

Hafren Dyfrdwy Cyfyngedig **Assurance Summary 2018/19**

1. About this document

The quality of the regulatory information we publish is important because it helps to give our customers and other stakeholders confidence that we're being open and honest about where we're delivering on our commitments to them, but also where we're not. To help to secure this confidence, we use assurance to thoroughly test information we publish in a manner that is independent and verifiable. Our Board oversees this process through our robust governance and assurance framework.

Ofwat's Company Monitoring Framework

On an annual basis, Ofwat assesses the level of trust it has in the information we produce and publish against three categories:

- **Self-assured** - indicating a high level of trust. Companies who are self-assured have greater levels of freedom to dictate their own assurance plans for the reporting year.
- **Targeted** – indicating a sufficient level of trust, however Ofwat dictates some areas that must receive assurance. Targeted companies must also publish, and consult on, an annual statement of risks, strengths and weaknesses and an accompanying assurance plan.
- **Prescribed** – indicating that Ofwat has concerns with the information provided and dictates what information should be assured by the company as well as the requirement to publish an annual statement of risks, strengths and weaknesses and an accompanying assurance plan.

This process is known as the Company Monitoring Framework ('CMF'). Under the CMF, we publish assurance and compliance documents throughout the year as shown in Fig: 1 below. By doing this, we make sure that our regulatory publications can be trusted by our customers and our stakeholders.

What is assurance?

We perform 'assurance' to check that the information we provide is robust, accurate and complete. Examples of assurance may include checking that a spreadsheet has no formula errors, that a customer call has been recorded accurately on our systems or consulting with our customer challenge group on our plans for vulnerable customers. You can read more about the levels of assurance we apply in section 3.0.

What is the Company Monitoring Framework?

Ofwat's company monitoring framework (published in June 2015) set out its expectations for how it will oversee information that we, and the 16 other largest water companies, provide to our customers. For more information please visit Ofwat's website - ofwat.gov.uk

Understanding your views

In November 2018, we published our Statement of risks, strengths and weaknesses and our draft Assurance plan for consultation. In addition to publishing this document on our website, we proactively contacted our key stakeholders to let them know we wanted to hear their views. We considered the feedback received and wider industry trends to produce our final Assurance plan published in February 2019. This document summarises the outcome of the assurance we have undertaken for the 2018/19 regulatory reporting year and considers requirements for 2019/20 onwards. Its main focus is the data assurance undertaken for our Annual Performance Report ('APR'), but also considers the outcome of our assurance activities more broadly.

This document contains the following information:

- A glossary to ensure you can understand any abbreviations used in this document.
- Information on our governance and assurance framework, which covers our Board arrangements and the different levels of assurance we apply.
- An overview of our internal compliance assessment framework – licence to operate – which helps us determine our greatest areas of risk.
- Details of the customer and stakeholder engagement we undertook to produce our final Assurance plan.
- Details and outcomes of the assurance undertaken for our APR.

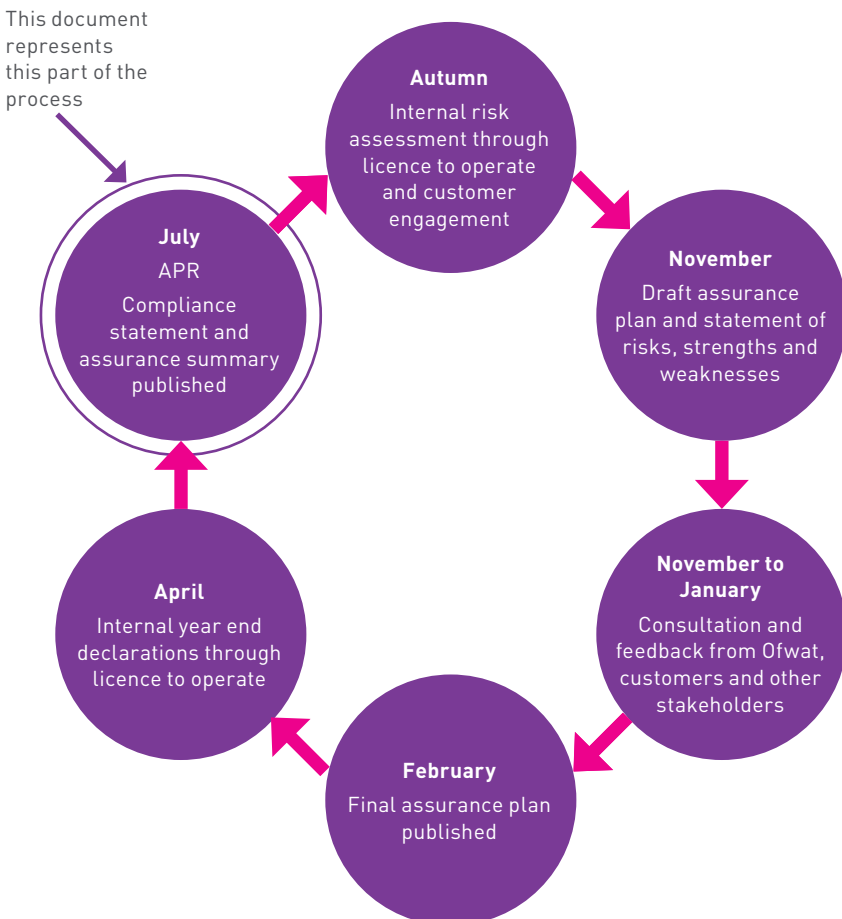
- Outcomes of assurance on other areas that we committed to reviewing in our final Assurance plan.

We recommend that this document is read in conjunction with our Board, governance and compliance section on page 12 of the APR, which includes our formal regulatory statements and our departures from compliance for this regulatory reporting year.

Changes this year

In July 2018, we aligned the boundaries of the two largest regulated water companies within the Severn Trent Plc group – Severn Trent Water and Dee Valley Water – to match the boundary between England and Wales. Severn Trent Water now serves customers in England, while our new company - Hafren Dyfrdwy - serves customers in Wales. This realignment has necessitated a change in how we report performance data and how we operate to ensure we fairly protect the interests of customers of both companies. Our assurance of the APR reflects this change as two technical auditors reviewed our data during this report year. Alongside our established auditor Black & Veatch - for the Wrexham area - Jacobs also reviewed customer Outcome Delivery Incentive ('ODI') data in respect of the Powys area, which reports against legacy Severn Trent Water performance commitments ('PCs').

Fig 1: The Company Monitoring Framework cycle



2. Glossary

To help to explain all the terms in this document, we've included the table below.

| Term | Definition |
|------------------------------|---|
| AIM | Abstraction Incentive Mechanism - AIM encourages water companies to reduce the environmental impact of abstracting water at environmentally sensitive sites when water is scarce. |
| AMP | Asset Management Period – this refers to Ofwat's 5 year planning period. For example, we are currently in AMP6. AMP7 will start in 2020. |
| APR | Annual Performance Report – includes information about whether we've achieved our PCs in a given year, and our financial performance – based on the accounting conventions in Ofwat's regulatory accounting guidelines. |
| ARA | Annual Report and Accounts – includes our annual financial statements based on International Financial Reporting Standards. |
| Assurance | A process that challenges the validity of our data and methodology. |
| CCG | Our Customer Challenge Group ('CCG'); includes independent experts, CCWater, our regulators including Natural Resources Wales and regional stakeholders. |
| CCWater | Consumer Council for Water – the statutory consumer representative body for the water industry. |
| Group compliance & assurance | Our internal team that monitors compliance with our statutory and regulatory duties in our appointed business. |
| ERM | Enterprise Risk Management – our system of identifying and managing risks within Severn Trent Plc. |
| HD | Hafren Dyfrdwy Cyfyngedig – the regulated water company within Severn Trent Plc whose area of appointment covers North-East and mid-Wales. |
| Internal Audit | Reporting directly to the Severn Trent Plc Audit Committee, the Internal Audit team provides independent assessment of the effectiveness of our processes, controls and risk mitigation strategies. |
| K Factor | K Factor is the price limit that companies can increase or decrease prices charged to customers. This is reviewed and determined by Ofwat. |
| MOSL | The market operator for England's competitive non-household market. A small number of our large user customers in Wales are eligible to change their retailer in the competitive market. |
| NAV | New appointments and variations - Companies which provide a water and/or waste water to customers in an area which was previously provided by an incumbent provider. |
| ODI | Outcome Delivery Incentives are individual performance measures, which have a financial reward or penalty attached to them. They are a sub component of our PCs (below). |
| Ofwat | The Water Services Regulation Authority – the statutory economic regulator for the water industry. |
| Performance Commitment | The level of performance we've committed to deliver either annually or during the five-year period covered by business plans. |
| PDT | Process Description Template – Internal documents which describe the process by which data is produced for many of regulatory publications. These documents include step by step guides for obtaining data from company systems, controls, risks and assumptions. |
| PR19 | Price Review 2019 - Every five years we publish our proposals for the next five year period. Ofwat reviews this and decides whether our plans are suitable in a determination process. |
| RACI | Responsible, Accountable, Consulted, Informed – a RACI details who is responsible for managing a duty or obligation, who is accountable and who should be consulted or informed of any changes. |
| RAG | Regulatory Accounting Guidelines – Every year Ofwat publishes guidance on how companies should complete their financial and non-financial tables for the ARA and APR. |
| RoRE | Return on Regulatory Equity – an indicator of the return generated by our regulated business. |
| SLA | Service Level Agreement – we have timescales and minimum levels of performance in place both internally and with our contractors. |
| STW/SVT | Severn Trent Water Limited – the regulated water company within Severn Trent Plc whose area of appointment covers the Midlands. SVE is often used by our auditors to denote when the subject matter concerns STW post boundary realignment. |
| ST Plc | Severn Trent Plc – the parent company and ultimate controller of Severn Trent Water and Hafren Dyfrdwy. |
| Third Party Auditor | An independent audit company or organisation that performs audit or assurance services. |

