - the ability of an organisation's infrastructure, and the skills to run that infrastructure, to avoid, cope with and recover from disruption in its performance;

In order to be corporately resilient, companies must ensure that they have the capability within their workforce to provide the services their customers expect not only today but over the long term, in the face of potentially significant changes in how they do this and in the wider employment landscape.

Ofwat PR19

Companies are expected to challenge their business plans and ensure that customers are not paying for inefficient or ineffective performance, delivery or risk mitigation.

The business plans must deliver resilience in the round in the long term, and not just for the price review period. Resilience measures must be informed by a comprehensive assessment of the company's resilience: **not only the resilience of its systems, procedures and people but also of its customers' views about the management of resilience in harmony with their long-term interests.**

Ofwat expects to see ambitious business plans. An ambitious business plan is one that raises the standard across the industry and therefore benefits all customers. This could be by significantly reducing customer costs, or by managing risks in an exceptional way.

Companies' boards are expected to be accountable for business plan robustness: they must provide the assurance that the expenditure forecasts included in the business plans are both robust and efficient, and **companies are expected to benchmark their performance** both within the sector and against other sectors.

Ofwat will set cost baselines for companies with a forward-looking view of efficiency in mind. In setting these baselines, Ofwat will incorporate forecast productivity gains in the wider economic picture.

Ofwat expects to see a strong link between the mitigation and management of operational risks and a company's outcome performance commitments. The performance commitments should also reflect future risks, as well as customer preferences.

Applying Resilience in the Round

In line with Ofwat's assessment framework, resilience contributes heavily (along with security, high quality customer service, ambition and innovation) in their decision of how to categorise a company's plans.

- Companies are expected to consider risks in relation to operational, financial and corporate resilience
- Companies should consider whether (and how) resilience risks can be best managed across company boundaries as well as at a regional and possibly a national level
- Companies' appraisals should include a robust, comprehensive and qualitative assessment of the risks to the resilience and delivery of services to their customers both over the five-year period (2020-2025) and provide long-term projections for at least ten years beyond
- Companies must ensure they have the right infrastructure in place and the right skills in order to effectively run that infrastructure to avoid, cope with and recover from service and performance disruptions
- Companies must consider possible failure points across both the organisation **and the supply chain**, including:
 - The risks of failure occurring in each of the three areas (operational, financial and corporate)
 - The impact on customers if those risks occur
 - The extent to which those risks have already been mitigated
- **The appraisals should cover risks associated with infrastructure and assets as well as systems, processes and people** and require the company to look at the future challenges as a whole
- Companies should look past their own internal boundaries in addressing the challenges they face and should exploit opportunities to work alongside partners and other water companies.

Timeline of Action Needed

| | |
|---|-------------------|
| Companies must submit business plans to Ofwat | 3 September 2018 |
| Ofwat's initial assessment and categorisation of business plans | Late January 2019 |
| Early draft determinations | March/April 2019 |
| Other draft determinations | July 2019 |
| Final determinations | December 2019 |

Ofwat will run a queries process for specific questions around the methodology. Companies and stakeholders should email PR19@ofwat.gsi.gov.uk with queries for clarification, corrections or further explanation. Ofwat will publish widely relevant queries on their website for other stakeholders to access.

Working with Energy & Utility Skills

All of the UK water companies and many of the major delivery partners are members of the Energy & Utility Skills Group. We work across the UK with policy makers, economic, quality, environmental and health and safety regulators, regulated companies, delivery partners and the main sector unions.

Companies can be supported on workforce resilience through:

- A CEO level strategic skills forum to set direction on ensuring future workforce renewal and resilience – The Energy & Utilities Skills Partnership
- A Director level cross-sector Delivery Board, deploying initiatives to address the key workforce issues of quantity, quality and transferability
- A UK-wide and cross sector Apprenticeship Levy and Technical Education Advisory Group, bringing together utility sector employers to assist workforce sustainability through quality apprenticeships and to optimise recovery of their Apprenticeship Levy

- The sector's apprenticeship end-point assessment service – the Energy & Utilities Independent Assessment Service
- Strategic workforce planning services to help companies understand their labour market needs and develop plans for sustainability
- Mass talent and sector attraction initiatives, such as Talent Source Network
- Investment in training and productivity through procurement contract commitments – The Procurement Skills Accord
- Competence and capability schemes – health and safety awareness; public health; water hygiene; UK-wide water industry competency frameworks
- Development of National Occupational Standards and input to the latest UK-wide apprenticeship and technical education fora
- Networks sharing best practice on diversity and inclusion across UK utilities