

PR24 company webinars
Delivering outcomes for customers – our
draft methodology proposals

13 July 2022



Agenda

Item	11:00 – 12:30
Introduction – Juliet Young (5 mins)	11:00 – 11:05
Performance commitments – Peter Jordan (15 mins)	11:05 – 11:20
Questions and answers (20 mins)	11:20 – 11:40
Break (5 mins)	11:40 – 11:45
Outcome delivery incentives – Jeevan Jones (15 mins)	11:45 – 12:00
Questions and answers (20 mins)	12:00 – 12:20
PR24 timeline and next steps (10 mins)	12:20 – 12:30

More details on our **draft methodology proposals** can be found in:

- the [main consultation document](#) (chapter 5);
- [Appendix 6 – Performance commitments](#);
- [Appendix 7 – Performance commitment definitions](#);
- [Appendix 8 – Outcome delivery incentives](#).





Performance commitments

Peter Jordan

Challenges and ambitions



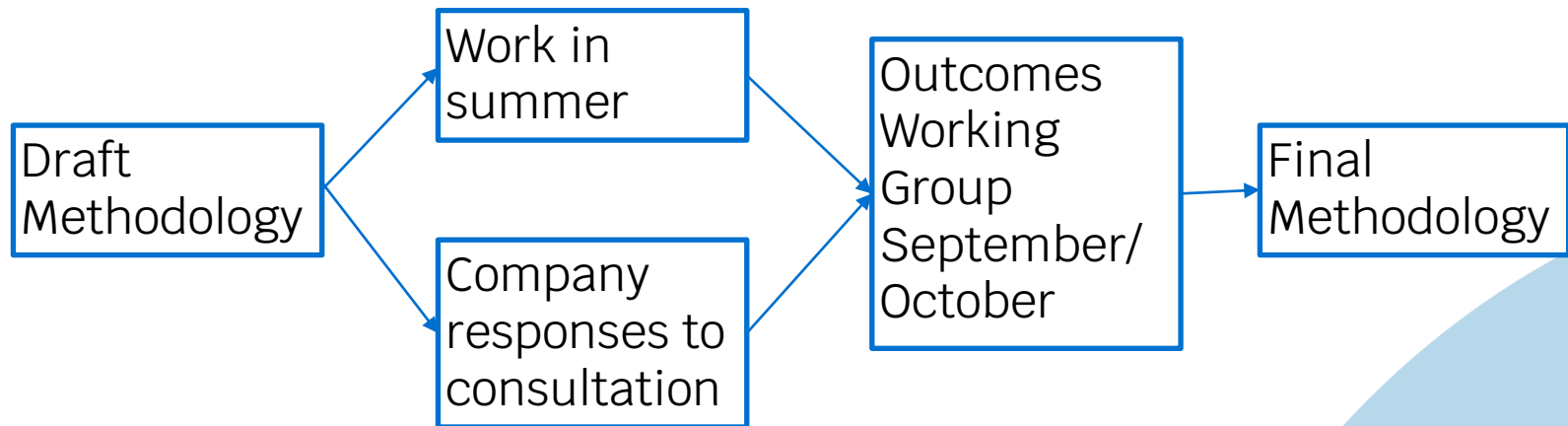
Outcomes – proposed common performance commitments for PR24

	Water and wastewater	Water only	Wastewater only
Customers receiving excellent service every day	C-MeX D-MeX BR-MeX [for English companies] Business customer satisfaction [for Welsh companies]	Water supply interruptions Compliance risk index (CRI) Customer contacts about water quality	Internal sewer flooding External sewer flooding
Environmental outcomes	Biodiversity	{ Leakage Per capita consumption Business demand } Operational greenhouse gas emissions – water	Pollution incidents Serious pollution incidents Discharge compliance Bathing water quality River water quality Storm overflows Operational greenhouse gas emissions – wastewater
Asset health		Mains repairs Unplanned outage	Sewer collapses

New performance commitments highlighted in **bold**. All measures financially incentivised



Draft to final methodology



Ofwat's [market monitoring](#) and review of incumbent company support for effective markets ([Project RISE](#)) conclude company support for the business retail market needs to improve.

We propose to include a business customer measure of experience common PC at PR24 for companies operating wholly or mainly in England capturing both:

- 1) Feedback from business customers:** To avoid Retailer performance influencing feedback, and consistent with the [Europe Economics study on B-MeX](#), we propose business customer feedback is sought via a survey following a specific contact with the water company. We will also consider the recommendations by the sector's [B-MeX sub group](#) on survey design.
- 2) Feedback from business Retailers:** This could be via surveys (like the [current R-MeX survey](#)), possibly supplemented with more granular feedback from Retailers following completion of each individual Retailer-Wholesaler interaction using the new [Bilaterals Hub](#).

We propose to work with MOSL and the sector to design the BR-MeX incentive, with the final design specifications set out in draft determinations. We suggest MOSL collects and reports on performance data in-period, supported by governance arrangements in the market codes.

Consultation question: What are your views on our proposal to introduce a single, combined common performance commitment ('BR-MeX') capturing the experience of both end business customers and retailers as intermediate customers?

