

4.1 UNPLANNED OUTAGE PC

30 August 2019

DRAFT DETERMINATION - NORTHUMBRIAN WATER REPRESENTATION

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Ofwat challenge

NES.OC.A35-A38 and NES.OC.C5 - Ofwat has intervened to set a tighter performance commitment and remove our underperformance collar between 2020-21 and 2024-25.

	2020-21	2021-22	2022-23	2023-24	2024-25	% reduction
NWL IAP	7.38%	7.2%	7.02%	6.84%	6.67%	-9.6%
Ofwat Draft Determination	6.37%	5.36%	4.36%	3.35%	2.34%	-63.3%

Company response

Unplanned outage is a new common measure being introduced at PR19 with the definition only being confirmed on 4 April 2019. Shadow reporting has already commenced and performance varies across the industry.

Due to the limited time operating this measure we believe there are different levels of compliance across the industry. Compliance has been checked via individual company auditors. However, there has been no industry horizontal audit of companies to confirm the same application of the measure.

We have reviewed the industry's commentary with regard to penalties on unplanned outage, and it is noticeable that companies, whilst agreeing to the measure, are advising caution on ODIs related to it. Yorkshire Water and Welsh Water have both argued that this should be reputational only, whilst a number of other companies have put forward other recommended collars to reflect a balanced exposure on risk, including Severn Trent Water.

This is consistent with Ofwat's own targeted review of this PC in 2018.

Ofwat's response has been to remove a number of collars and request penalty rates to be applied. Within the Technical appendix 1: Delivering outcomes for customers, Ofwat indicated an upper quartile value based on 9 of the 17 companies within the industry. This upper quartile value was deemed to be the lower bound underperformance rate at -£0.897 /HH/%.

We express concern at the inconsistent application of this 'lower bound underperformance rate' across the industry. Using data supplied by Ofwat (Draft Determinations), we find that 11 of the 17 companies (not including Thames Water with their two tier rates) have rates lower than this boundary. They range between -£0.627 and -£0.839 /HH/% of maximum production capacity. This gives an average value of -£0.694.

A further two companies have applied the lower bound rate as required by Ofwat.

The table below shows underperformance penalties in ranges, demonstrating that the largest number of companies have rates between -£0.6 and £0.69 /HH/%.

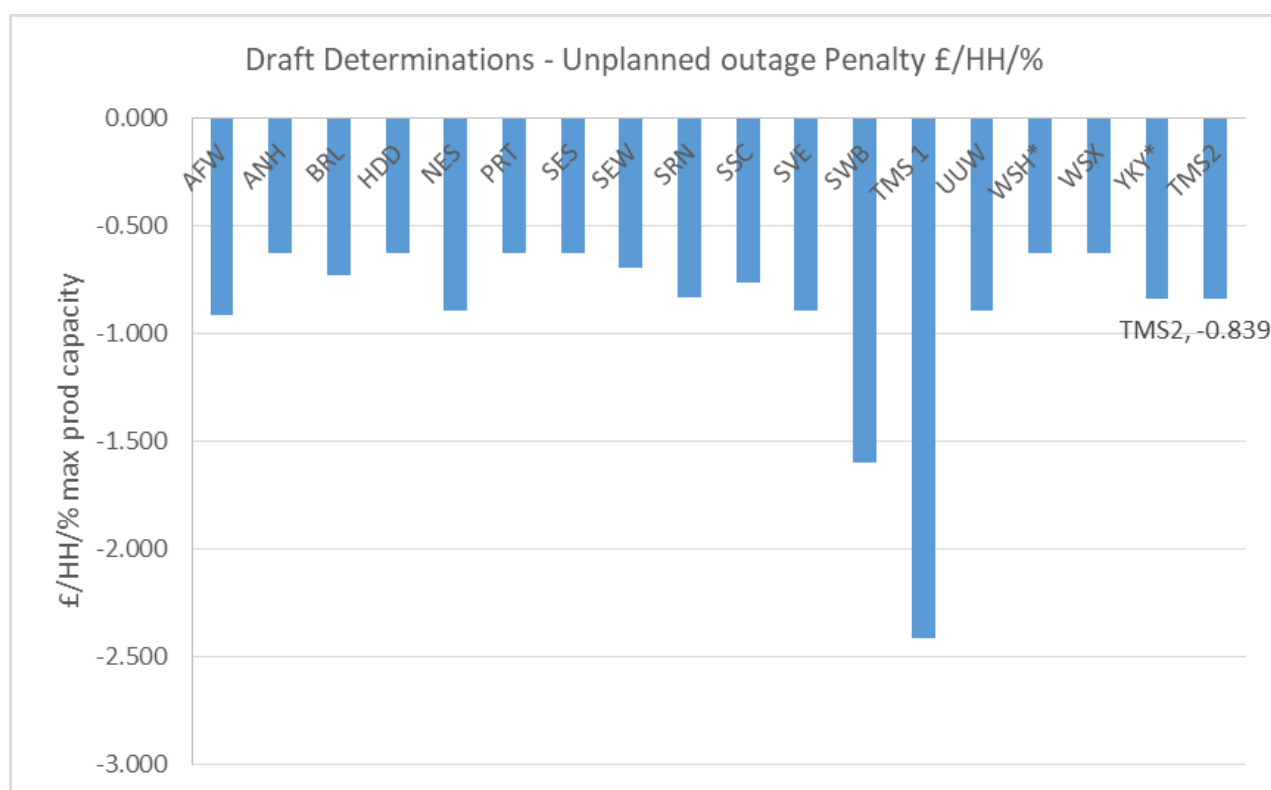
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Draft £/HH/% ranges	No of companies	Values
0.6 - 0.699	7	-0.627 x2, -0.628 x 3, -0.628, -0.631
0.7 - 0.799	2	-0.733, -0.765
0.8 - 0.899	5	-0.831, -0.839, -0.897 x 3
0.9 and over	3	-0.915, -1.601, -2.414

