

November 2016

Trust in water

# Company monitoring framework

2016 assessment

Individual company report – Severn Trent Water Ltd

[www.ofwat.gov.uk](http://www.ofwat.gov.uk)

ofwat

## Company monitoring framework assessment

This document outlines the results of our 2016 company monitoring framework (CMF) assessment of Severn Trent Water's assurance. It includes a summary of our assessment, and further information on the exercises we undertook to assess Severn Trent Water's assurance, and our findings.

In the context of our CMF, in order to be in the self-assurance category, we were looking for leading edge companies to meet the high standards of assurance that stakeholders expect. As well as providing clear, transparent and accurate data, we expect companies to present their information in a way that stakeholders can engage with. We were looking for companies who can demonstrate a successful and positive approach to stakeholder engagement, including in their approach to developing their assurance plans where appropriate. Transparency about company structures, procedures and decision-making processes is another important area of focus that helps companies to earn their stakeholders' trust and confidence.

Further information on this year's assessment is available in our ['Company monitoring framework 2016 assessment'](#) publication. The framework itself is available in our ['Company monitoring framework final position'](#), published in June 2015.

### Summary of our assessment

The company has exceeded our expectations on three of our eleven assessment areas - outcomes, assurance plan and the data assurance summary.

Severn Trent Water has met our expectations in all but one of the remainder where we have identified a minor concern with its approach to providing information on casework. There has been an improving trend on how the company has responded to our information requests on casework. We therefore do not consider that this minor concern impacts on our overall assessment of the company's performance on assurance.

Within the context of the CMF, in practice we are looking for leading edge performance, in which the company consistently meets the high standards expected, to support upgrading a company from 'targeted' with strong performance across the board – our approach to assessing this required that data and wider assurance 'meets expectations' in most if not all assessments, with examples of 'exceeds expectations' and good practice.

---

Severn Trent Water's performance fits this requirement, **we have decided to change Severn Trent Water's assurance status to 'self-assurance'**.

In this document we have set out a brief summary of the individual assessments that we undertook as part of our Company Monitoring Framework (CMF) assessment in 2016. The remainder of this document provides brief feedback on the company's performance against each of our eleven assessment areas for this year:

<b>Our view</b>	<b>Assessment</b>
Meets expectations	Financial monitoring framework
Meets expectations	Charges schemes assurance
Meets expectations	Financial information
Meets expectations	Final 2010-15 reconciliation data submission
Exceeds expectations	Outcomes
Meets expectations	Compliance with principles of board leadership, transparency and governance
Meets expectations	Risk & compliance statement
Exceeds expectations	Assurance plan
Meets expectations	Targeted reviews
Exceeds expectations	Data assurance summary
Minor Concerns	Evidence from casework activities

## Results of each assessment exercise

### 1.1 Financial monitoring framework

#### What we were looking for

In this assessment we looked at how the companies had followed our financial monitoring framework guidance. Our assessment focused on the quality of financial information published in the annual performance report, the transparency of disclosures and consistency of financial metric data published.

This is an area where companies' data assurance is particularly important, and companies need to ensure that the information that they publish is in line with the guidance provided by Ofwat. This enables Ofwat, and other stakeholders, to be confident that the information that each company publishes has been prepared on a consistent basis and allows meaningful comparisons to be made between companies.

---

## What we found

Our review identified that there is a minor unreconciled difference between the net debt figures disclosed and the borrowings figures shown on the balance sheet. The difference is not considered to be significant in the context of this assessment (and the overall assessment).

Our assessment: **meets expectations**

## 1.2 Charges schemes assurance

### What we were looking for

Companies must publish their forward charges schemes in February each year. We checked that companies:

- published and assured their charges schemes;
- complied with our charging rules;
- assessed and explained significant movements in charges
- devised and put into effect effective handling strategies to address significant movement in charges.

This is an important assessment, because our charging rules are designed to protect customers through stable, transparent and predictable charging, in the absence of competition.

### What we found

Overall the company demonstrated that it followed our guidance, and the quality of data and the transparency of the published information met our expectations. It provided evidence on incidence effects and associated handling strategies.

Our assessment: **meets expectations**

---

## 1.3 Financial information

### What we were looking for

In this assessment we looked for an absence of omissions or errors, where the companies reported their actual performance and to compare aspects of this performance to the assumptions made at the PR14 final determination. We did not look at all areas but chose four key risk areas to look at this year which were:

- wholesale total expenditure reporting;
- revenue and profit statements, disaggregated by price control;
- methodology statement on how costs are allocated across the price controls; and
- disclosures required for transactions with non-regulated associate companies.