Water demand

Given the pressures of climate change, all water companies need to reduce the demand for water where possible for the foreseeable future. As well as reducing leakage, companies have a significant role in water efficiency for both residential and business customers including:

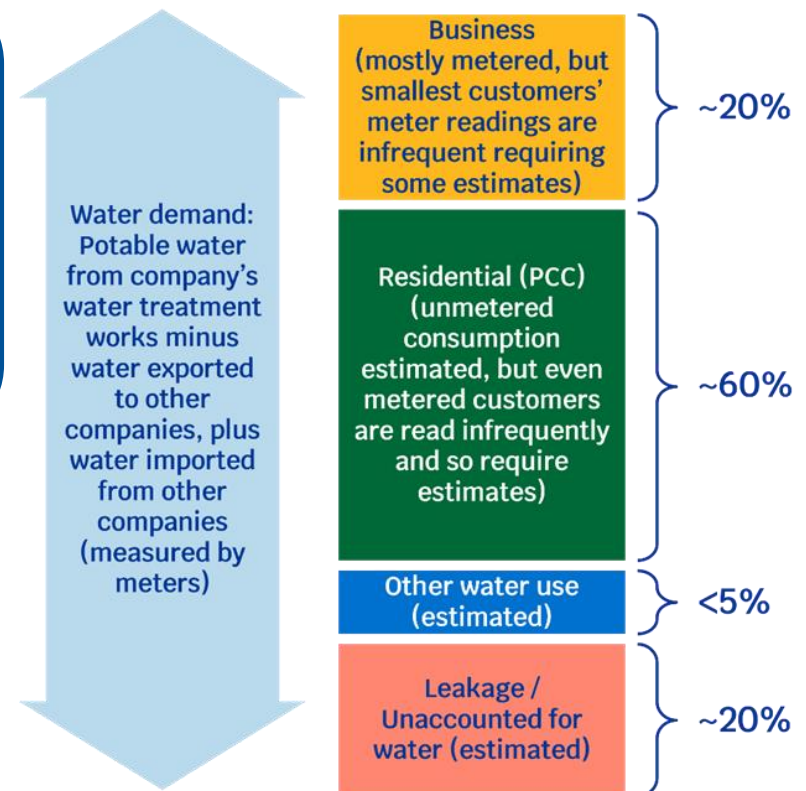
- providing the right metering;
- communicating with customers or providing the right information for others to communicate;
- setting water charges; and
- providing direct support to help water customers reduce their demand.

Consultation question: We invite views on whether we should either have:

- performance commitments to reduce leakage, per capita consumption, and business demand;
- A water demand performance commitment (potable water produced by water treatment works, adjusted for water transfers between water companies).

If we include the combined metric, we would still expect companies to report on the individual metrics. Likewise if we include separate metrics, we would expect companies to also report on the combined metric.

We propose to exclude business customers that use more than 50 Ml per annum.

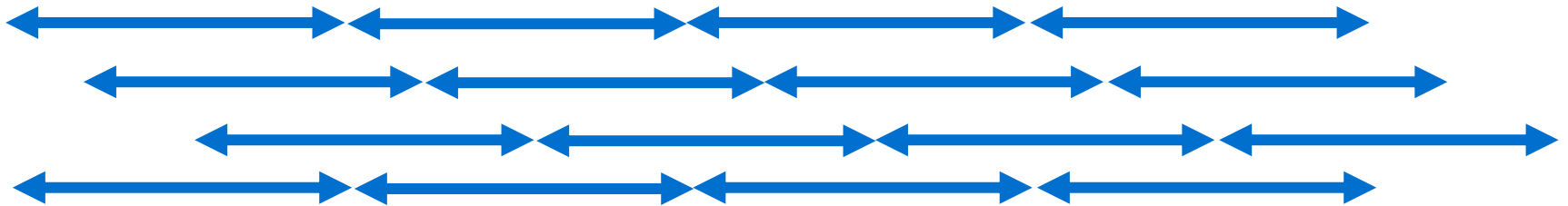


Biodiversity

We propose to base the PC on the Biodiversity Metric. It compares

- baseline pre intervention assessment
- Forecast post intervention assessment (could be decades in the future).

For the PC we propose we repeat the **baseline pre intervention assessment** every four years. Rather than all sites being assessed in a single year, we envision site visits being a rolling assessment across the four-year period.



- No change could be recorded until the second site visit, four years from the first visit.
- Companies should start these site visits before 2025 in order to record increases in biodiversity in the 2025-30 period.
- We expect companies to have completed at least a first visit at each site to assess biodiversity for company owned land by 31 March 2028.

Consultation question: Do you agree with our proposed definition for the biodiversity performance commitment?

River water quality

We propose a common PC for river water quality that measures the reduction in phosphorous from water company activities.

We intend for this to cover both:

- the reduction in the amount of phosphorus discharged at wastewater treatment works; and
- the phosphorous stopped from entering rivers from wider partnership working, including by using nature-based solutions and catchment management.

Propose a meeting of the River water Task & Finish Group in July/August, with further meetings from late September.

Consultation question: Do you agree with our proposal for the river water quality performance commitment to measure the reduction of phosphorus entering rivers?



Storm overflows

We propose that there should be a common performance commitment in this area to hold companies to account and incentivise them to go further in reducing the number of spills.

We propose it should be the average number of spills per overflow.

Need to consider the appropriateness of developing performance commitments in this area for Wales.

Operational greenhouse gas emissions

We propose introducing common operational greenhouse gas emissions performance commitments.

- Alignment with the definition we already use in the Regulatory Accounting Guidelines (RAGs). We will consider changing the RAG for the 2022-23 reporting year and may amend the definition in advance of PR24 final determinations.
- We propose to set separate performance commitments for water and wastewater based on a normalised measure to enable direct comparisons between companies.

