11 July 2017

Trust in water

Delivering Water 2020: consultation on PR19 methodology
Appendix 14: Initial assessment of business plans

Appendix to chapter 14: The initial assessment of business plans: securing high quality, ambition and innovation

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1. Summary

The initial assessment of business plans is our process to assess company business plans. We want companies to produce high-quality, ambitious and innovative business plans, pushing forward the performance of the sector as a whole and stretching the boundaries for delivery and efficiency. This will ultimately lead to benefits for customers, the environment and wider society.

In Chapter 14 of our PR19 methodology consultation document we set out what we aim to achieve with the initial assessment of business plans, the proposed process and how we will incentivise companies. We intend to use procedural, reputational and financial incentives to get all companies to produce well-evidenced and efficient plans, and the best companies to push the frontier for all companies.

In this document we set out:

- our reasons for proposing four categories;
- the tests we will use to assess business plans;
- the proposed schedule for the initial assessment of business plans.

We have published a draft pro forma alongside the PR19 methodology consultation document which we expect companies to submit with their business plans, which will highlight where information relevant to each question can be found in the company's business plan. A high-quality business plan should be easy to navigate and this pro forma will aid the assessment process.

Table 1 Summary Box – PR19 proposals for the implementation of the initial assessment of business plans

Proposal topic		**Our thinking and proposals**
Overall approach to the initial assessment of business plans	Test areas (covered in **Chapter 14**)	We propose to test company business plans in nine key areas: • Engaging customers • Addressing affordability and vulnerability • Delivering outcomes for customers • Securing long-term resilience • Targeted controls, markets and innovation • Securing cost efficiency • Aligning risk and return • Accounting for past delivery • Securing confidence and assurance

	Business plan characteristics (covered in **Chapter 14**)	We propose to assess against three key characteristics: • high quality • ambition • innovation
	Categorising business plans (covered in **Chapter 14**)	We propose to categorise companies into four categories: • exceptional • fast track • slow track • significant scrutiny
	Incentives **(covered in Chapter 14)**	We propose to incentivise companies through a range of incentives which can be: • financial • procedural • reputational
Assessing innovation capability (covered in **Chapter 14**)		We want to assess that companies are able to innovate as demonstrated through their business plans.
Test areas: questions and what we will look for **(covered in this appendix)**		Against each of the nine test areas, we set out key questions and what we will be looking for in terms of high quality, ambition and innovation.
Scoring business plans into categories: requirements and expectations **(covered in this appendix)**		Our starting assumption will be that all plans require significant scrutiny until shown otherwise. It is up to companies to demonstrate, through their business plan, that they can move up in terms of their categorisation. Where company business plans score well against our tests, the plan will move up through our categories. A plan will stay in the significant scrutiny category if it falls well short of what is needed to score well against a broad range of tests Slow track status will be given to plans where material interventions are required in some areas to protect the interests of customers. In order to move out of slow-track, the plan must be of high quality, requiring no material interventions from us. The threshold to progress to fast-track should be high. To move from fast-track to exceptional status, companies will need to demonstrate that they have a high-quality business plan with significant ambition and innovation for customers.
Schedule for initial assessment of business plans **(covered in this appendix)**		For PR19, we intend to make the initial assessment of business plans, and the associated categorisation of companies, a "one-shot" process for water companies. We intend to publish: • our categorisation decisions in January 2019; companies will have 'one shot' at this; • draft determinations for exceptional and fast-track companies in March/April 2019, and • draft determinations for slow-track and significant scrutiny companies in July 2019.

2. Rationale for proposed business plan categories

2.1 Why categorise companies' business plans?

The objective of the initial assessment is to incentivise companies to produce high-quality, ambitious and innovative business plans. It will enable us to focus our challenge and scrutiny of companies' business plans where it is most needed – and where we can deliver the greatest benefits for current and future customers, the environment and wider society.

We propose using the initial assessment of business plans to categorise companies' plans based on their quality, ambition and innovation. This will give companies clear incentives to produce high-quality business plans that will achieve good outcomes for their customers, wider society and the environment.

