

November 2021

# **Final determination of Dŵr Cymru's in-period outcome delivery incentives for 2020-21**

**Ofwat**

## About this document

This document provides our final decision on adjustments to Dŵr Cymru's price controls for the company's performance for the 2020-21 Charging Year, under Part 3A of condition B of the company's licence (Performance Measure Adjustments, referred to in this document as 'in-period' determinations). The specific changes, and our reasons for these, are set out in this document and ['Sector overview: Final determinations of in-period outcome delivery incentives for 2020-21'](#).

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

## Executive summary

This section sets out the results of our 2020-21 in-period outcome delivery incentive (ODI) assessment for Dŵr Cymru. ODIs are the financial or reputational consequences for companies of outperformance or underperformance against their 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 Dŵr Cymru's customers' bills in the 2022-23 Charging Year.

For 2020-21 Dŵr Cymru's reported net underperformance payments of £7.494m against its performance commitments with in-period outcome delivery incentives, excluding C-MeX and D-MeX. We assessed the company's performance against its performance commitments and, in October 2021, consulted on our [draft determinations](#) for companies' in-period ODIs for 2020-21.

Having considered the responses to our draft determination, in our final determination, we are intervening on the following performance commitments:

- Per capita consumption (PCC) –in line with our decision following our per capita consumption consultation, we are deferring our determination of payments for performance against this performance commitment for the 2020-21 Charging Year.
- C-MeX and D-MeX – we are including a C-MeX outperformance payment of £2.014m and a D-MeX underperformance payment of £0.354m, based on assessment of 2020-21 company performance in our final determinations.

Our final determination is 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 £4.524m. This figure includes C-MeX and D-MeX payments as well as bespoke adjustments but is before adjustments for inflation, tax and other relevant factors.

Further details regarding the responses we received, our final decisions and the adjustments that we have made are presented in sections 2 and 3, and ['Sector overview: Final determinations of in-period outcome delivery incentives for 2020-21'](#).

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# 1. Introduction

## 1.1 Background

Dŵr Cymru's performance commitments for the 2020-25 period are set out in [PR19 final determinations: Dŵr Cymru - Outcomes performance commitment appendix](#).<sup>1</sup> 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 incentives are end of period.

Dŵr Cymru reported its performance against these performance commitments in its annual performance report (APR) in July 2021. We considered this information and, where relevant, further information from companies' answers to our queries. In October 2021, we consulted on our draft determination for Dŵr Cymru's in-period ODIs for 2020-21. We have considered the responses we have received relating to our draft determination.

Our final determination sets out the adjustments to the company's price controls and will affect Dŵr Cymru's customers' bills from the 2022-23 Charging Year.

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<sup>1</sup> 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](#).

## 2. Results of our assessment

### 2.1 Reported performance

Dŵr Cymru reported performance for 2020-21 against its performance commitments with financial in-period ODIs is set out in table 3.1 below. The company's largest individual underperformance payment is £2.796m for its water supply interruptions performance commitment. The company's largest individual outperformance payment is £0.660m for its sewer flooding on customer property (external) performance commitment.

### 2.2 Key interventions

#### 2.2.1 Community education

##### Our draft decision

In its annual performance report, Dŵr Cymru requested that we intervene to remove its reported underperformance of £0.112m on its community education performance commitment. We set out our approach to assessing company requests for interventions, abatements and deferrals due to the impact of Covid-19 in [Sector overview: Draft determinations of in-period outcome delivery incentives for 2020-21](#). We said we understood that Dŵr Cymru's ability to carry out education activities has been affected by the Covid-19 lockdown, and we noted that the company has adapted to use virtual and digital delivery methods.

Based on the evidence provided we considered that the company had demonstrated that Covid-19 has impacted performance on this performance commitment and that the company had adapted. However, the purpose of the visits, outreach and open days in the performance commitment is to provide an interactive, face to face, experience in order to meet the intended quality of education. We considered that engagement through live, interactive online sessions with company representatives were sufficient to replicate a face to face experience, but that website materials or other self-guided activities fell short of this requirement. We also noted that other companies facing similar circumstances, who had adapted their delivery methods in a similar way, had met the targets for their education performance commitments.