Consultation question: Do you agree with our proposal to have separate operational greenhouse gas emissions performance commitments for water and wastewater, which are based on a normalised measure?



Bathing water quality

We propose a bathing water quality PC covering the bathing waters that can be impacted by the company.

Two current options:

1. Percentage of bathing waters achieving the **"excellent"** classification in a company's area;
2. **Improvement in bathing water categorisation** more generally (including, for example, waters that move from sufficient to good).

These measures would be based directly on the Environment Agency's and Natural Resources Wales' classifications, which are made on individual bathing waters.

However, these exclude samples. This is appropriate in the context of categorising bathing waters, but doesn't fully represent the outcome that customers receive.

We consider that a different approach could have benefits. In line with our general approach to performance commitments, we are considering whether we can reduce the number of exclusions, and increase the focus on the actual outcome for customers during each year.

We propose working with Environment Agency and Natural Resources Wales over the summer, before further wider engagement over the autumn.

Consultation question: Do you agree we should focus the bathing water performance commitment on the outcome that customers have received and should continue to develop an alternative definition to do this?

Serious pollution incidents

Longstanding expectation that all companies should reach zero serious pollution incidents (category 1 and 2) as soon as possible.

We are proposing a separate PC on serious pollution incidents for water and wastewater companies to hold companies to account for this.

Consultation question: Do you agree with our proposal that the performance commitment on serious pollution incidents should only apply to water and wastewater companies?





