

Severn Trent Water: Test question assessment

Test area	Overall test area grade	TQ#	Test question	Test question grade	Test question summary assessment
Engaging customers	B	EC1	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?	B	<p>Overall the business plan demonstrates high quality with convincing evidence in the areas set out below, but it is not sufficiently ambitious or innovative to be considered exceptional.</p> <p>The company sets out convincing evidence of the effective use of a wide range of research techniques, including online community research, deliberative workshops, social media scraping, analysis of business as usual customer satisfaction surveys and a range of quantitative research techniques. In many cases, these meet best practice, as evidenced by independent assurance of its approach. However the evidence base which informs its triangulation of customer valuations for use in performance commitments (PCs) and outcome deliver incentives (ODI) is much narrower. Furthermore the company does not provide sufficient detail on the steps it has taken to ensure its customer valuation research was robustly designed and implemented (including the survey design used and extent of testing conducted). While the results of the company's engagement on customer priorities and preferences generally appear to be reflected in its PCs (and the CCG has noted that it has no outstanding challenges) the company provides insufficient justification for adjustments made to its triangulated willingness to pay valuations such that its ODIs do not appear to reflect the outcomes of its customer engagement for a number of PCs.</p> <p>The company provides convincing evidence of having taken forward the four themes of customer participation as set out in the 'Tapped In' report (i.e. increasing customer participation to improve the current and future sustainability of water, encouraging customer behaviour change actions, increasing community ownership of particular aspects of water as an essential resource, and increasing customer control of water in their home or of the customer service experience). This includes: co-creation and deliberative workshops with customers looking at future facing issues; water efficiency promotion campaigns with households, communities and developers; use of its employee community champions volunteering scheme targeting areas affected by company disruption; launch of a web self-service tool; and trialling of a leak locator system that engages with the gig economy.</p> <p>The company provides insufficient evidence of engagement with future bill-payers. However, it did conduct an engagement exercise with 19-24 year old non-customers via a two week exploratory online community. There is sufficient evidence of the company engaging with over 3,000 current customers in its willingness to pay research including customers with experience of a service failure, hard to reach customers and initial non-responders (through direct targeting of postal surveys). However, the company provides insufficient evidence that a range of vulnerable customers have helped inform company decisions. The company uses a 'design your own plan' budget game to engage with customers who suffered service failures with a view to better understanding how failures impacted their experiences. The survey design and results are peer reviewed by an expert in the field.</p>
Addressing affordability and vulnerability	B	AV1	How well has the company demonstrated that its bills are affordable and value for money for the 2020-25 period?	B	<p>Severn Trent Water provides sufficient and convincing evidence that bills will be affordable and value for money for all customers from 2020-25.</p> <p>The company proposes to reduce real bills by 5% from 2019-20 to 2024-25. The company also has a highly efficient approach to providing overall affordability support to customers based on its level of growth in debt write-offs, the proportion of customers getting debt advice and the net benefits from water efficiency devices. Regarding wider affordability measures, the company is proposing a credible plan to improve its meter rollout, but currently is not sector leading on this. The company has sufficiently linked its metering programme to opportunities for customers to save money.</p> <p>However while the company conducted high quality and in some cases innovative engagement with customers, there were notable differences between the company's own research and the findings of CCWater on affordability and acceptability. Although the company monitors its customer's views on value for money through its own quarterly survey, it proposes to drop a PC to monitor this.</p>
		AV2	How well has the company demonstrated that its bills will be affordable and value for money beyond 2025?	C	<p>Severn Trent Water provides insufficient and unconvincing evidence of a high-quality approach to addressing affordability of bills beyond 2025. In particular, we are not satisfied with the company's use of financial levers. In addition, there is insufficient evidence of the company testing a long-term bill/bill profile with its customers. There is however some evidence that the company is proposing flat bills between 2025-2030, and the company has undertaken some long-term investment preference testing with customers.</p>

