PR19 Developer Services Measure of Experience (D-MeX): Policy decisions for the D-MeX shadow year 2019-2020

Ofwat

Contents

1. About this document

The December 2017 PR19 Final Methodology[1] ('the PR19 Final Methodology') set out our decision to introduce a new incentive mechanism at PR19 called the **developer services measure of experience (D-MeX)**. D-MeX is a mechanism to incentivise water companies to provide an excellent customer experience for developer services (new connections) customers.

After we published the PR19 Final Methodology, we appointed Navigator Research and its sub-contractor Allto Consulting ('Allto') to pilot D-MeX. The recommendations from Allto, as well as the views of stakeholders, informed our decisions for the shadow year. The D-MeX shadow year will run from 1 May 2019 to 31 March 2020.

This document outlines the key features of D-MeX from the PR19 Final Methodology, explains the policy decisions that we have taken for the shadow year and details outstanding issues which will be tested during the shadow year.[2] This document is structured as follows.

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[1] Delivering Water 2020: Our final methodology for the 2019 price review: https://www.ofwat.gov.uk/publication/delivering-water-2020-final-methodology-2019-price-review/. The summarised features of D-MeX are in this document.
[2] Incentive design decisions for the 2020-2025 period, will be informed by shadow year data gathered prior to publication of the Final Determinations.

Following the results of the pilot, the shadow year will provide an opportunity to further develop and test the methodology for how D-MeX will be run during the 2020-2025 period. Particularly for D-MeX, the pilot year focussed on survey design and we will use the shadow year to work with stakeholders to develop the incentive design elements.

The PR19 Final Methodology stated that we would finalise the D-MeX methodology between April and August 2019; we have decided to change this timetable. Having conducted the pilots, we have identified specific areas that need to be tested in the shadow year. We will engage and consult with stakeholders as necessary during the shadow year.

We plan to publish our decisions on D-MeX incentive design in the PR19 Final Determinations in December 2019. As set out in the PR19 Final Methodology, final D-MeX guidance for companies will be published by March 2020 ahead of D-MeX becoming operational from 1 April 2020. See Section 4 for more detail on what we propose to do in the shadow year and our timetable.

This document is published as part of a set of documents on C-MeX and D-MeX. These include:

Document Name	Author	Location
PR19 C-MeX guidance for the C-MeX shadow year 2019 2020	Ofwat	Here
PR19 D-MeX guidance for the D-MeX shadow year 2019 2020	Ofwat	Here
PR19 C-MeX Policy decisions for the C-MeX shadow year 2019 2020	Ofwat	Here
C-MeX Pilot For PR19	Allto	Here
D-MeX Pilot For PR19	Allto	Here

2. Introduction

The developer services measure of experience (D-MeX) is a mechanism to incentivise water companies to provide an excellent customer experience for developer services (new connections) customers. These customers include small and large property developers, self-lay providers (SLPs)[3], and those with new appointments and variations (NAVs).[4]

2.1 Background

The Service Incentive Mechanism (SIM), was introduced in 2010, to provide a reputational and financial incentive to encourage water companies to provide excellent customer service to residential (household) customers. There is evidence that the SIM has driven customer service improvements since its introduction.

However, there are limitations with SIM including that it does not address the customer service experience of developer services customers.

Developer services customers have historically raised concerns about the service they receive from water companies. In 2014, Water UK developed a set of comparative metrics (Levels of Service or 'LoS') as a reputational incentive for the industry. While reported performance against the metrics has improved substantially, customers still raise concerns about poor quality services from water companies.

Therefore, in July 2017 we consulted on a set of mechanisms aimed at incentivising water companies to provide excellent customer service for residential customers and developer services customers.[5] Following further development through separate

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[3] A developer can choose to "self-lay" any contestable works for a development site using an accredited contractor. The incumbent will subsequently take over responsibility for (adopt) the self-laid infrastructure.
[4] New Appointments and Variations (NAVs). Under the NAV regime a company can apply to Ofwat for a licence to replace the appointed undertaker as the monopoly provider of water and/or wastewater services for a specific site. The majority of applications are for new residential and mixed-use developments. A developer can choose between the incumbent, a self-lay provider or a NAV in order to provide connection services for a new development site.
[5] Delivering Water 2020: consultation on PR19 methodology - July 2017 https://www.ofwat.gov.uk/wp-content/uploads/2017/07/Delivering-Water-2020-Consulting-on-our-PR19-draft-methodology-2.pdf

working groups, including relevant stakeholders in the industry, in December 2017 we decided to replace SIM with two new incentive mechanisms:

- the customer measure of experience (C-MeX); and
- the developer services measure of experience (D-MeX).

D-MeX is designed to cover developers, SLPs and NAVs. We said in the PR19 Final Methodology that we consider that, by using comparisons across companies and financial incentives, D-MeX will be more effective than bespoke performance commitments, and purely reputational incentives to deliver a step-change in the quality of service delivered to these new connections customers.

2.2 D-MeX in the PR19 Final Methodology

We said in the PR19 Final Methodology[6] that D-MeX will be based on a single score using the combined results of:

- feedback from a regular developer services customer satisfaction survey; and
- quantitative measure of water company performance against a set of key metrics based on Water UK's existing Levels of Service (LoS) metrics for developer services customers, and any future iterations of the metrics.

We decided that we will rank company performance annually on D-MeX, and apply financial performance payments of up to 2.5% of annual developer services revenue, and performance penalties of up to 5% of annual developer services revenue for the best and worst performers, respectively. These performance payments and penalties would apply annually, in keeping with the approach for the other common performance commitments.

