

A14: Initial assessment of business plans pro forma

This appendix summarises where and how our plan evidences Ofwat's initial assessment of business plan tests.

IAP test area		Questions	Where is this addressed in the business plan?	Additional information/ explanation
Engaging customers	EC 1	What is the quality of the company's customer engagement and participation and how well is it incorporated into the company's business plan and ongoing business operations?	Our approach to engagement is in Chapter 6 , a summary of what we learned (in the context of the PCs we're proposing) is in chapters 10-18 , and we explain our approach to engagement (and the outcome in full) in Appendix A1 . Finally, the Water Forum (CCG) gives its view in its report.	Our plan starts with people. Drawing on our largest, and most in-depth programme of insight to date, we've first worked to better understand what's really important to our customers. Our plan has been built to meet these needs, so the outcome of our engagement is embedded throughout.
Addressing affordability and vulnerability	AV 1	How well has the company demonstrated that its bills are affordable and value for money for the 2020-25 period?	We summarise our approach to affordability in Chapter 7 (Section 7.1) . We explain the changes in customers' bills, including balancing the interests of customers today and tomorrow, and customers' acceptability rating of our plan in Chapter 10 and Chapter 22 (Section 22.1) . Appendix A2 sets out our approach in full. The Water Forum gives its view in its report.	While we offer the lowest average household bills in England, this is just one way we can tackle the much wider issue of affordability. We've developed six levers using customer insight to focus on affordability for all, long-term affordability and acute affordability issues. As a multi-faceted approach, we explain how we're using these levers in different areas of our plan.
	AV 2	How well has the company demonstrated that its bills will be affordable and value for money beyond 2025?	We consider the balance of benefits between current and future customers in the context of the financial levers we've used, and the overall balance of risk in our plan, in Chapter 22 (Section 22.2) . Our engagement about real options is in Appendix A8 (Section 8.3) . Our proposed balance of charges over time using CPIH is in chapters 10 and 22 .	Our research has covered intergenerational fairness with the results feeding into our plan throughout - including the financing levers we've used and the profile of bills we're proposing. In addition, to manage future uncertainties, we're using a real options mechanism to ensure customers only pay where the need is demonstrated.
	AV 3	To what extent has the company demonstrated that it has appropriate assistance options in place for those struggling, or at risk of struggling, to pay?	We summarise our overall approach to affordability in Chapter 7 (Section 7.1) . We explain our support options for customers' who may already be struggling to pay, or at risk of falling into debt, in Chapter 14 (Section 14.2 and 14.3) . Appendix A2 sets out our end-to-end affordability approach. The Water Forum gives its view in its report.	Building on our current assistance options, during 2020-25 we'll: make our current options more effective; introduce new support options (to better reflect our customers' circumstances); and improve how we identify those who may be in need or at risk of falling into debt.