3. Our governance and assurance framework

Assurance alone isn't infallible, and we believe that ensuring the balanced reporting that our customers and stakeholders can have confidence in, starts with the values of our company, our people and our behaviours.

Our Board is responsible for establishing Hafren Dyfrdwy's purpose, vision and strategy, and satisfying itself that its culture is aligned. Our Code of conduct, 'Doing the Right Thing', sets out clearly defined values and standards of behaviour that we expect from everyone who works for, and with, Hafren Dyfrdwy. These values embody the principles by which the Company operates, and provide a consistent framework for responsible business practices. The supporting policies codify how to identify and deal with suspected wrongdoing, fraud or malpractice; how to ensure that the highest standards of safety are maintained; and how to apply good ethics and sound judgment.

The Severn Trent Plc Board monitors compliance with the Code of conduct through consideration of mandatory training completion rates by all subsidiary companies including Hafren Dyfrdwy. Additional detail can be found in the Severn Trent Plc ARA on the Severn Trent Plc website.

Every day our people have to make choices about what they do and how they do it. Most of the time it is clear what the right thing to do is, whether it is about doing what's safe, doing the right thing for customers, doing what is right ethically and indeed what is right legally. But sometimes it's not so clear, so 'Doing the Right Thing', details the five values we work by, to help guide our people through those grey areas when there are no hard rules in place:

1. We put our customers first.
2. We are passionate about what we do.
3. We act with integrity.
4. We protect our environment.
5. We're inspired to create an awesome company.

These values apply to how we report information just as much as any other area of what we do.

A continuously evolving assurance approach

The assurance processes we use come from best practice identified across many organisations and industries ensuring that managers, senior managers and Directors are responsible for delivering high quality data through robust processes and methodologies in particular, we have benefited from becoming a member of the Severn Trent Group who have shared its learnings and assurance processes. For example, we introduced 'licence to operate' to Hafren Dyfrdwy in the last regulatory reporting year. Licence to operate has been operating in Severn Trent for over four years and ensures we understand our compliance with all of our statutory and regulatory obligations. More information on licence to operate can be found in section 4.

Our framework is underpinned by four main principles (as shown in Fig 2 below) which, while providing consistency and clarity for our people, allow the flexibility for our assurance processes to build and evolve with our Company and the environment we operate in. For example:

- A risk based approach to assurance i.e. targeting areas of greatest importance with three lines of assurance on the areas that matter most or are high risk. This approach ensures that our assurance programme maintains value for money while also giving confidence to our customers and stakeholders that the information they value is trustworthy.
- Implementing a twice yearly assurance process for the areas of greatest risk to ensure that any potential areas of non-compliance are noted at the mid-year point. This gives us the opportunity to rectify the issues before year end.
- Standardised process description templates to document each of our processes, providing us with an auditable methodology for producing our data.

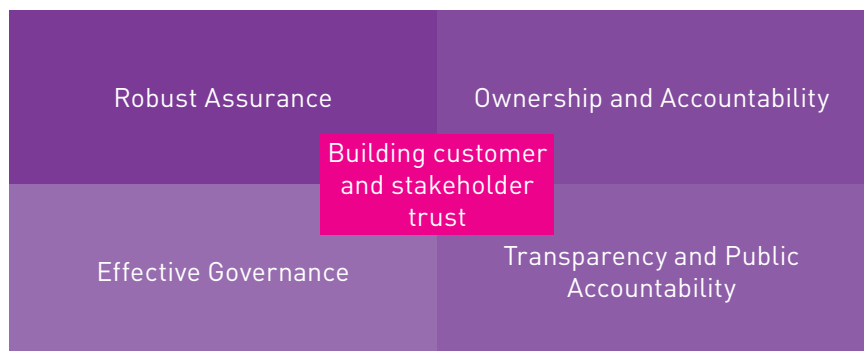


Fig 2: Our assurance principles

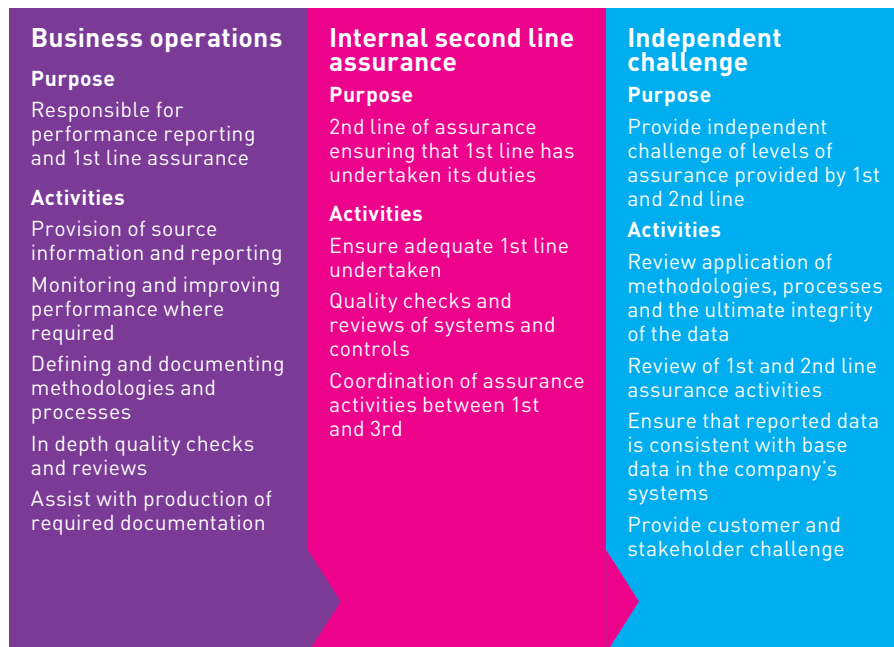
3.1 Robust assurance

To ensure we're applying an effective programme of assurance, while balancing value for money, we operate a three lines of assurance model. We target this model using a risk based approach so areas that we know are of prime importance to customers or may have a significant financial value or operational impact receive the full three lines of assurance while other areas may be targeted with first or second line only. This approach ensures our spending on assurance is proportionate and aligns to what our customers value most. Fig 3 below details the three lines and the typical activities that each level is responsible for.

First line activities are embedded within the teams that are responsible for reporting the performance so that colleagues with the right expertise are conducting in depth quality checks at the time the data is produced.

Second line activities are then conducted by a separate team that does not report into the same senior manager as the first line to ensure a level of independent checking is conducted. For elements of our APR, second line functions are embedded within the same directorate as the performance reporting. This ensures that we maintain a strong level of expertise and understanding of the source data.

Fig 3: Our Levels of Assurance



Third line activities are conducted by a number of different providers depending on the specialisation required. Generally the expertise can be divided into the following categories:

- **Engineering/technical** - where assurance requires an expert engineering / water industry technical background.
- **Regulatory** - where challenge is required around the methodology used and assumptions against our regulatory requirements.
- **Data integrity and consistency** – understanding the flow of data from source through to our final publications ensuring no data transposition errors are made.
- **Financial** - used for areas requiring specific financial expertise, such as pensions.
- **Model integrity** - where a complex financial model is used and requires specialist external expertise to test and challenge.

We use a combination of assurance providers for third line activity. The majority of our assurance is provided by the following:

- **Black & Veatch** – typically review non-financial operational performance processes and data.
- **Jacobs** – reviewing cost allocation activities, financial reporting processes and non-financial operational performance processes and data in respect of Powys.
- **Deloitte** – our financial data auditor.
- **Internal Audit** – internal control reviews, data audits and other ad-hoc audits.

