

Annual Performance Report 2017-18

Part 5 – Risk and Compliance Statement



RISK AND COMPLIANCE STATEMENT 2017/18

Scope of the Risk and Compliance Statement

Ofwat expects all water companies to provide a statement setting out how they have complied with their relevant statutory, licence and regulatory obligations for which Ofwat is the relevant enforcement authority (Obligations). The Risk and Compliance Statement is one of Ofwat's key regulatory tools and allows companies to demonstrate their accountability to their customers and demonstrate to Ofwat that they are complying with their obligations.

The Risk and Compliance Statement

We recognise the importance of demonstrating to our customers, stakeholders and regulators that we are meeting the statutory, licence and regulatory obligations that apply to our activities. We have set out in this Statement and our Annual Performance Report our compliance with and performance against certain key performance measures, legal requirements and regulatory outputs. We have also identified the risks that we are facing and the steps we are taking to manage and mitigate those risks.

In preparing this Statement we have considered, in particular, our compliance with those legal, licence and regulatory obligations for which Ofwat is the enforcement authority. In respect of these obligations, subject to the matters set out in this Statement, we confirm that:

- We have a full understanding of, and are meeting, our statutory and regulatory obligations.
- We have taken steps to understand and meet our customers' expectations.
- We are satisfied that we have sufficient processes and internal systems of control to meet our obligations.
- We have appropriate systems and processes in place to allow us to identify, manage, mitigate and review our risks.

In this Statement we also:

- explain links between the standards of performance we achieve and directors' and senior executives' pay (s35A Water Industry Act Statement);
- confirm that the auditors have been made aware of all relevant information (Companies Act 2006);
- explain our dividend policy (Licence Condition F6);
- confirm that we have sufficient financial and management resources available to us for at least the next 12 months to meet our obligations as a water and sewerage undertaker and outline the main factors taken into account when making this statement (Licence Condition F6A.2A/B);
- confirm that contracts entered into with associated companies include requirements concerning the standard of service to be provided, to ensure we can meet our obligations as a water and sewerage undertaker (Licence Condition F6A.2A);
- confirm that a report has been prepared by the companies' auditors and addressed to Ofwat, stating whether they are aware of any inconsistencies between the F6A.2A Statement and the financial statements or any information obtained in the course of their work. (Licence Condition F6A.4);
- confirm we will be able to continue in operation and meet our liabilities as they fall due over the period to March 2030 (UK Corporate Governance Code and Ofwat requirement);
- confirm that we have maintained an issuer credit rating which is classed as an Investor rating (Licence Condition F6A.6);
- confirm that if a special administration order were to be made, we would have available sufficient rights and assets (other than financial reserves) to enable a special administrator to manage the affairs, business and property of our regulated activities (Licence Condition K Statement); and
- confirm that transactions with associated companies are at arm's length (except where agreed by Ofwat) with no cross subsidy occurring (Licence Condition F6.1).

Our independent technical adviser on regulatory reporting issues (Jacobs Engineering Group) has reviewed the approach and processes we follow in assessing compliance with our obligations. A copy of their Assurance Statement is provided in Appendix A.

The Individual Statements

Dŵr Cymru fully recognises its accountability to its customers, its regulators and its other stakeholders and is pleased to provide the following Statements to demonstrate that it complies with its Obligations and is managing its risk in an appropriate manner.

1. The Company considers it has a full understanding of, and is meeting, its Obligations.

Our primary obligations and duties as a Water and Sewerage Undertaker are set out in the Water Industry Act 1991, the Water Resources Act 1991 and our Licence.

We keep our assurance processes continually under review to ensure they remain appropriate. A key emphasis is on ensuring the Company has sufficient processes and internal systems to fully meet our obligations. Our Legal Team works with colleagues throughout the business to identify new legal obligations and amendments to existing legislation. Colleagues in the Regulation Team keep abreast of developments or changes to our regulatory and licence obligations. The Compliance Team provides advice, guidance and support to the whole business on understanding the extent of any regulatory or licence obligation and implementing an appropriate internal control framework to ensure compliance with those obligations.

For the 2017/2018 Risk and Compliance Statement we mapped Company processes against our statutory and licence obligations. This was a desk exercise combined with consultation with operational managers. In each case the outcome of the process followed demonstrated that the obligation in question was recognised and that there were processes in place likely to ensure compliance. We continue to use a common reporting format which includes:

- responsible Member of the Dŵr Cymru Executive Team;
- formal description of the obligation;
- description of the obligation in plain English;
- details of policies, procedures and responsible Departments;
- internal governance and assurance arrangements;
- external assurance arrangements; and
- any material performance departures in the report year.