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[6] Further details about C-MeX and D-MeX are set out in Appendix 3 to the Final Methodology: Customer measure of experience (C-MeX) and developer services measure of experience (D-MeX): https://www.ofwat.gov.uk/publication/delivering-water-2020-final-methodology-2019-price-review-appendix-3-customer-measure-experience-c-mex-developer-services-measure-experience-d-mex/

2.3 Our engagement process

In our consultation on the PR19 Final Methodology we set out our proposal to convene Task and Finish Groups to discuss how to implement C-MeX and D-MeX.

In 2017, we established the C-MeX and D-MeX Working Groups (and their sub-groups) comprising industry and customer representatives. Since then, these groups have met to discuss results frompilot waves and initial views (from both Allto and Ofwat) on survey and incentive design.

2.3.1 Allto Consulting

The proposed D-MeX methodology was tested during the D-MeX pilot, conducted by Allto Consulting ('Allto'), during 2018-19. Allto is a market research consultancy, appointed to provide advice and make recommendations to us on the research methodologies for C-MeX and D-MeX. We have carefully considered Allto's recommendations and the stakeholder feedback from the D-MeX Working Group and the D-MeX sub-group when making our final policy decisions

2.3.2 D-MeX Working Group

We formed a D-MeX Working Group to aid the design and implementation of D-MeX and facilitate the development of the detailed pilot.

The **D-MeX Working Group** has a membership covering all water companies, Water UK, the house builders federation (HBF – represents large developers), Fair Water Connections (FWC – represent SLPs) and Independent Water Networks Ltd (IWNL – represents NAVs).

2.3.3 D-MeX Sub-Group

During the pilot phase, a sub-group, comprising a smaller number of representatives from the D-MeX Working Group was initiated, as a means of discussing some of the detailed working level D-MeX implementation issues.

The D-MeX sub-group has members representing water companies, NAVs, SLPs and developer customers.

In coming to our policy decisions for the shadow year, we have considered the findings and recommendations from Allto and all stakeholder representations, including those from the D-MeX Working Group and the D-MeX Sub-group meetings held during the pilot year. The dates of those meetings are set out in Annex 1 and a summary of the views provided by stakeholders are in Annex 2 to this document. Allto's D-MeX report is published alongside this document

2.4 Shadow year

For C-MeX and D-MeX, the purpose of the shadow year is to:

- give companies time to make any systems changes needed before the financial incentives are applied from April 2020 onwards; and
- allow us to monitor the operation of C-MeX and D-MeX incentives and make adjustments for the period 2020-2025.

Recommendations from the D-MeX pilot and information gathered in the shadow year, will inform our final decisions for how D-MeX will be run in 2020-2025 period. These will be reflected in PR19 Final Determinations in December 2019 and the Final D-MeX guidance, which we will publish by March 2020.

We will engage with stakeholders via the D-MeX Working Group and sub-group during the shadow year as and when necessary.

3. D-MeX Pilot

3.1 Pilot Background and Objectives

The qualitative element of the D-MeX mechanism (the customer satisfaction survey) was tested during the D-MeX pilot, conducted by Allto, so that we can refine the methodology in advance of it becoming fully operational in April 2020. The following success criteria, set out in the PR19 Final Methodology, were used:

- encourages companies to improve customer experiences and innovate;
- simple and meaningful for companies and customers;
- proportionate;
- practical to implement;
- measures performance across companies consistently, reliably and fairly; and
- reflects customer behaviour changes and market changes.