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	B	AV3	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?	B	<p>Severn Trent Water provides sufficient and convincing evidence that it has appropriate assistance options in place for those struggling or at risk of struggling to pay. In particular, the company has demonstrated high-quality and in-depth engagement with customers who struggle to pay, and ambitious engagement with customers around the social tariff cross-subsidy. Moreover, the company's social tariff is growing by over 50% between 2020-2025, and it provides evidence of increasing the accessibility by proposing a new tiered social tariff with different levels of discount.</p> <p>In the round, we consider its social tariff growth, alongside its ambitious and innovative approach to engagement with customers who struggle to pay and improved accessibility of support to demonstrate an effective overall approach.</p>
		AV4	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?	B	<p>Severn Trent Water provides sufficient and convincing evidence of a high-quality approach to supporting customers in vulnerable circumstances. In particular, it is proposing to increase the reach of its priority services register to 5% by 2024/25, which is relatively strong reach.</p> <p>In addition, it demonstrates the effective use of data to understand and support vulnerable customers. For example, its data sharing partnership with Western Power Distribution appears to be well developed and it has used several external data sources to understand the extent of different vulnerabilities in its area. Moreover, it provides sufficient evidence of high-quality and extensive engagement with vulnerable customers from across different types of vulnerability. Furthermore, it has evidenced robust partnerships with third parties, in particular through its vulnerability expert event.</p> <p>However, its PC to help 100% of vulnerable customers in a clean water incident is not sufficiently ambitious because we consider this represents business-as-usual for the sector, and therefore is not stretching.</p> <p>In the round, we consider that the company's high-quality engagement with vulnerable customers and approach to partnership working to be high-quality.</p>
Delivering outcomes for customers	C	OC1	How appropriate, well-evidenced and stretching are the company's proposed performance commitments and service levels?	C	<p>Overall the company provides insufficient evidence that it has selected appropriate PCs or that its PCs demonstrate stretching performance. However, there are elements of high quality within the plan.</p> <p>The company provides insufficient evidence that it is complying with the PR19 Final Methodology requirements. For two common PCs (leakage and unplanned outage) the company has high numbers of components of the definition where it was not complying when it reported data for 2017-28, but it provides insufficient evidence that it will comply with these definitions by 2020.</p> <p>We have identified that:</p> <ul style="list-style-type: none"> • There are no significant issues with the bespoke PCs it proposes. • There are no gaps in the coverage of its proposed PCs. • There are no issues identified with how past performance has been reflected in the plan. <p>The company provides insufficient evidence that its PCs are stretching:</p> <ul style="list-style-type: none"> • The company's proposed performance level for supply interruptions is significantly worse than the upper quartile (UQ). • The company proposes a deterioration in asset health measured by the level of mains repairs in the 2020 – 2025 period due to the expected increase in active leakage control, but provides insufficient evidence to support the proposed level. • There are concerns with the evidence for the proposed stretch of a number of bespoke PCs. <p>While the company did not propose performance that was above the UQ for a number of PCs the company proposals are close to UQ.</p> <p>We have confidence in the evidence that its performance reporting structures are robust, ambitious and innovative because:</p> <ul style="list-style-type: none"> • It provides sufficient and convincing evidence that it will report performance accurately. • It proposes to maintain customer engagement through its 'Tap Chat' online panel to increase the reputational strength of incentives • It will provide quarterly performance data to the Consumer Council for Water, although not directly to customers.

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		OC2	How appropriate and well-evidenced is the company's package of outcome delivery incentives?	C	<p>Overall, we consider that Severn Trent Water's approach to its outcome delivery incentives (ODIs) falls short of high quality. Although it provides some justification to its choice of ODI type, we identify a number of instances where outperformance payments are not suitably justified. We also have concerns over its approach to determining ODI rates, particularly for those relating to its sewer flooding. Overall we consider the company's approach to setting deadbands, caps and collars is appropriate, although we have identified some minor concerns relating to the evidence of the collars it proposes. The company has put forward two enhanced ODIs for which the thresholds it proposes are not sufficiently challenging.</p> <p>We have identified instances where the company has not sufficiently justified outperformance payments. This is a particular concern for sewer blockages.</p> <p>The company's plan is significantly short of the quality required to justify its ODI rates appropriately. We observe the following concerns with its package of ODI rates:</p> <ul style="list-style-type: none"> • There is insufficient evidence to justify the high outperformance rates for a number of PCs related to sewer flooding. This is a significant concern as the company has significantly outperformed on sewer flooding in the 2015-20 period. The resulting rates and expected performance would lead to asymmetric upside versus downside for the 2020-2025 period. Internal and external sewer flooding, together, contribute almost half of the outperformance payments in the total P90 expected by the company. P90 is the scenario for which there is a ten per cent chance that the outcome will be this or better. • The company's approach to triangulation for internal and external sewer flooding ODIs is determined at a top-down level and has the effect of attaching the lowest weight to the willingness to pay values obtained from the largest sample of customers, while more weight is given to values obtained using less statistically robust samples. • Within the final marginal benefit calculation, the company uplifts the willingness to pay values used in the construction of marginal benefits for both sewer flooding ODIs based upon its "Choices" research. It has not provided sufficient evidence to set out the research methodology or evidence of third party assurance for this research, which also forms the basis for a number of other ODI rate adjustments. • The company does not provide P10 and P90 estimates for some measures such as Improvements in WFD criteria, and has not provided sufficient evidence to clearly set out its ODI calculations in a number of cases. <p>Overall, the company's evidence to support the caps, collars and deadbands it proposes is insufficient. We have concerns over the company's approach to setting caps and collars. In particular we have a concern with its insufficient justification of setting a collar without a cap for its external sewer flooding PC. We noted no concern with its approach to deadbands.</p> <p>We identify concerns with the company's approach to enhanced outperformance and underperformance payments:</p> <ul style="list-style-type: none"> • Its target thresholds do not correspond to where we expect the frontier to be in the 2020-2025 period. • For pollution incidents, the threshold where penalty rates start to apply is less challenging than the current lower quartile level in the sector. <p>We note that the proposed enhanced reward rates strike a suitable balance between incentivising the company and protecting its customers.</p>

