

# Information notice

IN 16/07 May 2016

ofwat

This is a formal document that alerts our stakeholders to a change in the way that we regulate the water sector in England and Wales.

## Changes to outcomes in the 2014 price review company-specific appendices

This information notice explains our policy in relation to requests for changes to outcomes, performance commitments (PCs) and outcome delivery incentives (ODIs).

We published our final determinations for the 2014 price review (PR14) over a year ago in December 2014. In recent months a number of water companies have raised issues with us relating to the outcomes, PCs and ODIs that we published in the company-specific appendices to the PR14 final determinations (“PR14 company-specific appendices”).

### Background

We introduced outcomes, PCs and ODIs at PR14. Outcomes are those aspects of water and waste water services that customers and society care about. PCs are the commitments companies make about the service levels they intend to deliver in order to make progress on their outcomes. ODIs are the rewards and penalties that encourage companies to deliver their PCs. ODIs can be financial or reputational.

### Corrections to outcomes, PCs and ODIs

Our decisions on outcomes, PCs and ODIs at PR14 are final. These decisions were made

after considering company business plans, discussions with companies and public consultation on our draft determinations. Where a company has brought to our attention an error in its outcomes, and we have considered it to be an unambiguous error, we have corrected the error by issuing a corrigendum on our website next to the PR14 company-specific appendices.

Our expectation is that all such errors will have been brought to our attention by now as we made our PR14 final determinations over a year ago. If, however, a company has found an error which it has not yet brought to our attention and the company wants to raise it with Ofwat, the company should write directly

to David Black, Senior Director for Water 2020, explaining:

- what the error is;
- why it is an unambiguous error;
- why the error has only been identified at this point;
- what correction the company considers is necessary to rectify the error; and
- how the company has engaged with its customers and other relevant organisations on the proposed correction.

We will consider the explanation and decide whether the error is unambiguous, if a correction is necessary and what correction is necessary. We will also look for independent assurance from the company's Customer Challenge Group (CCG) that the company has appropriately engaged its customers and that this is reflected in the company's proposed correction.

## Major scheme PCs and ODIs

In relation to major scheme PCs and ODIs the final price control determination notice: policy chapter A2 – outcomes explains (on page 67) that we will undertake an additional assessment of incentives regarding major scheme non-delivery penalties when they are due to be applied to determine the circumstances around non-delivery and the extent of non-delivery. We explain that the penalties for non-delivery will apply unless a water company can demonstrate that it has delivered an alternative outcome that delivers greater benefit to customers or that the statutory requirement driving the scheme has been removed. Policy chapter A2 also sets out the approach for scheme-specific incentives regarding delay.

Our principles for assessing major schemes, including the ones just mentioned, are set out on pages 27 and 28 of the PR14 reconciliation rulebook policy document. In particular we state that: "In case of inconsistencies, the final determinations and any pre-acceptance clarifications of those determinations will take precedence over any other documentation."

## Performance commitments under development

In the PR14 company-specific appendices there were 24 PCs which were under development or where the appendix explicitly mentioned a future change would be made to the PC. A number of these referred to the service incentive mechanism (SIM) for which the methodology has now been decided and the abstraction incentive mechanism (AIM) for which guidelines have now been published. We now consider the SIM and AIM PCs to be finalised. Where the PCs relate to other areas the process for developing the PC during 2015-20 is set out in the PR14 company-specific appendix. We expect companies to follow the development approach set out in the PR14 company-specific appendices including following the outcome delivery and reporting process which is also set out in those appendices.

## Improvements to outcomes during 2015-20

Several companies have identified improvements they would like to make to their PCs. For example, improvements in the definition used or the methodology underlying the PC.

The Ofwat PR14 reconciliation rulebook explains how we expect to make adjustments to revenue and the regulatory capital value (RCV) at the 2019 Price Review (PR19) to reflect companies' performance during 2015-20, including on financial ODIs. We expect companies to use the definitions and methodologies for their PCs and ODIs as set out in their PR14 company-specific appendices for reconciliation purposes.

If a company suggests an improvement to a PC we expect it to follow the process set out below:

1. The company should engage with its customers and other stakeholders referred to in its outcome delivery and reporting process on why the new measure represents an improvement for customers. We expect CCGs to independently challenge the company on the quality of this engagement.
2. The company should capture information on its new measure in addition to the PR14 company-specific appendix measure.
3. The company should report both measures to their customers, CCG and other stakeholders on an on-going basis as part of its outcome delivery and reporting process set out in its PR14 company-specific appendix.
4. At PR19 it will be up to a company to provide clear and compelling evidence on why the new measure represents a material improvement for customers and why it should be used for reconciliation purposes instead of the measure in the PR14 company-specific appendix. We expect CCGs to provide independent assurance to us on the quality of this engagement and the degree to which the results of this engagement are reflected in the company's proposal.
5. The PR14 final determination definition of a PC and ODI remains the default position we will use for reconciling 2015-20 performance at PR19. We will use the PR14 company-specific appendix measure if a company has not provided clear and compelling evidence that there are material benefits to customers of using the new definition for reconciliation purposes.

## Enquiries

If you have any questions about this information notice please email [jon.ashley@ofwat.gsi.gov.uk](mailto:jon.ashley@ofwat.gsi.gov.uk)

## More information

[The company-specific appendices to the PR14 final determinations](#), December 2014,

[Final price control determination notice: policy chapter A2 – outcomes](#), December 2014,

[The PR14 reconciliation rulebook policy document](#), July 2015,

Ofwat (The Water Services Regulation Authority) is a non-ministerial government department. We regulate the water sector in England and Wales. Our vision is to be a trusted and respected regulator, working at the leading edge, challenging ourselves and others to build trust and confidence in water.

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Printed on 75% minimum de-inked post-consumer waste paper  
May 2016

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