In our draft determination, we did not intervene to remove Dŵr Cymru's underperformance payment of £0.112m. We requested that in its response to the consultation on our draft determinations, the company should confirm the total number of individuals who

participated in direct, or virtual, sessions with company representatives for a minimum of 15 minutes, so that we can make a final determination.

## Stakeholders' responses

In its response to our draft determination, Dŵr Cymru confirmed that 5,834 individuals participated in virtual interactive sessions with a company representative for more than 15 minutes.

Dŵr Cymru explained that in March 2020 schools were closed as a result of Covid-19 and that at the time there was a significant amount of uncertainty with regards to schools opening. The company said that its approach was to employ a number of different tools to provide educational material, including materials that could be used for home schooling. It notes that the draft determination only recognises interactive session as counting towards the performance commitment level.

Dŵr Cymru agrees that interactive sessions work best but disagrees with the approach taken in our draft determination which values at zero the benefit of the additional educational material that was developed and provided by them and used extensively during the pandemic. Dŵr Cymru believes that in these circumstances, this additional educational material should be recognised as counting towards the performance commitment, even if perhaps in a way that recognises the lesser value compared to interactive sessions.

Dŵr Cymru proposes that the measure is reviewed at the end of the 2020-25 period to consider the performance in the round. It says this approach maintains the incentives to outperform the stretching performance commitment whilst also allowing a decision to be made in the round with regards to the additional educational material developed during the pandemic

## Consideration of responses and final decision

We consider that only engagement through live, interactive online sessions with company representatives is sufficient to replicate a face-to-face experience, and that website materials or other self-guided activities fall short of this requirement as it does not meet the definition of the performance commitment.

Should Dŵr Cymru want to request a change to the definition of this performance commitment (for example to make this an end of period ODI) it will need to meet the requirements set out in annex 2 of [PR19 final determinations: Dŵr-Cymru – Outcomes performance commitment appendix](#).

Therefore, our final determination remains unchanged from our draft determination that 5,834 individuals participated in education activities in line with the definition of this

performance commitment. We do not consider that the changes proposed by the company would be consistent with the allocation of risk assumed within the regulatory framework.

## 2.2.2 Visitors to recreational facilities

### Our draft decision

In its APR, Dŵr Cymru requested that we intervene to remove its reported underperformance of £0.530m on its visitors to recreational facilities performance commitment. We set out our approach to assessing company requests for interventions, abatements and deferrals due to the impact of Covid-19 in [Sector overview: Draft determinations of in-period outcome delivery incentives for 2020-21](#).

In its APR, Dŵr Cymru stated that Covid-19 measures meant that individuals had not been able to visit its sites and/ or it could not open its sites to normal capacity and that, in the circumstances, under performance payments for 2020-21 were not appropriate. We recognised that Covid-19 affected this performance commitment during 2020-21. We noted the steps that Dŵr Cymru took to adapt its behaviour and respond to the new circumstances. However, we also considered whether the evidence provided demonstrated that intervening would be in customers' interests and would retain incentives on the company to deliver the relevant outcome.

Based on the evidence provided, the wider considerations set out in [Sector overview: Draft determinations of in-period outcome delivery incentives for 2020-21](#) and the specific operation of this performance commitment, which is to provide benefits to customers through access to company facilities, we considered that intervening in our draft determination to adjust the company's underperformance payment was not consistent with the allocation of risk assumed within the regulatory framework.

In our draft determination, we therefore rejected Dŵr Cymru' request that we intervene to remove its underperformance of £0.530m on its visitors to recreational facilities performance commitment.

### Stakeholders' responses

In its response regarding our draft determinations Dŵr Cymru stated that Covid-19 driven Government restrictions had severely restricted access to their visitor centres in 2020-21 and that it had put in place several measures to ensure they could open centres in a safe manner. It also said that it considers that significant outperformance will be needed to recover from 2020-21 underperformance and that there is uncertainty due to changes in consumer demand. Dŵr Cymru has proposed that the measure is reviewed at the end of the 2020-2025 period so performance can be considered in the round. The company says this approach

maintains the incentives to outperform but does not penalise it for factors beyond management control.