We will continue our efforts to improve the awareness of business units of the obligations they contribute to deliver and to further embed compliance within “business as usual” processes.

2. The Company has taken steps to understand and meet customer expectations.

Our Customer-led Success approach places the needs of our customers at the heart of everything we do. We take a lot of pride in shaping our services around the needs of our customers — and delivering the best service possible is our top priority.

Our vision is to “earn the trust of our customers every day”. This vision is fundamental to the way we work and enshrines our commitment that everything we do should be geared towards the benefit of our customers, not just our responses to high-profile events or campaigns.

The last year has seen a focus on how we are delivering services for our customers and how we are planning to deliver them in future. We know that while customers rightly expect us to deliver high-quality, safe and reliable services every day they also want us to ensure those services are sustainable and will withstand the many challenges the decades to come will present.

With our unique constitution Dŵr Cymru exists to serve its customers and the communities of which they are a part. Whilst our management are expert in this industry and our Board has a depth of understanding from which to challenge management’s plans of what we need to deliver to meet our regulatory requirements, it is for our customers to tell us what their priorities and their concerns are — which in turn form the base of our objectives. So we consulted deep and wide on Welsh Water 2050 during 2017.

Have Your Say

Dŵr Cymru is a customer-led company and we recognise that in future, customers will expect a more personalised service and control over their use of services from us to ensure that these respond to their specific needs.

In line with our commitment to listen to our customers and act on what we hear, we launched our biggest ever consultation with customers last year. In the summer of 2017, we asked our customers how we should prioritise our investments for our next five-year business plan to 2025, but also for the long-term. This aligns with Welsh Water 2050 which sets out how we plan to tackle a range of long-term challenges facing the water industry.

We reached a record of over 20,000 responses received over the 10 weeks the consultation was open, and we received the views of our customers in a number of ways, including:

- attendance at 10 key tourist events across Wales and Herefordshire including the National Eisteddfod, Royal Welsh Show and Pride Cymru;
- from a live bilingual Facebook Messenger chatbot;
- via feedback from our Customer Challenge Group; and
- through our permanent customer forum Welsh Water Online Community.

Listening to Customers

The Have Your Say consultation and the overwhelming response from our customers is only one part of how we are listening to customers and planning for the next investment period of 2020 to 2025, as well as the next 30-40 years. We have been conducting in-depth customer research and focus groups on what customers expect from us in terms of service, what they think about our long term resilience plans, as well as specific issues like how we can best-support vulnerable customers with their needs. We have ensured customers' views have a real influence on the millions of pounds we invest in our services through our not-for-shareholder profit "dividend".

We have also seen some really positive engagement from customers through our Have Your Say Online Community. This is a permanent resource for customers who want to feed in to our plans on a regular basis — from our operational planning, to customer service, to how we best protect the natural environment, as well as how we run our major campaigns. All our feedback from customers is vital to ensuring our customer-led way of working delivers the results that customers want and expect.

Welsh Water 2050

One of the key pillars underpinning customers' trust is their faith that we are planning and preparing to meet those challenges in future. The Welsh Water 2050 vision sets out 18 "strategic responses" to trends which we, our key stakeholders, and our customers believe will help us meet those challenges head on. The plan responds to the feedback and concerns that we have heard from customers and stakeholders. We are building flexibility into our plans to respond to shifts in customer priorities, as well as future events — with reviews every five years to ensure it is delivering the best outcomes for our customers. It also aims to be consistent with the well-being goals set out in the Well-being of Future Generations Act 2015.

We are piloting a project which combines our operational work with our customer-led vision. We are looking to take a different approach, to make sure customers feed in to every step we take in during this work. This includes having an ongoing, genuine dialogue with local people to minimise disruption from the essential work we do, how they can use our services more efficiently and save money, and also to raise awareness of the range of support available for vulnerable customers.

Business Customers

Dŵr Cymru serves around 100,000 business customers which range from water intensive manufacturers to small shops and hairdressers' salons. We know that the services we provide to businesses are essential — and we work to ensure we can help businesses make the most efficient and cost effective use of water and wastewater services. Business customers are supported to reduce their water usage, drive down energy costs, and reduce their carbon footprint.

Developer Customers

Dŵr Cymru provides services to housing, commercial and industrial developments, including major projects within our supply area, via our dedicated Developer Services team. In 2017-18, the Welsh Water Developer Services team continued to attain upper quartile performance in the water sector's Levels of Service scheme for developers, as it has done since April 2015. This is the most consistent performance across the sector in England and Wales.