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		OC3	How appropriate is the company's focus on service performance in its risk/return package?	C	<p>Overall, Severn Trent Water's business plan falls short of high quality with insufficient evidence that it has applies an appropriate and high quality approach to its focus on service performance in its risk/reward package. The company provides insufficient evidence to justify the skew of its ODI package towards wastewater and in particular sewer flooding measures, given its past performance on these. The company also does not set out any measures to protect customers in the event of outperformance payments that exceed expectation. However, there are elements of high quality within the plan. It demonstrates sufficient consideration of its past asset health challenges, aligns the timing of ODIs with its service performance, and provides some evidence of alignment between customer and shareholder interests resulting from the ODI package.</p> <p>The company does not meet our expectations for the appropriateness of the overall ODI package because:</p> <ul style="list-style-type: none"> the package is not considered balanced in terms of company challenges or the split between water and wastewater. It is heavily skewed towards wastewater and flooding measures, which is very concerning given the company's good past performance on this measure compared to the poor performance in the 2015-20 period on water; and there is lack of convincing evidence that overall return on regulatory equity (RoRE) range is bottom-up from individual customer valuations on individual ODIs, as some of the ODI rates have been uplifted after the calculation with insufficient evidence. <p>We have identified that:</p> <ul style="list-style-type: none"> The ODI package is within the indicative range. The company has provided a sufficient explanation of how its ODI package incentivises it, through better aligning the interests of management and shareholders with customers, to deliver on its PCs to customers. <p>The company's overall approach to align the timing of ODIs with its service performance is line with our expectations as it has proposed most of its financial ODI's as in-period and the ones that are end-of-period are well justified.</p> <p>We have confidence in the evidence that the company has met our expectations for ODIs for asset health PCs because:</p> <ul style="list-style-type: none"> the company has demonstrated that it understands and has addressed its asset health past performance challenges, as it has an appropriate PC and ODI on wastewater treatment works compliance; the company has demonstrated high quality customer engagement on asset health; the CCG challenged the company's approach to asset health and was satisfied with the responses; we consider that the nature and magnitude of the overall package of asset health ODIs, in terms of RoRE exposure, is sufficient to incentivise the company to meet its asset health challenges and protect customers; and the company has demonstrated customer support for its outperformance payments. <p>The company has provided insufficient evidence that the company's approach protects customers from higher than expected outperformance payments:</p> <ul style="list-style-type: none"> The company's P90 estimate at 2.60% RoRE is the second highest in the sector, but it does not propose to cap overall outperformance payments RORE range to protect customers. For individual PCs, the company proposes deadbands and caps for underperformance payments alone, and not for outperformance. This asymmetry exposes customers to further financial risk. The company proposes enhanced outperformance rates for internal sewer flooding and pollution incidents. The risk on these is especially high as it proposes no caps. The company has performed strongly on this area at AMP6 It does not provide any details on how it will smooth bills going forwards.

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Securing long-term resilience	C	LR1	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?	C	<p>Severn Trent Water presents a business plan that falls short of high quality and provides insufficient and unconvincing evidence of how the company objectively assesses and prioritises the diverse range of risks and consequences of disruptions to its systems and services.</p> <p>The company provides limited evidence of a systems-based approach to resilience expected in a high quality plan, where interdependencies and interactions between internal and external systems would be included. The plan also fails to present an assessment of the resilience maturity of its systems and services and aspirational levels of resilience for 2025 and beyond, which would allow the company to identify areas of concern to be targeted. Partly as a consequence of these omissions, risks are not considered in combination in the plan, which in turn appears to provide a mostly qualitative analysis of risks.</p> <p>While the plan considers a long list of risks, covering aspects of operational, financial and corporate resilience, these are not prioritised, providing a limited understanding of risk exposure within the company's systems. The plan lacks clarity and robustness in its consideration and assessment of risks, which are not treated holistically and are therefore limited in how they can truly inform the development of an in-the-round approach to resilience. The company demonstrates good customer engagement regarding resilience in a variety of topics, including levels of service and future uncertainty, supported by comparative information from the sector. Additionally, the plan describes well-established corporate systems to manage and assess risks; however, there is a limited consideration of risks to the delivery of the plan, mainly around supply chain management.</p> <p>The company's assessment of financial resilience demonstrates elements of high quality, but falls short of high quality in some limited areas of process. There is evidence that the assessment of financial resilience links to the company's internal risk assessment and the company's board assurance statement sets out its view that the company's plan is financeable and will deliver financial resilience over the next control period. However, the results of the financial resilience assessment are only presented as a 'red/amber/green' outcomes, which results in an assessment that the company demonstrates insufficient transparency about its long-term financial resilience.</p> <p>The company assesses the prescribed financial stress test scenarios and company specific scenarios derived from the company's own risk assessment process and relates the prescribed scenarios to its internal assessment of principal risks. It made a link to the stress testing of relevant plausible and severe scenarios for the long-term viability statement (LTVS) included in its annual report. However, the company does not assess its long-term viability beyond 2025.</p>