	AV 4	To what extent does the company identify and provide accessible support for customers in circumstances that make them vulnerable, including proposing a bespoke performance commitment related to vulnerability?	We summarise our overall approach to vulnerability in Chapter 7 (Section 7.2) . We explain how we're better tailoring our service to meet the different needs of our customers, including a new performance commitment in Chapter 14 (Section 14.4 - 14.6) . Appendix A2 sets out our end-to-end vulnerability approach. The Water Forum gives its view in its report.	In-depth customer research, and expert stakeholder challenge, underpin our eight-point plan which includes a more tailored service offering and better ways to identify customers that may benefit from it. Our bespoke performance commitment - supporting our priority service customers during an incident - has been developed with the Water Forum.
Delivering outcomes for customers	OC 1	How appropriate, well-evidenced and stretching are the company's proposed performance commitments and service levels?	We explain our approach to designing PCs in Chapter 9 . Chapters 10-17 show our PCs in the context of customer engagement, our track record and future plans. Our approach, the outcome and our updated PC definitions are included in Appendix A3 . The Water Forum gives its view in its report.	We've developed a package of performance commitments that span the service we deliver across different time horizons. We've developed a framework with the Water Forum to demonstrate that we've built in an appropriate level of stretch. Our ambition is demonstrated throughout our plan.
	OC 2	How appropriate and well-evidenced is the company's package of outcome delivery incentives?	We explain our approach to designing ODIs in Chapter 9 , and go into more detail in Appendix A4 . We explain how our ODIs work with our real options mechanism in Appendix 8 . The Water Forum gives its view in its report.	We've worked with the Water Forum to triangulate a range of customer valuations to determine incentive rates. Encouraged by customer support, our approach seeks to further build on the potential of incentives, by making more of our revenue - and therefore customers' bills - dependent on performance.
	OC 3	How appropriate is the company's focus on service performance in its risk/return package?	We explain our ODIs in the context of overall risk and return in Chapter 22 (Section 22.6) and Appendix A11 .	We've calibrated our incentives to ensure service performance represents the main contribution to RoRE, with a significantly higher downside risk than at PR14, and more stretching targets. This strongly places the onus on us to find new and innovative ways to deliver significant service improvements for our customers.
Securing long-term resilience	LR 1	How well has the company used the best available evidence to objectively assess and prioritise the diverse range of risks and consequences of disruptions to its systems and services, and engaged effectively with customers on its assessment of these risks and consequences?	We draw together our overall approach to 'resilience in the round' in Chapter 8 . Chapters 10-18 explain our approach to resilience in the context of the outcomes we're delivering. We discuss operational resilience, including managing supply/demand in more detail in our enhancement business cases in Appendix A8 . Our customer engagement approach is covered in Chapter 6 , and Appendix A1 .	We've considered resilience not only as a subject in its own right (Chapter 8), but also a means to an end (securing service for customers today and in the future). It is therefore considered in several places throughout our plan. In terms of customer engagement, we've used the unique perspective we gained at PR14 to shape our deliberative research to gather informed opinions on resilience, risks and impacts from our customers.

	LR 2	How well has the company objectively assessed the full range of mitigation options and selected the solutions that represent the best value for money over the long term, and has support from customers?	Our overall approach is explained in Chapter 8 . Appendix A8 has more detail on operational resilience and our approach to risk assessment, Appendix A11 has more detail on the scenarios run regarding financial resilience, and Appendix A12 has more detail on our approach to assurance. The Water Forum has scrutinised our strategic investment proposals and gives its view in its report.	Our strategic investment cases in Appendix 8 - particularly relating to the resilience of our water service - explain how we've built on the experience of our Birmingham Resilience Programme by taking a systems risk approach, and considered different mitigation options in response.
Targeted controls, markets and Innovation	CMI 1	How well does the company's business plan demonstrate that it has the right culture for innovation which enables it, through its systems, processes and people, to deliver results for customers and the environment from innovation?	Chapter 21 explains the framework, governance and funding we use for innovation. Chapters 10-18 summarise case-studies in the context of the outcomes innovation is helping to deliver. Appendix A7 include fuller case studies relevant to the types of innovation that Ofwat considered in its Spark! webcasts.	We've considered innovation not only as a subject in its own right (Chapter 21), but also a means to an end (delivering better outcomes and value). It is therefore considered in several places throughout our plan.
	CMI 2	2. How well does the company use and engage with markets to deliver greater efficiency and innovation and to enhance resilience in the provision of water and wastewater services to secure value for customers, the environment and the wider economy; and to support ambitious performance for the 2020-25 period and over the longer term?	Chapter 21 explains our overall approach to markets. Chapters 11,12 and 16 include more information on markets in the context of the outcomes they're helping to deliver. Appendix A6 provides more detail on the frameworks we've used to assess the potential of water trading and direct procurement for customers.	As with innovation, we've considered markets not only as a subject in their own right (Chapter 21), but also a means to an end (delivering better outcomes and value). In Appendix A8 we provide more detail on the frameworks we've used to assess the potential of different opportunities to deliver better value for our customers.
	CMI 3	To what extent has the company set out a well evidenced long-term strategy for securing resilient and sustainable water resources, considering a twin track approach of supply-side and demand-side options and integrating third party options where appropriate, to meet the needs of customers and the environment in the 2020-25 period and over the longer term?	Chapter 21 explains our overall approach and how we're proposing to use DPC. Chapter 12 includes information on water trading in the context of the outcomes it is helping to deliver. Appendix A6 includes further detail and the frameworks we've used. Appendix A8 explains how we've created a new 'real options mechanism' to protect customers from uncertainty around climate change, and how we propose to progress options for an North-West to South-East interconnector.	Our plan reflects our final Water Resource Management Plan, which itself responds to stakeholder responses to the draft that was published earlier this summer. Our statement of response will be published alongside our PR19 Plan, and will confirm our continued approach of ambitious demand-side targets and supply-side enhancements. We've also developed real options to protect customers from future uncertainty and an approach which could make inter-regional water trading a practical reality.