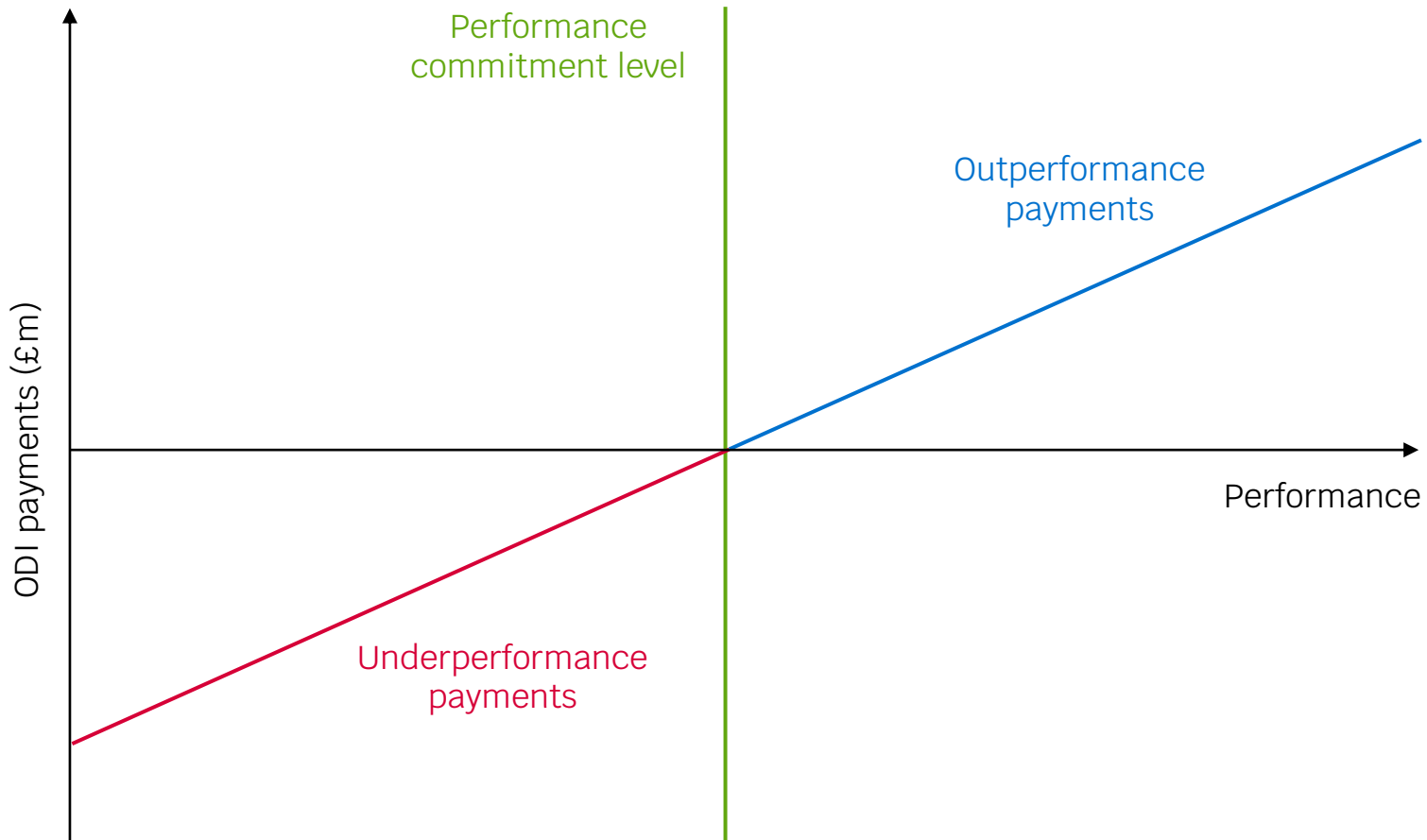


Outcome delivery incentives

Jeevan Jones

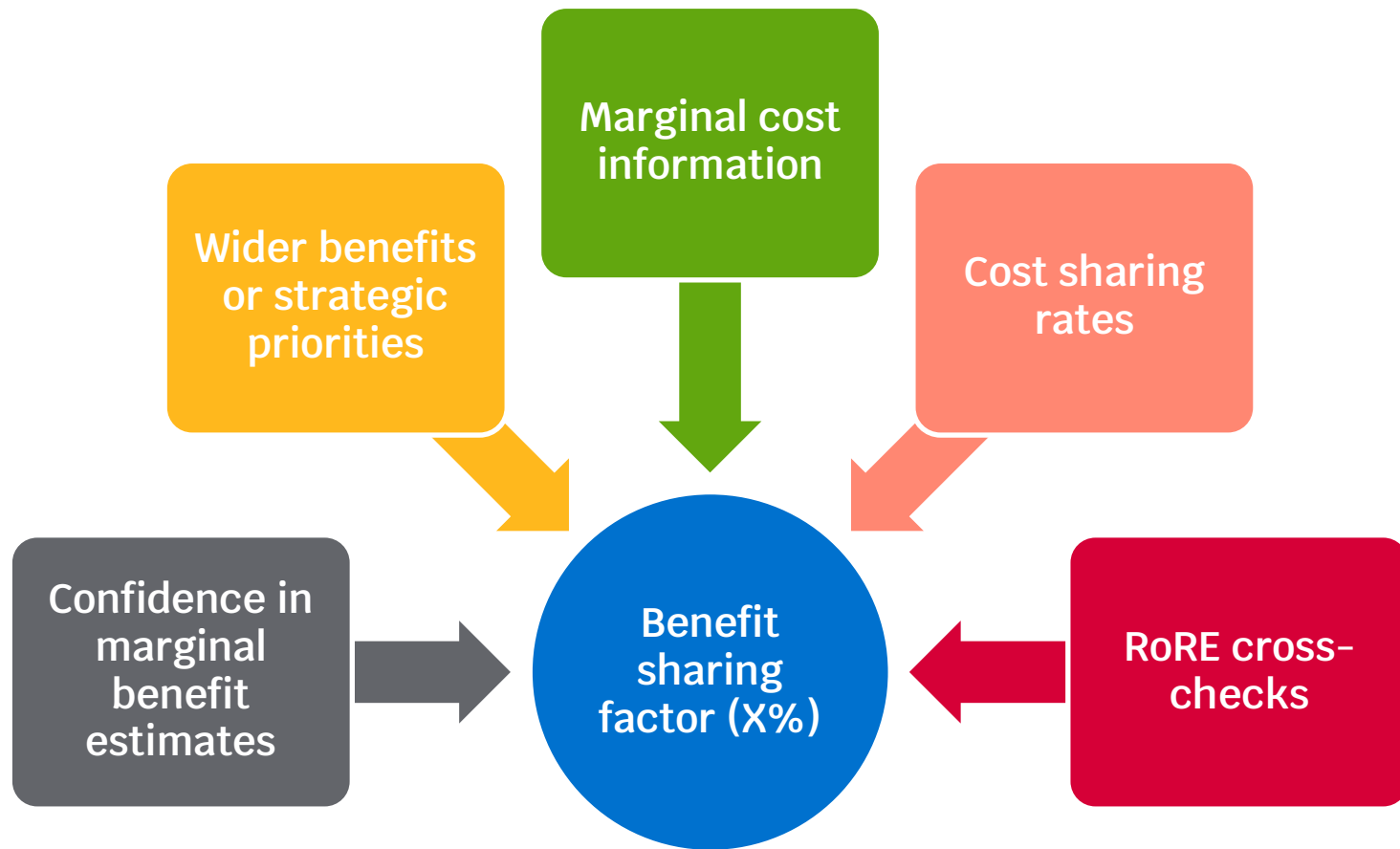
Standard incentive rates (1 of 2)

Simplified formula: $MB * X\%$



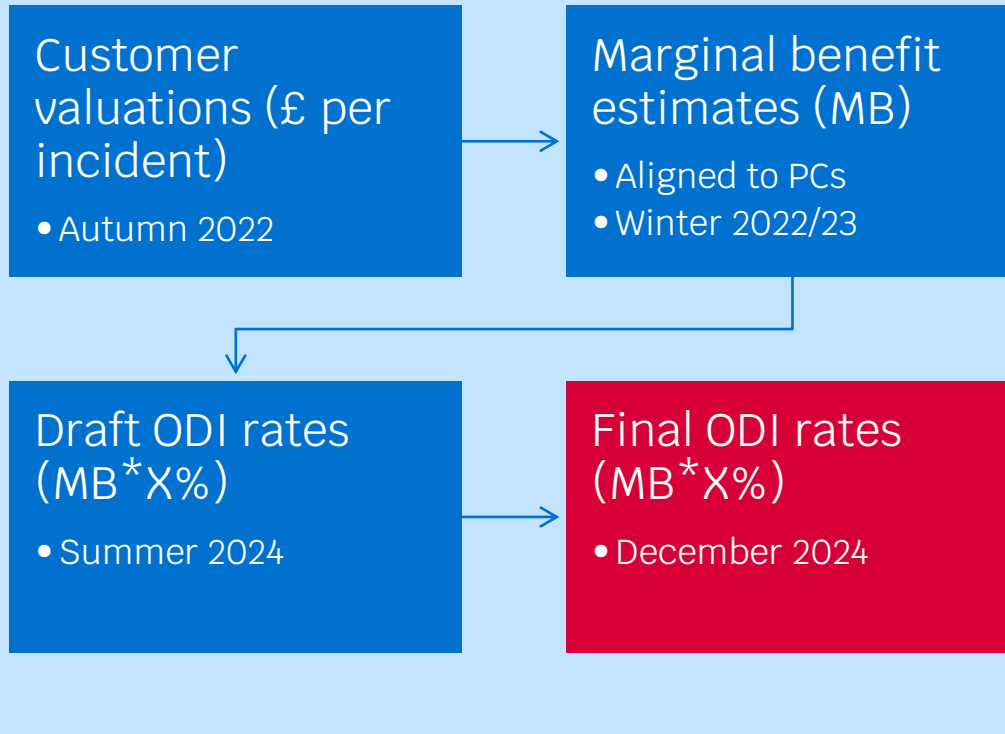
Standard incentive rates (2 of 2)

