

August 2014

Setting price controls for 2015-20
Draft price control determination notice:
company-specific appendix – Anglian Water



OFWAT

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Overview

This appendix sets out the details of the draft determination of price controls that are specific to Anglian Water. Our draft determination is based on Anglian Water's business plan as submitted by 27 June and its responses to our subsequent queries.

The revisions that Anglian Water made to its business plan have many strengths. In particular, the company has provided very high quality evidence to support the special cost claims in its revised business plan for wholesale water and wastewater, many of which we are now able to accept. The difference between the company's view and our view is now smaller, but there is a remaining gap in relation to wholesale water costs. In addition, we are making a number of further interventions in Anglian Water's plan designed to safeguard customers' interests. Some of these interventions are around outcomes and the associated delivery incentives which are common to all companies.

It should be noted that in order for the price controls to protect the interests of consumers, we consider that – in accordance with their licence obligations – companies must act in an economic and efficient manner in all circumstances. For the avoidance of doubt, this obligation overrides any individual incentive element.

This draft determination sets out the draft allowed revenues and K factors for Anglian Water, along with what they mean for average customer bills. We have summarised this information in 'Draft determination for Anglian Water – at a glance'. The draft determination also sets out:

- the outcomes we expect the company to deliver under each price control;
- the costs we are assuming the company will incur and, where appropriate, the assumptions we have made to arrive at the allowed revenue for each price control;
- the adjustments we are making to the wholesale water and wastewater price controls to reflect the company's performance in 2010-15; and
- our assumptions on risk and reward, including the uncertainty mechanisms that form part of each price control.

As part of this price review, we stated in '[Setting price controls for 2015-20 – final methodology and expectations for companies' business plans](#)' (our 'final methodology statement') that we would be setting separate price controls for wholesale and retail elements of the appointee business. We explained that these separate controls would be binding, confirmed through the modifications made to the price setting elements of companies' licence conditions.

This means that the companies cannot recover more revenue than allowed under each specific price control. The revenue allowance for each price control is determined by the costs specific to that particular price control. This means that companies cannot cross-subsidise between controls in terms of costs or revenues, which gives important benefits for providing more effective incentives. It also supports the development of the relevant markets and in particular those provided for by the Water Act 2014.

We have made this draft determinations in accordance with our final methodology statement and our statutory duties. We have also had regard to relevant guidance from the UK Government, and where appropriate Welsh Government, and the principles of best regulatory practice to be transparent, accountable, proportionate, consistent and targeted.

This draft determination is structured on an element-by-element basis and is separated into:

- wholesale water;
- wholesale wastewater;
- household retail; and
- non-household retail.

In each area, we have set out the relevant information after our interventions – that is, our draft determination. In those areas in which we have intervened, we discuss the difference between our view and the company view further in the specific annexes where appropriate.

At the appointee level, this draft determination sets out our view of the company's financeability over the period 2015-20.

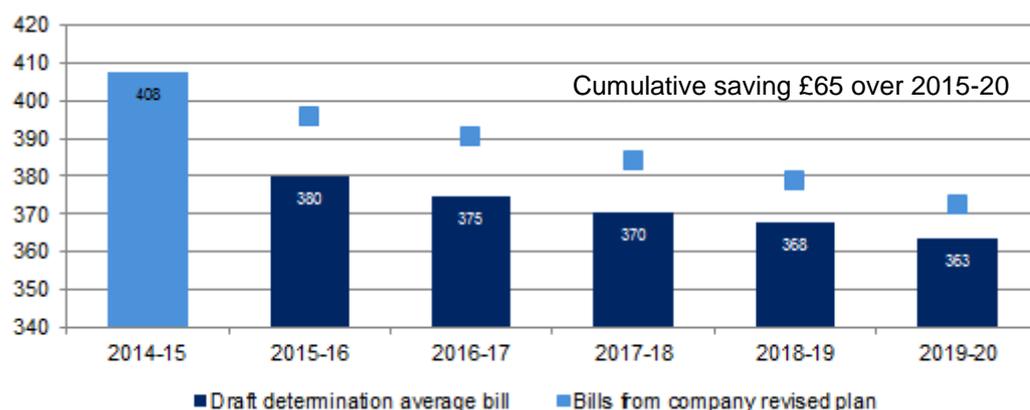
Annexes 1 to 4 form part of the draft price control determination.

A1. Draft determination for Anglian Water – at a glance

In this section we set out what the draft determination means:

- for customers, with respect to the average bills they will pay and the outcomes that the company will deliver in return; and
- for the company, with respect to the allowed costs/expenditure, return on regulatory equity (RoRE) range; financial ratios (under the notional structure) and the interventions we made to the company’s revised plan.

Combined average household bill (£)



Note:

The “Bills from company revised plan” is based on the data submitted by the company in its business plan but projected using our financial model, thereby ensuring consistency with the draft determination projection. As a consequence the company’s proposed bills illustrated above may not necessarily be the same as those described in the revised business plan.

Outcomes

Wholesale water	Wholesale wastewater
Satisfied customers	Satisfied customers
Fair charges	Fair charges
Resilient services	Flourishing environment
Supply meets demand	A smaller footprint
Flourishing environment	Caring for communities
A smaller footprint	Investing for tomorrow
Caring for communities	
Investing for tomorrow	
Safe, clean water	
Retail	
Satisfied customers	

Fair charges

A smaller footprint

Caring for communities

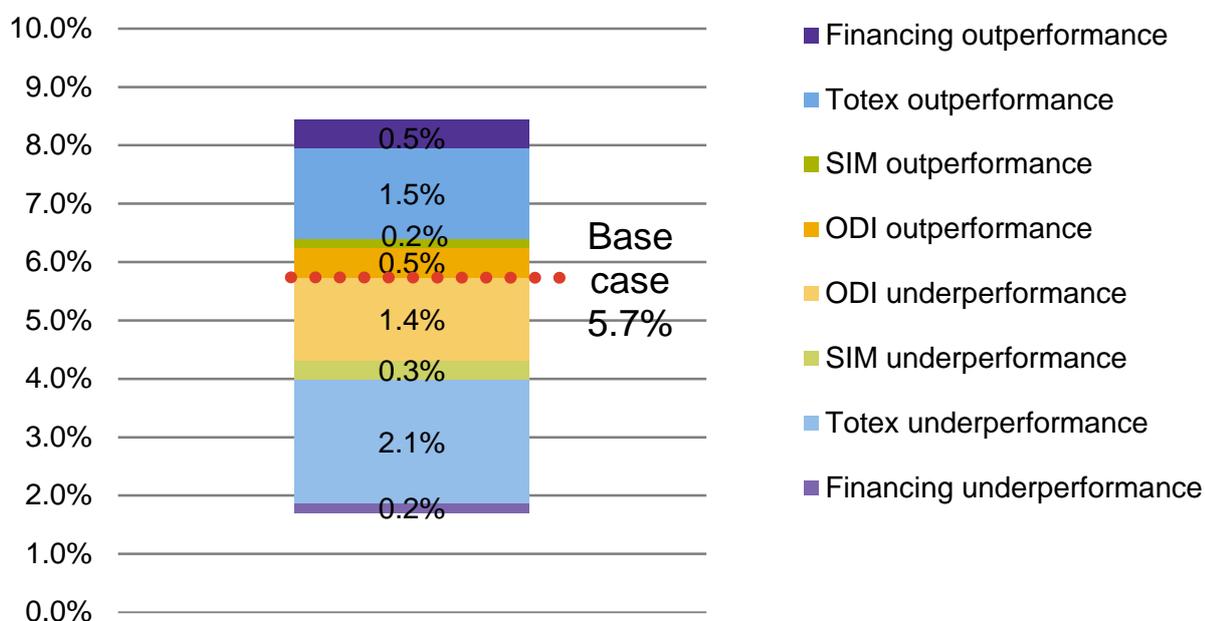
Allowed costs/expenditure¹

Wholesale	Water	Wastewater
Totex – 2015-20 total (£m)	1,669.4	2,490.6
Allowed weighted average cost of capital (%)	3.70%	3.70%
Allowed wholesale revenue in 2015-20 (£m)	2,079.5	3,062.5
Retail	Household	Non-household
Cost allowance – 2015-20 total (£m)	366.8	
Margin (%)	1.00%	2.5%
Retail allowed revenue (£m)	416.8	77.5
Average bill per household customer – retail component only (£)	33	

Note:

- Wholesale figures in 2012-13 prices and retail figures in nominal prices – this is consistent throughout this draft determination unless otherwise stated.

RoRE ranges – appointee



Ofwat's calculations of notional financeability ratios

Financial ratios for notional company	Ofwat calculation (average 2015-20)
Cash interest cover	2.84
Adjusted cash interest cover ratio (ACICR) – base case (average over five years)	1.46
Funds from operations/debt	8.66%
Retained cash flow/debt	6.04%
Gearing	62.26%
Dividend cover (profit after tax/dividends paid)	1.30
Regulatory equity/regulated earnings for the regulated company	17.67
RCV/EBITDA	11.17

Summary of interventions

<p>Outcomes</p> <ul style="list-style-type: none"> • Cap: We have imposed an overall cap and collar on outcome delivery incentives of +/- 2% of RoRE. • Horizontal check: We have improved performance commitments, deadbands, collars and caps to reflect upper quartile performance. Bottom-up analysis: We have applied conditions to rewards, corrected reward rates, adjusted penalty rates, ranges, deadbands and collars and introduced an intermediate PC level. • We are also requiring the company to add new performance commitments and outcome delivery incentives in relation to water quality contacts, pollution incidents and environmental compliance. • We have removed one performance commitment and associated outcome delivery incentive in relation to the qualitative service incentive mechanism (wholesale). 	<p>Wholesale costs</p> <ul style="list-style-type: none"> • The company proposed wholesale water totex of £1,773m in its plan which is £86m above our draft determination threshold of £1,687m. Its proposed wholesale wastewater totex of £2,518m was £36m below our threshold of £2,553m. • We have rejected some of the company's wholesale cost adjustments, or only partially allowed them. We also made some adjustments to reflect our modelling approach.
<p>Retail</p> <ul style="list-style-type: none"> • We have made minor adjustments to the company's price base of its costs. 	<p>Reconciling 2010-15 performance</p> <ul style="list-style-type: none"> • We have reduced the company's proposed revenue adjustments by £20m and a made a minor change to its proposed RCV adjustment.
<p>Risk and reward</p> <ul style="list-style-type: none"> • We have rejected uncertainty mechanisms proposed by the company for logging for the National Environment Programme and logging for household growth. 	<p>Financeability and affordability</p> <ul style="list-style-type: none"> • We have not intervened in this area.

A2. Wholesale water

A2.1 Company outcomes, performance commitments and delivery incentives

A2.1.1 Outcomes, performance commitments and incentives

In the [outcomes technical appendix](#), we discuss our approach to outcomes for the wholesale and retail controls.

We summarise the outcomes, performance commitments (PCs) and outcome delivery incentives (ODIs) for the wholesale water control for Anglian Water in Table A2.1 below.

We are intervening to impose an overall cap and collar on outcome delivery incentives for the 2015-20 period, thereby limiting total rewards and penalties. The maximum rewards for outperformance will be limited to +2% of RoRE and maximum penalties for underperformance are limited to -2% of RoRE. This will help ensure that the overall package of delivery incentives is calibrated to provide meaningful financial incentives and protect customers.

For some performance commitments and incentives types, we have intervened to change the underlying performance level or incentives. These interventions are listed in Table A2.1 below. Full detail of the wholesale water outcomes, performance commitments and incentives is provided in annex 4.

Table A2.1 Wholesale water outcomes, performance commitments and incentives

Company proposal			Intervention
Outcome	Performance commitment	Incentive type	
Satisfied customers	Qualitative Service Incentive Mechanism Score (wholesale water)	Financial – reward and penalty	Bottom-up analysis: Remove this PC and ODI. Company to add new water quality contacts PC and ODI which has upper quartile performance level.

Company proposal			Intervention
Outcome	Performance commitment	Incentive type	
	Water supply interruptions averaged over three years (reduction)	Financial – reward and penalty	<p>Horizontal check: Apply PCs, deadband, collar and cap for each year of 2015-20 and correct the reward rate.</p> <p>Bottom-up analysis: Correct the reward rate.</p>
	Properties at risk of persistent low pressure	Financial – reward and penalty	<p>Bottom-up analysis: Correct the reward rate calculation, apply an intermediate PC/ODI in 2017-18 and adjust the reward deadband.</p>
Fair charges	Value for money perception – variation from baseline against water and wastewater companies	Financial – reward and penalty	<p>Bottom-up analysis: Apply condition to reward so that the company does not earn a reward if its absolute score has gone down.</p>
Resilient services	Percentage of population supplied by single supply system	Financial – penalty only	No intervention.
	Frequency of level of service restrictions (hosepipe bans)	Reputational incentive	No intervention.
Supply meets demand	Security of Supply Index (SOSI) – dry year annual average	Reputational incentive	No intervention.
	Security of Supply Index (SOSI) – critical period (peak) demand	Reputational incentive	No intervention.

Company proposal			Intervention
Outcome	Performance commitment	Incentive type	
	Per Property Consumption (PPC) (litres/household/day reduction)	Financial – penalty only	No intervention.
	Leakage – three year average	Financial – reward and penalty	<p>Bottom-up analysis: Adjust the penalty rate to match the company's December business plan proposal.</p> <p>(Note: the company adjusted its approach to leakage between its December and revised business plan. It removed the totex associated with its planned reduction in leakage and proposed to deliver lower leakage via its ODI reward, which we have accepted).</p>
Flourishing environment	Percentage of SSSIs (by area) with favourable status (wholesale)	Reputational incentive	No intervention.
A smaller footprint	Operational carbon (percentage reduction from 2015 baseline in real terms) (whole business)	Reputational incentive	No intervention.
	Embodied carbon (percentage reduction from 2010 baseline) (whole business)	Reputational incentive	No intervention.

Company proposal			Intervention
Outcome	Performance commitment	Incentive type	
Caring for communities	Survey of community perception	Reputational incentive	No intervention.
Investing for tomorrow	Water infrastructure	Financial – penalty only	No intervention.
	Water non-infrastructure	Financial – penalty only	No intervention.
Safe, clean water	Mean Zonal Compliance	Financial – penalty only	Horizontal check: Adjust PC level for 2017-18, 2018-19 and 2019-20 and change penalty deadband, collar and rate.
			Bottom-up analysis: Company to add new PC and ODI for environmental compliance.

A2.1.2 Outcome delivery and reporting

In the [assurance technical appendix](#), we set out our proposed framework for the form and level of reporting, monitoring and assurance we will seek from companies during the five year regulatory period 2015-20 in relation to the delivery of their commitments for the price review. This sets out three levels of assurance and the opportunities available for a company to improve its category status through the finalisation of the price controls and during the regulatory period itself.

We are satisfied with the company's proposals for self-reporting. But consistent with the commentary in our assurance technical annex, we will need to consider the categorisation of the company for assurance purposes at the final determination.

Anglian Water's proposed approach to the measurement, reporting and governance of outcomes and our assessment of this approach is summarised in annex 4.

A2.2 Calculating the wholesale water price control

A2.2.1 Calculating allowed wholesale water expenditure

Our approach to calculating allowed wholesale expenditure is set out in the [wholesale water and wastewater technical appendix](#).

In Anglian Water's revised plan the company proposed wholesale water totex of £1,773 million over 2015-2020 (compared to £1,840 million in its December plan). We calculated the draft determination cost threshold at £1,687 million, giving rise to a difference of £86 million or 5.1%. The interventions in the company's plan for wholesale costs are set out in annex 1. We also note that the company made representations to our cost models following the publication of these in April. The representations made and our response is summarised in [wholesale water and wastewater technical appendix](#).

It is also important to bear in mind that the actual gap faced by the company is smaller than what would be implied when looking at the totex gap. This is because the use of menus and our approach to setting baselines reduces the difference faced by the company. In particular, the difference between the company's plan and the amount that it would ultimately recover from customers is only 2.7%.

The proposed wholesale water allowed expenditure for Anglian Water is detailed in Table A2.2 below. We provide a further breakdown of some of the calculations in annex 1. Further information about our assessment of each claim is set out in the [populated version of draft determination initial cost threshold models](#).

Table A2.2 Wholesale water allowed expenditure (£ million)

	2015-16	2016-17	2017-18	2018-19	2019-20	Total 2015-20
Draft determination cost threshold						1,687.1
Costs excluded from menu						47.6
Menu cost baseline ¹	338.3	387.3	332.2	295.3	286.5	1,639.6
Company's view of menu costs ²						1,718.7
Implied menu choice						104.8

	2015-16	2016-17	2017-18	2018-19	2019-20	Total 2015-20
Allowed expenditure from menu	342.4	392.0	336.2	298.8	290.0	1,659.4
Costs excluded from menu	9.6	9.5	9.5	9.5	9.5	47.6
Total allowed expenditure ³	352.0	401.5	345.7	308.3	299.5	1,706.9
Less pension deficit repair allowance	7.5	7.5	7.5	7.5	7.5	37.5
Totex for input to PAYG	344.5	394.0	338.2	300.8	291.9	1,669.4

Notes:

1. Menu baseline is equal to the draft determination threshold less pension deficit recovery costs, third party costs and market opening costs related to 2014-15 (see annex 1 for these costs and the derivation of the draft determination threshold).
2. Based on company plan totex minus costs for items excluded from the menu.
3. Includes pension deficit repair allowance.

A2.2.2 Calculation of revenues: pay as you go (PAYG) and regulatory capital value (RCV)-run off

Table A2.3 shows the company's proposed PAYG ratios and associated totex recovery for wholesale water, which we have used as the basis for this draft determination.

Table A2.3 Anglian Water wholesale water PAYG ratios

	2015-16	2016-17	2017-18	2018-19	2019-20	Total
Totex (£m)	344.5	394.0	338.2	300.8	291.9	1,669.4
PAYG %	59.2%	51.2%	58.3%	65.6%	67.3%	60.3%
Resulting PAYG (£m)	203.9	201.9	197.0	197.5	196.4	996.6

Table A2.4 shows the RCV run-off amounts included within the wholesale water charge. This reflects a run-off rate of 3.95% for the RCV as at 31 March 2015 and 26 years for the totex additions to the RCV over 2015-20.

