SRN-DDR-057: Ofwat's Quality and Ambition Assessment (QAA)
Draft Determination Response

28th August 2024
Version 1.0

from Southern Water

Contents

1 Summary

1.1 General Comments

Ofwat's Quality and Ambition Assessment (QAA) has its origin in PR14 and is based on incentives to address information asymmetry between regulator and company to encourage water companies to submit 'ambitious' and high-quality business plans.

In this response we explain why we have concerns with the QAA assessment and why we believe its design and application are no longer fit for purpose. We also respond to Ofwat's assessment of material issues around Board assurance, deliverability, financial resilience, and dividend policy. We have addressed each area, or explained how we will address each area, within our wider draft determination consultation response. We provide our draft Delivery Action Plan, a commitment to Ofwat's Delivery Monitoring Framework and our Financing Action Plan as part of our overall Draft Determination response. We also respond to Ofwat's assessment of non-material issues and respond on areas where, despite meeting Ofwat's minimum expectations, questions were raised with our original submission.

1.2 Ofwat's QAA of Southern Water

Whilst Ofwat acknowledges that our October 2023 Business Plan demonstrated a sufficient level of ambition, Ofwat's Quality and Ambition Assessment (QAA) gave an overall categorisation of our business plan as 'inadequate'. We disagree with this result, especially given the challenges facing the sector generally and Southern Water in particular, including the peculiarities of region and the associated step-change of our outputs compared with AMP7, which we feel we submitted good quality plans and targets that we feel are very ambitious.

We have concerns about the QAA incentive mechanism, both in terms of its design and its application, which we believe are no longer fit for purpose.

The design of the QAA has led to:

- **Discouragement of genuine information revelation:** We believe there are perverse incentives at play in the QAA, whereby companies are discouraged from revealing accurate forecasts and information. This runs counter to standard principles of economic regulation and may result in materially less accurate information being provided by some water companies; and
- **Disproportionate penalties**: These are not in line with regulatory precedent, and do not reflect the nature of any perceived deficiencies in our business plan. The incentive design is not proportionate to the benefit or harm any information asymmetry causes for customers and there is limited granularity in the incentives (i.e. pass or fail without any graduated assessment). The extreme nature of the penalties compounded with an already excessively challenging Draft Determination (including insufficient cost allowances, returns, and risk calibration) results in an overall risk and return package that falls far below what any company could reasonably accept. The result is that both penalties and cost sharing rates do not relate to the efficient costs of running the operation and financing its functions, which are statutory roles of Ofwat.

In terms of its application:

- **Focus is not on material areas:** In particular, those areas that matter to customers such as companies' positions on costs and outcomes. Indeed, one of the companies that was assessed as 'outstanding' did not meet Ofwat's requirements on outcomes. Southern Water appears to have been primarily penalised for raising concerns with deliverability (and despite also including a clear set of plans to improve its delivery capacity), and for caveating that its financial resilience and investability were contingent on regulatory mitigations being accepted.

The risk and return package as set out in the final methodology was not appropriate for the sector, as we have responded on separately. Furthermore, in its Draft Determination, Ofwat has proposed additional changes e.g., changing cost sharing rates, adding the MeX incentives into the ODI sharing mechanism, introducing new gated processes, and additional forms of indexation, among others. It is hard to see how any company could have credibly made an un-caveated assurance statement endorsing a regulatory framework that Ofwat itself has now materially moved away from; and

- **Decisions appear arbitrary:** The QAA assessment relies heavily on subjective assessments of business plans. There is a lack of clear, objective benchmarks or thresholds for business plan categorisation.

Further details on each of these points are set out in the following section.

As a result, we believe that the penalties and asymmetric cost sharing rates set, because of the QAA, should not apply to Southern Water in the Final Determination, especially given the further evidence and assurances we are providing in our response. Similarly, we see little reason why so many companies should receive positive QAA rewards despite proposing a less ambitious set of plans.