	CMI 4	To what extent does the company have a well-evidenced long-term strategy for delivering bioresources services, integrating an assessment of the value from the delivery of bioresources services by third parties for the 2020-25 period and over the longer term?	Chapter 21 explains our overall approach to markets. Chapter 16 summarises the role of trading bioresources in the context of our wider wastewater plans. Appendix A6 includes our fuller bioresources strategy.	We're supportive of the development of the bioresources market and have already begun trialling trades with Yorkshire Water. Our strategy explains how we propose to use our strong position on costs to deliver greater value not only to our customers but those of neighbouring companies.
	CMI 5	How appropriate is the company's proposed pre-2020 RCV allocation between water resources and water network plus – and, if relevant, between bioresources and wastewater network plus – taking into account the guidance and/or feedback we have provided?	Appendix A6 explains our RCV allocations for both water resources and bioresources, and how we've responded to Ofwat feedback.	We've updated our RCV allocation for both water resources and bioresources, building on feedback received and further challenging our own approach to ensure we have followed a robust process. All changes are transparently explained in Appendix 6.
	CMI 6	To what extent has the company produced a bid assessment framework for water resources, demand management and leakage services that demonstrates a clear commitment to the key procurement principles of transparency, equality/non-discrimination and proportionality and the best practice recommendations?	Appendix A6 provides more detail on our bid assessment frameworks. Appendix A8 explains how we've created a new, 'real options mechanism' to protect customers from any uncertainty associated with climate change in our long-term water resources planning.	We're committed to ensuring our water resources procurement process is transparent and non-discriminatory, and to create a level playing field against which all bids are measured. This ensures third parties are not disadvantaged. Our water resource procurement governance comprises three key components: market information (portal); bid assessment framework; and a trading and procurement code.
	CMI 7	5. To what extent has the company clearly demonstrated that it has considered whether all relevant projects are technically suitable for direct procurement for customers? Where it has one or more such projects, to what extent has the company provided a well-reasoned and well-evidenced value for money assessment supporting its decision on whether or not to take forward each technically suitable project using direct procurement for customers?	Chapter 21 and Appendix A6 explain our approach to DPC.	We've developed a transparent, repeatable framework using specialist external advice. We've used this to assess which major projects would create better value for customers if they were delivered through DPC. Our assessment has identified that using DPC for one new supply scheme could result in increased benefits for customers compared to our in-house approach - so we're pursuing an early tender process, going to the market for innovative solutions to test the appetite for DPC.

Securing cost efficiency	CE 1	How well evidenced, efficient and challenging are the company's forecasts of wholesale water expenditure, including water resources costs?	Chapter 20 provides an overview of how we've approached costs in our plan and the outcome of our benchmarking. Appendix 8 provides further detail.	We've a proven track record in delivering sustainable efficiency. Efficiency comes from finding new ways of doing things, making the right risk-based decisions and using commercial expertise drawn from other sectors. We've also responded to the challenge shown through a wide range of benchmarking.
	CE 2	How well evidenced, efficient and challenging are the company's forecasts of wholesale wastewater expenditure, including bioresources costs?	Chapter 20 provides an overview of how we've approached costs in our plan and the outcome of our benchmarking. Appendix 8 provides further detail.	Our plan includes 13% efficiency for wholesale. We've responded to the benchmarking we've undertaken, including reflecting a greater than expected opportunity for efficiency in wastewater, given our sector position.
	CE 3	How well evidenced, efficient and challenging are the company's forecasts of retail expenditure, including bad debt costs?	Chapter 20 provides an overview of how we've approached costs in our plan and the outcome of industry-wide benchmarking.	Our plan builds on our current track record of managing costs to serve with a further efficiency of around 10%. Despite a strong comparative performance on bad debt, we've embraced the outcome of Ofwat's cross-sector benchmarking and are introducing a range of new initiatives to tackle bad debt.
	CE 4	To what extent are cost adjustment claims used only where prudent and appropriate, and where they are used, are cost adjustments well evidenced, efficient and challenging?	Appendix 8 provides detailed cases for our proposed cost adjustment claims.	We've used our understanding of the PR19 cost models to identify four areas where adjustments may be required. For each of these areas we've challenged the need, optioneering and costs. Our Board, as well as stakeholders and customers, have been sighted on challenges and the emerging solutions for over two years.
Aligning risk and return	RR 1	Has the company based the separate costs of capital that underpin each of its wholesale price controls, and the net margin(s) that underpins its retail price control(s), on those we state in our early view? If not, to what extent has the company robustly justified, in terms of benefits for customers, its proposed costs of capital and retail margin(s) within the context of expected market conditions for 2020-25?	Chapter 22 explains our overall approach to financing with further detail by control in Appendix A11 .	Our plan assumes a Weighted Average Cost of Capital and retail margin levels that are in line with Ofwat's early view as set out in its December 2017 Final Methodology.

