

October 2021

**Draft determination of Hafren Dyfrdwy's
in-period outcome delivery incentives
for 2020-21**

About this document

This document provides our draft decision on the extent to which the price controls set by our [PR19 final determinations](#) need to be adjusted to reflect Hafren Dyfrdwy's performance for the 2020-21 Charging Year, under [Part 3A of Condition B](#) of the company's licence. The specific changes, and our reasons for these, are set out in this document and in [Sector overview: Draft determinations of in-period outcome delivery incentives for 2020-21](#), which concerns the impact of our draft determinations across the companies.

We also publish models related to our draft determinations on our [website](#).

Executive summary

This section sets out the results of our 2020-21 in-period outcome delivery incentives (ODI) assessment for Hafren Dyfrdwy. ODIs are the financial or reputational consequences for companies of outperformance or underperformance against its performance commitments. Performance commitments are the pledges companies made to their customers and stakeholders at the 2019 price review (PR19) about service levels to make progress towards their outcomes.

'In-period' ODIs bring ODI payments closer in time to when customers experience a given level of performance. We do this through an annual reconciliation process between July and November following the relevant reporting year, in this case 2020-21. The results of our assessment for 2020-21 will affect Hafren Dyfrdwy's bills in the 2022-23 charging year.

For 2020-21 Hafren Dyfrdwy reported net underperformance payments of £0.532m against its performance commitments with in-period outcome delivery incentives, excluding C-MeX and D-MeX. After applying its bespoke aggregate underperformance sharing mechanism, Hafren Dyfrdwy reported a net underperformance payment of £0.423m. We have assessed the company's performance against its performance commitments. In our draft determination, we are intervening on the following performance commitments:

- Per capita consumption (PCC) – in line with our July consultation proposals, we are changing the timing of our determination of the value of ODI payments for this performance commitment to end of period.
- C-MeX and D-MeX – we are including a C-MeX underperformance payment of £0.035m and a D-MeX outperformance payment of £0.035m, based on assessment of 2020-21 company performance in our draft determinations.

We also set out our proposed approach to applying Hafren Dyfrdwy's aggregate underperformance sharing mechanism.

See section 2.2, 2.3 and 3.1 for details of our interventions.

In our draft determination we propose that the amount of revenue the company can recover from its customers in 2022-23, as a result of its performance against its performance commitments with in-period ODIs in 2020-21, is reduced by £0.750m. This figure includes C-MeX and D-MeX payments as well as deferrals and bespoke adjustments but is before adjustments for inflation, tax and other relevant factors.

Contents

1. Introduction	4
1.1 Background	4
1.2 Purpose of this document	5
2. Results of our assessment	6
2.1 Reported performance	6
2.2 Key interventions	6
2.3 Payment deferrals and abatements	8
3. Impact of 2020-21 in-period ODI assessment on price controls	9
3.1 Our draft determination	9
4. Next steps	14

1. Introduction

1.1 Background

Hafren Dyfrdwy's performance commitments for the 2020-25 period are set out in [PR19 final determinations: Hafren Dyfrdwy - Outcomes performance commitment appendix](#).¹ Most of the company's performance commitments have financial incentives which are paid 'in-period'. This brings ODI payments closer in time to when customers experience a given level of performance. The remaining financial incentives are end of period.

Hafren Dyfrdwy reported its performance against these performance commitments in its annual performance report (APR) in July 2021. We have considered this information and, where necessary, further information from companies' answers to our queries. In our draft determination we set out relevant adjustments to the company's price controls, for one or more future years, in accordance with [Part 3A of Condition B](#) of its licence (Performance Measure Adjustments, referred to in this document as 'in-period' determinations). Our determination, when final, will affect Hafren Dyfrdwy's customers' bills from the 2022-23 charging year.

As set out in the PR19 final determinations, outperformance payments above 3% of a company's wastewater or water regulatory equity for that year are shared with customers. This means companies receive 50% of outperformance performance payments above this threshold.

In addition to this, Hafren Dyfrdwy's [PR19 final determination](#) sets out that total net ODI underperformance payments to customers of more than 3% of the company's regulatory equity for that year are also to be shared with customers. We said this was to mitigate the risk to the company of excessive downside outcome delivery incentives due to the lack of long-term historical data and the small size of the company.

These sharing mechanisms automatically apply to all ODI payments except to the customer measure of experience (C-MeX), developer measure of experience (D-MeX) and those allocated to retail price controls.

