

Statement of Risks, Strengths, Weaknesses and Draft Assurance

Our Consultation for 2019/20

Hafren Dyfrdwy

November 2019

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1. About this document

At Hafren Dyfrdwy we're responsible for providing water and waste water services to over 107,000 customers in North-East, mid-Wales and Monmouthshire. We strive to achieve the highest quality standards in everything we do. Whether it's the quality of our drinking water or the regulatory performance information we publish on our website, we want to make sure that our customers can trust us to deliver what matters to them most.

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. Not only 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 established governance and assurance framework.

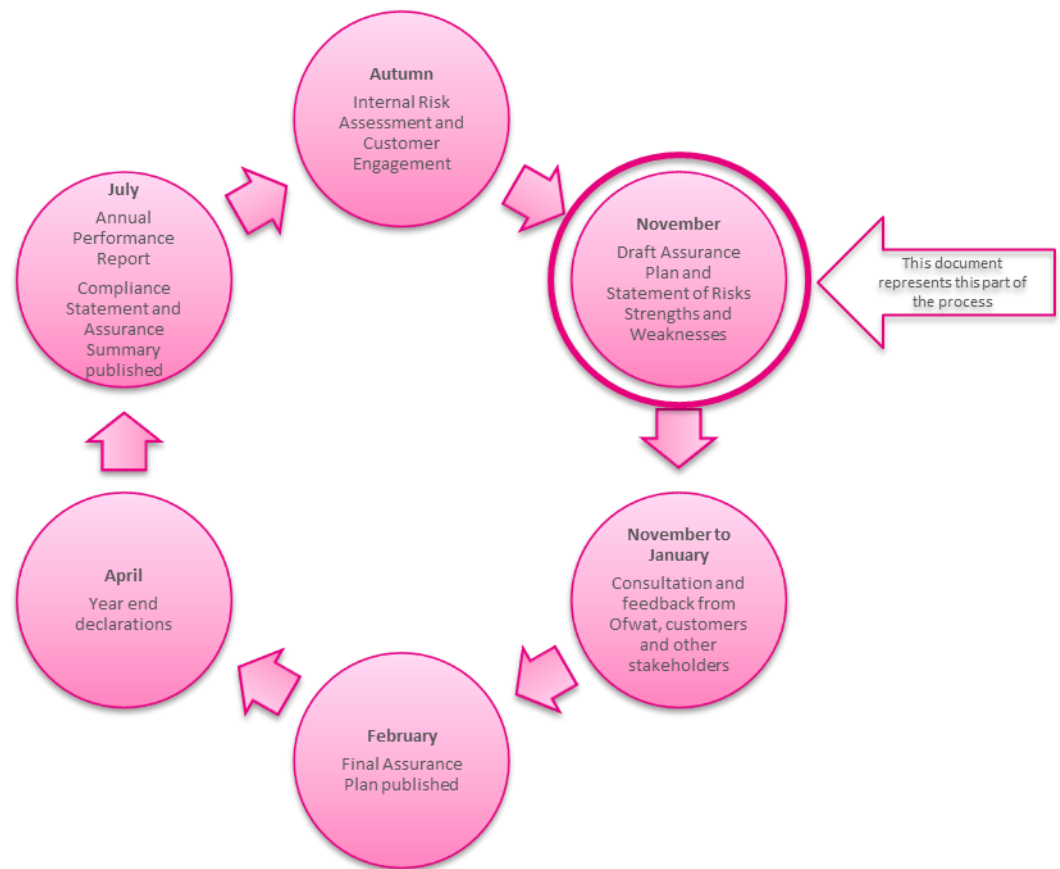
Understanding your views

This consultation document sets out our initial assessment of where assurance will be most important in the coming reporting year (2019/20). We'd welcome views on this and in particular: what regulatory information is most important to our customers; the level of risk associated with that information; and whether our proposed assurance plans are appropriate to mitigate those risks.

Historically, Ofwat assessed the levels of trust that it has in the data we produced by assessing us against number of different categories including for example, the accuracy of the data we've published, how we responded to Ofwat customer casework, or how we demonstrated wider engagement with our charges process. This assessment was known as the Company Monitoring Framework (CMF). This year Ofwat announced its intention to replace CMF with a new assurance framework¹. Until the new framework is announced companies are still required to ensure they meet the previous principles of the CMF and publish the required documents throughout the year. Fig 1 below shows what steps we take to meet the requirements and when our documents are published.

¹ <https://www.ofwat.gov.uk/publication/notice-update-on-information-quality-and-assurance/>

Fig 1. The Company Monitoring Framework cycle



This document contains two of the elements that we publish.

The first is our statement of risks, strengths and weaknesses. It has been developed using the feedback received from our stakeholders and insights from our customers about the information we provide. It also takes into account our own assessment of risks to our ability to provide information that they can trust. The second part is our draft assurance plan for 2019/20. This sets out how we plan to respond to those risks.

The document is open to consultation and we would welcome your views on it (details on how to respond can be found in section 3). Following feedback from our customers and stakeholders, we will publish a final assurance plan. In July 2020, we will publish an Annual Performance Report and an assurance summary setting out our progress against the assurance plan we have implemented.

The Severn Trent family

Hafren Dyfrdwy is an operating subsidiary of the FTSE 100 Company Severn Trent Plc, which means we operate at the high standards expected of a publically listed company. In July 2018, we realigned the boundaries of the two regulated water companies within the Severn Trent Plc group – Severn Trent Water and Dee Valley Water – to better match the boundaries between England and Wales. The company we created in 2018, Hafren Dyfrdwy, serves our customers in Wales while Severn Trent Water serves our English customers. This document relates to Hafren Dyfrdwy - our Welsh business.

