

## Wessex Water Services Ltd Response to Ofwat's PR19 Draft Determination – August 2019

**Representation reference:** Outcomes O3

**Representation title:** Internal sewer flooding

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### Summary of issue

The intervention in our draft determination sets our incentive rates by arbitrarily using the results of a single piece of customer research, rather than triangulating a wide range of research methodologies as required in the PR19 methodology. This is despite the fact that Ofwat said our customer research and triangulation were both high-quality. This decision does not reflect the views or preferences of our customers and so should be reversed. The same is true for our enhanced incentive rates.

Our original incentive rates were -£11.9m and +£7.1m per incident per 10,000 properties. These have been more than halved to -£4.715m and +£3.296m.

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### Change requested

We request that our incentive rates (including enhanced rates) are set at the values we proposed in our business plan, which are supported by customers and based on research and triangulation that Ofwat has called 'high quality' and has been assured by a respected and independent third party.

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### Rationale (including any new evidence)

Ofwat's regulatory framework is intended to reward and encourage efficiency and innovation. One of the draft determination's key justifications for limiting our incentive rates is that "*The company has strong past performance in this area and is forecast to earn a large net outperformance payment*". This is in clear opposition to Ofwat's intention.

We do not support the use of 'reasonable ranges'. Our customer research and triangulation has been widely praised and we are very confident that we have provided ODI rates that accurately reflect customer preferences.

If reasonable ranges are used, then it is important to ensure that the quality of research undertaken by different companies is high before assessing 'reasonable ranges' – there is no evidence that Ofwat has undertaken this at either IAP or DD stage. There should be clear and transparent explanations for removing companies from the comparison and for choosing ranges around the mean (or median) within which companies might be expected to fall. There should be a consistent approach that is well evidenced and supported by recognised good practice. This is not currently the case.

Should this approach be retained, we note that our outperformance incentive rate was the fourth highest of 11 companies at IAP stage. Whilst some companies have chosen to reflect the arbitrary ranges in the draft determinations, the value suggested by our customer research sits only slightly above the median of values proposed in business plans.

Below, we set out the specific valuations we received from each piece of research, the triangulation weightings applied to each and the calculation applied to define the incentive rate.

**Figure 1-1**

Data source	£ / hh / yr	Weighting
2017 Conjoint Analysis	0.0465	38.5%
Max Diff Approach 1	0.0028	1.3%
Max Diff Approach 2	0.3222	1.3%
Max Diff Approach 3	0.6639	1.3%
2012 Conjoint Analysis	0.3390	7.7%
Sliders - data set 1	0.0644	10.3%
Sliders - data set 2	0.0583	20.5%
Website game - data set 1	0.1248	3.8%
Website game - data set 2	0.1178	5.1%
Website game - data set 3	0.1137	10.3%
Weighted Average	0.10	£ / hh / year / incident
Gives us	0.1	£m / yr / incident
Gives us a marginal benefit	14.1	£m / yr / incident / 10k properties
With a 50% sharing rate gives us a reward rate of	7.1	£m / incident / 10k properties
With a marginal cost of £4.5m & a 50% sharing rate gives us a penalty rate of	<b>-11.9</b>	£m / incident / 10k properties

This was one of our most widely covered performance commitments in our research, featuring in ten separate surveys. The outcomes of these ten pieces of research also have a standard deviation that is smaller than the vast majority of performance commitments. It is also apparent from figure 1-1 that eight of the ten pieces of research assigned a higher reward value than that proposed in the draft determination.

It appears, therefore, that Ofwat's decision is based more around a concern about outperformance payments than it is on factual or fundamental points of evidence. This is not in customers' interests because we have shown through our customer research that customers do value this enough to pay incentives and, by making this change, the determination is not acting in customers' interests.

## Why the change is in customers' interests

Our customers supported our business plan, with evidence of high acceptability and affordability. Our incentive rates should act as encouragement to continue to outperform and Ofwat should not limit that through concerns that companies might earn outperformance payments. This encouragement is severely reduced by the more than halving of our incentive rates and will encourage the wrong behaviours (i.e. we will be incentivised to do

less to prevent sewer flooding where it costs more to do so, even though our customers have clearly indicated that they want us to do more).

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**Links to relevant evidence already provided or elsewhere in the representation document**

DD representation - Outcomes summary

Response to IAP – standalone document

Chapter 1 and associated appendices of business plan

Chapter 3 and associated appendices of business plan