

# Appendix 8

## Governance and Assurance Reports

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# Governance and Assurance Report

## 8.1 Black and Veatch Final Report

### Technical Assuror's Statement on Hafren Dyfrdwy's PR19 Business Plan

To support its own internal assurance and governance processes, Hafren Dyfrdwy has appointed Black & Veatch to provide independent technical assurance of aspects of its Business Plan (the 'Plan') for the period 2020 – 2025. The Plan is due to be submitted to Ofwat early in September 2018.

The Black & Veatch team consists of senior professional staff with wide experience of the water industry and its regulation and is led by Stephen Bentley, Technical Information Assuror for the former Dee Valley Water and previously Reporter for another UK water and sewerage company.

The team has reviewed, challenged and provided assurance on aspects of the Plan chosen by the company, which the company assessed as being medium and high risk. The team's role was to provide third-line assurance to validate Plan proposals and data tables, to support first- and second-line assurance carried out by the company itself, as part of the company's assurance framework.

Checks have been carried out by reference to company documentation and data, through interviews with the relevant company staff and with unrestricted access to data in the company's data systems. Full cooperation was shown. Detailed reports have been prepared on each of the areas listed below and Mr Bentley has attended the company's Disclosure Committee and Audit Committee to provide updates on the findings of assurance.

The work carried out and our findings are given below.

### Work Carried Out

#### 1. Review of proposed bespoke performance commitments for the May 2018 Ofwat submission

- Reviewed and challenged the process for defining bespoke performance commitments
- Checked that the process used was consistent with the Ofwat methodology
- Checked that customers had been consulted and their views taken into account
- Checked that proposed performance commitments were justified, measurable and supported by customers
- Checked that internal governance had been carried out

#### 2. Review of the company-specific methodology used for:

Affordability and vulnerability

Direct procurement

The approach to bad debt

Resilience

#### Compliance with statutory obligations

- Checked that the company followed a thorough and rational process to develop methodologies
- Checked that customers and other stakeholders had been consulted
- Checked that methodologies were appropriate to the scale and nature of the company's activities and were consistent with Ofwat methodologies
- Checked the integration of statutory and legislative obligations into the company's Licence to Operate framework

#### 3. Review of the setting of performance commitment targets and financial incentives reviewed and challenged:

- The process for defining regulatory expectations and estimating likely AMP7 upper quartile performance
- The assessment of historical performance and expectations for improvement
- Industry comparisons
- The process for canvassing customer views and taking them into account in the Plan
- Cost benefit analysis
- Checked that internal governance had been carried out

#### 4. Review of proposed cost adjustment claims

- Reviewed and challenged the process used to identify potential cost adjustment claims, including the degree of support from customers and other stakeholders and compliance with the Ofwat methodology
- Challenged the justification of each proposed claim
- Checked that costings were robust
- Checked that the cost and scope of each claim had been optimised for maximum customer benefit and was affordable
- Checked that internal governance had been carried out

#### 5. Checks on selected data tables

- Reviewed and challenged the process used to prepare data for the tables
- Checked that company procedures existed and were used
- Checked how numbers had been estimated
- Checked that numbers were consistent with 3 and 4 above
- Carried out sense-checks on the numbers reported, confirming that numbers were of the right order, showed a realistic trend and did not contain unexplained oddities or step-changes, and challenged zero entries
- We did not carry out detailed audit of the numbers given
- Checked that internal governance had been carried out

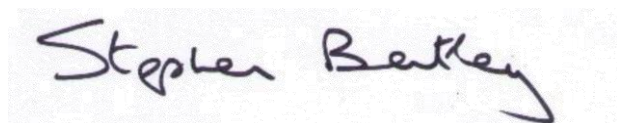
## Findings

We have noted the Board Statement included in the Executive Summary of the Business Plan. Our checks support this statement to the extent described below.

From our assurance work, we concluded that:

