

July 2019

Trust in water

# PR19 draft determinations

**Yorkshire Water – Accounting for past delivery actions and interventions**

## PR19 Draft Determinations: Yorkshire Water - Accounting for past delivery actions and interventions

Following our initial assessment of plans, we categorised two types of actions for slow-track and significant scrutiny companies:

- required actions for companies which in general were required for draft determinations (or final determinations for some aspects of past delivery); and
- advised actions for companies to do by a specific date but that are not required for our draft determinations.

Table 1 below sets out the required and advised actions, the model the action relates to, a summary of the company's response to the action, our assessment of the company's response, and any further interventions we are making as part of the draft determination. Table 1 also sets out any further interventions that are not resulting from an action which we are making as part of the draft determination.

Each action and further intervention that is not resulting from an action has a unique reference. The prefix 'YKY' denotes the company Yorkshire Water. The central acronym references the test area where the action has been identified, please see the 'PR19 draft determinations: Glossary' for a key to these acronyms. Actions whose numbers are preceded with an 'A' denote required actions. Actions whose numbers are preceded with a 'B' denote advised actions. Interventions not resulting from an action are preceded with a 'C' followed by a three digit code for the model the intervention is relevant to, and a two digit reference for the interventions in that model. The model codes are set out below.

Model	Code
ODIs	002
Land sales	003
WRFIM	005
Totex	006
Water trading	007
Residential retail	008
SIM	009
RCV adjustments feeder model	010
Revenue adjustments feeder model	011

For all other documents related to the Yorkshire Water draft determination, please see the [draft determinations webpage](#).

**Table 1 – Yorkshire Water’s response to required actions and interventions for draft determinations**

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
Land disposals	YKY.PD.A1	Required	<b>PR14 Land sales:</b> Yorkshire Water is required to provide sufficient evidence to support the forecast trajectory in table App9.	1 April 2019	Yorkshire Water provides evidence to support the forecast trajectory in table App9.	No intervention required. The evidence provided is sufficient to support the forecast years.	N/A

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
Outcomes	YKY.PD.A2	Required	<p><b>PR14 Outcome delivery incentives:</b> Yorkshire Water is required to demonstrate how the underperformance payments through poor performance are being spent on improvements (per its PR14 outcome delivery incentives specification) over and above what would otherwise be invested. It should provide totex cost of Yorkshire Water cost for each eligible intervention for WC2 and SB3: solutions delivered by working with others' performance commitments for 2015-16, 2016-17 and 2017-18 and forecasts for 2018-19 and 2019-20.</p>	1 April 2019	<p>Yorkshire Water has one outcome delivery incentive for which it is currently forecasting to incur underperformance payments within the 5-year review period. This is performance commitment WA3 (drinking water contacts).</p> <p>The Yorkshire Water initial assessment of plans response document discusses its rectification and reinvestment approach for this outcome delivery incentive and includes the totex cost of eligible interventions within WC2/SB3, along with its calculation methodology.</p> <p>The company's response set out that it has increased spending by £230 million approved by its board in November 2017 for five areas including leakage.</p> <p>Appendix 20 within Yorkshire Water's PR19 business plan (submitted in September 2018) stated:</p> <p>"In line with our Final Determination, the penalty value will not be returned to customers via a revenue or RCV adjustment. Instead with the agreement of our customers at PR14, it will be reinvested on further asset improvements within three years of the failure to meet targets. At PR14 customers determined that they would prefer to see reinvestment to drive material improvements in failing services, rather than receive a small rebate and continue to suffer service failures or performance that is not at targeted levels. We have ensured that the reinvested funds within this AMP and for the 2020-25 period are not included in totex out or under-performance sharing mechanisms."</p>	<p>Intervention required.</p> <p>Yorkshire Water's PR14 final determination company-specific appendix sets out that for ODIs "Penalty investment financed by shareholders, no RCV addition. Reward by 2020-25 year 1 revenues". All other companies' underperformance payments are either an adjustment to revenue or an adjustment to the RCV.</p> <p>The company has one ODI, WA3 (drinking water contacts), that it is expecting to underperform over the 2015-20 period with an aggregate value of - £18.7308 million (this is made up of - £6.5736 million in 2017-18, - £6.5736 million in 2018-19 and - £5.5836 million in 2019-20). This value takes into account the revised forecasts for 2018-19 and 2019-20 included in the company's IAP response document 1 April 2019 (page 135).</p> <p>We consider that Yorkshire Water provides insufficient evidence that the adjustment it proposes, as opposed to making a direct change to the RCV, will better achieve the desire of customers to see reinvestment. The company does not provide sufficient evidence that its approach results in additional investment over and above what would have been made in absence of the underperformance payment.</p>	<p><b>Performance commitment WA3 (drinking water contacts)</b></p> <p>We are intervening to apply the - £18.731 million (2012-13 prices, net of tax) underperformance payment as an adjustment to the RCV. This is made up of - £6.574 million in 2017-18, - £6.574 million in 2018-19 and - £5.584 million in 2019-20.</p> <p>Our intervention reduces the water RCV adjustment at the end of the 2015-20 period from £0 million to - £21.449 million (2017-18 FYA CPIH price base).</p>