2.2 The categories we propose to put business plans in

In chapter 14: The initial assessment of business plans: securing high quality, ambition and innovation we set out that we propose to use four categories for the initial assessment of business plans:

- **Exceptional** status will be awarded to plans that are high quality with significant ambition and innovation for customers. These plans will receive reputational, procedural and financial benefits.
- **Fast-track** status will be given to plans that are high quality and do not require material intervention to protect customer interests, but which are not ambitious or innovative enough to attain exceptional status. These plans will receive reputational and procedural benefits.
- **Slow-track** status will be given to plans where material interventions are required in some areas to protect the interests of customers. Companies may be required to resubmit some of their business plan or to provide additional evidence. There is a reputational and procedural impact of being in this category.
- **Significant scrutiny** status will be given to plans which fall well short of the required quality and where material interventions are required to protect the interest of customers. This may include expecting companies to substantially rework these plans. Companies whose plans fall into this category will require increased ongoing regulatory scrutiny and assurance. These plans will incur reputational and procedural disadvantages, reduced cost sharing rates, and potentially capped ODI rewards. We may put extra measures in place to protect

customers from risks associated with poor business planning. These companies may also be subject to strengthened reporting requirements.

As set out directly below, we consider that using four categories and associated incentives will produce the best balance between incentivising all companies to improve their plans, and running an effective price review process across all companies. For more information about the incentives for these categories please see chapter 14.

2.3 The options we considered for testing and categorising business plans

At the 2014 price review (PR14), our methodology focused our scrutiny and challenge on areas where it was most needed, and where we could deliver the greatest benefits for current and future customers, the environment and wider society. We did this by assessing the quality of companies' business plans using a risk-based review. The risk-based review set a number of tests. As a result of the scores from those tests, some companies substantially reworked their plans before we could reach a final determination.

At the 2019 price review (PR19), we have built on the lessons and successes of the risk-based review. We have renamed the process to better reflect its relationship to the overall price review, and to reflect the differences from the approach taken in PR14. Our objective is to use the initial assessment of business plans to encourage a step change in performance across all companies.

We considered whether the initial assessment of business plans should focus on incentivising improved quality; or quality and ambition; or quality, ambition and innovation. High-quality business plans which are also ambitious and innovative will stretch the boundaries for efficiency and delivery. Incentivising high-quality, ambitious and innovative plans will encourage all companies to push themselves to go further than in the past. There is also a disincentive at the bottom end.

At PR14, we originally intended to use three categories: resubmit, standard and enhanced. However, when we came to review business plan submissions, we only used the standard and enhanced categories.

We considered how many categories would give companies optimal incentives to produce high-quality, ambitious and innovative business plans. We do not consider that two categories would enable us to incentivise companies sufficiently to up their game, or to submit high-quality, ambitious and innovative business plans.

Having three categories (as originally proposed in PR14) would enable us to differentiate between poor and reasonable quality plans, but not between high-quality plans and ambitious and innovative ones. We consider this an important part of encouraging all companies to improve the quality of their business plans, and to drive innovation to achieve better outcomes for customers.

We considered a fifth category for plans which are ambitious and innovative, but which cannot initially be assessed as high quality. This would align with the recommendations of the PwC report[1]. However, we decided against this for two reasons.

First, we do not want to give companies financial rewards for ambition and innovation if their business plans do not give us confidence they will be able to achieve this ambition. Second, adding a fifth category (and hence another boundary) would unnecessarily complicate the process with limited (if any) benefit. Thirdly, we note that as the incentive package for ambitious and innovative plans are weighted to delivery via the ODI and cost sharing incentives and that these benefits could be earned by company who deliver ambitious and innovative plan, which is not high quality.

We therefore conclude that four categories gives the right balance between practicality and incentives across companies at all levels of performance.

At PR19, we consider it possible to categorise companies robustly into more categories by setting out clearly in advance how we will use relative and absolute tests to categorise business plans (table 14.2).

We considered whether there was a different way to assess the business plans, other than applying a set of tests, but we did not find a robust alternative. We do, however, propose a different set of tests this time. These are aligned to the key themes of PR19.

We investigated different ways to group the tests, and consider that the selected groupings allow us to identify which tests are important to each category. We also sought to minimise the total number of tests we require to reach an informed

[1] PwC, 'Refining the balance of incentives for PR19', June 2017

decision and achieve our objectives. A limited number of tests will make the results of the initial assessment of business plans easier to communicate.

Our experience at PR14 also showed the difficulty of categorising components of business plans individually, and so for PR19 we will apply categorisations to the business plan ‘in the round’.

3. Tests we will use to assess business plans

3.1 Test areas

In chapter 14, we explained that setting out a framework of tests will give companies a clear indication of our assessment expectations and priorities. The framework also breaks down the assessment into manageable portions, allowing us to carry out the initial assessment of business plans effectively within the limited time available.

