

October 2022

Draft determination of Severn Trent Water's in-period outcome delivery incentives for 2021-22

About this document

This document provides our draft determinations on the extent to which the price controls included in our [PR19 final determinations](#) need to be adjusted to reflect Severn Trent Water's performance for the 2021-22 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 adjustments, and our reasons for these, are set out in this document and in our [Sector overview: Draft determinations of in-period outcome delivery incentives for 2021-22](#).

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

We welcome your views by 21 October 2022. We will make our final determinations by 15 November 2022.

Background

At the 2019 price review (PR19), companies' made performance commitments, or pledges, to their customers and stakeholders about the service levels they would meet to make progress towards their outcomes. Severn Trent Water's performance commitments for the 2020-25 period are set out in [PR19 final determinations: Severn Trent Water - Outcomes performance commitment appendix](#).¹

Each performance commitment (PC) has an outcome delivery incentive (ODI) that provides either financial or reputational consequences for companies of outperforming or underperforming their performance commitments. Many of the financial ODIs are paid during the 2020-25 price control-period. The reason for this is to bring payments closer in time to when customers experience a given level of performance. The remaining incentives are paid at the end of the period.

ODIs act as an incentive for companies to deliver their committed levels of performance, returning funding to customers for foregone benefits if they deliver less than is expected. Companies that go beyond and deliver greater benefits than expected to customers and the environment can receive outperformance payments.

Severn Trent Water reported its performance against these performance commitments in its annual performance report (APR) in July 2022. We have considered this information and, where necessary, further information from companies' answers to our queries. In our draft

¹ We take account of performance commitments as set out in the PR19 definitions adjusted, if relevant, in accordance with Annex 2 of the company's performance commitment appendix. Annex 2 provides for changes and corrections to be made to 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](#).

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 each company's licence.

We will make our final determination by 15 November 2022. These will affect Severn Trent Water's customers' bills from the 2023-24 charging year.

As set out in the PR19 final determinations, if a company's outperformance is more than 3% of its wastewater or water regulatory equity for that year, it will receive only 50% of outperformance payments above this threshold, to protect customers against excessive costs. This applies 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.

In our [Sector overview Final determinations of in-period outcome delivery incentives for 2020-21](#) we deferred our determination of the value of companies' Per Capita Consumption (PCC) ODI payments for the 2020-21 to 2023-24 charging years to the end of the 2020-25 period. We set out this decision and the reasons for it in this [decision document](#) which we published after having considered stakeholder responses to our July 2021 consultation.

Executive summary

Having assessed the company's performance against its performance commitments in 2021-22, the ODI payments and performance are as reported by the company with the following exceptions:

- C-MeX and D-MeX – we are including a C-MeX outperformance payment of £0.234m and a D-MeX outperformance payment of £3.446m, based on the assessment of 2021-22 company performance;
- Reducing residential void properties – we are intervening to ensure that Severn Trent Water reports in line with the PR19 performance commitment definition and so maintains consistent reporting against the PR19 performance commitment levels. We are therefore intervening to include an outperformance payment of £0.230m.

See section 1 for details of our interventions and policy decisions.

We are allowing Severn Trent Water's requested deferral of £69.804m of its ODI outperformance payments, which includes the deferral of £46.214m from 2020-21. However, we expect the company to provide additional supporting evidence on its approach to managing the impact on customers ahead of the final determination.

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1. Results of our assessment

1.1 Interventions and policy decisions

Table 1.1 below sets out our view of the payments due, after any interventions, compared to the values reported by Severn Trent Water.

Table 1.1: Summary of interventions

Performance commitment	Company's reported payments 2021-22 (£m)	Our draft determinations after interventions 2021-22 (£m)	Difference (£m)
Reducing residential void properties	0	0.230	0.230

In our draft determination we are intervening on the following performance commitment:

Reducing residential void properties

We are intervening to ensure Severn Trent Water reports in line with its PR19 performance commitment definition, and so maintains consistent reporting against the PR19 performance commitment levels. We are therefore intervening in our draft determinations to include an outperformance payment of £0.230m for void supply points performance.

Severn Trent Water has restated the PCLs for 2021-22 (and the remainder of 2020-25 period) and changed its methodology for reporting. The company states in its APR and its response to query SVE-APR-IP-002 that it found errors in its reporting methodology when setting the PR19 PCLs. The reporting errors for 2021-22 amounted to 21,751 properties that had a status of 'invalid service provision', which it was including². The company explains that an invalid service provision relates to a property that has been substantially altered, demolished, or transferred to the wholesale market. It has restated the PCLs and changed its methodology to remove these types of properties from its reported performance. The company states it chose to follow the same approach taken in the 2015-2020 period, when it changed its Mains Bursts PCLs because of reporting methodology errors.

We have not allowed the change to the Residential Voids PCLs in our draft determination. Because the company's performance commitment levels were based on the information provided to us at PR19 and these levels therefore form part of the price control package agreed at PR19, there is a presumption that they will remain fixed for the 2020-25 period, to provide certainty for companies, customers and Ofwat. Therefore, we calculate the

² Performance is 166,437 voids reporting in line with the PR19 definition and 144,686 with the 'invalid service provision' properties removed.

company's performance in 2021-22 to be 166,437 voids (including the 'invalid service provision' voids) and an outperformance payment of £0.230m.

