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PR19

Board Assurance Statement

September 2018



Welsh Water
PR19 Board Assurance Statement
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Introduction

This statement has been produced in support of Dŵr Cymru Welsh Water's PR19 Business Plan. It sets out, in accordance with Ofwat's guidance, the Board's assurances on the quality of the submission's content and the process followed in preparing the plan itself.

Dŵr Cymru is a non-shareholder company, so the members of its Board are motivated solely by the interests of customers, rather than returns to shareholders. This plan is intended to deliver on the company's six promises to our customers, while also meeting its statutory duties and obligations.

The Board has provided strategic leadership and direction to the preparation of the company's PR19 plans from the outset of the process. The resulting plan is fully endorsed by the Board as delivering the best value to customers and the environment, over the next five years and beyond.

a. Business planning

Ofwat assurance requirement 1

How the Board has challenged and satisfied itself that all the elements add up to a business plan that is high quality and deliverable (and how it has challenged management to ensure this is the case).

The Board is satisfied that its Business Plan, taken as a whole, constitutes a high quality plan, affordable for customers. It includes stretching targets for customer service, for support for customers in vulnerable circumstances, for environmental performance and for cost efficiency, together with improved long-term service resilience and better value for money for customers.

The Board has provided detailed leadership of all aspects of the Business Plan throughout its development. Because our company is unique in that it has no shareholders, we are able to focus purely on the long-term interests of our customers.

- The Board set the approach to PR19 at the outset of the process in September 2016, requiring the plan to be driven by the views of customers and to be developed in the context of a long-term vision for Welsh Water in 2050.
- In 2017, the Board set the Strategic Parameters for the Business Plan, based on the extensive first phase of our customer engagement programme, ensuring that the plan strikes the optimal balance for customers between investment requirements for service improvements and resilience, and affordability for customers, both over the next five years and longer term.
- The Board has challenged management through an ongoing process of review at each stage of the development of the plan, to ensure that the targets set are challenging and deliverable, reflecting the criteria set by Ofwat, customer views, and historical and comparative information.
- The company has engaged directly with the Customer Challenge Group and other key stakeholders, including Natural Resources Wales and the Drinking Water Inspectorate, during the development of the plan. Board members have also attended customer engagement sessions and reviewed extensive customer research findings, to develop a personal understanding of customers' needs and priorities.
- The Board has reviewed its plan against Ofwat's expectations as set out in its detailed methodology statement and found it to have met the requirements for a high quality plan. Having approved a comprehensive assurance plan it has also had the benefit of external assurance from the Reporter and our Auditors on key aspects of the plan and supporting data, where appropriate.
- At the end of the process, the Board commissioned independent research into the overall acceptability of the plan for customers, which found that 92% of customers found the plan acceptable and 95% found it affordable (including those who considered that it would be affordable at "a stretch"), with consistently high support across all customer groups.

The Board is also satisfied that it is a financeable and deliverable plan, having reviewed the main delivery risks, planned mitigations, and also the financial and corporate resilience of the business to a range of severe and combined risk scenarios.

a. Business planning

Ofwat assurance requirement 2

How it has challenged and satisfied itself that the overall strategy for data assurance and governance processes delivers high-quality data

The Board is satisfied that the PR19 submission delivers **high-quality data** that has been subject to appropriate assurance.

- The Board approved a PR19 Assurance Framework which set out a systematic approach to ensuring that elements of the plan were subjected to appropriate assurance based on their impact on the plan.
- Lower risk elements have been subjected to appropriate internal assurance processes which include expert review, sign-off by data owners and overall Executive sign-off.
- The 'high risk' elements have also been subjected to external assurance from expert and independent third parties.

a. Business planning

Ofwat assurance requirement 3

How it has challenged and satisfied itself that the business plan will enable the company to meet its statutory and licence obligations, now and in the future and take account of the UK and Welsh Government's strategic policy statements

The Board is satisfied that the business plan will enable the company to meet **its statutory and licence obligations**, now and in the future, and takes into account the Welsh Government's Strategic Priorities and Objectives Statement to Ofwat.