¹ We take account of performance commitments as set out in the PR19 definitions adjusted, if relevant, by the annex 2 process. Annex 2 of the company's performance commitment appendix provides for changes and corrections to be made to its performance commitment definitions during the 2020-25 period in certain circumstances. An overview of changes and corrections made to companies' performance commitment appendices can be found at [PR19 Outcomes performance commitments: changes and corrections](#).

1.2 Purpose of this document

This document provides detailed information relating to the extent to which the price controls for the 2020-25 period need to be adjusted to reflect Hafren Dyfrdwy's performance for the 2020-21 Charging Year. These changes are the result of the company's performance against its in-period ODIs as set out in the PR19 final determinations. This is our draft decision for consultation. We welcome your views by 21 October 2021 as set out in section 4. We will make our final determinations by 15 November 2021.

2. Results of our assessment

2.1 Reported performance

Hafren Dyfrdwy's reported performance for 2020-21 against its performance commitments with in-period ODIs is set out in table 3.1. The company's largest individual underperformance payment was £0.618m for its water supply interruptions performance commitment. The company's largest individual outperformance payment was £0.150m for its performance commitment relating to the number of lead pipes replaced.

Hafren Dyfrdwy reports that it has triggered both the aggregate outperformance sharing mechanism, which can apply to all companies, and its bespoke underperformance sharing mechanism, which is set out in section 1.1.

2.2 Key interventions

We are not proposing any interventions on individual performance commitments in our draft determination, other than for C-MeX and D-MeX and for per capita consumption as set out in sections 2.3 and 3.1.

Leakage

The use of common, converged methods for reporting data increases transparency for all stakeholders and makes comparisons across the sector more meaningful. As stated in our overview document, we had expected that all companies would have been compliant with our [PR19 common performance commitment definitions](#) when reporting 2020-21 leakage performance. In IN21/01 we said that "If the data submitted is not based on a fully converged methodology then companies should clearly state this and demonstrate that not being fully compliant does not have a material impact on the reported performance. If the move to convergence affects baselines for any performance commitments then companies should also show this clearly." However, we note that for leakage and per capita consumption reporting Hafren Dyfrdwy has not achieved full compliance with this methodology.

Whilst most companies were able to demonstrate that the impact of not being fully compliant with the methodology for leakage data was not material, in the case of Hafren Dyfrdwy the company has not been able to quantify the impact of non-compliant components on reported performance. As part of its response to this draft determination, we expect Hafren Dyfrdwy to quantify the impact of non-compliant components of its leakage performance commitment on its reported performance. Should the impact of the non-compliant components be material, in our final determinations we may defer our decisions on these performance commitments to 2022.

It is our expectation that there should not be any components of the company's leakage and per capita consumption methodology that are not fully compliant when reporting 2021-22 performance. We will closely assess any non-compliant elements in the 2021-22 APR submissions and will consider what interventions might be appropriate in light of our findings. Should any leakage information be revised or restated, we will take account of adjustments we have made to the relevant price control in relation to the leakage performance commitment in making future in-period determinations.

Underperformance sharing mechanism

We have assessed Hafren Dyfrdwy's reported performance with respect to its bespoke underperformance sharing mechanism. We consider the company's calculations do not fully account for our PR19 final determination, where we state that we will share total **net** ODI underperformance payments if they are more than 3% of regulatory equity in any year. This is in contrast to the outperformance sharing mechanism which is calculated on a gross basis.

While we did not define whether the threshold for underperformance sharing would apply separately to water or wastewater regulatory equity, we consider it is reasonable and broadly consistent with the outperformance sharing mechanism for this to be the case.

We concur with the company that it has not triggered underperformance sharing for its water-related performance commitments but that it has triggered underperformance sharing for wastewater-related performance commitments. However, we calculate a different amount of underperformance payments to be shared as follows:

- Based on notional regulatory equity of £0.617m for wastewater (wastewater network plus and bioresources), we calculate the sharing threshold to be £0.018m.
- With gross outperformance payments of £0.021m and gross underperformance payments of £0.056m for performance commitments allocated to either the wastewater network plus or bioresources price controls, we estimate total **net** underperformance payments to be £0.035m.
- Since this is beyond the sharing threshold of £0.018m, then underperformance payments beyond this threshold are to be shared equally between customers and the company. We calculate this to be £0.008m (or £8,300). This is less than the company's calculation of £0.009m (or £9,000).

For simplicity we propose to apply this as a positive revenue adjustment using the new 'bespoke adjustments' function of the in-period adjustments model. The outperformance sharing mechanism will continue to be applied through the ODI performance model, consistent with all other companies.

