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PR19 final determinations

**Welsh Government priorities and our
2019 price review final determinations**



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1. Introduction

The 2019 price review (PR19) plays an important role in delivering the Welsh Government's strategic priorities and objectives.

The Welsh Government has set out [strategic priorities and objectives](#) for us,¹ which were adopted in January 2018. We are required to act in accordance with these priorities and objectives when carrying out our relevant functions relating wholly or mainly to Wales. In this document, we discuss how the PR19 final determinations for 'Welsh companies' (companies whose areas are wholly or mainly in Wales – Dŵr Cymru and Hafren Dyfrdwy) help to achieve those priorities and objectives (which we refer to as the Welsh Government's 'strategic policy statement').

The Welsh Government has set five **objectives** for us that are relevant to PR19:²

1. We expect Ofwat to develop the regulatory framework as applicable to Wales on the basis of sound evidence relevant in a Welsh context. It must demonstrate how it has taken into account the specific circumstances of Wales when developing and consulting on new proposals relating to Wales. Where appropriate it should adopt a different approach for UK Government and Welsh Government regulated undertakers.
2. We expect Ofwat to challenge companies to deliver for customers on the basis of comparison across companies in Wales and England, and across sectors where appropriate, while making appropriate allowances for differences in the operating and legal environments of companies in Wales, and taking into account variations in the priorities of customers and other stakeholders
3. We expect Ofwat to take due account of current and future differences in both policy and law between the UK and Welsh Governments including where new obligations on water companies in Wales emerge.
4. Ofwat should have regard to how it can enable or incentivise companies to contribute to the delivery of Welsh Government policy and strategies. Ofwat should set out clearly how any of its major decisions are consistent with the Welsh Government's strategic priorities and objectives, for example, when

¹ It has done so under section 2B of the Water Industry Act 1991, as amended by section 24 of the Water Act 2014.

² The final objective states that Ofwat should submit an annual report to Welsh Ministers. This is outside the scope of the PR19 final determination and so covered through our annual report, rather than here.

establishing the methodology for price reviews, presenting proposals for changes to the regulatory framework such as modifications to undertakers' conditions of appointment, or publishing determinations.

5. Ofwat should consider the clarity and cohesion of its regulatory framework taken as a whole and in a specific Welsh context. Ofwat should have regard to the desirability of a simple, effective and efficient regulatory framework. Ofwat should seek to maintain a transparent regulatory framework that allows companies, investors and customers to plan for the long-term, whilst incentivising efficiency improvements.

The Welsh Government has also set **priorities** for the economic regulation of the water sector in Wales under the following seven headings:

- affordability;
- innovation;
- long-term;
- markets and competition;
- resilience;
- strong customer focus; and
- sustainable management of natural resources.

The Welsh Government's objectives and priorities have played an important role in shaping the decisions we have made throughout the price review process. When we published our final **PR19 methodology**, we set out how that methodology would help to deliver the Welsh Government's strategic priorities and objectives. Our initial assessment of business plans evaluated company plans against that methodology.

When we made our **draft determinations** in July, we set out how those determinations supported the priorities and objectives of the Welsh Government.

This document begins by outlining how our approach to the price review aligned with the Welsh Government's objectives for us. The rest of the document outlines how our final determinations for Welsh companies support the achievement of the priorities of the Welsh Government.

2. The Welsh Government's objectives for Ofwat

Objective

We expect Ofwat to develop the regulatory framework as applicable to Wales on the basis of sound evidence relevant in a Welsh context. It must demonstrate how it has taken into account the specific circumstances of Wales when developing and consulting on new proposals relating to Wales. Where appropriate it should adopt a different approach for UK Government and Welsh Government regulated undertakers.

Our PR19 methodology took full account of the specific circumstances in Wales, including the specific legal requirements. It required Welsh water companies to develop business plans to address the needs of their customers and the environment in Wales. The PR19 methodology provided considerable scope for Welsh companies to develop business plans and make performance commitments that reflect the particular needs and preferences of Welsh customers. We assessed Welsh companies' proposals against how they planned to deliver for Welsh customers and the environment during 2020-25 and in the long term.

Throughout the PR19 process, we have considered the specific circumstances of Wales. We have also taken into account existing Welsh Government policy. For example, in our approach to markets in Wales, we have considered the Welsh Government's view that the development of markets should not reduce Welsh companies' overall accountability for the delivery of excellent services to customers and the environment, or the integrity and efficiency of the management of the network systems as a whole.