- The Board has ongoing mechanisms to understand the company's statutory and licence obligations and to ensure that they are being met. We have reviewed the relevant obligations that are not explicitly covered by the Risk and Compliance Statement and confirmed that no additional provision is required in our PR19 plans to account for them.
- We have taken into account the relevant existing obligations in developing the PR19 Business Plan. Any new obligations, such as those arising from the National Environment Programme (NEP) or the DWI, have also been addressed.
- There is no aspect of our business plan that prejudices our ability to meet our obligations through to 2025. For example, there is sufficient provision for maintenance of our treatment works and networks.
- We are therefore confident that the Board can provide assurance that the PR19 business plan enables the company to meet its statutory and licence obligations.
- In addition, our long-term planning document, Welsh Water 2050, is aligned with the Wellbeing Goals of the Well-being of Future Generations (Wales) Act 2015.
- We have reviewed the Welsh Government's Strategic Priorities and Objectives Statement to Ofwat, and the Water Strategy for Wales (2013), and confirm that our plan takes account of these objectives, which we fully endorse.
- We have engaged positively on our approach with the Welsh Government and other key stakeholders (CCG, NRW, DWI, CCWater).

a. Business planning

Ofwat assurance requirement 4

How it has challenged and satisfied itself that its plan will deliver operational, financial and corporate resilience over the next control period and the long term through its governance and assurance processes, taking account of its track record of performance

The Board has satisfied itself that its plan will deliver **operational, financial and corporate resilience** over the next control period and the long term through its governance and assurance processes, taking account of its track record of performance.

- We have developed a long-term plan - Welsh Water 2050 - which included a resilience framework (the Welsh Water 'Resilience Wheel') tested against worldwide best practice in the industry and beyond.
- We have conducted an external assessment of all aspects of resilience set out in the Resilience Wheel, comparing the current status and the status following implementation of our AMP7 plans for performance improvement and investment, with industry best practice benchmarks where available to guide the objectives we have set.
- We have tested and confirmed the financial resilience of the company to 2030 using a challenging set of financial scenarios, in accordance with Ofwat's guidance, using our PR19 plans as the baseline.
- We have a strong record of delivery against targets for cost efficiency and performance which we proposed at PR14, as demonstrated by published information in our Annual Performance Report.
- We have strong ongoing governance and risk management processes and procedures which protect the delivery of the essential services that we provide against unexpected shocks and stresses. These are set out in our Risk and Compliance Statement as part of our Annual Performance Report, in our annual Company Monitoring Framework, and in the Corporate Governance section of our Annual Report.

a. Business planning

Ofwat assurance requirement 5

How it has challenged and satisfied itself that it will enable its 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 such as its corporate and financial structures.

The Board is confident that our plan will maintain and enhance **customers' trust and confidence**.

- Securing and retaining the trust of our customers is at the core of everything we do, as reflected in our Vision 'Earning the Trust of Our Customers Every Day'. Transparency and engagement play an important role in achieving this.
- We are required under our licence to comply with the requirements of the UK Corporate Governance Code as if we were a listed company and the Board is answerable to our independently selected Members at each of our AGMs, just as a listed company is to its shareholders.
- In following the UK Corporate Governance Code, we fully disclose and explain our Group corporate and financial structures in our Annual Report, together with our dividend policy, our policy for returning outperformance to customers via 'customer dividends' and full details of our executive remuneration. We also include a long-term financial viability statement, most recently for the period to 2030.
- All our companies are registered in the UK. Dŵr Cymru Finance Limited is also registered in the Cayman Islands. It has always been UK resident for tax purposes and this has not caused any customer or stakeholder concerns. We are, however, implementing plans to repatriate this company fully to the UK.
- Dŵr Cymru Welsh Water is a wholly owned subsidiary of Glas Cymru. We publish our financial results in our Annual Performance Report which appears on our website. It is discussed with our Customer Challenge Group, the Consumer Council for Water and the Members of the company.
- Our Annual Report provides full transparency on our performance, and we review it each year, taking into account feedback from stakeholders, to ensure that it is as easy as possible for customers to understand.
- We publish an annual Impact Report for customers and we have taken steps to maintain and increase customer awareness of our not for shareholder model in AMP6 and will continue to do so in AMP7.
- Executive remuneration is linked to challenging customer performance objectives and is subject to approval by Members each year.

