



# **Service incentive mechanism (SIM) for 2015 onwards - a consultation**

## 1. Introduction

- 1.1 The Consumer Council for Water (CCWater) is the statutory consumer organisation representing water and sewerage consumers in England and Wales. CCWater has four regional committees in England and a committee for Wales.
- 1.2 We welcome the opportunity to respond to Ofwat's consultation on its proposal to change the service incentive mechanism (SIM) for 2015 onwards. We would first wish to acknowledge the improvements which SIM has helped to achieve since its implementation. The SIM has helped add weight to the pressure we are able to exert on companies to improve customer service through our handling of consumer complaints. The SIM's potential financial penalty of -1% and incentive of 0.5% has helped drive the right company behaviour.

## 2. Executive Summary

- 2.1 The SIM has helped improve customer service and supported our work in pressing companies to deliver better service. Written complaints and our investigations against companies on behalf of the consumer have reduced since their peak in 2007-08. The survey scores in the qualitative SIM show an improving trend with more customers satisfied with their contact with the company.
- 2.2 We welcome these improvements but have raised with Ofwat and stakeholders the following concerns about the SIM:
- companies have sometimes been reluctant to communicate with customers in case it attracts negative SIM points as a result of unwanted contacts;
  - some companies are still lagging behind the rest of the industry with high written complaint numbers and frequently poor performance on the qualitative survey, despite the potential penalty; and
  - inconsistencies in company interpretations of the SIM guidance bringing possible inaccuracy of the scores.
- 2.3 We would like to see the above issues resolved and the SIM build on the improvements it has helped to deliver. To address the above issues and ensure the SIM continues to deliver improving customer service, our preference for how the SIM should look is:
- a stronger SIM penalty (of up to -3% and incentive of 1%) to sufficiently incentivise the better performers and punish the poor performers. Failing this, ensure the full range of existing regulatory penalties and incentives are used;
  - the SIM penalty and incentive to be used for both retail and wholesale to ensure there are no gaps in service between each area and each element works together to resolve customer issues and improve service;
  - a higher weighting of 90% for the qualitative SIM survey to address the reluctance of companies to communicate with customers in case it attracts SIM points and the concerns about consistency of the quantitative contacts;
  - to ensure complaint handling is dealt with effectively by companies, the SIM survey to be extended to have an equal weighting of customers with complaints and enquiries;

- a smaller quantitative element of 10% based on complaints received by CCWater against companies, CCWater investigations and complaints which are upheld by the proposed alternative dispute resolution (ADR) provider, to encourage companies to resolve complaints effectively and not rely on CCWater to deal with their complaints;
  - CCWater to continue to collect written complaint information of business and domestic customers, which would show where companies stand on their service and help business customers make an informed choice on service when choosing a new retail provider.
- 2.4 The SIM will need to change in order to adapt to the UK Government’s proposal in the Water Bill for market reform. The SIM should incentivise through the value chain when the wholesale and retail elements of the industry are separated. There is a need to avoid gaps in customer service following this separation, especially with operational complaints. Using the SIM only for the customer facing retail elements of the business such as billing, meter reading and handling queries risks the wholesale areas of water supply and used water treatment falling behind in terms of customer service. Contractual negotiation between the retailers and wholesalers would not guarantee that the potential service gaps would be addressed.
- 2.5 The SIM should be applied to both the retail and wholesale elements of the value chain and the incentive and penalty applied to each. Customers should not be aware of any separation of retail and wholesale when they contact their company. In the event of problems, retail and wholesale should have a joined up approach to resolve customer issues. If customers are let down on service, then both retail and wholesale should take the hit.
- 2.6 We have pressed for an additional incentive and penalty outside the SIM based on the service and value for money experienced by all customers, and not just those who have contacted their company. This approach would encourage companies to communicate and engage more proactively with their customers, explaining what they do and how they are investing revenues.
- 2.7 CCWater’s views on areas of the SIM consultation not covered above are:
- continue with an asymmetric penalty and incentive as the better performing companies enjoy a reputational benefit and have lower administrative costs from dealing with fewer complaints;
  - unwanted contact information and written complaints information to still be collected but used as a reputational rather than financial penalty or incentive because of consistency concerns;
  - have the notice period for the survey data removed as companies are now sufficiently familiar with the collection and submission of the data;
  - continue to be based on relative rather than absolute performance, but companies must evidence improvement over the period before receiving a reward; and
  - businesses in Wales to be compared directly to business customers in England, through the comparable written complaint information provided by companies to CCWater and complaints against companies received by CCWater.

### 3. Business customers

CCWater will continue to collect written complaint information from incumbents and new entrants for our annual industry complaint report. Collecting this information will:

- highlight any issues developing from market reform;
- help business customers make an informed choice on whether to switch retail providers based on service levels;
- allow comparison with previous years in the water industry; and
- enable comparison with other industries, such as energy companies who publish their complaint numbers online every quarter.