Awards

In December 2017, at the Utility Week Awards in London, our Communications and Customer Strategy Team won the Utility Week Marketing Initiative of the Year Award for the Have Your Say campaign. This was followed by three further awards at the UK-wide Chartered Institute of Marketing Awards in April 2018 with the campaign winning the Best Advertising Campaign, Best Brand Building Campaign and Best Use of Innovation.

3. We have satisfied ourselves that we have sufficient processes and internal systems of control fully to meet our Obligations.

The Board has overall responsibility for the operation and effectiveness of the Group's system of internal controls and risk management. The system of controls is designed to manage the risk of failure to achieve business objectives, and comprises audited policies and procedures aimed at identifying and managing the most significant risks faced by the business.

A detailed review of risk is set out below. In considering the development of the system of controls, the Executive team reviewed the materiality and the relative cost benefit associated with each identified significant risk. The internal control systems are designed to provide reasonable assurance against misstatements, loss or failure. The key features of our system are typical for a business of our scale and complexity. They include:

- identification of key strategic risks and opportunities facing the business;
- reviewing emerging and current issues at meetings of the Executive and the Quality and Environment Committee;
- clear management accountability for risk management, supported by regular risk reporting to the Board, the Quality and Environment Committee and the Audit Committee;
- acceptable risk parameters set by the Board, particularly in the context of the business planning process for the purposes of the next five year period;
- implementing controls that recognise that the nature and balance of risk changes and evolves;
- implementing procedures that govern the approval and control of major items of capital expenditure, the acquisition and disposal of material assets, and commitment to any arrangement that could give rise to a material liability;
- ensuring that financial systems and procedures are fit for purpose for preparing management and financial accounts; and
- an appropriate design of management processes to ensure the effective direction and review of the business' operations supported by accurate and timely key performance indicators.

The Board receives assurance from independent work by Dŵr Cymru's technical advisor on regulatory reporting issues (Jacobs Engineering Group) and from the programme of internal audit, the major findings from which are reviewed at the Audit Committee and the Quality and Environment Committee.

Risk is reviewed and considered at each meeting of the Board and a strategic review of risk is considered twice a year under a process chaired by the Chief Executive, who submits an update to the Board of the Executive team's view of the key strategic risks facing the business so that this can be considered by the Board as a whole. The process to review the effectiveness of internal control includes discussion with management on significant risk issues and a review of plans for, and results from, internal and external audit. The Audit Committee reports the results of its review to the Board which then draws its collective conclusion on the effectiveness of the system of internal controls.

In fulfilling this responsibility, the Board considers periodic reports from the Audit Committee, Quality and Environment Committee and from management, and relies on its routine monitoring of key performance indicators and monthly reports of financial and operational performance. This enables the Board to review the effectiveness of the internal control system throughout the course of the year.

4. We have appropriate systems and processes in place to allow us to identify, manage, mitigate and review our risks.

All colleagues play a part in ensuring effective risk management, which is essential to underpinning decision-making at all levels of the organisation, and ultimately to ensure the long term success of the business.

Our Process

- Our systems of internal control are designed to identify, evaluate and manage risks affecting the business and these systems or internal control are regularly considered and monitored by the Audit Committee. Action plans with agreed timescales are adopted and tracked.
- Having risks identified and changes in the assessment of risks highlighted means that the Board is able to undertake its own informed assessment of the principal risks facing the company and to work with the Executive to agree the Group's tolerance of risk in these key areas on a regular basis.
- This assessment is used on a day-to-day basis to inform decision making including decisions concerning our investment programme. Every strategic update paper presented to the Board and its Committees includes a risk report and where risks identify the need for further mitigation, will include action plans with agreed timescales to enable progress to be tracked.

Our Approach to Risk Management

- Individual teams within the business take responsibility for managing risks within their areas of responsibility.
- Each business unit feeds into a "bottom up" risk management system, escalating risks through our governance structure of committees and team meetings. Risks recorded through that process are discussed during a more "top down" discussion of risk every month at a meeting of the Executive team.
- The Executive team's update on strategic risks affecting the business is reviewed at every Board Meeting and the Board carries out an in-depth review of strategic risks twice every year. The Board assesses both the current and target level of each risk.
- The Audit Committee has accountability for overseeing the risk management processes and procedures and reports to the Board on the adequacy of internal controls.
- This bottom up and top down approach to risk management provides assurance that risks are being effectively managed by the business and identifies those areas where further mitigation steps are needed.
- The Board and its Committees review a summary of strategic risks facing the business at every meeting.

Three Lines of Defence

We continue to use the 'Three Lines of Defence' model to mitigate risk of non-compliance with our processes and policies:

1. First line of defence is ownership and management of risk.
This is fulfilled by our operational teams and managers.
2. Second line of defence is risk management and risk control.
This is fulfilled by our Compliance team and internal committees.
3. Third line of defence is independent review and oversight.
This is fulfilled by Internal and External Auditors, including our technical adviser on regulatory reporting issues (Jacobs Engineering Group).