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
Outcomes	YKY.PD.A3a	Required	<p><b>PR14 Outcome delivery incentives:</b> Yorkshire Water is required to update its forecast for 2019-20 performance to take account of the actual 2018-19 performance for all its performance commitments.</p> <p>We expect the company to pay particular focus where we found the evidence provided in its business plan for the 2018-20 forecasts to be insufficient which was for:</p>	15 July 2019	No company action required for the draft determination.	<p>No intervention required.</p> <p>We will review Yorkshire Water's updated data before making any interventions for the final determination.</p>	N/A
Outcomes	YKY.PD.A3b	Required	WB4: Water network stability and reliability factor	15 July 2019	As YKY.PD.A3a	As YKY.PD.A3a	As YKY.PD.A3a
Outcomes	YKY.PD.A3c	Required	WB1: Leakage	15 July 2019	As YKY.PD.A3a	As YKY.PD.A3a	As YKY.PD.A3a
Outcomes	YKY.PD.A3d	Required	WA3: Drinking water contacts	15 July 2019	As YKY.PD.A3a	As YKY.PD.A3a	As YKY.PD.A3a
Outcomes	YKY.PD.A3e	Required	WA4: Water quality stability and reliability factor	15 July 2019	As YKY.PD.A3a	As YKY.PD.A3a	As YKY.PD.A3a
Outcomes	YKY.PD.A3f	Required	WC1: Length of river improved (note: PC is part of a total commitment at Appointee level - see also SB4)	15 July 2019	As YKY.PD.A3a	As YKY.PD.A3a	As YKY.PD.A3a
Outcomes	YKY.PD.A3g	Required	SB4: Length of river improved (against WFD component measures) (note: PC is part of a total commitment at Appointee level - see also WC1)	15 July 2019	As YKY.PD.A3a	As YKY.PD.A3a	As YKY.PD.A3a

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
Outcomes	YKY.PD.A3h	Required	SB2: Wastewater quality stability and reliability factor	15 July 2019	As YKY.PD.A3a	As YKY.PD.A3a	As YKY.PD.A3a
Residential retail	YKY.PD.A4	Required	<b>PR14 Residential retail:</b> Yorkshire Water is required to provide further clarity on the reasons for the difference between reforecast customer numbers and actual customer numbers in 2018-19 in table R9.	1 April 2019	The difference between actual and reforecast customer numbers in 2018-19 is due to the forecast actual customer numbers figure being a more recent forecast. Yorkshire Water responded to our action by reverting to an older forecast of actual customer numbers which is equal to the reforecast customer numbers.	Intervention required. We are intervening in Yorkshire Water's forecast actual customer numbers for 2018-19 to impose the values provided in September 2018. This is consistent with the principle that the draft determination should be based on the most up-to-date forecasts available. The intervention also ensures consistency with business plan table R1 in the April 2019 submission which contains the most up-to-date values for forecast actual customer numbers.	We are intervening to impose the values for forecast actual customer numbers for 2018-19 that Yorkshire Water provided in September 2018 to replace the values for forecast actual customer numbers provided in the April 2019 submission. This is because the numbers in the April submission replaced the September submission with an older forecast and so did not represent the latest view. The changes are to the following lines: <ul style="list-style-type: none"> <li>• unmetered water-only actual customer numbers 2018-19 – 56,875</li> <li>• unmetered wastewater-only actual customer 2018-19 – 61,196;</li> <li>• unmetered water and wastewater customer 2018-19 – 871,178;</li> <li>• metered water-only customer 2018-19 – 50,619;</li> <li>• metered wastewater-only customer 2018-19 – 49,462; and</li> <li>• metered water and wastewater customer 2018-19 – 1,090,430.</li> </ul> <p>Along with YKY.PD.C008.01 below, our interventions reduce the total residential retail revenue payment at the end of the 2015-20 period from - £3.169 million to - £3.130 million (2017-18 FYA CPIH deflated price base).</p> <p>Please see published draft determination residential retail revenue reconciliation model for Yorkshire Water.</p>