- The company followed a thorough and rational process to develop its methodologies and approaches to affordability, customer vulnerability, direct procurement, bad debt, resilience and meeting statutory and licence obligations. The process included consultation with customer bodies and other stakeholders. The approaches were appropriate to the scale and nature of the company's operations and geographic area and were consistent with Ofwat methodologies.
- The company followed a thorough and rational process to define proposed bespoke PR19 Performance Commitments (PCs), consistent with the Ofwat methodology, and to set target levels for bespoke and compulsory PCs taking into account regulatory expectations, historical performance, industry comparative performance, customer and CCG views and cost-benefit analysis.
- In defining PCs, the company took into account customer and CCG views on the relative priority of PCs and applied the most stretching targets in areas which customers confirmed as their highest priorities.
- The method used for the calculation of financial Outcome Delivery Incentives (ODIs) complied with Ofwat's methodology. The majority of PCs had financial penalties and rewards. The size of penalties and incentives was based as far as possible on customer willingness-to-pay. Most financial ODIs were proposed to apply in-period, to provide an incentive to make steady progress.
- An effective process was used to identify potential challenges justifying Cost Adjustment Claims (CACs) which met Ofwat criteria and were material. These were challenged internally, by customers and by other stakeholders. The proposed CACs were justified, supported by customers and had been robustly costed.
- Costs had been assessed for each CAC at an appropriate level of detail, based on similar work carried out by the company or estimates provided by others, and were as robust as possible at the planning stage. A proper assessment of options had been carried out and steps taken to optimise work scope and cost.
- The company had governance arrangements in place for the preparation of all aspects of the Plan. These included written methodologies for the preparation of business cases and written procedures for the completion of data tables, internal first- and second-line assurance, and the third-line assurance provided by our work. A risk-based approach was used to select the Plan areas covered by third-line assurance. During the development of the Plan, we reported from time-to-time to the company's Disclosure Committee and Audit Committee and, at the stage of final approval, to the Board.
- During our work, for the areas covered by our third-line assurance checks, we have not uncovered any deficiency in the methodologies used, the proposals made, or the completion of the required data tables, which we consider material.

Yours faithfully,

A handwritten signature in black ink that reads "Stephen Bentley". The signature is written in a cursive, slightly slanted style.

Stephen Bentley - Technical Information Assuror  
Black & Veatch

## 8.2 Internal Audit Future Reporting Processes - Board Statement

### Background and scope

As part of the PR19 submission, Ofwat set out in its final methodology that *“they expect a company’s full Board to take collective responsibility for assuring its business plan. To provide confidence in its plan, a company’s full Board needs to provide us with a statement, in its own words, of why it considers all the elements (including supporting data) add up to a business plan that is high quality and deliverable.”*

The Hafren Dyfrdwy Board has composed a statement which includes the required elements as set out by Ofwat. Each element of the statement has evidence to support it including reports from external assurance providers, minutes from STEC and Board meetings etc.

Internal Audit were asked to review evidence for the following statements:

*“The business plan will deliver, and the Board will monitor delivery of, its outcomes and performance commitments*

*The company's proposed approach to reporting on its performance commitments, ODIs and the projections of outcomes is robust”*

### Detailed observations

As evidence to support the above statements, Internal Audit have reviewed the relevant sections of the Securing Trust, Confidence and Assurance chapter and supporting appendix of the business plan along with the report provided by Jacobs and Black & Veatch on their review of legal and statutory obligations. We have also conducted meetings with the Head of Compliance and the Compliance Manager.

Hafren Dyfrdwy are proposing to continue with their current process of regular reporting through STEC and Board and half and full year assurance reporting of Performance Commitments and ODIs through Disclosure Committee and Audit Committee. The process will continue to follow the three lines of assurance approach with Black & Veatch carrying out technical assurance in this area until 2019 and Jacobs carrying out third line technical assurance until 2025. Shadow performance commitments are already reported in this way.

Hafren Dyfrdwy’s approach to governance includes the Board, STEC and Audit Committee. All of which are consulted and give approval on major regulatory submissions and this process is to be continued going forwards. The Customer Challenge Group are also a regular consultee and have been involved in the PR19 planning process and will continue to be consulted as part of future submissions.

Internal Audit recommends that an Internal Audit review of the reporting process for the PCs and ODIs is included in the 19/20 plan.

## Annex A - List of data tables and assurance provide

PR14 Reconciliation Tables (x13) Internal Audit	Black and Veatch (x28)	Financial Model (x32) Internal Audit	Zero tables (x15) Internal Audit	Other (x18) Internal Audit
<p>App5 App6 App9 App23 App25 App27 App31 WS13 WS15 WWS13 WWS15 R9 R10</p>	<p>WWS3      WS3 WWS4      WS4 WWn3      Wr1 WWn4      Wn1 Bio1        Wn2 Bio2        App2 Bio3        WS18 WWS2       WWS18 WWS2a      App1 Wr6         App4 WS12       App28 WS12a      WS2 Wn6         WS2a Wr8 WWn8</p>	<p>App7        App29 App8        App32 App10       Wn3 App11       Wn4 App11a      Wn5 App12       Wr3 App12a      Wr4 App13       Wr5 App14       WWn5 App15       WWn6 App15a      WWn7 App16       Bio4 App17       Bio5 App18       Bio6 App19       R7 App26       R8</p>	<p>R5 R6 WWS12 App33 App3 App21 WS10 WS17 WWS10 WWn2 Bio7 R2 Wr7 WS1a WWS1a</p>	<p>App20      Wr2 App22      WWS1 App24      WWS5 App24a     WWS7 WS1        WWS8 WS5        WWn1 WS7        R1* WS8        R3 App30 R4</p>