The overall objective of the pilot was to develop D-MeX to the point where it can be run in shadow form in 2019-20, and have financial incentives applied on an annual basis from April 2020 onwards. This involved designing and running two waves of pilot customer surveys for D-MeX that are consistent with the design decisions of the incentive outlined in the PR19 Final Methodology.
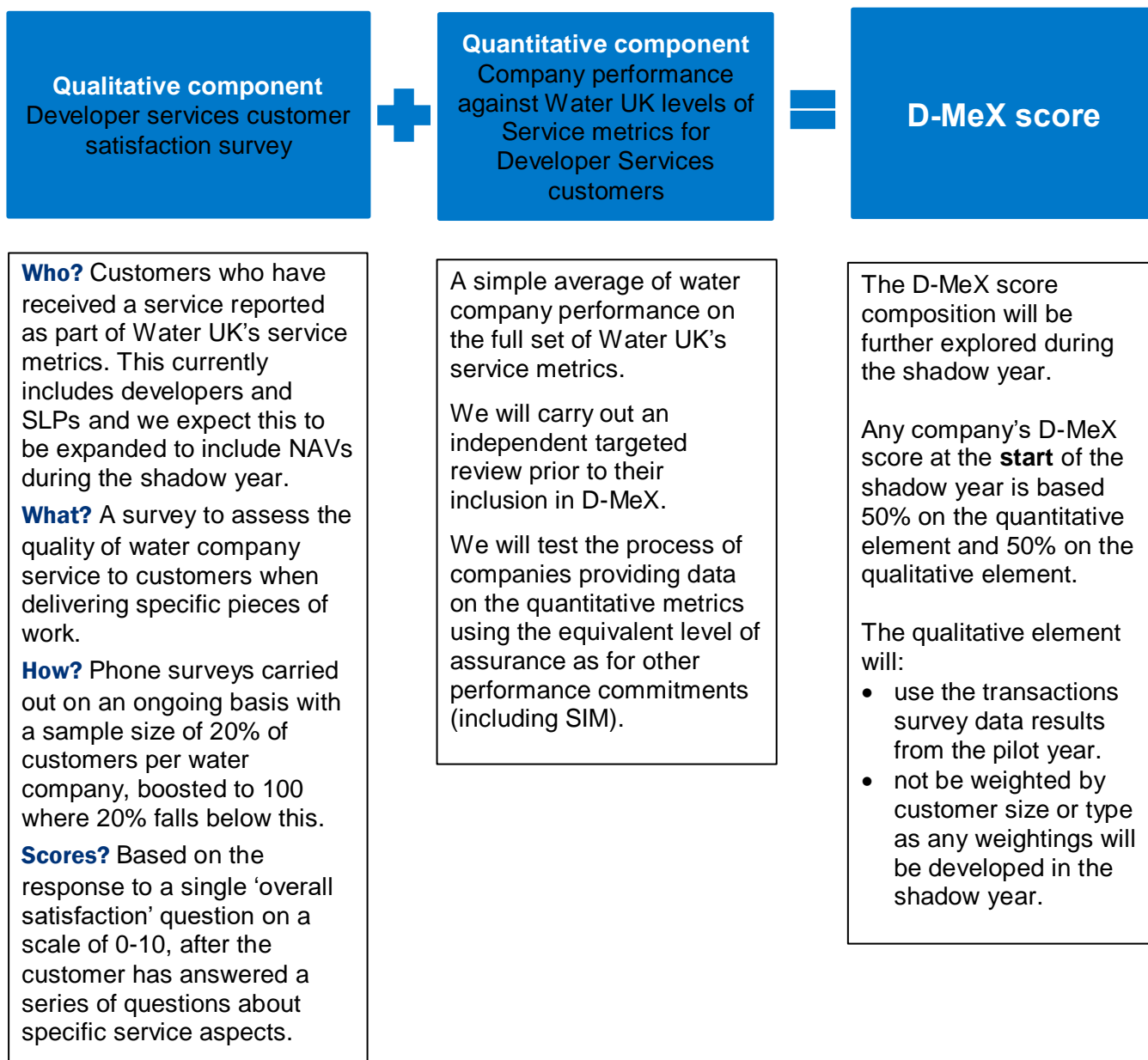
3.2 The pilot operation

The D-MeX pilot was conducted during 2018-19. The pilot phase involved designing and running two waves of customer surveys in which various approaches were trialled, to provide recommendations on the most appropriate survey design. More details about the pilot year and Allto's recommendations can be found in Section 1.3 of the Allto report, 'D-MeX pilot for PR19'.

4. Decisions on D-MeX Shadow Year Methodology

This section outlines the decisions which we have taken for the D-MeX shadow year.

4.1 Overview of how D-MeX will operate in the shadow year

Qualitative component Developer services customer satisfaction survey	**+**	**Quantitative component** Company performance against Water UK levels of Service metrics for Developer Services customers	**=**	**D-MeX score**

Who? Customers who have received a service reported as part of Water UK's service metrics. This currently includes developers and SLPs and we expect this to be expanded to include NAVs during the shadow year.

What? A survey to assess the quality of water company service to customers when delivering specific pieces of work.

How? Phone surveys carried out on an ongoing basis with a sample size of 20% of customers per water company, boosted to 100 where 20% falls below this.

Scores? Based on the response to a single 'overall satisfaction' question on a scale of 0-10, after the customer has answered a series of questions about specific service aspects.

A simple average of water company performance on the full set of Water UK's service metrics.

We will carry out an independent targeted review prior to their inclusion in D-MeX.

We will test the process of companies providing data on the quantitative metrics using the equivalent level of assurance as for other performance commitments (including SIM).

The D-MeX score composition will be further explored during the shadow year.

Any company's D-MeX score at the **start** of the shadow year is based 50% on the quantitative element and 50% on the qualitative element.

The qualitative element will:
- use the transactions survey data results from the pilot year.
- not be weighted by customer size or type as any weightings will be developed in the shadow year.

There are no financial or reputational incentives applied to D-MeX during the shadow year. We expect that companies will continue to collect and provide their LoS data submissions to Water UK. The continued collection of this data by water companies is important as it forms the basis for the sample for the D-MeX qualitative survey.

4.2   Survey Methodology decisions for qualitative element

4.2.1   General satisfaction survey

Decision: the qualitative element of D-MeX will be based on operational service delivery.

Both waves of the D-MeX pilot survey were based primarily on following up on discrete **transactions** that had taken place in the course of water company/customer interactions.

Allto outlined in section 3 of its D-MeX pilot report that an alternative method, would be to use a **contact** follow-up approach, similar to the customer service element of C-MeX. At present companies do not consistently log all their customer contacts, and we recognise that requiring them to do so could lead to unintended consequences around how customers are dealt with. A contact survey would also inevitably focus on how the contact itself was handled rather than the quality of the piece of work being undertaken by the water company. For these reasons Allto recommended that D-MeX maintains the transactional follow up approach for its surveys. We agree with Allto's recommendation.

4.2.2   Survey Scale

Decision: The scoring scale for the D-MeX satisfaction survey will be 0-10.

One of the primary drivers for replacing SIM was that companies' scores have been converging over time, making differentiating between them, in order to apply incentives, more challenging over time.

One of the proposed solutions to convergence was to move from a 5 point scoring scale to one that ranged from 0-10 in C-MeX.

Testing during the C-MeX pilot found that a 0-10 scale did indeed provide greater differentiation than the 5 point scale. The D-MeX pilot also tested the 0-10 scale, with similar results. As such, we agree with Allto's recommendation to use a 0-10 scoring scale in the D-MeX survey.