Table A2.4 Anglian Water wholesale water RCV run-off (£ million)

	2015-16	2016-17	2017-18	2018-19	2019-20	Total
Run-off of 2015 RCV	97.0	93.2	89.5	86.0	82.6	448.3
RCV run-off of totex additions	2.7	9.2	15.7	20.5	24.4	72.6
Total RCV run-off	99.8	102.4	105.2	106.5	107.0	520.9

A2.2.3 Return on the RCV

Our risk and reward guidance set out a single industry cost of capital for both wholesale water and wastewater services of 3.7%. The company has accepted this guidance and so we have used a cost of capital of 3.7% in this draft determination. This results in a return on capital of £475.4 million over 2015-20.

Table A2.5 shows our calculation of the opening RCV at 1 April 2015 taking account of the adjustments for 2010-15 performance discussed in section A2.2.4 below. The average RCV, set out in Table A2.6 for each year, takes into account the proportion of totex additions to the RCV determined by the PAYG ratio and RCV run-off.

Table A2.5 Anglian Water wholesale water opening RCV (£ million)

	2015-16
Closing RCV 31 March 2015	2,583.5
Land sales	-0.8
Adjustment for actual expenditure 2009-10	-5.1
Adjustment for actual expenditure 2010-15 ¹	-127.3
Net adjustment from logging up, logging down and shortfalls	-13.5
Other adjustments ²	19.6
Opening RCV 1 April 2015	2,456.3

Notes:

1. The adjustment for actual expenditure 2010-15 is explained further in annex 3 as part of the capital expenditure incentive scheme (CIS) adjustment.
2. The amount included in 'other adjustments' relates to the agreed correction in relation to Wing following the determination on developer contributions. See table AA3.17.
3. We have applied all of the CIS adjustment to the RCV at 1 April 2015. This is in line with our approach to all companies but differs to the approach used by the company.

Table A2.6 Anglian Water wholesale water return on RCV (£ million)

	2015-16	2016-17	2017-18	2018-19	2019-20
Opening RCV	2456.3	2497.1	2586.8	2622.8	2619.6
RCV additions (from totex)	140.6	192.1	141.2	103.3	95.6
Less RCV run-off	99.8	102.4	105.2	106.5	107.0
Closing RCV	2497.1	2586.8	2622.8	2619.6	2608.3
Average RCV (year average)	2476.7	2542.0	2604.8	2621.2	2613.9
Return on capital	91.6	94.0	96.3	96.9	96.7

A2.2.4 Reconciling 2010-15 performance

Our approach to reconciling 2010-15 performance is set out in the [wholesale water and wastewater technical appendix](#). The company proposed adjustments to the opening RCV and allowed revenue for the wholesale water services to reconcile performance in 2010-15. We have intervened and as a result the revenue adjustments for wholesale water have changed from £12.1 million to £3.2 million. We summarise these interventions in Table A2.7 below, and quantify the resulting adjustments within this draft determination. The impact on the opening RCV of 2010-15 adjustments is shown in Table A2.5 above. As noted in the table, we have applied -£13.5 million in (net) adjustments arising from logging up, logging down and shortfalls. It should be noted that the company proposed a logging down adjustment of -£13.2 million, however we have made a minor intervention to correct a calculation error. Further information on our interventions and rationale is set out in annex 3.

Table A2.7 Anglian Water wholesale water revenue adjustments to reflect 2010-15 performance (£ million)

Area	Intervention	Why we did it	Total 2010-15
Service incentive mechanism (SIM)	There are no interventions in this area.	n/a	7.2
Revenue correction mechanism (RCM)	We have intervened in the following areas. <ul style="list-style-type: none"> • FD09 assumptions. • Measured non-household revenues. 	We disagree with the company assumptions on the FD09 input variables for the RCM model.	-4.6

Area	Intervention	Why we did it	Total 2010-15
Opex incentive allowance (OIA)	There are no interventions in this area.	n/a	4.4
Capital expenditure incentive scheme (CIS)	In carrying out our assessment, we have: <ul style="list-style-type: none"> used the PR09 vanilla cost of capital when calculating the financing costs; used the PR09 pre-tax cost of capital when calculating the future value of the revenue adjustment; and included our view of the applicable change protocol amounts. 	The company has made tax adjustments to the PR09 cost of capital based financing and discount rates. We disagree with this approach and have applied Ofwat's published methodology.	-3.8
Other adjustments	There are no other adjustments in this area.	n/a	0.0
Total	n/a	n/a	3.2

A2.2.5 Calculation of allowed revenue

We set out the calculation of the allowed revenue for Anglian Water's wholesale water control in Table A2.8.

Overall, we consider that the company's wholesale water revenue allowance should be £415.5 million in 2015-16, increasing by 0.2% to £416.5 million in 2019-20.

Table A2.8 Anglian Water wholesale water allowed revenue (£ million)

	2015-16	2016-17	2017-18	2018-19	2019-20	Total
Totex	344.5	394.0	338.2	300.8	291.9	1669.4
PAYG ratio	59.19%	51.24%	58.25%	65.65%	67.26%	-
Totex additions to the RCV	140.6	192.1	141.2	103.3	95.6	672.8
RCV (year average)	2476.7	2542.0	2604.8	2621.2	2613.9	-
Wholesale allowed revenue build up:						
PAYG ¹	211.4	209.4	204.5	205.0	203.9	1034.1
Return on capital	91.6	94.0	96.3	96.9	96.7	475.4
RCV run-off	99.8	102.4	105.2	106.5	107.0	520.9
Tax ²	5.4	2.7	1.0	2.0	0.6	11.8
Income from other sources	-8.0	-8.1	-8.1	-8.1	-8.1	-40.4
Reconciling 2010-15 performance	2.2	0.8	0.8	-0.3	-0.3	3.2
Ex ante additional menu income	-2.1	-2.4	-2.0	-1.8	-1.8	-10.1
Capital contributions from connection charges and revenue from infrastructure charges	15.3	16.0	16.9	17.8	18.6	84.5
Final allowed revenues	415.5	414.9	414.7	417.9	416.5	2079.5

Notes:

1. PAYG includes the PAYG calculated from totex and the pension deficit repair allowance.
2. Including tax on adjustments for reconciling 2010-15 performance and ex-ante additional menu income.

A2.3 Uncertainty mechanisms

We outline our approach to uncertainty mechanisms in the [risk and reward technical appendix](#). In Table A2.9 below, we set out Anglian Water’s proposed wholesale water uncertainty mechanisms and our assessment of these proposals.

Table A2.9 Anglian Water proposals for wholesale water uncertainty mechanisms

Anglian Water proposals	Our assessment
<p>Anglian Water proposed an uncertainty mechanism for water business rates with a sharing rate of 75% customer and 25% company.</p>	<p>We consider that the materiality, comparability and control over risk criteria for water business rates are met. We have included a 75%:25% uncertainty mechanism for all companies consistent with our prior guidance and earlier draft determinations. The specific text of this Notified Item and the rationale for its inclusion in the draft determination is set out in the risk and reward technical appendix.</p>
<p>Anglian Water proposed an uncertainty mechanism to allow for logging for growth in numbers of households.</p>	<p>This uncertainty mechanism is excluded in our draft determinations. Household growth was included as a risk scenario in the original methodology statement and forms part of the risk range set out in our risk and reward guidance. The issue that companies do not receive additional revenue to respond to growth in numbers of households was considered in our consultation on the methodology and it was decided not to incorporate a risk mechanism to deal with it. In addition we do not consider that the uncertainty mechanism is consistent with our criteria for uncertainty mechanisms:</p> <p>Materiality – Pass. The downside scenarios presented by Anglian Water covering water and wastewater represent a combined variance of 1% of wholesale totex over the whole of 2015-20 and so we consider that the risk is material.</p> <p>Controllability – Fail. Anglian Water states that household growth patterns are highly sensitive to economic trends and forecasts of</p>

Anglian Water proposals	Our assessment
	<p>growth by all parties have proved to be inaccurate as evidenced by the substantial logging adjustments made in PR09 and PR14. While Anglian Water does not have control over household growth it does have control over the scale of costs incurred.</p> <p>Comparability with other companies – Fail. This risk is well understood and common to all companies. Anglian Water has not provided adequate justification to demonstrate why it requires specific protection from these risks when other companies do not.</p> <p>Customer protection – Fail. We consider that it would be inappropriate for Anglian Water customers to bear 100% of this risk when customers of all other companies bear only a portion of the risk with their respective companies through the totex menu.</p>

A3. Wholesale wastewater

A3.1 Outcomes, performance commitments and incentives

In the [outcomes technical appendix](#), we discuss our approach to outcomes for the wholesale and retail controls.

We summarise the outcomes, performance commitments and outcome delivery incentives for the wholesale wastewater control for Anglian Water in Table A3.1 below.

Similar to the wholesale water control, we are intervening to impose an overall cap and collar on outcome delivery incentives for the 2015-20 period, thereby limiting total rewards and penalties. The maximum rewards for outperformance will be limited to +2% of RoRE and maximum penalties for underperformance are limited to -2% of RoRE. This will help ensure that the overall package of delivery incentives is calibrated to provide meaningful financial incentives and protect customers.

In addition, for some performance commitments and incentives types we have intervened to change the underlying performance level or incentives. These interventions are listed in Table A3.1 below. Full detail of the wholesale wastewater outcomes, performance commitments and incentives is provided in annex 4.

Table A3.1 Wholesale wastewater outcomes, performance commitments and incentives

Company proposal			Interventions
Outcome	Performance commitment	Incentive type	
Satisfied customers	Qualitative Service Incentive Mechanism Score (wholesale wastewater)	Financial – reward and penalty	Bottom-up analysis: Remove this PC and ODI.
	Properties flooded internally from sewers – averaged over three years (reduction)	Financial – penalty only	Bottom-up analysis: Increase the penalty range. We are open to the company proposing a reward on this PC.

Company proposal			Interventions
Outcome	Performance commitment	Incentive type	
	Properties flooded externally from sewers – averaged over 3 years (reduction)	Financial – penalty only	Bottom-up analysis: Increase the penalty range.
	Percentage of sewerage capacity schemes incorporating sustainable solutions eg sustainable urban drainage solutions (SuDS)	Reputational incentive	No intervention.
Fair charges	Value for money perception – variation from baseline against water and wastewater companies	Financial – reward and penalty	Bottom-up analysis: Apply condition to reward so that the company does not earn a reward if its absolute score has gone down.
Flourishing environment	Percentage of bathing waters attaining excellent status	Financial – reward and penalty	No intervention.
	Percentage of SSSIs (by area) with favourable status	Reputational incentive	No intervention.
A smaller footprint	Operational carbon (percentage reduction from 2015 baseline in real terms) (whole business)	Reputational incentive	No intervention.

Company proposal			Interventions
Outcome	Performance commitment	Incentive type	
	Embodied carbon (percentage reduction from 2010 baseline) (whole business)	Reputational incentive	No intervention.
Caring for communities	Survey of community perception	Reputational incentive	No intervention.
Investing for tomorrow	Sewerage infrastructure	Financial – penalty only	No intervention.
	Sewerage non-infrastructure	Financial – penalty only	No intervention.
			Horizontal check: Company to add new PC and ODI for pollution incidents.
			Bottom-up analysis: Company to add new PC and ODI for environmental compliance.

A3.1.1 Outcome delivery and reporting

In the [assurance technical appendix](#), we set out our proposed framework for the form and level of reporting, monitoring and assurance we will seek from companies during the five year regulatory period 2015-20 in relation to the delivery of their commitments for the price review. This sets out three levels of assurance and the opportunities available for a company to improve its category status through the finalisation of the price controls and during the regulatory period itself.

We are satisfied with the company's proposals for self-reporting. But consistent with the commentary in our assurance technical annex, we will need to consider the categorisation of the company for assurance purposes at the final determination.

Anglian Water's proposed approach to the measurement, reporting and governance

of outcomes and our assessment of this approach is summarised in annex 4.

A3.2 Calculating the wholesale wastewater price control

A3.2.1 Calculating allowed wholesale wastewater expenditure

Our approach to calculating allowed wholesale expenditure is set out in the wholesale water and wastewater technical appendix.

In Anglian Water's revised plan the company proposed wholesale wastewater totex of £2,518 million over 2015-2020 (compared to £2,525 million in its December plan). We calculated the draft determination cost threshold at £2,553 million, which is £36 million or 1.4% below our threshold. This included making adjustments for the National Environment Programme Phase 5. The interventions in the company's plan for wholesale costs are set out in annex 1.

The proposed wholesale wastewater allowed expenditure for Anglian Water is detailed in Table A3.2 below. A further breakdown of some of the calculations is provided in annex 1. Further information about our assessment of each claim is set out in the [populated version of draft determination initial cost threshold models](#).

Table A3.2 Wholesale wastewater allowed expenditure (£ million)

	2015-16	2016-17	2017-18	2018-19	2019-20	Total
Draft determination cost threshold						2,553.2
Costs excluded from menu						57.4
Menu cost baseline ¹	436.5	557.5	493.4	506.9	501.5	2495.7
Company's view of menu costs ²						2462.6
Implied menu choice						98.7
Allowed expenditure from menu	435.0	555.7	491.7	505.2	499.8	2487.4
Costs excluded from menu	11.6	11.4	11.4	11.5	11.5	57.4
Total allowed	446.7	567.1	503.2	516.7	511.3	2544.9

	2015-16	2016-17	2017-18	2018-19	2019-20	Total
expenditure³						
Less pension deficit repair allowance	10.9	10.9	10.9	10.9	10.9	54.3
Totex for input to PAYG	435.8	556.2	492.3	505.8	500.4	2490.6

Notes:

1. Menu baseline is equal to the draft determination threshold less pension deficit recovery costs, third party costs and market opening costs related to 2014-15 (see annex 1 for these costs and the derivation of the draft determination threshold).
2. Based on company plan totex minus costs for items excluded from the menu.
3. Includes pension deficit repair allowance.

A3.2.2 Calculation of revenues: PAYG and RCV-run off

Table A3.3 shows the company's proposed PAYG ratios and associated totex recovery for wholesale wastewater, which we have used as the basis for this draft determination.

Table A3.3 Anglian Water wholesale wastewater PAYG ratios

	2015-16	2016-17	2017-18	2018-19	2019-20	Total
Totex (£m)	435.8	556.2	492.3	505.8	500.4	2490.6
PAYG %	67.8%	51.5%	56.4%	53.5%	52.5%	56.3%
Resulting PAYG (£m)	295.7	286.5	277.5	270.6	262.7	1392.9

Table A3.4 shows the RCV run-off amounts included within the wholesale wastewater charge. This reflects a run-off rate of 3.85% for the RCV as it stands on 31 March 2015 and 26 years for the totex additions to the RCV over 2015-20.

Table A3.4 Anglian Water wholesale wastewater RCV run-off (£ million)

	2015-16	2016-17	2017-18	2018-19	2019-20	Total
Run-off of 2015 RCV	153.7	147.7	142.1	136.6	131.3	711.4
RCV run-off of totex additions	2.7	10.4	19.7	28.2	37.2	98.2
Total RCV run-off	156.3	158.2	161.7	164.8	168.5	809.5

A3.2.3 Return on the RCV

As discussed in section A2.2.3, the company has accepted our risk and reward guidance and so we have used a cost of capital of 3.7% in this draft determination. This results in a return on capital of £759.7 million over 2015-20.

Table A3.5 shows our calculation of the opening RCV at 1 April 2015 taking account of the adjustments for 2010-15 performance discussed in section A3.2.4 below. The average RCV, set out in Table A3.6 below for each year, takes into account the proportion of totex additions to the RCV determined by the PAYG ratio and RCV run-off.

Table A3.5 Anglian Water wholesale wastewater opening RCV (£ million)

	2015-16
Closing RCV 31 March 2015	4185.3
Land sales	-1.4
Adjustment for actual expenditure 2009-10	0.5
Adjustment for actual expenditure 2010-2015	-182.1
Net adjustment from logging up, logging down and shortfalls	-11.2
Other adjustments	0.0
Opening RCV 1 April 2015	3991.2

Note:

We have applied all of the CIS adjustment to the RCV at 1 April 2015. This is in line with our approach to all companies but differs to the approach used by the company.

Table A3.6 Anglian Water wholesale wastewater return on RCV (£ million)

	2015-16	2016-17	2017-18	2018-19	2019-20
Opening RCV	3991.2	3975.0	4086.5	4139.6	4210.1
RCV additions (from totex)	140.1	269.7	214.8	235.3	237.8
Less RCV run-off	156.3	158.2	161.7	164.8	168.5
Closing RCV	3975.0	4086.5	4139.6	4210.1	4279.3
Average RCV (year average)	3983.1	4030.8	4113.1	4174.9	4244.7
Return on capital	147.3	149.0	152.1	154.4	156.9

A3.2.4 Reconciling 2010-15 performance

Our approach to reconciling 2010-15 performance is set out in the [wholesale water and wastewater technical appendix](#). The company proposed adjustments to the opening RCV and allowed revenue for the wholesale wastewater services to reconcile performance in 2010-15. We have intervened and as a result the revenue adjustments for wholesale wastewater have changed from -£33.1 million to -£44.4 million. We summarise these interventions in Table A3.7 below, and quantify the resulting adjustments within this draft determination. The impact on the opening RCV of 2010-15 adjustments is shown in Table A3.5 above. As noted in the table, we have applied -£11.2 million in (net) adjustments arising from logging up, logging down and shortfalls. It should be noted that the company proposed net logging down of -£63.5 million, however we have intervened and applied a logging down of -£11.2 million – this relates to (i) sewerage supply demand and (ii) private sewers. Further information on our interventions and rationale is set out in annex 3.

Table A3.7 Anglian Water wholesale wastewater revenue adjustments to reflect 2010-15 performance (£ million)

Area	Intervention	Why we did it	Total 2010-15
Service incentive mechanism (SIM)	There are no interventions in this area.	n/a	10.2
Revenue correction mechanism (RCM)	We have intervened in the following areas: <ul style="list-style-type: none"> • FD09 assumptions • Measured non-household revenues 	We disagree with the company assumptions on the FD09 input variables for the RCM model.	-67.5
Opex incentive allowance (OIA)	There are no interventions in this area.	n/a	0.2
Capital expenditure incentive scheme (CIS)	In carrying out our assessment, we have: <ul style="list-style-type: none"> • used the PR09 vanilla cost of capital when calculating the financing costs; • used the PR09 pre-tax cost of capital 	The company has made tax adjustments to the PR09 cost of capital based financing and discount rates. We disagree with this approach and	12.7

Area	Intervention	Why we did it	Total 2010-15
	when calculating the future value of the revenue adjustment; and <ul style="list-style-type: none"> included our view of the applicable change protocol amounts. 	have applied Ofwat's published methodology.	
Other adjustments	There are no other adjustments in this area.	n/a	0.0
Total	n/a	n/a	-44.4

A3.2.5 Calculation of allowed revenue

The calculation of the allowed revenue for Anglian Water's wholesale wastewater control is shown in Table A3.8.