Glossary

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

Term	Definition
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 performance commitments 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.
ERM	Enterprise Risk Management – our system of identifying and managing risks within Severn Trent Plc.
Group Compliance and Assurance	Our team in Severn Trent Plc that monitors compliance with our statutory and regulatory duties in our appointed and non-appointed businesses. We also oversee assurance activities within the business.
HD	Hafren Dyfrdwy Cyfyngedig – the regulated water company within Severn Trent Plc whose area of appointment covers North-East and mid-Wales and is the subject of this document.
Internal Audit	Reporting directly to the Severn Trent Plc Audit Committee, Internal Audit provides independent assessment of the effectiveness of our processes, controls and risk mitigation strategies.
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.
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 performance commitments (defined below).
Ofwat	The Water Services Regulation Authority – the statutory economic regulator for the water industry.
PC	Performance Commitment – the level of performance we've committed to deliver either annually or during the five-year period covered by business plans.
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.
RORE	Return on Regulated Equity – the percentage amount that we are allowed to give back to our investors, which is agreed as part of Ofwat's price limits.
SLA	Service Level Agreements – we have timescales and minimum levels of performance in place both internally and with our contractors.
ST	Severn Trent Water Limited – the regulated water company within Severn Trent Plc whose area of appointment covers the Midlands.
ST Plc	Severn Trent Plc – the parent company and ultimate controller of Severn Trent Water and Hafren Dyfrdwy.

Third Party Auditor /Assurer An independent audit company or organisation that performs audit or assurance services.

3. How to respond to this consultation

We welcome the views of our customers and our stakeholders. If you would like to respond to this consultation, please answer the following questions after reading this document:

Q1: How well have we adequately identified our areas of greatest risk?

Q2: Does our plan provides appropriate assurance to our identified areas of risk? If not, what improvements could we make?

a.) Do you think there are any areas we should increase the level of assurance?

b.) Do you think there are any areas we should decrease the level of assurance?

Q3: Do you think there are any additional areas we should focus our plans on for the next AMP (2020-2025)?

Q4: Do you have any other comments?

The consultation will remain open until **17 January 2020**.

Responses can be emailed to compliance.assurance@severntrent.co.uk or can be sent to our compliance team at:

**Group Compliance and Assurance Team
General Counsel
Severn Trent Centre
2 St John's Street
Coventry
CV1 2LZ**

4. Effective governance led by our Board

At Hafren Dyfrdwy, we have a governance framework, which is led by our Board. Our Board are fully committed to Ofwat's principles for Board leadership, transparency and governance with its emphasis on the importance of strong leadership and the special responsibilities attached to regulated monopoly companies, who provide an essential public service. We target ourselves against Ofwat's 2019 Board leadership principles² and will continue to build upon these into the next AMP.

Our purpose, values and culture

Our purpose is to serve our communities and build a lasting water legacy. This drives our vision to deliver an outstanding customer experience, best value service and environmental leadership. During 2019, we were delighted to see this commitment recognised when Severn Trent Plc was named as a pathfinder with the 'Purposeful Company Task Force' – an initiative that seeks to transform British business with purposeful companies, committed to creating long-term value, through serving the needs of society. We are the only utility to receive this honour. We are now in the process of refreshing our purpose and values.

This understanding and recognition of social purpose has never been more important – our purpose connects us with our customers and communities, inspires our people and reinforces that in the long-term we all share the same interests. We believe that transforming our services and driving growth will lead to mutual benefit for all, with performance that delivers benefits to one group while also delivering for others. The interests of our stakeholders are often interlinked, with many of our employees also being our customers.

You can read more in our social purpose section of the Hafren Dyfrdwy Cyfyngedig Annual Report and Accounts ('ARA')³. This document sets out what our social purpose is achieving for customers, the environment and society as a whole as well as our colleagues.

Our Board is responsible for establishing Hafren Dyfrdwy's purpose, vision and strategy, and satisfying itself that its culture is aligned with our Code of conduct, 'Doing the Right Thing', which sets out clear guidance on the standards of behaviour that we expect from everyone who works for, and with, Hafren Dyfrdwy. These values embody the principles by which we operate, 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 through consideration of mandatory training completion rates by all subsidiary companies including Hafren Dyfrdwy.

During the year, our Board spent time deepening its understanding of Hafren Dyfrdwy's culture, through consideration of the results of the Hafren Dyfrdwy employee survey 'QUEST' and other forms of employee engagement, discussing the Company's approach to addressing areas of employee focus. Additionally, our Board routinely interacts with employees as part of their site visit programme. These direct interactions with employees, specifically in relation to culture, allow our Board to understand first-hand the key issues identified by our workforce, and provide an opportunity to feedback specific insights.

Our Board continually monitors, assesses and reinforces our values and culture to satisfy itself that the behaviours throughout the business are aligned with the Company's purpose. Where misalignment is

² <https://www.ofwat.gov.uk/wp-content/uploads/2019/01/Board-leadership-transparency-and-governance-principles-2019-updated-July-2019.pdf>

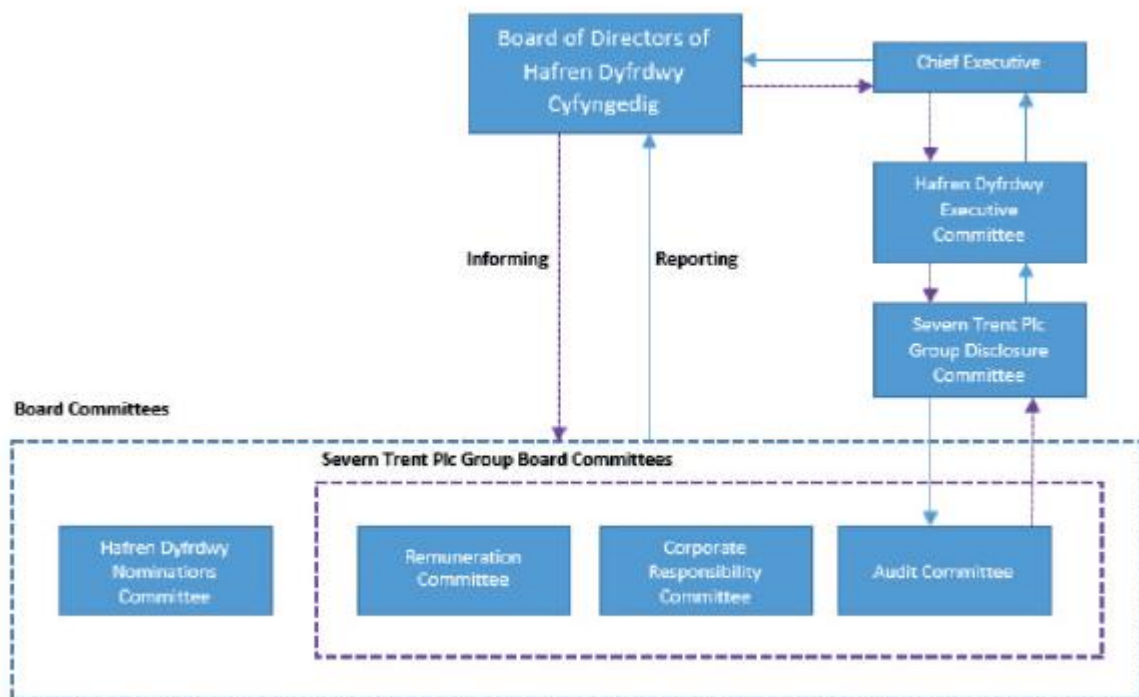
³ <https://www.hdcymru.co.uk/content/dam/hdcymru/regulatory-documents/hafren-dyfrdwy-annual-report-and-financial.pdf>

