The voice for water consumers
Llais defnyddwyr dŵr

CCW response to Ofwat's draft determinations of in-period Outcome Delivery Incentives for 2021-22

October 2022

1. Introduction

1.1 The Consumer Council for Water (CCW) is the independent voice for water consumers in England and Wales. Since 2005, we have helped thousands of consumers resolve complaints against their water company, while providing free advice and support. All of our work is informed by extensive research, which we use to champion the interests of consumers and influence water companies, governments and regulators.

1.2 We welcome the opportunity to respond to Ofwat's draft determinations on the 2021-22 in-period Outcome Delivery Incentives (ODIs).

2. CCW's response

2.1 CCW supports appropriate ODIs which drive the right outcomes for customers and which reward companies proportionately for delivering real market leading improvements that customers' value. ODI outperformance payments (rewards) should be a reflection of outstanding performance in areas of service customers' view as priorities.

2.2 ODI rewards earned by companies need to be commensurate with the benefits that customers receive, while penalties should be reflective of a company's failure to deliver its service delivery commitments.

2.3 This year sees an industry level net penalty £53.398m adjustment to existing price controls, reflecting a failure to meet targets across a range of Performance Commitments (PCs), with ten companies set to see reduced revenue allowances in 2023-24.

2.4 This sends a clear signal to consumers that these ten companies are failing to deliver their commitments. The resulting financial penalties and the reputational damage from the publicity this has generated should push companies to improve, particularly in areas of service that more directly reflect people and businesses' experience or customers' priorities.

2.5 Of the remaining companies, there are a number with net rewards, some of which are substantial. While customers will welcome companies being penalised for missing targets, we believe that targets haven't been sufficiently stretching for those companies who have significantly exceeded them. We want Ofwat to challenge the target levels, particularly for bespoke ODIs, and put further controls in place to ensure customers are not paying more than they should.

2.6 We support Ofwat's decision to adjust rewards and penalties where companies have been non-compliant with ODI reporting requirements.

2.7 We agree with Ofwat's decision not to make exceptions for Northumbrian, South West Water, South East Water and Yorkshire Water where a combination of extreme weather events and third party damage to company infrastructure contributed to failure. In our response to Ofwat's draft PR24 methodology[1], we stated that companies should not exclude

[1] CCW's response to Ofwat's draft methodology for the 2024 Price Review (see page 21)

performance affected by weather events relating to PCs that are affected by these issues (for example, sewer flooding and water supply interruptions). This is because companies should carry this risk, as they can also gain benefits if they experience a period of good weather leading to reduced pressure on their water and wastewater networks.

2.8 Severn Trent are an outlier in this year's ODI results with £62.86m net rewards. We agree that to reduce the impact of this on customer affordability, the collection of the reward should be deferred and spread over a longer period. Given the significant size of the deferral and the potential for further outperformance in future years, this implies that the company could be deferring a significant bill spike for customers to a later date. We welcome Ofwat's recognition of this risk and the request to Severn Trent to provide additional supporting evidence on its approach to managing the impact on customers ahead of Ofwat's final ODI determination. This should be in the context of potential risks and the company's wider performance and investment requirements at PR24.

2.9 Southern have a net penalty of £28.297m which includes a bespoke adjustment of £10.798m to remove the tax element of the company's 2020-21 ODI performance. Ofwat has made a reduction in the marginal tax rate to 0% as the company is not expecting to incur tax in the current AMP. We would like Ofwat to consider deferring this tax adjustment to 2024-25 as the resulting increase in the net penalty would help offset the impact of high inflation on customers' bills in 2023-24. The bespoke adjustment could be added to revenue allowances later at a time when inflation is possibly lower.

2.10 We want Ofwat to allow an acceleration of penalties for the remainder of the AMP, as a short term benefit to help offset the impact of high inflation in 2023-24 charges, and to help smooth bill profiles.

2.11 CCW is aware that some companies are considering the possibility of accelerating future penalties so they are applied to customers' bills earlier. This would be based on forecasts of future performance, supported by convincing evidence. The current ODI framework means there is a time lag between actual performance and the resulting ODI impact on customers' bills, so we suggest that flexibility to allow forecast penalties to be applied sooner would be beneficial for customers at a time when they are being impacted by higher inflation.

2.11 If actual performance turns out to be different to the company's forecast this could be adjusted later, though we recognise that this would need to be considered in the round with other true ups and adjustments companies may propose during a price review.

2.12 When setting its final determinations for 2021-22 ODIs, Ofwat should direct companies to:

- ensure that they publish easy to understand explanations of their performance against the various ODIs in customer-friendly terms;
- what the associated ODIs mean for customers' bills, and
- what the companies are doing to improve performance in areas where they are failing to deliver against their commitments.

Enquiries

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Date: 21 October 2022