We note the company had previously said it will not claim outperformance due to its change in methodology, it is for the company to confirm in its response if it intends to do so in light of our draft determination.

We also comment on our policy decisions for the following performance commitments:

Leakage and Per Capita Consumption (PCC)

In our final in-period determination for 2020-21 we allowed £1.170m outperformance for Severn Trent Water's leakage performance commitment.

We have included an adjustment to reduce Severn Trent Water's outperformance payment in relation to its leakage performance commitment by £1.040m for 2020-21.

Severn Trent Water told us in its 2021-22 APR submission that during the 2020-25 period it continued to work towards full compliance with the standard reporting methodology and was updating its methodology. The company provided its numerical data relating to pre and post methodologies for leakage and per capita consumption. This data included annual average and three-year average baseline values and performance commitment levels for each year in the 2020-25 period in Ml/d unit for leakage and litres/person/day unit for PCC, based on the company's PR19 performance commitment levels expressed in % change from baseline.

Severn Trent Water has reported that all components of its leakage methodology are fully compliant with the exception of the water balance residual gap. For PCC the company confirmed that all components are compliant with the common methodology.

In its APR submission the company reported that, based on its restated leakage value for 2020-21, it will be returning c.£1m to customers through the in-period determination.

We consider that the company's revised methodology brings the company in line with other companies, which have been reporting their leakage and PCC performance using the PR19 methodology since 2020-21. Based on the information provided to us, the revised methodology represents a more accurate method and allows a direct comparison with the rest of the industry.

At PR19 we made it clear that companies should commit that their outcome delivery incentive payments will only relate to real performance changes and not definitional, methodological or data changes in the performance commitment. The changes implemented by Severn Trent Water result in the company earning lower outperformance for leakage and lower underperformance for PCC, with an overall financial benefit for its customers in the aggregate for 2020-21 and 2021-22.

Based on the company's restated values we have revised its baseline for the remainder of the 2020-25 period.

Sewer Blockages

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 has provided further information to support its submission. Given the potential for future outperformance payments for this PC, we expect the company to provide additional supporting evidence on its approach to managing the impact on customers ahead of the final determination (see section 1.3).

Water supply interruptions

Severn Trent Water told us it identified an error in the calculation for supply interruptions related to the analysis of property heights. It has applied a retrospective correction to reported performance and ODI payment for 2020/21. This change results in 16 seconds being added to the reported performance, taking it from 11 minutes and 21 seconds to 11 minutes and 37 seconds and increasing underperformance by £0.288m. In its response to query SVE-APR-IP-011 the company confirmed that this change is related to correction of a calculation error and not associated with definitional, methodological or data changes. Based on the information provided to us, we have made this change to the 2020/21 reported performance and associated ODI payment.

Aggregate sharing mechanism

At PR19 we introduced a mechanism that means that a company shares 50% of its outperformance payments with customers once the outperformance payments in any year reach 3% of its wastewater or water RoRE for that year. Severn Trent Water's 2021-22 outperformance on wastewater has reached this 3% threshold so £0.602m of the outperformance above this threshold is returned to customers because of the sharing mechanism.

1.2 C-Mex and D-Mex

On 21 September we published the relative performance of all companies. Our draft determination includes a C-MeX outperformance payment of £0.234m and a D-MeX outperformance payment of £3.446m, based on our assessment of 2021-22 company performance.

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.

1.3 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.

Severn Trent Water requested that we defer £69.804m of its ODI outperformance payments³. This includes the deferral of £46.214m from 2020-21. For draft determinations, we allow for the amount of deferred revenue Severn Trent Water has proposed. However, the company only provided limited information to explain its plan for managing this deferred revenue. Given the significant size of the deferral and the potential for further outperformance in future years, we expect the company to provide additional supporting evidence on its approach to managing the impact on customers ahead of the final determination. This should be in the context of potential risks and its wider performance and investment requirements.

Severn Trent Water 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 determinations.

³ Of which £20.759m is for water resources, £11.213m is for water network plus and £37.832m is for the wastewater network plus price control

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

2.1 Our draft determination

In this section we outline the financial impacts of our draft determinations.

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

Table 2.1: Draft determinations on adjustment to 2023-24 price controls as a result of performance against ODIs

This table sets out our draft determinations on the ODI payments to be applied to price controls in the 2023-24 charging year after accounting for:

- the in-period ODI payments for each company based on their performance in 2021-22;
- our draft determinations on these payments after any interventions;
- brought forward deferrals;
- our draft determinations on 2022-23 deferrals and abatements;
- bespoke adjustments, including prior year restatements, where relevant; and
- our draft determination on C-MeX and D-MeX payments.

For further details on the interventions, deferrals, abatements and bespoke adjustments, see section 1.

This draft determinations on the ODI payments to be applied for Severn Trent Water is also set out in the in-period adjustments model published on our website.