Our approach has also taken into account specific areas that the Welsh Government has prioritised. For example, following evidence of strong support from Hafren Dyfrdwy customers, and need for investment from Dŵr Cymru, we allow increased funding for both Welsh companies for the removal of lead pipes from the water supply network. This allowance is in line with the Welsh Government's priority to reduce the risk of lead, as set out in the [Water Strategy for Wales](#) (2015). In addition, we allow Dŵr Cymru and Hafren Dyfrdwy investment to enact enhanced safety standards arising from the Reservoirs Act 1975 (as amended by the Flood and Water Management Act 2010) at the pace expected by Natural Resources Wales.

Objective

We expect Ofwat to challenge companies to deliver for customers on the basis of comparison across companies in Wales and England, and across sectors where appropriate, while making appropriate allowances for differences in the operating and legal environments of companies in Wales, and taking into account variations in the priorities of customers and other stakeholders

Our PR19 approach has emphasised comparative analysis of companies' plans, where appropriate. In order to establish truly stretching targets, Welsh companies' business plans were compared to:

- English companies – Our price control has the same broad structure across England and Wales. This has allowed Welsh companies to be measured against a wider range of companies, allowing us to set more stretching targets, which benefits Welsh customers. Two areas where cross company comparisons have been particularly important are:
 - common performance commitments – allowing customers and stakeholders to compare individual company performance with the rest of the sector; and
 - cost benchmarking – we have used data from all companies to set stretching cost baselines, while taking account of legitimate differences in scale and operating environment.
- Other sectors – During the period 2020-25, the customer service performance of Welsh companies will be compared to that of other water companies through the PR19 incentive mechanisms called the Customer Measure of Experience (C-MeX) and Developer Services Measure of Experience (D-MeX). In order to achieve higher performance payments, companies will have to demonstrate performance among the best companies in the wider economy (as measured by a cross-sector threshold).

Through these comparisons we made robust assessments of the relative strengths of the Welsh companies' plans.

Welsh companies developed their business plans through engagement with Welsh customers and stakeholders. Our approach, therefore, encouraged the business plans to reflect the distinct needs of Welsh customers and the environment.

Our [customer engagement policy](#) for PR19 set out expectations that companies will share comparative information on company performance with consistent definitions. Consultation in 2016 led to implementation of the [Discover Water](#) dashboard,

delivered by Water UK. The Discover Water members are UK water and wastewater service suppliers for England, Scotland, Wales and Northern Ireland.

We pushed companies to demonstrate that they are putting their customers at the heart of their business planning through a step-change in the range and quality of customer engagement. Our focus on customer engagement led to the Welsh companies taking into account the variations in the priorities of their customers.

Finally, we looked for independent assurance from customer challenge groups on the quality of each company's customer engagement and the extent to which customer views are reflected in company plans. The membership of Welsh companies' customer challenge groups include organisations and individuals that have a specific understanding of Welsh customers and Welsh issues. These include Natural Resources Wales, the regulatory body and principal advisor to the Welsh Government on environmental issues, as well as the Consumer Council of Water in Wales, the statutory representative of water consumers.

Objective

We expect Ofwat to take due account of current and future differences in both policy and law between the UK and Welsh Governments including where new obligations on water companies in Wales emerge.

Our PR19 approach has taken due account of differences in both policy and law between the Welsh and UK Governments. For example, public authorities, including Ofwat and Welsh water companies, are subject to a biodiversity and resilience of ecosystems duty under the Environment (Wales) Act 2016 in relation to Wales. The biodiversity duty under this act is different from the biodiversity duty that applies under the Natural Environment and Rural Communities Act 2006 in relation to England. Hafren Dyfrdwy, for example, proposed a bespoke performance commitment around hectares managed for biodiversity, which we are accepting.

Both Welsh companies proposed bespoke performance commitments around the provision of Welsh language services. This is in line with the Welsh Government's policy aim, set out in their [Cymraeg 2050 Welsh language strategy](#), of increasing the range of services offered to Welsh speakers.

We have also required company boards to provide assurance that their company will continue to comply with their statutory and licence obligations, now, and in the future. So the boards of Welsh companies provide assurance that they will continue to comply with all their legal obligations, including all distinct statutory obligations for

Wales stemming from the Welsh Government. Our final determinations will help companies to manage future change to statutory obligations so that companies remain able to finance their functions, while protecting customers.