identified by our Board, appropriate corrective action is taken. No instances of misalignment were identified during the year. Additional detail can be found in the Hafren Dyfrdwy Annual Report.⁴

4.2 A standalone regulated company

Our Board is supported by the Severn Trent Plc Governance Framework, which is set out below. 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 their 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 Board regularly reviews the Terms of Reference of each Committee. The Governance Framework is also subject to periodic review to ensure that it remains appropriate.

Fig 2. Our governance framework



Management of Conflicts of Interest

Following the integration of Hafren Dyfrdwy with the Severn Trent Group, we reviewed our governance arrangements in full consideration of Ofwat’s Board leadership, transparency and governance principles. Our Board recognises that there is potential for conflicts of interest to arise from the existence of shared directorships between Severn Trent Water, Severn Trent Plc and Hafren Dyfrdwy. Severn Trent Plc has a Conflicts of Interest policy in place for all Group companies, including Hafren Dyfrdwy, and our Board considers potential conflicts at the outset of every meeting. The policy promotes independent decision making by our Boards, specifically in respect of any matters where there might be a conflict between the interests of our Boards and the interests of another part of the Group. This ensures that the Boards act in the interests of their respective stakeholders, including customers. Our Boards review the authorisation of any potential conflicts of interest every six months. A copy of the policy is available on the Severn Trent Plc website.

⁴ <https://www.hdcymru.co.uk/content/dam/hdcymru/regulatory-documents/hafren-dyfrdwy-annual-report-and-financial.pdf>

In addition, the Hafren Dyfrdwy Board also conducted a six monthly review of individual Director conflicts of interest. This process sets out any actual or potential conflict of interest situations which a Director has disclosed to our Board in line with their statutory duties and the practical steps that are to be taken to avoid conflict situations. When reviewing conflict authorisations, our Board considers any other appointments held by the Director as well as the findings of our Board effectiveness evaluation. Should a conflict or potential conflict materialise, then we have a documented process which provides that the relevant Director(s) may not take part in the subject matters to which the conflict relates and may not vote in respect of any decision taken in relation to it. The policy continues to be applied practically throughout the year, for example in considering the potential conflict presented by Directors having roles on other Group companies. For example, in September 2018 modifications were made to the Audit Committee meeting structure to facilitate dedicated Committee focus for Hafren Dyfrdwy regulatory matters and remove a potential conflict of interest scenario in relation to John Coghlan who is a Director of both Severn Trent Water and Hafren Dyfrdwy.

4.3 Board leadership and transparency

Group Structure

Hafren Dyfrdwy is an operating subsidiary of the FTSE 100 Company Severn Trent Plc, which means we operate at the high standards expected of a publicly listed company.

Severn Trent Plc publishes its own Annual Report and Accounts (ARA) and a history of our dividend payments for Severn Trent Plc going back to 1990 is available on the Severn Trent Plc website. Severn Trent Plc's dividend policy is disclosed in its ARA to ensure clarity about how our investors are rewarded based on our performance through the Group's activities. We also include full details of the Severn Trent Plc executive pay policy, its principal risks and details of how often its committees meet are contained within the ARA.

We believe in and align ourselves to the principles set out in Ofwat's 'back in balance' publication⁵ that stressed the need for water companies to be transparent about these topics. We acknowledge that they continue to be matters of keen interest to our customers.

Risk Management

Risk is all about uncertainty which, we recognise, can manifest itself as both negative and positive impacts. Our goal is to minimise the threats and maximise the opportunities for the benefit of our customers, employees, supply partners and the environment. Our approach to risk reflects our status as a regulated utility providing essential services and operating as part of the Critical National Infrastructure for the UK. The nature of the business is such that there are some significant inherent risks.

Our Board has overall accountability for ensuring that risk is effectively managed across Hafren Dyfrdwy. The Board's mandate includes defining risk appetite and monitoring risk exposure to ensure significant risks are aligned with the overall strategy of Hafren Dyfrdwy. On behalf of the Board, the Audit Committee assesses the effectiveness of the Group's ERM process and internal controls to identify, assess, mitigate and manage risk. The Hafren Dyfrdwy Executive Committee reviews strategic objectives and assesses the level of risk taken in achieving these objectives. This 'top down' risk process helps to ensure the 'bottom up' ERM process, described below, is aligned to current strategy and objectives. The management of risk is embedded in our everyday business activities. We manage risks within the overall Governance Framework which includes clear accountabilities, delegated authority limits and reward policies. These are designed to provide employees with a holistic view of effective risk management.

⁵<https://www.ofwat.gov.uk/publication/putting-sector-balance-position-statement-pr19-business-plans/>

Our ERM process is controlled by the central ERM team and underpinned by standardised tools and methodology to ensure consistency. ERM Champions and co-ordinators operate throughout the business, with support and challenge from the ERM team, continually identifying and assessing risks in their business units and reporting on a quarterly basis. Criteria are used to consider the likelihood of occurrence and potential financial and reputational impacts. The potential causes and subsequent impact of the risks are documented to enable mitigating controls to be assessed. This assessment allows us to put in place effective strategies to remediate defective controls or implement additional controls. Business units' information is combined to form a consolidated view of risk - with risks being prioritised.