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
Residential retail	YKY.PD.C008.01	Intervention not resulting from an action	N/A	N/A	N/A	Intervention required. We are intervening to round Yorkshire Water's modification factor figures to two decimal places to ensure consistency with the 'PR14 reconciliation rulebook'.	We are rounding to two decimal places, modification factor figures for 2015-16 to 2019-20 associated with the following lines in business plan table R9: <ul style="list-style-type: none"> <li>unmetered water-only customer;</li> <li>unmetered wastewater-only customer;</li> <li>unmetered water and wastewater customer;</li> <li>metered water-only customer;</li> <li>metered wastewater-only customer; and</li> <li>metered water and wastewater customer.</li> </ul> Along with YKY.PD.A4 above, our interventions reduce the total residential retail revenue payment at the end of the 2015-20 period from - £3.169 million to - £3.130 million (2017-18 FYA CPIH deflated price base). Please see published draft determination residential retail revenue reconciliation model for Yorkshire Water.
SIM	YKY.PD.A5	Required	<b>PR14 Service incentive mechanism:</b> Yorkshire Water is required to provide an explanation for why it has made the changes to the 2015-16 and 2016-17 values; and provide evidence to support the forecast trajectory in table R10.	1 April 2019	Yorkshire Water provides an explanation for the 2015-16 and 2016-17 data changes and its forecast trajectory in its response. The changes relate to data that the company thinks we have incorrectly prepopulated in its business plan table R10.	No intervention required. We agree with the changes that the company has made as the values were prepopulated incorrectly.	N/A
SIM	YKY.PD.C009.01	Intervention not resulting from an action	N/A	N/A	N/A	Intervention required. We are intervening to adjust Yorkshire Water's household retail revenue as a result of its SIM performance from 2015-16 to 2018-19.	We are intervening to set the service incentive mechanism adjustment to +2.17% of household retail revenue, which is £7.023 million (2017-18 FYA CPIH deflated price base) in total over the period. We further explain how we calculate this in the 'Accounting for past delivery technical appendix'.
WRFIM	YKY.PD.A6a	Required	<b>PR14 Wholesale revenue forecasting incentive mechanism:</b> Yorkshire Water is required to update tables WS13/WWS13 and the WRFIM model to reflect actual reported values for grants and contributions from the annual performance report or provide compelling evidence to support why the adjustment the company made to remove connection charges from the data inputs is appropriate.	1 April 2019	Yorkshire Water provides more evidence on the previous accounting treatment of costs and the basis of APR submissions in support of the adjustment it made to remove connection charges from the water data inputs and sewer adoptions from the wastewater data inputs in the WRFIM model.	Intervention required. The claim relates to errors the company made in completing its business plan tables for connection expenditure at PR14 and we consider this to be outside of the reconciliation mechanism's scope.	We are intervening to reflect actual reported values for grants and contributions from the annual performance report in the WRFIM model.  Along with YKY.PD.A6b below, our interventions increase the total WRFIM adjustment at the end of the 2015-20 period from - £22.325 million (- £8.265 million for water and - £14.060 million for wastewater) to - £32.199 million (- £14.332 million for water and - £17.867 million for wastewater) (2017-18 FYA CPIH deflated price base).

