

PR24 draft methodology webinars: Delivering outcomes for customers – questions and answers

13 July 2022

Performance commitments

1. **Would potable water as measured by the proposed water demand performance commitment (PC) be adjusted for New Appointments and Variations (NAVs)? (Portsmouth Water)**

Yes, it would be removed if the new appointee has a bulk supply agreement with the incumbent company.

2. **For bespoke PCs, the consultation suggests that you propose to use standard definitions and may require all other companies to report these measures even if they do not have the PC. Could you talk about the practicalities of this? (Severn Trent Water)**

We may require all companies to report against the definition of bespoke PCs to help us understand a specific company's relative performance, such as for low pressure. But the other companies would not have financial incentives associated with them. We would only do this where it was relevant and not for all bespoke PCs.

Practically, we would introduce these reporting requirements through the Regulatory Accounting Guidelines (RAGs). In addition, where a few companies propose bespoke PCs that are driving the same outcome, where possible we would expect the same definitions for those companies.

3. **The bathing water performance commitment definition appears to apply only to coastal water (beaches). Is this correct? (Severn Trent Water)**

We are proposing that the PC only applies to bathing waters that are influenced by water companies. There is an open question about whether it will include inland rivers, as more get designated. We consider they should be included.

4. It seems a bit counterintuitive to exclude large users if we are considering moving to the distribution input target. What is the basis of the 50 megalitre per annum threshold? (South Staffs Water)

Large business customers have the resources to focus on water efficiency and we would expect retailers to target them. We also want to limit risks to water companies, including the impact of businesses moving out of a water company's area, where this can be done without affecting a company's focus on outcomes.

We consider 50 megalitres per annum is an appropriate level as this was the historic threshold for business customers prior to market opening in England, and it is a relatively small number of customers.

5. Could you clarify a statement that companies may have different definitions of common PCs? (Wessex Water)

Common PCs will have the same definitions across companies within a nation. We would also expect most common PCs to be the same across England and Wales.

However, some common PCs may have different definitions for Welsh and English companies. For example, the two Welsh companies will not have BR-MeX, but will have a common PC on business customer satisfaction that only applies to them.

6. Could you confirm what you mean by C-MeX, D-MeX and BR-MeX not being confirmed by the final methodology? You said that BR-MeX would be in the draft determinations. This seems quite late and creates uncertainty. (Wessex Water)

We note that C-MeX was developed following the final methodology at PR19, with some guidance coming after the final determinations.

We do not consider that companies need the detailed measure behind the measures of experience for their business plans. Unlike the other PCs which are absolute, rather than relative, measures.

This would allow further time to evaluate C-MeX and D-MeX. On BR-MeX, more work is required but we will publish a plan in the final methodology.

7. For the biodiversity metric, what is the rationale behind it being every four years and not every five years? (Wessex Water)

We want to strike a balance, as every year seems excessive and every five years seems too infrequent, but we welcome views on this.

8. We note there is no specific question on the storm overflows performance commitment. Where is it best to comment on this PC other than in the setting expenditure allowance section (Wessex Water)

There is a general question on the overall proposals in chapter 5 of the draft methodology.

9. On the bathing water PC, how it will account for the impact of other sectors on the bathing water? (Wessex Water)

We propose to exclude bathing waters when there is no impact by water companies. In other instances, we consider that water companies have a high degree of control over bathing water quality, notwithstanding third-party impacts. We consider that an outcome does not have to be fully in a water company's control to be worth incentivising. It is important to use incentives to achieve environmental benefits, including through partnership working.

We expect to use historical performance to set performance commitment levels and so the extent to which other sectors impact bathing water should on average be built in. In setting the performance commitment level, we would also want to take into account any expenditure under the water industry national environment programme (WINEP) and national environment programme (NEP) that will improve performance beyond historical levels of performance.