2.3 Payment deferrals and abatements

As set out in our [PR19 final determinations](#) and the [PR19 Reconciliation Rulebook: Guidance Document](#), companies can ask us to defer outperformance or underperformance payments, or abate outperformance payments on individual performance commitments. A deferral results in us delaying when the adjustment will be made to companies' revenue. An abatement results in no adjustment to the company's revenues in relation to the relevant performance commitment in the subsequent charging year.

Hafren Dyfrdwy reported underperformance payments relating to its per capita consumption performance commitment but did not include them as a payment deferral in its submitted in-period adjustments model. In our [July 2021 consultation](#) on changing the timing of ODI payments for per capita consumption performance commitments, we proposed that they should be end of period for all companies. Prior to our July 2021 consultation, we had asked relevant companies to include ODI payments arising from their per capita consumption performance commitments in the deferrals function of the in-period adjustments model. We now consider it would be more appropriate to reflect this proposed treatment through the ODI performance model, ensuring consistency with our policy proposals and ensuring that all ODI payments accrued during the 2020-25 period can be applied at PR24, when we will make our final decisions.

Hafren Dyfrdwy did not request any payment abatements. Based on our assessment of the company's performance, we do not consider any are required. As such, we do not apply any payment abatements in our draft decision.

3. Impact of 2020-21 in-period ODI assessment on price controls

3.1 Our draft determination

In this section we outline the financial impacts of our draft decisions. First, we set out our view compared to the company's requested ODI payments in table 3.1.

Table 3.2 sets out the C-MeX and D-MeX payments included in our draft determination.

Table 3.3 summarises the overall ODI payments, after other payments and relevant adjustments, that the company is due based on its performance in 2020-21.

Table 3.4 sets out our draft decisions on deferrals and abatements and how we propose that these payments should be applied in 2022-23.

Table 3.5 sets out the impact of our draft decisions on the company's relevant price controls.

Unless otherwise stated all values are £m in 2017-18 FYA CPIH prices.

Table 3.1: In-period ODI payments for 2020-21 by price control (excluding C-MeX and D-MeX)

This table sets out the in-period ODI payments requested by Hafren Dyfrdwy for 2020-21, by price control, and our draft determination on these payments after any interventions.

Further detail on how these overall numbers have been derived is set out in the ODI performance model, which we have published on our website as part of the draft determinations. Where we have applied interventions, this is set out in "Ofwat_PC_Interventions" in the ODI performance model for this company.

Price control	Company's reported payments (£m)	Our draft decisions after interventions (£m)	Difference (£m)
Water resources	-0.326	-0.276	0.050
Water network plus	-0.197	-0.147	0.050
Wastewater network plus	-0.037	-0.037	0.000
Bioresources	0.000	0.000	0.000
Residential retail	0.039	0.039	0.000
Business retail	-0.012	-0.012	0.000
Total payments	-0.532	-0.432	0.101

See section 2.2 for details of our interventions on the company's performance commitments.

Table 3.2: C-MeX and D-MeX payments

Our draft determinations include the following C-MeX and D-MeX payments for this company:

Price control	C-MeX payments (£m)	D-MeX payments (£m)
Residential retail	-0.035	n/a
Water network plus	n/a	0.034
Wastewater network plus	n/a	0.001
Total payments	-0.035	0.035

We have taken the data from the company's APR submissions and compared this against the recorded data from our survey agent, Accent.

Further details on C-MeX and D-MeX can be found on the [Customer and Developer Services experience](#) pages of the Ofwat website and in the published C-MeX and D-MeX models.

Table 3.3: ODI payments including C-MeX, D-MeX, bespoke adjustments and deferrals from 2019-20 (before 2020-21 deferrals and abatements)

This table sets out the composition of total ODI payments, including C-MeX and D-MeX, brought forward deferrals and bespoke adjustments where relevant, but before our draft decisions on 2020-21 deferrals and abatements.

Price control	Ofwat view of in-period ODI payments (£m)	C-MeX and D-MeX payments (£m)	ODI payments deferred from 2019-20 (£m)	Bespoke adjustments (£m)	Total ODI payments (£m, before 2020-21 abatements and deferrals)
Water resources	-0.276	0.000	-0.003	0.000	-0.279
Water network plus	-0.147	0.034	-0.172	0.000	-0.285
Wastewater network plus	-0.037	0.001	-0.152	0.008	-0.179
Bioresources	0.000	0.000	0.000	0.000	0.000
Residential retail	0.039	-0.035	0.000	0.000	0.004
Business retail	-0.012	0.000	0.000	0.000	-0.012
Total	-0.432	0.000	-0.327	0.008	-0.750

Table 3.4: 2020-21 ODI payments after deferrals and abatements

This table sets out our draft decisions on the ODI payments to be applied, after deferrals and abatements, as set out in the in-period adjustments model published on our website for this company.