Overall, we consider that Anglian Water's wholesale wastewater revenue allowance should be £625.4 million in 2015-16, decreasing by 3.3% to £604.7 million in 2019-20.

Table A3.8 Anglian Water wholesale wastewater allowed revenue (£ million)

	2015-16	2016-17	2017-18	2018-19	2019-20	Total
Totex	435.8	556.2	492.3	505.8	500.4	2490.6
PAYG ratio	67.8%	51.5%	56.4%	53.5%	52.5%	-
Totex additions	140.1	269.7	214.8	235.3	237.8	1097.7
RCV (year average)	3983.1	4030.8	4113.1	4174.9	4244.7	-
Wholesale allowed revenue build up:						
PAYG ¹	306.6	297.4	288.3	281.4	273.5	1447.2
Return on capital	147.3	149.0	152.1	154.4	156.9	759.7
RCV run-off	156.3	158.2	161.7	164.8	168.5	809.5
Tax ²	11.3	7.4	3.3	1.2	0.0	23.2
Income from other sources	-1.6	-1.6	-1.7	-1.8	-1.8	-8.5

	2015-16	2016-17	2017-18	2018-19	2019-20	Total
Reconciling 2010-15 performance	-8.9	-9.0	-8.9	-8.8	-8.7	-44.4
Ex ante additional menu income	0.7	0.9	0.8	0.8	0.8	4.1
Capital contributions from connection charges and revenue from infrastructure charges	13.7	12.6	13.6	16.4	15.5	71.6
Final allowed revenues	625.4	614.8	609.2	608.4	604.7	3062.5

Notes:

1. PAYG includes the PAYG calculated from totex and the pension deficit repair allowance.
2. Including tax on adjustments for reconciling 2010-15 performance and ex ante additional menu income.

A3.3 Uncertainty mechanisms

We outline our approach to uncertainty mechanisms in the risk and reward technical appendix. In Table A3.9 below, we set out Anglian Water's proposed wholesale wastewater uncertainty mechanisms and our assessment of these proposals.

Table A3.9 Anglian Water proposals for wholesale wastewater uncertainty mechanisms

Anglian Water proposals	Our assessment
Anglian Water proposed an uncertainty mechanism to allow for logging for additional NEP obligations	<p>We have excluded this uncertainty mechanism from our draft determinations.</p> <p>Anglian Water has proposed a downside scenario of £895m spend on NEP requirements compared to a base case plan of £103m (which we have accepted as part of our wholesale cost assessment). We consider Anglian Water's downside costs are overstated. In addition we do not consider that the uncertainty mechanism is consistent with our criteria for uncertainty mechanisms:</p> <p>Materiality – Pass. Anglian Water's downside scenario represents a variance of over 30% of</p>

Anglian Water proposals	Our assessment
	<p>wastewater totex over the whole of 2015-20, and over 70% in the final two years. A variance of this magnitude would exceed the IDoK threshold and, if it transpires should be dealt with through the IDoK process.</p> <p>Controllability – Fail. Anglian Water has not demonstrated that it is unable to influence the scope of the requirements and control over the cost of potential schemes for NEP5. The company also has timing flexibility as it has until December 2021 to meet obligations.</p> <p>Comparability with other companies – Fail. Other companies have not requested protection from changes to NEP5 requirements. Anglian Water should have a good understanding of the risks and has provided no evidence to demonstrate that the level of risk that it faces is different to other companies.</p> <p>Customer protection – Fail. Customer interests are best served by not allowing a straight forward pass through of costs of this magnitude. We consider that it would be inappropriate for customers to bear 100% of the risk as Anglian Water is able to influence and control the ultimate costs.</p>
<p>Anglian Water proposed an uncertainty mechanism to allow for logging for growth in numbers of households</p>	<p>We have excluded this uncertainty mechanism from our draft determinations. Household growth was included as a risk scenario in the original methodology statement and forms part of the risk range set out in our risk and reward guidance. The issue that companies do not receive additional revenue to respond to growth in numbers of households was considered in our consultation on the methodology and it was decided not to incorporate a risk mechanism to deal with it. In addition we do not consider that the uncertainty mechanism is consistent with our criteria for uncertainty mechanisms:</p> <p>Materiality – Pass. The downside scenarios presented by Anglian Water covering water and wastewater represent a combined variance of</p>

Anglian Water proposals	Our assessment
	<p>1% of wholesale totex over the whole of 2015-20 and so we consider that the risk is material.</p> <p>Controllability – Fail. Anglian Water states that household growth patterns are highly sensitive to economic trends. While Anglian Water does not have control over household growth it does have control over the scale of costs incurred.</p> <p>Comparability with other companies – Fail. This risk is well understood and common to all companies. Anglian Water has not provided adequate justification to demonstrate why it requires specific protection from these risks when other companies have not.</p> <p>Customer protection – Fail. We consider that it would be inappropriate for Anglian Water customers to bear 100% of this risk when customers of all other companies bear only a portion of the risk with their respective companies through the totex menu.</p>

A4. Household retail

A4.1 Company outcomes, performance commitments and delivery incentives

In the [outcomes technical appendix](#), we discuss our approach to outcomes for the wholesale and retail controls.

We summarise the outcomes, performance commitments and outcome delivery incentives for the household retail control for Anglian Water in Table A4.1 below. Full detail of the wholesale water outcomes, performance commitments and incentives is provided in annex 4.

Table A4.1 Household retail outcomes, performance commitments and incentives

Company proposal			Intervention
Outcome	Performance commitment	Incentive type	
Satisfied customers	Qualitative Service Incentive Mechanism Score (household retail)	Non-financial incentive	No intervention. (Note: This is a different performance commitment to that for wholesale water and wastewater where we are proposing to intervene).
	Service Incentive Mechanism	Financial – reward and penalty	No intervention.
	Customer Satisfaction Index prepared by UK Institute of Customer Service	Non-financial incentive	No intervention.

Company proposal			Intervention
Outcome	Performance commitment	Incentive type	
Fair charges	Fairness of bills perception – variation from baseline against water and wastewater companies	Financial – reward and penalty	No intervention.
	Affordability perception – variation from baseline against water and wastewater companies	Financial – reward and penalty	No intervention.
A smaller footprint	Operational carbon (percentage reduction from 2015 baseline in real terms) (whole business)	Non-financial incentive	No intervention.
	Embodied carbon (percentage reduction from 2010 baseline) (whole business)	Non-financial incentive	No intervention.
Caring for communities	Survey of community perception	Non-financial incentive	No intervention.

A4.1.1 Outcome delivery and reporting

We are satisfied with the company's proposals for self-reporting. But consistent with the commentary in our assurance technical annex, we will need to consider the categorisation of the company for assurance purposes at the final determination.

Anglian Water's proposed approach to the measurement, reporting and governance of outcomes and our assessment of this approach is summarised in annex 4.

A4.2 Costs

Our approach to the household retail control is set out in the [household retail technical appendix](#).

A4.2.1 Allocation of costs

In Table A4.2 below, we summarise our assessment of Anglian Water's cost allocation methodology.

Table A4.2 Our assessment of Anglian Water's cost allocation methodology

Area assessed	Assessment
No potential material misallocations	Pass
Adequate assurance provided	Pass
Reconciliation to regulatory accounts and December business plan provided	Pass
Correct price base used	Fail

The company has submitted information to suggest that it has allocated its costs in line with our guidance. In our draft determination, we have used the company's cost allocations between retail and wholesale and between household and non-household.

On the whole we were satisfied with the external assurance that the company had obtained over its cost allocations. However we did note one gap in the external assurance provided. The company had undertaken sampling to allocate its network and non-network enquiries and complaints between household and non-household but had not obtained external assurance on this sample as required by our guidance.

This was because the company did not believe that these costs were material. We disagree with this. We consider these costs to be material (as they represent 13.2% of retail costs and 115% of non-household retail costs) and so conclude that external assurance should have been obtained over this sample. We expect the company to provide us with external assurance over this sample with its draft determination representations on 3 October.

While reviewing the company's cost allocations, we also noted that the company had submitted tables R3 and R4 in 2013-14 outturn prices. This is not in line with our guidance which required these tables to be prepared in 2012-13 base year prices. We have amended our models to deflate the company's household and non-household costs to 2012-13 base year prices.

A4.2.2 Adjustments

Anglian Water did not propose any average cost to serve (ACTS) adjustments. The adjustments proposed by Anglian Water and Ofwat are quantified in Table A4.4.

Table A4.3 Anglian Water proposals for ACTS adjustments

		Adjustment assessment criteria			
Adjustment	Value (£m over 2015-20)	Materiality	Beyond efficient management control	Impact company in materially different way	Value of adjustment appropriate
No adjustments proposed	n/a	n/a	n/a	n/a	n/a

Table A4.4 Household retail adjustments (£ million, nominal prices)

	2015-16	2016-17	2017-18	2018-19	2019-20	Total
Adjustments proposed in Anglian Water's business plan						
Pension deficit repair costs	1.656	1.656	1.656	1.656	1.656	8.281
Adjustments included in business plan	1.656	1.656	1.656	1.656	1.656	8.281
Adjustments included in draft determination						
Pension deficit repair costs	1.718	1.718	1.718	1.718	1.718	8.588
Adjustments included in draft determination	1.718	1.718	1.718	1.718	1.718	8.588

Note:

There will be no indexation for retail price controls.

A4.2.3 New costs

In Table A4.5 below, we outline Anglian Water's proposed 'new costs' and our assessment of these proposals.

Table A4.5 Anglian Water proposals for household retail new costs

Value (£m over 2015-20)	New costs assessment criteria				
	Materiality	Need	Options and CBA	Robustness of costs	Customer protection
10.3	Pass	Pass	Pass	Pass	Pass

Anglian Water proposed an investment in a new billing system and upgrades to its central IT systems.

Ofwat accepts Anglian Water's proposed new costs. All new costs are included in the calculation of allowed revenues. We have accepted these new cost proposals because the need for the costs is well evidenced through business cases, good quality options analysis is provided, the cost estimates used are robust and customer protection has been sufficiently considered.

Anglian Water's new cost increases are material (2.8% of total household retail operating expenditure plus depreciation over 2015-20).

The cost increases are driven by capex investments in a Customer Relationship Management system (CRM) and central IT systems that are recharged to retail. Operating expenditure is held nearly constant per customer over time. The need for these investments is well justified through business cases for each investment.

That these are the most cost beneficial investments has been evidenced through sufficient options analysis. This assesses different options that are sufficiently detailed and show that the most cost beneficial solutions are chosen.

Cost estimates have been generated robustly through comparison to costs of completed projects and through the construction of commodity cost estimates.

Customer protection has been considered through surveys and ensuring each investment is linked to customer benefits. Customers are also protected through the SIM, including through proposed enhancements to the SIM.

Table A4.6 New household retail costs (£/customer)

	Value
Modification made to 2013-14 CTS for ACTS calculation	0.32

Note:

There will be no indexation for retail price controls from this 2012-13 price base.

A4.3 Calculating the allowed revenues

Using the average industry allowances per customer, and the projected customer numbers in the company's revised business plan, we have calculated the total allowed household retail revenues, including the efficiency challenge and the household retail net margin.

A4.3.1 Net margins

Table A4.7 below shows the household retail net margin over 2015-20.

Table A4.7 Household retail net margins (%)

	2015-16	2016-17	2017-18	2018-19	2019-20
Household retail net margin	1.00%	1.00%	1.00%	1.00%	1.00%

Table A4.8 below sets out the components of the allowed household retail revenue.

Table A4.8 Components of the allowed household retail revenue (nominal prices)

	2013-14	2015-16	2016-17	2017-18	2018-19	2019-20
Company cost to serve (£/customer)						
Unmetered single service customers	19.88					
Unmetered water and wastewater customers	25.85					
Metered water only customers	22.34					
Metered wastewater only customers	22.95					
Metered water and wastewater customers	29.25					
Industry average cost to serve (£/customer)						
Unmetered single service customers						20.73
Unmetered water and wastewater customers						26.78
Metered water only customers						24.04
Metered wastewater only customers						33.31
Metered water and wastewater customers						26.95
Allowed cost to serve¹ (£/customer)						
Unmetered single service		19.13	19.68	20.02	20.17	20.30

	2013-14	2015-16	2016-17	2017-18	2018-19	2019-20
customers						
Unmetered water and wastewater customers		24.86	25.58	26.02	26.22	26.40
Metered water only customers		21.54	22.09	22.43	22.58	22.72
Metered wastewater only customers		22.18	22.73	23.07	23.22	23.36
Metered water and wastewater customers		28.26	28.97	29.41	29.61	29.79
Total allowed (£ million)						
Cost to serve (excluding net margin)		69.4	71.9	73.8	75.2	76.5
Forecast household wholesale charge (including forecast RPI ²) ³		1,108.8	1,134.2	1,164.9	1,201.9	1,232.9
Household retail revenue (including an allowance for the net margin) ⁴		79	82	84	85	87

Notes:

There will be no indexation for retail price controls.

1. Allowed cost to serve includes pension deficit repair costs.
2. The household wholesale charge includes forecast RPI so that the total household retail revenue can be displayed on the same price base as other retail costs.
3. The allocation of allowed wholesale revenue to different wholesale charges will be at the company's discretion, subject to charging rules and licence conditions.
4. This number is indicative as allowed revenue will depend upon actual customer numbers.

A4.4 Uncertainty mechanisms

We outline our approach to uncertainty mechanisms in the [risk and reward technical appendix](#). In Table A4.9 below, we set out Anglian Water's proposed household retail uncertainty mechanisms and our assessment of these proposals.

Table A4.9 Anglian Water proposals for household retail uncertainty mechanisms

Anglian Water proposals	Our assessment
Anglian Water did not propose any uncertainty mechanisms beyond those that will already form part of the regulatory framework for 2015-20.	n/a

A5. Non-household retail

In the [non-household retail technical appendix](#), we outline our overall approach to the non-household retail price control. Further information regarding our observations on companies' proposals for their non-household retail price controls is set out in [IN 14/14: 2014 price review – non-household customer engagement ahead of draft determination representations](#).

In this chapter, we provide details of Anglian Water's non-household retail draft determination.

A5.1 Indicative non-household retail total revenue

Table A5.1 below shows the indicative total of non-household allowed revenue. The table is indicative, as it does not assume any gains or losses from competition or impacts from the company charging customers at levels different to the relevant default tariffs for the projected customers in each customer type.

Table A5.1 Indicative non-household retail total revenue price control including net margins (£ million, nominal prices)

	2015-16	2016-17	2017-18	2018-19	2019-20
Indicative non-household retail total revenue price control including net margins	15	15	16	16	16

Note: There will be no indexation for retail price controls from this price base. The non-household wholesale charge includes forecast RPI so that the total non-household retail revenue can be displayed on the same price base as other retail costs. Figures exclude retail services to developers and revenues associated with miscellaneous charges.

A5.2 Net margins

The company proposed net margins that summated in aggregate to 2.5%. This is in line with our risk and reward guidance. We have therefore accepted the company's proposals.

A5.3 Cost proposals

Below we set out our interventions on the company's costs, including for:

- consistency with existing policy, including for example ensuring that companies cost information is presented in a consistent price base and pension deficit costs are presented as per our stated policy; and
- cost escalation, including for example material new investments or increases in costs or requests for input cost allowances.

The table requirements stipulated the use of 2012-13 prices. The company did not deflate its costs; therefore we have deflated its submission from 2013-14 prices to 2012-13 prices.

In '[IN 13/17: Treatment of companies' pension deficit repair costs at the 2014 price review](#)' we explained how we would treat the costs associated with water companies reducing the deficits in their defined benefit pension schemes at the 2014 price review. Where companies' proposals have differed from our calculations we have over-written their proposals in line with our overall approach.

This resulted in the company's proposals being adjusted from £1.065 million over the control period, to £1.377 million.

Overall the company's proposed costs do not increase by more than our non-household retail materiality threshold of 5.3% between 2015 and 2020. We have therefore accepted the company's cost proposals (post the pension deficit recovery adjustment).

In total, this resulted in the company's proposed costs being adjusted from £45.189 million over the control period to £44.273 million.

However, we also note that the company's opex in 2013-14 is significantly higher than the preceding two years. As part of its representations we request for the company to provide us with a clear explanation as to the cost increase, and to explain why the increase should not be treated as an exceptional one-off event.

A6. Appointee

In this section we discuss at an appointee level:

- bills and k factors;
- return on regulated equity;
- financeability; and
- affordability.

We note that in relation to affordability the company has withdrawn the proposed RPI sharing mechanism it included in its December business plan. This involved the company sharing any increase in RPI between 3% and 4.5% with customers.

This innovative mechanism, which does not form part of our methodology, was voluntarily offered by the company. We were disappointed to see it removed from the company's revised business plan and we would encourage Anglian Water to consider adopting it again once it has considered our draft determination.

A6.1 Bills and K factors

Table A6.1 below sets out the allowed revenues we have assumed in our draft determination for Anglian Water to deliver its:

- statutory duties;
- outcomes; and
- associated performance commitments.

It also sets out the average customer bills on the basis of the draft determination.

Table A6.1 Anglian Water’s draft determination – K factors, allowed revenues and customer bills (in 2012-13 average prices)¹

	2015-16	2016-17	2017-18	2018-19	2019-20	Total
Wholesale water – allowed revenues (£m) ²	415.5	414.9	414.7	417.9	416.5	2,079.5
Wholesale water – K (%) ³	0.00%	-0.15%	0.05%	0.60%	-0.54%	-
Wholesale wastewater – allowed revenues (£m)	625.4	614.8	609.2	608.4	604.7	3,062.5
Wholesale wastewater ³ – K (%)	0.00%	-1.69%	-0.81%	-0.32%	-0.79%	-
Retail household allowed revenue (£m)	78.9	81.6	83.8	85.5	87.1	416.8
Retail non-household expected revenue (£m)	15.2	15.4	15.5	15.7	15.8	77.5
Average household bill – water (£)	174	173	172	171	169	-
Average household bill – wastewater (£)	223	219	216	214	212	-
Average household bill – combined (£) ^{4, 5}	380	375	370	368	363	-

Notes:

1. Wholesale figures in 2012-13 prices and retail figures in nominal prices
2. The allowed revenue for our draft determination is based on an implied menu choice. The company will have the opportunity to make its own menu choice, which will impact on its allowed revenues and customers’ bills.
3. As discussed in the [wholesale water and wastewater technical appendix](#), K is set to zero for 2015-16 for wholesale water and wastewater because there are no directly equivalent wholesale revenues for 2014-15 (on account of the new price review structure). As such, there is no reference point against which to express a change in K.
4. The average combined household bill is not equal to the sum of the average household water bill and the average household wastewater bill due to the use of the economies of scope factor in the household retail price control.
5. It should be noted the average household bill illustrated above reflects a notional allocation (by Ofwat but based on the company’s split of household and non-household customers) of the overall wholesale revenue requirement across Anglian Water’s household and non-household customer base. In practice, this will depend upon the structure of wholesale charges implemented by Anglian Water.