We developed a log of the issues, errors and inconsistencies we uncovered as part of our analysis. We assessed the nature and number of issues identified to form a view on the quality of assurance in each company's published financial information.

This is an area where companies' data assurance is important, because a range of stakeholders will use this information and rely on its accuracy. It also informs important preparatory work for PR19.

### What we found

We identified no negative issues during our review of the four areas we chose to look at this year. We have noted data inconsistencies between the published Annual performance report and the tables submitted to us, but these inconsistencies were relatively minor weaknesses in the context of this assessment (and the overall assessment).

Our assessment: **meets expectations**

## 1.4 Final 2010-15 reconciliation data submission

### What we were looking for

In this assessment we assessed companies' adherence to our guidance ([IN15/17](#), December 2015) covering assurance, data and commentary requirements. Our

---

guidance covered a range of requirements including data table completion, explanatory requirements, supporting evidence and board signoff.

This is an important area for companies' data assurance, because the submission is used to update the final reconciliation of the PR09 incentive arrangements for the 2010-15 period which directly impact the companies' revenue allowances they can recover from customers.

## What we found

Overall we have no concerns with the assurance of the final 2010-15 reconciliation submission. The company met our expectations for the submission in respect of all the elements that are relevant to the company.

We noted minor data ambiguities in and across tables which when queried were easily corrected and we considered them to be in part a consequence of interpreting our guidance in a not unreasonable way. However there was insufficient level of detail provided in the initial commentary to allow us to assess serviceability and change protocol. Consequently we raised a number of queries seeking to clarify our understanding of the information provided in the submission which the company resolved proactively to our satisfaction.

Our assessment: **meets expectations**

## 1.5 Outcomes

### What we were looking for

In this assessment we looked for:

- reliable, timely and appropriate information for customers and other stakeholders;
  - transparent and accessible information for customers and other stakeholders;
  - appropriate data assurance;
  - evidence that the company has listened and responded to its customers and other stakeholders; and
  - compliance with the outcome delivery and reporting proposals as set out in the PR14 final determination company-specific appendix.
-

This is an important assessment, to ensure that stakeholders can understand what companies are doing to deliver the outcomes that customers expect.

## **What we found**

Severn Trent Water provided accurate, reliable information in table 3A (outcome performance) and its annual reporting commentary.

There is comprehensive evidence that the company's reporting is transparent and accessible to customers and other stakeholders. The performance information in the 'Annual Performance Report 2015-16', 'Annual Performance Report 2015-16 - a summary for our customers' and 'Assurance summary 2015-16' is relevant, easy to understand and well sign-posted. Where the company has not met its committed performance levels or Jacobs, the company's independent technical assurer, identified concerns or weaknesses the company has provided a clear explanation of the issue. Where appropriate, the company has provided an explanation of how it will be rectified.

There is very clear evidence that the company has been transparent with customers and stakeholders about the data assurance that has been put in place. Jacobs has provided assurance over the performance commitments and associated outcome development incentives. Based on their feedback, all performance commitments in the 'Annual Performance Report 2015-16' underwent independent technical assurance at both the half and full financial year. The 'Assurance summary 2015-16' includes the outcome of this assurance. These documents are available to view/download from the company's website. This is evidence that the company has carefully considered how to be transparent with customers and stakeholders about the data assurance that they have put in place.

There is sufficient evidence that the company has provided the wider assurance to demonstrate it is listening to customers and delivering the services they want and can afford. For example, at both the half and full financial year, the company's Water Forum challenged the delivery of performance commitments in line with the PR14 final determination.

There is sufficient evidence that the company is implementing its proposals for outcome delivery and reporting as set out in the PR14 final determination company-specific appendix. The 'Annual Performance Report 2015-16' and 'Assurance Summary 2015-16' both contribute to the explanation of how the company's approach is being followed.

---

Our assessment: **exceeds expectations**

## **1.6 Compliance with principles of board leadership, transparency and governance**

### **What we were looking for**

In this assessment we looked for how the information which the company provided demonstrated that it has met our board leadership transparency and governance principles. This included the provision of:

- transparent governance information, including group structure and on director remuneration;
- evidence that the board of the regulated company has full control over the company, including its long-term strategy, and is fully focused on its obligations; and
- clear information on the composition of the board and its sub-committees.

This is an important assessment, designed to give stakeholders trust and confidence that the company is structured appropriately and transparently, and complies with its legal obligations.

### **What we found**

The information provided in the company's annual reporting has demonstrated that it has met all our board leadership transparency and governance principles.

Our assessment: **meets expectations**

## **1.7 Risk & compliance statement**

### **What we were looking for**

In this assessment we looked for a statement, explicitly endorsed by the company's board, which confirms that the company has complied with all its relevant statutory, licence and regulatory obligations and is taking appropriate steps to manage and/or mitigate any risks it faces.