2 Concerns about QAA Mechanism

2.1 Discouragement of genuine information revelation

Effective economic regulation relies on the principle of the revelation of reliable, accurate and transparent information from regulated entities to regulators and other stakeholders. **The QAA however incentivises companies to align with Ofwat's assumptions rather than providing complete, truthful, and company-specific data.**

For example, the expectation on Outcome Delivery Incentives was to align with Ofwat's incentive rates. Despite the flaws and timing of the publication of Ofwat's ODI research, companies were identified as not meeting Ofwat's expectations if they proposed alternative incentive rates which prevented taking into consideration best available data or having rates that aligned to customer priorities.

By setting minimum expectations that include the use of Ofwat's assumptions (e.g. on the allowed return on capital and ODI rates based on sector-wide research), the QAA incentivises conforming to regulatory policy positions, rather than revealing company own data and insights to calibrate a package that better meets the priorities of our customers, stakeholders and the environment.

There is a risk that the QAA framework stifles innovation and has limited Ofwat's line of sight to companies' own customer research and the risks and challenges within the sector. This may limit Ofwat's ability to truly understand the challenges faced by individual companies and tailor effective regulatory responses.

A key concern is that the **QAA incentives may inadvertently have led to some companies not revealing their true or complete risk positions** within their business plan - simply to meet Ofwat's minimum expectations and achieve financial rewards. The QAA did not account for any evidence of a company's own risk analysis in decision making so companies' plans are likely to be carrying more risk than has been revealed to Ofwat. **This may hinder Ofwat's ability to appropriately balance risk and reward in the framework.**

Similarly, it is possible that some companies have understated their cost proposals, resulting in lower cost allowances for the sector due to Ofwat's approach to comparative benchmarking. This could potentially explain why all but one company has overspent allowances through the first four years of AMP7.

The PR19 CMA re-determination highlighted the importance of incentivising information revelation stating that *"contrary to Ofwat's assumption in its submissions, we agree that it is appropriate for our determination to support the principle of providing incentives for information revelation."*[1]

Ofgem's RIIO business plan incentive similarly places significant emphasis on 'truth-telling' with specific incentives attached to complete and transparent information – not just conforming to the regulator's assumptions. Ofwat's QAA is a conformity incentive and does not incentivise accurate information revelation.

2.2 Disproportionate penalties

Our projected financial penalty is 30 bps on RoRE along with a 60:40 cost-sharing rate that will be applied to base expenditure. This is disproportionately large and does not reflect the nature of any perceived deficiencies in our business plan nor the efforts we have made to address Ofwat's concerns since October 2023. The result is that penalties and cost sharing rates bear little resemblance to the efficient level of costs that a regulatory methodology should be looking to identify, undermining financeability and investability in the sector, just when the requirement for investment is increasing at an unprecedented rate.

At PR19, only those companies who were 'fast-tracked' at Ofwat's Initial Assessment of Plans (IAP) stage received an upfront 10 bps RoRE uplift reward. There was no upfront RoRE penalty for those companies identified as requiring 'significant scrutiny'. **PR19 incentives and penalties were applied with a view to encouraging improvement in plans rather than the QAA framework which applies punitive penalties for perceived deficiencies.**

The CMA PR19 re-determination identified that varied cost-sharing rates may lead to unintended consequences, for example *"to avoid being penalised in relation to cost-sharing rates when there is a difference between a company's genuine efficient costs and the results of Ofwat's modelling of an efficient company, a company may seek to under bid on its costs"*[2]

The CMA departed from Ofwat's PR19 determination and determined that that a 55:45 cost sharing rate (i.e., less asymmetry than Ofwat's QAA) between companies and customers was more appropriate to:

> *"(a) Be sufficiently close to a symmetric cost-sharing rate to avoid creating a significant risk of perverse incentives, particularly over multiple periods.*
>
> *(b) Maintain a distinction between the rates applied to fast and slow track companies, as part of the package of information revelation incentives applied in AMP7.*
>
> *(c) Avoid some of the potential distortions which result from the formulaic approach, particularly the theoretical incentive to under-bid in some areas of base and over-bid in some areas of enhancement; and*
>
> *(d) Balance the need to set strong efficiency incentives with the need to appropriately mitigate the risks of over or under performance, some of which will be likely to relate to factors outside the companies' control."*[3]

[1] Final report (publishing.service.gov.uk) pp6.101
[2] Final report (publishing.service.gov.uk)pp6.90
[3] Final report (publishing.service.gov.uk) pp6.105

The asymmetry provided through the QAA cost-sharing mechanism potentially creates a perverse incentive to under-invest earlier in multi-AMP schemes which may run counter to Ofwat's objective of encouraging companies to make the right decision now for the long-term.