Our PR19 approach has been consistent with the Welsh Government's policy regarding competition. For example, our final determinations reflect that:

- Business retail competition has not been extended to wastewater customers and water customers who use less than 50 million litres of water a year – so we will protect these customers by setting an average revenue control based on net margins for retail activities.
- We expect Welsh companies, in carrying out a direct procurement for customers³ process, to make sure that the approach they follow will take the Welsh Government's strategic priorities and objectives into consideration, as well as reflecting best value for money.
- Upstream competition is not going to be extended to Welsh companies. The water resources price controls for Welsh companies do not, therefore, need to reflect this possibility and the regulatory burden on Welsh companies is lower.

Objective

Ofwat should have regard to how it can enable or incentivise companies to contribute to the delivery of Welsh Government policy and strategies. Ofwat should set out clearly how any of its major decisions are consistent with the Welsh Government's strategic priorities and objectives, for example when establishing the methodology for price reviews, presenting proposals for changes to the regulatory framework such as modifications to undertakers' conditions of appointment, or publishing determinations.

This document sets out how our approach has taken account of the Welsh context. In addition, we have carefully considered the wider context of Welsh Government policy objectives, such as those put forward in the Well-being of Future Generations (Wales) Act 2015. This was reflected in our PR19 final methodology, in which we emphasised our approach to long-term resilience. This approach is also reflected in

³ Direct procurement for customers is a process where water companies competitively tender for a third-party to design, build, finance, operate and maintain new infrastructure.

the seven resilience principles that we expect companies to include in their business plans. In our draft and final determinations we have intervened, where necessary, to make sure that companies' approach to resilience is consistent with these principles.

A number of the common and bespoke performance commitments have been designed to incentivise a long-term approach to resilience, in line with the Well-being of Future Generations Act (see 'Long-term' priority below).

In addition, our approach to environmental sustainability has been informed by relevant Welsh policy, including Natural Resource Wales's [State of Natural Resources Report](#) and the Welsh Government's [Water Strategy for Wales](#).

Objective

Objective: Ofwat should consider the clarity and cohesion of its regulatory framework taken as a whole and in a specific Welsh context. Ofwat should have regard to the desirability of a simple, effective and efficient regulatory framework. Ofwat should seek to maintain a transparent regulatory framework that allows companies, investors and customers to plan for the long-term, whilst incentivising efficiency improvements.

Our PR19 approach has reflected our enduring price control principles, which we set out at the last price review. These principles include:

- the better regulation principles of targeted price controls;
- proportionate price setting;
- effective incentives; and
- transparency and predictability.

From our initial consultation, 'Delivering Water 2020', to our draft methodology, to our draft determinations and, now, in our final determinations, we have placed an emphasis on transparency and consultation in our approach to PR19. The consultations on our draft determinations were public consultations and open to all stakeholders.

Throughout the PR19 process, we have engaged Welsh stakeholders in order to fully consider the specific context of Wales. These stakeholders include:

- the Welsh Government;
- Natural Resources Wales; and
- other Welsh companies.

We have also engaged with company and NGO stakeholders in Wales as part of the Welsh Government's PR19 Forum. We would like to thank them for their contribution.

As set out in the section on the Welsh Government's 'Long-term' priority below, we have challenged companies to plan on a long-term basis. We expected companies' business plans to reflect longer-term strategies and their water resources management plans.

Finally, we incentivise companies to be more efficient by considering wider evidence of efficiency gains and frontier shift, to drive a step change in efficiency across the sector. We develop our view of the efficient total expenditure (totex) allowance by benchmarking water companies to the most efficient companies within the sector. We challenged companies' investment proposals to make sure customers pay only for efficient investment and that they are protected if the investment is not delivered.

3. The Welsh Government's priorities for the water sector

Priority

Affordability

Affordability has been one of the key themes of PR19. The Consumer Council for Water reports that 77% of customers of Welsh companies agree that their water and/or sewerage charges are affordable.⁴ For those Welsh customers who do not find their bills affordable, we have gone further than any other price review to make sure they are protected. We consider affordability in both the short and long term (see 'Long-term' priority below).

In our final methodology for PR19, we set out the five principles against which we would assess companies' plans on improving affordability:

- customer engagement;
- customer support;
- effectiveness;
- efficiency; and
- accessibility for customers who are struggling to pay.

We have pushed companies to improve their efficiency to make sure that Welsh customers are paying a fair price for the service they receive. We benchmark companies (within the sector and against other sectors, where appropriate) to assess cost efficiency and set efficient and stretching cost baselines. We have challenged Welsh companies' service quality commitments through our outcomes assessment, so customers receive good value for money. And we are also setting a record low cost of capital for the sector, which will help to reduce bills.

⁴ See 'Water Matters' 2019, p. 47.