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		LR2	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 have support from customers?	C	<p>Severn Trent Water presents a business plan that falls short of high quality and provides insufficient and unconvincing evidence to objectively assess the full range of mitigation options and select the solutions that represent the best value for money over the long term.</p> <p>While the company considers a range of mitigation options, the plan relies on traditional infrastructure options and less on the improvement of response and recovery plans or soft infrastructure options, including a rather limited promotion of nature-based options. The plan is generally aligned with the risks identified, however, given the unclear prioritisation of risks, the plan lacks the robustness and clarity expected from a high quality plan in this area.</p> <p>The plan incorporates uncertainty in its planning and subsequent development of efficient options through an adaptive pathways approach, which is welcomed. However, there is limited evidence that addressing multiple risks or integrating water and wastewater/drainage strategies have been used in developing options.</p> <p>There is convincing evidence that tangible corporate mitigations are in place to enhance cyber security and future skills gaps, which demonstrate commitment to deliver improvements in these areas. Additionally, the company provides evidence that customers have been consulted on mitigation options and that they have participated in the co-creation/planning of these (e.g. real-options deliberative research to plan for uncertainty).</p> <p>Overall, the company's business plan provides convincing evidence that the company is financially resilient under a range of stress scenarios. There is evidence of processes to manage and mitigate financial risks and demonstrate that its capital structure is resilient for the long term. Severn Trent's gearing level is around 60% and it says that it expects to maintain gearing in a range from 57.5% to 67.5%. The company provides some evidence that it could maintain required liquidity and credit rating metrics under the stress test scenarios when mitigation measures are taken into account.</p> <p>The company sets out details of its financing requirements in the period from 2020 to 2025 and includes an assessment of the risk of increased costs relating to its defined benefit pension deficit as one of the financial stress scenarios that it chose to model.</p> <p>The company provides evidence in its plan of risk management through its three lines of assurance model and in respect of compliance requirements applicable to the listed group of which it is part. There is also reference to the board's annual risk and compliance statement and the enterprise risk management system used in the business. The company states that it has a system for weekly monitoring of key financial performance indicators covering its liquidity position, adherence to its treasury policy, credit rating position, debt mix, and financial covenant headroom.</p> <p>There is convincing evidence that the company has considered a range of mitigating actions it would take to secure its long term resilience in stress scenarios, including cost savings, investment phasing, sale of non-regulated assets, reductions to dividend payments and liaison with finance providers.</p>
Targeted controls, markets and Innovation	C	CMI1	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?	B	<p>Severn Trent Water's business plan is overall of high quality with sufficient and convincing evidence to 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. It provides a wide range of high quality evidence that its employees are empowered and continuously challenged to address business challenges now and in the future through initiatives such as 'The Challenge Cup', its internal crowd sourcing platform #BrightSparks, and its 'Open Innovation' ideas inbox. There is limited evidence to demonstrate how it proactively encourages interdisciplinary debates which bring together teams from across the business. Further evidence is needed to demonstrate how those conversations links to the implementation of innovative outputs for it to be considered an exceptional plan. While the company encourages all employees to try new approaches with permission to make mistakes from which it can constructively learn from, there is limited evidence to demonstrate how risks are managed and on how it learns from innovation failures. Further evidence to demonstrate how it manages risk and how it learns and builds on past failures is needed in a high quality plan. While its remuneration framework aligns to its strategic framework with innovation being one of the strategic priorities and it has a company-wide bonus scheme in place which makes sure that all employees share in and receive recognition for the successes of the company, there is limited evidence/examples to demonstrate that employees are rewarded or recognised for efforts and achievements that lead to generating or implementing innovative ideas. There is also convincing evidence on resourcing to demonstrate that the company has invested time and resources to promote innovative solutions to be applied to problems, with limited evidence that the resources available for innovation were carefully considered to help ensure resources provided were value for money. We consider that in many cases the company meets best practice, but the proposals and processes in the business plan are not sufficiently evidenced in enough areas or ambitious enough to be exceptional.</p>

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	A	CMI2	How well does the company use and engage with markets to deliver greater efficiency and innovation and to enhance resilience in the provision of wholesale and retail 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?	B	<p>Overall, Severn Trent Water provides a high quality plan in relation to this test question. Severn Trent provides sufficient evidence related to identification and management of gap sites and voids – they plan financial incentives for business properties and have a good in-house approach to managing residential gap sites. However, there is insufficient evidence related to residential voids.</p> <p>Regarding the use of markets, catchment management and partnership working for delivery services related to water network-plus, Severn Trent has an ambitious plan with particularly strong evidence related to use of markets to enable a catchment-based approach. However, on the wastewater side, the evidence is more limited and we have concerns that an undue engineering-based focus remains.</p> <p>Severn Trent provides limited evidence related to looking for lessons learned and innovation adopted from the business retail market and how they plan to adopt a similar approach in non-contestable markets.</p>
		CMI3	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?	B	<p>Severn Trent Water provides a high quality plan on its long-term strategy for water resources incorporating the use of markets to this aim. The company can do more in setting up an appropriate risk sharing mechanism for their proposed water resource scheme. Overall, the company is graded as a 'B' in this area.</p> <p>The company provides sufficient and high quality evidence on effective use of third-party delivery options for both demand-side and supply-side solution. On supply side, the company has put in place innovative mechanism to make progress on trading opportunities such as the interconnector transfer work running from the North West-South East. Demand options, include their collaboration with Atkins digital incubator for leakage detection. However, on the future deployment of bilateral markets the company does not go beyond providing the required business tables Wr6 and Wr7.</p> <p>In relation to WRMP, the company adequately addresses majority of the issues raised by Ofwat by providing a high quality long-term strategy for management of water resources.</p> <p>Additionally, the company lists three water resource schemes to be delivered in the AMP7, all of which are covered by company's proposed Real Options Uncertainty Mechanism. The proposed approach potentially reduces the risk of a significant new water resource being developed needlessly by waiting until more evidence is available that would help to confirm need. However, it does not meet our objectives or design criteria for a LTRSHA particularly around the balance of risk between customer and company if the scheme is not required. Therefore the company needs to update their 'Real Options Uncertainty Mechanism' such that there is appropriate level of risk sharing between the customer and the company.</p>
		CMI4	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?	C	<p>Severn Trent Water has an insufficiently well-evidenced long-term strategy for delivering bioresources services. The company provides a credible forecast, but there is a lack of commentary to explain the numbers. It appears from the plan that the company is using instrument for measurement, though no detail is provided. Although company clearly presents a strategy where it aims to be a net importer of sludge, it does not outline as to how it will share the benefits with customers. The plan demonstrates that it intends to engage with third parties, but does not provide evidence on how those third parties would be engaged.</p>
		CMI5	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 plus - taking into account the guidance and/or feedback we have provided?	B	<p>We issued guidance on RCV allocation for the purposes of separate price controls in early 2017. The company submitted draft RCV allocation proposals for bioresources in September 2017 and for water resources in January 2018. We issued generic feedback on the companies' approaches to draft RCV allocation proposals in early 2018. Taking into account the company's response to our initial guidance and our subsequent feedback on its draft proposals, the company's proposed RCV allocations appear appropriate.</p>