## Consideration of responses and final decision

We understand Dŵr Cymru's argument that Covid-19 driven Government restrictions did restrict access to their visitor centres during 2020-21. But, it is not uncommon for exogenous factors to affect company performance. As stated in our draft determination, we also need to consider whether the evidence provided demonstrates that intervening would be in customers' interests and would retain incentives to deliver the relevant commitments.

Should Dŵr Cymru want to request a change to this performance commitment (for example to make this an end of period ODI), it will need to meet the requirements set out in annex 2 of [PR19 final determinations: Dŵr-Cymru – Outcomes performance commitment appendix](#).

Having considered Dŵr Cymru's response, our final decision on its underperformance payment for this performance commitment is as stated in our draft decision. We do not consider that the changes proposed by the company would be consistent with the allocation of risk assumed within the regulatory framework.

### 2.2.3 C-MeX and D-MeX

#### Our draft decision

Our draft determination included a C-MeX outperformance payment of £2.014m and a D-MeX underperformance payment of £0.354m, based on assessment of 2020-21 company performance in our final determinations.

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.

#### Stakeholders' responses

We did not receive any specific comments on this issue.

#### Consideration of responses and final decision

Our final decision is unchanged from our draft determination, as stated above.

## 2.2.4 Taxation

### Our draft decision

In our draft determinations we applied a uniform marginal tax rate of 19% in each company's in-period adjustments model to reflect the headline rate of corporation tax.

### Stakeholders' responses

Dŵr Cymru requests that we adjust the marginal tax rate in its in-period determination to 0% because it does not expect to pay corporation tax for the rest of the 2020-25 period, which it says was reflected in its December 2019 PR19 final determination.

### Consideration of responses and final decision

We acknowledge the evidence the company has provided in its annual performance report, its response to our draft determination and subsequent correspondence relating to whether it will incur taxable losses in 2022-23 and beyond, though we note the uncertainty around internal business forecasts. We want to maintain a targeted and proportionate assessment during the in-period determinations process. We also note that if the company is not liable to pay corporation tax in 2022-23 as it has no taxable profits, it can carry forward taxable losses to offset corporation tax liabilities in future years. As such, provided the company returns to taxable profits in the coming years, we do not consider there is a strong case to change our assumption.

We will therefore maintain the 19% assumption in our final determination for this company. We also note that, as set out in the [PR19 reconciliation rulebook: guidance document](#) (page 58), if there is a material impact on customers or companies as a result of a difference between the marginal rate of tax that a company pays in the following charging year and our assumption, we may consider reconciling this at PR24.

## 2.3 Payment deferrals and abatements

As set out in our [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.

The company suggested that we could make payment abatements in relation to its education and recreation performance commitments. Based on our assessment of the company's

performance and as discussed in section 2.2, we do not consider any are required. As such, we do not apply any payment abatements in our final determination.

## 2.3.1 Per capita consumption (PCC)

### Our draft decision

In line with our July consultation proposals, we proposed changing the timing of payments for this performance commitment to end of period. Dŵr Cymru also asked us to defer underperformance payments for its per capita consumption performance commitment for 2020-21.

In our [July 2021 consultation](#) on changing the timing of our determination of the value of ODI payments for per capita consumption performance commitments, we proposed that this 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.

### Stakeholders' responses

We did not receive any specific comments on this issue.

### Consideration of responses and final decision

Our consultation on moving the timing of the per capita consumption performance commitment to the end of the 2020-25 period has [concluded](#). After carefully considering the responses to that consultation, we have confirmed that ODI payments for per capita consumption performance commitments will be determined at the end of the period for all years within the 2020-25 price control period. Consequently, we have not included any adjustment in relation to this performance commitment in our final determination.

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

#### 3.1 Our final determination

In this section we outline the financial impacts of our final 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 final 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 final decisions on deferrals and abatements and how we propose that these payments should be applied in 2022-23.

Table 3.5 sets out the changes that we are determining to the company's relevant price controls because of those decisions.