Our final determinations make water services more affordable, through:



A 9% fall in bills before inflation for customers in Wales: By reducing the average bill, we are making water more affordable for customers, including for those struggling to pay. This is driven by our lower cost of capital and our efficiency challenge.



Additional support measures for those who find their bills unaffordable: Companies in Wales have engaged their customers on the benefits of social tariffs and are planning to increase the number of customers supported. By 2025, 137,000 customers in Wales should receive help through social tariffs and WaterSure Wales.⁵



New approaches to dealing with problem debt: In relation to dealing with debt, Hafren Dyfrdwy has stated it will offer 'payment matching', whereby the company forgoes debt for customers who make regular payments.

Priority

Innovation

Innovation has been one the key themes for PR19. Innovation is critical to empowering Welsh companies to deliver against the ambitious policy goals for Wales, as well as delivering benefits to customers, the environment and wider society. Throughout the PR19 process, we have incentivised companies to produce ambitious and innovative plans through financial and reputational incentives. Examples of innovative plans proposed by Welsh companies include Dŵr Cymru's RainScope strategy in central Llanelli, where 20% of the urban drainage area has

⁵ WaterSure Wales is a scheme that caps bills for certain customers with a water meter.

been diverted into natural watercourses using green infrastructure such as roadside planters, trees, larger basins and swales.

Innovation will play an important role in enabling Dŵr Cymru and Hafren Dyfrdwy to deliver against the strong efficiency challenge and stretching performance commitments we include as part of the final determination packages, such as to reduce:

- leakage;
- per capita consumption; and
- the amount of lead in drinking water at customers' taps (where lead concentration is detected above 5 µg/l) by replacing lead communication and customer-owned supply pipes.

Our final determinations support innovation in the water sector in Wales, through:



Outcome-focused incentives framework: Water companies will need to innovate to meet the challenges facing the sector in Wales from climate change, while improving affordability. Our outcomes framework provides flexibility and freedom to innovate and to develop solutions reflecting the preference of their customers and communities. By setting stretching outcome performance commitments, we have challenged Welsh companies to innovate and to go further for their customers. This will encourage companies to look for innovative ways to deliver better services to customers and improve the environment.



Going further: In addition to our existing package of measures, which encourages companies to innovate individually, we are considering more widely how we can stimulate innovation within the sector. In our new strategy for regulating water and wastewater companies, we highlight that innovation is crucial for meeting the challenges the sector faces.

The adoption of innovative approaches is key to delivering long-term resilience and great customer service at an affordable price, and the sector will need to step up and increase innovation in order to meet the strategic challenges it faces in a cost-effective and sustainable way. We also want to see companies work more effectively together and with their supply chain to better tackle these challenges.

In our [consultation](#) earlier this year, 'Ofwat's emerging strategy: Driving transformational innovation in the sector', we explored options for customer-funded interventions designed to drive innovation to benefit customers in the longer-term. Having reviewed the responses to the consultation, we have published our decision alongside the PR19 final determinations. We are making up to £200m available for innovation activities for the period 2020-25 through the introduction of an innovation competition. We will work together with companies and other stakeholders in the sector to set up a competition which will drive innovation in the sector to the benefit of customers across Wales.

Priority

Long-term

In our PR19 methodology, we challenged companies to plan on a long-term basis and for their business plans to reflect longer-term strategies and their water resources management plans.

We pushed companies to consider the appropriate balance between short-term affordability and long-term affordability, resilience and performance.

Our challenges have been reflected in positive examples of long-term planning presented as part of companies' business plans, such as the Welsh Water 2050 strategic vision, which provides a high level assessment of future trends that will have an impact on the resilience of the business.

We also required companies to provide a detailed work programme to assure us they will deliver appropriate drainage and wastewater management plans to inform PR24 business plans.

Our final determinations support a long-term approach to planning and delivery, through:



Investing to meet the water supply needs of future

customers: Our final determinations provides Welsh companies with £49 million funding for new water supply solutions and programmes to manage water demand that are consistent with the needs identified in the water resources management plans, which account for climate change, environmental protection, and population growth. These include solutions for severe drought resilience and water efficiency activities to support customers reduce their water consumption.