10. In the outcomes working group, low pressure was excluded from the list of proposed common PCs because it was deemed to not be a material issue. Are you now suggesting that this PC could apply to all companies if one company proposes it as a bespoke PC? (Bristol Water)

No, if a company has a bespoke PC, we may require other companies to report on it so we can set a benchmark. There would be no financial incentives for these other companies.

11. Could you confirm when is the early submission for PC definitions please, is it April or May 2023? (United Utilities)

April 2023.

12. Would you consider a proposal for a company-specific outcome measure focused on resilience that tracks progress towards a 2050 ambition on resilience, such as a risk reduction measure? Would this be a bespoke PC or a Price Control Deliverable (PCD)? (Dŵr Cymru)

It would depend on the purpose of the resilience measure, and whether having it as a bespoke PC with financial incentives rather than a reporting measure would provide significant additional benefits for customers.

If it relates to clawing back money for something that is not delivered, we would refer to this as a price control deliverable at PR24.

13. How will a combined water demand PC account for growth? If we have a combined measure, growth may be greater than water efficiency reduction leading to increase over time or at least a stable level. (South Staffs Water)

14. How would a combined measure on distribution input align with the Environment Act targets? (South West Water)

15. Would issues around growth and business cycles apply equally to a business demand PC? How can a PCL be set for this? (Severn Trent Water)

We are considering options for how we could account for growth and welcome views on this. Expectations about future growth will be built into water resources management plans (WRMPs). We expect companies to set out a best value approach to delivering long-term water demand reduction targets within their WRMPs.

Our current proposal on the water demand PC is that it would not be normalised by population. Currently, per capita consumption is normalised by population. There are a number of potential issues with normalisation, including the scale of population change and uncertainties around any estimates. We note that the Environment Act targets include normalisation.

Excluding the largest users reduces the risk on water companies from the economic behaviour of business customers, such as closing down or relocating sites outside of a water company's area. Water companies have to plan for how they will deliver water to customers for the future and manage the overall risk.

16. The common PC list does not cover community initiatives. Would this be a good candidate for bespoke PCs? (South Staffs Water)

We want to focus bespoke PCs on areas that deliver significant additional benefits to customers of the company, beyond the set of common PCs. The outcomes of some community initiatives may already be covered by other PCs, such as greater water efficiency and reduced sewer flooding.

We would only expect a bespoke PC related to community initiatives where the company does not already have incentives to deliver such initiatives through the set of common PCs, there is compelling evidence that significant additional benefits will be delivered through the bespoke PC, and it is suitable for financial incentives.

17. The draft methodology proposes to deal with vulnerability outside of the price review, with the priority service register no longer a common PC. How will you ensure clear incentives for such an important area? Do you expect companies to explore bespoke PCs instead? (Thames Water)

We do not expect companies to propose bespoke PCs relating to vulnerability. We recognise this is an important area and consider that it can be better addressed outside of the price review, through parallel work that is more flexible.

We also propose to continue to monitor the number of people on the priority services register and will consider taking action outside of the price review if progress in this area reverses. It may also be appropriate for companies that are poor performers in this area to have an underperformance-only bespoke PC.

18. There is a clear message from Ofwat to reduce the number of bespoke PCs. But it also wants to see ambition. Will putting forward bespoke PCs be seen as negative or positive in the business plan assessment? (South Staffs Water)

Ambition is about doing the most for your customers in the areas they care about. This is therefore likely to include proposing ambitious performance commitment levels on common PCs. Not proposing bespoke PCs will not be seen as unambitious in the business plan incentives (BPI) assessment if they are not required.

If there is an area that is important to customers, and is not covered by other PCs, we encourage companies to propose a bespoke PC if it meets our criteria for bespoke PCs. We discourage companies from submitting bespoke PCs that do not meet these criteria. If they are not required, bespoke PCs are not needed to reach the top category in the BPI assessment.

19. You mention a 'monitoring regime'. Could you confirm which metrics will be included in the monitoring regime or confirm when further information will be published? (Bristol Water)

We propose to monitor using a variety of different approaches. This includes the regulatory accounting guidelines (RAGs) – where we will consult on future monitoring. It could include information from [Discover Water](#). We also expect to use targeted information requests if needed to carry out our functions.

