

January 2019

Trust in water

Company monitoring framework: 2018 assessment Individual company report – South Staffs Water

Company monitoring framework assessment

This document outlines the results of our 2018 company monitoring framework assessment of South Staffs Water's assurance. It includes a summary of our assessment, and explains how we assess the company's assurance, and our findings.

In the company monitoring framework (CMF), we are looking for evidence that companies are meeting the high standards of assurance that stakeholders expect. We consider whether companies are providing clear, transparent and accurate data, and we assess the way companies present information to customers and other stakeholders. We also look at how transparent companies are in explaining, company structures, decision-making processes or any performance issues. For 2018 we also considered under the company monitoring framework data quality and consistency in company business plans submitted as part of the price review.

Further information on this year's assessment is available in our '[Company monitoring framework 2018 assessment](#)' publication. The framework is available in our '[Company monitoring framework final position paper](#)', which we updated in June 2018.

Summary of our assessment

Considering the issues in the round, **we have retained South Staffs Water in the 'targeted' assurance category.**

We have looked at how well the company has performed against the expectations we have set for each of our assessments, including whether they have:

- met or exceeded our expectations by a clear margin,
- demonstrated leading edge behaviour, and
- displayed behaviours that could lead to a reduction in trust and confidence.

We have also considered any other issues or information relevant to the confidence that can be placed in the company's information in making our overall assessment.

The company has met our expectations in six assessment areas and exceeded our expectations in one area (outcomes). However, we had minor concerns in three areas (cost assessment, water resources management plan and market information and business plan data consistency) and serious concerns in one area, charges

engagement, where the company's new connections charging document lacked transparency as it did not describe what charges would be incurred for what purposes and did not contain details of many of the charges required under our rules.

We consider that, looking at the company's performance in the round, these concerns are not sufficient to demote the company to prescribed status. Therefore we have retained the company in the targeted assurance category for 2018.

Results of our assessment

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

Overall the company has met our expectations in relation to financial monitoring. South Staffs Water has followed our guidance, and the quality of data and the transparency of the published information met our expectations in many areas. However, we had to request that the company provide more complete information on how the sale of their business retail business had been reflected in their Return on Regulatory Equity (RORE) calculation. This was addressed by the company in a second query response. There were also a number of minor clarification queries raised. These clarification queries were not assessed to have had an impact on the overall confidence in the information presented.

Our assessment: **meets expectations**

1.2 Charges engagement

What we were looking for

We have to date issued three sets of charging rules: Charges Scheme Rules; Wholesale Charging Rules; and Charging Rules for New Connection Services (English Undertakers). Each of these ‘charging rules’ require companies to publish a document in which they set out their charges relating to these rules. Their publications are charges schemes, charges schedules and charging arrangements respectively.

For this assessment, we focus on how well companies have engaged with their stakeholders about their charges and charging policies through their publications and actual interactions. We based our assessment primarily on the documents that the charging rules require companies to publish or submit to us, as per [IN17/09](#), including but not limited to:

- the published charging documents;
- Board assurance statements;
- assurance of companies’ engagement on and publication of charges information, where appropriate under the charging rules;
- the information companies provide in their Statement of Significant Changes (if applicable); and
- the handling strategies companies devise and put in place to address significant changes to charges.

Where we considered it appropriate, we supplemented the information by submitting queries to some companies, looking more widely at material published on company websites, and cross-checking against customers’ and stakeholders’ comments or complaints on charging.

This year our assessment has included new connection services charging rules for companies wholly or mainly in England, which came into force in April 2018, for the first time.

What we found

We had serious concerns regarding the company's communication of its charges to its customers in its new connections charging arrangements. The document did not contain many of the relevant charges that the company is required to publish under our rules. Instead, many were listed simply as 'POA' (which we presume means 'price on application', but the document itself did not define this acronym).

The arrangements also lacked textual descriptions of what charges would be incurred for what purposes. Two worked examples were provided, but these were virtually identical and of limited assistance. The arrangements did not take account of varying levels of expertise, and the charges were not published in a way that customers could work out a reasonable estimate of charges incurred. They were also difficult to find on the company's website.

We have discussed these issues with the company and are content that the company intends to address them.

The company published separate assurance statements for each of its charging schemes. The new connections assurance statement was in a different place on the company's website to the other documents and was difficult to find. The assurance statements were quite brief. It was helpful that the new connections statement set out an explanation of how the relevant charging rules had been complied with.

Our assessment: **serious concerns**

1.3 Outcomes

What we were looking for

We want to ensure that stakeholders understand company performance to deliver the outcomes that the company committed to deliver at PR14. This year our assessment focused on the availability and accessibility of published performance data and how that information is communicated to stakeholders. We expect companies to be transparent, provide accessible information for customers and other stakeholders and show that they have listened and responded to their customers and other stakeholders.

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

This year our assessment did not include the quality of companies' *assurance* over published data, in order to avoid duplication with the data consistency and data quality assessments in the initial assessment of company business plans (see sections 1.11 and 1.12).