In chapter 14, we propose that there are nine test areas in the initial assessment of business plans:

- Engaging customers
- Addressing affordability and vulnerability
- Delivering outcomes for customers
- Securing long-term resilience
- Targeted controls, markets and innovation
- Securing cost efficiency
- Aligning risk and return
- Accounting for past delivery
- Securing confidence and assurance

We determined these test areas by considering how the initial assessment of business plans incorporates and reflects the UK Government draft strategic priorities and Welsh Government policies and draft objectives for the water sector, and can best deliver the PR19 themes:

- great customer service that shows real innovation, reliability and responsiveness, to match the experience that customers get from the best companies in other sectors;
- affordable bills that offer value for money;
- long-term resilience – meaning resilience ‘in the round’, building on our resilience framework; and
- innovation and new ways of doing things.

Some of the test areas will directly relate to specific themes, such as past delivery addressing great customer service, while other tests (such as markets and innovation) will address aspects of a number of the themes.

3.2 What we will look for in each test area

We have set out in table 14.2 the focus of each test area. We have also developed a draft set of questions we propose to help us assess business plans’ performance against each test area. The aims of the individual questions are discussed in each chapter of our PR19 methodology consultation document.

We have considered what criteria could be used for each of the test areas in reaching our decision on categorisation – this information is indicative but not exhaustive. Some of the potential criteria within each test area will be absolute, but many will be relative to the monopoly companies and other service providers in the sector and, where possible, to comparators outside the water sector.

Table 2 Proposed focus, test questions and what we will look for when scoring plans against the tests

Test area	Focus	Questions	High quality, ambition and innovation	Link to associated chapters
Engaging customers	The quality of the company's customer engagement, including its approach to customer participation How well the company's customer engagement has been reflected across its business plan	1. What is the quality of the company's customer engagement and participation and how well is it incorporated into the company's proposals?	**In a high-quality plan:** The company will demonstrate real leadership on customer engagement and customer participation. The company will provide strong evidence that it has effectively addressed the principles of good customer engagement, including evidence from its CCG. The company will demonstrate, with evidence, that it has effectively taken forward the themes of customer participation, including evidence from its CCG. The company will show that it has engaged effectively with customers on longer-term issues such as resilience, and taken into account the needs and requirements of future customers. **In an ambitious and innovative plan:** The company will demonstrate sector-leading approaches to customer participation in the creation of its business plans and in its delivery.	Engaging customers: Chapter 2
Addressing affordability and vulnerability	Whether a company's plan is affordable and offers value for money, both for PR19 and over the longer term, including for those who are struggling or are at risk of struggling to pay. How the company is supporting customers in	1. How well has the company demonstrated that its bills are affordable and value for money for the 2020-25 period? 2. How well has the company demonstrated that its bills will be affordable and value for money beyond 2025? 3. To what extent has the company demonstrated that it has	**In a high-quality plan:** The company's approach to affordability will be based on high-quality customer engagement. This is supported by strong evidence, including well-informed customer support for the affordability of the plan and appropriate range of alternatives and the views of the customer challenge group (CCG). The company's approach to affordability for those struggling to pay will be highly efficient. This is supported by strong evidence, for example, a cost–	Addressing affordability and vulnerability: Chapter 3 Securing cost efficiency: Chapter 9

Test area	Focus	Questions	High quality, ambition and innovation	Link to associated chapters
	circumstances that make them vulnerable by providing sensitive, well-designed and flexible support and services.	appropriate assistance options in place for those struggling, or at risk of struggling, to pay? 4. To what extent does the company identify and provide support for customers in circumstances that make them vulnerable, including proposing a bespoke performance commitment related to vulnerability?	benefit analysis of a company's social tariff, demonstrating that the company has taken the most cost efficient approach. The company will take a high-quality approach to supporting customers in circumstances which might make them vulnerable. This approach will bring about a step change in accessibility and support for these customers. It will be targeted, efficient and effective. This should be supported by strong evidence, including the views of the CCG. The company will adopt a high-quality bespoke performance commitment on its approach to supporting customers in circumstances which might make them vulnerable. **In an ambitious and innovative plan:** The company will innovate to deliver a plan which leads the sector in delivering affordability for all customers as well as for customers struggling to pay and for customers in circumstances which might make them vulnerable.	Engaging customers: Chapter 2
Delivering outcomes for customers	How appropriate, stretching and well-evidenced the company's performance commitments and outcomes delivery incentives (ODIs) are Whether the company's business plan demonstrates an	1. How appropriate, well-evidenced and stretching are the company's proposed performance commitments and service levels? 2. How appropriate and well-evidenced is the company's package of outcome delivery incentives? 3. Does the company show appropriate focus on service	**In a high-quality plan:** All the company's performance commitments will be set at stretching levels, including for leakage and water efficiency. These should be supported by high-quality evidence that the performance commitments are both stretching. The company will take a robust, stretching approach to developing its bespoke performance commitments and service levels. The company's approach should be supported by high-quality evidence, including	Delivering outcomes for customers: Chapter 4

