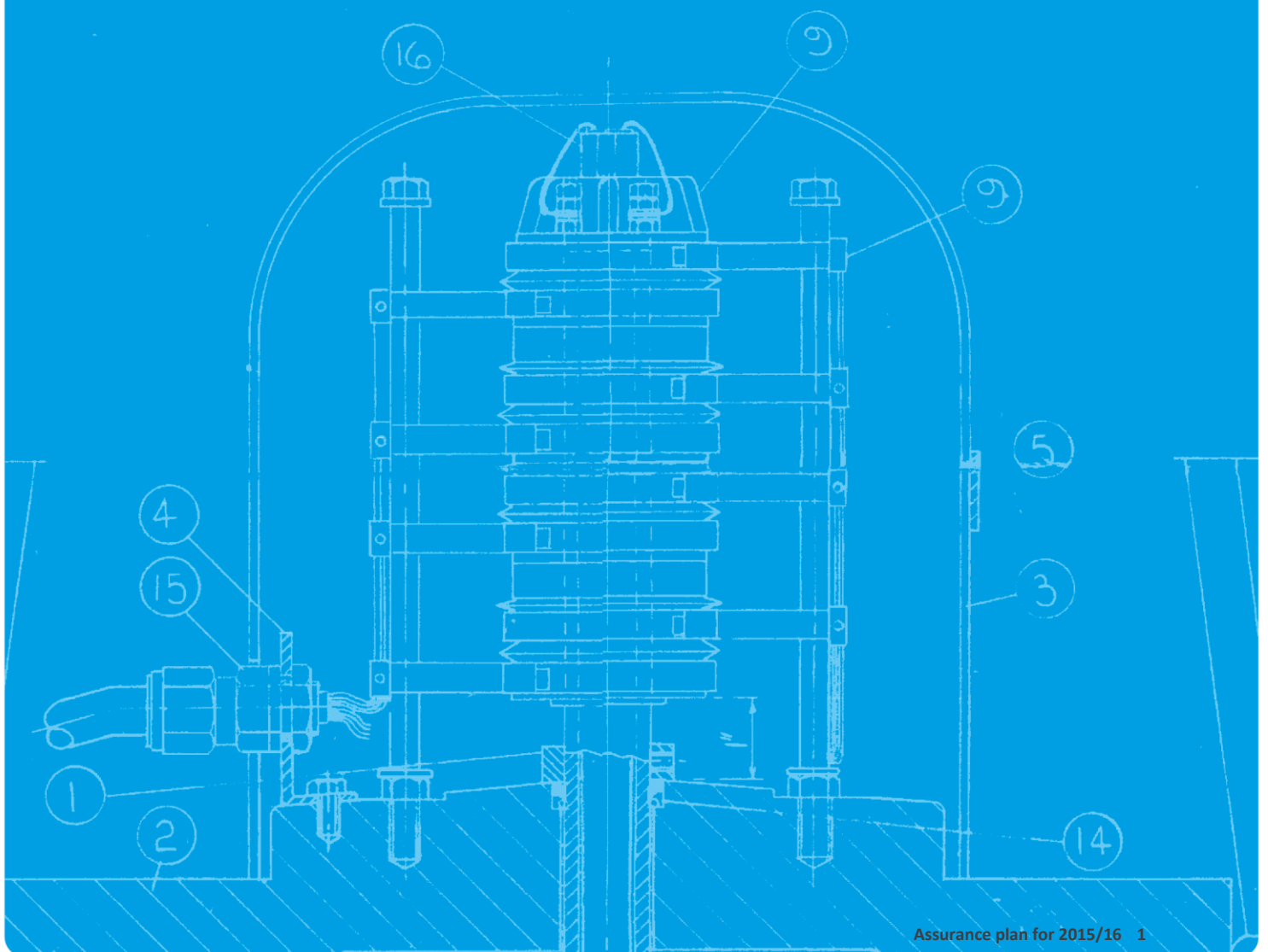


# Assurance plans for 2015/16

February 2016



## About this document

*Severn Trent Water is one of the largest of the ten regulated water and sewerage companies in England and Wales. We strive to provide high-quality services to more than 4.3 million households and businesses in the Midlands and mid-Wales. Our customers pay the lowest average bills in the UK.*

By 2020, we want to be the most trusted water company: delivering an outstanding customer experience, the best value service and environmental leadership.

Every year we publish a wide range of information about our services and our performance. This information is used in a variety of ways; not least it may shape the choices our customers and stakeholders make. We therefore want to make sure that it can be relied on.