The strength of Ofwat's PR24 QAA incentive produces a disproportionate gap in rewards and penalties between the categories of companies' plans that does not accurately reflect the difference in the quality of business plans and their ability to deliver outcomes for customers and the environment.

Ofgem's recent RIIO-3 sector specific methodology decision related to its Business Plan Incentive is clear that it is only intended to issue *"rewards or penalties where there is a genuine information asymmetry, calibrating the value to be proportionate to the benefit or harm caused to consumers."*[4]

The QAA incentive design is not proportionate to the benefit or harm any information asymmetry caused to customers and there is limited granularity in the incentives i.e., Ofwat passes or fails companies into the categories without any graduated assessment.

Should Ofwat seek to still apply its QAA in the Final Determinations, we believe that our Draft Determination response should help to improve Ofwat's quality assessment of our plan and move Southern Water out of the 'inadequate' category.

2.3 Focus is not on material areas

The **QAA outcome appears to lack focus on very important areas of the price review framework, particularly those areas that matter to customers such as companies' positions on costs and outcomes**. Although the QAA scoring mechanism and weightings are generally opaque, it appears Ofwat has placed a disproportionate and far greater emphasis on areas such as board assurance statements and commentary as to deliverability of the plan, notwithstanding clear evidence of deliverability challenges, rather than on outcomes for customers.

The governance and strategic oversight of company boards are crucial to the business planning process. However, the **quality of a water company's business plan should be centred on the capacity to deliver outcomes for customers and the environment at an efficient cost** – not whether Ofwat agrees or not with the reasonable caveats that boards have no choice but to include within their assurance statements given the various challenges and uncertainties faced. This is particularly notable for the deliverability challenges and associated concerns raised by companies, for example, on the deliverability challenge related to WINEP. Companies appear to have been penalised for providing qualifications based on the inherent uncertainties within their business plans driven by emerging regulatory requirements.

We raised legitimate concerns with Ofwat around the uncertainty in delivery of some of our schemes in AMP8. The delivery mechanisms subsequently afforded to us (and Thames Water) support the qualifications within our board assurance statements on deliverability of the October 2023 business plan. **Our board's approach to these deliverability challenges was to directly acknowledge them and set out a series of plans for further increasing the company's delivery capacity.** We believe these qualifications should be acknowledged by Ofwat as evidence of robust corporate governance and risk management rather than being penalised for disclosing these concerns.

[4] https://www.ofgem.gov.uk/sites/default/files/2024-07/RIIO_3_SSMD_Overview.pdf pp7.28

2.4 Decisions appear arbitrary

The QAA assessment relies heavily on subjective assessments of business plans. There is a lack of clear, objective benchmarks or thresholds for business plan categorisation.

The criteria for meeting Ofwat's minimum expectations were not sufficiently detailed or transparent, providing Ofwat with a significant degree of discretion in making subjective decisions. This has resulted in Ofwat decisions that appear arbitrary; this undermines the fairness of the assessment framework.

Some of Ofwat's assessments, particularly in areas like deliverability, financial resilience, and Board assurance, involve a significant degree of subjectivity. There is ambiguity in what Ofwat may consider sufficient evidence or adequate assurance, which are not clearly defined, and which has therefore led to arguably arbitrary decisions.

Ofwat identified that we did not meet its expectations for consistency between the '*business plan and long-term delivery strategy and achievement of statutory requirements and relevant government targets'*. It noted that our *"business plan and long-term delivery strategy are consistent with the achievement of government targets in relation to distribution input per population, leakage, and per capita consumption targets"*[5] but cited concerns with meeting the government targets for storm overflows and our ambition and progress in meeting the greenhouse gas emissions net zero target.