Price control	Total ODI payments (£m, before 2020-21 deferrals and abatements)	Ofwat proposed deferrals (£m)	Ofwat proposed abatements (£m)	Total ODI payments to be applied in 2022-23 (£m)
Water resources	-0.279	0.000	0.000	-0.279
Water network plus	-0.285	0.000	0.000	-0.285
Wastewater network plus	-0.179	0.000	0.000	-0.179
Bioresources	0.000	0.000	0.000	0.000
Residential retail	0.004	0.000	0.000	0.004
Business retail	-0.012	0.000	0.000	-0.012
Total	-0.750	0.000	0.000	-0.750

See section 2.3 for our decisions relating to deferrals and abatements for this company.

Table 3.5: Changes to price controls (draft determinations)

This table sets out the impact of our draft decision on the company's price controls, as set out in the in-period adjustments model published on our website. See [Sector overview: Draft determinations of in-period outcome delivery incentives for 2020-21](#) for how propose to apply adjustments for tax and inflation.

Price control		2021-22	2022-23	2023-24	2024-25
Water resources (K factors)	Previous determination	-5.24	-26.84	-3.91	1.45
	Revised	-5.24	-38.72	13.87	1.45
Water network plus (K factors)	Previous determination	4.42	3.49	2.30	-0.96
	Revised	4.42	1.30	4.45	-0.96
Wastewater network plus (K factors)	Previous determination	1.50	8.14	3.95	6.18
	Revised	1.50	-0.79	13.05	6.18
Bioresources (unadjusted revenue, UR_t – £m, 2017-18 Nov CPIH prices)	Previous determination	0.761	0.769	0.776	0.784
	Revised	0.761	0.769	0.776	0.784
Residential retail (total revenue, TR_t – £m, nominal prices)	Previous determination	2.861	2.888	2.917	2.942
	Revised	2.861	2.894	2.917	2.942
Business retail (allowed average retail cost component, rc_t – £, nominal prices)	Previous determination – water: unmeasured and < 5 Ml/a	50.81	50.67	51.89	52.56
	Revised – water: unmeasured and < 5 Ml/a	50.81	48.78	51.89	52.56
	Previous determination – water: ≥ 5 and < 50 Ml/a	177.35	178.89	184.45	187.97
	Revised – water: ≥ 5 and < 50 Ml/a	177.35	169.45	184.45	187.97
	Previous determination – wastewater services: unmeasured supply and < 5 Ml/a	45.60	44.49	45.08	45.09
	Revised – wastewater services: unmeasured supply and < 5 Ml/a	45.60	42.66	45.08	45.09
	Previous determination – wastewater services: ≥ 5 Ml/a and < 50 Ml/a	188.19	192.69	199.48	203.84
	Revised – wastewater services: ≥ 5 Ml/a and < 50 Ml/a	188.19	182.68	199.48	203.84
	Previous determination – wastewater services: ≥50 Ml/a	60.83	61.69	63.25	64.20
	Revised – wastewater services: ≥50 Ml/a	60.83	59.10	63.25	64.20

We have based Hafren Dyfrdwy's draft determination on the data and commentary provided to us by Hafren Dyfrdwy. Should any of this information be revised or restated in future years, we will take account of adjustments we have made to the relevant price control in relation to the performance commitment(s) in question in making future in-period determinations.

4. Next steps

We welcome any written comments or representations on our draft determinations by **21 October 2021**. Representations can be made by all stakeholders. Representations can be sent to our inbox OfwatPandO@ofwat.gov.uk.

To ensure transparency, we expect companies to publish their representations in full. We also intend to publish all the written representations we receive on our website once we set out our final decisions.

In view of this, if respondents consider that some of the information in their representations should not be disclosed (for example, because they consider it is commercially sensitive information) they should identify that information and explain why. We would expect strong, robust reasons that are specific to the information concerned. We will take such explanations into account, but we cannot give an assurance that information included in representations will not be disclosed.

Information provided in response to this document, including personal information, may be published or disclosed in accordance with access to information legislation – primarily the Freedom of Information Act 2000 (FoIA), the General Data Protection Regulation 2016, the Data Protection Act 2018, and the Environmental Information Regulations 2004. For further information on how we process personal data please see our [privacy policy](#).

Where companies are making representations, they should consider what further evidence may be necessary to submit with their representations.

We will publish our final decisions by 15 November 2021, after considering representations from all stakeholders.

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