This document sets out our assurance plans for 2015/16.

### Background

As we developed our [business plan for 2015-20](#), we recognised that the introduction of performance commitments with associated Outcome Delivery Incentives (ODIs) would create a new area of focus for our assurance plans.

There are 45 performance commitments in our plan. Of these performance commitments, 33 have financial rewards and penalties attached to them as ODIs – which may impact our customers' bills. We are one of just three companies able to apply some of these ODIs during the 2015-20 period (i.e. before our plan is completed).

In recognition of this, we set out detailed proposals for assurance in our business plan with the aim of ensuring that our customers and stakeholders can trust the data and information that we provide on our performance. This document builds on those proposals. It also considers how we can ensure our customers and stakeholders can have confidence in the information we publish more widely.

### Ofwat's company monitoring framework

Ofwat's company monitoring framework (published in June 2015) set out its expectations for how it will oversee the information that water companies provide to our customers. There are 18 water companies serving household and business customers in England and Wales – 10 provide water and wastewater services. The remaining eight provide water only. Under its company monitoring framework, Ofwat assessed Severn Trent and 14 other companies out of the total of 18 as requiring targeted assurance. This means we need to work with our customers and stakeholders to target issues, and consult on our draft assurance plans to make sure they are sufficient to address them.

We are supportive of this approach – we cannot expect to build and maintain the trust of our customers and stakeholders if we do not first understand if they have any concerns, and then seek to address them.

## Using customer and stakeholder engagement

This document marks the end of a six-month long period of consultation.

- In September 2015 we undertook a programme of customer and stakeholder research to better understand how they use the information we produce and the extent to which they trust it. This built on our established channels of 'business as usual' engagement with our regulators, investors, customers and other stakeholders. We used this information, and our own assessment, to produce a **statement of risks, strengths and weaknesses**. Section 1 of this document summarises that statement.
- In November 2015 we published a written consultation on our risk statement and a draft assurance plan for 2015/16. Our assurance plan set out how we proposed to respond to our risk statement. We asked for views about whether it was sufficient to mitigate the risks identified.

In section 2 of this document we set out our **final assurance plan for 2015/16** which takes into account comments from our stakeholders.

Three stakeholders responded to our consultation in writing. Two of the respondents to the consultation were supportive of our approach. We have responded to the suggestions of the third below.

Stakeholder comment	Our response
Enhance our end-of-year reporting on performance by including how bills are impacted by any over or under performance on ODIs.	We believe that if we report on bill impacts, it is important that we are able to report information clearly. We have agreed to work with CCWater on how we present information to customers and have included our calculation of the indicative impact of ODI performance on average household bills in our assurance plans for this year.
Ensure that as we make preparations for the new non-household retail market, that we not only ensure we are ready, but also ensure that we help to address the concerns of business customers entering into the market.	We regard ensuring our customers receive a great retail service and indirectly, wholesale service - as well as complying with the relevant customer protection measures that are introduced - as an important part of 'being ready' and have therefore been factored into our assurance plans.

We also discussed our plans with the Water Forum. The Water Forum is an independently chaired, multi-stakeholder group created to challenge how our customers' priorities were reflected in our 2015-20 plan. The Forum now has a continuing role to challenge whether we are delivering our commitments to our customers, and how we communicate that performance. It includes representation from the Environment Agency, CCWater, Natural England, National Farmers Union (NFU), East Midlands Councils and the CBI. It has endorsed our approach.

# 1. Our statement of risks, strengths and weaknesses: summary

*In this section we re-cap on how we carried out our risk assessments, and the target areas we identified. Our assurance plan in section 2 sets out how we are responding to these risks.*

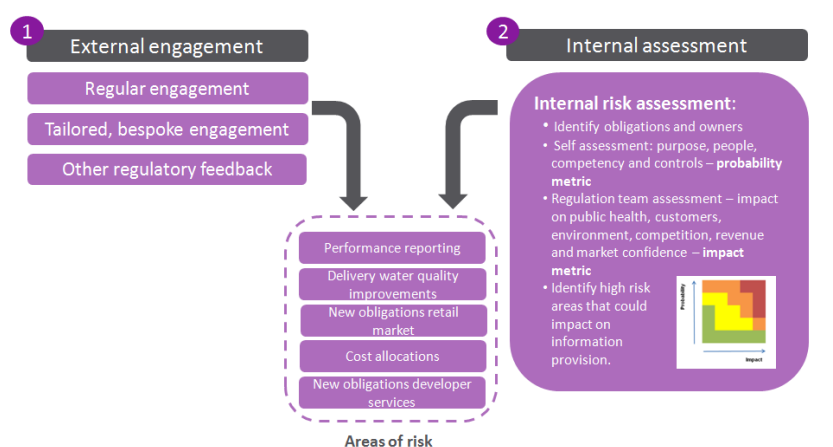
## Approach

Figure 1 below illustrates how we developed our statement of risks, strengths and weaknesses using two inputs:

1. External engagement. We built upon our existing channels of engagement by asking our regulators, customers and other stakeholders about how they use information we produce and whether they have any concerns about the integrity or quality of that information.
2. Internal assessment. We used a framework to identify potential risks to complying with our statutory and regulatory obligations (relating to our regulated water business). This assessment considers the probability of not complying and the impact.

This was a separate exercise to the assessment of risks inherent in our business activities and mitigation measures, which we include in our [annual report and accounts](#).

**Figure 1: Approach to developing this risk assessment**



## Statement of risks

The risks we have included in our statement principally reflect:

- new reporting requirements and statutory obligations; and
- other changes in our external environment or our customers' and stakeholders' expectations.

They are:

*Performance reporting – performance commitments and ODIs.*

2015-20 marks a new era of performance reporting for us. The introduction of financial ODIs means that our performance has the potential to directly impact customers' bills. And every single one of our performance commitments, regardless of whether a financial incentive is attached, could impact our customers' and

stakeholders' perceptions of us, and shape the choices they make. Given the importance that we, and they, attach to performance commitments, we have developed a rigorous assurance plan. Rather than carrying out a risk assessment to target performance commitments for greater assurance at the end of the financial year, our assurance plan (section 2) provides for all performance commitments to undergo full external assurance at both the half and full year (in addition to our ongoing internal quality checks, controls and improvement plans). Our half year review allows us to identify performance commitments where further assurance 'deep dives' may be required in the run up to full-year reporting.

### *Delivery of drinking water quality improvements*

In our 2015 annual report and accounts we explained that drinking water quality would be an important area that we would be focusing on to improve performance over the coming year. We need to provide stakeholders with confidence about the progress we are making.

### *New obligations for the retail market*

The Water Act 2014 introduces a new framework for retail competition for non-household customers. As an incumbent in the market, we need to provide assurance that we will be ready for market opening on 1 April 2017.

### *Cost allocations (and segmental reporting)*

The introduction of retail competition will place further customer (retailer) scrutiny on how we allocate our costs between wholesale and retail activities, and in turn household and non-household activities. Ofwat did not raise any concerns with the allocations in our 2014/15 regulatory accounts submission. However, this is an area that we will continue to focus assurance activities on in order to make sure market participants can have confidence in our charges.

### *Developer services*

The Water Act 2014 introduced new obligations in relation to the services we offer to developers. We have also begun to voluntarily report our performance along with other water companies, so that customers can compare the standard of service they receive from us in context with the rest of England and Wales. Given these new requirements, and in the light of forthcoming statutory changes, this will be an area of focus for our future assurance plans.

## 2.1 Assurance plan 2015/16: our approach

*This section sets out our assurance plan for 2015/16. The first part provides an overview of our approach to assurance. The second part focuses on the key areas identified in our risk statement as well as where we already have established third-line assurance processes that we propose to continue in 2015/16.*

We have an established assurance and performance reporting framework. Our proposed assurance plan for this financial year, 2015/16, continues the processes we have developed for reporting of company KPIs in our annual report and accounts and for regulatory submissions in previous years.

Our framework is underpinned by four key principles:

- *Robust assurance* – we operate a three-lines of defence 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, Disclosure Committee and with additional challenge provided by the Water Forum.
- *Transparency and public accountability* – we publicly report on our performance, and hold ourselves to account where we do not meet our commitments.

In this section we provide an overview of each principle.

### Robust assurance

We have an established approach to internal controls and related assurance. We operate a ‘three lines of defence model’ which distinguishes between first line processes and controls, second line oversight and third line independent assurance.