To further enhance our ERM information, we report risk flight paths or have a plan to complete investigations needed to define the flight path. These demonstrate the level of risk we face and the timeline for the key risk mitigation steps to manage the risk to the target position. The flightpaths help to facilitate a more thorough review of the target risk positions, consider risk appetite and assess whether actions are on target with the correct prioritisation in place. In addition, individual risks and specific risk topics are also discussed by the Board during the year.

4.4 Board structure and effectiveness

Our Board's role is to ensure the long-term success of Hafren Dyfrdwy. Maintaining the highest standards of governance is integral to the effective delivery of our strategy and ensuring that our Board takes decisions that create sustainable long-term value for the mutual benefit of our customers, employees and the communities we serve. The operation of our Board is supported by the collective experience of the Directors and the diverse skills and experience they possess. Details of the experience of our Hafren Dyfrdwy Board can be found on our website⁶.

Our Board's collective experience enables it to reach decisions in a focused and balanced way, supported by independent thought and constructive debate between our Directors. Trust and mutual respect are the cornerstones of relationships between our Directors, with a Board dynamic that supports open and honest conversations to ensure decisions are taken for the benefit of the Company in full consideration of the impact on all stakeholders. Responsibility to all of our stakeholders for the approval and delivery of Hafren Dyfrdwy's strategy and for creating and overseeing the framework to support its delivery sits with our Board.

The majority of our Board and Board Committees comprise independent Non-Executive Directors and there is a clear division of responsibilities between the roles of Chair and CEO. To allow these responsibilities to be discharged effectively, our Chair and CEO maintain regular dialogue outside the boardroom, to ensure an effective flow of information.

The requirements of our Board are clearly documented in the Hafren Dyfrdwy Cyfyngedig Articles of Association and Schedule of Matters Reserved to the Board. These set out matters that are reserved for the parent Company (where applicable). They also contain provisions in respect of Hafren Dyfrdwy's regulated business, including strategy and management.

Board appointments and induction

Any new appointments to our Board result from a formal, rigorous and transparent procedure, responsibility for which is delegated to the Plc Nominations Committee (although decisions on appointments are a matter reserved to our Board). Further information can be found in the Severn Trent Plc ARA⁷.

⁶ <https://www.severntrent.com/about-us/corporate-governance/the-board/hafren-dyfrdwy-board/>

⁷ <https://www.severntrent.com/investors/annual-reports/2019-annual-report/>

We have an established induction programme in place which can be tailored to meet the requirements of individual Directors and includes the following elements/details:

- Ofwat pre-appointment process.
- Our business and how we are regulated, including performance.
- Our non-regulated business, including performance.
- Strategy.
- Key operations and processes including an immersive, practical journey through the water and waste cycles.
- Key stakeholder relationships.
- Customer delivery.
- Capital delivery and commercial.
- How the business is financed and financial performance.
- Our people and how we work, including health, safety and wellbeing, talent and succession, Trade Unions and an overview of our Remuneration policy.
- Risk and audit, including the risk profile and our approach to risk.
- Face-to-face meetings with key senior colleagues.
- Directors' duties.
- Governance matters and Company policies.

We continually enhance our Board's induction process, in full consideration of feedback from new appointees and the Board effectiveness evaluation.

Board effectiveness

The effectiveness of our Board is reviewed at least annually, and the 2018/19 evaluation was internally conducted by the Chair with support from the Company Secretary through a series of one-to-one meetings in January and February 2019.

The evaluation concluded that our Board and Nominations Committee were effective and that all Directors were considered to have demonstrated considerable commitment and time to their roles. The Board is considered to be of the right size and has an appropriately diverse and complementary mix of background, skills and cognitive thought.

The Board noted that PR19 approval and submission had been particularly well managed and that the use of additional Board Committee meetings and briefing papers had ensured that this topic had not distracted the Board from considering other strategic issues and operational performance oversight.

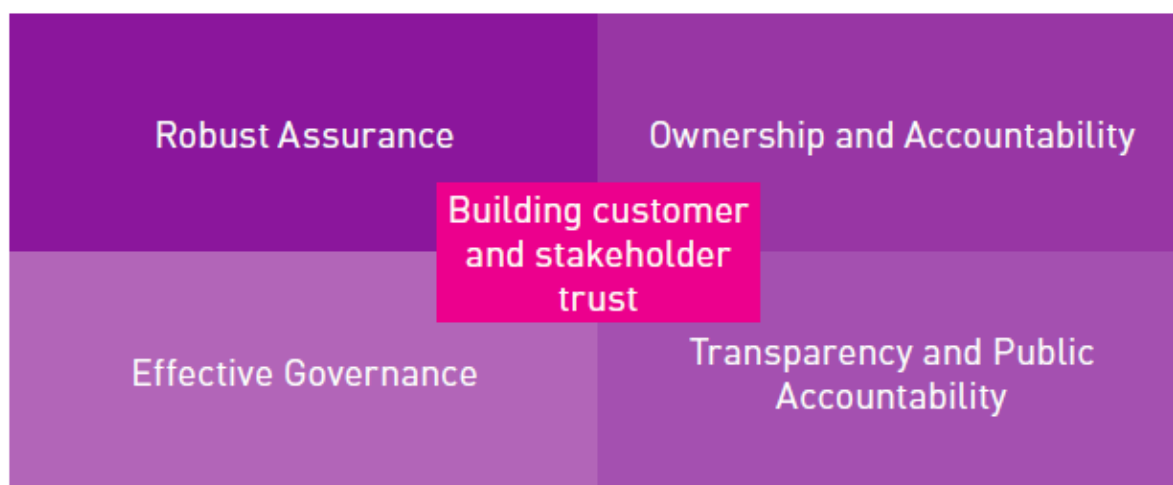
One of the other success factors of the PR19 submission was the ability of the Board to verify the statements it was required to make directly against assurance evidence provided to it. As a result, the Group Compliance and Assurance team have continued this approach by providing a forward plan of other regulatory submissions in advance with any required Board assurance statements. With each statement we have noted the evidence that will be provided so that Board could satisfy itself that the statement can be endorsed.