4.2.3   Survey channel

Decision: The D-MeX surveys will be conducted by phone

The pilot surveys were conducted predominantly by telephone, although Allto also trialled online surveys during the pilot phase. The grounds for doing so were to test whether an online survey would provide more representative results by giving multiple team members the opportunity to contribute, rather than focussing on a single designated phone contact. However, in practice, Allto found that the online approach resulted in substantially lower response rates than the phone channel. Given the sample sizes involved and the lower response rates online, it was not possible to test whether the online approach would produce more representative results.

Allto also advised that, achieving as representative a sample as possible is crucial to successfully delivering a fair financial incentive mechanism, which means minimising non-response. In addition, based on its experience with the business market, a professional telephone interviewer will be able to elicit a higher quality, more consistent set of results than an unsupervised online survey. We also consider that as the services being interviewed about have the potential to be more complex than for the household market, a phone interview is likely to generate a more representative reflection of service quality than the online channel. Therefore, we agree with Allto's recommendation that the D-MeX surveys be carried out via phone.

4.2.4   Customer type

Decision: We will survey SLPs, NAVs and the other developer customer types using the same survey methodology in D-MeX.

During wave 1 of the pilot, Allto used the same survey approach across all developer customer types. That is, using each company's Developer Services transactions list under a selection of key Water UK metrics, Allto interviewed the relevant customer contact for the transaction. However, in doing so, Allto was only able to achieve a relatively small sample of SLPs, and found it was not always possible to identify SLP customers from the records submitted by companies. In addition, as there are no NAV metrics in the Water UK list, it was not possible to use this approach for NAVs.

Wave 2 of the pilot, attempted to address these issues by surveying the SLP customer segment separately from the other developer types. The opportunity was also taken to separate out the NAV customer segment. These tailored approaches involved targeting SLPs and NAV customers with an online, site-based (as opposed to transaction based) survey. The approach also included some bespoke questions for both SLPs and NAVs, in order to gain a more targeted view of their specific needs and views.

Allto found that the response rate for these targeted surveys was significantly lower than for the survey as a whole and that using a site based approach meant that results could not easily be analysed alongside the transactional data gathered from the other developer customers.

Therefore, in the interests of statistical robustness, and maintaining the simplicity of the overall incentive, Allto recommended surveying SLPs and NAVs using the same methodology as the other developer customers during the shadow year. We agree with Allto's recommendation.

As mentioned later in this document we encourage industry to continue the work that we understand is currently being undertaken to develop metrics for incumbent services provided to NAVs, so that these are included in the list of services that are the basis of the quantitative survey sample for D-MeX.

4.2.5   Survey scope

Decision: The D-MeX survey will capture consultants and agents, as well as end users.

Questions were raised during the pilot phase about whether consultants and other agents (intermediaries) appointed by the developer services customer should be considered valid respondents for the D-MeX survey. We agree with Allto's view that customers are explicitly contracting these agents to act on their behalf, and they should therefore be considered valid contacts. During the shadow year, we will engage with stakeholders to refine definitions of different customer types, including the definition of end users and consultants or agents - i.e. an agent at pre-development stage could be an agent but also the end customer.

4.2.6 Sampling frequency

Decision: The sampling and fieldwork process for D-MeX will be ongoing throughout the year, with water companies providing monthly sample data to our appointed agent.

The transactions survey can be run either periodically or on an ongoing basis.

After running the pilot surveys, Allto recommended the ongoing sampling approach. This would provide two major benefits: it would enable the smaller companies to be able to draw their sample from as large a pool of customers as possible, i.e. not be limited by the relatively small numbers they are able to generate in a discrete month; and, a continuous approach should help mitigate the impact of seasonal peaks and troughs on the survey results.

We agree with Allto's recommendation and rationale.

4.2.7 Sample size

Decision: We will use a sample size equal to approximately 20% of each company's customer base for D-MeX. This will be boosted to a minimum of 100 customers where 20% of the sample would yield less than 100 customers.

Through the pilot, Allto identified three feasible methods for determining the sample size for the qualitative element of D-MeX:

- a fixed sample size could be specified for each company;
- companies could be tasked with achieving samples that will meet a particular confidence interval; or
- a sample representing a fixed proportion of each of the companies' customer base.

Allto advised that the large variation in the size of the companies' customer bases makes choosing a fixed sample size problematic. Basing the sample on confidence intervals would also provide difficulties for the smaller companies.

As such, Allto recommends the fixed proportion approach, and after analysis of the two pilot waves, concluded that a sampling proportion of 20% of customers (with an uplift to a minimum of 100 for smaller companies) would provide a satisfactory balance between data reliability, effective representation of the customer types, and practicality. We agree with Allto's recommendation and rationale.

As mentioned later, and recommended by Allto, we will gather information in the shadow year on customer populations and confidence intervals in order to further develop the league table approach for D-MeX,

For information regarding the data within the sample, including permitted exclusions, please see the D-MeX Shadow year guidance document.

4.2.8 Relationships survey

Decision: D-MeX will not include a relationship survey component.

Alongside the transactions survey, the pilot phase included a relationships survey, designed to capture more strategic issues and those emerging during the regular interactions between developer services teams and their key developer customer contacts.

In its analysis of the pilot phase, Allto acknowledged that a relationship survey would help capture a wider range of customer perspectives (particularly those of larger customers). Allto also presented a number of arguments for not continuing with the relationship survey, and concluded that, on balance, adding a relationship survey to the transactional survey was not necessary.