We note that customer bills in the regulatory period from 2020 will be affected by Anglian Water's performance in the forthcoming regulatory period in relation to costs and the regulatory incentives in place for performance delivery and revenue projection performance.

Anglian Water has also proposed that the financial rewards and penalties associated with its leakage performance commitment could be applied within the 2015-20 regulatory period. This means that its customers' bills could vary over the period from those set out above.

For a company to be able to recover outcome rewards between price controls we would need to change its licence. Anglian Water has proposed a draft licence modification that it considers would enable its approach and we are reviewing this as part of its proposal. We need to consider how any modification would ensure that the company remains within the overall cap and collar on outcome delivery incentives for the 2015-20 period which we are setting. We also require the company to demonstrate that its customers support the idea of their bills varying during the period to reflect the company's performance. If we accept the company's proposed approach to its leakage performance commitment and incentives we will formally consult on a licence change before we make our final determination.

A6.2 Return on regulated equity range

We set out our approach to calculating the expected range in RoRE in the [risk and reward technical appendix](#). The whole company RoRE range, based on RoRE information provided by Anglian Water, and reflecting our interventions on ODIs, is shown in Table A6.2 below.

Table A6.2 Whole company RoRE range

	Lower bound (%) (appointee)	Upper bound (%) (appointee)
Overall	-4.0%	+2.7%
ODIs	-1.4%	+0.5%
Totex	-2.1%	+1.5%
Financing	-0.2%	+0.5%
SIM	-0.3%	+0.2%

Commentary:

The whole company RoRE range is from 1.7% to 8.4%, with a base case of 5.7%. This translates to a downside impact of -4.0% and an upside variance of +2.7% as shown in the table.

Anglian Water has modelled totex performance variance by combining an assumption of +/- 15% capex out-/under-performance and +/- 6% opex out-/underperformance (pre-cost sharing) with macro-economic factors. The skewness towards the downside reflects its focus on serviceability ODIs and its intention to deploy additional expenditure to rectify any shortfall in performance. We consider its approach to be robust and the resultant RoRE impacts, ranging from -2.1% to +1.5%, are broadly in line with other companies. As set out in the technical annex, we have not adjusted totex performance range to take account of our interventions on wholesale totex.

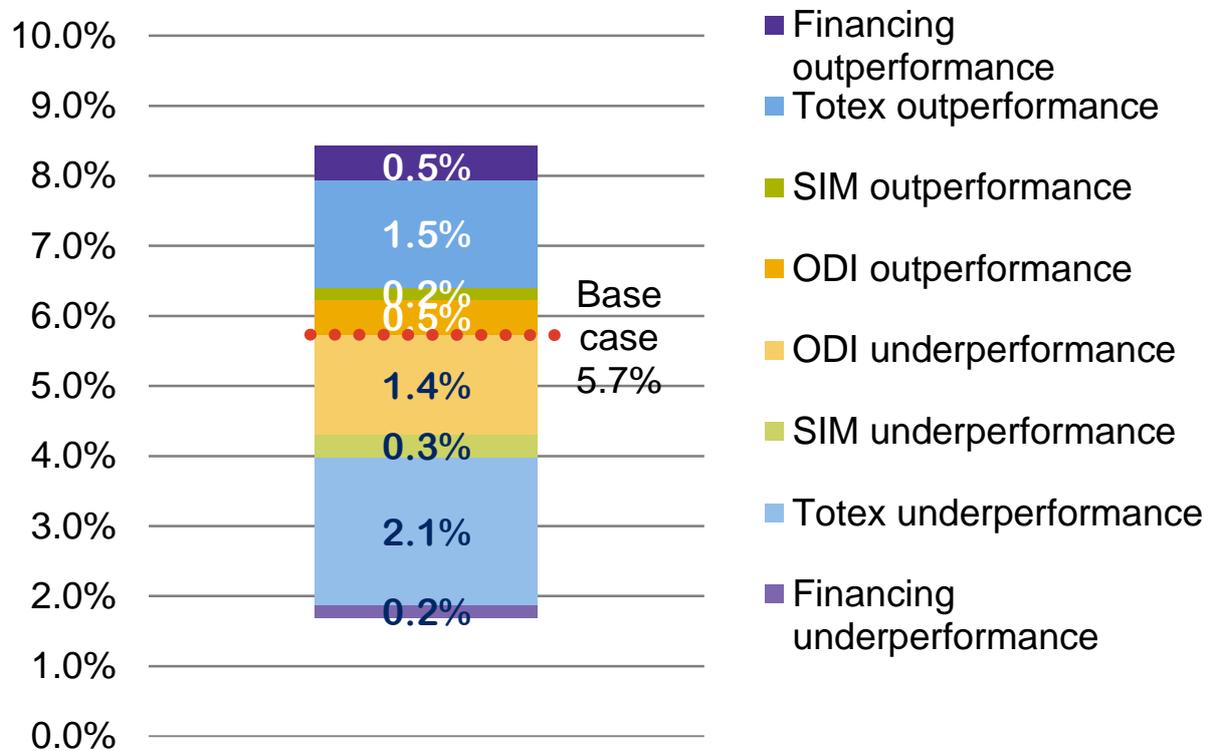
The ODI range proposed by Anglian Water was from -1.3% to +1.1%. We have adjusted this range to -1.4% to +0.5% to take account of our interventions discussed in annex 4.

Anglian Water has assessed financing impacts on a notional basis based on analyst forecasts for the cost of new debt. This results in a RoRE range of -0.2% to +0.5% which we consider to be reasonable.

Anglian Water has estimated SIM range based on maximum reward and penalties (+0.5% to -1% of revenue) reflecting its view that it would be feasible for it to achieve a SIM outturn at either end of the range. We accept its rationale.

The composition of the RoRE range for Anglian Water at an appointee level is shown in Figure A6.1 below.

Figure A6.1 Anglian Water RoRE range – appointee



Source:

Ofwat calculations based on information from Anglian Water.

A6.3 Financeability

We have compared the financial ratios provided by Anglian Water and our calculation of its financial ratios implied by the company’s business plan proposals submitted on 27 June, when both are prepared on a notional basis. We illustrate these in Table A6.3 below. The final column of Table A6.3 sets out the financeability ratios based on our draft determination revenues and costs.

Table A6.3 Company and Ofwat financial ratio calculations based on the company business plan and financial ratios based on our draft determination

Financial ratios for notional company	Financial ratio calculations based on the company business plan (average 2015-20)		Financial ratio calculations based on our draft determination (average 2015-20)
	Company calculation	Ofwat calculation	
Cash interest cover (ICR)	2.86	2.78	2.84
Adjusted cash interest cover ratio (ACICR) – base case (average over five years)	1.52	1.41	1.46
Funds from operations(FFO)/debt	8.96%	8.39%	8.66%
Retained cash flow/debt	6.43%	5.79%	6.04%
Gearing	63.39%	64.67%	62.26%
Dividend cover (profit after tax/dividends paid)	1.18	1.31	1.30
Regulatory equity/regulated earnings for the regulated company	16.76	17.16	17.67
RCV/EBITDA	9.86	10.95	11.17

Commentary:

Financial ratios: The company provided Board assurance on an actual and notional basis. The company's financial ratios are at least consistent with its target credit rating of Baa2. Anglian Water's proposed actual dividend is consistent with the notional dividend. Our calculated financial ratios are similar to the company's based on both the company's plan our draft determinations. We therefore consider that the draft determinations are financeable.

Use of PAYG: Anglian Water has increased PAYG rates since December business plan. Its PAYG rate is now 101% of Opex and IRE and 109% of opex plus IRE expensed. The CCG accepts the company's reasoning behind the PAYG adjustment, and considers that the company's PAYG ratio is not out of step with others across the industry.

Pass though of weighted average cost of capital (WACC): Anglian Water has passed through around 30% of the reduction in WACC (4.29% to 3.70%) in terms of lower customer bills in the 2015-20 period.

Conclusion on intervention: Anglian Water use of PAYG since December appears consistent with maintenance of financeability on a notional basis. We therefore do not propose to intervene on PAYG on the basis of financeability. However the company should engage with its customers by providing further information on the impact of the use of PAYG levers and the proposed amount of pass through of the WACC reduction including the benefits to customers and discuss why alternative scenarios of pass through of the WACC reduction in 2015-20 are not the best interest of customers. Any engagement on financeability should be undertaken on the basis of notional financeability.

Table A6.4 sets out the PAYG and RCV run-off rates which shows whether revenue has been brought forward compared to the December plan and the impact that this has on RCV growth and longer term affordability and financeability.

Table A6.4 Impact on the longer term

	PAYG rate	RCV run-off	RCV growth % 1 April 2015 to 31 March 2020
Company December plan	53.9%	3.90%	4.6%
Company June plan	58.3%	3.90%	0.4%
Draft determinations	58.3%	3.90%	6.8%

A6.4 Affordability

Table A6.5 sets out the change in household bill profile between the company's December and June business plans and the draft determinations.

Table A6.5 Household bill profile

	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Company December plan	412	404	397	391	384	377
Company June plan	406	399	394	388	383	377
Ofwat calculation for June plan	408	396	390	384	379	372
Ofwat calculation for	408	380	375	370	368	363

	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
draft determinations						

Companies have not necessarily used the same method of calculating household bills as Ofwat – for example, we have included economies of scope for household retail when calculating combined water and sewerage bills. So the Ofwat calculations (lines 3 and 4 of Table A6.5) are not directly comparable to the company plans (lines 1 and 2 of Table A6.5). We have not intervened to reprofile customer bills as the draft determinations bill profile is similar to that in the company's June plan, although with a lower starting bill.

Table A6.6 sets out the reasons why this draft determination is assessed as affordable. It describes key changes in relation to Anglian Water's December business plan that we assessed as affordable.

Table A6.6 Business plan affordability assessment

	Commentary
Acceptability	<p>Anglian Water's customer engagement, carried out in support of its December submission, found that the business plan was considered acceptable by 90% of its customers.</p> <p>In its June submission, the company's proposed average bills across 2015-20 around 1% lower than those in the December submission, although the bill in the final year is the same. There is no evidence that there has been any reduction in the scope or scale of the service package being offered in the June plan. It is reasonable to assume that the further reduction in bills resulting from our interventions in the this draft determination will remain acceptable to the majority of the company's customers.</p>
Identification of affordability issues and appropriate support measures	<p>In its December submission, the company proposed an appropriate range of measures designed to help those customers identified as having affordability problems. These include: the Water Sure and Aqua care assistance tariffs (which between them help 44,000 customers), water efficiency advice, meter promotion, a trust fund (investment in which is planned to increase from £0.75m to £1m in the next price control period, 2015-20). The company is also developing a new social tariff which it plans to have on line for the 2015-16 charging year.</p> <p>In the revised submission, the company has maintained the scale and scope of the package of affordability measures proposed in the December plan.</p>

	Commentary
Longer-term affordability – cost recovery tools	<p>In its December plan, there was no indication that either current or future customers would be adversely impacted by the company's approach to cost recovery.</p> <p>In its June submission, the company explains how accepting the lower WACC has necessitated an increase in PAYG in order to remain financeable. The RCV run-off ratios remain unchanged from the December plan.</p>
Longer-term affordability – ODIs	<p>The company has revisited its package of ODIs for the June submission, in accordance with the risk and reward guidance. The company undertook a new piece of acceptability research which concluded that most customers found the new ODI approach and the concept of bills being impacted by the company over or under performing, to be acceptable. The CCG gave its qualified support of the revised ODI package.</p>

Annex 1 Wholesale costs

Establishing draft determination thresholds

Our approach to establishing draft determination thresholds is outlined in the [wholesale water and wastewater technical appendix](#).

In the tables below, we provide information for some of the company-specific numbers that support these calculations.

Further information about our assessment of each claim is set out in the [populated version of draft determination initial cost threshold models](#).

Table AA1.1 Movement from basic cost threshold to draft determination menu threshold for wholesale water totex (£ million)

Basic cost threshold	Policy additions ¹	Unmodelled costs adjustment ²	Deep dive	Draft determination threshold	Deep dives fully or partially not added ³
1,417.3	253.2	15.3	1.4	1,687.1	8

Note:

1. See Table AA1.2 below.
2. We accepted the company's special cost claims for investment to deliver RSA schemes and to deliver the Eels part of the NEP, and investment in dual supplies for populations over 30,000. We rejected the company's claim for investment in energy resilience.
3. Deep dives are net of implicit allowances. A value of zero means deep dives are wholly covered by implicit allowances.

Table AA1.2 Policy additions to the wholesale water basic cost threshold (£ million)

Business rates	Pension deficit payments	Third party costs	Open market costs ¹	Net v gross adjustments	Total
204.6	37.5	9.9	1.1	0.0	253.2

Note:

1. Of this amount, £0.170m relates to 2014-15 open market costs.

Table AA1.3 Comparison of company wholesale water totex with the draft determination threshold and 2010-15 totex (£ million)

Plan	DD threshold	Gap ¹	Plan v 2010-15
1,773.3	1,687.1	86.1	100.3

Note:

1. This gap will not equal the deep dives fully or partially not added in Table AA1.1 if the company's claims for special treatment in the costs thresholds are not equal to the gap.

Table AA1.4 Summary of wholesale water deep dive assessments

Company proposal		Assessment				DD allowance	
Claim	Amount sought	Implicit allowance	Need	CBA	Robust costs	Assessment	Amount allowed
Re-specification of the supply demand unit cost model	£34.5m	£0m	Partial pass	Partial pass	n/a	Partially accept	£19.6m

Note:

1. The company also made representations to our cost models following the publication of these in April. The representations made and our response is summarised in [wholesale water and wastewater technical appendix](#).

Table AA1.5 Movement from basic cost threshold to draft determination threshold for wholesale wastewater totex (£ million)

Basic cost threshold	Policy additions ¹	Unmodelled costs adjustment ²	Private sewage pumping stations	NEP5	Deep dive	Draft determination threshold	Deep dives fully or partially not added ³
2,195.7	178.8	-18.6	67.0	106.8	23.5	2,553.2	None

Note:

1. See Table AA1.6
2. We reduced our view of unmodelled costs to match those in the company's plan (after we had reallocated some costs to base and growth categories).
3. Deep dives are net of implicit allowances. A value of zero means deep dives are wholly covered by implicit allowances.

Table AA1.6 Policy additions to the wholesale wastewater basic cost threshold (£ million)

Business rates	Pension deficit payments	Third party costs	Open market costs ¹	Net v gross adjustments	Total
119.9	54.3	2.9	1.7	0.0	178.8

Note:

1. Of this amount, £0.248m relates to 2014-15 open market costs.

Table AA1.7 Comparison of company wholesale wastewater totex with the draft determination threshold and 2010-15 totex (£ million)

Plan	DD threshold	Gap	Plan v 2010-15
2,517.6	2,553.2	-35.5	372.5

Note:

1. This gap will not equal the deep dives fully or partially not added in Table AA1.5 if the company's claims for special treatment in the costs thresholds are not equal to the gap.

Table AA1.8 Summary of wholesale wastewater deep dive assessments

Company proposal		Assessment				DD allowance	
Claim	Amount sought	Implicit allowance	Need	CBA	Robust costs	Assessment	Amount allowed
Investment to allow for wastewater growth including UWWTR minimum treatment standards	£117.0m	£53.7m	Pass	Partial pass	Partial pass	Partially accept	£23.5m

Note:

1. We also note that the company made representations to our cost models following the publication of these in April. The representations made and our response is summarised in the [wholesale water and wastewater technical appendix](#).

Annex 2 Household retail revenue modification

We outline our approach to revenue modification in the household retail price control in the [household retail technical appendix](#).

Table AA2.1 sets out the amount per customer, by customer type, that allowed revenues will be modified by if outturn customer numbers differ from forecast customer numbers and Table AA2.2 sets out the baseline number of customers.

Table AA2.1 Household retail allowed revenue modification factors by class of customer (£/customer)

Revenue modification per:	2015-16	2016-17	2017-18	2018-19	2019-20
Unmetered water only customer	21.74	22.33	22.72	22.93	23.11
Unmetered wastewater only customer	21.74	22.33	22.72	22.93	23.11
Unmetered water and wastewater customer	28.26	29.03	29.54	29.81	30.04
Metered water only customer	24.48	25.07	25.46	25.67	25.85
Metered wastewater only customer	25.21	25.80	26.19	26.40	26.58
Metered water and wastewater customer	32.11	32.88	33.39	33.66	33.90

Note:

There will be no indexation for retail price controls.

Table AA2.2 Assumed number of customers for household retail total revenues (000s)

Number of customers	2015-16	2016-17	2017-18	2018-19	2019-20
Unmetered water only	98.3	90.9	83.5	76.4	69.7
Unmetered wastewater only	269.9	258.7	247.5	236.3	225.2
Unmetered water and wastewater	296.9	264.9	233.9	203.9	176.9
Metered water only	138.6	147.7	156.8	165.8	174.4

Number of customers	2015-16	2016-17	2017-18	2018-19	2019-20
Metered wastewater only	538.0	553.2	568.7	585.1	602.6
Metered water and wastewater	1417.5	1464.8	1512.2	1559.6	1605.0

Annex 3 Reconciling 2010-15 performance

We set out our methodology for calculating the adjustments to 2015-20 wholesale price controls resulting from the company's actual performance during the 2010-15 period in the [wholesale water and wastewater technical appendix](#).

In this annex, we set out the draft determination adjustments to 2015-20 price controls for Anglian Water resulting from the company's actual performance during the 2010-15 period.