AREAS IDENTIFIED FOR IMPROVEMENT 2018/19

Our vision is to earn the trust of our customers every day. Strong governance and leadership, with the correct focus on customers at the heart of everything we do, together with properly transparent reporting, can play an important part in helping us achieve this vision.

As part of our processes to enable our Board to sign off the Risk and Compliance Statement we are mindful of the key messages outlined by Ofwat in their publication “Board leadership, transparency and governance – principles”.

Message 1 *“establish and maintain adequate procedures, systems and controls to enable companies to comply with their obligations”.*

Works Discharge Register

Under Section 166 of the Water industry Act 1991, Dŵr Cymru requires consent to make certain discharges for works purposes. A copy of the application, and any subsequent consent, must be served on any customers who live within 3 miles downstream of the proposed discharge. Section 197 requires Dŵr Cymru to keep a register of the name and address of the owners/occupiers of any property which abuts the water course affected by the Section 166 consent application.

We do not currently maintain a Register, however there have been no recent Section 166 consents applications. We are however in early discussions about a potential Section 166 application. Our Environmental Permitting Specialist is currently implementing a documented process and developing a Works Discharge Register. ✓

Written Procedures

Although there were no instances of non-compliance with legislation we identified opportunities to improve our internal written procedures for the following areas:

- Bathing Water Quality;
- Shellfish Protection;
- Marine Water Protection;
- Requests by businesses for fire hydrants;
- Interruptions to supply to carry out necessary works;
- Applications and consents for discharging Trade Effluent;
- Location of stopcock on private premises; and
- Trade Effluent Register.

In each case, a plan to improve written procedures within a three month period has been put in place. ✓

Message 2 *“a key theme that overarches the principle of Board Leadership is transparency”.*

Engaging with CCWater

The respective Licence Conditions on Codes of Practice require us to:

“consult with CCWater and consider any representations made by it about the Code”.

CCWater were consulted about the latest revision to:

- The Code for the collection of unpaid charges from household customers; and the
- Leakage Code of Practice.

However, they were not formally consulted about the 2018/19 “How we handle your complaints and compliments”. The process for handling complaints had not changed and was exactly the same as outlined in the 2017/18 Code. However, we did take the opportunity to use the revision to inform customers about our Priority Services. The revised Code was discussed with CCWater, and they were provided with a copy, at the Assessment meeting held on 1st May 2018. ✓

Although there were no changes to the complaint process for CCWater to comment on, we nevertheless see this as an opportunity to strengthen the governance arrangements surrounding the consultation and approval of Codes of Practice, other Codes (both statutory and non-statutory) and key Policies. We consider that stakeholder engagement is a cornerstone of our Company Monitoring Framework.

Compliance Code

“Competition compliance” is simply a method of making sure that we, as both the company and individuals, comply with the various legal rules which are designed to ensure that competition within the UK is not restricted. The object of these competition laws is to prohibit agreements or behaviour that damage competition in the UK market.

Our Conditions of Appointment also require us to have in place a compliance code which adheres to Ofwat guidance. Our Compliance Code complies with this guidance and provides an overview of the main rules of competition law, as applies to Dŵr Cymru, and sets out procedures and guidelines which must be followed.

Information Notice IN 16/01 Expectations for company compliance codes, issued by Ofwat in March 2016 states that:

“we also expect compliance codes to go through an appropriate level of internal approval, for example Board assurance, given the importance of these documents”.

Areas identified for improvement:

- Our Compliance Code has been approved by the Board but there was no mention of this in the Code itself. We considered that transparency would be enhanced if the Code made clear that it had been approved by the Board.
- In accordance with our Licence Condition, the Compliance Code is reviewed annually and published on our website. However, we considered that transparency would be improved if it contained a Version Control history that provided a robust trail of any amendments made. If no amendments are required following the annual review a note along the lines of “Annual update: no material change” will be made. Where appropriate, this will also be applied to all other relevant Codes and Policies.

The Compliance Code available on our website was dated April 2017 at the time of the review. The Code was reviewed in March/April 2018 and minor revision was identified. The revised version was approved by the Board at the June Board meeting for publication, and addressed both of the points raised above. ✓

Network Access Code

The Water Industry Act 1991, as amended by the Water Act 2003, permits a licensee access to a water undertaker’s supply system in order that the licensee may supply water to eligible premises. Condition S of the Conditions of Appointment requires every water undertaker to publish an access code setting out the basis upon which it will permit access to its supply system. Our Access Code complies with the Guidance on Access Codes produced by Ofwat and is reviewed annually and published on our website.