The key arguments which Allto presented for not adopting a relationship survey were that:

- the benefits to developer customers of building of relationships would be expected to also show in the results of the transactional survey;
- identifying the most suitable contacts to sample for the relationships survey could prove time consuming, and inflate the cost of the survey;
- budgetary pressures could potentially result in companies having to compromise overall sample sizes in order to keep two separate surveys running; and
- it would be possible to weight the results of the transactional survey in such a way as to give more emphasis to the experiences of large customers, which would reduce the need for a distinct relationships survey.

We agree with Allto's recommendation and consider that a dedicated relationship survey would add complexity to the overall incentive design, and would ultimately prove unnecessary, as we would expect the effects of ongoing company/customer relationships to be reflected in the transactional survey scores. We will therefore not be implementing a relationships survey element in the shadow year.

4.3   Decisions on service metrics for quantitative element

4.3.1   Introduction

The rationale for including a quantitative element to D-MeX is to strengthen the incentive by providing an objective measure to D-MeX such that the D-MeX score is not solely based on the qualitative survey component.

In consultation with their customers, water companies agreed a set of 24 levels of services and to monitor and report performance quarterly from April 2015. Water UK currently collects and publishes data around the levels of service provided to developers by all Water and Water and Sewerage Companies, under a voluntary system.

In the PR19 Final Methodology, we decided to include the Water UK LoS in D-MeX on the basis that these are a well-established and widely understood set of metrics, developed over a number of years with the sector. Their inclusion in D-MeX was supported by developer services customers during the engagement phase of D-MeX development, and prior to the publication of the PR19 Final Methodology.

Currently there are currently 32 metrics. The data is presented quarterly in an interactive dashboard on the Water UK web site showing, for example the 'proportion

of quotations provided within 28 day target' for each company.[7] The metrics are primarily based on achievement of an activity within time-based targets, showing the success of a water company in completing an action or communication for the customer within a defined time period.

We recognise that since the inception of these metrics there has been improvement across the industry from an average of 88.6% to over 97%. The metrics have therefore brought about service improvements. Nevertheless, some issues exist in relation to the metrics including:

- Inconsistent application of definitions. The July 2017 CH2M Horizontal Review covered the metrics that existed at the time and found that 16% were identified as inconsistently applied across companies. This analysis has found inconsistency to be spread across all metrics.

- Low volume measures. Some metrics capture very low volume of activity which would make the metric highly sensitive to random changes associated with any of the customers. As a result the metrics would be both volatile and unreliable.

- Coverage of measures across companies. The full suite of Water UK metrics cover c.70% of all types of interactions between customers and water companies, with the top 5 metrics covering c.20% of this. For example the metrics do not currently cover water company performance in services provided to NAVs.

- High reliance on few metrics. The Water UK average performance score is calculated using a volume weighted approach, however the high volumes associated with acknowledgements and quotations means the average is primarily driven by these two metrics. These types of metrics could be deemed to be 'too transactional' though we understand that their inclusion is based on requests from customers to have such metrics incorporated, and that performance in this area has since improved.

- High scores and little headroom for improvement. There is a feeling amongst customers that the high scores do not reflect the user experience with

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[7] The latest results for the Water UK Levels of Service metrics are here:
https://developerservices.water.org.uk/latest-reports

companies (mainly as a result of point immediately above) and are not sufficiently stretching. The high scores also leave little room for improvement.

As a result, while the Water UK metrics have encouraged service improvements to developer services customers in the sector, it has been recognised that these metrics will need to be improved before they are included in D-MeX. We understand that work to improve the metrics is currently underway.

4.3.2   Review of metrics

Decision: Ofwat will carry out an independent, targeted review of the Water UK metrics prior to their inclusion in D-MeX to ensure these are fit for purpose.

We are encouraging industry to continue its work on improving the quality of the Water UK metrics, to address the issues set out in section 4.3.1 above. Expected improvements include clearer definitions of measured activities and a consistent application of these definitions across companies, and the inclusion of metrics for services provided to NAVs. We expect this improvement work to be complete by the end of July 2019, before industry proposes to us which metrics we should consider as being part of the quantitative element of D-MeX.

To ensure companies are incentivised to continue improving performance across the period 2020-2025, we consider that this is an opportunity for industry to identify where the time-based targets could be reset to make them more stretching, and to implement this.

We will then carry out an independent targeted review of the metrics prior to their inclusion in D-MeX. If we are satisfied with the results of the review, we are minded to apply an equal 50:50 weighting to both the quantitative and qualitative parts of D-MeX. However we will gather further information in the shadow year to inform our decision on the composition of the D-MeX score for the period 2020-2025.

4.3.3   Selection of metrics for D-MeX

Decision: For the shadow year D-MeX will use all of the existing Water UK Levels of Service metrics as the basis for the quantitative component of the D-MeX score. During the shadow year we expect industry to improve and propose the metrics to be included in D-MeX for the period 2020-2025.

For the purposes of the shadow year for D-MeX, will use a simple average across all of the existing Water UK Levels of Service metrics as the basis for the quantitative component of the D-MeX score.

We consider this to be the simplest approach, where all included metrics carry the same weight and the overall average is most comparable across companies. During the shadow year we will consider other approaches for combining the scores from each individual performance metric to achieve the overall score for the quantitative element of the D-MeX score.

In terms of the selection of the metrics, as mentioned in section 4.3.2, during the shadow year we expect industry to continue to improve the current set of metrics and to propose to us those to be included in D-MeX for the period 2020-2025.