For example, contrasting our assessment with South West Water's, a company graded Outstanding, for the same expectation, Ofwat noted *"concerns about the presented performance trends in the business plan and long term delivery strategy not achieving the business demand target (15% reduction by 2050) for the company's South West area and meeting the leakage target (50% reduction by 2050) in its Bristol area."*[6] and *"concerns with delivery of the distribution input per population target (20% reduction by 2037-38) for the company's Bristol area."*

Similarly opaque assessment benchmarks were, we believe, used by Ofwat in its assessment of whether companies used its '*early view of the allowed return on capital or provided compelling evidence that another rate is more appropriate*'. Our business plan included an allowed return of 3.82% (real, CPIH) which was higher than Ofwat's published 'early view' of 3.29%. Ofwat cited concerns around our approach to estimating the return on equity. Ofwat concluded we did not meet its expectations in this assessment.

Northumbrian Water's business plan similarly included a cost of capital (3.55% real, CPIH) which was higher than the Ofwat early view. Ofwat also identified inconsistencies between Northumbrian's use of historical data used for equity beta and other components of the estimation. However, in this instance Ofwat identified that Northumbrian had met its expectations.

The above examples raise concerns over the consistency of benchmarks Ofwat have used to assess companies. Given the materiality of the penalties applied between categories, we consider that there is a need for full disclosure of any benchmarks and methods of comparison undertaken by Ofwat between water companies in forming its view of QAA categorisation. Publication of a fully transparent assessment framework will enhance the credibility and perceived fairness of the QAA process.

[5] https://www.ofwat.gov.uk/wp-content/uploads/2024/07/PR24-draft-determinations-Southern-Water-Quality-and-ambition-assessment-appendix.pdf
[6] https://www.ofwat.gov.uk/wp-content/uploads/2024/07/PR24-draft-determinations-South-West-Water-Quality-and-ambition-assessment-appendix.pdf

3 Responses to Ofwat's QAA assessment of material issues

There were four categories that Ofwat assessed Southern Water as not meeting Ofwat's minimum requirements and the impacts were material. These related to:

- Board assurance
- Deliverability
- Financial resilience
- Dividend policy

We address each of these below.

3.1 Board assurance

In its QAA, Ofwat stated that Southern Water did not meet several of its requirements. The table below sets out the QAA finding where we didn't meet the minimum expectation, and our response to the assessment made:

QAA finding	Response to assessment
The Board did not provide a statement that it challenged and satisfied itself that the long-term delivery strategy will enable the company to meet its statutory and licence obligations, now and in the future	In our long-term delivery strategy (SRN12), we explicitly included a section on Board Assurance in relation to meeting statutory and licence obligations (section 22.6). The assurance statement raised three areas of uncertainty: regulator agreement on the WRMP, regulatory agreement on WINEP phasing, and regulatory agreement on alternative delivery. All of these factors are largely outside of our control, and have a material effect on our long term-delivery strategy. As such, it is right that these should be flagged as key areas of uncertainty, albeit with clear plans on how we intend to proceed.
The Board did not provide a statement that it took steps to secure long-term affordability and fairness between current and future customers. The business plan included a reference to the requirement for the statement and described Board interaction in this area but did not include the statement itself.	In our long-term delivery strategy (SRN12), we explicitly included a section on Board Assurance in relation to long-term affordability and fairness (section 22.5).
The Board did not provide a statement that it challenged and satisfied itself that the 2025-2030 business plan implements the first five years of the long-term delivery strategy.	Whilst the Board did not make this specific statement, the reference to the Board statement included detail on how engagement on both the DWMP and the WRMP implicitly supported the long-term delivery strategy including alignment to the PR24 business plan covering the 2025-2030 timeframe.

The Board did not provide a statement that it challenged and satisfied itself that the needs for enhancement investment are not influenced by non-compliance or non-delivery of programmes of work (both base and enhancement) that customers have already funded.	The Board did not make this statement in our original Business Plan but will do so as part of our Draft Determination response. Considering the detailed assessment and review of our base and enhancement investment proposals we are satisfied that the needs for enhancement investment are not influenced by non-compliance or non-delivery of work already funded.
The Board did not provide a statement that PR24 plans and the expenditure proposals within them are deliverable and that the company has put in place measures to ensure that they can be delivered.	In our data and assurance submission (SRN11) we included an explicit statement that 'the Board believe that our plan is customer-led; affordable, supportive of the vulnerable, financeable, and deliverable' (section 11.4.4).
The Board did not provide a statement that it challenged and satisfied itself that the expenditure proposals are affordable by customers and do not raise bills higher than necessary.	See note above.
The company has not met the requirement that it should provide Board assurance that the business plan is financeable based on the notional capital structure in a form which meets our expectations. The statement provided in this area is caveated in way which materially undermines it.	In our data and assurance submission (SRN11) we included an explicit statement that the company is financeable, taking account of mitigating actions as set out in the SRN10: Risk and Return chapter. It is clear that the risk and return package as set out in the final methodology was not appropriate for the sector. This is apparent from the major changes that Ofwat made in its Draft Determination (including, changing cost sharing rates, adding the MeX incentives into the ODI sharing mechanism, introducing new gated processes, and additional forms of indexation among others). It is hard to see how any company could have credibly made an un-caveated assurance statement endorsing a regulatory framework that Ofwat itself has now materially moved away from.