Promoting long term sustainability in wastewater planning:

We have welcomed the scope of the National Environment Programme developed by Natural Resources Wales. We scrutinised companies' plans to make sure that they deliver the programme efficiently. In addition, as a part of our initial assessment of companies' business plans, we required relevant companies to deliver appropriate and timely plans for their drainage and wastewater management plans. We asked companies to make sure that they can prepare and consult on their first drainage and wastewater management plan no later than the summer of 2022. This deadline will give companies time to prepare revised plans in early 2023 to inform PR24 business plans. Companies were asked to produce a detailed work programme before the end of August 2019. All companies have submitted work programme plans that meet the requirement. Our price review also introduces a separate control for bioresources: wastewater sludge transport, treatment, recycling and disposal. This control is designed to encourage management focus on bioresources activities and so encourage companies to use and trade this resource in a more efficient and sustainable way to the benefit of customers and the environment, such as by increasing the transformation of waste to energy.



Maintaining high standard of drinking water quality over the long term:

We have placed a common performance commitment on Welsh companies regarding the quality of the water supply. Quality will be measured against the compliance risk index, which the Drinking Water Inspectorate has developed in consultation with the industry. As noted above, we have also allowed increased funding for Welsh companies for the removal of lead pipes from the water supply network.



Engaging customers on long term issues: In developing their plans, we expected companies to engage their customers on longer term issues, such as resilience, and take into account the needs and requirements of future customers. This included, but was not limited to:

- independent evidence from their customer challenge groups on the quality of engagement; and
- the extent to which customer views are reflected in company plans.

For example, Hafren Dyfrdwy explained that it conducted specific asset health and resilience research, which shaped performance commitments and investment decisions. Dŵr Cymru explored long term and intergenerational issues with future customers by using its Youth Board. Their views helped to shape the Welsh Water 2050 strategy document and the company's business plan for 2020-25.

Priority

Markets and competition

Our regulatory approach is consistent with the Welsh Government's policy not to extend retail competition or introduce upstream competition.

In line with the Welsh Government's policy, we have sought to consider opportunities where the promotion of markets can help to achieve other priorities of the Welsh Government, such as:

- affordability;
- innovation;
- resilience; and
- a strong customer focus.

Direct procurement for customers is a process where water companies competitively tender for a third-party to design, build, finance, operate and maintain new infrastructure. We have considered carefully how we can best ensure that our

approach to direct procurement furthers the Welsh Government's strategic priorities and objectives, including the priority that Ofwat's approach to markets should not undermine the accountability of existing undertakers or the integrity and efficiency of the management of the network.

The direct procurement for customers process in Wales – where we have identified Dŵr Cymru's new Merthyr treatment works as offering best value for money when delivered this way – will help to deliver the following priorities of the Welsh Government:

- Affordability — by ensuring that Dŵr Cymru evaluates efficiency gains and seeks to deliver more for less in order to deliver value for money in water and wastewater services.
- Innovation — by Dŵr Cymru considering new ways of delivering services for customers and the environment more efficiently.

As the appointee, we expect Dŵr Cymru to follow the direct procurement for customers process in its delivery of projects. We also expect that as it develops projects, Dŵr Cymru will take into consideration the Welsh Government's aims in its economic action plan especially with regard to procurement, innovation and employment in Wales.

We, therefore, are confident that the direct procurement for customers approach will actively support the delivery of the Welsh Government's priorities and objectives for the sector in Wales.

There are currently no plans for a bilateral market in Wales. By 'bilateral market', we mean a third party provider of water resources other than a water company (such as the holder of an abstraction licence) contracting directly with a retailer to sell water to its business customers. Any model for water resources that is put in place for companies whose areas are wholly or mainly in England will, therefore, not apply to incumbent companies whose areas are wholly or mainly in Wales.

Our final determinations promote the development of markets in Wales, to the extent that this is consistent with Welsh Government policy, through:



Creating new markets in bioresources: By enabling companies to procure bioresources services from a range of suppliers, we will unlock efficiencies that can be reinvested in the areas that customers value most. Dŵr Cymru provided a good example of how to conduct an initial assessment of market opportunities, carrying out geospatial analysis using publically-available bioresources market information. The company showed that it has 21 raw sludge producing sites that are closer, by road distance, to the treatment centres operated by other water companies than they are to its own treatment centres. This analysis provided an initial indicator of the scale of possibilities and where it should look to undertake further work.



Implementing our new framework for direct procurement:

The direct procurement for customers approach promotes innovation and resilience by allowing new participants to bring fresh ideas to the delivery of key projects where it can deliver greater value for customers.

We identified Dŵr Cymru's new Merthyr treatment works, which replaces 3 smaller obsolescent water treatment works in Cwm Taf, as offering best value for money when delivered by a direct procurement for customers process, while also maintaining both the accountability of existing undertakers and the integrity and efficiency of the management of the network.