It is important that any problems from market reform are captured and addressed. Competition in the energy sector brought problems with mis-selling disputes. Consumer Focus' 2012 research, 'Under the microscope - reviewing the micro business energy market,' highlighted some negative aspects for small business energy customers:

- high prices in some roll over offers which small businesses migrate to automatically when their contract expires;
- high out of contract prices when suppliers provide energy to customers without a negotiated contract (new businesses or where existing contracts have lapsed); and
- retailers blocking a customer from switching because of contractual terms, to the detriment of the customer.

If problems become evident after market reform, such as high complaint numbers about mis-selling, or other areas of customer concern then Ofwat should take the same approach as the energy industry and consider alternative penalties such as fining problem companies.

### 4. Incentivising frontier companies

**Q1 Should the SIM focus on incentivising innovation and out performance or bringing poor performers up to an acceptable level?**

For the SIM to be effective it must do both. Poorer performing companies must be sufficiently incentivised to improve or be penalised when they fail. Companies with better SIM scores should equally be encouraged to innovate further. The industry is still not where it should be on service and complaint handling as it is looking to introduce an alternative dispute resolution to deal with deadlocked complaints.

Customers should not lose out from their company being content to stand still and the water industry fall behind other sectors. Technological advances, such as website assistance, social media, text messaging and analytical software have all helped companies reduce unwanted contacts.

Whatever form the future SIM takes, it must continue to drive better service for customers. For the frontier companies to innovate and the poorer performers to improve, the SIM should:

- deliver a stronger penalty and incentive;
- have a strong reputational impact, which is not clear the SIM has currently delivered;
- sufficiently encourage companies to innovate.

Companies with a high proportion of complaints have committed to CCWater to improve and we look to the SIM to add weight to our pressure. It is not beyond a company to turn itself around, as we have seen from our work with United Utilities who showed a big improvement over the last three years with fewer complaints and higher SIM survey scores.

Future challenges for the industry mean continuing good performance should be incentivised. Over half of the written complaints to water companies are about billing, with more than half of those from customers who are charged by a meter. As the spread of metering increases, there is a potential for more complaints, especially as currently less than half household customers pay metered charges.

We have pressed for additional measures based on perceptions of value for money and service from a sample of the whole customer base. Including these measures would encourage companies to communicate proactively with customers, innovate further and identify good practice.

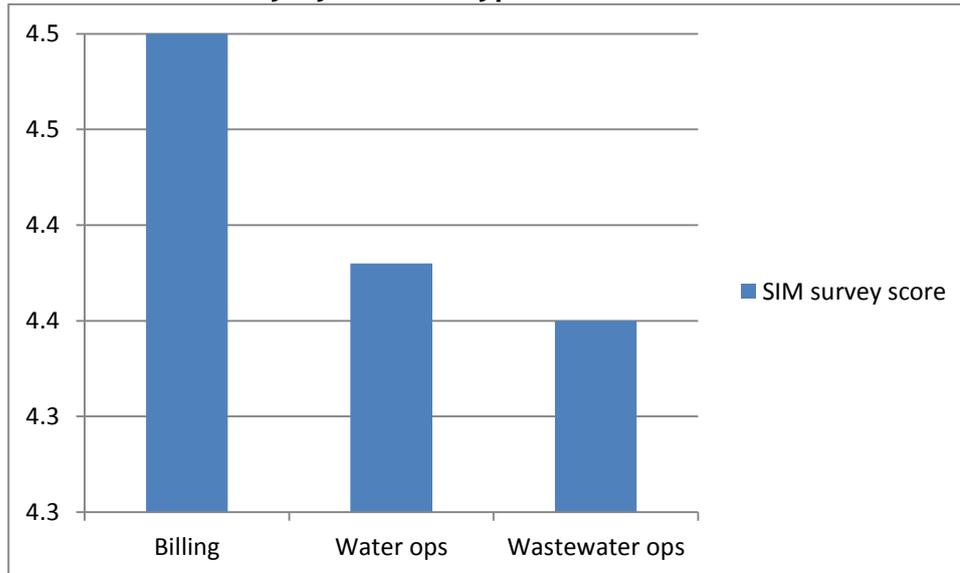
## **5. Incentivising companies across the value chain**

**Q2 Should the SIM be focussed upon customer-facing retail issues or continue to cut across the whole value chain?**

It would not be appropriate for the SIM to focus solely on the retail business. Retail and wholesale separation should be invisible to customers when they contact their company. Retail and wholesale should work together to resolve customer issues and improve service. The SIM penalties and incentives should be applied separately to retail and wholesale with both areas sharing the pain or reward. Contractual negotiations would not guarantee both sides of the business taking a joined up approach. We do not want a rift to develop between retail and wholesale, with one side blaming the other when things go wrong, or wholesale not adequately incentivised to deliver good service.