5. Assurance Framework

To support our Governance Framework, we have an established, rigorous and robust assurance and performance reporting framework. The assurance processes we use come from best practice identified across many organisations and industries ensuring that managers, senior leaders and Directors are responsible for delivering high quality data. Our assurance plan for this financial year, 2019/20, builds on the high standard processes we have developed and implemented in prior years to provide accurate data.

Our established framework is underpinned by four main principles (as shown 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.

Fig 3. The principles of our assurance framework



- **Robust assurance** – we operate a three-lines of assurance model, targeted at areas of greatest risk.
- **Ownership and accountability** – we have clear lines of ownership for both the delivery of performance, and the accuracy of the data provided.
- **Effective governance** – provided by our Board, Audit Committee, Executive Disclosure Committee and Executive Committee with additional challenge provided by our Customer Challenge Group.
- **Transparency and public accountability** – we publicly report on our performance and hold ourselves to account where we do not meet our commitments.

5.1 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 which considers areas that we know are of prime importance to our customers and regulators or may have a significant financial value, alongside the likelihood of reporting issues. Areas that are higher risk receive the full three lines of assurance while other areas, where the risk is lower, may be targeted with first or second line only.

This approach ensures we can continually reassess our assurance activity as risk is reduced in certain areas, where mature and stable process exist, and increased where new risks are emerging, resulting in a proportionate and value-added assurance spend.

Fig 4. Our three lines of assurance



First line activities are embedded within the teams that are responsible for reporting the performance so that staff 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, additional second line reviews are undertaken within the same directorate to ensure that we maintain a strong level of expertise and understanding of the source data.

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 providers:

- **Jacobs** - typically review non-financial operational performance processes and data. Also responsible for cost allocation activities and financial reporting processes.
- **Deloitte** – our financial auditors who mainly focus on our statutory accounts.
- **Internal Audit** - used for ad-hoc activity and data audits.

5.2 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 (described in detail in section 7), 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 compliance statement following review, scrutiny and remedial action by our senior leadership team and our Disclosure and Audit Committees.

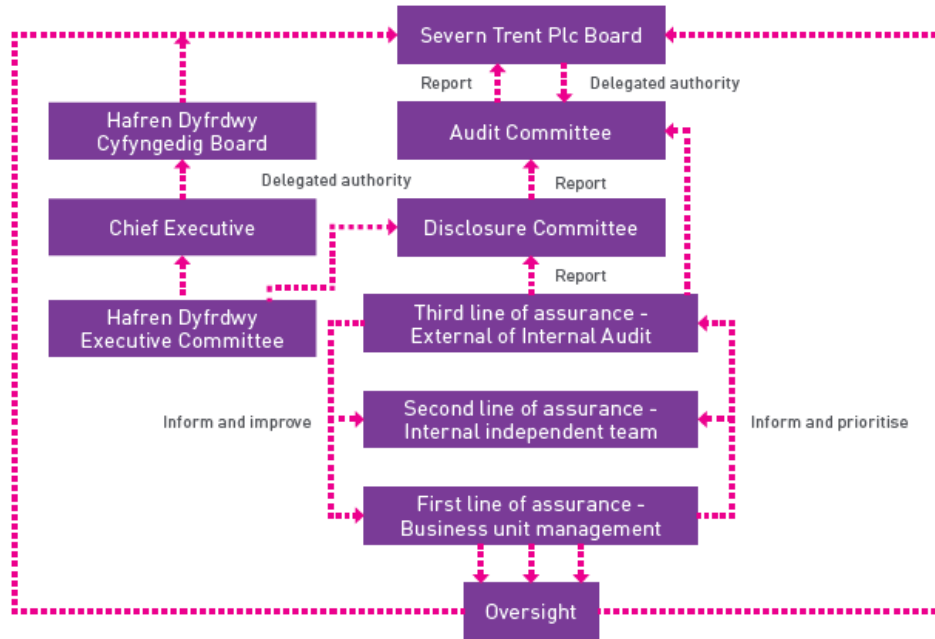
Overall accountability for the preparation and production of the APR (which includes reporting of performance against performance commitments and associated Outcome Delivery Incentives - ODIs) rests with the Chief Financial Officer. The outcome of the assurance undertaken is reviewed by the Severn Trent Plc Audit Committee (the 'Audit Committee') on behalf of the Severn Trent Plc Board.

5.3 Effective Governance

As described in section 4, our established governance and internal controls fully meet our statutory requirements 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. 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 figure below shows how our assurance framework interacts with our governance framework to ensure appropriate oversight of our assurance process at all levels.

Fig 5. How assurance interacts with governance



We use this model for our regulatory returns so that we, and our customers, have a level of assurance that our submissions have been well prepared and accurate. The effectiveness of the controls over reporting are monitored by the Audit Committee, which receives regular reports of the testing conducted by the Internal and External Auditors.

5.4 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 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 our customer version of our APR and hold ourselves to account where we do not meet our commitments. Where appropriate we have translated our documents into Welsh e.g. our customer APR summary.

We also include details on Executive pay and how Severn Trent Plc pays dividend payments in the Severn Trent Plc ARA.

6. Customer and stakeholder engagement

To understand which areas matter most to our customers and stakeholders, we used our regular engagement methods to inform this plan.

6.1 Customer engagement

During PR19 we ran targeted focus groups to understand what areas were most important to our customers. The key messages we received were that typically our customers rely on us to ensure we are producing accurate information, particularly with the introduction of customer ODIs where the information we produce can have a direct impact on their bills.