The construction of the new treatment works spans the 2020-25 and 2025-30 price controls, so a 'direct procurement for customers' approach will provide greater long-term certainty for the delivery of this scheme.

Resilience is vital to current and future Welsh customers. The water sector faces serious resilience challenges including climate change and population growth, which present real threats to the resilience of assets, water resources and services to customers; for example, from the risks of flooding. The combination of these threats and changes in people's expectations – including about how we treat the environment itself – makes tackling these resilience challenges urgent.

This is a key priority for the Welsh Government and us, and long-term resilience has been one of the key themes for PR19.

Customers expect reliable water and wastewater services that can avoid, cope with and recover from disruption, as well as protect the natural environment. This means in order to make decisions about their operations, maintenance and investment in the short and long term, water companies need the right:

- information;
- systems;
- processes;
- governance;
- capabilities; and
- finances.

They need to have operational, financial and corporate resilience: to be 'resilient in the round'.

We expected companies to identify and act on the risks of flooding, including the additional challenges created by climate change, and make sure these risks are reflected in their investment and delivery plans. We asked companies to develop drainage and wastewater management plans to support integrated approaches to wastewater flooding.

Asset health⁶ is an important element of operational resilience and central to the long term delivery of services to customers. We required companies to make a set of

⁶ The maintenance of physical items, such as pipes and sewers, that allow companies to provide water and wastewater services.

performance commitments reflecting asset health of water and wastewater services, as part of their business plans.

We pushed companies to take a ‘twin track’ approach to improving resilience of water resources, with investment in new water supplies complementing measures to reduce the demand for water. In our final methodology, we expected companies to consider a wide range of options to achieve long-term resilience in water supply, including:

- new supply investment;
- demand management;
- water efficiency measures;
- leakage reduction;
- water trading; and
- solutions that extend beyond traditional boundaries.

We worked closely with Natural Resources Wales and the Welsh Government during the consultation and assessment of companies’ water resources management plans (WRMPs). WRMPs set out the likely range of interventions that companies plan to make sure that there is secure, sustainable and affordable supplies of water over at least the next 25 years. This collaboration aimed to make sure that the plans meet the needs of the environment, accounting for climate change, as well as the expectations of customers for best value resilience.

A WRMP is an important process that helps to inform a water company’s business plan. We took into account the identified needs and preferred solutions in the latest WRMPs but undertake a more in depth analysis of the proposed solutions when assessing the business plan. In assessing companies’ proposals, we have aimed to ensure that companies invest efficiently to make sure water is available in both the short term and the longer term (i.e. beyond 2025). Where appropriate, we allow funding for water resources solutions that may not deliver benefits straight away but are important for long-term drought resilience.

In line with our resilience planning principles, we expected companies to consider ‘resilience in the round’, taking an objective and comprehensive view of the risks they face. We considered whether companies took a systematic and integrated approach to identifying and assessing all the diverse risks to the resilience of systems and services across the business.

We also expected companies to apply a robust, objective, comprehensive and well evidenced assessment of priority risks to the delivery of the services their customers

depend on, over the next five years and over the longer term. This assessment needed to consider risks to infrastructure, systems, processes, and people.

Companies were also required to consider hazards and threats, such as:

- physical and cyber-attacks;
- extreme flood events; and
- disruptions to energy supplies.

While some of these individual aspects have been considered by companies' plans, they need to do more to make sure 'resilience in the round' is embedded across the whole of the business. As a result, we asked companies to provide resilience action plans by 22 August 2019, to demonstrate that they have put tangible measures in place to implement their resilience frameworks promptly and to provide confidence that frameworks will be applied in practice. The action plans should build on the companies' revised business plans and provide a set of actions that address key elements of our feedback.

All Welsh companies have now submitted an action plan. In general, the action plans suggest that Welsh companies have further to go in developing a systems based approach to resilience, although this varies significantly between companies. In particular:

- While Dŵr Cymru has commissioned a review of best practice in resilient systems approaches to inform its action plan going forward, Hafren Dyfrdwy's plan lacks elements to integrate systems thinking in its approach to resilience.
- While Dŵr Cymru uses a baseline assessment of resilience maturity to inform its action plan, Hafren Dyfrdwy's fails to do this, so areas in need of improvement are not identified and supported by specific actions.
- Both companies' action plans lack applied elements of their resilience frameworks (e.g. prioritisation and assessment of risks) and fail to demonstrate a line of sight between risks, mitigations and outcomes.
- Action plans provide limited information on reporting, monitoring, assuring and resourcing the plan, leading to concerns around its deliverability.