4.3.4   Data submission for quantitative element

Decision: During the Shadow year we will test the approach of companies assuring their Water UK Levels of Service metrics data for the quantitative element of D-MeX and submitting it to Ofwat, using a similar process as is used for other Ofwat performance commitments.

Currently the collection and publication of these metrics take place on a voluntary basis. The D-MeX shadow year guidance sets out steps we expect companies to undertake during the shadow year to assure the data.

The publication of the LoS metrics by Water UK serves as an important reputational incentive for companies to improve their service provision to developer services customers.

We expect companies to continue to provide their monthly levels of service data submissions to Water UK throughout the shadow year.

4.4   D-MeX incentive design issues

The aspects of the incentive design below relate to the design of the D-MeX incentive not covered elsewhere in this document.

4.4.1   Survey question upon which to base the D-MeX score

The D-MeX survey asks a number of questions covering a range of service factors developer customers may experience as they interact with water companies (e.g. ease of contact, timeliness of responses, value for money), before then asking about overall satisfaction. This means there is an opportunity for the financial incentive to be based either purely on companies' overall satisfaction scores, or on a composite score calculated from the different service factor scores.

Allto's analysis of the pilot wave results found that an average of companies' amalgamated service factor scores did not differ significantly from the overall satisfaction scores, suggesting that using a composite score would not have a noticeable influence on the rankings of D-MeX scores.

However, a composite measure could also be used to highlight specific areas where companies are performing poorly, and therefore help focus efforts on making improvements. Although, achieving this, would rely on company specific weightings being applied to each service factor and would also have to be able to capture changes in relative importance of service factors over time. This would significantly complicate the D-MeX calculation.

We agree with Allto's findings. We note the positioning of the overall satisfaction question at the end of the questionnaire - after customers have been asked to think about each of the individual service factors - should mean all elements of their customer journey are captured by their response to the single score. We consider that identifying the service factors would create unnecessary complexity. Therefore, and to meet our objective of an incentive mechanism that is simple, **the qualitative**

component of the D-MeX score will use the overall surveyed customer satisfaction score for the shadow year and we are minded to adopt this approach for the period 2020-2025.

4.4.2   The level of the financial incentive for D-MeX

We said in the Methodology that D-MeX performance payments will be up to 2.5%, and underperformance payments will be up to 5%, of a company's annual developer services revenue. We consider that there is a good case to increase the level of financial incentives. One reason for this is that service quality in this area can have a disproportionate impact on the wider economy/society (for example poor service for developer services customers may have knock on impact in terms of housing development). **We will review the level of the financial incentive for D-MeX during the shadow year and will engage with stakeholders.**

4.4.3   Definition of Developer Services Revenue

In the PR19 Final Methodology regarding the definition of developer services revenue, we said our initial view is that developer services revenue includes, as a minimum, revenue for the following services for both water and wastewater: infrastructure charges, connections charges and requisitions, before any deduction for efficiency incentives.

Following some queries about this point in September 2018, we are taking the opportunity to clarify this position. For the avoidance of doubt we set out below the constituent parts of the total 'grants and contributions' which make up the D-MeX relevant revenues. We have used the references set out in the business plan table App28 as far as possible.

We confirm our view that **developer services revenue for D-MeX now includes, for both water and wastewater: infrastructure charges (gross), connections charges (gross), requisitions, diversions and other price-control contributions, before any deduction for efficiency incentives.**

Infrastructure charge receipts and connection charges should be considered on a 'gross' basis – ie before any discounts for water efficiency. This is in contrast to App28 where they should be disclosed 'net'.

The highlighted rows are included in D-MeX

C	Grants and contributions received ~ wholesale water service	
7	Connection charges (s45)	BC11271IN
8	Infrastructure charge receipts (s146)	BC11270IN
9	Requisitioned mains (s43, s55 & s56)	BC11272IN
10	Other contributions (price control)	BA1086PC
11	Diversions (s185)	BC11273IN
12	Other contributions (non-price control)	BA1086NPC
13	Total grants and contributions ~ wholesale water service	BA1090

G	Grants and contributions received ~ wholesale wastewater service	
24	Infrastructure charge receipts (s146)	BC11370IN
25	Requisitioned sewers (s100)	BC11372IN
26	Other contributions (price control)	BA2086PC
27	Diversions (s185)	BC11373IN
28	Other contributions (non-price control)	BA2086NPC
29	Total grants and contributions ~ wholesale wastewater service	BA2090

5. Next Steps

5.1 Issues to be explored in the shadow year

There are no financial incentives for companies based on performance on D-MeX during the shadow year. The PR19 Final Methodology stated that we would finalise the D-MeX methodology between April and August 2019, and publish the final D-MeX guidance in March 2020 or earlier if possible.

We have decided to change this timetable. Having conducted the pilots, we have identified specific areas that need further work, as set out below. To allow sufficient time to explore these issues and for the quantitative metrics to be improved, and for us to be satisfied with their quality, prior to us making final decision for how D-MeX will run for the 2020-25 period. Section 5.2 sets out the revised timetable.

This section sets out the outstanding issues which will be finalised during the shadow year. These are areas where we would like to gather more information or where we need to allow some more time for improvements to take place, before we can be in a position to take a decision for the final design of D-MeX for the period 2020-2025.