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	A	CMI6	To what extent has the company produced a company 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?	D	Severn Trent Water has produced a bid assessment framework (BAF) that falls significantly short of demonstrating the key principles of transparency, non-discrimination and proportionality. While the overall process is described, little detail is provided on what information third-parties would have to provide, how the bids will be evaluated, what feedback they might expect to receive, or how any appeals might be handled. The assurances about non-discrimination rest on a claim that the evaluation criteria (not in the BAF) will ensure a rule-based process and the presence of an in-house water resources procurement team that is independent of in-house options being developed. The relative lack of detail makes it difficult to assess whether the process would be proportionate.
		CMI7	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 technically suitable 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?	C	<p>Severn Trent Water provides evidence that it considered DPC as part of its business planning process. It assessed schemes on whether they met the £100m threshold, carried out a technical analysis on the relevant schemes and carried out a Value for Money (VfM) assessment for the East Midlands Reservoir scheme. In the appraisal of the the company DPC plan we took into account the following:</p> <ul style="list-style-type: none"> • The company clearly identified that it had considered DPC in its business plans. It provided evidence of a process to identify schemes and reviewed 11 projects • The company provided technical assessments for four schemes. The process followed the guidance and was clearly evidenced in a supplemental report. The information and evidence provided about the schemes and the scoring against each criterion fell short of being convincing for the rejection of the Church Wilne WTW expansion and proposed Anglian transfer. Due to the lack of supporting evidence and unconvincing decisions on two projects the technical assessment was not considered to be high quality. • The company undertook some analysis for VfM. However there was insufficient evidence that the company had fully followed the Five Case Treasury model in their analysis. <p>In summary, Severn Trent Water's assessment of DPC has some good aspects but it falls short of high quality because its decisions in some areas are not supported by sufficient convincing evidence.</p>
Securing cost efficiency	B	CE1	How well evidenced, efficient and challenging are the company's forecast of wholesale water expenditure, including water resources costs?	C	Severn Trent Water's wholesale water total costs are around 12% above our view of efficient costs. A particular area where Severn Trent's projected costs appear high relative to its peers is in new developments. The company's leakage reduction unit costs are lower than the industry benchmark and it plans to reduce leakage by marginally more than 15%. We therefore make an allowance for the leakage reduction above 15%. Company metering costs are higher than the benchmarked comparative modelled allowance.
		CE2	How well evidenced, efficient and challenging are the company's forecast of wholesale wastewater expenditure, including bioresources costs?	B	Severn Trent Water outperforms our view of efficient costs in wholesale wastewater by around 4%. Its base costs are around 7% below our view of efficient costs. In the round, wastewater enhancement proposals seem efficient. We are allowing business plan costs for all wastewater enhancement proposals apart from those in bioresources, where the evidence for requested investment is insufficient.
		CE3	How well evidenced, efficient and challenging are the company's forecast of retail expenditure, including bad debt costs?	A	Severn Trent Water's residential retail costs are around 6% below our view of efficient costs.