What we found

South Staffs Water has exceeded our expectations for this assessment because it has published monthly information on the 'Performance dashboard'. This can be accessed using the 'About us' link from the home page. The dashboard provides customers and other stakeholders with easy to understand, up-to-date information about performance and service improvements.

Overall there is clear evidence that the company's reporting is transparent and accessible to customers and other stakeholders. South Staffs Water has published performance information on the 'Our Annual Performance' page of its website; this is accessed using the 'About us' link from the home page. Cambridge Water has published the same report on the 'Our Annual Performance' page of its website; this is accessed using the 'About Us' link on the home page.

The South Staffs Water and Cambridge Water websites both also include a 'Summary Annual Performance Report'. Performance Reports for previous years are available on the South Staffs Water and Cambridge Water websites; they can be accessed from links on the 'Annual Performance' web pages.

Our assessment: **exceeds expectations**

1.4 Water resources management plan and market information

What we were looking for

Companies are required to produce a water resources management plan every five years setting out their approach to maintaining the long-term supply and demand balance in a way that delivers best value for customers and the environment for the next 25 years. We review and provide comments on draft water resource management plans to Defra and the Welsh government, in our capacity as a statutory consultee.

Our assessment in the company monitoring framework considered the quality of the information in companies' draft water resources management plans for the period 2020 to 2025. The assessment considered the quality of data and internal consistency in the plans, the extent to which stakeholders had been involved in the development of the plans, how clearly plans had been communicated to stakeholders and evidence of assurance of the plans. The assessment also considered the quality of the water resources market information published by the company. In that respect, the assessment considered the quality and completeness of the data, the clarity of its presentation and its consistency with the company's draft water resources management plan.

This is the first time that water resources management plans and market information have been included within the company monitoring framework.

What we found

Overall we had minor concerns in this area, principally due to inconsistent and unclear representation of the supply forecast associated with the levels of service considered in the draft plan narrative and planning tables. We raised this in our representations on the draft water resources management plan ([South Staffs Water draft WRMP19 consultation response](#) and [Cambridge Water draft WRMP19 consultation response](#)). We also identified minor concerns with the market information such as an unclear representation of the reasons for zonal constraints.

Our assessment: **minor concerns**

1.5 Long-term Viability Statement

What we were looking for

This assessment focused on the transparency and assurance of companies' long-term financial resilience as set out in their long-term viability statements.

This assessment is important in providing Ofwat and other stakeholders with assurance that companies have the long-term financial resilience to meet the needs of consumers in the long-term.

The assessment considered the extent to which companies have followed our guidance for issuing long term viability statements as set out in [IN18/04](#) and in

particular the approach they have taken to assessing their long-term financial viability. The assessment considers how their long-term financial viability statement linked to their wider risk assessment including mitigating actions, the extent to which companies stress tested their projections, whether they clearly explained their approach and the evidence of assurance over the process.

This is the first time that information on the long-term viability statement has been included as a separate category in the company monitoring framework (last year it was included within the “financial monitoring framework”).

What we found

Overall South Staffs Water has met expectations for the long-term viability statement included in the Annual Performance Report. The directors have provided a statement that they have a reasonable expectation that the company will continue to operate and meet its liabilities as they fall due for a period of seven years to 31 March 2025, clearly setting out the approach to the assessment and the basis for the period reviewed.

The risk management process has been clearly detailed with appropriate mitigation provided for each principal risk. The company has completed stress and scenario testing providing the figures for the key assumptions that have underpinned the tests. There is evidence that the Board has been engaged throughout the long-term viability statement and has considered the impact of the testing on the overall company performance as well as the group structure.

The company has set out the assurance undertaken on the assessment of long-term viability within the statement. It has provided details of the internal audit review, which cross-checked the calculations used. It has also provided evidence that a third party assurer has reviewed the calculations and sensitivities used within the financial projections.

An area where improvement could be made would be to provide a clearer link between the company’s principal risks and the scenario tests as this would provide further assurance that the level of testing was appropriately challenging.

Our assessment: **meets expectations**

1.6 Financial Flows

What we were looking for

The requirement for companies to submit financial flows covering the periods 2015-16, 2016-17 and 2017-18 is one of the key ways in which we are improving the transparency of financial flows to investors.

In our assessment, we focused on companies' compliance with the requirements of [IN18/08](#) in terms of data quality and assurance, as well as how meaningful the data and supporting commentary is to stakeholders.

This is the first time that information on financial flows has been included within the company monitoring framework.

What we found

The company met our expectations in this area. All data tables were complete and the company published its data and provided evidence of external assurance. There were a few errors in the data submission but we do not consider that this had an impact on stakeholder confidence.

Our assessment: **meets expectations**

1.7 Risk & compliance statement

What we were looking for

This assessment is designed to test our confidence in companies' approach to compliance and risk management. The risk and compliance statement is intended to facilitate a company-led approach to compliance.¹

¹ Our findings here, and throughout our company monitoring framework assessment, are without prejudice to any issues that we may investigate under our enforcement powers and subsequently find

Our assessment looks 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 year we have also taken into account relevant information provided in companies' annual reporting to ensure that they are consistent.