As part of the draft determination of the 2010-15 adjustments we have undertaken detailed calculations within our models for the RCM, OIA, CIS and serviceability shortfalls. While we have covered an explanation of our interventions within this annex, each model covers the detail of the specific calculation. Similarly, our detailed calculations behind the midnight adjustments such as land sales (but excluding those relating to the Change protocol) are contained within the RCV midnight adjustment model. A copy of any of these models is available on request.

Table AA3.1 below compares the company's view of the required revenue adjustments included in its revised business plan for each of the incentive tools for water and wastewater services, with our own view. Our view reflects our understanding of the company's performance using these incentives, based on information provided in its revised business plan and subsequent query responses. The table also shows other adjustments, such as those relating to tax resulting from the company's actual performance during the 2010-15 period.

Table AA3.1 Revenue adjustments 2015-20 (£ million)

	Water service		Wastewater service	
	Company view	Ofwat view	Company view	Ofwat view
Service incentive mechanism (SIM)	7.300	7.180	10.254	10.231
Revenue correction mechanism (RCM)	-4.024	-4.566	-67.410	-67.547
Opex incentive allowance – post-tax (OIA)	4.383	4.383	0.194	0.197
Capital expenditure incentive scheme (CIS)	4.469	-3.778	23.865	12.703
Tax refinancing benefit clawback	0.000	0.000	0.000	0.000

	Water service		Wastewater service	
	Company view	Ofwat view	Company view	Ofwat view
Other tax adjustments	0.000	0.000	0.000	0.000
Equity injection clawback	0.000	0.000	0.000	0.000
Other adjustments	0.000	0.000	0.000	0.000
Total wholesale legacy adjustments	12.127	3.220	-33.098	-44.416

Notes:

Totals may not add up due to rounding.

For the CIS mechanism, there is a corresponding adjustment to the RCV made at 1 April 2015 (part of the midnight adjustments). The impact on the RCV for both water and wastewater can be seen in Table AA3.15. This adjustment is net of any logging up, logging down or shortfalls. A full reconciliation showing all of the midnight adjustments to the RCV, including the impact of logging up, logging down and shortfalls, can be seen in Table A2.5 and Table A3.5.

Service incentive mechanism (SIM)

We provide our view of each company's SIM reward/penalty in the [wholesale water and wastewater technical appendix](#).

Table AA3.2 provides the annualised rewards from the company's SIM performance. The slight difference in views is due to rounding.

Table AA3.2 SIM annualised rewards (£ million)

		2015-16	2016-17	2017-18	2018-19	2019-20	Total
Water	Company view	1.460	1.460	1.460	1.460	1.460	7.300
	Ofwat view	1.436	1.436	1.436	1.436	1.436	7.180
Wastewater	Company view	2.051	2.051	2.051	2.051	2.051	10.254
	Ofwat view	2.046	2.046	2.046	2.046	2.046	10.231

Revenue correction mechanism (RCM)

This draft determination includes our view of the company's RCM annualised adjustment amounts as detailed in Table AA3.3 below. Table AA3.4 summarises our interventions in relation to Anglian Water's proposed 2010-15 RCM adjustments.

Table AA3.3 RCM annualised adjustments for 2015-20 (£ million)

		2015-16	2016-17	2017-18	2018-19	2019-20	Total
Water	Company view	-0.805	-0.805	-0.805	-0.805	-0.805	-4.024
	Ofwat view	-0.913	-0.913	-0.913	-0.913	-0.913	-4.566
Wastewater	Company view	-13.482	-13.482	-13.482	-13.482	-13.482	-67.410
	Ofwat view	-13.509	-13.509	-13.509	-13.509	-13.509	-67.547

Table AA3.4 Interventions on proposed 2010-15 RCM adjustments

Area of intervention	What we did	Why we did it
FD09 assumptions	Our assumptions at the draft determination includes our view of the FD09 assumptions.	There are inconsistencies between the company's and our view of the FD09 assumptions used in the company's populated RCM model.
Measured non-household revenues	Our assumptions at the draft determination use the data the company submitted in business plan tables W17 and S17 to calculate our view of the RCM adjustment.	There were inconsistencies with the measured non-household revenues between business plan tables W17 and S17 and the company's populated RCM model.

Operating expenditure incentive allowance (OIA)

Table AA3.5 below summarises the company's view and our view of the incentive allowances for 2015-20. Table AA3.6 summarises our interventions in relation to Anglian Water's proposed 2010-15 OIA adjustments.

Table AA3.5 Operating expenditure incentive allowances for 2015-20 (£ million)

		2015-16	2016-17	2017-18	2018-19	2019-20	Total
Water service							
Incentive allowance (post-tax)	Company view	2.339	1.022	1.022	0.000	0.000	4.383
	Ofwat view	2.339	1.022	1.022	0.000	0.000	4.383

		2015-16	2016-17	2017-18	2018-19	2019-20	Total
Wastewater service							
Incentive allowance (post-tax)	Company view	0.194	0.000	0.000	0.000	0.000	0.194
	Ofwat view	0.197	0.000	0.000	0.000	0.000	0.197

Table AA3.6 Interventions on proposed 2010-15 OIA adjustments

Area of intervention	What we did	Why we did it
There are no interventions in this area. The small differences in wastewater allowances are due to minor rounding differences in the application of efficiencies to the logging up/down adjustments.	n/a	n/a

Change protocol (logging up, logging down and shortfalls)

Table AA3.7 and Table AA3.8 below summarise Anglian Water's view and our baseline view of total adjustments to:

- capex included in the CIS reconciliation; and
- the FD09 opex assumptions used in the calculation of the opex incentive revenue allowances.

Table AA3.9 summarises our interventions in relation to Anglian Water's proposed change protocol adjustments.

Table AA3.7 Summary of post-efficiency capex for logging up, logging down and shortfalls included in the CIS reconciliation (£ million)

2009-10 to 2014-15 – post-efficiency capex	Water service		Wastewater service		Total service	
	Company view	Ofwat view	Company view	Ofwat view	Company view	Ofwat view
Logging up (two-sided)	0.000	0.000	34.815	27.014	34.815	27.014

2009-10 to 2014-15 – post-efficiency capex	Water service		Wastewater service		Total service	
	Company view	Ofwat view	Company view	Ofwat view	Company view	Ofwat view
Logging down (two-sided)	-13.287	-13.523	-98.329	-38.177	-111.616	-51.700
Shortfalls (one-sided)	0.000	0.000	0.000	0.000	0.000	0.000

Notes:

1. Includes two-sided adjustments from the PR09 agreed overlap programme as set out in Table AA3.13.
2. We exclude shortfalls for serviceability from the CIS reconciliation, but instead make direct adjustments to the RCV in 2015-16. We do this to allow the actual capex the company incurred in seeking to maintain serviceability, to be reflected in the rewards or penalties earned through the scheme. But to also ensure customers are not required to pay for the regulatory output the company has failed to deliver.

Table AA3.8 Summary of post-efficiency opex for logging up, logging down and shortfalls included in the opex incentive allowance calculation (£ million)

2009-10 to 2014-15 – post-efficiency opex	Water service		Wastewater service		Total service	
	Company view	Ofwat view	Company view	Ofwat view	Company view	Ofwat view
Logging up	0.000	0.000	16.856	16.856	16.856	16.856
Logging down	0.000	0.000	-0.167	-0.167	-0.167	-0.167
Shortfalls	0.000	0.000	0.000	0.000	0.000	0.000
Shortfalls for serviceability	0.0	0.0	0.0	0.0	0.0	0.0

Table AA3.9 Interventions on proposed 2010-15 change protocol adjustments

Area of intervention	What we did	Why we did it
Beck Row WTW – Logging down	<ul style="list-style-type: none"> • The company proposed a log down of £12.9m (pre-efficiency) due to the removal of the Beck Row scheme. This value is £13.287 in post efficiency terms. • We have assessed the proposed logging down claim 	We have assessed the information provided to us by the company and identified an error in the calculation; although the calculation was correct in principle. The correction of the error increased the value of the capex to £13.130m (£13.523m in

Area of intervention	What we did	Why we did it
	<p>and increased the value of the capex to £13.130m (pre-efficiency). In post efficiency terms this is £13.523m.</p>	<p>post efficiency terms).</p>
<p>Sewerage Supply Demand – Logging down</p>	<ul style="list-style-type: none"> • The company proposed a pre-efficiency log down of £87.787m (capex) and £0.179m (opex) due to less activity than forecast in the sewerage supply demand programme. In post efficiency terms the company has therefore proposed a log down of £98.329m (capex) and £0.167m (opex). • We have assessed the proposed logging down and determined that the net capex to be logged down is £33.956m. In post efficiency terms this value is £38.177m. • The difference between the company view of capex and our view of capex is that our view takes account of grants and contributions (£53.8m). • We are therefore accepting the company’s proposed log down as stated in its commentary to table S13. • We did not apply a challenge to the opex. The company proposed a pre-efficiency opex of £0.179m opex (post efficiency – £0.167m) 	<p>The forecast information provided by the company predicts that some 81,900 new connections will not be delivered as per FD09. The gross capital expenditure applicable to the reduced number of new connections is £87.787m, with a corresponding reduction in grants and contributions of £53.8m. This results in a net capex reduction of £33.956m (£38.177m in post-efficiency terms). We have accepted the company’s proposed log down.</p>
<p>Private Sewers – Logging up</p>	<ul style="list-style-type: none"> • The company proposed a log up in pre-efficiency terms of £30.518m (capex) and £17.948m (opex). Expressed as post efficiency this is 	<p>We have assessed the company’s proposed logging up claim and reduced the collapse-related capex by 12.56% in order to bring the normalised capex/collapse to</p>

Area of intervention	What we did	Why we did it
	<p>£34.815m (capex) and £16.856m (opex).</p> <ul style="list-style-type: none"> • We have applied a challenge to the capex proposed. We have assessed the total amount of capex to be logged up as £23.678m. In post efficiency terms this value is £27.014m. • We have not challenged the company’s proposed pre-efficiency opex values (£17.948m). There is therefore no intervention for the opex. In post efficiency terms the opex is therefore £16.856m. 	<p>the industry unweighted average.</p>

Service standard outputs

The final determination supplementary reports in 2009 contained defined project(s) where the primary output was the service standard specified¹. These outputs were set out to recognise that companies may decide to prioritise investment differently in order to achieve the service output in a more innovative and efficient manner, while still holding the company to account for the benefits to customers and the environment.

Where companies have not reported progress on these service standards, we would have expected them to demonstrate achievement of the service standards to both customers and Ofwat as part of the price review process.

¹ In the final determination supplementary reports we said: “Both the project activity (as proposed in your final business plan) and the service standard are the defined output. You must demonstrate delivery of the stated service standard output through the June return. The service standard output is the primary output. We recognise that companies may decide to prioritise activity differently in order to achieve the service output in a more efficient manner. All material changes to the project activity must be reported and explained through your June return.”

We have considered applying shortfalls equal to the cost of the FD09 project(s) with defined service standards. However, in many cases there is some evidence that the projects and activities have been delivered, but there is a lack of compelling evidence that the service standards specified have been achieved.

For the purposes of these draft determinations, we will not applying shortfalls on this issue conditional upon this information being provided as part of companies’ draft determination representations. We would expect companies to respond to this issue in their representations. If they do not provide adequate evidence to demonstrate achievement of the service standards set out, then they should assume that we will apply a shortfall equal to the costs assumed for the project(s) at FD09 within our final determinations in December 2014.

Serviceability performance

Table AA3.10 below summarises our serviceability assessments for Anglian Water and Table AA3.11 quantifies the value and impact of any serviceability shortfall on the RCV. Table AA3.12 summarises our interventions in relation to Anglian Water’s proposed adjustments for serviceability.

Table AA3.10 Serviceability assessments for 2010-15¹

		2010-11	2011-12	2012-13	2013-14	2014-15 ²
Water infrastructure	Company view	Stable	Stable	Stable	Stable	Stable
	Ofwat view	Stable	Marginal	Marginal	Stable	Stable
Water non infrastructure	Company view	Stable	Stable	Stable	Stable	Stable
	Ofwat view	Stable	Stable	Stable	Stable	Stable
Wastewater infrastructure	Company view	Stable	Marginal	Marginal	Stable	Stable
	Ofwat view	Marginal	Deteriorating	Deteriorating	Stable	Stable
Wastewater non-infrastructure	Company view	Stable	Stable	Stable	Stable	Stable
	Ofwat view	Stable	Stable	Stable	Stable	Stable

Notes:

1. Assessments are based on actual and forecast performance submitted in the company's revised business plans.
2. Assessments for 2014-15 are based on forecast data and are subject to review once actual performance data becomes available.

Table AA3.11 Impact of serviceability shortfalls on the RCV (£ million)

2009-10 to 2014-15		Water	Wastewater	Total
Amount subtracted from RCV	Company view	0.0	0.0	0.0
	Ofwat view	0.0	0.0	0.0

Table AA3.12 Interventions on proposed 2010-15 serviceability adjustments

Area of intervention	What we did	Why we did it
Burst mains	For the purposes of the draft determination we have assumed no intervention. This is conditional upon the performance in 2014-15 being improved to a position such that it could be considered as stable. We may consider a shortfall adjustment if this is not achieved. We would expect the company to demonstrate its latest performance as part of its representations and in advance of the final determination.	The company has had two breaches of the upper control limit in 2010-11 and 2011-12. However, performance has recently recovered to just below the upper control limit. The company has provided evidence to show that adverse weather impacted on performance in those years. Considering the weather impacts, only 2011-12 remains above the upper control limit. We require the company to demonstrate stable serviceability in 2014-15, if this is not achieved, we may consider a shortfall adjustment.
Flooding other causes	For the purposes of the draft determination we have assumed no intervention. This is conditional upon the performance in 2014-15 being improved to a position such that it is considered stable. We may consider a shortfall adjustment if this is not achieved. We would expect the company to demonstrate its latest	The company has had three breaches of the upper control limit between 2010-11 and 2012-13. The company has provided evidence to show severe weather impact on performance in 2012-13 and 2013-14 performance recovered to near the reference level. However, we require the company to demonstrate stable serviceability in 2014-15. If this is

Area of intervention	What we did	Why we did it
	performance as part of its representations and in advance of the final determination.	not achieved, we may consider a shortfall adjustment.

Note:

The shortfall calculation methodology is detailed within the [wholesale water and wastewater technical appendix](#).

The 2009 agreed overlap programme

Table AA3.13 below confirms the 2009 agreed overlap programme assumptions included in this draft determination. Table AA3.14 summarises our interventions in relation to Anglian Water's proposed adjustments for the PR09 agreed overlap programme.

Table AA3.13 PR09 agreed overlap programme adjustments and assumptions (£ million)

		2010-15		2015-20	
		Two-sided adjustment for inclusion in the CIS		Expenditure forecasts to complete the projects	
		Capex	Opex	Capex	Opex
Water service	Company view	0.000	0.000	21.772	0.433
	Ofwat view	0.000	0.000	21.772	0.433
Wastewater service	Company view	0.000	0.000	0.000	0.000
	Ofwat view	0.000	0.000	0.000	0.000

Table AA3.14 Interventions on proposed 2010-15 PR09 agreed overlap programme adjustments

Area of intervention	What we did	Why we did it
SEMD	Although we raised a query on this scheme following submission of the company's December 2013 business plan, which prompted the company to report against this in its revised business plan, we have not considered this programme of works as part of the PR09 overlap reconciliation.	There are two main reasons for this decision. Firstly, because the company did not originally report on this scheme in its December 2013 business plan, implying that this was not recognised as an overlap project. And secondly, because the company's FD09 assumptions are notably different from values we might have expected to see suggesting that this was not well defined at PR09.

Capital expenditure incentive scheme (CIS)

Table AA3.15 provides details of the CIS ratios and performance incentive. It also gives the:

- monetary amounts of the CIS performance reward or penalty;
- true-up adjustment to 2015-20 allowed revenues; and
- midnight adjustment to the closing 2014-15 RCV.

Table AA3.16 then sets out the profiled values of the revenue adjustments in each year 2015-20.

Table AA3.15 Legacy true-up adjustments

		Water service	Wastewater service	Total service
Restated FD09 CIS bid ratio	Company view	105.107	99.077	-
	Ofwat view	105.121	95.281	-
Outturn CIS ratio	Company view	91.038	87.417	-
	Ofwat view	90.907	87.868	-

		Water service	Wastewater service	Total service
Incentive reward/penalty (%)	Company view	2.401	3.870	-
	Ofwat view	2.437	3.752	-
Reward/penalty (£m)	Company view	22.387	46.747	69.134
	Ofwat view	22.757	45.085	67.842
Adjustments to 2015-20 revenue (£m)	Company view	4.150	22.163	26.313
	Ofwat view	-3.508	11.797	8.289
CIS adjustment to RCV (£m)	Company view	-140.850	-193.289	-334.139
	Ofwat view	-140.830	-193.276	-334.106

Commentary:

The company has made tax adjustments to the PR09 cost of capital based financing and discount rates. We disagree with this approach and have applied Ofwat's published methodology:

- We have used the PR09 vanilla cost of capital when calculating the financing costs.
- We have used the PR09 pre-tax cost of capital when calculating the future value of the revenue adjustment.
- We have included our view of the applicable change protocol amounts.

Notes:

The restated FD09 CIS bid ratio takes account of the adjustments for the change protocol (Table AA3.9) and the 2009 agreed overlap programme (Table AA3.13).

The reward/(penalty) is adjusted for the additional income included in the 2010-15 determination and the financing cost on the difference between actual spend and capital expenditure assumed in the 2010-15 determination to derive the value of the adjustment to 2015-20 revenue.

The adjustment to 2015-20 revenue values shown in this table assume a single year adjustment in the first year, and do not include the NPV profiling used for the draft determination.

Table AA3.16 Profiled revenue adjustments from the CIS reconciliation (£ million)

		2015-16	2016-17	2017-18	2018-19	2019-20	Total
Water	Company view	0.830	0.861	0.893	0.926	0.960	4.469
	Ofwat view	-0.702	-0.728	-0.755	-0.782	-0.811	-3.778
Wastewater	Company view	4.433	4.597	4.767	4.943	5.126	23.865
	Ofwat view	2.359	2.447	2.537	2.631	2.728	12.703

Other adjustments

Table AA3.17 below confirms the assumptions included in this draft determination with respect to the following adjustments:

- tax refinancing benefit clawback;
- other tax adjustments;
- equity injection clawback; and
- other adjustments.