Last year, we opted for focus groups again however we wanted to specifically ask customers about how they felt about the boundary realignment of Severn Trent and Hafren Dyfrdwy, particularly in the three geographical areas most impacted by the change i.e. Powys, Wrexham and Chester. As such we conducted three targeted focus groups in these areas and asked customers to rate which areas they felt were important for us to target with assurance. In addition to ensuring that any activities impacted by the boundary realignment were assured, the following areas were identified by customers:

- Charges
- ODIs
- Annual Performance Report
- CCWater Report
- Water Resources Management Plan

Given the consistency of messages we have continued to see throughout all of our engagement, this year we have opted to ensure that the previous areas identified from customers are included in our assurance plan, while also using regular engagement throughout the year with our customers on a wide range of topics. Our key measures of customer satisfaction are described below:

6.1.1 Quarterly trust tracker

This year we have continued our regular customer tracker, which is conducted by an independent market research company. A representative sample of c400 HH and NHH customers in Powys and Wrexham are asked by telephone about a number of factors including levels of trust, customer experience, value for money and communications.

6.1.2 SIM (Service Incentive Mechanism) / CMEX (Customer Measure of Experience)

The aim of SIM was to capture the views of those customers who have had dealings with the company, not only through the main contact centre but to any part of the business or to a contractor. It was intended to capture views on how the contact was handled and was a common measure implemented by Ofwat for all water companies in England and Wales to create comparative satisfaction data. An annual score produced by four waves of customer satisfaction surveys took place at intervals throughout the year. The surveys were based on contact data that the company provides to an independent market researcher (BMG). On the back of every wave, we conducted in-depth analysis to understand any pinch points in our processes and where improvements could be made to enhance the customer's experience. Over the lifetime of SIM, we have made a number of a changes to improve our position although we were disappointed with our mid table position at the end of SIM's lifecycle.

For the next AMP, SIM is being replaced with CMEX, which aims to be a broader measure of customer satisfaction than the original SIM measure. We are part of Ofwat's working group and are already conducting pilot surveys in preparation for the changeover. Again similar to SIM, we are already conducting in-depth insight analysis into the customer feedback we received to enable us to address common complaints.

6.1.3 Non-household SIM (Service Incentive Mechanism)

Alongside our household CMEX measure, we also run CMEX score based service driven surveys for non-household customers who are not eligible for the market (customers using less than 50 mega litres of water per year) to ensure that we gain their customer views and convert to SIM equivalent scoring for reporting purposes. We are working with CCWater to understand the best measure of customer experience in the next AMP.

6.1.4 Regular engagement

We passionately believe in engaging with our customers to understand what matters to them in the information we produce, and address any concerns that they may have. Throughout the year we continue to use our established channels of customer engagement:

- regular meetings with our statutory customer representative (CCWater);
- ongoing customer research, including instant feedback mechanisms.
- ongoing analysis of customer sentiment including root cause analysis of customer complaints through all channels (telephone, social media, email and written).

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 have implemented a new tool, Sprinklr, which will greatly enhance our ability to gain insight from our social media platforms (primarily Twitter and Facebook). We will also continue to use customer focus groups and other bespoke survey methods on 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 in a way that is effective and cost appropriate for Hafren Dyfrdwy.

6.2 Stakeholder engagement

Our regulatory stakeholders' views are very important to us and we use the following channels to gain feedback from them:

- regular meetings and correspondence with our regulators;
- regular meetings and events with broader stakeholders (for example, partnership working on flooding issues and other stakeholder forums);

6.2.1 Ofwat

We continue to pursue a positive and engaging relationship with Ofwat through regular meetings and correspondence. We have a dedicated Ofwat inbox to help address any queries or customer concerns directly with Ofwat.

Under its last assessment in the Company Monitoring Framework, Ofwat noted improvement in our position from 2017. While no serious concerns were noted in the assessment, we remained in the 'prescribed' category. Last year's assessment was published later to align with the PR19 Initial Assessment of Plans in January 2019; we have continued to improve the areas identified through our Draft Determination response

and our APR19 publications and will continue to look at further ways we can address the themes noted in Ofwat's assessment:

- **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.
- **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.
- **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.
- **Company performance statement.** 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. In APR19, we included this statement upfront in our APR publication and will continue to do so in APR20.

Going forward, we welcome the opportunity to input into Ofwat's new quality and assurance framework and we will continue to focus on this into the next AMP.

6.2.2 Other stakeholders

We have continued to develop our open and honest conversations with a number of our environmental regulators including the NRW and DWI. We have reviewed our licence to operate and governance frameworks to ensure that our environmental regulatory and statutory obligations receive the appropriate oversight. As a result of this review we have included more environmental obligations in our licence to operate to capture oversight at a more granular level, and have increased the number of reports receiving scrutiny at our Disclosure Committee.

As we look to AMP7 and the changing regulatory environment, we are reviewing how we interact with our regulators to ensure that we are able to understand common themes in the types of enquiries or casework we receive and can build this into our governance and assurance frameworks.

7. Our internal assessment – licence to operate

As well as ensuring we account for our customers' views, we use the wealth of expertise within the business to assess all of our statutory and regulatory obligations relating to provision of water and wastewater. We call this assessment 'licence to operate' and it has been operating within the Severn Trent group for five years.

7.1 The process

We have applied our learning gained within group over the last four years to continuously review and improve the process by using new tools such as SharePoint to track the assessments and approvals from all levels of management. We used the licence to operate process last year to gain an understanding of the risks in delivering our obligations of our newly formed company. This year we have increased the number of duties we monitor through this process to over 500 obligations and over 900 lines of Annual Performance Report data lines.

Licence to operate is a two stage process that operates through the mid and year-end of the annual regulatory cycle.

7.1.1 Mid-year risk assessment

In September we ask our responsible managers to complete a risk assessment of their regulatory and statutory obligations. This involves assessing the following five categories as either low, medium low, medium high or high risk, which we use to indicate likelihood:

- **Purpose** – Does the responsible manager understand the purpose of the duty and what their obligations are?
- **Process** – Has the responsible manager ensured that there is an adequate process in place to comply with our obligation and is this documented?
- **RACI** – Is it clear which employees are responsible for which part of the process?
- **Competency** – Are employees suitably trained and is there a clear skill matrix defined?
- **Controls** – Are there measures in place to monitor performance and is regular quality checking undertaken?