What we found

The Board has provided a clear statement confirming that the company has an understanding of, and is meeting, its obligations. It has also confirmed that the company has sufficient processes and internal systems of control to meet those obligations and has systems and processes in place to identify, manage and review its risks. The statement has been appropriately signed off on behalf of the Board.

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 assurance framework and their approach to it;
- evidence of stakeholder engagement undertaken to develop the plan;
- clear scope, and rationale for targeting specific areas; and
- 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.

wanting. It would be inappropriate to pre-empt the outcome of any investigations that might consider whether the assurance provided is indeed appropriate or accurate. Any adverse findings in this respect may be taken into account in future assessments.

What we found

The company's assurance plan met our expectations. It contains a good summary of the company's overall assurance framework and the role of internal and external audit. The context and scope of assurance procedures has been updated from last year. The company has set out clearly changes made in response to our assessment last year, for example financial metrics. The company has produced a detailed update of its risks, strengths and weaknesses and how the assessment has been carried out. The plan provides a detailed list of risk scores for outcome delivery incentives and for other information and how this has been assessed from their consultations with stakeholders. The company has identified five key areas of targeted information and detailed how internal controls will assist in minimising any risk that could occur. Some of the initiatives that the company will undertake such as reporting of key metrics in a consistent way could have been discussed in more detail.

Our assessment: **meets expectations**

1.9 Cost assessment

What we were looking for

Our assessment focused on the assurance of cost assessment data submitted in the annual performance report. The assessment of efficient costs is a key element of setting price controls. We need good quality, consistently reported cost assessment data to do this effectively. This year's assessment considered the completeness and accuracy of the cost assessment data, allocation of costs and assurance over data. It also considered how meaningful the data and supporting commentary is to stakeholders.

This is the first time that cost assessment has been included as a separate category in the company monitoring framework (last year it was included within "wider assurance and information").

What we found

We had minor concerns in this area. All cost assessment tables were complete with no missing data. However, some queries were raised where additional commentary would have been beneficial, and some of these resulted in data changes to several

tables. The accounting separation methodology was available and had been externally assured.

Our assessment: **minor concerns**

1.10 Casework

What we were looking for

This assessment relates to the information that companies provide to us when we engage with them to carry out our investigation and enforcement functions. We looked at companies' responses to cases from 1 April 2017 onwards. We considered companies' responses 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 confidence in companies' information provision, and complemented the other assessments that focused on information published by companies.

What we found

No assessment was made because we did not have any live cases involving South Staffs Water during the assessment period.

Our assessment: **not applicable**

1.11 PR19 Initial assessment of business plans – data consistency

What we were looking for

In September 2018, companies provided us with their business plans for the 2020-25 period. Our initial assessment of business plans tests how companies have met our expectations and requirements for meeting the needs of customers. The initial assessment incentivises companies to submit high quality, ambitious and innovative

business plans. The quality of companies' information, and their track record on assurance are important parts of a high quality business plan.

As set out in our '[Company monitoring framework final position paper](#)', updated in June 2018, we take account of how companies' business plans have performed against our initial assessment tests on data quality and assurance as part of our 2018 company monitoring framework assessment. The relevant parts of the initial assessment tests are: confidence and assurance test 5 which covers data consistency (considered here), and test 6 which covers data quality (covered below). The full scope of test 5 is:

“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?”

In our company monitoring framework assessment we have focused on the elements related to data consistency and not included the initial assessment of business plan element related to the company monitoring framework to avoid double counting.

What we found

We found minor issues overall with the consistency of performance and financial data reported in the company's business plan tables with previous data submissions. This was due to minor inconsistencies between the company's business plan tables and Annual Performance Report in the areas of cost assessment and outcomes. In addition, we identified omissions of actual data and unsupported assumptions in the affordability and vulnerability assessment for outcomes.

Our assessment: **minor concerns**

1.12 PR19 Initial assessment of business plans – data quality

What we were looking for

This section considers confidence and assurance test 6 which looks at:

“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?”

What we found

Overall the business plan provides sufficient and convincing evidence that its PR19 business plan tables including the allocation of costs between business units, information on corporation tax, and the assurance and commentary provided are consistent, accurate and assured. We identified some issues with financial modelling, outcomes and risk and return data tables, but these did not affect our overall confidence in the company’s business plan data quality.

Our assessment: **meets expectations**

1.13 Wider assurance and information

What we were looking for

This assessment considers any information - across a range of publications, regulatory submissions and bilateral engagement - that could potentially impact on confidence in the information produced by companies and that we therefore considered relevant to our overall decision for each company. In carrying out this assessment, we consider the context in which any relevant information was published or shared.

What we found

We found no issues that we considered relevant to our assessment of the company in relation to wider assurance and information this year.

Ofwat (The Water Services Regulation Authority) is a non-ministerial government department. We regulate the water sector in England and Wales. Our vision is to be a trusted and respected regulator, working at the leading edge, challenging ourselves and others to build trust and confidence in water.

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