3.2 Ownership and accountability

We have clear lines of ownership for both the delivery of performance, and the accuracy of the data provided through our ‘licence to operate’ process, which every year assigns ownership of all of our statutory and legal obligations in our appointed business to managers, senior managers and Directors. These managers are responsible for ensuring compliance with our duties and raising potential risks or issues of non-compliance. Any areas that are noted as non-compliant are disclosed by the Board as departures in its annual Risk and compliance statement following review, scrutiny and remedial action by our senior leadership team and our Severn Trent Plc’s Disclosure and Audit Committees.

Section 4 includes more information on our licence to operate process.

3.3 Effective governance

Hafren Dyfrdwy was created on 1 July 2018 and has its own Board, which is supported by existing Severn Trent Plc governance arrangements. To ensure a level of independence between Severn Trent Plc and Hafren Dyfrdwy’s Board members, in April 2018 we appointed three new Non-Executive Directors to specifically look at our Welsh business and provide independent challenge. We continue to adhere to the principles set out in Ofwat’s ‘updated assessment of monopoly water companies’ governance arrangements’ published in June 2015. Additional challenge is provided by the CCG who challenge us to evidence how the voice of the customer has been considered in our decision making processes.

The Hafren Dyfrdwy Board is supported by the Severn Trent Plc governance framework, which is

set out in Fig 4. The Governance Framework comprises the Board, Executive Committee and their respective Committees.

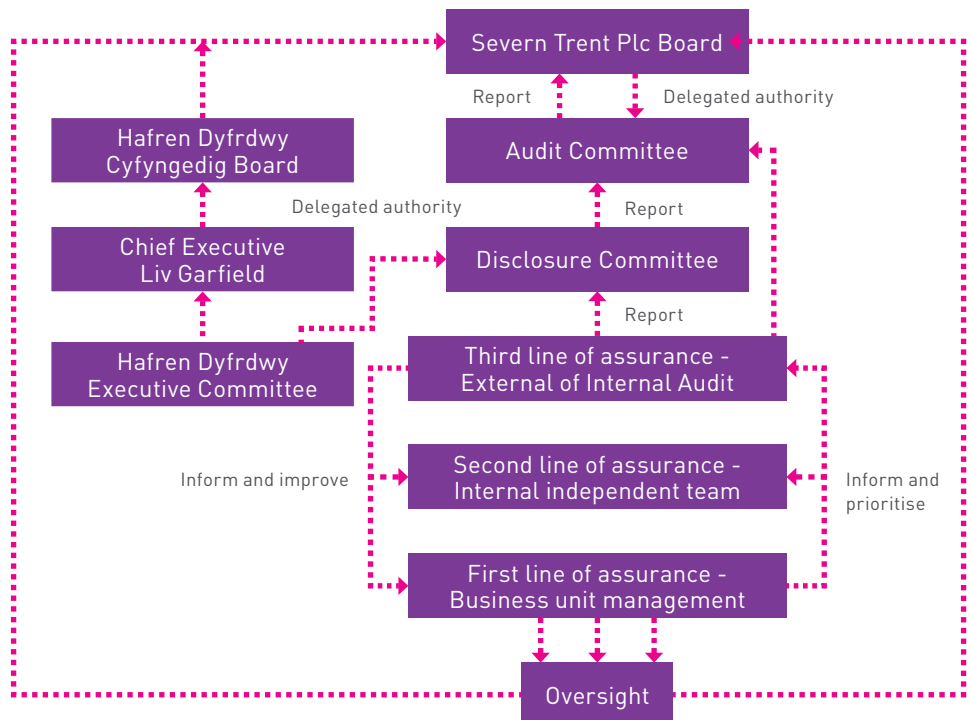
In line with the 2016 UK Corporate Governance Code, the Board delegates certain roles and responsibilities to its various Committees. The Committees assist the Board by fulfilling its roles and responsibilities, focusing on its specific activities, reporting to the Board on decisions and actions taken, and making any necessary recommendations to the Board in line with its Terms of Reference. The Severn Trent Plc Board regularly reviews the Terms of Reference of each Committee, with the exception of the Hafren Dyfrdwy Nominations Committee (which was reviewed by the Hafren Dyfrdwy Board during the year). The individual Committee Terms of Reference are available on the Severn Trent Plc website. The Governance Framework is also subject to periodic review to ensure that it remains appropriate.

The Disclosure Committee oversees the Group’s reporting obligations under the Companies Act 2006, the UK Corporate Governance Code, the UKLA Listing, Rules, Disclosure Guidance and Transparency Rules and the Company’s annual and continuing regulatory reporting requirements, considering the materiality, accuracy, reliability and timeliness of information disclosed and assessment of assurance received.

To support our Governance Framework, we have a well-established, rigorous and robust assurance and performance reporting framework. Our assurance plan for the financial year, 2018/19, continued the high standard processes we developed and implemented in prior years, for reporting our PCs in our ARA and APR.

Fig 4 shows how our assurance framework interacts with our governance arrangements to ensure that all levels of the business have oversight of our assurance processes.

Fig 4: Our governance arrangements



We operate an ERM system for identifying, assessing and managing our significant risks – including risks to our corporate objectives, core processes, key dependencies, stakeholder expectations and legal and regulatory obligations. A number of risk management systems feed our ERM process including water quality risks, and health and safety. Significant risks feed into our Company risk profile and are reported to our Executive Committee and to our Audit Committee and Board at least every half year.

3.4 Transparency and public accountability

As a public service we want to be transparent about how we balance the needs of our customers, our strategic plans as a business and a fair return for our investors. We believe we are prudent in how we manage financial risk and even-handed in the way we share the returns from our outperformance with customers and shareholders; we pay our taxes in full and on time; we pay Executive salaries that are reasonable and sustainable and linked to the delivery of outcomes to customers; we avoid complex offshore financial vehicles; we publicly report on our performance, and hold ourselves to account where we do not meet our commitments.

Each year we evolve and update our reporting to make sure that it not only complies with our regulatory obligations but also responds to our customers' and stakeholders' feedback. We have simplified the customer version of our APR and included our comparative performance against other companies to make our overall performance more transparent for our customers. We also publish our company structure on our website, which shows how the companies including Hafren Dyfrdwy and other associated companies are connected under the Severn Trent umbrella. In addition we already include details on Executive pay and how Severn Trent Plc pays dividend payments in the Severn Trent Plc ARA, and have improved the way we display this information in our APR.

4. Our internal assessment – licence to operate

We use the wealth of expertise within the business to assess all of our statutory and regulatory obligations relating to provision of water and waste water. We call this assessment ‘licence to operate’ and it has been operating in Hafren Dyfrdwy, and previously Dee Valley Water, for two years.

4.1 The process

Since joining the Severn Trent group we implemented, and continued to embed, the licence to operate process within Hafren Dyfrdwy. We have continuously reviewed the process to improve it by using tools such as SharePoint to track the assessments and approvals from all levels of management. We monitor over 400 obligations including those specific to a business now operating wholly in Wales. Licence to operate is a two stage process that operates through the mid and year-end of the annual regulatory cycle. We describe the process in more detail in our Statement of risks, strengths and weaknesses and final Assurance plan, which can be found on our website.

4.1.2 Year-end declarations

Prior to publication of our annual regulatory reporting we ask our responsible managers to declare whether they have been compliant or non-compliant with their obligations. If they have been non-compliant, we ask them to complete a ‘departures’ form, which details what issue has occurred during the reporting year, the action taken, and what will be done to prevent it in future.

All departures are then reviewed by the accountable senior manager and Director who will assess the level of materiality. Some departures, while representing an instance of non-compliance with process may not be material or, for example, it may be within the stated confidence of the measure.

All departure assessments are tracked on the departures form to ensure that we maintain a visible audit trail of all areas of potential non-compliance.

Departures that are assessed to have a material impact are included in our Board annual Risk and Compliance Statement, which is published in July within our APR. This document is reviewed and scrutinised by the Severn Trent Plc Disclosure Committee and Audit Committee before it is endorsed by our Board prior to publication, ensuring that all levels of the business are made aware of any significant risks or issues.

4.2 2018/19 risk assessment outcome

In this year’s assessment, the following areas were noted as either a high or medium-high risk, or our internal group compliance and assurance team has decided to include the area. This may include areas that may not necessarily score high on our internal risk assessment at present, but that we know are subject to, or could be subject to, regulatory change or emphasis:

- **Performance commitments** – in recognition of the potential impact our PCs have on our customers, the environment and market confidence, our customer ODIs continue to feature in our assurance plans as part of the APR. Customer ODIs remain a high priority for our customers and other stakeholders because:

- i) our PCs reflect the areas of service that our customers have told us are most important to them – we have an obligation to accurately report if we’re meeting our commitments; and
- ii) our investors can make decisions as to whether to invest in our company based on the

performance data we provide – we have a duty to all interested parties to accurately report how we are performing.