While we will not be providing further specific actions to Welsh companies to develop their action plans, we expect to engage the sector further through the implementation of our strategy. This will encourage further shared learning and development of resilience approaches, to accelerate best practice across the industry. We may

consider the progress companies have made in this area as part of assessing company business plans in the 2024 price review.

Finally, companies are responsible for making sure that their financial structures will be resilient for 2020-25 and for the long term. We expected them to assess their financial resilience using both prescribed and company-specific stress tests covering cost and revenue shocks. We also expected companies to demonstrate that they have appropriate risk management and mitigation approaches in place.

Our final determinations will enhance the sector's resilience in the round, through:



Investing in resilience and sustainability: During the 2020-25 period, Welsh companies will invest £23.2 million to improve resilience in water and wastewater, including £15 million to mitigate the risk of water supply asset failures in south Wales. We challenged companies to demonstrate the resilience benefits of their investment proposals and our allowance is for well-evidenced proposals.



Incentivising companies to prevent sewer flooding and pollution incidents: Welsh companies are committing to a 32% reduction in pollution incidents by 2024-25, as well as a 32% and 25% reduction of internal and external sewer flooding incidents, respectively.



Security funding: We are providing funding of £14 million to protect against physical and cyber threats in Wales. This builds on the physical security funding provided during the 2015-20 period to make sure companies are compliant with the Security and Emergency Measures Direction (SEMD). We are also providing funding to improve cyber security in the sector. This includes compliance with the Security of Network and Information Systems (NIS) Directive.



Challenging companies' plans on asset health: We intervened in Welsh company asset health performance commitments where these commitments did not improve their asset health during the 2020-25 period and where they were not in line with other companies' performance commitments in Wales and England. Both companies will be required to maintain performance of the sewer network in line with their best historical performance. Both companies are committed to a small improvement in performance of the number of mains repairs that are undertaken where our interventions take into account the link between proactive mains repairs and leakage reduction. For treatment works, both companies will be required to ensure their treatment works meet compliance requirements all of the time.



Incentivising investment in assets: We also made sure that asset health performance commitments are backed by appropriate financial incentives. Welsh companies have our four common asset health performance commitments alongside their bespoke asset health performance commitments. These will help make sure that companies have the incentives to invest in and maintain their assets so that they will be able to provide services now and into the future, which is what matters to customers. In addition, we have allowed Dŵr Cymru £97 million to improve water quality through asset upgrades.



Assuring financial resilience: Hafren Dyfrdwy provided Board assurance it will remain financeable through the 2020-25 period. Dŵr Cymru made representations on its financial resilience in the context of the draft determination. We have considered carefully the representations made by Hafren Dyfrdwy and Dŵr Cymru and we consider that our final determinations provide sufficient revenues for both Hafren Dyfrdwy and Dŵr Cymru to be financeable on a notional basis. Each company will be responsible for maintaining financial resilience under its actual capital structure in 2020-25 and beyond.

Priority

Strong customer focus

Great customer service was one of four key themes of our PR19 final methodology. We place great importance on companies responding to the identified preferences and priorities of their customers. When operating their businesses, and developing their business plans, we expect Welsh companies to actively, meaningfully and effectively engage with their customers and stakeholders. This will help them to develop an in-depth understanding of customers' preferences for services, outcomes and investment, and of the affordability of their plan over the long term.

Throughout the PR19 process, we have tested the quality of Welsh companies' customer engagement, including their approach to customer participation and how well their customers' views are reflected across their business plans.

We set out in our PR19 methodology that we expect companies to reflect their customers' preferences in the levels they propose for common performance commitment levels and outcome delivery incentives as well as in bespoke performance commitments. We also expected companies to challenge the level of stretch in their performance commitments against a range of approaches (for example, against comparative and historical information). In our PR19 methodology we also expected companies to use customer valuations to set outcome delivery incentive rates and noted that we would compare these valuations and rates and challenge companies where appropriate. Therefore, when making our decisions, we have taken into account several factors in setting our final determination outcome delivery incentive rates including the quality of customer evidence provided. Our

suite of final determination documents explains the rationale for our decisions, including the evidence used to inform our decisions.

Two of our 14 common performance commitments directly relate to customer experience, with one commitment on residential customers' experience and one on developer services customers' experience. Our customer measure of experience (C-MeX) includes the experiences not only of customers who contact their companies, but also of customers who do not, so that companies are incentivised to deliver for all their customers.