Our starting point is: $X=70\%$



Estimating marginal benefits

Majority of common PCs expected to use the collaborative customer research



Alternative approaches for some common PCs

Biodiversity

- Starting point: Defra net gain market, informed by a range of valuations
- Could vary by company

Greenhouse gas emissions

- Starting point: external valuations, informed by PR24 bidding process

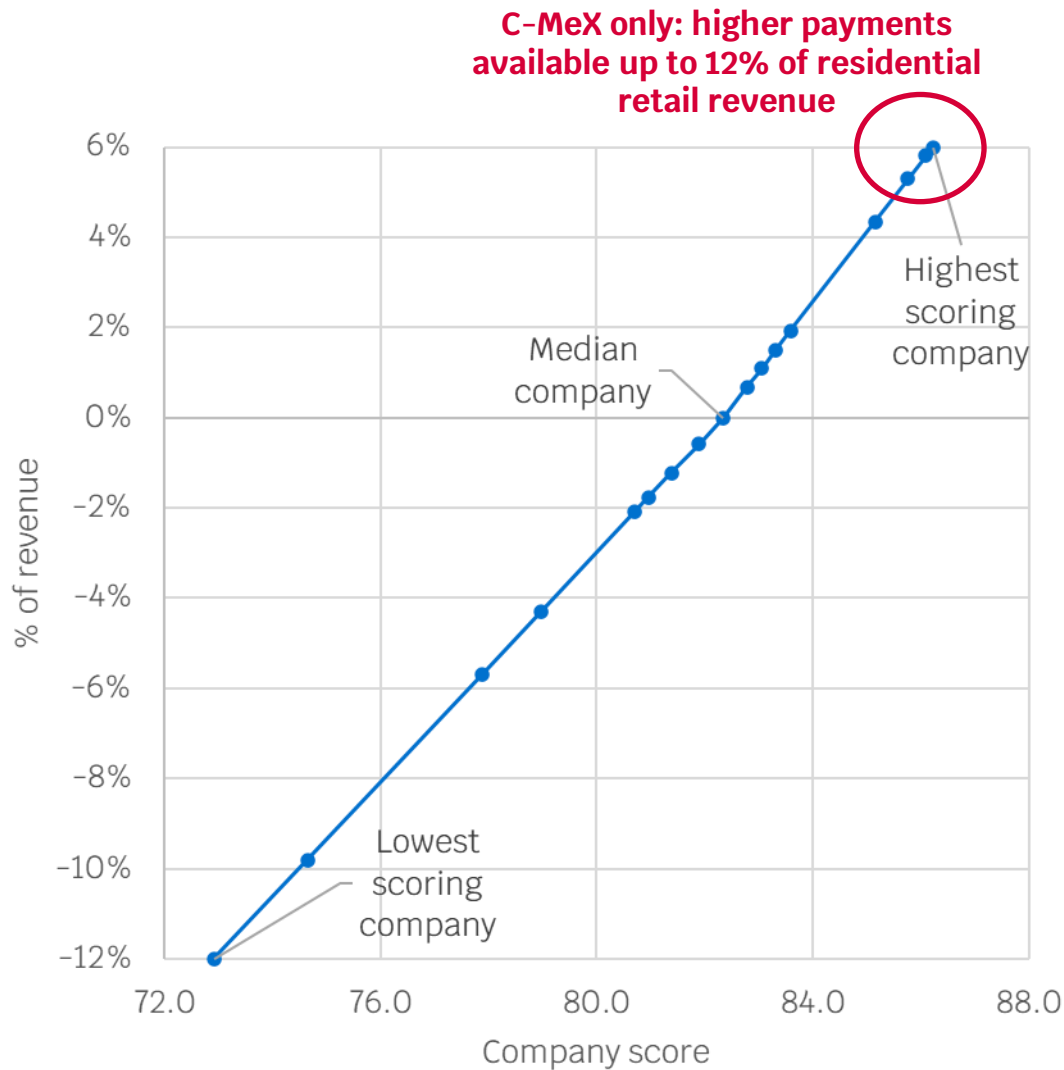
Asset health PCs

- Starting point: inferred benefits approach
- Top-down approaches may be required

Bespoke performance commitments

Companies provide complementary research that is **broadly consistent in approach** to the collaborative customer research, and in line with customer engagement standards for PR24.