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
WRFIM	YKY.PD.A6b	Required	<b>PR14 Wholesale revenue forecasting incentive mechanism:</b> The adjustment calculated in the WRFIM model should not be amended to reflect only the blind year revenue correction mechanism element, or is required to provide compelling evidence that the amendment is appropriate.	1 April 2019	Yorkshire Water does not provide a response on this point.	Intervention required. The company does not provide compelling evidence that the amendment is appropriate and so we are removing the amendment.	We are intervening to calculate the WRFIM adjustment in accordance with the ' <a href="#">PR14 reconciliation rulebook</a> '.  Along with YKY.PD.A6a above, our interventions increase the total WRFIM adjustment at the end of the 2015-20 period from - £22.325 million (- £8.265 million for water and - £14.060 million for wastewater) to - £32.199 million (- £14.332 million for water and - £17.867 million for wastewater) (2017-18 FYA CPIH deflated price base).
All models	YKY.PD.A7	Required	<b>PR14 reconciliations:</b> Further to the actions we have set out to address our concerns over the evidence provided in its business plan for the individual reconciliations, we will require the company to refresh all of its PR14 reconciliations to replace its 2018-19 forecast performance with 2018-19 actual performance and update the evidence for its forecast 2019-20 performance taking into account of the actual 2018-19 performance.	15 July 2019	No company action required for the draft determination.	No interventions required. We will review Yorkshire Water's responses to its actions and further information provided for all the PR14 reconciliation models before making any further interventions for the final determination.	N/A
Revenue adjustments	YKY.PD.C011.01	Intervention not resulting from an action	N/A	N/A	N/A	Intervention required. We are standardising the discount factor used to profile revenue adjustments. Companies can choose to apply revenue adjustments either in the first year, or, spread over a number of years in the 2020-25 period to minimise the impact on bills or to generate a bill profile that is appropriate for its customers. We consider the wholesale WACC is an appropriate discount factor as this is a measure of the time value of money that is consistent with the price control framework. We are not intervening in Yorkshire Water's choices for profiling revenue adjustments in 2020-25.	We are using our view of the wholesale WACC (3.09%) as the discount factor to preserve the net present value of the outperformance or underperformance payments due when spreading adjustments over the period.

Model	Ref.	Action type	Action	Date required	Summary of company response to the action	Our assessment and rationale	Interventions
N/A	YKY.PD.B1	Advised	<p>Yorkshire Water should produce and provide additional evidence that it has identified:</p> <ul style="list-style-type: none"> <li>the drivers of incidents performance and customer communication and support performance during and after major incidents, pollution incidents and where statutory and licence obligations enforced by the EA/NRW, DWI and Ofwat have not been met;</li> <li>lessons learnt from good and poor past and current performance;</li> <li>the performance gap between current performance and proposed performance in the 2020-25 business plan; and</li> <li>measures planned or already in place to ensure deliverability of the 2020-25 business plan.</li> </ul>	24 May 2019	The company provides further evidence to support the deliverability of its plan.	<p>No intervention required.</p> <p>Because our deliverability concerns were not substantial in this area, and so we set an advised action, we will conduct a risk-based review of the company's response to the action and will determine the need for further interventions for the final determination.</p>	N/A
N/A	YKY.PD.B2	Advised	<p>Yorkshire Water should produce and provide an action plan that sets out:</p> <ul style="list-style-type: none"> <li>how Yorkshire Water will continuously monitor incidents performance and customer communication and support during and after major incidents and deliver targets set by the EA/NRW in the Environmental Performance Assessment (EPA), by DWI and by Ofwat's regulations, including what evidence it will look for beyond itself and the sector;</li> <li>how Yorkshire Water will identify drivers of performance and lessons learnt from both good and poor performance;</li> <li>how Yorkshire Water will identify measures to improve performance and integrate these into its business; and</li> <li>how Yorkshire Water will ensure that this is a continuous rather than one-off process.</li> </ul>	24 May 2019	The company provides an action plan as requested.	<p>No intervention required.</p> <p>Because our deliverability concerns were not substantial in this area, and so we set an advised action, we will conduct a risk-based review of the company's response to the action and will determine the need for further interventions for the final determination.</p>	N/A

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