	RR 2	To what extent has the company demonstrated a clear understanding and assessment of the potential risks in its RoRE assessment, including the effect of the risk management measures it will have in place, across each of the price controls?	Chapter 22 summarises our RoRE assessment, while Appendix 11 provides further detail of ODI RoRE ranges by price control.	We've calculated RoRE ranges (with the P10 to P90 ranges developed using monte carlo analysis) for totex, new debt, ODIs and revenue levers to understand the impact of potential deviations. For each area we've considered risks and set out how we plan to manage and mitigate them, using past experience where appropriate.
	RR 3	Has the Board provided a clear statement that its plan is financeable on both an actual and a notional basis? Is the statement appropriate and how robust is the supporting evidence?	Chapter 2 comprises the Board's statement, Chapter 22 explains that our plan is financeable, while Appendix 11 explains in further detail our assessment of financeability which evidenced the Board's statement.	Our plan is financeable at the appointee level on a notional company basis after account is taken of our ODI rewards from AMP6, and on the basis of actual structure. We've also assessed financeability at control level to assess the extent to which charges are balanced between controls.
	RR 4	How appropriate are the company's PAYG and RCV run-off rates? How well evidenced are they, including that they are consistent with customers' expectations, both now and in the longer term?	Chapter 22 summarises our approach and the outcome of our customer engagement. Appendix 11 provides further detail and Appendix 1 explains how we engaged customers.	We've been guided by three principles - each generation of customers should pay its fair share; bills should be stable over time; and the balance of charges over time should enable us to maintain a stable platform for investment - to explore the use of financeability levers to balance charges over time in customer research. 88% of customers supported the balance we're proposing.
Accounting for past delivery	PD 1	How well has the company given evidence for its proposed reconciliations for the 2015-20 period, and has it proposed adjustments by following the PR14 reconciliation rulebook methodology?	Chapter 19 summarises our forecast position to the end of the AMP and Appendix A5 provides a fuller reconciliation.	We've followed the PR14 reconciliation rulebook methodology. We provided supporting evidence in July, including detailed information on the impacts of the licence variation, a detailed update on our Birmingham Resilience Programme and forecast performance for the remainder of the 2015-20 period.
	PD 2	How well has the company performed, and is forecast to perform, over the 2015-20 period and, taking into account this overall performance, how well has it put measures in place to ensure that it maintains confidence that it can successfully deliver its PR19 business plan?	Chapter 19 summarises our forecast position to the end of the AMP and Appendix A5 provides a fuller reconciliation. Chapters 10-17 provide more detail on our track record against our existing performance commitments and future delivery plans.	We've transparently explained our track record in our Annual Performance Reports, including drivers of performance, comparative data, Water Forum feedback and clarifications following Ofwat queries. We've scrutinised planned improvements to ensure alignment and appropriate resource allocation. We've been open about our latest forecasts, including impacts on submitted data.