a. Business planning

Ofwat assurance requirement 6

How it has provided ownership of the overall strategy and direction of the plan in the long term.

The Board has provided **ownership of the overall strategy and direction** of the plan, including setting it firmly in the context of our long-term plan - Welsh Water 2050.

- The Board set the approach to PR19 at the outset of the process in September 2016, requiring the plan to be driven by the views of customers and to be developed in the context of a long-term vision for Welsh Water in 2050 - see statement (a1) above.
- Substantial time has been allocated to the PR19 process at 17 Board meetings since September 2016.
- Internal planning processes and external stakeholder engagement have been subject to ongoing Board oversight.
- All strategic decisions have been made at Board level.
- Feedback from the CCG and Members of Glas Cymru have been taken into account.
- Board members have attended the CCG and the CCG Chair has provided updates to Board meetings on six occasions as to the progress being made by the CCG and their issues and challenges.
- Board committees have met regularly with environmental and drinking water quality regulators to understand their objectives and challenges.

b. Customer engagement

Ofwat assurance requirement 1

Assurance that the company's business plan has been informed by customer engagement.

The Board confirms that the plan has been **informed by an innovative, differentiated and wide-ranging customer engagement programme.**

- As set out in statement a1 above, our approach to PR19, agreed by the Board, was to develop a long-term strategy, Welsh Water 2050, setting out what we need to achieve in the context of the stated priorities of customers determined by specific research and consultation. Our plan has, therefore, been based on, rather than informed by, customer engagement. This then provided the basis for the development of PR19 as an important step forward in the implementation of our long-term plan.
- The company's decisions are informed by an ongoing, thorough and wide-ranging programme of customer engagement, for example 'Have Your Say' campaign in 2016. Around 40,000 customers have participated in this process, a 'step change' compared to the PR14 process.
- A comprehensive programme of customer research and engagement has been carried out specifically for PR19, which was reviewed and approved in advance by the Board. The Board has itself provided oversight of the customer engagement programme and has been involved directly by observing focus groups. Members of the Board have also attended selected CCG meetings to talk directly with CCG members.
- The Board has itself reviewed the outcomes of each of the three phases of customer research and further developed the plan in light of those results.
- Two workshops have been held on PR19 for the Members of Glas Cymru.
- The Board decided to commission "options testing" customer research during the later stages of the development of the plan, in which customers could choose between different packages of service and bills. The resulting final plan was then subject to final "acceptability" research, which found that 80% of customers found the plan acceptable (on an "uninformed" basis) and 92% once the plan had been presented to them ("informed" basis).

b. Customer engagement

Ofwat assurance requirement 2

Assurance that the company's business plan has been informed by feedback from the company's CCG about the quality of its customer engagement and how this has been incorporated into its plan.

The Board confirms that the business plan has been **informed by feedback from the CCG** about the quality of its customer engagement and that this has been incorporated into its plan.

- Members of the Board have attended CCG meetings on several occasions.
- The CCG Chair has attended Board meetings on six occasions and provided written updates to Board on progress with the customer engagement programme. The customer engagement programme has taken account of CCG views and feedback on an ongoing basis.
- The Board and Executive have responded to the written statements from the CCG Chair provided after each CCG meeting as to the challenges and issues raised in relation to the customer engagement programme, and the way in which its results have been incorporated into the plan.
- The Board has reviewed the CCG report.

c. Affordability

Ofwat assurance requirement

Assurance that the company's business plan is affordable for all customers, including in the long term and including appropriate assistance for those struggling, or at risk of struggling, to pay.

