

November 2021

Final determination of Severn Trent Water's in-period outcome delivery incentives for 2020-21

About this document

This document provides our final decision on adjustments to Severn Trent Water'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 Severn Trent Water. 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 Severn Trent Water's customers' bills in the 2022-23 Charging Year.

For 2020-21 Severn Trent Water reported net outperformance payments of £59.716m 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 and conducted further analysis, in our final determination we are intervening on the following performance commitments:

- Per capita consumption (PCC) – in line with our decision following our PCC consultation, we are deferring our determination of payments for performance against this performance commitment for the 2020-21 Charging Year.
- Business void and gap site supply points – we include an outperformance payment of £0.154m in our final determinations, this is a change from our draft decision.
- Persistent low pressure – in line with our draft determinations we include in the final determination an outperformance payment of £2.828m rather than £5.143m.

- C-MeX and D-MeX – we are including a D-MeX outperformance payment of £3.881m, based on assessment of 2020-21 company performance in our draft 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 increased by £25.276m. 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

Severn Trent Water performance commitments for the 2020-25 period are set out in [PR19 final determinations: Severn Trent Water – 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 incentives are end of period.

Severn Trent Water 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 Severn Trent Water'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 Severn Trent Water's customers' bills from the 2022-23 Charging Year.

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](#).

2. Results of our assessment

2.1 Reported performance

Severn Trent Water's 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 £5.249m for its water supply interruptions performance commitment. The company's largest individual outperformance payment is £39.113m for its sewer blockages performance commitment.

2.2 Key interventions

2.2.1 Business void and gap site supply points

Our draft decision

In our draft determination we intervened to remove Severn Trent Water's business void and gap site supply points outperformance payment of £0.154m. This is because our engagement with the company in this area identified some uncertainty in the reported performance figure. We required further evidence to support the reported performance. The company was not able to provide this to us in time for our draft decision. Consequently, as part of its response to the draft decision we expected Severn Trent Water to provide additional assurance, such as from a third-party auditor, that its reported performance for bringing void and gap sites into charge was accurate and that it was not incorrectly benefiting by counting the removal of temporary Covid-19 vacancy flags.

Stakeholders' responses

In its response to our draft determination Severn Trent Water provided additional clarity and assurance that it had not benefited from retailers applying for a vacancy reward after bringing a temporary Covid-19 vacancy back into charge. In response to our draft determination request for further evidence, Severn Trent Water asked its third-party assurer, Jacobs, to assure a breakdown of the data relating to this performance commitment PR19SVE_A03." This additional information split void sites from gap sites and identified which void properties were marked as void prior to 1 February 2020 (before the use of temporary Covid-19 vacancy flags).

The company told us that it considers the third-party assurance and updated information demonstrates that its data is accurate and has not been increased by supply points with covid-19 vacancy flags being brought back into charge. The company argued that the

reported number of 783 business void and gaps supply points should be used for the purpose of the ODI.

Consideration of responses and final decision

Taking into account the additional information and third party assurance received from Severn Trent Water we are making a change from our draft decisions. Our final determination includes an outperformance payment of £0.154m, based on the reported value of 783 for 2020-21 performance.

2.2.2 Persistent low pressure

Our draft decision

Ahead of our draft decisions, we engaged with Severn Trent Water in relation to its persistent low pressure performance commitment, for which the company reported an outperformance payment of £5.143m. We identified that, while the performance commitment definition required the company to report the number of residential properties only, the associated performance commitment level was set with reference to numbers for both residential and non-residential properties. There was, therefore, an inconsistency between the performance commitment levels and the scope of the performance commitment definition. Through our engagement with the company, Severn Trent Water indicated that it was open to amending the definition to ensure that the inconsistency was addressed for the remaining years of the control period and we expect this change to be taken forward.

For 2020-21, the company provided additional evidence that allowed us to understand the allocation of performance between residential and non-residential properties. This suggested that if the performance commitment level and reported performance were on a consistent basis, then the outperformance payment would be £2.828m rather than £5.143m.

Consequently, in our draft decision, we intervened to adjust the outperformance payment to £2.828m.

Stakeholders' responses

The company accepts that there is a difference between the original design of the performance commitment levels and the scope of the PR19 final determination. The company agrees with changing the definition going forward, but states that a retrospective adjustment for 2020-21 runs counter to the interventions made at PR19.