Measures of experience



C-MeX

- Retain overall incentive design, including higher payments?
- Considering increasing incentive size from $\pm 12\%$ of residential retail revenue

D-MeX

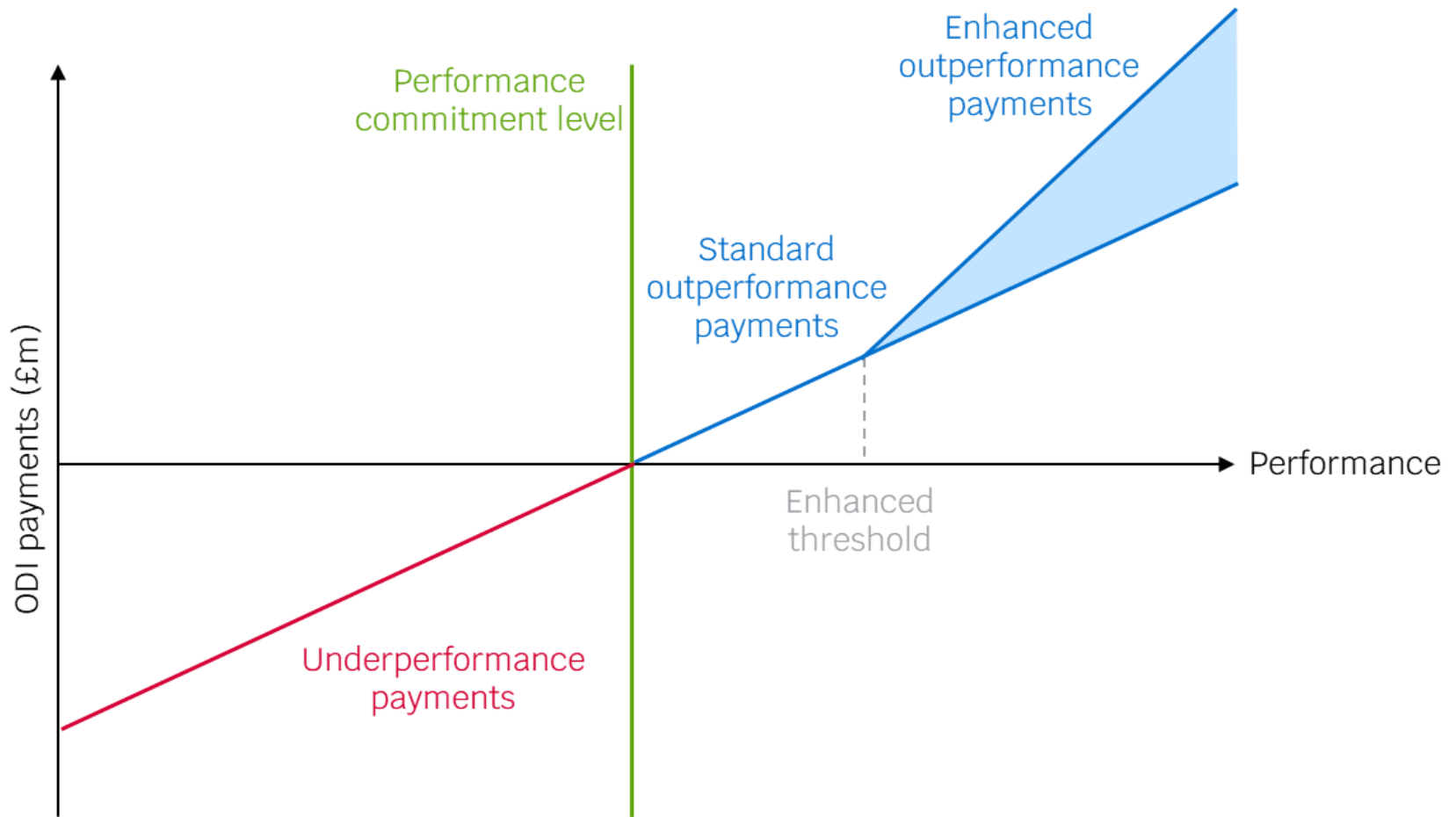
- Retain overall incentive design
- No change to incentive size from $+6\%$ to -12% of developer services revenue

BR-MeX

- Proposed design similar to D-MeX and standard payments for C-MeX
- Proposing $+0.5\%$ to -1.0% of wholesale revenue from business customers – proportionate to current C-MeX RoRE impacts

Enhanced incentives

Retaining enhanced incentives, **expanding** to all companies, while **streamlining** how we set them – with no enhanced underperformance payments.

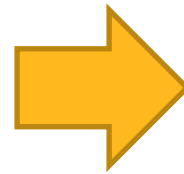


Enhanced incentives – design features

Proposed performance commitments for enhanced incentives

Key criteria:

- ✓ Clear benefits
- ✓ Well-established
- ✓ Limited company-specific factors
- ✓ No perverse interactions



- ▶ Water supply interruptions
- ▶ Internal sewer flooding
- ▶ External sewer flooding
- ▶ Total pollution incidents