The Board has taken all reasonable steps to ensure that the business plan is **affordable for all customers**, including in the long term and including appropriate assistance for those struggling, or at risk of struggling, to pay.

- Affordability has been a primary consideration in the Board's deliberations on the company's plans during the development of PR19. This is especially the case in a region that has average incomes below the UK average, and a relatively high poverty rate.
- In this context the company will have delivered ten years of below inflation (RPI) price increases by 2020.
- We have done this while maintaining a strong balance sheet and credit rating, to ensure that bills are sustainable and do not impose an undue burden on future customers.
- Our PR19 plan delivers a substantial real terms reduction in bills by 2025 and a forecast to 2030 that demonstrates that the resulting lower level of real bill is broadly sustainable over the longer term.
- 95% of customers surveyed say that they consider our proposed average household bills for 2020-25 to be affordable (including those who say it will be affordable at "a stretch"). Our research programme has explored in depth the views of vulnerable customers and non-household customers as well as household customers.
- Our plan will deliver a £22 reduction in the average bill for household customers in 2020, and flat bills in real terms thereafter until 2025.
- We have by far the highest number of customers on social tariffs in the industry, and we plan to increase this number by a further 50% to 150,000 during AMP7, with a direct financial contribution ('customer dividend') from the company above and beyond the customer cross-subsidy, with the latter being maintained at around the current level in line with the feedback from our consultation with customers.
- Our social tariffs are targeted at those who struggle to pay, or who are at risk of struggling to pay, and offer a substantial discount on the average bill. We also provide advice on metering, water efficiency, payment options and benefit entitlement to help those customers.

d. Outcomes

Ofwat assurance requirement 1

Assurance that the business plan will deliver – and that the Board will monitor delivery of – its outcomes and performance commitments.

The Board is confident that the business will deliver the **outcomes and performance commitments** set out in the plan, and will monitor delivery of the outcomes and performance commitments on an ongoing basis.

- The Board has scrutinised and challenged evidence provided by the Executive that the company can meet the stretching targets set out in the business plan.
- Performance against regulatory commitments is monitored by the Board on a monthly basis against annual and 5-year targets.
- The Board has reviewed the key risks associated with delivering the plan, together with planned mitigating actions.
- We have a strong record of delivery against targets for cost efficiency and performance which we proposed at PR14, as demonstrated by published information in our Annual Performance Report.
- Remuneration schemes (both for Directors and for the Colleague Reward schemes) are based on the delivery of stretching targets both for operational performance for customers and also for progress towards long-term service and resilience objectives. Details of our remuneration schemes are published in our Annual Report and Accounts and approved by Members at our AGM.

d. Outcomes

Ofwat assurance requirement 2

Assurance that the company's proposed outcomes, performance commitments and outcome delivery incentives (ODIs) reflect customer preferences and are stretching.

The Board is satisfied that the proposed outcomes, performance commitments and ODIs, taken as a whole, reflect customer preferences and constitute **a stretching set of performance targets** that will represent a significant performance improvement for customers.

- The Board has reviewed the results of research into customers' preferences for performance targets, including willingness to pay and ODIs.
- It has also reviewed proposed targets against its current performance relative to the rest of the industry, and taken into account both historical and projected upper quartile performance.
- The Board has challenged management to ensure that stretching targets have been set for performance measures and cost efficiency, which are both challenging and deliverable.
- The Board has challenged and approved our innovation plan and investment programme, in support of the performance improvements that underlie our plan.

d. Outcomes

Ofwat assurance requirement 3

Assurance that the company's proposed approach to reporting on its performance commitments, ODIs and projections of outcomes is robust.

The Board is satisfied that the company's approach to **reporting on its performance commitments**, ODIs and projections of outcomes is robust.