3.2 Deliverability

In its QAA, Ofwat stated that Southern did not meet several of its requirements. The table below sets out the QAA finding, where we didn't meet the minimum expectation, and our response to the assessment made:

QAA finding	Response

There is basic commentary on increasing capacity, and a discussion on what is planned in the future rather than what it has achieved already or actual figures/programmes it will roll out.	
The Board provided a statement confirming that it has challenged and satisfied that the plan and expenditure proposals within them are deliverable. However, the company sets out that this is dependent on phasing WINEP investment over 8 years, and that without the proposed re-phasing, the plan is neither affordable nor deliverable. The company also states that the plan is contingent on gaining agreement to £2 billion of alternative delivery projects.	It is not clear why this should result in a failed assessment. In engagement with its regulators, the company has sought to re-profile expenditure and has sought alternative delivery mechanisms to aid with deliverability. These are exactly the sorts of actions a company should consider in order to ensure that the sector's biggest capital programme in history is deliverable.
The company subsequently provided an update to its plan and stated that it could not be assured that any water company could manage the complexity, timing and scale of the updated plan. Further it could not be assured that any water company could achieve the increase in output required from its supply chain, given the market based constraints on that sector, both in the South East of England and across the whole country. These significant caveats raise concerns about the company's ability to deliver.	We made a proposal for Ofwat to develop the Delayed Approval Mechanism, which is aimed at ensuring that delivery can be approved on revised project schemes and costings during the AMP. Ofwat has accepted this mechanism (now called the Delivery Mechanism). This indicates that it was a legitimate concern raised by Southern Water, yet we were penalised for doing so. Correct application of this mechanism should alleviate such concerns. However, this still relies on Ofwat accepting the detailed workings of the mechanism as we set out in the Deliverability chapter of this response document.
The company states that it has started to look at and work with the supply chain, but with the exception of the Low Complexity Delivery Route (LCDR) Framework, has not got agreements in place yet, and only plans to do this 12 months prior to the 2025-30 period. We have concerns that this limited timeframe is insufficient to expand capacity to the required level.	There is no evidence that establishing framework arrangements a year in advance is insufficient. Many other companies in the sector are placing contracts with their supply chain at the same time as Southern Water, yet passed their QAA assessment.
There is a large focus on the supply chain but insufficient evidence indicating that the company has engaged with the supply chain and received assurance that it will be able to deliver against the company's plan.	We made references in the deliverability chapter of our October 2023 plan to the substantial market engagement and procurement exercises we were undertaking to enable delivery of our plan. On 16 August 2024, we completed and announced award of two capital delivery framework contracts worth approximately £3.7bn, following an extensive and intense procurement process with potential partners over several months, achieving a major milestone in our AMP8 readiness programme, which will allow us to deliver the largest capital investment programme we have ever undertaken, to support our plans for WINEP and WRMP, and the service

	we are seeking to deliver for customers. We engaged with the bidders on the subject of deliverability throughout the procurement and appointed contractors to these frameworks who will help us deliver the plan. We met with our appointed suppliers on 22 August 2024 to test our investment profile, reviewing at both programme level and overarching plan level. Their feedback has helped inform and shape our Deliverability Action Plan and our Engagement Planning activity.
There is limited discussion of risks, despite regularly mentioning that risks are assessed and well governed.	We discussed the sector-wide challenges at length in SRN56. This included: - Supply chain capability and capacity - Plan stability - Competition for skilled labour - Competition for materials - Portfolio complexity - Adapting to new business models