Applying the lowest range maximum and minimum values to our 2022/23 water households, as per Ofwat's methodology, would derive a range of penalties between £1.20m and £1.6m. This is lower than the rate of £1.7m per % that Ofwat asked us to apply at IAP.

Only three companies have rates above the Ofwat lower bound rate of -£0.897, as shown in the graph below.



Ofwat has allowed collars on performance for five companies, Affinity Water, Bristol Water, South West Water, Thames Water and Wessex Water, as shown below.

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		2020-21	2021-22	2022-23	2023-24	2024-25	£m	£/HH
AFW	PC	1.9	1.9	1.9	1.9	1.9		
	Collar	4.3	4.3	4.3	4.3	4.3		
	Max Penalty	-3.139	-3.139	-3.139	-3.139	-3.139	-£15.70	-£10.98
BRL	PC	1.5	1.5	1.5	1.5	1.5		
	Collar	3	3	3	3	3		
	Max Penalty	-0.572	-0.572	-0.572	-0.572	-0.572	-£2.86	-£5.50
SWB*	PC	1.04	1.04	1.04	1.04	1.04		
	Collar	1.6	1.6	1.6	1.6	1.6		
	Max Penalty	-0.885	-0.885	-0.885	-0.885	-0.885	-£4.42	-£4.48
WSX	PC	2.34	2.34	2.34	2.34	2.34		
	Collar	4.68	4.68	4.68	4.68	4.68		
	Max Penalty	-0.861	-0.861	-0.861	-0.861	-0.861	-£4.31	-£7.34
TMS	PC	3.51	3.22	2.92	2.63	2.34		
	Collar 1	3.51	3.22	2.92	2.63	2.34		
	Collar 2	3.79	3.79	3.79	3.79	3.79		
	Max Penalty	-2.489	-5.068	-7.735	-10.314	-12.892	-£38.50	-£10.45

Unplanned Outage is a common measure, therefore it is expected that a common approach should be applied across companies. Ofwat has not been consistent in the application of the 'lower acceptable boundary'.

We have revised our proposal taking into consideration our previous submissions, Ofwat's Technical Appendix 1, our own Draft Determination and those across the industry.

We propose to set an underperformance payment aligned with other companies across the industry. We will apply a value of -£0.628 /HH/% which is the most used underperformance penalty rate. This equates to a penalty rate of -£1.204m per %.

We propose to set a new collar on underperformance aligned to the range of the value of £/HH/% shown across the table above. The new collar is set at 6.5% across the AMP. This collar provides an increasing level of customer protection over the AMP for company underperformance.

As shown in the table below, the P10 performance scenario (collar of 6.5% across the AMP) would mean we incurred £12.91 million of penalty over the AMP. This equates to approximately 10.5% of all potential water penalties, excluding the enhancement cases.

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NES	PC	6.37	5.36	4.36	3.35	2.34		
	Collar	6.5	6.5	6.5	6.5	6.5		
	Max Penalty	-£0.157m	-£1.373m	-£2.577m	-£3.794m	-£5.010m	-£12.91	-£6.73