Test area	Focus	Questions	High quality, ambition and innovation	Link to associated chapters
	appropriate focus on service performance	performance in its risk/reward package?	CCG support for the effectiveness of its customer engagement. The company will propose a robust package of ODIs to incentivise itself to deliver on its performance commitments to customers. This approach should use reputational and financial outcome delivery incentives grounded in customer research. The company's overall risk and reward package will focus strongly on service delivery. **In an ambitious and innovative plan:** The company will propose innovative and sector-leading performance commitments with stretching levels and an ODI incentive package which supports outstanding achievement and innovation as well as protecting customers against the risk of delivery failure. The company will present high-quality evidence on its plans to achieve exceptional service performance.	
Securing long-term resilience	The company's approach to organisation-wide resilience management, including managing uncertainties and any interconnected risk across the full range of systems and services underpinning outcomes delivery	1. How well has the company used the best available evidence to objectively assess and prioritise the risks and consequences of disruptions to its systems and services and engaged effectively with customers on the risks and consequences? 2. How well has the company objectively assessed the full range of mitigation options and chosen the interventions that represent	**In a high-quality plan:** The company will take an organisation-wide, integrated approach to appraising risks to resilience. It should support this with strong evidence that takes suitably long-term views and uses a range of forward-looking appraisal techniques across key service areas. The company will effectively engage with customers on resilience in the round, including providing accurate and high-quality comparative data to facilitate informed choices.	Securing long-term resilience: Chapter 5 Targeted controls, markets and innovation: wholesale controls: Chapter 6

Test area	Focus	Questions	High quality, ambition and innovation	Link to associated chapters
	Whether the company's proposed intervention/outcomes are consistent with the principles of good resilience as set out in chapter 5 and our September 2017 'Resilience expectations' document	best-value for money over the long term, and support from customers?	The company will use innovative approaches to the appraisal of risks to resilience. These will be supported by sophisticated and global best practice techniques to understand and appraise uncertainty across the full range of pressures, from acute shocks to longer term chronic stresses. It should also consider hazards and threats, such as cyber security, flooding and disruptions to energy supplies. The company will include cross-references to changes in operational risk and planned levels of service, supported by strong evidence. The company will thoroughly appraise options for mitigating resilience. It will present a full range of options as evidence that the plan will deliver the best value long-term options for customers. This will include utilising options beyond its boundary to mitigate risks in its own area (and also looking beyond its boundary to understand how it can support long-term resilience elsewhere). **In an ambitious and innovative plan:** The company will present strong evidence that its innovative approaches will deliver sector-leading operational resilience. It will be expected that the company will include the role of partnership, use of markets, catchment management and other softer option in combination with fixed asset based solutions.	Targeted controls, markets and innovation: retail controls: Chapter 8
Targeted controls,	Whether and how companies will use innovation to deliver more efficient costs	1. How well does the company's business plan demonstrate that it is able, through its systems, processes and people, to deliver	**In a high-quality plan:** The company will show it is capable of using innovation to deliver for customers, the environment	Targeted controls, markets and innovation:

Test area	Focus	Questions	High quality, ambition and innovation	Link to associated chapters
markets and innovation	and/or improved service levels Whether companies are making the best use of markets to deliver resilient and affordable services in the interest of customers	results for customers and the environment from innovation? 2. How well has the company used markets to drive efficient costs and harness innovation? 3. To what extent has the company set out a well evidenced long-term strategy for delivering resilient water resources, integrating an assessment of the value of third party options (both supply- and demand-side), to help deliver future water needs for the 2020-25 period and over the longer term? 4. To what extent does the company have a well evidenced long-term strategy for bioresources, integrating an assessment for delivery of bioresources services by third parties for the 2020-25 period and over the longer term? 5. Has the company (appointee[2]) clearly demonstrated that it has considered all relevant projects for	and wider society – including details of plans, systems and processes, and people needed to support innovation. The company will maximise effective use of markets to harness innovation and reveal information about efficient cost of service. The company will present a robust strategy for meeting water resource and bioresources needs now and in the future, having assessed the opportunities for third party providers to help deliver outcomes in a resilient and affordable manner. The company will actively and effectively consider third-party delivery options for water resources and bioresources for both this review period and the longer term. Strong evidence to support this should include details of third party engagement, a strategy for maximising the use of third party resources where it is economic to do so, and (for companies in England) to demonstrate an understanding of how the future bilateral market for water resources will affect future supply requirements. Water resources companies will also be required to produce a high-quality bid assessment framework to provide clarity to third parties on bidding arrangements.	wholesale controls: Chapter 6 Targeted controls, markets and innovation: direct procurement for customers: Chapter 7 Targeted controls, markets and innovation: retail controls: Chapter 8 The initial assessment of business plans: Chapter 14

[2] We use the term ‘appointee’ in *Chapter 7: Targeted controls, markets and innovation: direct procurement for customers* for water only companies and water and wastewater companies.

Test area	Focus	Questions	High quality, ambition and innovation	Link to associated chapters
		direct procurement for customers, and has it provided a well-reasoned value for money analysis to support its decisions about whether or not to take forward any of these projects using direct procurement for customers? 6. 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 any feedback we have provided?	The company will explain how its governance and management will be aligned to implement separate price controls and facilitate the development of new resource markets. The company will take a high-quality approach to direct procurement, supported by a value for money assessment where appropriate. It will have considered this approach for potentially qualifying projects. As a minimum, the company should consider our expectations around potential project types and how we expect companies to appraise potential projects, as outlined in our methodology document. The company should include transparent, well evidenced and acceptable proposals on pre-2020 RCV allocation. **In an ambitious and innovative plan:** In its appraisal of the options, the company will demonstrate innovative and sector leading strategies for delivering water resource and bioresources services, aligned with the use of third party options. The company will have a sector leading strategy and plan (supported by strong evidence) for delivering qualifying projects through direct procurement for customers, where value for money assessment indicates a direct procurement approach will provide value for customers. The company will have an explicit plan for delivering customer value through innovation. To maximise the value for customers, this plan should include the	

Test area	Focus	Questions	High quality, ambition and innovation	Link to associated chapters
			company sharing innovation learning across the sector and more widely.	
Securing cost efficiency	Cost efficiencies across the different controls (wholesale and retail) Whether the company raised well evidenced and efficient cost adjustment claims and only where appropriate	1. How well evidenced, efficient and challenging are the company's forecasts of wholesale water expenditure, including water resources costs? 2. How well evidenced, efficient and challenging are the company's forecasts of wholesale wastewater expenditure, including bioresources costs? 3. How well evidenced, efficient and challenging are the company's forecasts of retail expenditure, including doubtful debt costs? 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?	**In a high-quality plan:** The company will submit an efficient level of total expenditure in all areas. The company will have an effective approach to managing and reducing doubtful debt and improving revenue recovery. This will include identifying current barriers to revenue recovery, benchmarking with best practice outside the sector and how these barriers will be addressed in PR19. The company will avoid cost adjustment claims where possible, including by taking account of offsetting favourable circumstances. Where the company raised claims, they are efficient and well evidenced. **In an ambitious and innovative plan:** The company will present strong evidence of sector-leading cost efficiency.	Securing cost efficiency: Chapter 9
Aligning risk and return	The company's costs of capital and retail margins The company's assessment and management of risk and uncertainty	1. Has the company based the separate costs of capital that underpin each of its wholesale price controls, and the margin that underpins its retail price control(s), on those we stated in our methodology statement? If not, has the company robustly justified,	**In a high-quality plan:** Where business plans are underpinned by a different **cost of capital or retail margin**, we expect to see clear and compelling evidence to justify why it should be different within the context of expected market conditions for 2020-25. We expect the company will have a clear understanding of the risks that could affect delivery of	Aligning risk and return: Chapter 10 Aligning risk and return: financeability: Chapter 11