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		CE4	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?	D	Severn Trent Water proposes twelve cost adjustment claims. The overall quality of its claims is poor. We assess three as of reasonable quality and scored as marginal pass, two we assess as partial pass and seven fail. We do not make an allowance for any of the cost adjustment claims because many of them are straightforward enhancement proposals.
Aligning risk and return	C	RR1	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 2020-2025?	B	The company has provided sufficient and convincing evidence that it has based its business plan for 2020-25 on the cost of capital and retail margin caps set out as our PR19 Final Methodology 'early view'.
		RR2	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?	C	While Severn Trent Water's Business plan demonstrates high quality in some areas there is insufficient evidence on risk management and risk mitigation measures in the context of the RoRE scenarios. The company has assessed the scenarios prescribed by Ofwat that are relevant to its circumstances. The company has identified risk factors and clearly set out its findings, however, there is insufficient evidence that the variances to expected RoRE outcomes have been sufficiently explored. There is insufficient detail on mitigation measures which have been explained at a high level, and are limited to general statements about financing and cost management. The company proposed 'real options' mechanisms for uncertainties related to supply demand balance; climate change; metering rollout; the wastewater environmental programme (WINEP); and work associated with an interconnector for water trading. We have assessed the mechanism for metering within our IAP assessment for outcomes and the mechanism for the wastewater environmental programme as a cost assessment item. In cost assessment we have made an additional allowance for development of North-South strategic supply solutions. Evidence that a mechanism for uncertainty associated with the supply demand impacts of climate change is unconvincing given the totex sharing arrangements that underpin the price determinations and as funding could be recovered through a transitional funding arrangement at PR24.
		RR3	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?	B	Overall, Severn Trent's business plan is high quality, providing sufficient and convincing evidence to support its board's statement that the plan is financeable on both the notional and its actual capital structure. The following areas of the plan are high quality: <ul style="list-style-type: none"> The company has set out the steps taken to make the financeability assessment and to provide assurance, supported by third party assurance of the procedures and calculations of the business plan data tables that support financeability. The business plan provides sufficient evidence to support the target credit ratings of Baa1/BBB+ (Moody's and S&P) for the notional company structure and Baa1/BBB+ for its actual structure and that the plan is consistent with maintaining the target credit ratings for the notional and actual structures. The company has identified a notional financeability constraint and has proposed an uplift to RCV run-off rates to address this. The company has proposed to limit the uplift and use ODI rewards from the current period to meet the expectations for the key financial ratios whilst minimising the impact on customer bills. The company has provided sufficient and convincing evidence that, in the round, using the ODI rewards to help address the financeability constraint protects customers from bills that would otherwise be higher in 2020-25. The company has not identified a financeability constraint on its actual capital structure.

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		RR4	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	C	<p>Despite some aspects of Severn Trent's business plan which are high quality, shortcomings in other aspects mean that, overall, it falls short of providing sufficient and convincing evidence to support its choice of PAYG and RCV run-off rates.</p> <p>The business plan does provide some evidence of high quality in specific areas:</p> <ul style="list-style-type: none"> the company's PAYG rates are supported by sufficient and convincing evidence. No adjustment to the starting point for PAYG rates has been proposed. overall, there is sufficient and convincing evidence that the final bill profile, which includes the impact of the transition to CPIH, is supported by customer preferences and there is evidence that bills are consistent with customers' preferences both now and in the future. <p>There are two main areas where the plan falls short of high quality. It does not provide sufficient and convincing evidence:</p> <ul style="list-style-type: none"> to support the starting point for RCV run-off rates. The company has provided insufficient evidence that the rates are in line with the company's approach to RCV run-off rates. to support the adjustment to RCV run-off rates for the transition to a CPIH based plan. The company has proposed two adjustments to RCV run-off rates, to address a financeability constraint on the notional company structure and to transition the business plan fully to a CPIH basis. The plan contains insufficient evidence to support the level of the adjustments.
Accounting for past delivery	B	PD1	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?	C	<p>Severn Trent Water's plan falls short of high quality with insufficient evidence to support the PR14 reconciliation adjustments overall.</p> <p>The company's plan falls short of high quality on the rationale provided to support the PR14 reconciliations. However there is sufficient evidence in terms of the accuracy of the calculated adjustments. The deviation of the overall value of the adjustments from what we would expect using the data in the business plan is marginal at 0.1% of the 2019-20 PR14 allowed revenue.</p> <p>Severn Trent Water has used the published versions of PR14 reconciliation models to calculate the proposed revenue and RCV adjustments with appropriate modifications to the models for residential retail and wholesale revenue forecasting incentive mechanism in relation to the 2018 NAV.</p> <p>We have not found major data consistency issues between the submitted tables and populated reconciliation models. We have found minor consistency issues for land sales, residential retail, totex and wholesale revenue forecasting incentive mechanism.</p> <p>Reported actual performance and resulting underperformance and outperformance payments are consistent in the annual performance report document and our independent checks of the reported ODI underperformance and outperformance payments are identical to those reported by the company for all PCs for Severn Trent Water. We have not taken into account the new PCs since 1 July 2018 for the Chester area as these form a minimal part of the company's area. Our independent checks of the reported ODI underperformance and outperformance payments have found significant differences between our checks and those reported by the company for customer satisfaction measures.</p> <p>For some areas, the forecast trajectory appears reasonable in light of actual performance and PR14 determination, but for nine of the 25 PCs, land sales, residential retail, service incentive mechanism and totex there is insufficient evidence to provide confidence that the forecasts are appropriate or to support the forecast trajectories.</p>