Table AA3.17 Other adjustments 2015-20 (£ million)

	Water service		Wastewater service		Commentary
	Company view	Ofwat view	Company view	Ofwat view	
Tax refinancing benefit clawback	0.000	0.000	0.000	0.000	No adjustment was proposed by the company
Other tax adjustments	0.000	0.000	0.000	0.000	No adjustment was proposed by the company
Equity injection clawback	0.000	0.000	0.000	0.000	No adjustment was proposed by the company
Other adjustments	19.610	19.610	0.000	0.000	Adjustment to the RCV for the determination regarding the WING strategic main.

Annex 4 Outcomes, performance commitments and outcome delivery incentives

This annex sets out in detail the performance commitments and outcome delivery incentives (ODIs) for the company's wholesale water, wholesale wastewater and household retail outcomes, presented in that order.

The table and figure below first provide an overview of these performance commitments and ODIs. Table AA4.1 shows the balance between reward and penalty, penalty only and reputational incentives in the package of incentives for the company and Figure AA4.1 shows the potential financial impact of each of the financial incentives.

Table AA4.1 The composition of the proposed package of ODIs

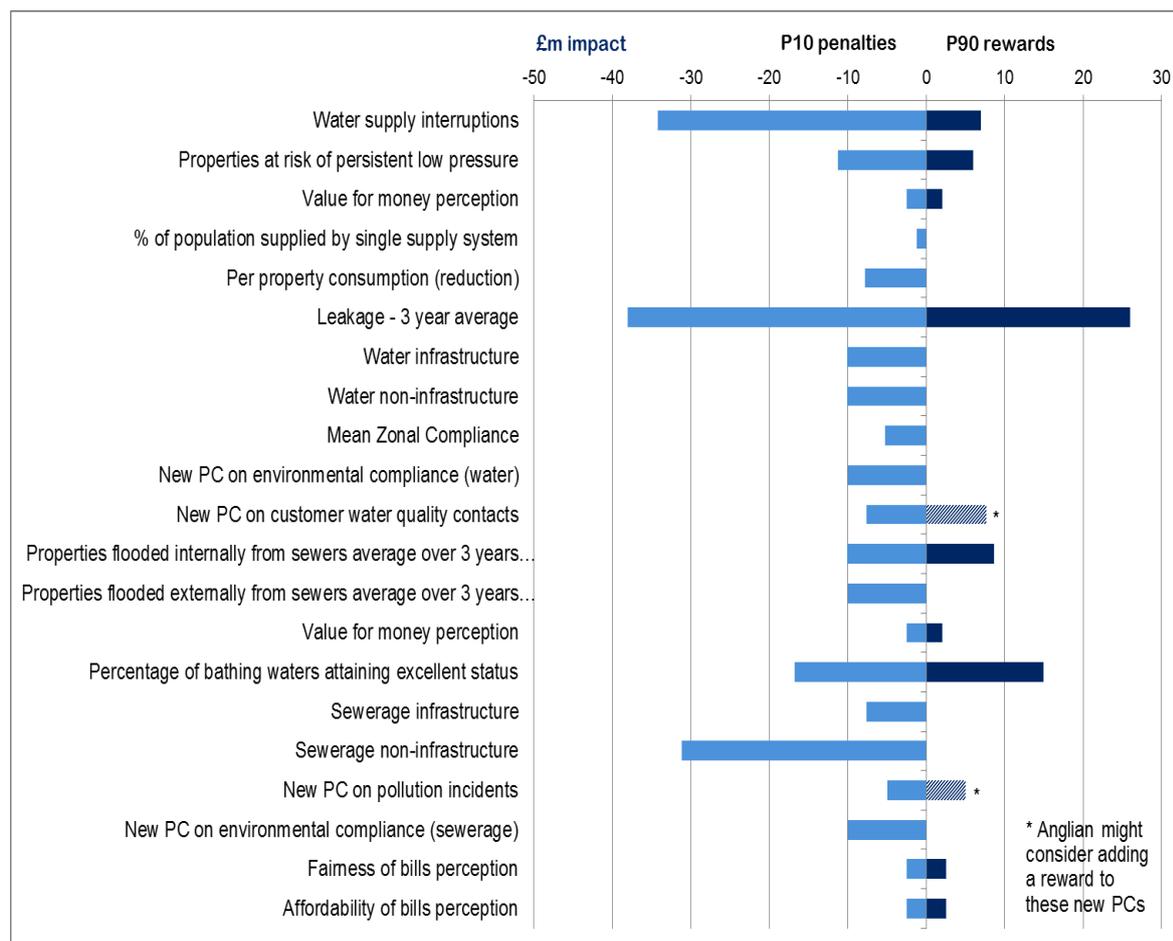
	Reward and penalty	Penalty only	Non-financial incentive
Wholesale water	4	7	7
Wholesale wastewater	2	6	5
Household retail	3	0	5
Total	9	13	17

Note:

Table AA4.1 includes the performance commitments for water quality contacts, pollution incidents and the two environmental compliance performance commitments (water and wastewater) that we have added to this draft determination as 'Financial – penalty only'. For the water quality contacts, pollution incidents and internal sewer flooding performance commitments Anglian Water might choose to propose a reward.

The following figure shows the potential financial consequences of the individual financial ODIs. The figures represent the penalties and rewards associated with the p10 and p90 scenarios over the five years (2015-16 to 2019-20). This means there is a 10% chance of performance being higher or lower than these assumed levels. In most cases the potential maximum will be bigger but is very unlikely to occur. The p10 and p90 scenarios therefore represent a more realistic estimate of potential financial impacts.

Figure AA4.1 Overview of financial ODIs



As explained in the [outcomes technical appendix](#), we are proposing the introduction of an aggregate cap on rewards and collar on penalties from the outcome delivery incentives. Details of how the cap/collar will operate are set out in section A5 of the [outcomes technical appendix](#).

There are a small number of specific exclusions from the cap/collar. For Anglian Water, the exclusions are as follows: Leakage – three year average, the new PC on environmental compliance (water) and the new PC on environmental compliance (wastewater).

Tables AA4.2, AA4.3 and AA4.4 set out a more detailed explanation of our interventions in the company’s wholesale water, wholesale wastewater and household retail outcomes.

Although the company did well against the tests we applied to outcomes during the risk-based review, we have intervened in several performance commitments and

outcome delivery incentives for this draft determination because:

- as set out in our risk and reward guidance we did not assess company's outcome delivery incentives as part of our risk-based review;
- the company changed aspects of its proposals, including the design and level of some of its performance commitments, between its December and revised business plans; and
- following the submission in June of revised company business plans, and updated information on current performance, we have carried out bottom-up assessments and consistency checks, both across company's outcomes and within individual company plans (see the [outcomes technical appendix](#) for more information).

Table AA4.2 Summary of interventions on wholesale water outcomes, performance commitments and incentives

PC/ODI affected	What we did	Why we did it
A2 – Water supply interruptions	<p>We converted the performance commitment into minutes rather than seconds.</p> <p>We converted the performance commitment into absolute levels rather than changes.</p> <p>We moved the performance commitment and penalty deadband to 10 minutes in 2017-18 with a glide path from current performance for the performance commitment.</p> <p>We moved the reward deadband down to 10 minutes from 2015-16 onwards.</p>	<p>We carried out a horizontal comparison of interruptions to supply across the industry. The majority of companies used minutes rather than seconds for their interruptions measure so we changed Anglian Water's measure to minutes. Anglian Water was the only company who proposed a change rather than an absolute level for interruptions in its performance commitment. We therefore converted the performance commitment to a level based on Anglian Water's recent past performance.</p> <p>Consistent with our approach to other companies we reduced the performance commitment level and penalty deadband to 10 minutes (upper quartile) in 2017-18. We reduced the penalty collar to approximately maintain the company's proposed maximum penalty. We moved the reward deadband down to 10 minutes so that Anglian Water will only earn a reward for upper quartile performance over 2015-20.</p> <p>We recalculated the reward rate according to the formula set out in our July 2013 methodology, appendix 1.</p>

PC/ODI affected	What we did	Why we did it
	We recalculated the reward rate.	
A3 – Properties at risk of persistent low pressure	<p>We introduced an intermediate target for 2017-18.</p> <p>We moved the reward deadband to 230 properties.</p> <p>We recalculated the reward rate according to the formula in PR14 final methodology appendix 1.</p>	<p>Anglian Water proposed that the rewards and penalties for this performance commitment would be based on its 2019-20 performance only. To incentivise the company to make progress towards its performance commitment over 2015-20, we have set an intermediate target in 2017-18 based on Anglian Water delivering three fifths of the improvement in its 2019-20 performance commitment. We have attached one fifth of the penalties Anglian Water proposed to the intermediate target.</p> <p>When comparing companies' performance in relation to properties at risk of persistent low pressure we found that Anglian Water was a relative poor performer. We moved the reward deadband to ensure the company has to deliver a larger reduction in properties at risk of persistent low pressure before it can earn a reward.</p> <p>We recalculated the reward rate according to the formula set out in our July 2013 methodology, appendix 1.</p>
B1 – Value for money perception – variation from baseline against WASCs (water)	We applied a condition requiring that the company does not earn a reward if its absolute score has gone down.	To protect customers from paying for a reward to Anglian Water when their perception of value for money of the company has gone down.
D4 – Leakage – three year average	We increased the penalty rate from £0.103m to £0.400m.	We carried out a horizontal comparison of leakage across the industry. This identified that Anglian Water's penalty rate was one of the lowest in the industry. We therefore restored Anglian Water's penalty rate back to its December 2013 proposal of £0.400m per MI/day per year.
I1 – Mean Zonal	We set the PC level	We carried out a horizontal comparison of

PC/ODI affected	What we did	Why we did it
Compliance	<p>at 100.0% for 2017-18 to 2019-20.</p> <p>We set the penalty deadband at 99.96% from 2017-18.</p> <p>We set the penalty collar at 99.90% for 2017-18 to 2019-20.</p> <p>We raised the penalty rate by applying the company's maximum penalty to the revised penalty range.</p>	<p>mean zonal compliance across the industry. Our comparison identified that Anglian Water needs to have a more stretching performance commitment level in 2017-18, 2018-19 and 2019-20. It also identified that the company had one of the widest penalty ranges and lowest penalty rates in the industry.</p> <p>The company has defined Outcome Delivery Incentives for drinking water quality compliance with a penalty at less than 100%. This penalty represents an incentive to the company not to reduce its compliance with water quality measures. This threshold represents the point at which financial incentives will be applied to the company through the price setting process. All companies are subject to drinking water quality obligations regulated by the DWI, which are the overriding statutory obligations that a water company must comply with as part of their Section 37 obligations. The company's Board has confirmed as part of its business plan submission that it will comply with all relevant statutory obligations.</p>

Table AA4.3 Summary of interventions on wholesale wastewater outcomes, performance commitments and incentives

PC/ODI affected	What we did	Why we did it
A2 – Properties flooded internally from sewers – three year average (reduction)	<p>We introduced a reward for this performance commitment.</p> <p>We increased the penalty range by a factor of two.</p>	<p>We carried out a horizontal comparison of internal sewer flooding across the industry. This identified that Anglian Water was the only WaSC not to have a reward relating to internal sewer flooding. We are open to Anglian Water proposing a reward for this performance commitment.</p> <p>In this annex we have suggested a reward deadband, cap and rate which Anglian Water could choose to accept, or propose modifications to, as part of its</p>

PC/ODI affected	What we did	Why we did it
		representations on our draft determinations. We also identified that Anglian Water's penalty range was relatively small compared with other companies. We have intervened to double the penalty range by adjusting the penalty collar.
A3 – Properties flooded externally from sewers – three year average (reduction)	We increased the penalty range by a factor of four.	Anglian Water's penalty range was relatively small (22 properties) compared with its historical performance (around 4,700 properties per year) and other companies' penalty ranges. We have intervened to quadruple the penalty range by adjusting the penalty collar.
B1 – Value for money perception – variation from baseline against WASCs (wastewater)	We applied a condition requiring that the company does not earn a reward if its absolute score has gone down.	To protect customers from paying for a reward to Anglian Water when their perception of value for money of the company has gone down.

Table AA4.4 Summary of interventions on household retail outcomes, performance commitments and incentives

PC/ODI affected	What we did	Why we did it
We have not intervened on any household retail outcomes.		

Outcome delivery and reporting

In the [outcomes technical appendix](#), we outline a framework against which we have assessed Anglian Water's proposals in relation to outcome delivery and reporting.

The table below summarises Anglian Water's proposed approach to the measurement, reporting and governance of outcomes and our assessment of this approach.

Table AA4.5 Anglian Water’s proposals for outcome delivery and reporting

Anglian Water proposals	Our assessment
<p>In the June 2014 Business Plan submission, Anglian Water committed to publishing progress against its outcome commitments and specified outputs in the plan on an annual basis for customers. The company states that it has a track record of open reporting and holding themselves to account through its Love Every Drop goals and commitments, through its annual report and accounts, and website. The company further states that it will:</p> <ul style="list-style-type: none"> – include the metrics in its monthly board reports to check progress; – track progress of all regulatory commitments through its Regulatory Issues Group; – assign internal owners to each measure to manage performance and reporting; – annually assess performance in its ‘Yearbook’ – the internal summary of data and performance which it implemented to replace the June return; – continue to engage third party assurance on all aspects of the Yearbook, but particularly ODI measures, to a comparable standard as the June return (including audits of data, processes and governance); – engage third party assurance of any annual publication of results, either to the CEF or directly with customers; – include its performance against its regulatory commitments in its annual report and accounts; and – make information about its performance available on its website, along with justification for any variations. <p>Ultimately the company will submit an</p>	<p>In our methodology statement we set out our expectation that companies should demonstrate that their proposed PCs can be measured and recorded consistently and that they will have the appropriate governance and quality assurance processes in place to achieve this. We also expect companies to be transparent with customers about their performance against their outcomes and commitments.</p> <p>Anglian Water has provided sufficient evidence demonstrating the approach it will undertake to ensure the PCs will be measured and reported consistently, and the proposed governance and assurance processes. Therefore, we have accepted the company’s proposal.</p> <p>In time, we may develop further information requirements with regard to outcomes, as we review and change current requirements relating to performance indicators and each company’s annual risk and compliance statement.</p>

Anglian Water proposals	Our assessment
assessment of its performance to Ofwat during the next price review, supported by third party assurance, to give confidence that commitments have been met and the appropriate levels of rewards or penalties have been applied.	

In the remainder of this section, we provide the following information on each performance commitment we are proposing as part of this draft determination.

- The name and detailed definition of the performance commitment.
- The type of incentive.
- The performance commitment level.
- For financial incentives:
 - the limits on rewards and penalties (caps and collars) and neutral zones (deadbands) as applicable²; and
 - the incentive rates.
- Additional details on the measure.
- Where Ofwat has not accepted the company’s proposals, the nature of the intervention made is also explained.

Appendix 1 of our final methodology statement contains a number of worked examples that illustrate how the different incentive types will operate.

We have intervened in relation to a number of performance commitments proposed by the company. Where our intervention is to remove the performance commitment in question, details and reasoning are provided in Table AA4.6. Where we have amended the company’s proposed incentive but retained the performance commitment, we have intentionally set out our interventions below using a ~~strike through~~. What this means is that we have rejected the proposal that has been struck through and instead we have either used a different value or not included a value at all (for example, in the case of some rewards).

² In general, the cap or collar is the level of service at which the maximum penalty or reward occurs and a deadband is the level of service at which the incentive first applies. However, where a greater than or less than symbol precedes the figure this denotes that the maximum or initial incentive only occurs if service is greater than or less than this level.

Anglian Water will be able to finalise its proposed menu choice and affected ODI calibrations following our consideration of responses to these proposals.

Table AA4.6 Performance commitments proposed by the company that we have removed from this draft determination

Performance commitment	Reason for its removal
Wholesale water	
A1- Qualitative service incentive mechanism (SIM) score (water)	Anglian Water has not sufficiently justified why it should be adding further rewards and penalties to the qualitative part of SIM.
Wholesale wastewater	
A1 – Qualitative service incentive mechanism (SIM) score (wastewater)	Anglian Water has not sufficiently justified why it should be adding further rewards and penalties to the qualitative part of SIM.
Household retail	
n/a	

Table AA4.7 Performance commitments that we have added to this draft determination

Performance commitment	Reason for its addition
Wholesale water	
Water quality contacts	<p>We have removed Anglian Water’s two performance commitments on qualitative SIM. This has left Anglian Water with fewer performance commitments relating to customer service.</p> <p>We carried out a comparison of water quality contacts across the industry. This comparison identified that Anglian Water does not have a performance commitment that directly measures water quality contacts.</p> <p>We are requiring Anglian Water to adopt a performance commitment and outcome delivery penalty along the lines in the table below. We are open to Anglian Water proposing a reward for this new performance commitment provided the company justifies its proposal sufficiently.</p> <p>Performance commitment: complaints received from customers because they are dissatisfied with the taste, odour or colour of their</p>

Performance commitment	Reason for its addition						
Wholesale water							
	tap water per 1,000 customers.						
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
	PC	1.51	1.41	1.32	1.22	1.22	1.22
	Penalty Collar		2.73	2.73	2.44	2.44	2.44
	Penalty deadband		1.51	1.51	1.22	1.22	1.22
	Reward deadband	We are open to Anglian Water proposing a reward for this performance commitment. If Anglian Water proposes a reward the reward deadband would need to be at 1.22 in each year.					
	Reward cap						
		Incentive type	Performance level (number of contacts per year)		Incentive rate (£m/1,000 contacts/year)		
			Lower	Upper			
		Penalty	1.22	2.73	1.25		
	Reward	For Anglian Water to propose					
	We expect the company to consider this as part of its representations on our draft determination; we will consider Anglian Water's proposal for inclusion in our final determination for the company.						
Environmental compliance (wholesale water)	<p>Anglian Water has proposed wholesale water cost exclusions for the delivery of Restoring Sustainable Abstraction (RSA) schemes and for delivering Eels Regulations schemes as part of the National Environment Programme (NEP).</p> <p>To protect customers financially from non-delivery we are requiring Anglian Water to propose a new environmental compliance performance commitment within the wholesale water element to cover this special claim as part of its representations on our draft determination.</p> <p>We will consider Anglian Water's proposal for inclusion in our final determination for the company.</p>						

Performance commitment	Reason for its addition					
Wholesale water						
Wholesale wastewater						
Pollution incidents	<p>We carried out a horizontal review of the industry’s approach to pollution incidents. Our objective was to ensure that all customers have a similar level of protection in the event that a company underperforms.</p> <p>Anglian Water is the only WaSC not to propose a performance commitment that directly measures pollution incidents. We are therefore requiring the company to adopt a new performance commitment and outcome delivery penalty within the wholesale wastewater element to cover this, as part of it representations on our draft determination. We are open to Anglian Water proposing a reward for this new performance commitment provided the company justifies it proposal sufficiently.</p> <p>Performance commitment: pollution incidents (category 3)</p>					
	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	408	383	332	293	293	293
Penalty collar	For Anglian Water to propose penalty collar.					
Penalty deadband	408	408	293	293	293	
Reward deadband	We are open to Anglian Water proposing a reward for this performance commitment.					
Reward cap	If Anglian Water proposes a reward the reward deadband would need to be at 293 in each year.					