**Table 1: Three lines of defence model**

Line	Functions	Purpose	Typical activities
1a	<i>Business operations:</i> Wholesale operations, Customer teams.	Responsible for the delivery of service and performance.	<ul style="list-style-type: none"> <li>• Provision of source information.</li> </ul>
1b	<i>Embedded first line:</i> Wholesale planning and performance, Retail planning and performance.	Responsible for the reporting of performance.	<ul style="list-style-type: none"> <li>• Reporting of performance information.</li> <li>• Defining and documenting methodologies and processes.</li> <li>• Quality checks and reviews.</li> </ul>
2	<i>Oversight functions:</i> Chief Engineers Office, Finance, Regulation, General Counsel.	Define policy and provide assurance.	<ul style="list-style-type: none"> <li>• Development of assurance framework.</li> <li>• Quality checks and reviews of systems and controls.</li> </ul>
3	<i>Independent assurance:</i> Internal Audit, external assurance providers.	Provide independent challenge of levels of assurance provided by first and second line.	<ul style="list-style-type: none"> <li>• Review methodologies and processes.</li> <li>• Review application of methodologies and</li> </ul>

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- processes and ultimate integrity of the data.
  - Review completeness and appropriateness of assurance framework (Internal Audit).
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Assurance is a year round activity for us. First and second line activities are on-going, continuous processes that are undertaken throughout the year. For areas identified as higher risk, or where we have specific reporting obligations (eg financial accounts), we employ external third line assurance at relevant points during the year, much of which is brought together and culminates in our year-end financial and performance reporting.

Section 2.2 sets out where we will employ third line assurance this year (2015/16), and in the light of the risks identified in section 1.

## Ownership and accountability

Strong personal and collective ownership is critical for ensuring the accuracy of information we produce, driving improvements and holding ourselves to account. Regular internal performance reporting to our Executive Committee (weekly and monthly) and Board (at every meeting), and half-yearly performance reporting to the Water Forum reinforces this culture of ownership and accountability. Every year we refresh our compliance framework to ensure that individual accountabilities are assigned to our regulatory and statutory obligations. And we operate a rigorous process of sign-off for our performance data – sign-off by the data owner, the responsible senior manager and finally the accountable director in addition to our Board governance arrangements (see below).

Our three lines of defence assurance model ensures that there is clear separation of accountabilities between those responsible for delivery of a performance commitment or a regulatory/statutory obligation and those responsible for ensuring the integrity of that data. This division is mirrored in our governance arrangements.

## Effective governance

As a publicly listed company we have committed to comply with reporting requirements under the UK Corporate Governance Code, the Transparency Directive and UKLA Listings Rules. Ofwat's June 2014 'Commentary on company governance codes' assessed our governance code as fully meeting its principles.

Our assurance plans provide for governance of our performance commitments and other external reporting with a clear delineation of accountabilities.

- The Board's role is to meet its obligations to the company's stakeholders. It reviews performance in the light of the company's strategic objectives and business plan commitments – ensuring that any necessary corrective action is taken.
- The Board's Audit Committee assists the Board in discharging its responsibilities for the integrity of the company's financial statements, the assessment and effectiveness of internal controls and the effectiveness of internal and external auditors.
- The Board's Disclosure Committee oversees the company's reporting obligations under the Companies Act 2006, the UK Corporate Governance Code and the UKLA Listings, Disclosure and Transparency Rules.
- The Water Forum provides independent external challenge of both our performance against our commitments and the information we provide on it.

## Transparency and public accountability

Since 2008 we have had a Continuous Disclosure and Communications policy. This sets out our commitment to earn the trust of our customers and stakeholders by being open in our communications and performance reporting.

Our communications are based on transparency, integrity, accessibility and timeliness. Each year we publish annual reports and accounts for Severn Trent Plc and Severn Trent Water Ltd and have historically published an annual performance report against our regulatory KPIs for the latter.

This year we will continue to hold ourselves publically to account with the publication of a new annual performance report (which will incorporate Ofwat's reporting requirements). We will also publish a report specifically tailored to our customers.



## 2.2 Assurance plan 2015/16: in detail

*In this section we set out our assurance plan for 2015/16.*

We have not detailed every assurance activity that we carry out during the year, particularly using first and second lines of defence, but rather focused on the key areas of risk identified in section 1 as well as where we have established third-line assurance processes (for example, audit of statutory accounts) that we will continue.

Some of the activities are already underway or have been completed. In particular, we made a decision as we developed our business plan in 2013/14, in discussion with the Water Forum, that our 45 performance commitments should be a priority area for a high degree of assurance. This was 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;
- our investors can make decisions as to whether to invest in our company based on the performance data we provide – we have a fiduciary duty to accurately report how we are performing; and
- we are just one of three companies that are able to apply some of the financial ODIs during the 2015-20 period (before our full plan is completed) – 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.

In recognition of these risks, rather than undertake a risk assessment to target specific performance commitments for greater assurance, we have already undertaken third line assurance during the first half of 2015/16 to review our methodologies, documented processes, and their application. We reported the outcome of this half-year assessment both internally to our Audit Committee and externally to the Water Forum. It will be used to target the further third line assurance – 'deep dives' - we employ during the second half of 2015/16 and at the financial year end.