Test area	Overall test area grade	TQ#	Test question	Test question grade	Test question summary assessment
		PD2	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?	B	<p>In the round we have no concerns with the evidence for deliverability for the 2020-25 plan, with some concerns for customer complaints.</p> <p>There is good outcomes performance as the company has or is forecast to deliver 78% of its PCs with financial ODIs in 2015-20. The company provides sufficient evidence that it understands the drivers of its performance and has learnt lessons from that performance, although we would like to see a greater level of understanding for drinking water quality complaints, related to this PC. The greatest level of stretch in the plan is where the company is performing well, for example on external sewer flooding. For example, for drinking water quality complaints the company plans to have mid-level performance in the industry. The plan provides sufficient evidence that it includes appropriate measures to improve its performance. Taking into account the proposed level of stretch in the plan, we therefore do not have concerns with the evidence for deliverability of outcomes.</p> <p>There is good performance on cost efficiency as the company's actual and forecast costs are below cost allowances for 2015-20 for wholesale water and wastewater. The company provides sufficient evidence it understands the drivers of its performance and that it has learnt lessons from its performance, such as the need to work with supply chain partners to identify innovative solutions and to impose lean manufacturing. The company is proposing an efficiency challenge for 2020-25 and provides sufficient evidence of improvement measures to meet that challenge. For example, it proposes to introduce better online services for customers, automation of back-office services and automated meter reading. We therefore do not have concerns with the evidence for deliverability of the planned costs.</p> <p>We have some concerns around performance on major incidents. It had four major incidents, but had a below average number of category one and two pollution incidents per 10,000km of sewers and has an EA performance rating of four stars. However, it had two prosecutions from the EA and nine formal cautions from the EA and DWI. It was also required to provide an externally assured action plan following the 2018 freeze and thaw. The company provided sufficient evidence it understands the drivers of its performance and has learnt lessons on major incidents, such as its need to improve extreme weather response and recovery and the reliability and resistance of its network. The plan provides sufficient evidence the company has measures in place to improve performance in relation to major incidents, such as reassessing its emergency plan, improving its alternative supplies provision and improving identification of customers experiencing transient vulnerability. We therefore do not have concerns with the evidence for deliverability of performance in relation to major incidents.</p> <p>The company is meeting CCWater's 2020 customer complaint target of resolving 95% of customer complaints at stage one but the proportion is falling. It has an above average number of complaints per 10,000 connections in 2017-18, although this is declining. The company provided insufficient evidence it understood the drivers of its performance and learned lessons. For example, it identifies its efforts to simplify bills and improve real-time data during customer calls as drivers of improved performance, but fails to outline clear lessons for improvement. The plan provides insufficient evidence that it includes appropriate measures to improve its performance. For example, it proposes to develop its interaction analysis, but fails to provide sufficient detail. We therefore have some concerns with the evidence for deliverability of customer complaints handling performance.</p>

Test area	Overall test area grade	TQ#	Test question	Test question grade	Test question summary assessment
Securing confidence and assurance	B	CA1	To what extent does the company's business plan contain evidence that its full Board has 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?	B	<p>Severn Trent Water's business plan provides sufficient evidence that its full Board provides comprehensive assurance to demonstrate that all the elements of its business plan add up to a plan that is high quality and deliverable, and that it has challenged management to ensure this is the case.</p> <p>High quality Board assurance statements include compliant statements as set out in the PR19 Methodology which, in general, are supported by sufficient evidence that Boards have challenged management and satisfied themselves prior to making the statements.</p> <p>The majority of the Board assurance statements within the company's business plan comply with those we request in the PR19 Final Methodology. The company provides fifteen compliant statements. The statement on whether the expenditure forecasts included in the company's business plan are robust and efficient is partially-compliant.</p> <p>For statements on business planning, we request that Boards demonstrate how they challenged management and satisfied themselves prior to making their statements. The Board states that it has challenged the plan, which is supported by a record of topics discussed at Board meetings. However, the details insufficiently cover the topics of the assurance statements.</p> <p>For statements on the remaining topics, we request that Boards demonstrate how they satisfied themselves. The company provides a record of topics discussed at Board meetings and a list of proof points and associated evidence considered by the Board prior to making its statements. This evidence sufficiently demonstrates how the Board satisfied itself prior to making eight of the compliant statements. There is insufficient evidence of how the Board satisfied itself prior to making its statements on whether the company's business plan has been informed by a comprehensive and objective assessment of interventions to manage resilience in customers' long-term interests; and risk and return.</p>
		CA2	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?	C	<p>Severn Trent Water's business plan falls short of providing sufficient and convincing evidence that its full Board has 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.</p> <p>High quality assurance means that the Board provides a compliant statement, supported by suitable supporting evidence.</p> <p>The Board's assurance statement advises that "Our business plan will deliver operational, financial, corporate and reputational resilience over the next control period and the long term, through our well established, robust and independently assured governance and assurance processes."</p> <p>This is a suitable statement of assurance, however the company provides insufficient evidence of the Board's assurance process to support its statement.</p>

