Draft determination of Hafren Dyfrdwy's in-period outcome delivery incentives for 2022-23

Hafren Dyfrdwy response

October 2023

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Overview of our response

We welcome the opportunity to respond to Ofwat's consultation on the draft determination of our in-period delivery incentives for 2022-23. We are pleased that Ofwat has accepted nearly all of our Outcome Delivery Incentive (ODI) calculations.

On the leakage front, we recognise there is a need to improve our data so that we are less reliant on data from Severn Trent and that Ofwat has adjusted the underperformance payment to reflect this.

Regarding the interventions made in relation to supply interruptions, we have identified additional points that we would like to raise with Ofwat. These are set out below.

Fair comparisons with targets and with other companies

Ofwat's stated policy is that ODI outperformance payments should relate to real changes in performance rather than to definitional, methodological or data changes in the performance commitment. We agree with this position. It is right that performance and targets should be set using a common approach as this enables a like-for-like comparison.

As a general principle, if different measurement would have led to a different target being set at the determination, then there are two ways to deal with this:

- **a change to the target**, such that it is consistent with the new basis of measurement; or
- **continuing with the previous basis of measurement** for the duration of the control period, even if this is less accurate.

The position with supply interruptions is different, because Ofwat set the identical sector-wide targets for all companies by reference to the best performing companies in the industry. Crucially, this means that our previous approach to reporting had no influence on the way that the Performance Commitment Level (PCL) was set.

With this in mind, our change to reporting would bring our actual performance measurement closer to the basis on which the PCL was set – measuring pressure in the main rather than at ground level. Moreover, even if we had reported on this basis at the end of AMP6, the position of the bast performers would have remained unchanged in the sector and so too the PCL would have remained unchanged. The only benefits would have been a better entry point into AMP7 and improved levels of reported performance in each of the first three years of this AMP. Nevertheless, we are not seeking to revise the calculated ODI underperformance payments for either 2020-21 or 2021-22, given that we did not raise this issue at the time.

Rather, we are seeking to address the issue this year and moving forwards. The key part of our logic is that this will allow us to report performance in a way that is consistent with the underlying basis of the PCLs. Were we not to take this approach, we'd effectively be signing ourselves up for a tougher set of targets for the remainder of the AMP.

Open and transparent reporting

The principle we follow whenever we change our approach to reporting any measure is to always be transparent about this and not seek to claim any outperformance payments where we do not think this is warranted.

Consistent with this mindset, our Annual Performance Report (APR) disclosed that, for supply interruptions, we had undertaken height analysis to demonstrate when the network had reached an appropriate level of pressure that would allow us to stop or remove temporary supply arrangements. Critically, the change required us to include an assessment of mains depth, so that we could assess how much pressure we would need to restore supplies to a property.

Response to specific challenges in Ofwat's in-period determination

Other companies in the sector adjusting their performance for mains depth

Within the timeframe available for this consultation, it has been difficult for us to obtain a comprehensive view of practice across the industry. This is an area where we think Ofwat may be better placed to obtain a fuller picture more quickly than ourselves.

As we set out in our query response, we consider this to be the best practice approach and not something that ought to be discouraged. We consider that more accurate measurement is in the customer interest as it will drive a better operational response via:

- quicker removal of temporary supplies, reducing the risk of discolouration;
- faster clearance of worksites and roadworks that reduces disruption for customers; and
- greater cost efficiency – with customers benefitting through the totex efficiency incentives.

It follows that if we are required to continue reporting on the old basis, then our customers will forgo the above benefits and we will need to continue with our existing, more traditional approach to supply interruptions.

Application of adjustment to both the start and stop time for interruptions

We have complied with the requirement – per the reporting guidance – that the starting time for interruptions should be measured from the time at which the property does not receive at least 3m of pressure in the main (or sooner if notified by the customer). The change we have made is simply a better assessment of the time at which properties have their supply restored using the same measure of pressure. This has been done using an assessment of the mains depth, which affects the point at which properties will receive the relevant level of pressure.

In our approach, the same assessment of depth has been used for both the start and stop times. It is worth noting that taking this into account for the starting point will also tend to shorten the duration of interruptions, because the pressure in the main will always be higher than the pressure at ground level. However, the effect on the starting point will be much more limited, because the loss of pressure during an interruption event usually happens extremely quickly – for example, due to a burst. By contrast, restoring pressure is a much more gradual process to avoid jumps in pressure than can cause further burst and interruptions – with the water than necessarily taking time to circulate through the network.

It's also worth calling out that some start times are determined by the point at which customers contact us to indicate that there is an interruption to supply, so the start time is not based on network modelling. For the avoidance of doubt, the difference of 43 seconds stated in our query response is the full impact of the change in approach.

Compliance with reporting requirements in previous years

We have complied with the reporting requirement in previous years:

- our start point began at the time when there was insufficient pressure (or earlier if notified by a customer).
- our end point began at the time when we assessed that there was sufficient pressure.

The only change has been the way in which we assess whether properties are receiving sufficient pressure for their performance to be considered as restored. In terms of why we did not report this way in previous years, it's simply because we had not considered the effect of mains depth before.

Change in performance not related to real operational improvement

It is true that the change in performance compared to 2021-22 is partly due to a change in measurement. If we were calculating a percentage change compared to the prior year, that would be slightly distorted by this change in methodology. However, this would only be important if our target was set relative to the prior year, which it is not. Rather, we have over-stated the duration of supply interruptions in the first two years of AMP7 and we have borne the consequences of doing so.

As noted above, we are not seeking to make this change retrospectively to the levels of performance we have reported in previous years. Instead, we are only requesting that we be allowed to report on the same basis as other companies – and the basis of the PCL – going forwards. More broadly, as our PCLs will remain unchanged, there does not seem to be a case for pushing back this change in reporting approach to AMP8 rather than implementing it now – particularly once the benefits for customers identified above are taken into account.

Consistency of information in Ofwat's draft determination

We are struggling to reconcile some of the narrative and tables in Ofwat's draft determination.

Leakage underperformance payment

- Executive summary and Table 1.1: increases by £0.071m
- Main document: a "bespoke adjustment" of £0.081m, but this is represented as being an increase from £0.031m to £0.102m – a difference of £0.071m
- Table 1.1: calculates the movement from £0.031m to £0.102m as £0.071m

We assume that table 1.1 is correct, but it would be helpful if Ofwat could confirm.

Summary of interventions

- Executive Summary and Table 1.1: £0.150m (£0.071m for leakage and £0.079m for supply interruptions)
- Table 2.1: Ofwat DD ODI payments for water network plus are £0.345m compared to a company total of £0.234m (a difference of £0.111m).
- Table 2.1 then adds a "bespoke adjustment" of £0.085m, bringing the total underperformance payment to £0.395m (a difference of £0.196m).

The only reference to a "bespoke adjustment" in the document is the £0.081m in the main document, which we believe to be incorrect as it does not match the difference between the company and Ofwat view of leakage. In any case, this does not appear to be separate from the challenge on leakage

performance, which is already reflected in table 1.1. Subject to our challenge on supply interruptions we believe that table 1.1. is correct, but again it would be helpful if Ofwat could confirm this.