---

This assessment is designed to give stakeholders trust and confidence in companies' approach to compliance and risk management. The statement is intended to facilitate a company-led approach to compliance.

## What we found

The company has provided a clear statement that it has complied with all its relevant statutory, licence and regulatory obligations and is taking appropriate steps to manage and/or mitigate any risks it faces. However, the statement is only signed by the chief executive (for and on behalf of the board) and therefore it may not be sufficiently clear to all stakeholders that it has the endorsement of the whole board. Additional sign off by an independent member of the board could help add legitimacy for stakeholders.

Our assessment: **meets expectations**

## 1.8 Assurance plan

### What we were looking for

In this assessment we looked for the following in companies' assurance plans.

- Explanation of the framework and their approach to it.
- Evidence of stakeholder engagement undertaken to develop the plan.
- Clear scope, and rationale for targeting specific areas.
- Appropriate language and accessibility for all stakeholders.

This is a key test of whether companies are listening to their stakeholders and using their views to improve their practices.

### What we found

The assurance plan clearly sets out context and work done to date which demonstrates good stakeholder engagement, highlighting where the company has amended its draft plan as a result of feedback. The plan clearly explains the company's approach and explains/justifies where risks lie and where the resulting assurance should be targeted. We are supportive of the company's approach to further enhance future reporting for stakeholders. The risk assessment undertaken

---

was thorough and the scope of information considered was sufficiently wide. The assurance plan transparently details how the framework has been applied, with a good summary of approach covering internal and external assurance.

Our assessment: **exceeds expectations**

## 1.9 Targeted reviews

### What we were looking for

In this assessment we looked at:

- companies' tax reconciliation notes published in the annual performance report to see if they acted on our tax targeted review recommendations; and
- improvements companies have made to 2015-16 reporting in response to our sludge and water resources targeted review.

These are two areas we have recently highlighted for companies to focus on, and we want to see evidence that they are taking steps to improve their assurance.

### What we found

The quality of the published tax reconciliation note was acceptable overall but a clearer explanation of variances in a narrative format would have been helpful as the capital allowances comment was unclear.

The company's published cost allocation methodology statement clearly set out the changes made for 2015-16 reporting as a result of the CEPA recommendations made following our targeted review of sludge and water resources.

Our assessment: **meets expectations**

## 1.10 Data assurance summary

### What we were looking for

We checked that companies have:

---

- published a data assurance summary for 2015-16 activities;
- covered the targeted areas from the company's assurance plan; and
- provided an overview of the company's assurance methods and processes, the audit exercises carried out and their findings.

This assessment is designed to ensure that companies provide accessible assurance to stakeholders, to build trust and confidence in their data publications.

## What we found

The company published a succinct and comprehensive summary of the data assurance carried out throughout the year. The data assurance summary takes the reader through assurance process and links to previous documents published. There is good coverage of all areas targeted in the assurance plan with a short summary of work performed and issues found in each area. It also covers other assurance activities in 2015-16 beyond the annual performance report and recognises learnings and considers their impact for future assurance plans.

The data assurance summary is written as a self-standing document that is easy to read. Though the data assurance summary is not prominent on the company's website pages, it does appear in the search results when searching "data assurance".

Our assessment: **exceeds expectations**

## 1.11 Casework

### What we were looking for

In this assessment we looked at companies' responses to cases from 1 April 2015 onwards. We considered the company's response to our requests for information. We checked that companies had provided complete, accurate information within our timescales, and engaged effectively with us.

This assessment focused on our trust and confidence in companies' information provision, and complemented the other assessments that focused on information published by companies.

---

## What we found

We have opened one case concerning Severn Trent Water since April 2015 and this is a trade effluent appeal. This case is currently open and as we have not requested any information from Severn Trent Water we have not included this case in our assessment. We also opened two cases concerning Severn Trent Water before April 2015. One of those cases is a dispute under section 94 of the Water Industry Act 1991 (the Act) and is still open. In this case, prior to a senior member of Severn Trent Water staff taking over the case, the information provided by Severn Trent Water was inconsistent, not provided in a timely manner and did not provide us with certainty that we could rely on that information to progress our investigation. Since November 2015, the quality of the information has increased and we have had no further issues. We also opened a determination under section 45 of the Act in December 2014, which has subsequently been closed, and we had no issues with the information that was provided in that case. Overall, we consider Severn Trent Water could have scored “serious concerns” if the poor actions prior to November 2015 had continued or an “exceeds expectations” if Severn Trent Water had acted as it did post November 2015 for the entirety of the year.

Our assessment: **minor concerns**

---