5.1.1 Qualitative element of D-MeX

5.1.1.1 League table and annual customer population size for each company

As mentioned above, the PR19 Final Methodology explained that we consider D-MeX, by using comparisons across companies and financial incentives, will be more effective than bespoke performance commitments and purely reputational incentives at driving better service for developer customers. We consider D-MeX to be a necessary and proportionate approach for incentivising a step-change in the quality of service delivered to new connections customers, which we are developing in conjunction with our stakeholders.

We maintain this position. For the shadow year of D-MeX we will adopt a sampling proportion of around 20% of customers for each water company, boosting to 100 for those companies where 20% would fall below this minimum number, as this has a systematic basis, maximises the reliability of the data within the bounds of what it will

be practical to achieve, and ensures effective representation of the range of customer types that each company services.

In addition and as recommended by Allto, during the shadow year we will gather companies' annual population sizes (calculated from a count of unique customer contacts throughout the year), to confirm sample size and confidence interval estimates. This will give us further information for the development of the league table approach for D-MeX.

5.1.1.2 Consistency across companies

We set out in the PR19 Final Methodology we are taking account of the regulatory differences between England and Wales as we design D-MeX, for example that mandatory adoption of sewerage infrastructure exists in Wales, whereas it does not in England.

While we recognise that national and regional differences exist, we have not seen evidence from the pilot of the need to apply company-specific or other adjustments to D-MeX, as the impact of these variations on the services covered by D-MeX appears to be minor. We are therefore not minded to treat companies differently, either in relation to differences in law or the developer market. This is because we want to preserve the integrity of the incentive, avoid undue complexity, and evidence from the pilot does not suggest that particular companies are disadvantaged by our intended approach to D-MeX, which is to rank companies in a league table (as above).

We will, however, continue to monitor the impact of the D-MeX survey on companies in the shadow year before making a final decision.

5.1.1.3 Incorporating the experience of NAVs into D-MeX

The experiences of NAV customers need to be effectively captured as part of the D-MeX process. As mentioned previously, we understand that there is work being undertaken to develop NAV metrics (similar to the work that was undertaken to include SLP metrics) in the levels of service metrics. As these metrics form the basis

of the sample for the D-MeX transactions survey, including metrics for NAVs will ensure the views of this customer segment are captured in D-MeX.

5.1.1.4 A consistent classification system to weight different customer types

The developer services market to which D-MeX applies is diverse. Customers range from high volume one-off individual connection transactions customers, to lower volume large scale projects by big developers. A key issue that has been discussed throughout the development of the qualitative component of D-MeX has been how best to capture the relative size and importance of the various developers (individuals, large developers, SLPs and NAVs). Larger customers like the major housing developers will have fewer transactions in any given month, as a group, than the smaller builder population. According to Allto, it is how these large developers are serviced that could have greater impact on improving industry efficiency and helping to stimulate growth in residential completions, than the way in which smaller developer services customers are serviced.

Allto recommends using the shadow year to establish a workable means of classifying customers, especially where there is no relationship survey dedicated to larger developers within D-MeX. Allto's recommendation for an approach to test is simple customer grouping. Survey responses would be split into simple groups which could represent one off connections, small builders and large builders. Responses within the group relating to larger builders, which would be lower volume but higher importance, would receive the highest weight to reflect their relative importance. This could work as follows: using weights of 1 for one off connections, 2 for small builders and 3 for large developers.

We agree that without accounting for the relative size and volumes of these customers D-MeX is likely to underrepresent larger developers. We are therefore minded to incorporate a weighting system into D-MeX for when it becomes operational from 1 April 2020. Over the shadow year we will work with stakeholders to investigate how customers should be segmented based on size, and how to best define these for consistency across companies.

5.1.1.5 Water companies' systems readiness for D-MeX for the period 2020-2025

We recognise from the D-MeX pilot that the level of development of IT systems varies across companies. We are also aware that some companies may find it administratively stretching to provide monthly files at this stage. Hence we are providing the D-MeX guidance in advance of the shadow year to enable systems changes as much as possible. Ultimately, it is the responsibility of the companies to effectively embed the learning opportunities afforded to them by the pilot year and shadow year, and be ready to report for D-MeX for the period 2020-2025.

5.1.2 Quantitative element of D-MeX

5.1.2.1 Selecting the metrics to be included in D-MeX

The quantitative element of D-MeX measures company performance against a set of key metrics derived from Water UK's existing levels of service (LoS), and we decided to include this element to add an objective component to the overall D-MeX incentive.

As mentioned in section 4.3.2, during the shadow year we encourage industry to continue its work to improve the quality of these metrics, and to make recommendations for the package of existing (or additional) metrics to be included in D-MeX. We will then carry out an independent targeted review prior to their inclusion in D-MeX for the period 2020-2025.

In selecting which metrics to include in the quantitative component of D-MeX, we will consider a number of factors including, but not limited to, the following:

- Coverage. Do metrics cover the key performance areas and market segments covered by D-MeX?

- Consistency. Is data collected and processed in a consistent manner to allow for cross-company comparisons?

- Quality. What level of assurance has been done on underlying data; can we be confident in its accuracy?

- Value to customers: as what is the value to developer services customers of including any specific metric given that the qualitative part of D-MeX will be measuring overall satisfaction and capturing aspects of service quality including customer service?

- Proportionality. Is the burden, in terms of complexity and workload required to gather and manage the data, feasible from a company and regulatory perspective?

The final decision on which metrics to include in D-MeX will be taken by Ofwat.