It was not readily apparent from the Access Code itself which governance function within Dŵr Cymru approved the Code. It was considered that governance would be more robust and transparent if the Code contained a “grid” showing it was approved at an appropriate level within the Company. Consequently, the Code was published in revised form at the end of June 2018. ✓

Message 3 “information is accessible to the audiences for this information”.

Codes of Practice for Non-Household Customers

Our licence obligations currently require us to submit to Ofwat: a code of practice for customers and relations with CCWater; a code of practice on debt and disconnection; and a code of practice on leakage. However, this information does not need to be packaged separately to reflect the three licence conditions.

Ofwat has made it clear that companies have freedom to design their code in a way that best meets customer needs as long as they meet their information provision obligations in their licences by reference to the information principles.

We currently have three separate Codes of Practice covering each of the above issues. However, Ofwat are currently undertaking a Licence Simplification Project that may involve combining the current three licence conditions into one consolidation condition.

We will monitor developments in this area to ensure we continue to meet our Customer Monitoring Framework objective of providing transparency and helping to build trust and confidence through “having information that is easy to understand and navigate.” We may propose consolidating the three Codes into a simple piece of guidance. ✓

Water Quality

Under Section 68 of the Water Industry Act 1991, water companies are under a statutory duty to supply wholesome water. Regulation 4 of the Water Supply (Water Quality) Regulations 2010 in Wales provides that water is wholesome if it contains concentrations or values in respect of various properties, elements, organisms and substances that do not contravene the prescribed maximum, and in some cases, minimum concentrations or value.

Each year we carry out sampling at water treatment works, service reservoirs and customer taps to ensure our water meets the European and National Standards. During the 2017 calendar year we carried out 224,032 tests and found 46 had failed the required Standard (0.02%).

An investigation report is completed for each failure and this is shared with the Drinking Water Inspectorate (DWI). Any recommendations or suggestions made by DWI are recorded in action plans with agreed timescales to enable progress to be tracked. Our Quality and Environment Committee review the findings of investigations into all water quality failures and receive regular progress reports on action plan progress. ✓

Drinking Water Safety Plans

A continuous supply of safe clean drinking water is vital to maintain public health. Ensuring the quality of that drinking water is fundamental to the service we provide to our customers. We do this by ensuring that the risks to drinking water quality are identified and managed. A Drinking Water Safety Plan (DWSP) is the most effective way of ensuring that a water supply is safe for human consumption and that it meets the health based standards and other regulatory requirements. It is based on a comprehensive risk assessment and risk management approach to all the steps in a water supply chain from catchment to consumer.

All water quality failures trigger a review of the asset specific DWSP to enable the capture of new risks and the review of existing risk scores. If any of our DWSPs identify a potential danger to human health we inform DWI immediately. The DWI may consequently issue a legal Notice requiring the company to complete a programme of remedial actions.

We currently have 28 Improvement Programmes in place and the last Notice received from DWI was in January 2017. We hold quarterly meetings with DWI to discuss progress. In addition, our Quality and Environment Committee also monitor progress against agreed timescales. Regular reports are provided to our Board. ✓

Treating Wastewater

The Urban Waste Water Treatment Regulations and the Environmental Permitting Regulations set standards for sewage treatment. For each of our wastewater treatment works there is a permit which regulates the quality of wastewater we are allowed to discharge into rivers and coastal waters.

During the 2017 calendar year we confirmed 10 non-compliant discharges out of the 559 permitted waste water treatment works discharges. Five of the ten failures coincided with challenging weather conditions in April 2017 following a period of very dry weather. These have been judged by NRW as not having any significant environmental impact.

Although this is the lowest number of total regulatory sample exceedances since 2012 the performance in 2017 has led to a comprehensive review of our compliance strategy with the stated aim of achieving 100% Waste Water Treatment Works compliance and our vision of "All works being compliant all of the time". Our performance in this area is monitored by our Quality and Environment Committee. ✓

STATEMENT OF DIRECTOR'S RESPONSIBILITIES FOR REGULATORY INFORMATION

The following confirmations from our Directors are provided to comply with the requirements of Condition F of our Licence, which requires that accounting statements are prepared in accordance with the Regulatory Accounting Guidelines issued by Ofwat. In particular, Regulatory Accounting Guideline 3.10 issued in November 2017 requires the following Statements to be made by our Directors:

- Statement of Directors' pay and standards of performance.
- Statement on disclosure of information to auditors.
- Statement on Dividend Policy.
- Statement on diversification and protection of the core business.
- Statement on Long Term Viability.
- Statement on sufficient rights and assets (sometimes referred to as Ring Fencing).