Test area	Focus	Questions	High quality, ambition and innovation	Link to associated chapters
	Whether the plan is financeable on both an actual and a notional basis Whether the proposed pay as you go (PAYG) and regulatory capital value (RCV) run-off rates are well justified	for customers, its proposed costs of capital and retail margin(s) within the context of expected market conditions for 2020-25? 2. How clearly has the company understood and assessed the potential risks and shown evidence of the risk management measures it will have in place across each of the price controls? 3. Has the Board provided a clear statement, with appropriate supporting evidence, that its plan is financeable on both an actual and a notional basis? 4. How appropriate are the company's PAYG and RCV run-off rates? How well evidenced are these, including whether they are consistent with customers' expectations both now and in the longer-term?	the plan, and that it has appropriate management practices in place to manage the impacts of risks should they arise. It will provide strong evidence of the scenario analysis it has undertaken. The company will provide strong evidence that: • PAYG and RCV run-off rates are based on the underlying economic assessment of the proposed expenditure; • subsequent adjustments, made to smooth bills or address financeability or affordability constraints, are well justified and consistent with notional approach to financing; and • the rates represent an appropriate balance between the interests of current and future customers, will not result in undue bill volatility and protect customer interests in the short and the long term. When assessing that the plan is financeable on both a notional and an actual basis, we will take into account: • the statement given by each company's Board as to why they consider the plan to be financeable for both the notional and the actual capital structure; • the level of credit rating that the company has targeted for the notional company, and the reasons why the company considers that level appropriate; and	

Test area	Focus	Questions	High quality, ambition and innovation	Link to associated chapters
			• the company's financial metrics and other evidence provided to support the selected credit rating.	
Accounting for past delivery	How well evidenced the proposed reconciliations for the 2015-20 period are How achievable the plans are, taking into account levels of past performance	1. How well has the company given evidence of its proposed reconciliations for the 2015-20 period, and whether it has proposed adjustments by following the PR14 reconciliation rulebook methodology? 2. How well has the company delivered its business plan to customers over the 2015-20 period, and how well has it engaged with its customers on its performance?	**In a high-quality plan:** The company will provide high-quality information to justify its performance forecast for the last two years of the 2015-20 period. The company will present strong evidence that it has engaged well with customers to explain its performance, the outcome of reconciliations and proposals for adjustments in the 2020-25 price controls. The company will present strong evidence that its proposals for adjustments in the 2020-25 price controls are well supported by customers and the CCG. The company has a robust approach to delivering its business plan taking into account its performance over the 2015-20 period.	Accounting for past delivery: Chapter 12
Securing confidence and assurance	Whether the company and its Board has provided assurance that the business plan is of high quality, provided ownership of the overall strategy and direction of the plan in the long term	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 has challenged management to ensure this is the case?	**In a high-quality plan:** The company's Board will provide assurance, supported by appropriate evidence that the business plan is of high quality and has been challenged accordingly. The Board will provide assurance that that the company has identified relevant operational, financial and corporate risks and taken a balanced approach to managing them.	Securing long-term resilience: Chapter 5 Aligning risk and return: financeability: Chapter 11

Test area	Focus	Questions	High quality, ambition and innovation	Link to associated chapters
	and will meet its current and future obligations Whether the data in the plan has been subject to strong assurance processes to ensure it is consistent and accurate	2. To what extent has the company's full Board been able to demonstrate that its governance and assurance processes provide operational, financial and corporate resilience over the control period and long term? 3. To what extent has the company's full Board provided comprehensive assurance to demonstrate that the business plan will deliver and monitor delivery of its outcomes (which should meet relevant statutory requirements and licence obligations and take account of the UK and Welsh Government strategic policy statements)? 4. 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 assessment of the company against the 2018 company monitoring framework? 5. How consistent, accurate and assured are the company's PR19 business plan tables including the allocation of costs between business units, information on	The company's plan will provide assurance that it will deliver and monitor delivery of its outcomes, meet relevant statutory requirements and licence obligations and take account of the UK and Welsh Government strategic policy statements. The company will provide a high-quality data submission, including evidence of the assurance process. This should demonstrate how it has addressed issues identified in previous company monitoring framework (CMF) assessments to the extent they are relevant to the business plan. The company's PR19 business table submission – including the allocation of costs between business units, assurance of the tables and any commentary on the tables will be consistent, accurate and assured.	Securing confidence and assurance: Chapter 13

Test area	Focus	Questions	High quality, ambition and innovation	Link to associated chapters
		corporation tax, and the assurance and commentary provided?		