3.3 Financial resilience

In its QAA, Ofwat stated that Southern Water did not meet several of its requirements. The table below sets out the QAA finding, where we didn't meet the minimum expectation, and our response to the assessment made:

QAA finding	Response
In the business plan submission, the board confirmed that the company is financially resilient under its actual structure in 2025-30, however, the assurance was strongly caveated and included the statement: "financial resilience is therefore limited" due to the pressure of a large investment plan for PR24 and associated rapid growth of the business. The board's assurance statement on financial resilience was also predicated on Southern Water's risk mitigations (related ODIs, totex and return adjustment mechanisms) being accepted by us.	We do not know of any company in the sector where financial resilience is not limited. Our Board statement in this regard merely emphasised this point explicitly. It is clear that the risk and return package as set out in Ofwat's final methodology was not appropriate for the sector. This is apparent from the major changes that Ofwat made in its draft determination (including, changing cost sharing rates, adding the MeX incentives into the ODI sharing mechanism, introducing new gated processes, and additional forms of indexation among others). It is hard to see how any company could have credibly made an un-caveated assurance statement endorsing a regulatory framework that Ofwat itself has now materially moved away from.

The company's financial resilience assessment was based on its own estimate of the allowed return of 3.83%, but it did not include a scenario test using our early view of the allowed return to show the impact on its financial resilience. No company-specific scenarios were tested by Southern Water. Additionally, in its assessment of financial resilience, there were unexplained discrepancies between the financial ratios for the base case and those reported in the business plan data tables, meaning that we had to raise queries. The company's response was insufficient to fully explain the differences other than to say its own model is quite different to our model. Southern Water subsequently provided further detail on the base case and stress testing it conducted on allowed return assumptions of both 3.77% and 4.58%. The company stated although financeable, the increased strain on the business (with an allowed return at 3.77%) is material, and it would need to call upon equity injection to maintain its gearing and covenant thresholds. There was, however, no further assurance or indication given of receiving addition equity injections in the 2025-2030 period.	We discussed our approach to assessing financeability and financial resilience in detail in SRN60. Our assessment was based on a cost of capital parameters consistent with the PR24 FM, updated to reflect the recent changes in market variables with the point estimate of the unlevered beta and TMR at the top of the range, reflecting the large scale and complexity of our capital programme which increased exposure to systematic risk. To deepen the notional financeability analysis, we assessed how an efficient company with the notional capital structure could deal with a range of downside scenarios, including those prescribed to test financial resilience during 2025-30 and beyond. These scenarios include the suite suggested in the PR24 FM for the actual company, and two combination scenarios based upon the P50 RoRE risk exposure for the notional company, with and without risk mitigations. The further points around assurance or indication of receiving additional equity injection in the period 2025-2030 challenge the credibility of any company in making such un-caveated assurance statements. In our Draft Determination response, as set out in our Financeability chapter, Financial Resilience Action Plan and Board Assurance Statements, we specifically address Ofwat's findings.

3.4 Dividend policy

In its QAA, Ofwat stated that Southern did not meet a number of its requirements. The table below sets out these criticisms and provides response:

QAA finding	Response
The policy did not set out the company's approach to determining dividends with respect to the following key factors in our dividend guidance: • how it will account for current and future investment needs; • that the dividend policy applies to the payment of any dividend regardless of the purpose of that dividend; • how past performance will be factored into dividend decisions;	As detailed in the Board Assurance Statements, the Board has committed to reviewing and updating Southern Water's Dividend Policy to reflect the points made by Ofwat in the QAA assessment, including strengthening delivery for customers, the environment, employees and other stakeholders. Our Draft Determination response assumes that the updated dividend policy, applicable for AMP8, will be formulated to only consider paying dividends where gearing is below 70% of regulatory capital value. And, given the significant level of enhancement investment in our business plan,

• that the base dividend yield can be adjusted up or down depending on performance; and • the circumstances under which it may be appropriate for dividends to be restricted or withheld.	dividends – if paid – are expected to be lower than 2% of regulated equity over AMP8. This process has commenced and will continue into Autumn 2024 as we finalise the updates to the policy and seek the necessary shareholders resolutions. We expect to publish our updated dividend policy in advance of the start of AMP8.