Enhanced thresholds

Beyond the current frontier of performance

Incentive rates

Twice standard rates

Caps

No caps on enhanced outperformance

Knowledge sharing

Required to receive payments

Sector-wide benefits

Certainty in long-term benefits

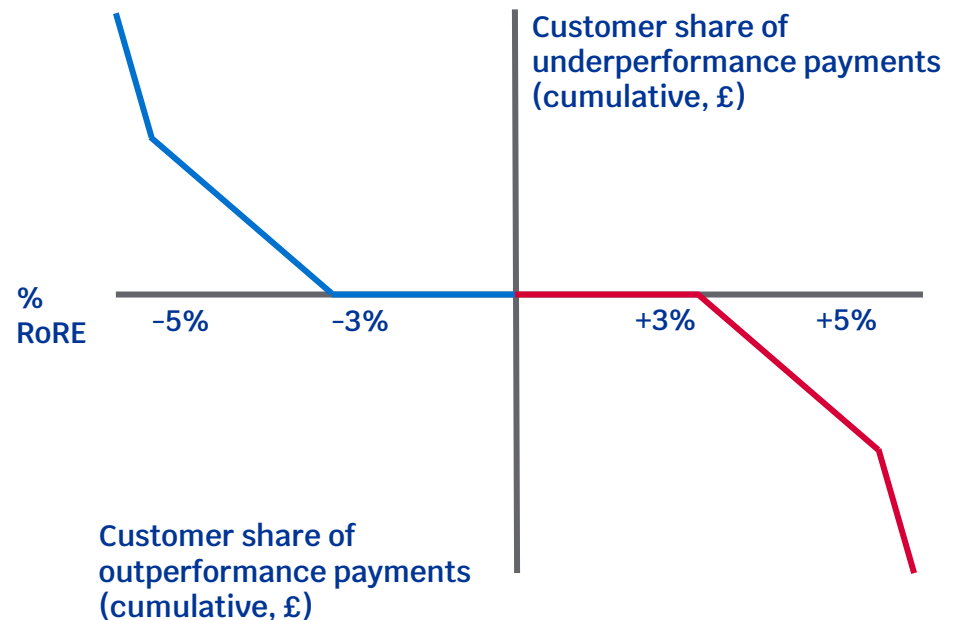
Assessing and managing risk

Targeted use of caps and collars on individual performance commitments – only where they are new, bespoke or have uncertain benefits from high outperformance. Use a top-down approach to set the levels of caps and collars.

Primarily use **aggregate sharing thresholds** to manage risk – set separately for water and wastewater payments. Proposing 50% sharing beyond $\pm 3\%$ RoRE and 90% sharing beyond $\pm 5\%$ RoRE.

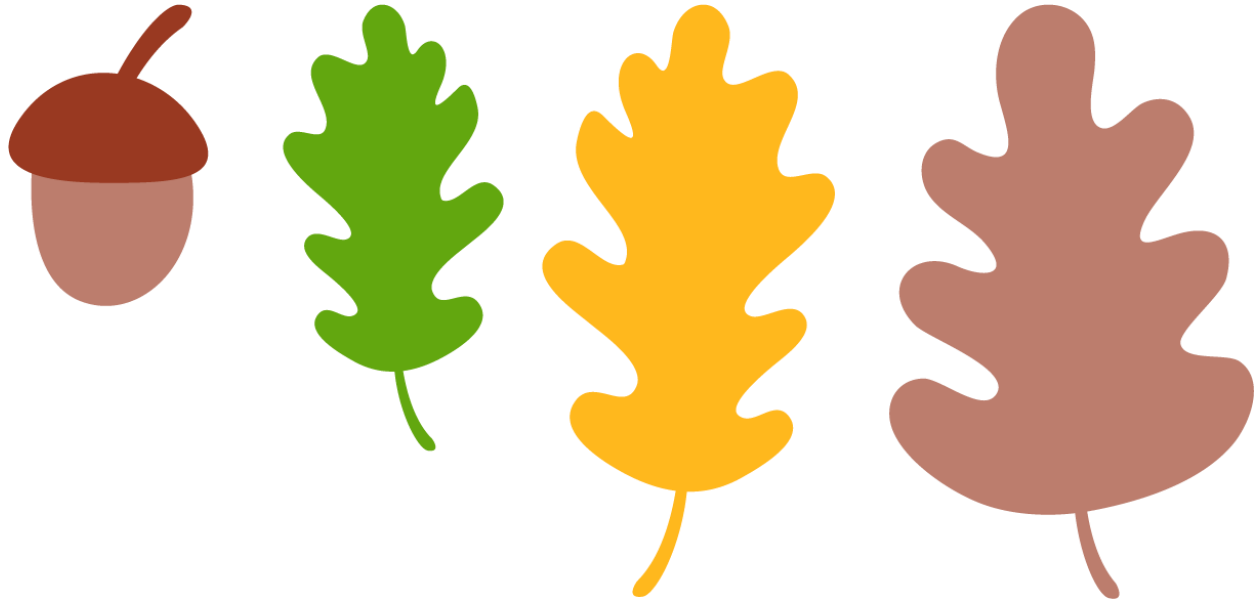
No deadbands, including on statutory compliance performance commitments.

Prefer a **light-touch approach to estimating ODI risk** – see consultancy report for options.