Statement on Directors' Pay and Standards of Performance

The Company is required under s35A of the Water Industry Act 1991 to provide a Statement that the remuneration paid to Executive Directors is linked to standards of performance. This Statement is provided within the Directors' Remuneration Report which can be found in our Report and Annual Accounts for 2017/18 available at www.dwrcymru.com.

Statement on disclosure of information to auditors

In the case of each of the persons who are Directors at the time when the Annual Performance Report is approved under Section 418 of the Companies Act 2006 the following applies:

- a) so far as the Director is aware, there is no relevant audit information of which the Company's auditors are unaware; and
- b) he/she has taken all the steps that he/she ought to have taken as a Director in order to make himself/herself aware of any relevant audit information and to establish that the Company's auditors are aware of the information.

Statement on Dividend Policy

Paragraph 6 and line 1A of the Appendix to Licence Condition F requires companies to report on the value of any dividend paid and provide a comprehensive explanation of the basis of the dividend.

Dŵr Cymru's ultimate parent undertaking is Glas Cymru Holdings Cyfyngedig, a company formed with the single purpose to manage Dŵr Cymru. As a company limited by guarantee, and having no shareholders, all financial surpluses are reinvested for the benefit of customers. The reserves built up from retained profits help to insulate Dŵr Cymru and its customers from any unexpected costs and also to improve credit quality to keep the cost of finance as low as possible.

A new Dividend Policy was approved by Ofwat in December 2015 and formally adopted by the Board in the June 2016 Board meeting. No monies are transferred out of the Glas Cymru group of companies under this Policy and all financial surpluses are retained for the benefit of customers. Our Dividend Policy expressly provides that dividends will not be paid unless the Directors are satisfied that this would not impair Dŵr Cymru's ability to finance its regulatory activities.

During the year to 31 March 2018 no dividends were paid or received by the Company.

Statement on diversification and protection of the core business

The Directors have resolved that a Certificate required under Condition F6A.2A be issued to the Water Services Regulation Authority confirming that in the opinion of the Directors:

- a) the Company will have available to it sufficient financial resources and facilities to enable it to carry out, for at least the next twelve months, the Regulated Activities (including the investment programme necessary to fulfil the Company's obligations under the Appointment); and
- b) the Company will, for at least the next twelve months, have available to it management resources which are sufficient to enable it to carry out those functions.

In providing this Certificate, the Directors have taken into account:

- a) the Company's Licence, which is in place on a rolling 25 year basis;
- b) the certainty on customer tariffs to March 2020 provided by the 2014 Final Determination of prices by Ofwat, following its acceptance by the Board;
- c) the financial strength of the Company and the management and other resources available to the Company as recorded in the Financial Statements for the year ended 31 March 2018;
- d) the bond programme of financing implemented by Dŵr Cymru (Financing) Limited, an associate Company, inter alia, to provide future financing for the Company (including the investment programme necessary to fulfil the Company's obligations under the Instrument of Appointment);
- e) the strong credit rating of the Company's bonds;
- f) the results from the ongoing monitoring of financial, operational and compliance controls and the risk management process reported to the Board via four formal committees; the Audit Committee; the Remuneration Committee; the Nominations Committee; and the Quality and Environment Committee. The Group's internal audit function has carried out a programme of work, which incorporates a review of the control environment;
- g) the annual review of the effectiveness of internal controls in compliance with the requirements of the UK Corporate Governance Code;
- h) the Company's formal risk and governance arrangements which are monitored by the Audit Committee and Board;
- i) the Company's employment policies and strategy;
- j) the Company's plans for the remainder of this regulatory period; and
- k) the Undertaking that Glas Cymru Cyfyngedig ("Glas Cymru") has given following the acquisition of the Company, in which Glas Cymru confirms that it (and each of its subsidiaries other than the Company) will:
 - provide the Company with all such information as may be necessary to enable the Company to comply with the requirements of the conditions of Appointments, or such additional information as the Director may reasonably require about their activities and the financing of them;
 - refrain from any action which would or may cause the Company to breach any of its obligations under the Act or conditions of Appointments;
 - ensure that at all times the Board of the Company contains a majority of Non-Executive Directors;
 - comply with the Principles of Good Governance outlined in the current UK Corporate Governance Code published by the Financial Reporting Council (or any successor document having a similar purpose or intent) as may from time to time be appended to or approved for the purposes of the Listing Rules of the UK Listing Authority; and
 - not make any changes to their respective Memorandum and Articles of Association without the consent of Ofwat.