4 Responses to Ofwat's QAA assessment of non-material issues

There were a range of further issues that Ofwat assessed Southern Water as not meeting Ofwat's minimum requirements, but the impacts were not material. We address each of these below.

QAA finding	Response
• Reduce the number of Ofwat queries on data and information provided.	We have good governance and controls in place to assure data. We continue to follow our robust assurance processes for evidence and data. Our view is that the number of queries received reflects the complexity and challenges we face in our plan rather than the quality of the data being provided.
• Confirm back to Ofwat how our CCG was governed and confirm how independent assurance was maintained.	Our CCG was independently chaired by Professor Martin Hurst, to ensure good governance and assurance was maintained. We can provide more evidence to Ofwat on this if required, but no further evidence is provided in our draft determination response on this as our original business plan documents provide this information.
• Sharing all customer research documents on its website.	We have not addressed this in our Draft Determination response. However, as confirmed with CCW and Ofwat in post business plan submission correspondence, not disclosing this information was not down to lack of transparency but down to concerns that some of this data could be misused if made public. Additionally, it was felt that the many hundreds of documents we have on customer research was too much to upload on our website. There is no issue sharing any of this data upon request and we did share all of this information with water companies, interested stakeholder groups, Ofwat and CCWater. We will continue to make this information available upon request.
• Able to provide more confidence that the demand target trend to 2050 (15% reduction) is	We have provided our update and response to the Greenhouse Gas Emissions performance

achievable. Similarly, provide more confidence that GHG emissions net zero short and long term targets can be achieved.	commitment and ODI in the Performance Commitments and Outcome Delivery Incentives chapter.
• Ensure that WRMP aligns to our submission response and any variances are clearly marked and good reasons provided. Make sure we address WRMP concerns raised by Ofwat.	We have updated the schemes and costs in data table CW3 to align with our latest WRMP for consultation in September. Any misalignment is by exception only. We provide explanation for these exceptions in the relevant WRMP cost evidence case documents.
• Address specific Ofwat outcome and ODI rate challenges by providing more compelling evidence to support each case (or accept the Ofwat approach).	We provide more evidence on this in our Performance Commitments and Outcome Delivery Incentives response document.
• Provide more compelling evidence on each bespoke AIM performance commitment.	We have dropped the AIM bespoke performance commitment.
• Ofwat want us to use their view of WACC and not our own	We provide more evidence on this in our financeability response document.
• Provide more compelling evidence to change Ofwat's view on RORE range.	We provide more analysis and evidence in our response on Risk and Investability.
• Further evidence on bespoke uncertainty mechanisms and notified items.	We provide more information and supporting evidence on uncertainty mechanisms and notified items within the Risk and Investability response document.
• Explain how the DWMP aligns with the business plan and LTDS. Clearly explain the changes to the DWMP (if there has been) and confirm the reasons for any decrease in expenditure on the DWMP.	Our DWMP is one of the main components that feeds into the development of our LTDS. We have provided no further information in our draft determination response but previously submitted information can be provided on this to confirm the linkages if required.

5 Responses to Ofwat's QAA assessment of minimum expectations met

There were a range of further issues that Ofwat assessed Southern Water as having met minimum requirements, but raised questions, nevertheless. We address each of these below.

QAA finding	Response
• Address Ofwat concern on Exec pay policy - some areas of uncertainty.	We commit to reviewing the Exec Pay Policy ahead of the commencement of AMP8. The process has commenced but requires governance and approval steps to be completed which cannot be completed within the Draft Determination response timeframe.

	Our approach will build on the positive feedback we received from Ofwat on our Short Term Incentive Plan (STIP) and Long Term Incentive Plan (LTIP) framework.
• Provide reasons for redacting documents.	We have provided a full list of all business plan submission redactions to Ofwat in an email on 3rd July 2024. We will provide redaction list for our response docs as requested.
• Provide a clearly articulated strategy to achieve net zero carbon - improve credibility of our GHG	Our net zero carbon strategy is reviewed and updated regularly. We publish our net zero strategy on our website here: https://www.southernwater.co.uk/about-us/our-plans/net-zero-plan/. This provides public clarity on our net zero carbon roadmap and approach.