Securing confidence and assurance	CA 1	To what extent has the company's full Board provided comprehensive assurance to demonstrate that all the elements add up to a business plan that is high quality and deliverable, and that it has challenged management to ensure this is the case?	Chapter 2 comprises the Board's statement. Chapter 23 summarises the basis on which the Board has made its statement and Appendix A12 provides more detail on the outcome of assurance undertaken.	Our Board has signed its compliance statement, underpinned by a bespoke, risk-based approach that took into account the specific nature of risks associated with developing business plans. The approach we developed contained four key components: a bottom-up risk assessment; a top-down Board statement; assurance allocation aligned to risk; and oversight through robust governance.
	CA 2	To what extent has the company's full Board been able to demonstrate that its governance and assurance processes will deliver operational, financial and corporate resilience over the next control period and the long term?	Chapter 2 comprises the Board's statement. Chapters 8 and 23 describe the Board's governance and assurance processes in relation to resilience. Appendix A11 explains the different scenarios that the Board has considered as part of its stress-testing.	Within our plan we've sought to give a rounded view of how we identify and manage risks. For example, producing a seven-year viability statement; focusing on skills development; and building on a systems view of operational risk; a greater focus on catchment management and managing flood risks; while also recognising we need to embed the lessons learned from the recent freeze/thaw event.
	CA 3	To what extent has the company's full Board provided assurance that the company's business plan will enable customers' trust and confidence, through appropriate measures to provide a fair balance between customers and investors (which include outperformance sharing, dividend policies and any performance related element of executive pay) and high levels of transparency and engagement, on issues that matter to customers (which extends to their ability to understand corporate and financial structures and how they relate to its long-term resilience)?	Chapter 2 comprises the Board's statement. Chapter 18 explains our dividend policy, including the introduction of a new community dividend, our approach to executive remuneration, and commitment to engagement and reporting on this issues that are important to customers. Chapter 22 provides more detail on how we've balanced the interests of customers and investors.	Our new outcome 'a company you can trust' focuses on four pillars: our Board's leadership and governance (and their commitment to acting fairly to all our stakeholders); our culture, values, and behaviours; engaging with our customers (to build a stronger mutual understanding of each other); and aligning incentives for investors, customers and our people. It concludes with the proof of our intent - that everyone receives their fair share of our success. While we've not created any performance commitments for this outcome, we've instead have created a new community dividend.

	CA 4	To what extent has the company's full Board provided comprehensive assurance to demonstrate that the business plan will deliver – and that the Board will monitor delivery of – its outcomes (which should meet relevant statutory requirements and licence obligations and take account of the UK and Welsh Governments' strategic policy statements)?	Chapter 2 comprises the Board's statement. Chapter 23 summarises the basis on which the Board has made its statement and Appendix A12 provides more detail on the outcome of assurance undertaken. Chapter 5 summarises where we've taken into account our stakeholders' requirements and guidance in our plan.	Our plan builds on our established processes, including our bi-annual 'licence to operate' assessment which is the principal basis on which the Board signs its annual compliance statement, together with our 'three lines of assurance' approach that is used for data reporting.
	CA 5	To what extent does the company have a good track record of producing high-quality data, taking into account the company's data submission, assurance process and statement of high quality, and our 2018 assessment of the company under the company monitoring framework?	Chapter 23 explains our track record of reporting and how we've responded to Ofwat feedback on the Company Monitoring Framework (CMF).	Over the last decade we've worked to continuously improve our assurance approach and we actively review Ofwat's feedback and reassess areas noted as requiring improvement. We were pleased this resulted in our 'assurance plan' being recognised as 'exceeds expectations' over the last two years. We've also responded to Ofwat's feedback from its assessments, for example, by publishing a group structure on our website.
	CA 6	How consistent, accurate and assured are the company's PR19 business plan tables, including the allocation of costs between business units, information on corporation tax, and the assurance and commentary provided?	Chapter 2 comprises the Board's statement. Chapter 23 summarises the basis on which the Board has made its statement. Appendix A12 provides more detail on the outcome of that assurance.	Our assurance framework included face to face training sessions to over 100 colleagues, a standard set of assurance templates and sign-off processes for second line assurance. Approvals were subsequently tracked by our compliance team and reviewed by our third line assurers to ensure all areas had received appropriate scrutiny and sign off.