- The Board has put in place an audit and assurance framework designed to allow the systematic monitoring and evaluation of the various aspects of our performance to ensure that appropriate standards of quality are being met. This involves a “3 lines of defence” model for ensuring compliance with reporting requirements, with appropriate governance arrangements, close involvement by our Board in the assurance process, and the right level of independence in the process by our Reporter and auditors providing third party review and challenge.
- Every year, the company consults with relevant stakeholders (Customer Challenge Group, CCWater, Welsh Government, DWI and NRW) on the form and content of its Annual Performance Report, to ensure that its reporting meets the needs of customers and stakeholders.

e. Resilience

Ofwat assurance requirement

Assurance that the company's business plan has been informed by

- a robust and systematic assessment of the resilience of the company's systems and services
- customers' views about managing resilience
- a comprehensive and objective assessment of interventions to manage resilience in customers' long-term interests.

The Board confirms that the company's PR19 plans have been informed by:

- a robust and systematic assessment of **the resilience of the company's systems and services**;
 - customers' views about managing resilience; and
 - a comprehensive and objective assessment of interventions to manage resilience in customers' long-term interests.
- The company's long-term plans were informed by a review of global best practice on resilience, working with Arup, Cardiff University and others.
 - The company developed and published for consultation a major document setting out its long-term vision in the context of a 'Resilience Wheel' developed with Arup, which covers operational, corporate and financial resilience, and how it intends to respond to long-term challenges and opportunities – Welsh Water 2050.
 - The company has undertaken a number of customer research projects in which we have asked their views on how we should respond to long-term challenges the company is facing, including a major public consultation on Welsh Water 2050. We changed and enhanced our Welsh Water 2050 plan in light of customer and stakeholder feedback.
 - We commissioned an external review of the state of resilience in the company against the Welsh Water Resilience Wheel, which identified strengths and opportunities for improvement, and which the company has taken into account in developing its plans for AMP7, AMP8 and beyond. The external consultants were then asked to re-assess our resilience levels, in light of our plans for AMP7 and beyond, to give a quantification of the progress that will be made.
 - Our investment proposals for PR19 are the result of an objective assessment of the most cost effective interventions over the long-term to manage resilience, with input from NRW and DWI as to where they see the principal areas for improvement. This has included optioneering considered by the Board to select the most appropriate solution to meet resilience requirements.
 - The Board has reviewed the investment and business plans for AMP7 and AMP8 in light of progress towards its goals set out in Welsh Water 2050 and customers' views on long-term service priorities, resulting in increased emphasis in the plans on certain resilience priorities.
 - We maintain an internal corporate risk register and risk management system which is regularly reviewed and updated at Board level. This includes risks to the company's systems and services.
 - We have developed our own scorecard which looks systematically at the resilience of critical assets and plans for significant improvement on these scorecards over the next period and beyond, with bespoke ODIs to incentivise improvements in asset resilience in the long-term interests of customers.

- We conducted our own internal lessons learned review of the company's performance during the Storm Emma and freeze-thaw of March 2018 and have set out a programme to implement the lessons learned from those reviews, which will be completed in the current year. We have reviewed the findings of the reports from Ofwat, the Consumer Council for Water and the Drinking Water Inspectorate and responded appropriately.
- We have assessed the service areas where we have most progress to make against standards in the rest of the industry, and prioritised our process improvements and investment in order to make significant progress during the next AMP, whilst striking the right balance between investment and affordability.

f. Cost assessment

Ofwat assurance requirement 1

Assurance that the expenditure forecasts included in the company's business plan are robust and efficient.

The Board confirms the expenditure forecasts included in the company's business plan **are robust and efficient**.

- We have conducted a detailed internal cost efficiency planning process over more than 12 months, which has been subject to regular Board review and challenge.
- Our expenditure forecasts for AMP7 have been subject to external review and challenge by Jacobs.
- We have set challenging efficiency targets for AMP7 capital delivery through our Capital Alliance, which are reflected in new commercial arrangements for AMP7, including incentivisation of cost outperformance, which have been subject to Board scrutiny and approval.
- We are negotiating commercial arrangements for our new AMP7 Network Alliances, to incentivise the most cost-effective delivery of water and wastewater network maintenance and investment activities.
- Capital projects are costed using a well-established unit cost database, with ongoing efficiency targets to incentivise further improvements.
- Cost efficiency plans target around a 10% reduction total costs over the AMP7 period as a whole, as compared to current levels of cost efficiency.