Once this assessment has been completed, centrally the Compliance team assess the impact of non-compliance in this area using six factors:

- **Customer service impact** – what would be the impact on customers of non-compliance?
- **Competition compliance** – does the duty or obligation interact with competition law?
- **Impact on the environment** – could we damage the environment if we didn't comply with this obligation?
- **Health and Safety** – could someone be hurt as a result of non-compliance?
- **Regulatory impact** - is this a measure of prime importance to our regulators? Is it a key industry measure?
- **Financial impact** – could non-compliance result in financial fines? Would stakeholders lose confidence in the business?

By combining the likelihood assessment with the impact assessment we are able to understand the areas of compliance risk that require either management action and/or our assurance plan needs to target. This allows us the opportunity to put action plans in place prior to our year-end reporting of performance. For further

verification, we also review these risks against our ERM register to ensure there has been a consistent assessment of risk across the two processes.

7.1.2 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 and what action will be taken 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 annual Compliance Statement, which is published in July within our regulatory reporting. This document is reviewed and scrutinised by 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.

7.2 Changes in 2019/20

This year we added new obligations to our 'licence to operate' process to respond to changes in our operating model and our statutory obligations:

- Added a further level of granular environmental legislation into licence to operate for example ISO Environmental standards, Clean Air Act, Control of Pollutions Regulations etc.
- Introduced a conflict of interest declaration for all responsible and accountable managers whereby managers who may have responsibility for both appointed and non-appointed activity; or between entities have a responsibility to ensure they are transparent about any potential conflicts in their role. This gives us the ability to target these roles with further training and guidance.

For the next AMP we are looking to make further streamlining improvements to the licence to operate process by using technology improvements such as Office365 to give us the ability to track local action plans for improvement throughout the year rather than on a bi-annual basis.

7.3 Obligations identified by assessment

In this year's licence to operate assessment, the following areas were noted as either high or medium high risk in order of risk:

- **PR14 performance commitments** - in recognition of the potential impact our performance commitments have on our customers, the environment and market confidence, our customer ODIs continue to feature in our assurance plans as part of the Annual Performance Report. Customer ODIs remain a high priority for our stakeholders and customers because:
 - our performance commitments 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 are meeting our commitments;
 - we apply financial incentives to some of our ODIs – if we are to make decisions that impact our customers' bills, we must have confidence that it is on the basis of high quality information.
- **PR19 Performance commitments** – in the next AMP, the PR14 obligations will expire and be replaced with the new PR19 performance commitments. For the same reasons noted above we are ensuring

that in preparation for 2020-2025 we can fulfil and accurately report on our performance commitments.

- **Cost allocation / RAG5** – Cost allocation activities within our finance team are part of our established third line assurance annual processes. We are on a journey of continuous improvement to ensure that our processes are suitably documented within both the two appointed businesses (Severn Trent Water and Hafren Dyfrdwy) and other non-appointed businesses within the Severn Trent family. Last year we created a RAG5 steering committee to oversee these risks at the group level.
- **Licence Conditions E1 and M1** – these licence conditions were implemented as part of our licence in January 2019 and relate to the provision of information in Ofwat’s designated ‘new markets’ i.e. bioresources, water resources, demand management and leakage services. While we do not believe we are non-compliant with these obligations as existing policies will cover our compliance with them e.g. competition law and ‘doing the right thing’, we need to ensure that we have suitable processes in place in relation to these emerging markets.
- **Licence condition L** – 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 in Powys and Wrexham to ensure visibility of outputs and control frameworks however, we still in the process of gaining better visibility of HD’s risk and opportunities in this area.
- **Water quality obligations** - We are currently in the process of making improvements to our drinking water safety plan to ensure that all of our required risk assessments are completed on time and to suitable standard.

Where appropriate, action plans have been put in place to address these areas and reduce the level of risk associated.

7.4 Obligations identified by wider engagement and insight

Our internal group compliance and assurance team also provides further oversight of our assurance plan to ensure that we include areas that may not necessarily score high on our internal risk assessment in the present, but that we know are subject to or could be, subject to regulatory change or emphasis such as the requirement to have a board assurance statement.

- **Annual Performance Report including sections 1, 2, 3 and 4** – 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:
 - Section 1: Regulatory financial reporting
 - Section 2: Price review & other segmental reporting
 - Section 3: Performance summary
 - Section 4: Additional regulatory information

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.

In addition some of our PCs have a financial reward or penalty associated so customer bills will be directly affected by our performance.

- **Annual Report and Accounts (ARA)** - 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.
- **Annual Report to CCWater** - CCWater are the statutory customer representative body for our industry and a member of our CCG. We want to ensure the information we provide on a quarterly and annual basis is accurate. The majority of this data is directly from our PC reporting.

- **Charges including draft wholesale charges, final charges and access prices** - 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:
 - 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.
 - 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.
- **New Connections charges** - Our developer services customers want the ability to accurately predict what their costs will be when they build and connect a property to our network. Therefore, it's important then we publish our annual charges for new connections that they are accurate, easy to understand and cost reflective. Furthermore new connections charges are subject to competition law and is an area of focus for Ofwat. To ensure we meet these requirements, we have put in place a comprehensive set of assurance checks.
- **PR14 reconciliation** - We provide a set of data spreadsheets to Ofwat on an annual basis so that it can calculate our in year ODI reward / penalty and reconcile our past performance with our forecasted targets etc. Following Ofwat's review, we acknowledged that a small number of errors were made in similar submissions previously which had been missed by our second line assurance process.
- **Market information (bioresources and 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.
- **Market Performance Standards (MPS) and Operational Performance Standards (OPS)** - On a monthly 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. Failure to meet OPS and MPS SLAs will also result in a financial penalty.
- **Natural Resources Wales submissions** – Following the case raised against Southern Water, we wanted to ensure that we undertook a review of our compliance against similar obligations in our own company. As a result, we have added a further governance review of our NRW submissions by our Disclosure Committee.
- **Drought plan and other drought obligations:** 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 our customers. We published our final plan this year.
- **Water Resources Management Plan** – Last year, our Water Resource Management Plan was published and was open to consultation with all our customers and other stakeholders. We have now been given approval to publish the final plan. We have a duty to review our plan on a regular basis to ensure it is kept up to date with the latest understanding of water demand and climate change. Given the complexity and strategic importance of managing our water resources, we wanted to make that our final publication was subject to third line review.