This Directors' Certificate also confirms that in the opinion of the Directors all contracts entered into with any associated company include all necessary provisions and requirements concerning the standard of service to the Company, to ensure that it is able to meet all its obligations as a water and sewerage undertaker.

Section 6A.4(2)(a) of Licence Condition F requires our independent auditors to produce a report that sets out:

- whether they are aware of any inconsistencies between the Director's Certificate and any of the accounting records; and
- the extent to which the Company has complied with its obligations under Licence Condition F6A.2A.

A copy of the auditor's report can be found in our 2017/18 Annual Performance Report available at www.dwrcymru.com.

Licence Condition F6A.6 – Maintaining an Investment Grade Rating

The Directors confirm that throughout 2017/18 the Company, or an Associated Company as issuer of debt on its behalf, has ensured that it has maintained at all times an issuer credit rating which is an Investment grade rating. Dŵr Cymru has the strongest credit ratings in the water sector, reflecting the Company's high level of creditworthiness. The ratings of the Company's Class A and B debt at 31 March 2018 were [A/A2/A] from Standard & Poor's, Moody's and Fitch Ratings.

Statement on sufficient rights and assets

Under paragraph 3.1 of Condition K of the Licence, the Company is at all times required to ensure, so far as is reasonably practicable, that if a special administration order were made, the Company would have available to it sufficient rights and assets (other than financial resources) to enable the special administrator to manage the affairs, business and property of the Company.

The Directors are satisfied that the business has adequate resources to continue in business for the foreseeable future. Accordingly, the Financial Statements for the year ended 31 March 2018 have been prepared on a going concern basis.

Long Term Viability Statement

Our customers need to know they can rely on the services we provide over the long term. Ensuring the long-term resilience of our business, including financial resilience, is therefore a key area of focus for us. Ofwat expects companies to confirm that they are financially viable over the longer term. Our approach to doing this complies fully with section C.2.2 of the UK Corporate Code.

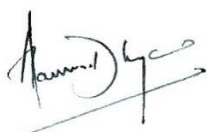
As a result of our assessment, the Directors have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period to March 2030. The Long Term Viability Statement is provided within our Report and Annual Accounts for 2017/18 which is available at www.dwrcymru.com.

Licence Condition F6.1 – Trading with Associate Companies at Arm's Length

We have an Obligation to ensure that every transaction between the Appointed Business and any Associated Company is at arm's length so neither gives to nor receives from the other any cross-subsidy. There were no transactions with any associated companies except for:

- the Directors of Dŵr Cymru Cyfyngedig are also directors of other companies within the Glas Cymru Group. However, the emoluments of the Directors are paid in full by Dŵr Cymru Cyfyngedig as their activities are predominantly related to the regulated water and sewerage business. During the year the Directors' emoluments amounted to £2,184,565 (2017: £2,267,566);
- no dividends were paid or received by the Company during the year. In 2016/17 the Company declared and paid dividends totalling £30,226,000. Distributions were made in accordance with the Company's Dividend Policy which has been approved by Ofwat and formally adopted by the Board;
- during the year £69,864 [2017: £346,038] of Welsh Water Infrastructure Ltd (WWIL) costs were paid by the Company on behalf of WWIL. This value has been included in the Company's Balance Sheet as a loan to WWIL;
- during the year £300,458 of Cambrian Utilities Limited costs were paid by the Company on behalf of Cambrian. This has been included in the Company's Balance Sheet as a loan to Cambrian; and
- intercompany interest payable to Dŵr Cymru (Financing) Limited (DCF) was £144,527,000 (2017: £124,339,000). As at 31 March 2018 the balance outstanding on the intercompany loan from DCF stood at £2,560,975,000 (2017: £2,279,260,000). All borrowings raised by DCF are immediately on-lent to Dŵr Cymru Cyfyngedig (DCC) on an arm's length basis. The Intercompany loan agreement is subject to the terms and conditions of the whole business securitisation structure of Glas Cymru Anghyfyngedig and to its subsidiaries. DCC, in its capacity as debtor, repays such principal and interest as is due on each borrowing in the due date plus a margin of 0.01%.

Approved on behalf of the Board of Dŵr Cymru Cyfyngedig,



Alastair Lyons

Chairman, Dŵr Cymru Cyfyngedig

5th July 2018



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30 May 2018

Attention: The Board
DCWW
Pentwyn Road
Nelson
Treharris
CF46 6LY

Project Name: Dwr Cymru Welsh Water (DCWW) non-financial assurance
Project Number: B2271300

Subject: 2017-18 Risk and compliance statement - assurance statement

To the Board

As set out in IN 18/07 Ofwat requires companies to publish an annual risk and compliance statement, confirming they have complied with all relevant statutory, licence and regulatory obligations and are taking appropriate steps to manage and/or mitigate any risks they face. Companies are required to do this within the context of the Company Monitoring Framework (CMF).