Some of the complaints CCWater receives against companies show poor communication between the call centre and operational staff. Examples include missed appointments, delays for site visits and the company call centre not being updated when a visit has taken place. We do not want to see these differences widen. Previous qualitative SIM surveys have shown customer satisfaction already differs between the customer facing retail element and the operational areas of business (see Chart 1).

**Chart 1 SIM survey by contact type 2012-13**



## **6. Symmetric or asymmetric incentive?**

The SIM incentive should remain asymmetric with the penalty carrying the greatest weight. Companies which perform well with lower written complaint numbers enjoy the following benefits:

- reputational, as in the past those companies which performed well released their own press notice with the poorer performers pledging to improve.
- reduced administrative costs from fewer negative or repeat contacts and complaints.

An equal incentive to penalty would risk customers perceiving the SIM negatively. Affordability remains a significant issue for many customers and an equally high reward could be unacceptable and even generate complaints. Companies should deliver good service as a matter of course and be rewarded a lower amount if they choose to go above and beyond what other companies offer.

## **7. Magnitude of financial incentive**

We have previously pushed for an increased penalty of -3% and incentive of 1% to better reflect a competitive market. Despite the existing penalty and incentive some companies are still behind the rest of the industry with high complaint numbers and poor SIM survey scores.

Companies that fail to provide adequate standards of service should be sufficiently penalised. Should Ofwat choose to continue with its preferred, existing level of -1% penalty and 0.5% incentive, then there should be something in place to impose fines on companies if their service falls to unacceptable levels. At the very least, the full range of regulatory penalty and incentive should be used for the current and future SIM performance.

Ofwat itself, in its rationale for ADR, has argued that companies need to overcome the perception amongst some customers that it is not worth complaining.

## **8. Balance of quantitative and qualitative elements**

We feel the interests of customers are best served by the qualitative survey having a 90% weighting in the SIM. This measure reflects consumer views directly and provides a strong insight into company performance. The survey also provides more detailed information about the consumer contact and provides companies with information on where they need to improve.

A stronger weighting for the survey would help resolve the following issues:

- some inconsistency of company reporting information;
- company reluctance to innovate or communicate with customers in case it might attract negative SIM points, an example was the company communication when they took ownership of private sewers; and
- the quantitative measures are not easy for consumers to understand, have not always been published on a comparative basis and have therefore had limited effect as a reputational incentive.

Companies have raised concerns to us about the consistency of reporting for the quantitative elements of the SIM. We want to see companies rewarded in the SIM for their service rather than their interpretation of the guidance.

## **9. Detailed design of the quantitative and qualitative measures**

Because of the issues about consistency and company reluctance to communicate with customers in case it attracts SIM points, we would like the SIM to consist of:

- a 90% weighting of the qualitative survey, extended to include an equal number of consumers who contacted with a complaint and enquiry;
- the notice period for the data submission for the survey to be removed;
- the remaining 10% of the SIM to consist of consumer complaints about their company received by CCWater, CCWater investigations and complaints upheld by the proposed ADR scheme.

The options in the consultation do not resolve the issues on consistency or some company reluctance to communicate to customers. A measure on the complaints we deal with against companies would mitigate the risk of some companies passing complainants to us when they are experiencing high volumes of contact or when they want an 'easy' way out of a complaint. An escalating score for CCWater investigations and complaints upheld by the proposed ADR provider would ensure companies are incentivised to resolve complaints earlier in their process.

An equal weighting between customers who contacted their company with a complaint and an enquiry in the SIM survey would capture complaint handling issues beyond the reporting of the total complaint numbers. This would also widen the range between the best and worst performers in the SIM survey and provide companies with better information on areas of customer service they need to improve.

We will still collect the written complaint data for our annual report which provides a strong reputational incentive for companies. We would also like companies to continue to collect unwanted telephone contact information as it provides a useful insight into industry performance and complements the written complaint information.

#### **10. Absolute or relative performance**

Our preference is for the SIM to be measured on relative performance, although companies should not be rewarded if their customer service has declined. The consultation mentions the difficulties in deciding what would be an acceptable level of absolute performance. Comparing performance on an absolute basis risks subjectivity and creating either too easy or too difficult a target for companies. Using historic levels as an absolute measure would not take into account technological changes, such as contacts through social media which is likely to grow further in the future.

#### **11. Non-household SIM design for Wales**

Written complaint information and complaints against companies to CCWater complaints would provide a comparison for business customers in Wales, and identify any problems. As business customers have different priorities to domestic households, comparison between the SIM scores for domestic customers would not fully reflect business customer needs. Using an absolute performance measure would bring the same difficulties as mentioned in our response at point 10 above.

### **Enquiries**

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