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 Dŵr Cymru's for 2020-21, by price control, and our final 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 final 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)	Our final decisions after interventions (£m)
Water resources	-0.530	-0.530	-0.530
Water network plus	-6.357	-5.047	-5.047
Wastewater network plus	-0.591	-0.591	-0.591
Bioresources	0.454	0.454	0.454
Residential retail	-0.308	-0.308	-0.308
Business retail	-0.162	-0.162	-0.162
<b>Total payments</b>	<b>-7.494</b>	<b>-6.184</b>	<b>-6.184</b>

See section 2 for details of our interventions on the company's performance commitments.

### Table 3.2: C-MeX and D-MeX payments

Our final 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	2.014	n/a
Water network plus	n/a	-0.239
Wastewater network plus	n/a	-0.115
<b>Total payments</b>	<b>2.014</b>	<b>-0.354</b>

See section 2 for further details on C-MeX and D-MeX.

### 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 final 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	-0.530	0.000	0.000	0.000	-0.530
Water network plus	-5.047	-0.239	0.000	0.000	-5.286
Wastewater network plus	-0.591	-0.115	0.000	0.000	-0.706
Bioresources	0.454	0.000	0.000	0.000	0.454
Residential retail	-0.308	2.014	0.000	0.000	1.706
Business retail	-0.162	0.000	0.000	0.000	-0.162
<b>Total</b>	<b>-6.184</b>	<b>1.660</b>	<b>0.000</b>	<b>0.000</b>	<b>-4.524</b>

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

This table sets out our final 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 final deferrals (£m)	Ofwat final abatements (£m)	Total ODI payments to be applied in 2022-23 (£m)
Water resources	-0.530	0.000	0.000	-0.530
Water network plus	-5.286	0.000	0.000	-5.286
Wastewater network plus	-0.706	0.000	0.000	-0.706
Bioresources	0.454	0.000	0.000	0.454
Residential retail	1.706	0.000	0.000	1.706
Business retail	-0.162	0.000	0.000	-0.162
<b>Total</b>	<b>-4.524</b>	<b>0.000</b>	<b>0.000</b>	<b>-4.524</b>

See section 2 for our decisions relating to deferrals and abatements for this company.

**Table 3.5: Changes to price controls (final determinations)**

This table sets out the changes to the level of the company's price controls that we are determining for the Charging Years beginning on 1 April 2022 and 1 April 2023. The details for other charging years are included for completeness and ease of reference. The in-period adjustments model published on our website shows how these changes reflect the impact of our final decisions. See <https://www.ofwat.gov.uk/publication/sector-overview-final-determinations-in-period-odis-2020-21/> for how we have applied adjustments for tax and inflation.

Price control		2021-22	2022-23	2023-24	2024-25
<b>Water resources (K factors)</b>	Last determination	6.76	5.09	2.49	-4.59
	Final determination	6.76	3.24	4.28	-4.59
<b>Water network plus (K factors)</b>	Last determination	-5.71	1.39	-1.24	0.26
	Final determination	-5.71	-1.25	1.33	0.26
<b>Wastewater network plus (K factors)</b>	Last determination	-0.30	-1.07	-1.29	-1.45
	Final determination	-0.30	-1.31	-1.05	-1.45
<b>Bioresources (unadjusted revenue, <math>UR_t</math> – £m, 2017-18 Nov CPIH prices)</b>	Last determination	34.573	34.926	35.278	35.630
	Final determination	34.573	35.487	35.278	35.630
<b>Residential retail (total revenue, <math>TR_t</math> – £m, nominal prices)</b>	Last determination	46.830	47.340	47.850	48.357
	Final determination	46.830	49.670	47.850	48.357
<b>Business retail (allowed average retail cost component, <math>rc_t</math> – £, nominal prices)</b>	Last determination – water supplies < 50 Ml	31.06	31.06	30.97	31.04
	Final determination – water supplies < 50 Ml	31.06	29.98	30.97	31.04
	Last determination – wastewater services	40.81	41.01	41.12	41.44
	Final determination – wastewater services	40.81	39.51	41.12	41.44

We have based Dŵr Cymru's final determination on the data and commentary provided to us by Dŵr Cymru (and, where relevant, other water companies). 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.

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