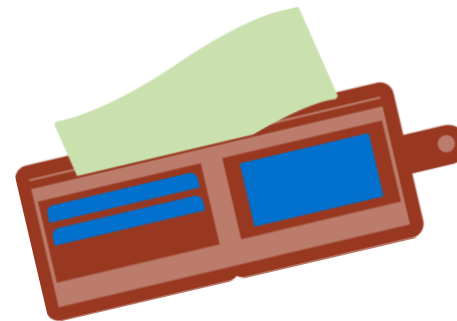
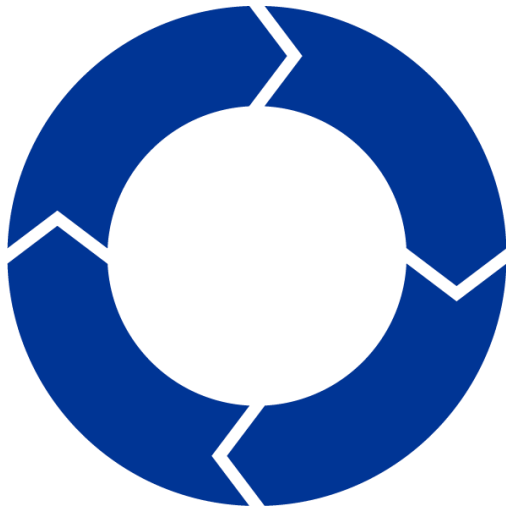
Incentivising outcomes beyond PR24

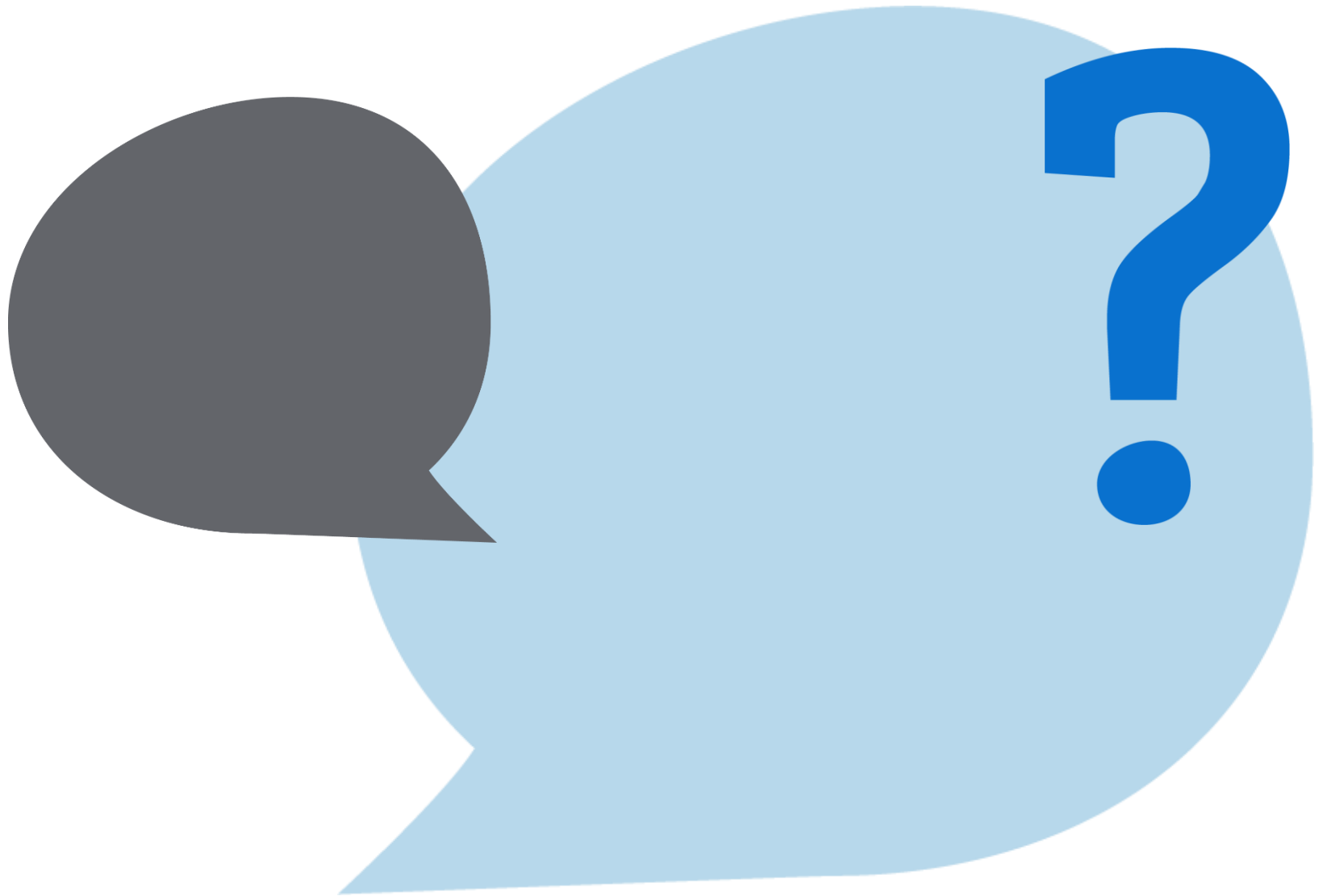
- We are committed to maintaining the outcomes framework in future price reviews, so **top performers should expect to continue to earn outperformance payments in future price control periods.**
- We are inviting views on whether there would be benefits to customers in providing greater certainty over incentive rates at PR29.



Implementing payments

- We propose to maintain our overall approach to in-period reconciliation, with incentive payments for all performance commitments expected to be applied through **annual revenue adjustments** for every company.
- We propose to continue to **allow deferrals each year**, and invite views on how we could **streamline the in-period process**.





The background features a large, solid blue shape on the left side, which is a quarter-circle or a similar curved form. To the right, there are several overlapping circles in various shades of light blue and white, creating a layered, abstract effect. The overall aesthetic is clean and modern.

Next steps

PR24 timeline and next steps

Consultation responses are due by **Wednesday 7 September at 5pm.**