Consideration of responses and final decision

Having considered stakeholder responses, our final decision on the company's performance payment for this performance commitment is unchanged from our draft determination intervention. We intervene because we consider that there was an unambiguous error in relation to the setting of this performance commitment because the performance commitment definition required the company to report the number of residential properties only, while the associated performance commitment was set with reference to numbers for both residential and non-residential properties. The company identified this inconsistency in its response to our PR19 draft determination, but the error was unfortunately not corrected in our PR19 final determination. We therefore consider that our intervention is to correct an error rather than to make a retrospective adjustment.

We intend to use the Annex 2 process to set out a formal change to the definition for the 2020-25 period.

2.2.3 Sewer blockages

Our draft decision

In our draft determinations we included the full outperformance payment of £39.113m for sewer blockages performance. We engaged with the company on this performance commitment to better understand the drivers of outperformance, how they relate to improvements in service to customers and the assurance associated with this. The company provided further information to support its submission. There remained some additional evidence outstanding at the time of the draft decision, but we said that subject to the company providing us with the reassurance we required, we did not propose intervening on this performance commitment.

Stakeholders' responses

Since the draft decision, Severn Trent Water provided additional evidence to demonstrate that its outperformance in 2020-21 was the result of significant investment and operational practice improvements, leading to fewer reportable blockages, and improved service to customers.

Severn Trent Water also provided the additional third-party assurance that we requested through our draft determination to support the reported performance. It:

- Set out a detailed analysis of the activities undertaken to achieve the improvement, providing new detail quantifying the impact of each activity;

- Provided evidence to show that the majority of improvements have been achieved through a reduction in repeat events and through implementation of targeted cleansing and repairs as part of its targeted 'blockbuster' cleansing and repair programme;
- Clarified that CCTV is only used once a suspected blockage is confirmed by the initial response team. It is not used to identify 'nothing founds' and provided third party assurance to support its view that the introduction of CCTV survey on first visit had not resulted in a reclassification of incidents to 'no blockage found; and
- Provided data and evidence to explain increases in reported cases of 'nothing found'.

Consideration of responses and final decision

Based on all the evidence provided, we maintain our position from draft determination not to intervene. Our final determination therefore includes the full outperformance payment of £39.113m for sewer blockages performance.

The level of detailed evidence we required from the company reflects how important it is that companies are transparent with customers about the drivers of significant out and underperformance of performance commitments levels. This is especially the case where there are significant associated outperformance payments.

Where a company is likely to report substantial outperformance payments in any given year, we would expect it to be able to demonstrate and quantify in detail the drivers of the outperformance. We expect the company to fully understand and clearly articulate how it has improved performance and service to customers.

To provide confidence that reported performance is linked to real improvements in service to customers, rather than changes in methodology, the company should also provide an independent audit report providing confirmation that the reported performance is in line with the guidance and exclusions have been correctly applied. The audit report should detail the sample checking carried out by the independent auditor, the size of the sample check should be commensurate with the scale of the outperformance and include exclusions.

2.2.4 C-MeX and D-MeX

Our draft decision

Our draft determination included a D-MeX outperformance payment of £3.881m, based on assessment of 2020-21 company performance in our draft determinations. Severn Trent Water did not incur ODI payments for C-MeX because it was the median performing company in 2020-21.

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 comments on this issue.

Consideration of responses and final decision

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

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.

This company 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 final determinations.

2.3.1 Payment deferrals

Our draft decision

Severn Trent Water requested to defer £47.246m in total outperformance payments, split across its water resources, water network plus and wastewater network plus price controls, to the following year. This figure excluded per capita consumption, which is addressed below. The company stated this was an early view and reflected the net ODI payments it had earned in 2020-21 (including a draft view of D-MeX payments) and the impact of other mechanisms (such as the revenue forecasting incentive and the blind year reconciliation of 2019-20 performance) which it said would put upward pressure on customer charges in 2022-23.

In its initial submission, the company included estimates of likely bill impacts on customers if these payments were not deferred. With its proposed deferral, the company stated that annual average combined residential bills would rise by 2.7% (or £9 per customer) compared to 6.7% (or £24 per customer). The company also observed that unmetered customers are more likely to be exposed to bill increases due to the impact of other customers switching to meters throughout the year.

For our draft determination, we assessed the company's submission and considered the impact of other drivers on the company's revenue in 2022-23, such as the green recovery funding, the impact of PR19 reconciliation mechanisms and ODI deferrals from previous years. While we noted that the company has the ability to manage the impact on customers of changes to its allowed revenue when setting its charges, we recognised there was a risk that customers might be adversely affected if high outperformance payments were not spread over future years.