For developers, the new developer services customer measure of experience (D-MeX) incentivises companies to deliver excellent customer service to new connections customers. In addition, we require Welsh companies to have at least one bespoke performance commitment on the quality of the retail services they provide for their business customers.

We set out in our '[Putting the sector in balance](#)' position statement that we required companies to set out clearly in their business plans how their dividend policies and performance related executive pay policies for 2020-25 will align the interests of company management and investors with the interests of customers.

Our final determinations incentivise companies to have a strong customer focus, through:



Delivering excellent service and experience for current

customers: By taking forward a wide range of measures to boost resilience, Welsh customers should benefit from stretching performance for water supply interruptions greater than 3 hours, and a 32% reduction in internal sewer flooding incidents in the 2020-25 period. Companies will also be incentivised to deliver excellent service to their current customers through our new customer and developer services customer experience measures, C-MeX and D-MeX.



A step change in customer engagement: We used evidence presented by each company and its customer challenge group to assess the quality of the company's customer engagement and participation⁷ and how well customers' views are incorporated into the company's business plan and ongoing business operations. In total, Welsh companies engaged with about 45,000 customers during the development of their PR19 plans.



Increasing public value: We accept Dŵr Cymru's plans to invest £5 million in new recreational facilities at reservoirs near Cardiff. Recent housing development in the area is likely to increase demand for access to open spaces.



Increased take-up of priority service register support: We introduced a common performance commitment on priority service registers (a record of consumers who have expressed a need for specific help or service) – this will incentivise companies to:

- make sure that at least 7% of customers are on the priority service register by 2025; and
- make sure the register is accurate and up to date.

As a result of our actions, the number of customers registered for priority services in Wales is set to increase by 81,000 in the years 2020-25.

⁷ See 'Tapped In' report.



Additional support measures to help customers in vulnerable circumstances: Dŵr Cymru is planning on rolling out its place based approach to supporting vulnerable customers, trialled in Rhondda Fach, to five more locations in the 2020-25 period.

Priority

Sustainable management of natural resources

The importance of investing in natural resources and making our ecosystems more resilient is recognised by Natural Resource Wales's [State of Natural Resources Report](#) and Welsh Government's [Water Strategy for Wales](#). Our approach to Welsh companies in the price review process has encouraged companies to engage with customers and stakeholders on sustainable management of natural resources and sought to incentivise companies to manage natural resources in a way which is sustainable for the long term.

In our PR19 methodology, we required companies to have comprehensive coverage of their environmental challenges in their bespoke performance commitments and to take into account customers' preferences and, where appropriate, the environment, biodiversity and natural capital when setting their performance commitment levels and outcome delivery incentives.

These bespoke environmental performance commitments sit alongside the abstraction incentive mechanism (AIM), on which all companies have a bespoke performance commitment. The AIM incentivises water companies to reduce the environmental impact of abstracting water at environmentally sensitive sites during defined periods of low surface water flows.

Our final determinations support the sustainable management of natural resources in Wales, through:



Major environmental investment: We provide £218 million of funding for the National Environment Programme (NEP), which will improve the natural environment in Wales. Dŵr Cymru has a performance commitment to work with landowners to reduce pollution in areas where there is a risk of further treatment being required because land use is causing pollution of raw water. It is far better to reduce pollution than increase treatment, which has additional impacts in terms of carbon.



Promoting sustainable management: We are supportive of the adoption of 'sustainable drainage' approaches to surface water management to reduce spill from combined sewer overflows, for example, Dŵr Cymru's Menai Straits programme. More broadly, environmental resilience and natural capital valuation appear to be at an early stage within companies' plans.



Reducing water wastage: Welsh companies are committing to a 15% reduction in annual average leakage from 2019-20 commitments over the price review period. This should save 27 million litres of water per day in Wales during the 2020-25 period.



Reducing water consumption: Welsh companies will take forward a range of measures to reduce overall household consumption of water by 22 million litres of water per day as a result of helping their customers use water more efficiently. This will reduce the burden on water supplies. Per capita, consumption is set to be reduced to 136 litres per person, per day in Dŵr Cymru's region, and to 135 litres per person, per day in Hafren Dyfrdwy's region. This is as a result of water efficiency activities and educational campaigns. We have accepted the commitment made by Hafren Dyfrdwy, but intervened to tighten Dŵr Cymru's commitment from 138 to 136 litres per customer, per day, matching both the upper quartile of reductions promised by companies in Wales and England and the company's WRMP when taking into account the difference between a dry year and a normal year.

Ofwat (The Water Services Regulation Authority) is a non-ministerial government department. We regulate the water sector in England and Wales.

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