- **Reservoir resilience** – our highest risk in our ERM risk management system and highlighted in our PR19 plan. There are some inherent risks with our reservoirs. In the short term, we have carried out detailed risk assessments and as a result we have increased the inspection regime carried out by trained reservoir engineers and improved the emergency plans in place. However, to ensure we address this longer term we have carried out additional inspections and developed a business case that sets out the required interventions to ensure these assets remain compliant with all relevant legislation and to ensure they are safe and serviceable. This risk is monitored through our ERM and licence to operate systems.

- **Charges** – We are conscious that this may be a sensitive area for our customers in part due to the recent creation of Hafren Dyfrdwy. We want to be transparent with customers about how charges are calculated and be clear that any change in price is not a direct result of this. We will engage with CCWater and our CCG to help alleviate customer concerns.

- **Water Quality obligations** – Due to existing processes that are in place, we believe we are compliant with our obligations under the Water Quality (Water Supply) Regulations and the Water Industry Act. All of our managers are competency checked and trained, whether they are new or existing in role as part of a three year programme, however, due to staff changes in the teams that carry out these

duties we want to ensure that all of our managers have an up-to-date understanding of what their responsibilities are. Our regulatory performance team are conducting an internal review to ensure an appropriate RACI is in place.

- **Licence condition L (Asset management)** – Following creation of Hafren Dyfrdwy, we want to ensure that we have confidence in our programme to maintain our underground assets. Following integration of the two companies we have merged our programmes of work to ensure visibility of outputs and control frameworks.
- **Boundary realignment** – Following the creation of Hafren Dyfrdwy on 1 July 2018, our regulatory reporting has now been split according to the new boundaries specified in the licence. We have asked all lines of assurance (including third line) to consider how the boundary realignment has impacted regulatory reporting and whether performance has been allocated to the correct entity.
- **Cost allocation** – Cost allocation activities within our finance team are part of our established third line assurance annual processes, the following factors have meant that we wanted to place additional emphasis on this area for 2018/19:
 - i) Boundary realignment and the creation of Hafren Dyfrdwy meaning that we wanted to ensure costs are allocated correctly between our businesses; and
 - ii) Ofwat's licence simplification consultation that embedded RAG 5.07 into our licence as of January 2019.
- **Drought plan** - The Water Act (2003) made it a statutory requirement for water companies to produce and maintain a drought plan. We update these plans every five years. Our Drought plan sets out how we will manage our resources and supply system in dry years, to maintain our service to our customers.
- **Governance of regulatory and statutory duties** – As noted above, we want to ensure we can demonstrate that we have good governance arrangements in place in order for us to meet our regulatory and statutory obligations. During PR19, Black & Veatch reviewed our governance arrangements and our processes for meeting these obligations to ensure these were appropriate.
- **K factor and ODI model**– Ofwat noted in its 'in period ODI draft determination' that it had found a small number of errors and inconsistencies in the spreadsheets we provided, which were used to calculate our reward / penalty for performance on our ODIs. We acknowledged that these errors had been missed by our two lines of assurance. This year this submission was superseded by the PR19 process, which had its own assurance processes as described below in section 7.
- **PR19 future reporting** – As part of our PR19 business plan we proposed a suite of PCs for the next five year period (2020-2025), a number of which require new reporting processes to be developed. As such, we want to ensure we can report our data accurately before the next AMP starts. Last year we asked our regulatory technical auditor to review our plans in advance to check that we had suitable action plans in place to address any areas where we would potentially

be unable to report the new measures. This year we're using the same process that we use for our PC data in 'shadow' i.e. half year and full year audits to ensure we get a snapshot of risk areas prior to year-end.

- **Water Resource Management Plan** – Our draft Water resource management plan was published in January 2018 and was open to consultation with all our customers and other stakeholders. This year we will be publishing the final plan that requires a signed Board Assurance statement to be published alongside it. Given the complexity and strategic importance of managing our water resources, we wanted to make sure that our Statement of response and final publication was subject to third line review.

We used these areas as part of our customer engagement described in section 5 and published them as part of our November consultation document to understand whether our customers and stakeholders believed we were targeting the right areas. The outcome of assurance for these areas are covered in sections 6 and 7.

5. Customer and stakeholder engagement

To understand which areas matter most to our customers and stakeholders, we used our regular engagement methods and also bespoke research specifically designed to inform this plan. We also put this plan out for consultation in November 2018.

5.1 Customer engagement

Prior to publishing our draft Assurance plan in November we undertook customer focus groups to understand what areas mattered most to them by using the results from our internal assessment described in section 4 above. Further details on the engagement we undertook can be found in our final risk and assurance plan on our website. In summary customers largely agreed with our internal assessment and helped us to prioritise in particular our charges and PCs as areas of keen interest to them.

5.2 Stakeholder engagement

As well as listening to our customers, we wanted to take on board feedback from other stakeholders.

5.2.1 Ofwat – 2018 CMF Assessment

While Ofwat noted improvement in our position from 2017 (with no serious concerns noted in the assessment) we have remained in the 'prescribed' category. We will continue to work with our customers and stakeholders to address the themes noted in Ofwat's assessment:

1. Data Quality. Ofwat noted there were some instances where regulatory submissions (APR, PR19 and the draft WRMP) included either data that was incorrect or incomplete. For example, there were differences between our submitted excel tables and the final APR publication. To prevent this from reoccurring, we have reviewed our change control process.
2. Data commentary and explanation of variance. Another common theme was that sometimes we failed to adequately explain variances in our data or provided no commentary resulting in Ofwat requesting clarification from us through the formal query process e.g. our Accounting separation methodology did not provide enough detail around our cost allocation of water resources and raw water distribution price controls. To address both this concern and the one above, we reviewed the APR and PR19 queries we received in 2018 and made changes to our assurance process to mitigate these risks.

3. Long-term viability statement. Ofwat were concerned our long term viability statement did not include enough detail around the impacts of our principal risks. We have reviewed our disclosure in the viability statement in light of other companies in the sector with the objective of drawing on best practice whilst reflecting the particular circumstances of Hafren Dyfrdwy.

4. Meeting the requirements of IN18/07. Last year Ofwat asked all companies to provide a performance statement, setting out how the company is delivering for the stakeholders that rely on its services and how its aspirations have been shaped in the APR. While we did publish this statement within our customer summary on our website, we acknowledge that we did not include it within the APR itself. We have included this in this year's APR on page 8 .

5.2.2 Customer Challenge Group

Our Customer Challenge Group ('CCG') represents the voice of our customers following extensive engagement during the development of our business plan. While we received no specific comment from our CCG following publication of the consultation, moving forward we will look at the role the CCG will play in the next AMP to ensure we continue to hear their views.

Prior to the publication of our final APR we shared our performance with the CCG for review and comment.

5.2.3 Other stakeholders

Following publication of the consultation, we sent out notices to nearly 100 stakeholders including Natural Resources Wales, CCWater, local environmental groups and local councils to ask them for their views. While we received no direct feedback on our assurance plan for Hafren Dyfrdwy, we have incorporated wider feedback into our final assurance plan:

- Expanding the scope of licence to operate – when licence to operate was implemented, we made a decision to only cover the most material regulatory and statutory obligations, using the risk based approach as described in section 4 above. Given the amount of regulatory and legislative change that has occurred, the next AMP gives us an opportunity to review what is currently included and whether the scope should be expanded further. We will also look at potential technical solutions to ensure that the risk assessment process does not become overly burdensome.
- Customer Engagement - we are committed to engaging with our customers throughout the AMP using a range of survey types through our existing tools; Pipe Up (Qualtrics SMS Surveys), Qualtrics Research Campaign Surveys (SMS and Email based), Qualaroo (website surveys), and our quarterly customer tracker. We will continue to use customer focus groups and other bespoke survey methods on an ad-hoc basis to consult on specific issues where required. Our future goal is survey through the customer's channel of choice to help us achieve the best response rate from a broad range of people.

6. Assurance of our Annual Performance Report

In this section we explain how the data included in our APR has been assured, and the outcome of that assurance.

6.1 Governance

We have an established assurance and reporting framework, which incorporates Ofwat’s APR requirements and the RAGs. Across the business we assign accountable and responsible managers for all reporting lines in our APR. These managers review and approve the process documentation and data as part of our first line assurance and prior to third line assurance. Following third line audits, all individuals within the approval process sign off the data and commentary, culminating in the relevant Director who will approve

both the data and commentary. Subsequently the APR is reviewed by Severn Trent Plc Disclosure Committee who are accountable for ensuring that all year end publications comply with applicable disclosure requirements. The Audit Committee, who has delegated authority from our Board, then reviews to ensure the adequacy of the year end assurance process prior to our Board reviewing and approving the final submission.

