

September 2023

Draft determination of Southern Water's in-period outcome delivery incentives for 2022-23

Ofwat

About this document

This document provides our draft determination on the extent to which the price controls included in our PR19 final determinations, need to be adjusted to reflect Southern Water's performance for the 2022-23 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 2022-23](#).

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

We welcome your views by 18 October 2023. We will make our final determinations by 15 November 2023.

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. Southern Water's performance commitments for the 2020-25 period are set out in PR19 final determinations: Southern Water – Outcomes performance commitment appendix, which is available on our [website](#).¹

Each performance commitment 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.

Southern Water reported its performance against these performance commitments in its annual performance report (APR) in July 2023. 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 2023. This will affect Southern Water's customers' bills from the 2024-25 charging year.

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 2022-23, 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 underperformance payment of £3.657m and a D-MeX underperformance payment of £1.817m, based on the assessment of 2022-23 company performance.

See section 1 for the results of our assessment.

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1. Results of our assessment

1.1 Interventions and policy decisions

The company has not requested any interventions to its reported performance and ODI payments. Based on our assessment of the company's performance, we do not consider any are required.

We make comments with respect to the following areas:

Leakage

Southern Water has reported a 0.2% reduction against its leakage performance commitment level of 9.0% for 2022-23. We are applying the reported underperformance payment of £2.332m in line with the operation of this performance commitment.

In its 2022-23 APR submission, the company states that it has maintained reporting in line with the baseline methodology in accordance with the expectation set out in our [Final determination of Southern Water in-period outcome delivery incentives for 2021-22](#), and that all water balance data submitted in the APR has been produced in a way that is entirely consistent with the three-year rolling average baseline. Southern Water has confirmed that there has been no change to the RAG compliance checklist submitted in 2020-21 and 2021-22. We note this means that the company has still not achieved full compliance with the [PR19 common performance commitment definitions](#) and the [leakage reporting guidance](#).

Southern Water also stated that it continues to run parallel reporting internally with amendments being made to address the remaining amber elements and whilst it is yet to be fully compliant, further changes are being introduced to this shadow reporting with the aim of being fully compliant by the start of the 2025-2030 period.

We expect all companies to be reporting full compliance with the leakage and PCC methodology. Should any leakage information be revised or restated in future, our subsequent determinations will take account of the company's relevant performance and the adjustments we have made to the relevant price control in relation to the leakage performance commitment.

Tax

In its 2021-22 APR, Southern Water submitted information to support its view that it does not expect to pay corporation tax within the 2020-25 period. Based on the information provided, in our [Final determination of Southern Water's in-period outcome delivery incentives for 2021-22](#), we adjusted the modelled tax rate to 0% for 2021-22 and the remainder of the 2020-25 period.

In its 2022-23 APR, the company submitted updated information to support its view that its view that it does not expect to pay corporation tax within the 2020-25 period, due to its high capital allowances and taxable losses that reduce its future tax liabilities. Based on the information provided this year, we consider that a tax rate of 0% for 2022-23 remains appropriate.

Pollution incidents

In its 2022-23 APR, Southern Water states that it is reporting pollution incidents identified retrospectively and that other companies may not have reported these incidents in the same way. It questions whether the total number of pollution incidents reported in the Environmental Performance Assessment (EPA) is comparable across companies. The Environment Agency undertook a review to ensure that guidance was being followed and that there was a level playing field between companies. The review concluded that guidance was being followed in the vast majority of cases but did identify a small number of Southern water incidents which were being reported differently to other companies. These remained classified by the Environment Agency as incidents and /or permit breaches but were not included in the EPA to ensure fair comparison across companies. This did not affect the company's pollution incident or overall EPA rating. Consequently, for the purpose of calculating the company's performance, we use the number of pollution incidents for which the company is responsible, as determined by the Environment Agency.

If in the future additional pollution incidents are identified that should have been reported, we may adjust performance payments accordingly.

1.2 C-MeX and D-MeX

On 26 September we published the relative performance of all companies. Our draft determination includes a C-MeX underperformance payment of £3.657m and a D-MeX underperformance payment of £1.817m, based on our assessment of 2022-23 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.

Southern Water did not request any payment deferrals or 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 deferrals or abatements in our draft determination.

2. Impact of 2022-23 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 determination on adjustment to 2024-25 price controls as a result of performance against ODIs

This table sets out our draft determination on the ODI payments to be applied to price controls in the 2024-25 charging year after accounting for:

- the in-period ODI payments for each company based on their performance in 2022-23;
- our draft determination on these payments after any interventions; and
- our draft determination on C-MeX and D-MeX payments.

For further details, see section 1.

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

Price control	Company's reported ODI payments (£m)	Ofwat DD ODI payments (£m)	ODI payments deferred from 2021-22 (£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 2024-25 (£m)
Water resources	-0.958	-0.958	0.000	0.000	0.000	0.000	0.000	0.000	-0.958
Water network plus	-14.399	-14.399	0.000	0.000	0.000	0.000	0.000	-0.795	-15.193
Wastewater network plus (WaSCs only)	-20.187	-20.187	0.000	0.000	0.000	0.000	0.000	-1.022	-21.209
Bioresources (WaSCs only)	-1.286	-1.286	0.000	0.000	0.000	0.000	0.000	0.000	-1.286
Residential retail	-0.600	-0.600	0.000	0.000	0.000	0.000	-3.657	0.000	-4.257
Total	-37.429	-37.429	0.000	0.000	0.000	0.000	-3.657	-1.817	-42.903

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)	Time value of money adjustment on prior year total (£m)	Green recovery (£m)	Total bespoke adjustments to be applied to customer bills in 2024-25 (£m)
Water resources	0.000	0.000	0.000	0.000
Water network plus	0.000	0.000	0.000	0.000
Wastewater network plus (WaSCs only)	0.000	0.000	0.000	0.000
Bioresources (WaSCs only)	0.000	0.000	0.000	0.000
Residential retail	0.000	0.000	0.000	0.000
Total	0.000	0.000	0.000	0.000

Table 2.3: Changes to price controls (draft determinations)

This table sets out the impact of our draft determination 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 2022-23](#) for how we apply adjustments for tax and inflation.

Price control		2021-22	2022-23	2023-24	2024-25
Water resources (K factors)	Previous determination	-2.04	2.55	1.54	-3.45
	Revised	-2.04	2.55	1.54	-7.06
Water network plus (K factors)	Previous determination	0.83	-4.00	0.69	-0.10
	Revised	0.83	-4.00	0.69	-9.38
Wastewater network plus (K factors)	Previous determination	0.99	-9.29	2.90	4.29
	Revised	0.99	-9.29	2.90	-1.07
Bioresources (unadjusted revenue, URt - £m, 2017-18 FYA CPIH prices)	Previous determination	46.880	45.628	46.688	48.187
	Revised	46.880	45.628	46.688	46.900
Residential retail (total revenue, TRt - £m, nominal prices)	Previous determination	50.921	44.094	48.454	52.911
	Revised	50.921	44.094	48.454	47.468

We have based Southern Water's draft determination on the data and commentary provided to us by Southern 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 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:

IPD2023 Consultation response
Ofwat
Centre City Tower
7 Hill Street
Birmingham B5 4UA

Or IPD2023 Consultation response Ofwat, 11 Westferry Circus, Canary Wharf, London, E14 4HD.

The closing date for this consultation is **18 October 2023**. 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 draft determination 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 overview document, 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 2023**, after considering representations from all stakeholders.

**Ofwat (The Water Services Regulation Authority)
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