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

Representation reference: **Accounting for Past Delivery P1**

Representation title: **SIM**

Summary of issue

The proposed calculation of the SIM reward is not in line with what was expected. It represents a material change from how things were done previously and from how things will operate under C-MeX.

Change requested

Revert to a calculation similar to PR14, where if you are 1 standard deviation over the mean you receive the full reward of 6% of retail revenues, with a linearly increasing reward up to that level. We provide our view of these calculations based on the 4 years of data we have as an appendix to this representation.

Rationale (including any new evidence)

In your final methodology for PR14 you stated that:

> We proposed that SIM scores for 2015-20 should be calculated using data from household customers only, and that we would apply financial incentives to household retail prices in a way that delivers a similar financial outcome to the current SIM.

The current proposal represents a material change in the overall quantum of reward / penalty which is at odds with this statement.

At PR14 the net SIM adjustment was -£79.3m @12-13 prices, or £89.1 @2017-18 prices. The proposed adjustment of -£128.2 represents a step change in the overall financial outcome, the overall penalty being 43% higher.

At PR14 each company that performed above one standard deviation above the mean received the full reward and you then applied lesser rewards gradually for companies that did not achieve more than one standard deviation. At PR19 you are proposing that only the best performing water company receives the fill reward and you graduate any rewards from that point.

The approach we propose in our appendix mimics that of PR14, if the average SIM score is greater than 1 standard deviation from the mean then the company earns 6% of household retail revenues, otherwise we extrapolate linearly between the mean and the 1 standard deviation over it, rounding down to the nearest 0.1%. We treat the penalty similarly, with

mean less two standard deviations reflecting a penalty of 12% of retail revenues. This approach results in an overall adjustment of a more similar magnitude (-£73.7m or 16% less) to that at PR14.

We set out these calculations of the SIM reward / penalty in our appendix to this representation.

Why the change is in customers' interests

This ensures a strong incentive for companies to continuously improve customer service.

Under the current proposal if you are a significant way off the industry leader the incentive to continue to improve is reduced, by opening up the maximum level of reward to multiple companies this retains this incentive.

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

See the appendix to this document.