5.1.2.2   Method for combining the quantitative metrics

Companies are being measured on their delivery of a range of services to developer services customers. Some of these services are arguably easier to fulfil than others, such as acknowledging applications and providing quotations. These easier to fulfil variables however account for over 50% of activity. When using a volume-weighted-average approach for measuring overall performance on these metrics (as is currently the case with the Water UK metrics), it reduces incentives for high performance in all activities.

To encourage performance across all service areas, we will adopt a simple average approach (rather than volume weighted) for measuring each companies' performance on the quantitative metrics in the shadow year, and we are minded to adopt this approach for D-MeX moving forward.

5.1.2.3   Company assurance process for quantitative metrics (4.1.3.3)

When D-MeX becomes operational, from 1 April 2020, we expect companies to provide us with data for the quantitative element of D-MeX, which has gone through sufficient assurance processes, similar to the data provided for other performance commitments. To test this process, companies will be expected to provide data which has undergone a quality assurance process (as detailed in the D-MeX shadow year guidance document).

For the period 2020-2025, we expect the level of assurance when providing the data to Ofwat around these metrics to be aligned to the approach companies currently employ for performance commitments. We will work with stakeholders during the shadow year to further develop this assurance process.

5.1.2.4 Testing the process for companies' data submissions

One of the key functions of the shadow year is that it provides companies with the opportunity to ensure they have robust systems in place for the timely submission of D-MeX data once the incentive mechanism goes live. Following our independent targeted review, we will ask companies to submit data for the quantitative element of D-MeX to us that had undergone sufficient levels of quality assurance as set out in the D-MeX guidance.

5.2 Our timetable

For those methodological matters which are unlikely to be the subject of, or altered by, shadow year monitoring or consultation, we intend to set out our minded to position in company draft determinations. The final D-MeX methodology will be set out in company final determinations.

We will adopt the following timetable for the development of D-MeX:

Month	Topic
March 2019	Publish shadow year guidance, pilot reports and policy decisions for the shadow year
May 2019*	Shadow Year starts
May – December 2019	Industry works to improve quantitative metrics and to include NAV metrics and proposes to Ofwat quantitative metrics to be included in D-MeX. We expect companies to complete this work by the end of July 2019. Mid-July to end of August: minded to position on certain aspects, and seek stakeholder views on other D-MeX incentive design issues, as part of draft determinations process. Ofwat carries out independent targeted review of Water UK metrics
11 December	Publish decision on final D-MeX incentive design for 2020-2025 as part of Final Determinations
Mar 2020	Publish D-MeX Guidance for 2020-2025
1 April 2020	Run D-MeX

*Please note that the shadow year will run from 1 May 2019 to 31 March 2020. This is to ensure sufficient time for us to appoint an agent to run the shadow year, following the publication of the suite of documents related to the shadow year for C-MeX and D-MeX.

D-MeX Working Group meetings will take place throughout the year and we will communicate relevant dates through that channel.

Annex 1

Schedule of 2017-2019 Working Group meetings for C-MeX & D-MeX

Below is a list of the C-MeX and D-MeX Working Group meetings held between 2017 and 2019.

Meeting	Date	Location
C-MeX		
Full Working Group 1	07/09/17	Bath – WSX offices
Full Working Group 2	03/10/17	Ofwat
Full Working Group 3	23/03/18	Ofwat
Full Working Group 4	30/07/18	Ofwat
Sub-group 1	24/05/18	Telecon
Sub-group 2	14/06/18	Telecon
Sub-group 3	05/07/18	Telecon
Sub-group 4	23/07/18	Telecon
Sub-group 5	25/09/18	Ofwat
Sub-group 6	23/10/18	Ofwat
Sub-group 7	21/11/18	Ofwat
Full Working Group 5	3/12/18	Ofwat
Sub-group: Shadow year guidance	19/02/19	Telecon
D-MeX		
Full Working Group1	19/9/17	London – Water UK office
Full Working Group2a	09/10/17	Ofwat
Full Working Group2b	24/10/17	Ofwat

Full Working Group3	22/03/18	Ofwat
Full Working Group4	31/07/18	Ofwat
Sub-group 1	03/09/18	London - Water UK hosted
SLP Meeting - Wave 2 pilot	05/09/18	Offsite – FairWater Connections hosted
NAV meeting – Wave 2 pilot	13/09/18	Ofwat
IPG Meeting	20/09/18	Water UK hosting
Water UK developer day	15/09/18	Water UK hosting
Full Working Group 5	4/12/18	Ofwat
Sub-group: Shadow year guidance	19/02/19	Telecon

Annex 2 Stakeholder responses

The Annex to Allto's PR19 D-MeX report deals with stakeholder comments received in relation to Allto's draft recommendations for the D-MeX Shadow year. These were shared at the December 2018 D-MeX Working group meeting.

We also received some responses from stakeholders on the draft D-MeX shadow year guidance that we shared with the D-MeX Working Group in February 2019.

Stakeholders requested further detail on the challenge process for D-MeX. They also asked how customers who have told their company that they do not want to be contacted for marketing or other purposes.(DNCs) will be defined, for example whether the definition would cover a whole company, and whether those opting out of marketing contact should be classed as DNC. We also received stakeholders' comments regarding sending data securely. Having considered and included further information on these matters in the D-MeX Shadow Year guidance.

There were a number of queries on how we would apply any weights to the customer segments in the D-MeX calculation. Definitions on the customer segments used (customer size) are outlined in the D-MeX shadow year guidance document. A number of stakeholders have also queried whether NAVs will be included in the D-MeX score. Our response to these matters is covered in section 4 of this document.

Some stakeholders raised concerns regarding timelines. Our response to this is covered in section 5 of this document.

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