We considered the overall principle of the company's proposal to defer outperformance payments equal to the net ODI payments it has earned in 2020-21 minus the underperformance payments deferred from 2019-20 was reasonable, particularly given the existence of other upward pressures on allowed revenues in 2022-23, such as the operation of the revenue forecasting incentive correcting for revenue under-recovery in 2020-21. We considered the deferral would reduce the short-term bill impacts on customers from high outperformance payments. However, longer term, we noted the importance of ensuring that in-period ODI payments are applied close in time to when customers experience a given level of performance, a key aspect of the PR19 outcomes framework.

For our draft determination, we replicated the methodology proposed by Severn Trent Water but reflected our interventions on individual performance commitments and the final performance data for D-MeX. We proposed to defer £44.749m in outperformance payments to 2022-23 in our draft determination for Severn Trent Water.

Stakeholders' responses

Severn Trent Water and CCW say they support our draft decision to defer some of the company's outperformance payments to help manage the impact of bill changes on customers in 2022-23.

CCW also makes wider comments on our approach to deferrals, which we address in ['Sector overview: Final determinations of in-period outcome delivery incentives for 2020-21'](#).

Consideration of responses and final decision

We have maintained our draft determination approach, adapted for our final view of the company's net in-period ODI payments in 2020-21 after interventions on individual performance commitments as set out in section 2.2 of this document. This results in our final decision to defer £44.903m in outperformance payments. We set out the price control impacts of this decision in section 3.1.

2.3.2 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. Severn Trent Water also asked us requested 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.

2.4 Green recovery

Our draft decision

As part of our final decisions on the [green recovery](#), published in July 2021, we agreed to allow Severn Trent Water additional funding during the current (2020-25) price control period. Severn Trent Water receives this additional funding through a new performance commitment with in-period ODI payments (PR19SVE_GR), introduced through a licence [modification](#) that came into effect on 1 September 2021.

The company has met the requirement for a revenue adjustment for the 2022-23 charging year by accepting our green recovery final decision by 8 August 2021 and we therefore include a positive revenue adjustment of £25.257m. We apply this through the in-period adjustments model, with relevant adjustments as set out in the overview document.

Stakeholders' responses

We received no comments on this issue.

Consideration of responses and final decision

We make no changes to our draft 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 Severn Trent Water 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	7.819	9.639	9.639
Water network plus	3.653	1.260	1.337
Wastewater network plus	48.225	48.148	48.225
Bioresources	0.000	0.000	0.000
Residential retail	0.019	0.019	0.019
Total payments	59.716	59.066	59.220

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	0.000	n/a
Water network plus	n/a	2.969
Wastewater network plus	n/a	0.912
Total payments	0.000	3.881

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	9.639	0.000	0.434	1.445	11.518
Water network plus	1.337	2.969	-1.691	9.383	11.998
Wastewater network plus	48.225	0.912	-16.923	14.429	46.643
Bioresources	0.000	0.000	0.000	0.000	0.000
Residential retail	0.019	0.000	0.000	0.000	0.019
Total	59.220	3.881	-18.180	25.257	70.178

See section 2 for details of the bespoke adjustments we have applied for this company.

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	11.518	10.073	0.000	1.445
Water network plus	11.998	2.615	0.000	9.383
Wastewater network plus	46.643	32.214	0.000	14.429
Bioresources	0.000	0.000	0.000	0.000
Residential retail	0.019	0.000	0.000	0.019
Total	70.178	44.903	0.000	25.276

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 '[Sector overview: Final determinations of in-period outcome delivery incentives for 2020-21](#)' for how we have applied adjustments for tax and inflation.

Price control		2021-22	2022-23	2023-24	2024-25
Water resources (K factors)	Last determination	3.45	6.02	5.95	-7.80
	Final determination	3.45	8.31	3.79	-7.80
Water network plus (K factors)	Last determination	-0.50	-1.63	-1.70	0.28
	Final determination	-0.50	0.29	-3.52	0.28
Wastewater network plus (K factors)	Last determination	-1.85	-1.29	-0.98	1.02
	Final determination	-1.85	1.41	-3.53	1.02
Bioresources (unadjusted revenue, UR_t – £m, 2017-18 Nov CPIH prices)	Last determination	76.857	77.205	77.395	77.743
	Final determination	76.857	77.205	77.395	77.743
Residential retail (total revenue, TR_t – £m, nominal prices)	Last determination	105.067	106.062	107.008	107.922
	Final determination	105.067	106.087	107.008	107.922

We have based Severn Trent Water's final determination on the data and commentary provided to us by Severn Trent Water (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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Ofwat
Centre City Tower
7 Hill Street
Birmingham B5 4UA
Phone: 0121 644 7500

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