In addition to these existing governance arrangements, we enhanced the process this year by creating a year end programme steering group and programme board, which was incorporated into our governance framework as set out in Fig 5 below. This gave the Boards of Hafren Dyfrdwy, and

Severn Trent Plc greater oversight of year end reporting with regular updates noting progress against key milestones and the ability to escalate key risks and issues as required.

6.2 Assurance

The APR comprises the four sections outlined by Ofwat in RAG 4.08 – Guideline for the table definitions in the Annual Performance Report:

1. Regulatory financial reporting.
2. Price review and other segmental reporting.
3. Performance summary.
4. Additional regulatory information (includes cost assessment information).

Our existing assurance framework as detailed in section 3.1 above was used for the APR i.e. a risk based approach whereby we targeted our most critical areas with our three lines of assurance model. We used a number of third line assurance providers aligned with their areas of expertise.

We summarise below the assurance undertaken and the outcome by our assurance providers. We have also included letters of assurance from our technical assurers, Jacobs and Black & Veatch on page 22 and page 23 of the APR respectively. Deloitte provide an audit opinion on the Regulatory Accounting Statements, which is set out in full on page 42.

Fig 5. Our year end governance arrangements

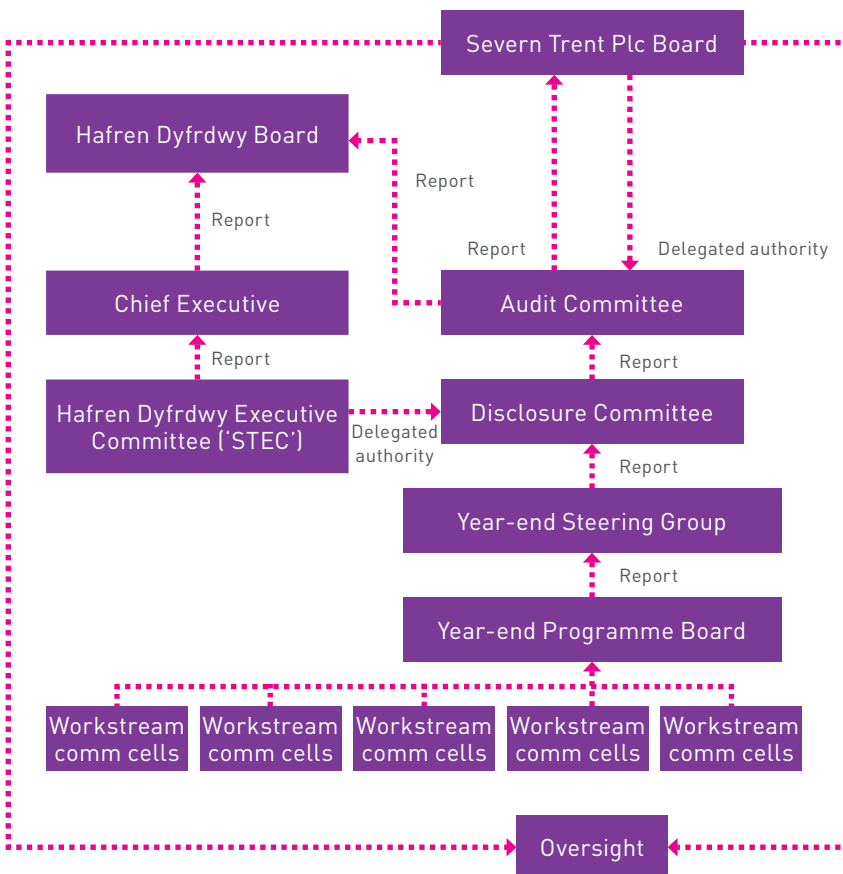


Fig 6: Sections 1-3 assurance

| Assurer | APR Section | Methodology and Process | Data |
|----------------|-----------------------------|-------------------------|------|
| Deloitte | Section 1 | ✓ | ✓ |
| | Section 2 | ✘ | ✓ |
| Jacobs | Section 1 (Financial flows) | ✓ | ✘ |
| | Section 2 | ✓ | ✘ |
| | Section 3 (Powys Only) | ✓ | ✓ |
| Black & Veatch | Section 3 (Wrexham Only) | ✓ | ✓ |

Fig 7. Section 4 assurance

| Table | Methodology and Process | Data |
|-------|---|----------------|
| 4A | Jacobs | Jacobs |
| 4B | Internal Audit | Internal Audit |
| 4C | Internal Audit | Internal Audit |
| 4D | Internal Audit (upstream services cost driver calculations) | Internal Audit |
| 4D | Jacobs (Volumetric information submission) | Jacobs |
| 4E | Internal Audit | Internal Audit |
| 4F | Internal Audit | Internal Audit |
| 4G | Internal Audit | Internal Audit |
| 4H | Internal Audit | Internal Audit |
| 4I | Internal Audit | Internal Audit |
| 4J | Internal Audit | Internal Audit |
| 4K | Internal Audit | Internal Audit |
| 4L | Internal Audit | Internal Audit |
| 4M | Internal Audit | Internal Audit |
| 4N | Internal Audit | Internal Audit |
| 4O | Jacobs (Non-financial data) | Jacobs |
| 4O | Internal Audit | Internal Audit |
| 4P | Jacobs | Jacobs |
| 4Q | Jacobs | Jacobs |
| 4R | Jacobs | Jacobs |
| 4S | Jacobs | Jacobs |
| 4T | Jacobs | Jacobs |
| 4U | Jacobs | Jacobs |
| 4V | Internal Audit | Internal Audit |
| 4W | Internal Audit | Internal Audit |

6.2.1 Deloitte

Scope

Deloitte provided assurance procedures over sections 1 and 2 of the APR. These sections provide a baseline level of historical cost financial information and is aligned to our price controls (and associated regulatory performance commitments and incentives) set out in Ofwat's 2014 Final Determination. Deloitte audits the following tables within section 1 of the APR:

- Regulatory financial reporting tables comprising the income statement (table 1A).
- Statement of comprehensive income (table 1B).
- Statement of financial position (table 1C).
- Statement of cash flows (table 1D),
- Net debt analysis (table 1E).

The following tables in section 2 are also audited by Deloitte:

- Regulatory price review and other segmental reporting tables comprising the segmental income statement (table 2A).
- Totex analysis for wholesale water and waste water (table 2B).
- Operating cost analysis for retail (table 2C).
- Historical cost analysis of fixed assets for wholesale and retail (table 2D).
- Analysis of capital contributions and land sales for wholesale (table 2E).
- Household water revenues by customer type (table 2F).
- Non-household water revenues by customer type (table 2G).
- Non-household waste water revenues by customer type (table 2H).

- Revenue analysis & wholesale control reconciliation (table 2I).
- Infrastructure network reinforcement costs (table 2J).
- Infrastructure charges reconciliation (table 2K) and the related notes.

Deloitte refer to these tables as the 'Regulatory Accounting Statements' and their audit opinion is included on pages 42 to 45 of the APR.

Table 1F is not subject to audit procedures. As agreed with Ofwat, Deloitte have performed agreed upon procedures in relation to this table.

Outcome of Deloitte's assurance

Deloitte's audit opinion confirms:

- Proper accounting records have been kept by the appointee as required by licence condition F.
- The Regulatory Accounting Statements are in agreement with the Appointee's accounting records and returns for the purpose of preparing the Annual Performance Report.
- The Regulatory Accounting Statements have been properly prepared in accordance with Condition F, the Regulatory Accounting Guidelines issued by WSRA (RAG 1.08, RAG 2.07, RAG 3.11, RAG 4.08 and RAG 5.07) and the accounting policies (including the accounting separation methodology).

6.2.2 Jacobs

Scope

We asked Jacobs to provide technical assurance on the following elements of APR reporting:

- Performance against legacy STW PCs including associated customer ODIs and key supporting processes and data

for properties and volumes and Customer Operations Service Centre regulatory inputs in respect of the Powys area.

- Non-financial data included in the APR section 4 tables
- Common PCs reporting (PR19 ODIs)
- RoRE and financial flows.
- Cost allocation between appointee associates STW and HD, between HD price controls and to third parties.

Process

Jacobs undertake assurance using a three staged approach on a risk basis taking account of prior years assurance. Stages one and two focus on documentation and process. During stage one, Jacobs reviewed the PDT which are followed in order to report against PCs. Stage two included both desktop reviews and face-to-face interviews. These reviews ensure that:

- Processes are in place to produce data that are consistent with the RAGs, performance commitment definition or non-financial data definition.
- Improvements and changes in processes from previous assurance rounds are clearly stated.
- Accountability and responsibility of each stage of the process is clear with dependencies, assumptions, risks and mitigations identified.
- There is appropriate quality assurance with checks and controls identified.

Stage three focuses on data produced and associated commentaries which explain our performance in more detail. Audits are carried out in person with the responsible data owners. These audits ensure that:

- Data produced are consistent with the PDT and any deviations from this are identified and evidenced.