3.3 Scoring into business plan categories: requirements and expectations

The companies are monopolies. We face asymmetry of information – we know less about their businesses than they do – when assessing their business plans. Therefore our starting assumption will be that all plans require significant scrutiny until shown otherwise. It is up to companies to demonstrate through their business plan that they should move up to a higher category. Where company business plans score well against our tests, the plan will move up through our categories.

A plan will stay in the **significant scrutiny** category if it falls well short of what is needed to score well against a broad range of tests. Our assessment will take account of both the number of tests failed and the extent of failure. A plan under significant scrutiny is one which is not high enough quality and which has significant flaws. It fails to give us confidence that it will deliver good outcomes for customers. The quality of data, customer engagement and assurance may be sufficiently poor as to not provide a satisfactory basis for making a draft determination. For example a plan with performance commitments which have weak evidence and justification including of customer support and where the performance commitment levels are well below stretching levels. Another example would be a plan which is outside the cost thresholds for most or all price controls and well outside the cost threshold for at least one control, with no robust explanation and poorly evidenced special cost factor claims.

We do not expect that any plans will be assigned to the significant scrutiny category at the end of our initial assessment of business plans process. However, if we do see a plan that does not meet the quality necessary to achieve a higher category, then we will use this category.

A plan in **slow-track** will be one where material interventions are required in some areas to protect the interests of customers. In order to move out of slow-track, the plan must be of high quality, requiring no material interventions from us. The threshold to progress to **fast-track** should be high. The broad range of tests and the requirement for a company to have efficient costs and stretching outcomes is likely to mean that a significant proportion of companies remain in the slow-track category. For fast-track companies, we would not expect to make material interventions on behalf of customers. We might make limited and minor interventions, including for limited non-material or technical failures in the plan.

To move from fast-track to **exceptional** status, companies will need to demonstrate that they have a high-quality, ambitious and innovative business plan. We intend exceptional status to be achievable only by a small number of the most ambitious and innovative companies (compared to their peers). We do not consider it necessary for any company to be given exceptional status, if none is deemed to have submitted a plan sufficiently ambitious and innovative to differentiate them clearly from others.

It is important that there are both relative and absolute measures of ambition and innovation. Due to the relative aspect, we do not want to predetermine what ambition or innovation would be sufficient to be assigned the exceptional category; this would reduce the incentive for companies to stretch themselves and innovate.

4. The schedule for the initial assessment of business plans: a "one-shot" approach

For PR19, we intend to make the initial assessment of business plans, and the associated categorisation of companies, a "one-shot" process for water companies. As we confirmed in May 2016 companies will be required to submit business plans by 3 September 2018. The business plan submitted by 3 September 2018 should and will be reviewed as the final version for the purposes of the initial assessment of business plans and the associated categorisation. During the initial period after receipt of the business plans we will review the plans and submit queries of clarification to companies. After this short period we will limit the interaction between Ofwat and water companies on business plans until we have reached our decision on the initial assessment of business plans.

In January 2019 (after a period of approximately 4 months) we intend to announce the outcome of our assessment, setting out the category that we have assigned to each business plan. We intend to publish our detailed internal methodology for the initial assessment of business plans after the January 2019 categorisation announcement.

Depending on the number of exceptional and fast-tracked business plans, we intend to announce at this point whether these companies' draft determinations will be made in March/April 2019. We intend that slow-tracked and significant scrutiny companies will receive their draft determinations in July 2019.

Figure 1 PR19 timeline

2017	
11 July	PR19 draft methodology consultation published
July-August	Continued engagement through consultation period
30 August	PR19 draft methodology consultation closes
Mid December	Final PR19 methodology published
2018	
3 September	Companies submit business plans to Ofwat
2019	
January	Initial assessment of business plans published
March/April	Draft determinations (exceptional and fast track plans)
April	Companies submit revisions to business plans (significant scrutiny and slow track)
July	Draft determinations (Slow track and significant scrutiny)
December	Final determinations published

5. Consultation questions

Q1. Do you agree with the key questions under each of the test areas?

Q2. Do you agree with what we will look for in terms of high quality, ambition and innovation under each of the test areas?

Q3. Do you agree with our high-level approach for scoring business plans into the four categories (significant scrutiny, slow-track, fast-track, exceptional)?

Q4. Do you agree with our proposed schedule for the initial assessment of business plans?