Draft determination of Severn Trent Water's in-period outcome delivery incentives for 2021-22

Price control	Company's reported ODI payments (£m)	Interventions (£m)	ODI payments deferred from 2020-21 (£m)	Ofwat DD deferrals (£m)	Ofwat DD abatements (£m)	Bespoke adjustments (£m)	C-MeX payments (£m)	D-MeX payments (£m)	Total ODI payments to be applied to customer bills in 2023-24 (£m)
Water resources	16.707	0.000	10.367	-20.759	0.000	1.684	0.000	0.000	8.000
Water network plus	6.263	0.000	2.692	-11.213	0.000	9.383	0.000	2.384	9.509
Wastewater network plus (WaSCs only)	31.717	0.000	33.155	-37.832	0.000	16.765	0.000	1.061	44.866
Bioresources (WaSCs only)	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Residential retail	0.021	0.230	0.000	0.000	0.000	0.000	0.234	0.000	0.485
Total	54.708	0.230	46.214	-69.804	0.000	27.832	0.234	3.446	62.860

Table 2.2: Breakdown of bespoke adjustments

This table provides a breakdown of the bespoke adjustments included in our draft determinations.

Price control	Prior year restatements (£m)	Prior year C-Mex indexation (£m)	Prior year D-Mex indexation (£m)	Prior year total (£m)	Time value of money adjustment on prior year total (£m)	Green recovery (£m)	Total bespoke adjustments to be applied to customer bills in 2023-24 (£m)
Water resources	0.000	0.000	0.000	0.000	0.000	1.684	1.684
Water network plus	-1.328	0.000	-0.183	-1.512	-0.044	10.939	9.383
Wastewater network plus (WaSCs only)	0.000	0.000	-0.056	-0.056	-0.002	16.822	16.765
Bioresources (WaSCs only)	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Residential retail	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Total	-1.328	0.000	-0.240	-1.568	-0.046	29.446	27.832

The prior year C-Mex and prior year D-Mex values correct an error in how the C-Mex and D-Mex models applied indexation in 2020-21. Where applicable we adjust for the time value of money.

Table 2.3: Changes to price controls (draft determinations)

This table sets out the impact of our draft determinations 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 2021-22](#) for how we are applying adjustments for tax and inflation.

Price control		2021-22	2022-23	2023-24	2024-25
Water resources (K factors)	Previous determination	3.45	8.31	3.79	-7.80
	Revised	3.45	8.31	16.16	-16.91
Water network plus (K factors)	Previous determination	-0.50	0.29	-3.52	0.28
	Revised	-0.50	0.29	-1.47	-1.63
Wastewater network plus (WaSCs only)	Previous determination	-1.85	1.41	-3.53	1.02
	Revised	-1.85	1.41	5.23	-6.72
Bioresources (WaSCs only)	Previous determination	76.857	77.205	77.395	77.743
	Revised	76.857	77.205	77.395	77.743
Residential retail (total revenue, TRt – £m, nominal prices)	Previous determination	105.067	106.087	107.008	107.922
	Revised	105.067	106.087	107.739	107.922

We have based Severn Trent Water's draft determination on the data and commentary provided to us by Severn Trent Water. 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.

3. Responding to this consultation

We would welcome any comments on this document. Please email them to in-periodODIs@ofwat.gov.uk or post them to:

IPD2022 Consultation response
Ofwat
Centre City Tower
7 Hill Street
Birmingham B5 4UA

[Or Ofwat, 11 Westferry Circus, Canary Wharf, London, E14 4HD if that is more appropriate.]

The closing date for this consultation is **21 October 2022**. If you wish to discuss any aspect of this consultation, please contact the In-period ODI team by post or by email at in-periodODIs@ofwat.gov.uk

We intend to publish responses to this consultation on our website at www.ofwat.gov.uk. Subject to the following, by providing a response to this consultation you are deemed to consent to its publication.

If you think that any of the information in your response should not be disclosed (for example, because you consider it to be commercially sensitive), an automatic or generalised confidentiality disclaimer will not, of itself, be regarded as sufficient. You should identify specific information and explain in each case why it should not be disclosed and provide a redacted version of your response, which we will consider when deciding what information to publish. At a minimum, we would expect to publish the name of all organisations that provide a written response, even where there are legitimate reasons why the contents of those written responses remain confidential.

In relation to personal data, you have the right to object to our publication of the personal information that you disclose to us in submitting your response (for example, your name or contact details). If you do not want us to publish specific personal information that would enable you to be identified, our [privacy policy](#) explains the basis on which you can object to its processing and provides further information on how we process personal data.

In addition to our ability to disclose information pursuant to the Water Industry Act 1991, information provided in response to this draft determination, including personal data, may be published or disclosed in accordance with legislation on access to information – primarily the Freedom of Information Act 2000 (FoIA), the Environmental Information Regulations 2004 (EIR) and applicable data protection laws.

Please be aware that, under the FoIA and the EIR, there are statutory Codes of Practice which deal, among other things, with obligations of confidence. If we receive a request for

disclosure of information which you have asked us not to disclose, we will take full account of your explanation, but we cannot give an assurance that we can maintain confidentiality in all circumstances.

We will publish our final determinations by **15 November 2022**, after considering representations from all stakeholders.

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