Ofwat assurance requirement 2

Assurance that large investment proposals are robust and deliverable, that a proper assessment of options has taken place, and that the option proposed is the best one for customers.

The Board confirms that the **large investment proposals are robust and deliverable**, that a proper assessment of options has taken place, and that the option proposed is the best one for customers.

- The Board has received assurance from the Executive including those directly responsible for the delivery of investment schemes that the proposals are robust and deliverable, following discussion with the responsible Directors of the Capital Alliance partners.
- All major capital schemes are subject to optioneering to determine the best value solutions, managed through a Gateway process which is overseen by the Executive team.
- The Board reviewed in June 2018 the optioneering process for investment schemes. Board Committees have also reviewed the choice of lowest whole life cost options for several major investment programmes, including Zonal Studies, reservoir safety and the Loughor estuary improvements.
- An optioneering assessment assessing the lowest cost option to meet customers' future demands is integral to our Water Resources Management Plan process, which was reviewed and approved by the Board in October 2017.
- We commissioned a detailed study of eligible schemes to assess their suitability for a Direct Procurement approach to delivery, with review by KPMG.

g. Risk and return

Ofwat assurance requirement

Assurance that the Board has identified the risks associated with delivering the plan.

Assurance that the risk mitigation and management plans the Board has in place are appropriate.

The Board confirms that it has **identified the key risks** associated with delivering the plan and that the **risk mitigation and management plans** the Board has in place are appropriate.

- The Board has reviewed the key risks associated with delivering the plan, together with planned mitigating actions.
- The Board has considered the potential impact of a number of risk scenarios, including all the risk scenarios prescribed by Ofwat and our own combined scenarios, out to 2030.
- Our ongoing operational risks are captured and managed in our Investment Manager system, which proposes mitigating investments. This has been used to derive our AMP7 plan.
- The company has a system of internal controls which includes management of strategic risks, which the Board reviews on a regular basis and which is subject to external scrutiny and assurance.
- We provide a comprehensive report to customers on strategic risks, trends and mitigations in our Annual Report.
- Our Welsh Water 2050 document identified 8 future risks and trends to 2050, which were used to prioritise investment plans and our innovation programme.

h. Financeability

Ofwat assurance requirement

Assurance that the company's business plan is financeable on both the notional and actual capital structure and that the plan protects customer interests in both the short and the long term. The statement should clearly set out the steps taken to provide this assurance.

The Board confirms that **the company's business plan is financeable** on both the notional and actual capital structure and that the plan protects customer interests in both the short and the long term. Our plan delivers financial metrics consistent with sustaining investment grade credit ratings across the period, on both a notional and actual basis, evaluated out to 2030.

- The Board has considered the implications of the company's non-shareholder constitution, in the actual capital structure, and has approved targeted levels of gearing that are lower than the average of the sector, consistent with maintaining credit ratings that assure access to financial markets.
- We have tested our plan with satisfactory outcomes in the round against the financial 'sensitivities' scenarios set out by Ofwat in their response to the 'Restoring the Balance' consultation and our own combined downside risk scenarios, in all cases modelled to 2030.
- KPMG performed a set of agreed upon procedures on the inputs and outputs of the Ofwat financial model that has been used to generate the financial metrics. We also asked KPMG to prepare a report benchmarking credit ratings and observed credit metrics across the sector.
- We publish a long-term viability statement in our Annual Report and Accounts, the latest of which gives assurance for the 12-year period to 2030.
- The Board have considered and approved potential financial mitigation measures which could be used to protect the business and customers against prolonged and extreme downside financial scenarios.