Performance commitment	Reason for its addition			
Wholesale water				
	Incentive type	Performance level (number of contacts per year)		Incentive rate (£m/incident/year)
		Lower	Upper	
	Penalty	293	For Anglian Water to propose	For Anglian Water to propose
	Reward	For Anglian Water to propose		
We will consider Anglian Water’s proposal for inclusion in our final determination for the company.				
Environmental compliance (wholesale wastewater)	<p>Anglian Water has significant expenditure relating to the Water Framework Directive (WFD) that is not covered by a performance commitment directly measuring the impact on water bodies.</p> <p>Anglian Water has proposed investment to allow for population growth, including Urban Wastewater Treatment Directive (UWWTD) minimum treatment standards. The company is proposing an extension of 24 wastewater treatment works to ensure no deterioration (under UWWTD) due to population growth.</p> <p>To protect customers financially from non-delivery we are requiring Anglian Water to propose a new environmental compliance performance commitment within the wholesale wastewater element to cover environmental compliance issues, as part of its representations on our draft determination.</p> <p>We will consider Anglian Water’s proposal for inclusion in our final determination for the company.</p>			
Household retail				
n/a				

Wholesale water outcome A: Satisfied customers

~~Performance commitment W-A1: Qualitative SIM score (water)~~

~~Detailed definition of performance measure:~~ The absolute score for the water element of the qualitative component of the service incentive mechanism (SIM).

~~Incentive type:~~ Financial – reward and penalty.

~~Performance commitments~~

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	Qualitative SIM score	4.40	4.60	4.60	4.60	4.60	4.60
Penalty collar	Qualitative SIM score		4.00	4.00	4.00	4.00	4.00
Penalty deadband							
Reward deadband							
Reward cap	Qualitative SIM score		4.90	4.90	4.90	4.90	4.90

~~Incentive rates~~

Incentive type	Performance levels (Qual SIM score)		Incentive rate (£m/Qual SIM score/year)
	Lower	Upper	

Incentive type	Performance levels (Qual SIM score)		Incentive rate (£m/Qual SIM score/year)
Penalty	4.00	4.59	8.333
Reward	4.61	4.90	16.666

Additional details

Necessary detail on measurement units	The absolute score for the water element of the qualitative component of the Service Incentive Mechanism (SIM) (1 to 5). Incentive rate is per whole unit.
Frequency of PC measurement and any use of averaging	Annually.
Timing and frequency of rewards/penalties	Annual assessment in AMP6, rewards or penalties applied to AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	Rewards are only earned if the overall company qualitative score (billing/water/sewerage) is among the top 3 WASC scores for that year. If there is a significant change to industry scores arising from a change in how this is measured in AMP6, the absolute targets may need adjusting.

Performance commitment W-A2: Water supply interruptions averaged over three years (reduction)

Detailed definition of performance measure: A reduction in ~~the total number of seconds minutes lost by customers for all interruptions lasting longer than three hours, divided by the number of connected properties for water (the same measure as in the current suite of Ofwat KPIs, although here expressed as a reduction in seconds), averaged over three consecutive years. A three year average is proposed as limited historic data is available, and the measure is to some extent variable due to factors outside our control (for example, weather and the actions of third parties).~~

Incentive type: Financial – reward and penalty.

Performance commitments

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	Mins/ prop/ year Sec/ total props	0 19.36	na 16.2	na 13.1	na 10	na 10	90 10
Penalty collar	Mins/ prop/ year Sec/ total props		20.56	20.56	11.2	11.2	0 11.2
Penalty deadband	Mins/ prop/ year Sec/ total props		19.36	19.36	10	10	75 10
Reward deadband	Mins/ prop/ year Sec/ total props		10	10	10	10	405 10
Reward cap	Mins/ prop/ year Sec/ total props		7.5	7.5	7.5	7.5	250 7.5

Incentive rates

Incentive type	Performance levels (reduction in min/total props)		Incentive rate (£m/min/total props/year)
	Lower	Upper	
Penalty	0	74	0.095
	10	20.56	5.70
Reward	406	250	-0.086
	7.5	10	2.9

Additional details

Necessary detail on measurement units	The total number of minutes seconds lost by customers for all interruptions lasting longer than three hours, divided by the number of connected properties for water (the same measure as in the current suite of Ofwat KPIs, although here expressed in seconds), averaged over three consecutive years .
Frequency of PC measurement and any use of averaging	The PC will be measured each year in line with the approach adopted by other companies. A three year average is proposed as limited historic data is available, and the measure is to some extent variable due to factors outside our control (for example, weather and the actions of third parties). Assessment in 2019-20.
Timing and frequency of rewards/penalties	Assessment of rewards or penalties made each year during AMP6 on 2019-20 performance and applied to annual AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19.
Any other information or clarifications relevant to correct application of incentive	

Performance commitment W-A3: Properties at risk of persistent low pressure

Detailed definition of performance measure: The number of properties deemed to be at risk of low pressure.

Incentive type: Financial – reward and penalty.

Performance commitments

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	No. props	517			na		257
Penalty collar	No. props				na		337
Penalty deadband	No. props				na		262
Reward deadband	No. props						252 230
Reward cap	No. props						150

Incentive rates

Incentive type	Performance levels (no. props)		Incentive rate (£m/no. props/year)
	Lower	Upper	
Penalty	337	263	0.030
Reward	251 230	150	0.025 0.015

Additional details

Necessary detail on measurement units	The number of properties deemed to be at risk of low pressure.
Frequency of PC measurement and any use of averaging	2019-20
Timing and frequency of rewards/penalties	Assessment of rewards or penalties made on 2019-20 performance, assessment of penalties made on 2017-18 and 2019-20 performance and applied to annual AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	One fifth of the total penalties over AMP6 apply to the intermediate 2017-18 performance commitment. Fourth fifths of the total penalties over AMP6 apply to the 2019-20 performance.

Wholesale water outcome B: Fair charges

Performance commitment W-B1: Value for money perception – variation from baseline against WASCs (Water)

Detailed definition of performance measure: This measure is based on the CCWater tracker survey question:

“How satisfied or dissatisfied are you with the value for money of water services in your area?”

On average, the company’s score for this question is 1% below the WASC average. This measure is the change from this baseline relative to the WASC average.

Incentive type: Financial – reward and penalty.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	0	0	0	0	0	0
Penalty collar	%		-20	-20	-20	-20	-20
Penalty deadband	%						
Reward deadband	%						
Reward cap	%		20	20	20	20	20

Incentive rates

Incentive type	Performance levels (%)		Incentive rate (£m/%/year)
	Lower	Upper	
Penalty	-20	-1	0.025
Reward	1	20	0.025

Additional details

<p>Necessary detail on measurement units</p>	<p>The survey result is expressed as a percentage. This measure is the difference between the company score and the WASC average (less the baseline adjustment for starting position). For example, if the company scores 75%, and the WASC average is 70%, this would be a 6% improvement on the baseline: $(75\% - (70\% - 1\%))$.</p>
<p>Frequency of PC measurement and any use of averaging</p>	<p>Variance from baseline to be measured annually.</p>
<p>Timing and frequency of rewards/penalties</p>	<p>Annual assessment in AMP6, rewards or penalties applied to AMP7 revenue.</p>
<p>Form of reward/penalty</p>	<p>Adjustment to revenue at PR19</p>
<p>Any other information or clarifications relevant to correct application of incentive</p>	<p>Anglian Water will not earn a reward if its absolute score has gone down.</p>

Wholesale water outcome C: Resilient services

Performance commitment W-C1: % of population supplied by single supply system

Detailed definition of performance measure: Our existing supply systems carry varying levels of resilience risk. Assessment of these risks is difficult and highly subjective. In contrast, a crude but objective indicator of a wide range of risks is the percentage of the population we supply which can only be served by a single supply system.

Incentive type: Financial – penalty only.

Performance commitments

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	27.5					24.7
Penalty collar	%						27.5
Penalty deadband	%						

Incentive rates

Incentive type	Performance levels (%)		Incentive rate (£m/%/year)
	Lower	Upper	
Penalty	27.5	24.8	0.088

Additional details

Necessary detail on measurement units	The percentage of the population we supply which can only be served by a single supply system.
Frequency of PC measurement and any use of averaging	2019-20
Timing and frequency of	Assessment of penalties made on 2019-20

rewards/penalties	performance and applied to annual AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	

Performance commitment W-C2: Frequency of service level restrictions (hosepipe bans)

Detailed definition of performance measure: This is a measure of the expected frequency of service restrictions (hosepipe bans). While no improvement is expected in AMP6, we will consider proposing an improvement in the level of service for AMP7, and so have included this within our suite of performance measures in anticipation of this.

Incentive type: Reputational.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	Freq / 10yrs	1					1

Additional details

Necessary detail on measurement units	This is a measure of the expected frequency of service restrictions (hosepipe bans). While no improvement is expected in AMP6, we will consider proposing an improvement in the level of service for AMP7, and so have included this within our suite of performance measures in anticipation of this.
Frequency of PC measurement and any use of averaging	2019-20

Any other information or clarifications relevant to correct application of incentive

Wholesale water outcome D: Supply meets demand

Performance commitment W-D1: Security of Supply Index (SoSI) – dry year annual average

Detailed definition of performance measure: A well established and understood measure in water resource management planning.

Incentive type: Reputational.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	SoSI	100					100

Additional details

Necessary detail on measurement units	A well established and understood measure in water resource management planning.
Frequency of PC measurement and any use of averaging	2019-20
Any other information or clarifications relevant to correct application of incentive	

Performance commitment W-D2: Security of Supply Index (SoSI) – critical period (peak) demand

Detailed definition of performance measure: A well established and understood measure in water resource management planning.

Incentive type: Reputational.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	SoSI	100					100

Additional details

Necessary detail on measurement units	A well established and understood measure in water resource management planning.
Frequency of PC measurement and any use of averaging	2019-20
Any other information or clarifications relevant to correct application of incentive	

Performance commitment W-D3: Per Property Consumption (PPC) reduction

Detailed definition of performance measure: Reduction in per property (household) consumption in litres/household/day (measured and unmeasured included) from the 2014-15 figure.

Incentive type: Financial – penalty only.

Performance commitments

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	l/hh/day	0					7
Penalty collar	l/hh/						0

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
	day						
Penalty deadband	l/hh/ day						

Incentive rates

Incentive type	Performance levels (l/hh/day)		Incentive rate (£m/l/hh/day/year)
	Lower	Upper	
Penalty	0	6	0.224

Additional details

Necessary detail on measurement units	Reduction in per property (household) consumption in litres/household/day (measured and unmeasured included).
Frequency of PC measurement and any use of averaging	2019-20
Timing and frequency of rewards/penalties	Assessment of penalties made on 2019-20 performance and applied to annual AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	

Performance commitment W-D4: Leakage – three year average

Detailed definition of performance measure: A three year average of the MI/d lost to leakage, including customer supply pipe leakage. Leakage performance is heavily weather dependent. In order to stand a good chance of meeting the annual

target at the end of March, we have to enter the winter months significantly below the target, so that a rise in leakage levels resulting from adverse winter weather can be accommodated. When severe weather occurs, such as the winter of 2010-11, it is very difficult to recover leakage levels, despite this preparation. When the winter is milder than anticipated, the leakage target is likely to be outperformed in that year. In both cases, because there is little time to adjust following the winter period before the end of the financial year, there is likely to be significant variability in leakage performance. A three year average helps to smooth performance and allows the measure to more closely reflect management performance at controlling leakage.

Incentive type: Financial – reward and penalty.

Performance commitments

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	MI/d	192	192	192	192	192	192
Penalty collar	MI/d		211	211	211	211	211
Penalty deadband	MI/d						
Reward deadband	MI/d						
Reward cap	MI/d		191	187	182	177	172

Incentive rates

Incentive type	Performance levels (MI/d)		Incentive rate (£m/MI/d/year)
	Lower	Upper	
Penalty	211	193	0.403 0.400
Reward 1	191	177	0.509
Reward 2	191	172	0.509

Additional details

Necessary detail on	A three year average of the MI/d lost to leakage.
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measurement units	
Frequency of PC measurement and any use of averaging	3 year average assessed annually.
Timing and frequency of rewards/penalties	Assessment of penalties or rewards made annually at time t+1 (t, t-1, t-2 averaged), with in period revenue adjustment at t+2.
Form of reward/penalty	Adjustment to in-period revenue.
Any other information or clarifications relevant to correct application of incentive	If there is a significant change to how this is measured in AMP6, the absolute targets may need adjusting.

Wholesale water outcome E: Flourishing environment

Performance commitment W-E1: Percentage of SSSIs (by area) with favourable status

Detailed definition of performance measure: This is the percentage of our total SSSI hectares which are in favourable status.

Incentive type: Reputational.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	49					50

Additional details

Necessary detail on measurement units	This is the percentage of our total SSSI hectares which are in favourable status.
Frequency of PC measurement and any use of averaging	2019-20
Any other information or clarifications relevant to correct application of incentive	

Wholesale water outcome F: A smaller footprint

Performance commitment W-F1: Operational carbon (% reduction from 2015 baseline)

Detailed definition of performance measure: The percentage reduction in real terms in operational carbon emissions across the entire business measured in t/CO₂e from a 2014-15 baseline.

Incentive type: Reputational.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	0					7

Additional details

Necessary detail on measurement units	The percentage reduction in real terms in operational carbon emissions across the entire business measured in t/CO ₂ e from a 2015 baseline.
Frequency of PC measurement and any use of averaging	2019-20
Any other information or clarifications relevant to correct application of incentive	

Performance commitment W-F2: ~~Operational~~ Embodied carbon (% reduction from ~~2015~~ 2010 baseline)

Detailed definition of performance measure: The percentage reduction in embodied carbon emissions across the entire business measured in t/CO₂e from a

2010 baseline.

Incentive type: Reputational.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	50					60

Additional details

Necessary detail on measurement units	The percentage reduction in embodied carbon emissions across the entire business measured in t/CO2e from a 2010 baseline.
Frequency of PC measurement and any use of averaging	2019-20
Any other information or clarifications relevant to correct application of incentive	

Wholesale water outcome G: Caring for communities

Performance commitment W-G1: Survey of community perception

Detailed definition of performance measure: The company will develop a survey of customer perception of the entire business (wholesale and retail) over a number of factors around how the communities in which we operate perceive us. This will include such factors as noise, odour or traffic disruption. The survey will be designed and run by a specialist research company on the company's behalf.

Incentive type: Reputational.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%						Improved

Additional details

Necessary detail on measurement units	An improvement in community perception.
Frequency of PC measurement and any use of averaging	2019-20
Any other information or clarifications relevant to correct application of incentive	

Wholesale water outcome H: Investing for tomorrow

Performance commitment W-H1: Water infrastructure

Detailed definition of performance measure: An assessment of serviceability of water infrastructure assets across a range of indicators, resulting in a GREEN, AMBER or RED assessment. Data will be collected and analysed annually across 4 sub-services, and penalties will automatically apply annually (as adjustments to AMP7 revenue).

Incentive type: Financial – penalty only.

Performance commitments

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	RAG	Stable	Green	Green	Green	Green	Green
Penalty collar	RAG						
Penalty deadband	RAG						

Incentive rates

Incentive type	Performance levels (RAG)		Incentive rate
	Lower	Upper	
Penalty	Red	Amber	An automatic mechanism has been designed by the company based on the number of sub-measures which are less than Green status.

Additional details

Necessary detail on measurement units	An assessment of serviceability of water infrastructure assets across a range of indicators, resulting in a GREEN, AMBER or RED assessment. Data will be collected and analysed annually across four sub-services, and penalties will automatically apply annually (as adjustments to AMP7 revenue).
Frequency of PC measurement and any use of averaging	Annually
Timing and frequency of rewards/penalties	Assessment of penalties made annually and applied to AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	An automatic mechanism for calculating penalties has been designed by the company based on sub-measures, reference levels and upper control limits.

Performance commitment W-H2: Water non-infrastructure

Detailed definition of performance measure: An assessment of serviceability of water non-infrastructure assets across a range of indicators, resulting in a GREEN, AMBER or RED assessment. Data will be collected and analysed annually across four sub-services, and penalties will automatically apply annually (as adjustments to AMP7 revenue).

Incentive type: Financial – penalty only.

Performance commitments

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	RAG	Stable	Green	Green	Green	Green	Green
Penalty collar	RAG						

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Penalty deadband	RAG						

Incentive rates

Incentive type	Performance levels (RAG)		Incentive rate
	Lower	Upper	
Penalty	Red	Amber	An automatic mechanism has been designed by the company based on the number of sub-measures which are less than Green status.

Additional details

Necessary detail on measurement units	An assessment of serviceability of water non-infrastructure assets across a range of indicators, resulting in a GREEN, AMBER or RED assessment. Data will be collected and analysed annually across four sub-services, and penalties will automatically apply annually (as adjustments to AMP7 revenue).
Frequency of PC measurement and any use of averaging	Annually
Timing and frequency of rewards/penalties	Assessment of penalties made annually and applied to AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	An automatic mechanism for calculating penalties has been designed by the company based on sub-measures, reference levels and upper control limits.

Wholesale water outcome I: Safe clean water

Performance commitment W-11: Mean Zonal compliance

Detailed definition of performance measure: Mean Zonal Compliance, as defined by the DWI and published annual annually in the Chief Inspector's Report.

Incentive type: Financial – penalty only.