Test area	Overall test area grade	TQ#	Test question	Test question grade	Test question summary assessment
		CA3	<p>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 with customers, on issues that matter to customers (which extends to their ability to understand the company's corporate and financial structures and how they relate to its long-term resilience)?</p>	C	<p>Overall we consider the plan falls short of high quality with insufficient evidence in some areas that the plan will enable customers' trust and confidence through appropriate measures to provide a fair balance between customers and investors and high levels of engagement and transparency on corporate and financial structures and how they relate to financial resilience.</p> <p>Severn Trent Water's plan contains sufficient evidence that the company will commit to adopt two of the expectations set out in the 'Putting the sector in balance' position statement:</p> <ul style="list-style-type: none"> • The company forecasts gearing to be marginally above 65% during the 2020-25 price control period and although it does not state that it will adopt our benefits sharing mechanism it does commit to sharing benefits with customers if gearing exceeds 70%; and • The company proposes a base dividend yield less than 5%. <p>The company is proposing a bespoke voluntary benefits sharing mechanism to donate 1% of profits to support local good causes and to spend £10m on a technical training academy, which we estimate could jointly represent sharing of £4.5m per year on average. The company is also proposing donations to social tariffs and hardship funds which we assess could have a value of £3.5m per year. We assess the total value of the company's proposals as being high quality in the context of its size as a company.</p> <p>However we have concerns in three areas.</p> <p>On dividend policy, the plan falls short of high quality with insufficient evidence that the company's proposed dividend policy for 2020-25 takes account of delivery of obligations and commitments to customers and other stakeholders. The proposed dividend policy stated in the business plan refers to all of the required elements from the position statement with the exception of a specific reference to pension obligations. This is a material omission since the pension scheme is currently in deficit. No evidence is provided on how the elements will be taken into account when determining dividends. The company states it will continue to be transparent about the areas of its business that matter most to its stakeholders – which includes dividend payments. However, there is no specific reference to annual publishing or signalling of changes in dividend policy to stakeholders.</p> <p>On executive pay, the plan falls short of high quality with insufficient evidence that the company takes full account of all of the required elements. However there are some elements of high quality. The company commits to continued transparent reporting in its annual remuneration report. It states it has two schemes- annual and long term incentives. For the long term scheme a large proportion relates to the delivery of service to customers. The annual scheme contains no evidence relating to the setting of stretching targets. The company states it has recently enhanced its long term incentive by setting stretching targets based on upper quartile return on regulated equity delivery for the sector, but does not state that this will apply within the next price control. The company states that the remuneration committee will operate at the parent company level but there is insufficient evidence that the remuneration policy will be monitored and rigorously applied. There is also no reference to how changes and their justification will be communicated.</p> <p>The plan falls short of high quality with insufficient evidence that the company's full Board provides assurance that the company's business plan will enable customers' trust and confidence through high levels of transparency and engagement on corporate and financial structures and how this relates to financial resilience. The Board's assurance statement is partially compliant as it states that engagement with customers is important to the company but does not provide assurance that it will engage. On demonstrating transparency on its corporate and financial structures, the company's business plan refers to its Annual Performance Report which sets its corporate structure but it falls short of high quality with insufficient evidence on transparency of its financial structure.</p>

Test area	Overall test area grade	TQ#	Test question	Test question grade	Test question summary assessment
		CA4	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 and licence obligations and take account of the UK and Welsh Governments' strategic policy statements)?	B	<p>Severn Trent's business plan provides sufficient and convincing evidence that its full Board has provided comprehensive assurance to demonstrate that the business plan will deliver - and that the Board will monitor delivery of – its outcomes.</p> <p>The Board provides assurance that it will monitor delivery of its outcomes and PCs through the following compliant statement "Having approved the assurance framework, reviewed the assurance findings and management's response, and considered the Water Forum challenge, we have collectively satisfied ourselves that our business plan can deliver our outcomes, PCs and ODIs, and we will continue to monitor delivery of them through our well established governance approach".</p> <p>It advises how the Board will monitor outcome delivery through the following statement "Our established governance arrangements will continue to apply with performance regularly being monitored by the Executive Committee and Board, and through the Disclosure Committee and Audit Committee at least during mid-year and year end points in the reporting cycle." The company's plans for monitoring outcomes delivery in the 2020-25 period have also been reviewed by their Internal Audit team and by their external technical advisors. This is sufficient evidence.</p>
		CA5	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?	C	<p>Severn Trent Water falls short of sufficiently demonstrating 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 in the 2018 Company Monitoring Framework (not including the elements related to the PR19 business plans).</p> <p>The plan has aspects of high quality:</p> <ul style="list-style-type: none"> • The company sufficiently describes its data assurance, governance and audit processes within its business plan. • Overall, the performance and financial data reported in the company's business plan tables is consistent with previous data submissions, with only inconsistencies in the area of cost assessment which do not materially affect our overall assessment. • The company adequately references interventions it has implemented as a result of the company's 'Targeted' status in the 2017 Company Monitoring Framework. <p>However in our assessment of the company in the 2018 Company Monitoring Framework (not including the elements related to the PR19 business plans) while the company meets expectations in 7 areas, it has minor concerns in 2 areas.</p>
		CA6	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?	B	<p>Overall, Severn Trent's business plan provides sufficient and convincing evidence that its PR19 business plan tables, including the allocation of costs between business units, consistency of tax information and the assurance and commentary provided are consistent, accurate and assured. We identify some issues within our assessments of the data tables in the policy areas of outcomes, risk and return, financial modelling and cross cutting themes (water resources), but these do not materially affect our overall assessment.</p>