**Table 2: Established assurance processes**

Area	Reason for inclusion	Overview of activity
Charges scheme	We have established processes to ensure that our scheme of charges and principal statement are consistent with charging principles and our revenue caps.	<ul style="list-style-type: none"><li>• External third line assurance of tariffs model and application.</li><li>• External third line assurance of data inputs and application of charging principles.</li><li>• External third line review for 'margin squeeze'.</li></ul>

<b>Statutory and regulatory accounts</b>	The continuation of established processes to audit our accounts in line with statutory and regulatory requirements.	<ul style="list-style-type: none"> <li>• External third line audit of accounts in line with agreed procedures.</li> </ul>
<b>Access prices</b>	This is an established process. Input data is updated each year to produce indicative access prices.	<ul style="list-style-type: none"> <li>• External third line review of inputs.</li> </ul>

**Table 3: Third line assurance processes for 2015/16 driven by statement of risks, strengths and weaknesses**

<b>Area</b>	<b>Reason for inclusion</b>	<b>Overview of activity</b>
<b>Performance commitments and ODIs</b>	In our own assessment, and in our stakeholders' view, all performance commitments are a priority area given the immaturity/complexity of some performance commitments and the potential impact on customers, environment and market confidence. Third line assurance is undertaken at both half and full year (to identify any issues well in advance of final end of year reporting). Further 'deep dives' may be applied to areas of greater risk identified at half-year review and during the year.	<ul style="list-style-type: none"> <li>• External third line review of methodology.</li> <li>• External third line face to face review of methodology application.</li> <li>• External review of reported performance figures.</li> <li>• Additional deep dives into key customer priorities and emerging areas of process risk from half-year review.</li> </ul>
<b>Annual performance report</b>	This report is the principal way that we will document our annual performance and hold ourselves publicly to account. The report will include inputs from other areas covered by this assurance plan (e.g. financial accounts) and require some forecasts of performance. We are also aiming to include the indicative impact of our performance against ODIs on average bills. It is important that we present information in a fair and balanced way that is accessible to our broad range of customers and stakeholders.	<ul style="list-style-type: none"> <li>• External third line assurance of data, performance forecasts (and methodologies) and the presentation of information.</li> <li>• Water Forum review of the presentation and dissemination of information.</li> </ul>
<b>Cost allocation and segmental reporting</b>	Although Ofwat were satisfied with the additional information on cost allocation we provided in response to a query on our business plan, and subsequent regulatory accounts submissions, with the pending introduction of greater competition and a scheduled non-household default tariff review in 2016, we want to ensure retailers and our customers can continue to have confidence about the costs that are reflected in their charges.	<ul style="list-style-type: none"> <li>• External third line review of methodologies and application of regulatory accounting guidelines 2 and 5.</li> </ul>
<b>Preparations for non-household competition (Water Act 2014)</b>	Failure to demonstrate readiness and compliance with a level playing field could have a significant impact on customers, market confidence and competition. New reporting requirements (letters of assurance) will be required from companies in order to provide assurance to market stakeholders.	<ul style="list-style-type: none"> <li>• External third line assurance of programme plan, resources, and management of delivery risks.</li> </ul>

<b>Drinking water quality performance</b>	We recognised in our 2014/15 Annual Report and Accounts the need to place a greater focus in this area and provide stakeholder assurances that operational and performance improvements are being made.	<ul style="list-style-type: none"> <li>• Creation of 'cleanest water' improvement programme.</li> <li>• Internal audit third line assurance of programme plan, resources, and management of delivery risks.</li> </ul>
<b>Voluntary reporting on developer services</b>	Given that this a new voluntary reporting requirement introduced in 2014/15 and our statutory duties are changing (following the Water Act 2014), this will be an area of focus for our assurance plans.	<ul style="list-style-type: none"> <li>• Internal Audit third line assurance of reporting processes and methodology.</li> </ul>
<b>Strategic casework</b>	Ofwat currently has one strategic case about Severn Trent open regarding sewerage provision in Derbyshire. Its inclusion in this plan reflects our commitment to find a satisfactory resolution for all parties.	<ul style="list-style-type: none"> <li>• Escalated senior manager to case manage reaching a resolution (second line). Regular reporting to executive on action being taken.</li> </ul>

## Any questions?

If you have any questions about our assurance plans, you can contact us at:

[future.consultation@severntrent.co.uk](mailto:future.consultation@severntrent.co.uk)

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