- Any rewards/penalties or further data points are calculated in line with Final Determination requirements. This focusses on the mechanistic calculation to give the gross reward/penalty position.
- Commentaries accurately reflect the data and performance within the year.

The assurance undertaken by Jacobs this year complements our overall assurance framework and reflects our view of the level of risk, which is in part informed by the previous assurance findings. Application of each stage of the Jacobs assurance approach for 2018/19 was guided by the level of risk.

Outcome of Jacobs' assurance

APR Section 2 – Cost allocation

As part of the industry's annual performance reporting, Ofwat requires companies to publish regulatory accounts that, among other things, set out financial information:

- on the allocation of costs by price control and subsections of the value chain;
- on non-appointed activity; and
- on transactions between associate companies.

In reporting on the above, we are required to comply with Ofwat's RAGs – in particular RAG 2.07 (Guideline for classification of costs across the price controls) and RAG 5.07 (Guideline for transfer pricing in the water and sewerage sectors).

Over and above the RAGs, companies' licences also place an obligation on them to ensure that every transaction between the appointee and any associated company is at arm's length, so that neither gives to nor receives from the other any cross subsidy

(Condition F). This also applies to appointed and non-appointed activity within the appointee.

Following the acquisition of Dee Valley Water, and the implementation of the subsequent NAV application to align STW and HD to the geographical border between England and Wales, Ofwat still expects transactions between STW and HD to be at arm's length.

Ahead of your year-end financial reporting, we asked Jacobs to review a sample of our cost allocation processes. We selected the sample based on your view of the risk associated with them. In total Jacobs reviewed 36 PDTs and processes, which covered:

- Allocations across price controls within STW and HD.
- Allocations between appointed and non-appointed activity within STW and HD.
- Allocations and recharges of costs between the associate companies STW and HD.

Consistent with previous work in this area, Jacobs reviewed the documentation and processes with a focus on the consistency of our allocation approach with the RAGs. To that end, Jacobs sought to understand:

- The areas/activities that were being provided.
- The costs associated with that activity – which for the PDTs we reviewed were operating costs.
- How those costs are recharged, allocated and why.
- How our approach is compliant with RAGs.

Jacobs acknowledged that many improvements had been made from the prior year and that we are continuing to improve our processes.

APR Section 3 – Performance Commitments

Half year

This year we asked Jacobs to focus the above staged approach on targeting PCs that we considered as high risk. The desk top reviews focused on whether actions from last year's assurance had been addressed. Process and data meetings were held where:

- We had made significant changes to our process since last year and/or the PCs did not meet our target confidence grade.
- There is potential to impact the customers' bill due to earning a significant reward or incur significant penalties.
- We may be underperforming and/or lack confidence in the data quality feeding into the AMP7 PCs's.

During their half year review Jacobs identified three areas that potentially had material risks:

- **SIM** – Following the integration of Hafren Dyfrdwy into Severn Trent's systems Jacobs noted some inconsistencies with regional allocation tags for unwanted calls and written complaints i.e. some contacts were appearing as 'unknown' in the reports and could not be allocated to a geographical area.
- **Properties and Volumes** – Jacobs identified that changes to reports to make them more robust mean the team was unable to simply produce Q1 data as the new reports took snapshots of a live system. Additionally Jacobs asked us to explain how we had accounted for changes in market eligibility following our NAV as there were some inconsistencies in the business and residential figures.
- **Leakage** – During their review, Jacobs noted that at half year there was a risk of our water balance gap being greater than 5%, which could mean our current reporting method is not the most appropriate.

We addressed these risks following half year assurance and are pleased to say that Jacobs agreed that these had been resolved during our year end assurance.

Full year

Jacobs reviewed the reported full year performance for the vast majority of the PCss set out in our Final Determination and the processes that were used to produce the figures. In line with our risk-based assurance framework, Jacobs did not review the PCs data or process where it is deemed low risk, for example 'Improved understanding of our services through education', which has no financial reward associated and has had no methodology changes from the prior year.

Jacobs' scope of assurance work included checking the following:

- The processes used are robust, enabling risks to be identified, managed and reviewed.
- The processes are sufficient, demonstrating an internal system of control and are consistent with the requirements of the regulatory obligations.
- The processes are managed with a system of governance that demonstrates a sufficient internal system of internal control.
- Data is competently sourced, processed and reported and fit for purpose.

Jacobs noted *'Overall, for the legacy STW PCs and non-financial APR section 4 tables and lines we reviewed we observed robust processes and reporting procedures. For the 2018-19 data we reviewed we note there are no remaining material issues...'*

We are pleased that our improvements made in the year have been recognised and Jacobs were satisfied with our reporting of the PCs.

APR Section 3 – Leakage

In 2018/19 we undertook our established assurance process which included process and data audits on our PCs at half-year and again at year-end with Jacobs, our assurance partners. At half year, Jacobs raised a potential risk to our year end position on the legacy Severn Trent customer ODI in Powys:

'During our half year exercise we observed that there is a potential material risk for 2018-19 full year reporting as your teams half year analysis indicates the [water balance] gap is continuing to grow...'

Although the Ofwat methodology changes planned for AMP7 would close the gap, we were aware that it was increasing. As a result of this risk, our teams undertook a number of improvement actions to understand why our water balance gap was growing:

- We reviewed all elements of our leakage calculation and ensured that the data is as accurate as possible. The rigour around understanding and improving our data accuracy helped us to know where leaks were taking place by eliminating areas where we were simply unable to account for water use. Through this we also improved our understanding of the additional water consumption observed during the hot weather period.
- Using our small area monitors, commercial consumption monitors and half yearly consumer meter readings we gained greater confidence in our ability to differentiate between true increases in water consumption and leakage. Based on the success this work delivered, we plan to continue this work throughout 2019/20.

As part of the work to better understand our data all components of the water balance

were reviewed and Jacobs were engaged in November to provide additional assurance and challenge and also to undertake regular interim audits of components and overall approach prior to year-end. Outputs of the interim audits were fed back to the head of leakage, head of group compliance and assurance and director of strategy and regulation.

The water balance investigation identified areas to reduce the water balance gap which consisted of data corrections, data improvements and methodology changes which were reviewed and agreed with Jacobs. The data changes have been included in the APR19 leakage reporting. The methodology changes, along with the previously identified consistency changes, have been included in our AMP7 shadow reporting. As a result of our work, Jacobs were satisfied that we had addressed the material risk noted at half year.

APR Section 3 – Common PCs

Ofwat has been working to develop consistent guidance for the 14 common PCs that it intends all companies to report on in the next AMP. While we are not required to formally report on these measures until 2020/21, Ofwat has included these measures in Table 3S of the APR for 2018/19. As a result, we asked Jacobs to use its three staged assurance approach in line with our other PCs by reviewing our processes, methodology and data.

Overall, Jacobs noted that for the majority of measures we were compliant with the reporting requirements, they did flag two common PCs required improvements in certain components of our leakage and per capita consumption measures to ensure we are fully compliant for 2020. Action plans are in place to ensure that all PR19 PCs including the common ones are fully compliant and ready for reporting in 2020.

APR Section 4 – non financial APR

Jacobs noted *'For the non-financial APR section 4 lines we reviewed we note that whilst there are no outstanding issues from our data audits that should have a material impact on your overall APR reporting for 2018-19, there are some lines where you will be monitoring reporting risk more closely, or implementing improvements, due to issues we identified during our work. We also recommended you carry out a review of how data is being aggregated for the purposes of HD APR19 reporting.'*

For all areas of risk or recommendations noted by Jacobs, we will review these and ensure we address any concerns next year.

6.2.3 Black & Veatch

Scope

Black & Veatch Ltd provided technical assurance on performance reported against annual PCs and against Ofwat common measures for Leakage, Interruptions to Supply and Per-Capita Consumption in respect of the Wrexham area.

Process

Black & Veatch conducted a one stage audit, which reviewed both process and data and included both desktop review and face-to-face interviews. As part of the process audit, Black & Veatch reviewed the PDTs which are followed in order to report against PCs. These reviews ensure that:

- Processes are in place to produce data that are consistent with the PC definition.
- Improvements and changes in processes from previous assurance rounds are clearly stated.

- Accountability and responsibility for each stage of the process is clear, with dependencies, assumptions, risks and mitigations identified.
- There is appropriate quality assurance with checks and controls identified.

The data audit focused on the data produced and associated commentaries which explain our performance in more detail. Audits are carried out in person with the responsible data owners. These audits ensure that:

- Data produced are consistent with the PDT and any deviations from this are identified and evidenced.
- Commentaries accurately reflect the data and performance within the year.