We may publish the information that we collect. We also monitor information that comes to us from other sources including from other regulators, customers and environmental groups.

20. Does the early submission for bespoke performance commitments only cover definitions, or does it include PCLs and ODI rates? (Bristol Water)

Definitions only. We will consider PCLs and ODI rates later in the PR24 process.

21. Are price control deliverables (PCDs) intended to be one-way adjustments only to return funding? (Thames Water)

This will be covered in the webinar on setting expenditure allowances.

Outcome delivery incentives

22. Which PCs are you proposing will not have both outperformance and underperformance payments? Does this include the asset health-related PCs? (South East Water; Wessex Water)

We expect that all PCs will have outperformance underperformance except for:

- the two statutory compliance PCs – because their performance commitment levels (PCLs) are set at 100% compliance then outperformance is not possible for these PCs; and
- bespoke PCs where we set them to address to poor performance for certain companies, which may be underperformance-only.

We confirm that we intend to set outperformance and underperformance payments for the asset health-related PCs (mains repairs, unplanned outage, sewer collapses). We note there is a mistake in Appendix 7 which incorrectly suggests these are underperformance only PCs.

23. The timing of receiving draft ODI rates may impact on the testing of overall plans with customers (South West Water)

This is actively being considered through the customer engagement steering group. We will share customer valuations and indicative ODI rates as soon as possible.

24. Who will set PCLs and by when? Do companies need to set targets in their business plans? (South East Water)

This will be covered in the webinar on setting expenditure allowances.

25. C-MeX relates to wholesale plus retail, and retail activities such as billing issues are the most common reasons for customer contacts. Is it right that BR-MeX should carry a similar weight in proportion to the activities that wholesalers undertake? (Severn Trent Water)

We have calibrated our proposed incentive range for BR-MeX proportionate to the activities covered by C-MeX.

We note that the scope of BR-MeX is slightly wider than C-MeX. For clarity, we calculated this by comparing residential retail revenue plus the wholesale revenue collected from residential customers, with the wholesale revenue collected from business customers and used this to inform a rate.

We welcome views on this approach.

26. What is the approach to caps and collars where companies had a bespoke PC in a previous period, but this is now a new common measure? In particular, external sewer flooding. (South West Water)

We want to take a consistent approach across companies when setting caps and collars. For common PCs that are well-established (such as external sewer flooding), we do not propose to set caps or collars. We propose to set caps and collars for new PCs.

27. Are the aggregate sharing thresholds applied at price control level or just at water/wastewater? (Southern Water)

This will be at an aggregate level: for water (water resources and water network plus) and wastewater (wastewater network plus and bioresources).

28. Will no deadbands on the compliance risk index likely create a recurring penalty for most companies every year? Is this proportionate? (South Staffs Water; Southern Water)

Yes, if this reflects a detriment to customers, which is the intention of the regime. This also provides a stronger incentive on companies to meet their PCLs.

29. On the 'light touch approach' in estimating ODI risk, will companies only provide overall ODI risk in RoRE terms but not P10/P90 per PC, and will Ofwat only estimate ODI risk for a notional company. Is this to avoid different views on estimating ODI risk between companies and Ofwat? (Thames Water)

We provide detail on this in the methodology and are interested in views from stakeholders. It is right that the light-touch approach would rely more on historical performance data, rather than companies' probability estimates at a PC level. However, we may need to ask for data on the new PCs.

There is some discussion on how we could estimate performance distributions for a notional company in PwC's report on [Methodologies for measuring outcome delivery incentive risk](#), see pages 8 to 14. We invite views on this.

30. Payments for C-MeX s are only paid by residential customers. Are you considering a charging rule to make sure that residential customers do not pay for BR-MeX payments? (Severn Trent Water)

We agree and we are considering using a charging rule, as well as other methods.