In preparing the statement companies are required to consider their obligations in both legislation and their licences. As with other company information, it is important that stakeholders can have trust and confidence in your risk and compliance statement. Building on our approach in the last two years, we have reviewed the processes that support the declarations in your statement.

Our review focused on the approach and processes you follow to assess your compliance with your obligations. We held meetings with your Compliance Manager, Paul Marsh and Nicola Williams (General Counsel and Company Secretary) to understand the changes and developments you have implemented since our review last year. This included a risk based check on an obligation area to test the robustness of documented existing checks and controls. In addition, we note that as part of our assurance of the information you are submitting in your Annual Performance Report (APR) and your annual scheme of charges, we have directly examined a number of the processes and controls you have in place to support your obligations in relation to reporting information and compliance with specific licence obligations.

Our main observations from our assurance activity are as follows.

- Following our feedback last year, you have continued to broaden understanding across the organisation of the areas relevant to the compliance statement.
- Through our work assuring your APR and annual scheme of charges and submissions, we have seen evidence of appropriate systems and controls.
- You have also continued to enhance your existing processes and controls by adding details in the documentation for each licence condition so that it sets the requirement

and how you achieve compliance including the relevant controls. Including details of the relevant owner, the main contact, any associated internal guidance and the governance surrounding each obligation; and,

- You have also designed a pro forma for Director's to sign off those Licence conditions for which they are responsible which you are planning to implement during 2018-19.

Last year you expanded upon the broad areas that you considered as relevant for the scope of this exercise, identifying additional key sources of legislation that impact on your activities. You have continued to assess your compliance using this broader definition of relevant obligations. We are aware that you do have processes to manage compliance with other obligations and duties, but that they are not explicitly covered as part of your risk and compliance statement (e.g. compliance with Health and Safety legislation and requirements).

As part of our review across the sector we observed that some companies continue to note exceptions, or areas for improvement as part of their annual statements. For example, in 2016-17, United Utilities referenced that five Wastewater Treatment works were not complying with their discharge consents. We understand that you are proposing to list three breaches of your obligations relating to: -

- sample failures under Section 68 of the Water Industry Act 1991,
- non-compliant discharges from permitted waste water treatment works under UWWTD and Environmental Permitting Regulations; and
- the failure to upload the revised version of your Compliance Code onto your website.

We recommend that areas where exceptions and potential compliance risks have been identified are noted and address in your assurance plan. As the statement is not required to be part of the APR for 2017-18 we recommend that you link to the APR where you can provide further information on your performance.

We note that whilst enhancements have been made to the process, we consider there are opportunities for improvement. Last year we recommended that you embed ownership of these obligations in the business and look to obtain formal sign off for each area on an annual basis. Whilst we note progress has been made in identifying owners we recommend that annual sign off would help to reduce risk across the organisation. This sign off should cover a review risks, the sufficiency of current processes and controls, and annual compliance. We observed that you have not obtained formal sign off by respective owners for 2017-18 although we understand you are considering introducing a formal process for 2018-19.

We observed that you already capture information on governance (checks and controls) for each obligation, but we note that you have not yet put in place a process to verify the application or test the robustness of the checks and controls. As part of your work preparing the 2017-18 Risk and Compliance Statement we observed that you have identified some areas where these controls were not applied, for example relating to the requirement under Licence Condition R to review your Compliance Code.

As your process continues to mature we recommend that the focus of your process would benefit from being more proactive and recommend moving towards risk based verification and evidencing of documented checks and controls. In addition, for each of the obligations, we recommend that part of the verification should challenge respective owners to identify and document who/what part of the organisation need to be aware of the obligation.

We understand that both the Legal team and individual teams in the business carry out horizon scanning to identify new legislation. We consider that this process could be improved by embedding it into the risk and compliance process, for example you could include a formal requirement for an annual review of the obligations and duties by respective obligation owners

as part of your overall annual risk and compliance process. This could include verification as to who/what parts of the business need to be aware.

We therefore consider that, other than where indicated otherwise in this letter and/or the feedback we provided:

- you have a full understanding of the company's relevant obligations (as you have interpreted the scope required for this exercise); and
- you have appropriate systems and processes in place to run your business and identify and manage risks in a way that meets the relevant obligations (as you have interpreted the scope of these).

Yours sincerely

A handwritten signature in black ink, appearing to read 'A McGeoghan', with a long horizontal flourish extending to the right.

Andrew McGeoghan

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