Outcome

Overall, Black & Veatch noted: *'From our assurance work we are satisfied that for the topics we covered, the information reported in and supporting the APR19 was compiled using appropriate data and methodologies and provides a realistic representation of actual company performance. We identified no material weaknesses or deviations from established procedure. In our opinion, the company's framework of three lines of assurance provides a good level of confidence that assurance is robust and governance in place. The reporting process and the information for reporting are scrutinized and approved by the Audit Committee and performance is reviewed by the Board.'*

Black & Veatch's summary of assurance is included on page 23 of the APR.

6.2.4 Internal Audit

Scope

Internal Audit conducted a number of checks across section 4 and the APR which included:

- Ensuring that all required statutory and regulatory disclosures were included in the text of the APR.
- Data checks on low and medium low risk tables and lines in Section 4. In some instances the tables checked derived from other financial tables in sections 1 and 2 that had been previously assured and Internal Audit would verify that the number used in both tables was the same.

Process

As part of its assurance, Internal Audit performed the following checks:

- Confirmed that the processes followed appeared appropriate to produce the data required for the submission.
- Traced historical data used in the tables back to source or previous published submission.
- Checked that data was produced in line with the methodology documents and RAG4 requirements.
- Data from the working files was agreed to the APR data tables to be submitted.
- A sample of business cases were reviewed to check the correct allocation of costs.

Outcome

Internal Audit confirmed that no material issues had been found and that *'all additional supporting evidence and answers to any queries raised were provided.'*

7. Outcome of assurance in other areas

In February 2019, we republished our 'Statement of risks, strengths and weaknesses' that we had published in November, alongside our final 'Assurance plan'. This document set out our key risks and included details of how we would address these with assurance this year in our final assurance plan. The table below details the outcome of that assurance. We believe that this table represents the majority of our high / medium high risks and stakeholder prioritised activity within the Company, however as a part of our risk and compliance framework we are always challenging our teams to ensure the data that they produce and publish is of a sufficiently high quality. We believe that good assurance is an integral part of the way we work and that checks are undertaken in both a formal and informal manner as part of our business as usual activity. We also complete numerous self-assessments of compliance at first and second line across the business.

| Risk Area | Why? | Summary of assurance undertaken |
|---|---|--|
| Annual Performance Report including our PCs | <p>This report is the principal way that we will document our annual performance and hold ourselves publicly to account. The report is divided into the following sections:</p> <p>Section 1: Regulatory financial reporting Section 2: Price review & other segmental reporting Section 3: Performance Summary Section 4: Additional regulatory information</p> <p>The report will include inputs from other areas covered by this assurance plan (e.g. financial accounts) and require some forecasts of performance. It is important that we present information in a fair and balanced way that is accessible to our broad range of customers and stakeholders.</p> <p>In addition some of our PCs have a financial reward or penalty associated so customer bills will be directly affected by our performance.</p> | As described in section 6 above. |
| Annual Report and Accounts | We have a statutory obligation to ensure that our financial accounts are prepared in accordance with the relevant financial reporting framework and give a true and fair view of the assets, liabilities, financial position and profit or loss of the company. | Our ARA has been subject to our established assurance and governance framework with the majority of data being subject to three lines of assurance. Deloitte have provided our financial audit opinion in line with statutory and regulatory guidelines. Their opinion is included in our ARA. Additionally any data that is included in both the APR and ARA is subject to the assurance as described in section 6. Our Internal Audit team also conducted some cross checks of the data used in the publication to ensure consistency. |
| Annual Report to CCWater | CCWater are the statutory customer representative body for our industry and a member of the CCG. We want to ensure the information we provide on a quarterly and annual basis is accurate. The majority of this data comes directly from our PC reporting. | Each quarterly submission is subject to internal first and second line assurance. Where the data is used for a PC the data is also subject to our assurance approach as described in section 6 above. |
| Boundary realignment | Following the creation of Hafren Dyfrdwy on 1 July 2018, our regulatory reporting has now been split according to the new licence lines. We have asked all lines of assurance to consider how the boundary realignment has impacted regulatory reporting and whether performance has been allocated to the correct entity. | Having completed the majority of our system integration programme at the beginning of the year, the focus for assurance this year was ensuring that our regulatory reporting reflected the changes. This led to us asking all areas to be able to report on a '4-box' model basis so that the four geographical areas within both companies could be identified e.g. STW England, Wrexham, Powys and Chester. As part of its third line assurance, we then asked Jacobs and Black & Veatch respectively to check we could report performance on the basis agreed in Ofwat's final NAV determination. Thanks to the significant work undertaken by our operational and financial reporting teams, no material issues relating to boundary realignment have been identified. |

| Risk Area | Why? | Summary of assurance undertaken |
|---|---|---|
| Charges including access prices and non-primary | <p>We want to make sure that what we charge our customers is correct. We have established assurance processes to ensure we are within our revenue cap and compliant with Ofwat's charging rules. The charges process is split into two parts:</p> <p>Draft – Since the non-household retail market opened, we have been required to publish draft wholesale charges in October to give retailers early sight of charges for the next financial year. Access prices are also reviewed at this stage.</p> <p>Final – In January, companies are required to publish all of their proposed charges for the next financial year i.e. non-household and household, retail and wholesale and non-primary charges.</p> <p>New Connections – On an annual basis we publish information relating to our New Connections charges as per the requirements of the Water Industry Act. Ofwat have now confirmed the new rules will not apply until 2022. While this won't impact our current year's assurance plans we will comply with any future requirements.</p> | <p>Our Scheme of Charges reporting is subject to three lines of assurance with a number of providers.</p> <ul style="list-style-type: none"> • Numeritas who reviewed our financial model • Jacobs who reviewed our methodology, processes and data outputs • Internal Audit who conducted final consistency checks on the model outputs, published documents and tracked noted assurance actions through to completion. <p>The outcome of their assurance was reported to the Audit Committee prior to approval. No material issues were outstanding and our final Scheme of Charges for 2018/19 was approved by our Board ahead of publication in line with our established governance. A Board assurance statement was published alongside our charges.</p> |
| Cost allocation activities | <p>Following the creation of Hafren Dyfrdwy we wanted to ensure that across the business we allocate costs correctly so that Hafren Dyfrdwy customers in Wales only pay for the services they receive, and vice versa for customers of Severn Trent in England.</p> | <p>In addition to the established activities described above (e.g. licence to operate and ERM) and in order to comply with the requirements of RAG 5.07, during 2018/19 we have added further controls and governance by establishing a Steering Committee responsible for overseeing RAG5 compliance and reporting directly to the Disclosure Committee. We have also established a RAG5 working group reporting directly to the Steering Committee, ensuring that any improvement actions are undertaken at an operational level.</p> |
| Drought Plan | <p>The Water Act (2003) made it a statutory requirement for water companies to produce and maintain a drought plan. We update these plans every five years. Our Drought Plan sets out how we will manage our resources and supply system in dry years, to maintain our service to our customers.</p> | <p>For our draft Drought Plan we performed second line assurance including technical assurance with no material issues identified.</p> <p>For the Statement of Response in September three lines of assurance were undertaken with Jacobs undertaking third line for any material changes or responses. No material issues were identified by Jacobs.</p> <p>We plan to carry out three lines of assurance on a risk based approach for the final plan.</p> |
| Reservoir resilience | <p>Highlighted as high risk in ERM due to potential loss of life and our obligations under the Reservoirs Act. Due to the nature of these assets, which are large water retaining structures, they have the potential to cause significant damage.</p> | <p>The risk levels associated with our reservoirs have been continuously monitored throughout the year through our ERM reporting, including bi-annual reporting to the Hafren Dyfrdwy Board. We have an action plan in place to ensure that inspections are completed on time and have been liaising with the EA to ensure any areas of concern are addressed.</p> |
| Governance of regulatory and statutory duties | <p>As noted above, we want to ensure we can demonstrate we have good governance arrangements in place in order for us meet our regulatory and statutory obligations. During PR19, Black & Veatch reviewed our governance arrangements and our processes for meeting these obligations to ensure these were appropriate</p> | <p>Our licence to operate process was subject to review through our established governance. This year we also added an extra step whereby we conducted face to face signoff sessions with members of our executive to highlight departures and areas of risk. This led to an increased level of engagement and challenge in the licence to operate process and acted as an additional level of assurance. In one instance a member of our executive team requested his managers re-visit their assessments before his sign off.</p> |
| K factor and ODI Model | <p>We provide a set of data spreadsheets to Ofwat on an annual basis so that it can calculate our in year ODI reward / penalty. Following Ofwat's review, we acknowledged that a small number of errors were made in our submission and had been missed by our second line assurance process.</p> | <p>This year this submission is superseded by the PR19 process, therefore please refer to 'PR19 – Future reporting and Initial Assessment of Plan ('IAP').</p> |