How we have targeted these areas with assurance is described in section 8.

Areas of risks and our draft assurance plan for 2019/20

Following both our external and internal engagement we consider the following areas, or components of these areas, are categorised as either high or medium high risk and therefore should be subject to a greater level of assurance, which is detailed in the table below.

Risk Area	What assurance will we be doing?	New in 2019/20?	2021-2025 Plans
Annual Performance Report (APR) including our PR14 Performance Commitments	<ul style="list-style-type: none"> On an annual basis all performance data is subject to assurance. In addition, using a risk based approach, some of our measures are also subject to half year assurance to get early sight of any potential risk areas, which we can address prior to year-end. For sections 1 and 2 of the APR, the data and methodology is subject to three lines of assurance with our financial auditor performing third line assurance. For section 3 and 4 of the APR, the data and methodology is assessed and subject to our three lines of assurance model based on risk with our regulatory technical auditor or Internal Audit performing third line assurance as appropriate. Customer Challenge Group (CCG) also review the performance and assurance processes prior to publication. 	Established process	Established APR process will continue and evolve to include the PR19 Performance Commitments
PR19 Performance Commitments	<ul style="list-style-type: none"> The data and methodology is assessed and subject to our three lines of assurance model based on risk with our regulatory technical auditor performing third line assurance as appropriate in parallel with our PR14 performance commitments. 	Process established in 2018/19	Process will be incorporated into APR
Cost allocation / RAG5	<ul style="list-style-type: none"> Cost allocation data and methodology is subject to three lines of assurance with our regulatory technical auditor performing third line assurance. Focus on the boundary realignment and non-appointed businesses. Our updated RAG5 compliance Framework will be subject to three lines of assurance with an external auditor completing third line assurance. 	Established process	Established process will continue and Internal Audit will undertake annual assurance of the RAG5 Compliance Framework.
Licence Conditions E1 and M1	<ul style="list-style-type: none"> Data and methodology subject to second line assurance with third line process assurance undertaken by Internal Audit on new areas. 	Process established in 2019/20	Established process will continue and will be refined to take account

			of evolving regulatory requirements
Licence Conditions L	<ul style="list-style-type: none"> The process will be assessed and subject to our three lines of assurance model based on risk with third line assurance as appropriate. 	Process established in 2019/20	Established process will continue and will be refined to take account of evolving regulatory requirements
Water quality obligations	<ul style="list-style-type: none"> Where data is provided to DWI as part of our Performance Commitments, the data and methodology is subject to three lines of assurance with our regulatory technical auditor performing third line assurance. Other areas, including our safety plan, are assessed and subject to our three lines of assurance model based on risk with our regulatory technical auditor performing third line assurance as appropriate. Submissions reviewed at Disclosure Committee. 	Established process updated for 2019/20	Established process will continue and will be refined to take account of evolving regulatory requirements
Annual Report and Accounts (ARA)	<ul style="list-style-type: none"> The methodology and data is subject to three lines of assurance with our financial auditor performing third line assurance. The methodology and data of our RORE calculations is subject to three lines of assurance with our regulatory technical auditor performing third line assurance. 	Established process	Established process will continue and will be refined to take account of evolving regulatory requirements
Annual Report to CCWater	<ul style="list-style-type: none"> Where information is derived from performance commitment data, assurance is as noted above. Where information is not derived from performance commitment data, second line assurance is performed. 	Established process	Established process will continue and will be refined to take account of evolving regulatory requirements
Charges including access prices	<ul style="list-style-type: none"> Methodology is subject to three lines of assurance with our regulatory technical auditor performing third line assurance. Model assurance undertaken by specialists, Numeritas. An assurance statement signed by our Board demonstrating Board oversight and scrutiny. Engagement with customers and CCWater to ensure bill impacts are understood (particular where these are greater than 5%). 	Established process	Established process will continue and will be refined to take account of evolving regulatory requirements

New connections charging	<ul style="list-style-type: none"> The Data and methodology is subject to 2nd line assurance. Engagement with developer services customers. 	Established process	Established process will continue and will be refined to take account of evolving regulatory requirements
PR14 reconciliation	<ul style="list-style-type: none"> The data and methodology is assessed and subject to our three lines of assurance model based on risk with third line assurance undertaken as appropriate. 	Process established in 2018/19	Established process will continue and will be refined to take account of evolving regulatory requirements
Market information (bioresources and water resources)	<ul style="list-style-type: none"> The data and methodology is assessed and subject to our three lines of assurance model based on risk with our regulatory technical auditor performing third line assurance as appropriate. 	Established process	Established process will continue and will be refined to take account of evolving regulatory requirements
Market Performance Standards (MPS) and Operational Performance Standards (OPS)	<ul style="list-style-type: none"> The data and procedures are subject to three lines of assurance with Internal Audit performing third line assurance on OPS. Performance reviewed on a quarterly basis at Disclosure Committee. 	Established process	Established process will continue and will be refined to take account of evolving regulatory requirements
NRW submissions	<ul style="list-style-type: none"> Where data is provided to NRW as part of our Performance Commitments, the data and methodology is subject to three lines of assurance with our regulatory technical auditor performing third line assurance. Other areas are assessed and subject to our three lines of assurance model based on risk with our regulatory technical auditor performing third line assurance as appropriate. Submissions reviewed at Disclosure Committee. 	Established process updated for 2019/20	Established process will continue and will be refined to take account of evolving regulatory requirements
Drought plan and other drought obligations	<ul style="list-style-type: none"> The data and methodology is assessed and subject to our three lines of assurance model based on risk with our regulatory technical auditor performing third line assurance as appropriate. 	Established process	Process will continue with next review cycle

**Water Resources
Management Plan**

- The data and methodology is assessed and subject to our three lines of assurance model based on risk with our regulatory technical auditor performing third line assurance as appropriate.
- An assurance statement signed by our Board demonstrating Board oversight and scrutiny.
- Independent challenge from external stakeholders including NRW.

Established process

Process will continue
with next review cycle

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