Performance commitments

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	99.96	99.96	99.96	99.96 100.00	99.96 100.00	99.96 100.00
Penalty collar	%				n/a 99.90	n/a 99.90	90.00 99.90
Penalty deadband	%				n/a 99.96	n/a 99.96	99.96

Incentive rates

Incentive type	Performance levels (%)		Incentive rate (£m/%/year)
	Lower	Upper	
Penalty	90.00	99.95	0.105
	99.90	99.96	17.4125

Additional details

Necessary detail on measurement units	Mean Zonal Compliance, as defined by the DWI and published annual in the Chief Inspector's Report.
Frequency of PC measurement and any use of averaging	Annually.
Timing and frequency of	Annual assessment in AMP6, penalties applied to

rewards/penalties	AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	

Wholesale wastewater outcome A: Satisfied customers

~~Performance commitment S-A1: Qualitative SIM score (wastewater)~~

~~Detailed definition of performance measure:~~ The absolute score for the wastewater element of the qualitative component of the Service Incentive Mechanism (SIM).

~~Incentive type:~~ Financial – reward and penalty.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PG	Qualitative SIM score	4.53	4.60	4.60	4.60	4.60	4.60
Penalty collar	Qualitative SIM score		4.00	4.00	4.00	4.00	4.00
Penalty deadband							
Reward deadband							
Reward cap	Qualitative SIM score		4.90	4.90	4.90	4.90	4.90

Incentive rates

Incentive type	Performance levels (Qual SIM score)		Incentive rate (£m/Qual SIM score/year)
	Lower	Upper	
Penalty	4.00	4.59	8.333
Reward	4.61	4.90	16.666

Additional details

Necessary detail on measurement units	The absolute score for the sewerage element of the qualitative component of the Service Incentive Mechanism (SIM) (1 to 5). Incentive rate is per whole unit.
Frequency of PC measurement and any use of averaging	Annually.
Timing and frequency of rewards/penalties	Annual assessment in AMP6, rewards or penalties applied to AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	Rewards are only earned if the overall company qualitative score (billing/water/sewerage) is among the top 3 WASC scores for that year. If there is a significant change to industry scores arising from a change in how this is measured in AMP6, the absolute targets may need adjusting.

Performance commitment S-A2: Properties flooded internally from sewers – three year average (reduction)

Detailed definition of performance measure: Reduction in the three-year average number of properties flooded internally from sewers. This measure includes severe weather events and flooding from transferred assets.

Incentive type: Financial – penalty only.

Performance commitments

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	No. props	0					27
Penalty collar	No. props						<u>0</u> -24
Penalty deadband	No. props						24
Reward deadband	No. props						30*
Reward cap	No. props						78*

Incentive rates

Incentive type	Performance levels (No. props)		Incentive rate (£m/prop/year)
	Lower	Upper	
Penalty	0 -24	23 24	0.042
Reward	30*	78*	0.036*

* We are open to Anglian Water proposing a reward for this performance commitment. We have suggested a reward deadband, cap and rate which Anglian Water could choose to accept, or propose modifications to, as part of its representations on our draft determinations.

Additional details

Necessary detail on measurement units	Reduction from 2014-15 three year average in the number of properties flooded internally.
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Frequency of PC measurement and any use of averaging	2019-20. Three year average.
Timing and frequency of rewards/penalties	Assessment of rewards or penalties made on 2019-20 performance and applied to annual AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	

Performance commitment S-A3: Properties flooded externally from sewers – three year average (reduction)

Detailed definition of performance measure: Reduction in the three-year average number of properties flooded internally from sewers. This measure includes severe weather events and flooding from transferred assets.

Incentive type: Financial – penalty only.

Performance commitments

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	No. props	0					22
Penalty collar	No. props						0 -66
Penalty deadband	No. props						n/a 21

Incentive rates

Incentive type	Performance levels (No. props)		Incentive rate (£m/prop/year)
	Lower	Upper	
Penalty	0 -66	n/a 21	0.023

Additional details

Necessary detail on measurement units	Reduction from 2014-15 three year average in the number of properties flooded externally.
Frequency of PC measurement and any use of averaging	2019-20. Three year average.
Timing and frequency of rewards/penalties	Assessment of penalties made on 2019-20 performance and applied to annual AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	

Performance commitment S-A4: Percentage of sewerage capacity schemes incorporating sustainable solutions for example, SuDS

Detailed definition of performance measure: Of the schemes we undertake to deal with sewerage capacity issues in AMP6 (supply demand or flooding schemes), we wish to encourage the use of sustainable solutions which might include SuDS.

Incentive type: Reputational.

Performance commitments

	Starting level	Committed performance levels

	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%						25

Additional details

Necessary detail on measurement units	The percentage of the number of schemes completed in AMP6.
Frequency of PC measurement and any use of averaging	2019-20.
Any other information or clarifications relevant to correct application of incentive	

Wholesale wastewater outcome B: Fair charges

Performance commitment S-B1: Value for money perception

Detailed definition of performance measure: This measure is based on the CCWater tracker survey question:

“How satisfied or dissatisfied are you with the value for money of sewerage services in your area?”

On average, the company’s score for this question is 2% below the WASC average. This measure is the change from this baseline relative to the WASC average.

Incentive type: Financial – reward and penalty.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	0	0	0	0	0	0
Penalty collar	%		-20	-20	-20	-20	-20
Penalty deadband	%						
Reward deadband	%						
Reward cap	%		20	20	20	20	20

Incentive rates

Incentive type	Performance levels (%)		Incentive rate (£m/%/year)
	Lower	Upper	
Penalty	-20	-1	0.025
Reward	1	20	0.025

Additional details

<p>Necessary detail on measurement units</p>	<p>The survey result is expressed as a percentage. This measure is the difference between the company score and the WASC average (less the baseline adjustment for starting position). For example, if the company scores 75%, and the WASC average is 70%, this would be a 7% improvement on the baseline: $(75\% - (70\% - 2\%))$.</p>
<p>Frequency of PC measurement and any use of averaging</p>	<p>Variance from baseline to be measured annually.</p>
<p>Timing and frequency of rewards/penalties</p>	<p>Annual assessment in AMP6, rewards or penalties applied to AMP7 revenue.</p>
<p>Form of reward/penalty</p>	<p>Adjustment to revenue at PR19</p>
<p>Any other information or clarifications relevant to correct application of incentive</p>	<p>Anglian Water will not earn a reward if its absolute score has gone down.</p>

Wholesale wastewater outcome C: Flourishing environment

Performance commitment S-C1: Percentage of bathing waters attaining excellent status

Detailed definition of performance measure: This is the percentage of bathing waters attaining excellent status.

Incentive type: Financial – reward and penalty.

Performance commitments

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	58%					67%
Penalty collar	%						58%
Penalty deadband	%						
Reward deadband	%						
Reward cap	%						75%

Incentive rates

Incentive type	Performance levels (%)		Incentive rate (£m/%/year)
	Lower	Upper	
Penalty	58%	66%	0.373
Reward	68%	75%	0.373

Additional details

Necessary detail on measurement units	This is the percentage of bathing waters attaining excellent status.
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Frequency of PC measurement and any use of averaging	2019-20.
Timing and frequency of rewards/penalties	Assessment of rewards or penalties made on 2019-20 performance and applied to annual AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	

Performance commitment S-C2: Percentage of SSSIs (by area) with favourable status

Detailed definition of performance measure: This is the percentage of our total SSSI hectares which are in favourable status.

Incentive type: Reputational

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	49					50

Additional details

Necessary detail on measurement units	This is the percentage of our total SSSI hectares which are in favourable status.
Frequency of PC measurement and any use of averaging	2019-20
Any other information or clarifications relevant to correct application of incentive	

Wholesale wastewater outcome D: A smaller footprint

Performance commitment S-D1: Operational carbon (% reduction from 2015 baseline)

Detailed definition of performance measure: The percentage reduction in real terms in operational carbon emissions across the entire business measured in t/CO₂e from a 2015 baseline.

Incentive type: Reputational

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	0					7

Additional details

Necessary detail on measurement units	The percentage reduction in real terms in operational carbon emissions across the entire business measured in t/CO ₂ e from a 2015 baseline.
Frequency of PC measurement and any use of averaging	2019-20
Any other information or clarifications relevant to correct application of incentive	

Performance commitment S-D2: Operational Embodied carbon (% reduction from 2015 2010 baseline)

Detailed definition of performance measure: The percentage reduction in embodied carbon emissions across the entire business measured in t/CO₂e from a

2010 baseline.

Incentive type: Reputational

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	50					60

Additional details

Necessary detail on measurement units	The percentage reduction in embodied carbon emissions across the entire business measured in t/CO ₂ e from a 2010 baseline.
Frequency of PC measurement and any use of averaging	2019-20
Any other information or clarifications relevant to correct application of incentive	

Wholesale wastewater outcome E: Caring for communities

Performance commitment S-E1: Survey of community perception

Detailed definition of performance measure: The company will develop a survey of customer perception of the entire business (wholesale and retail) over a number of factors around how the communities in which we operate perceive us. This will include such factors as noise, odour or traffic disruption. The survey will be designed and run by a specialist research company on the company's behalf.

Incentive type: Reputational

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%						Improved

Additional details

Necessary detail on measurement units	An improvement in community perception.
Frequency of PC measurement and any use of averaging	2019-20.
Any other information or clarifications relevant to correct application of incentive	

Wholesale water outcome F: Investing for tomorrow

Performance commitment S-F1: Sewerage infrastructure

Detailed definition of performance measure: An assessment of serviceability of sewerage infrastructure assets across a range of indicators, resulting in a GREEN, AMBER or RED assessment. Data will be collected and analysed annually across four sub-services, and penalties will automatically apply annually (as adjustments to AMP7 revenue).

Incentive type: Financial – penalty only

Performance commitments

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	RAG	Stable	Green	Green	Green	Green	Green
Penalty collar	RAG						
Penalty deadband	RAG						

Incentive rates

Incentive type	Performance levels (RAG)		Incentive rate
	Lower	Upper	
Penalty	Red	Amber	An automatic mechanism has been designed by the company based on the number of sub-measures which are less than Green status.

Additional details

Necessary detail on measurement units	An assessment of serviceability of sewerage infrastructure assets across a range of indicators, resulting in a GREEN, AMBER or RED assessment. Data will be collected and analysed annually across four sub-services, and penalties will automatically apply annually (as adjustments to AMP7 revenue).
Frequency of PC measurement and any use of averaging	Annually
Timing and frequency of rewards/penalties	Assessment of penalties made annually and applied to AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	An automatic mechanism for calculating penalties has been designed by the company based on sub-measures, reference levels and upper control limits.

Performance commitment S-F2: Sewerage non-infrastructure

Detailed definition of performance measure: An assessment of serviceability of sewerage non-infrastructure assets across a range of indicators, resulting in a GREEN, AMBER or RED assessment. Data will be collected and analysed annually across four sub-services, and penalties will automatically apply annually (as adjustments to AMP7 revenue).

Incentive type: Financial – penalty only

Performance commitments

	Unit	Starting level	Committed performance levels				
			2014-15	2015-16	2016-17	2017-18	2018-19
PC	RAG	Stable	Green	Green	Green	Green	Green
Penalty collar	RAG						

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Penalty deadband	RAG						

Incentive rates

Incentive type	Performance levels (RAG)		Incentive rate
	Lower	Upper	
Penalty	Red	Amber	An automatic mechanism has been designed by the company based on the number of sub-measures which are less than Green status.

Additional details

Necessary detail on measurement units	An assessment of serviceability of sewerage non-infrastructure assets across a range of indicators, resulting in a GREEN, AMBER or RED assessment. Data will be collected and analysed annually across four sub-services, and penalties will automatically apply annually (as adjustments to AMP7 revenue).
Frequency of PC measurement and any use of averaging	Annually
Timing and frequency of rewards/penalties	Assessment of penalties made annually and applied to AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	An automatic mechanism for calculating penalties has been designed by the company based on sub-measures, reference levels and upper control limits.

Retail outcome A: Satisfied customers

Performance commitment R-A1: Qualitative SIM score (retail)

Detailed definition of performance measure: Relative rank of our qualitative SIM score (billing element) among WASCs. The commitment is to remain among the top three WASCs.

Incentive type: Reputational.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	WASC rank	3 rd +	3 rd +	3 rd +	3 rd +	3 rd +	3 rd +

Additional details

Necessary detail on measurement units	Relative rank of our qualitative SIM score (billing element) among WASCs.
Frequency of PC measurement and any use of averaging	Annual
Any other information or clarifications relevant to correct application of incentive	

Performance commitment R-A2: Service Incentive Mechanism (SIM)

Detailed definition of performance measure: The SIM will continue to apply as a comparative financial incentive according to the rules set by Ofwat. The entire incentive will be applied to the retail control, but the company will then internally

allocate the incentive roughly proportional to costs for retail, sewerage and water.

Incentive type: Financial – reward and penalty.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	Nr	85	Comparative measure				
Penalty collar							
Penalty deadband							
Reward deadband							
Reward cap							

Incentive rates

Incentive type	Performance levels		Incentive rate
	Lower	Upper	
Penalty 1			Up to -1% of revenue in total
Reward			Up to + 0.5% of revenue in total

Additional details

Necessary detail on measurement units	As specified by Ofwat to operate the SIM
Frequency of PC measurement and any use of averaging	Annual
Timing and frequency of rewards/penalties	Annual assessment in AMP6, rewards or penalties applied to AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	

Performance commitment R-A3: Customer Satisfaction Index prepared by UK Institute of Customer Service

Detailed definition of performance measure: The company has recently begun participating in the UK Institute of Customer Service Customer Satisfaction Index. This is a new measure for the company and includes a number of possible metrics. The company is currently base-lining these metrics to understand which are the most appropriate comparators for benchmarking its performance. The commitment is to target upper quartile performance on an appropriate metric among utility providers participating in the index.

Incentive type: Reputational.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	tbc	tbc					Upper quartile utility

Additional details

Necessary detail on measurement units	As defined by UK Institute of Customer Service Customer Satisfaction Index
Frequency of PC measurement and any use of averaging	2019-20
Any other information or clarifications relevant to correct application of incentive	

Retail outcome B: Fair charges

Performance commitment R-B1: Fairness of bills perception – variation from baseline against WASCs

Detailed definition of performance measure: This measure is based on the CCWater tracker survey question:

“How much do you agree or disagree that the water and sewerage charges you pay are fair?”

On average, the company’s score for this question is 3% below the WASC average. This measure is the change from this baseline relative to the WASC average.

Incentive type: Financial – reward and penalty.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	0	0	0	0	0	0
Penalty collar	%		-20	-20	-20	-20	-20
Penalty deadband	%						
Reward deadband	%						
Reward cap	%		20	20	20	20	20

Incentive rates

Incentive type	Performance levels (%)		Incentive rate (£m/%/year)
	Lower	Upper	
Penalty	-20	-1	0.025
Reward	1	20	0.025

Additional details

Necessary detail on measurement units	The survey result is expressed as a percentage. This measure is the difference between the company score and the WASC average (less the baseline adjustment for starting position). For example, if the company scores 75%, and the WASC average is 70%, this would be an 8% improvement on the baseline: $(75\% - (70\% - 3\%))$.
Frequency of PC measurement and any use of averaging	Variance from baseline to be measured annually.
Timing and frequency of rewards/penalties	Annual assessment in AMP6, rewards or penalties applied to AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or clarifications relevant to correct application of incentive	

Performance commitment R-B2: Affordability perception – variation from baseline against WASCs

Detailed definition of performance measure: This measure is based on the CCWater tracker survey question:

“How much do you agree or disagree that the water and/or sewerage charges you pay are affordable to you?”

On average, the company’s score for this question is 2% below the WASC average. This measure is the change from this baseline relative to the WASC average.

Incentive type: Financial – reward and penalty.

Performance commitments

	Unit	Starting level	Committed performance levels				
		2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	0	0	0	0	0	0
Penalty collar	%		-20	-20	-20	-20	-20
Penalty deadband	%						
Reward deadband	%						
Reward cap	%		20	20	20	20	20

Incentive rates

Incentive type	Performance levels (%)		Incentive rate (£m/%/year)
	Lower	Upper	
Penalty	-20	-1	0.025
Reward	1	20	0.025

Additional details

Necessary detail on measurement units	The survey result is expressed as a percentage. This measure is the difference between the company score and the WASC average (less the baseline adjustment for starting position). For example, if the company scores 75%, and the WASC average is 70%, this would be an 7% improvement on the baseline: (75% – (70%-2%)).
Frequency of PC measurement and any use of averaging	Variance from baseline to be measured annually.
Timing and frequency of rewards/penalties	Annual assessment in AMP6, rewards or penalties applied to AMP7 revenue.
Form of reward/penalty	Adjustment to revenue at PR19
Any other information or	

clarifications relevant to correct application of incentive

Wholesale water outcome C: A smaller footprint

Performance commitment R-C1: Operational carbon (% reduction from 2015 baseline)

Detailed definition of performance measure: The percentage reduction in real terms in operational carbon emissions across the entire business measured in t/CO₂e from a 2015 baseline.

Incentive type: Reputational.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	0					7

Additional details

Necessary detail on measurement units	The percentage reduction in real terms in operational carbon emissions across the entire business measured in t/CO ₂ e from a 2015 baseline.
Frequency of PC measurement and any use of averaging	
Any other information or clarifications relevant to correct application of incentive	

Performance commitment R-C2: Operational Embodied-carbon (% reduction from 2015 2010 baseline)

Detailed definition of performance measure: The percentage reduction in embodied carbon emissions across the entire business measured in t/CO₂e from a

2010 baseline.

Incentive type: Reputational.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%	50					60

Additional details

Necessary detail on measurement units	The percentage reduction in embodied carbon emissions across the entire business measured in t/CO2e from a 2010 baseline.
Frequency of PC measurement and any use of averaging	
Any other information or clarifications relevant to correct application of incentive	

Wholesale water outcome D: Caring for communities

Performance commitment R-D1: Survey of community perception

Detailed definition of performance measure: The company will develop a survey of customer perception of the entire business (wholesale and retail) over a number of factors around how the communities in which we operate perceive us. This will include such factors as noise, odour or traffic disruption. The survey will be designed and run by a specialist research company on the company's behalf.

Incentive type: Reputational.

Performance commitments

		Starting level	Committed performance levels				
	Unit	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
PC	%						Improved

Additional details

Necessary detail on measurement units	An improvement in community perception.
Frequency of PC measurement and any use of averaging	2019-20
Any other information or clarifications relevant to correct application of incentive	

Ofwat (The Water Services Regulation Authority) is a non-ministerial government department. We are responsible for making sure that the water sector in England and Wales provides customers with a good quality and efficient service at a fair price.



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