| Risk Area | Why? | Summary of assurance undertaken |
|--|--|---|
| Licence condition L | Following creation of Hafren Dyfrdwy, we want to ensure that we have confidence in our programme to maintain our underground assets. | Governance and associated processes are in place, and cost plans are reported. The work on asset health dashboards that is being developed for STW will be implemented across HD over the next year to give direct visibility of performance and how it relates to the health of our assets, to give further reassurance that maintenance and investment levels are proportionate to the service need. |
| Market information (water resources) | To help these markets grow successfully, it is important that customers and potential market participants can trust our costs are accurate in these areas for activities such as demand management, treatment, transport and other 'search costs'. We will support these new market areas and ensure our data is accurate and has had a third line review before publication. | For our bioresources submission, we supply a nil return on behalf of Hafren Dyfrdwy. For our water resources submission, much of the process, data and assurance is derived from the WRMP. As the water resources submission publication deadline is set to one month after publication of a company's final WRMP we will conclude our assurance at that time. We will ensure a consistency check is performed between the two publications. |
| Market Performance Standards ('MPS') and Operational Performance Standards ('OPS') | On a quarterly basis, we are required to submit a number of key performance indicators to the market operator, MOSL which then publishes the information on its website. This information is used by retailers, Ofwat and MOSL to ensure that wholesalers are delivering a competitive and fair service to all customers in the market. This year, failure to meet MPS SLAs will also result in a financial penalty. | OPS and MPS performance is reviewed throughout the month by the responsible managers and monthly with the accountable senior manager. Assurance has been completed on all our OPS submissions with third line assurance provided by Internal Audit periodically throughout the year. |
| PR19 – Future reporting and Initial Assessment of Plan ('IAP') | We want to ensure that in advance of the next reporting period (2020-25) we have adequate processes in place to report our new measures especially for our PCs that have a financial reward associated with them. Additionally, following Ofwat's IAP assessment our business plan was categorised as requiring 'significant scrutiny'. As a result we have had to resubmit our business plan to Ofwat, including a full set of data tables, as well as responding to a number of queries. | <p>As part of the PR19 process this year we have made several submissions to Ofwat</p> <ul style="list-style-type: none"> • PR19 submission - our submission to Ofwat was subject to an extensive programme of assurance which followed our established risk based approach and governance procedures. The assurance was specifically developed for PR19 with substantial third line assurance being undertaken by a number of assurance providers and industry experts. A statement of the assurance undertaken was submitted alongside our plan which can be found on our website. • PR19 queries – throughout the year we have received requests for clarification from Ofwat on our PR19 submission. Typically these have a two day turnaround and as such we aim to produce high quality responses within the timescale provided. Responses are produced by the responsible operational team and then reviewed by the Group Compliance and Assurance team as a second line check. Responses are always approved by a senior manager prior to being sent to Ofwat. • PR19 Plan resubmission and IAP Response - For both submissions, we applied the same risk-based third line assurance approach as was used for the original submission and included third line review by external assurers and peer review by industry experts. This included the resubmission of a new Board assurance statement. • PR14 reconciliation – Any data derived from APR19 was subject to assurance as described in section 6 above. Additionally our Internal Audit team reviewed our data. |

| Risk Area | Why? | Summary of assurance undertaken |
|--------------------------------|--|--|
| Water quality obligations | Our internal risk assessment noted this as potentially medium high risk due to recent staff changes within the teams involved. We believe we are compliant with our obligations due to existing processes but we want to refresh our managers on their obligations. | Annual reporting of our water quality measures with ODIs are also subject to three lines of assurance as described in section 6 above. In addition, since publication of our final assurance plan, we have reviewed our licence to operate assessments of water quality obligations and reduced the risk associated by completing or clarifying RACIs across the organisation. Following on from this review, we have also changed some of the accountable managers to reflect roles and responsibilities. |
| Water Resource Management Plan | This document sets out how we plan to meet our customers' need for clean water both now and in the future, taking into account the changing impacts of climate change and population growth. NRW has set out the approach it expects companies to follow in completing the submission and has outlined specific requirements for the Board to provide assurance that 'it is satisfied the plan represents the most cost effective and sustainable long-term solution.' | External third line assurance of data, methodologies and the presentation of information was provided by Black & Veatch. They found no material issues in the plan however made recommendations which we have implemented. Our WRMP was approved by our Board in line with our established governance and the assurance reviewed by the Audit Committee. Our Board provided a statement of assurance with the publication of our draft WRMP. |

8. Our approach to assurance from 2020 onwards

Our approach to assurance is constantly evolving and as we look to the next AMP, we want to develop our assurance processes further and innovate new methods to build trust.

8.1 Board governance and oversight

Our Board will continue to remain fully engaged in monitoring our performance and providing challenge where required through our established governance arrangements in the next AMP. In particular, performance against our new PR19 measures will be monitored by the Executive Committee and Board, and through the Severn Trent Plc Disclosure Committee and Audit Committee at least during mid-year and year end points in the reporting cycle. Our assurance plans will continue to be reviewed by Severn Trent Plc Disclosure Committee and Audit Committee for their input and challenge.

8.2 Our risk based approach to assurance

We will continue to use our risk based three lines of assurance approach to target the areas that matter most to our customers and to respond to changing regulatory conditions. To ensure we spot potential issues early, our future assurance plans will continue to highlight new reporting requirements or new legislation as an area of focus. For example, we expect all new PR19 PCs to go through both mid-year and year end audits in the first year to enable us to adequately assess areas for improvement and ensure we've the best data available to report our performance.

As part of our established processes, our new PCs will also be added to our licence to operate framework with accountable managers assigned to ensure strong business ownership and to capture any risk of non-compliance with the measures. Any business critical risks associated with our PCs will also be captured through our established ERM system.

8.3 A transparent approach to historic restatement

We are committed to continuously improving our data and information to support our regulatory returns and other information we publish in two ways:

- Striving to improve our current reporting methods – we review our internal processes and look externally for improved ways of reporting especially in areas where our information gathering process may still be maturing. For example, we acknowledged
- Correcting errors in a transparent manner and protecting our customers – while we believe our assurance framework reduced the risk of errors occurring in the first place, we recognise that as we review our historical performance retrospectively we may discover examples where we didn't get things right first time. In these small number of instances, we are committed to issuing clear and public corrections in the regulatory publications affected where we consider that this may impact on the trust of our customers.

8.4 Commitment to independent assurance

Trusted independent assurance is a critical part of providing confidence so we have already engaged our technical and regulatory assurance specialist, Jacobs, to work with us from now until 2025. We received and reviewed comprehensive bids from a number of external assurers through an OJEU tender process - an advertised tender with a scoring mechanism designed in advance of receiving full bids. As a result of this process, we've selected Jacobs as our technical auditor for the next six years. They offered the strongest package of assurance while also demonstrating value for money. During the last few years, Jacobs have provided a number of independent reports for our parent company, Severn Trent Water, and presented their findings to Severn Trent Plc Disclosure Committee the Severn Trent Plc Audit Committee and both STW, and more recently, HD Boards, while developing a cooperative relationship with data providers and owners across the wider business. Jacobs have built a strong historical knowledge of systems and processes now in place across HD, which will enable them to continue to act as a 'critical eye' and challenge us in areas of potential risk or non-compliance over the coming years

8.5 Transparency and challenge

From an external stakeholder perspective, we will continue to share our operational performance with CCWater on a quarterly basis and consult with external stakeholders on our assurance plans to ensure we receive appropriate levels of customer challenge and scrutiny. Our communications and customer research teams will also continue to look at the best ways of sharing our regulatory reporting information in a transparent way that is accessible and engaging to our customers.

As a public service we want to be transparent about how we balance the needs of our customers, our strategic plans as a business and a fair return for our investors. We believe we are prudent in how we manage financial risk and even-handed in the way we share the returns from our outperformance with customers and shareholders; we will continue to pay our taxes in full and on time; pay dividends and executive salaries that are reasonable and sustainable and linked to the delivery of outcomes to customers; and avoid complex offshore financial vehicles.

Detailed historical financial information is shared with customers and stakeholders through the Hafren Dyfrdwy website where we will continue to disclose this information throughout the next period to 2025. Our regulatory financial reporting is subject to external assurance by our third line financial auditors, Deloitte, as detailed in section 6 and 7.

Hafren Dyfrdwy is part of the Severn Trent Plc group, which also publishes its own ARA.

This contains information regarding our dividend policy. We also publish a history of our dividend payments for Severn Trent Plc going back to 1990. This ensures clarity about how our investors are rewarded based on our performance through the Group's activities.

This information will continue to be subject to third line assurance prior to publication.

We recognise that these elements are growing areas of interest to our customers given the ongoing national debate around executive pay and renationalisation. While the information we've published in our ARA and APR is very detailed, we recognise that it may not be accessible to all segments of our customer base. So we will provide a summary of this information in our customer APR and going forward, we'll consider how best to display this information while complying with current and future statutory and regulatory reporting requirements.