



**TW-OC-A5**

**SEMD PC Update**



# Table of contents

<b>Section 1</b>	<b>Purpose of this document.....</b>	<b>2</b>
<b>Section 2</b>	<b>AMP7 SEMD Programme.....</b>	<b>3</b>
<b>Section 3</b>	<b>Background .....</b>	<b>4</b>
<b>Section 4</b>	<b>Updated PC Definition .....</b>	<b>5</b>
<b>Section 5</b>	<b>Explanation of Changes to our September Performance commitment .....</b>	<b>7</b>
<b>Section 6</b>	<b>Why this PC is right for our customers .....</b>	<b>9</b>
<b>Section 7</b>	<b>Design of the Outcome Delivery Incentives .....</b>	<b>11</b>
<b>A</b>	<b>Introduction .....</b>	<b>11</b>
<b>B</b>	<b>Part A: Performance based ODI.....</b>	<b>11</b>
<b>C</b>	<b>Performance based ODI definition .....</b>	<b>11</b>
<b>D</b>	<b>Incentive description .....</b>	<b>12</b>
<b>E</b>	<b>ODI Calculation.....</b>	<b>12</b>
<b>F</b>	<b>Summary of Performance based Performance Commitment.....</b>	<b>13</b>
<b>G</b>	<b>Part B: Uncertainty mechanism ODI definition .....</b>	<b>14</b>
<b>H</b>	<b>Incentive rates (uncertainty mechanism) .....</b>	<b>15</b>
<b>I</b>	<b>Summary of the performance commitment.....</b>	<b>17</b>
<b>Section 8</b>	<b>Reporting and assurance .....</b>	<b>19</b>

## List of tables:

Table 1: Forecast profile of our level of performance .....	6
Table 2: Our proposed AMP7 investment.....	6
Table 3: Additional details .....	13
Table 4 SEMD ODI Part B: Uncertainty mechanism explanation of parameters.....	15
Table 5: Our performance commitment .....	17
Table 6: Incentive rates.....	17
Table 7: Additional details .....	18



## Section 1

# Purpose of this document

- 1.1 This document provides an update to the PC Summary Document DWS02: Securing our sites. It also provides a finalised definition of our performance commitment, including an explanation of the financial under and out performance adjustments that will be applied based on performance and investment.
- 1.2 This document is structured as follows:
- Section 2 describes the AMP7 SEMD programme.
  - Section 3 provides background information.
  - Section 4 provides an updated definition of the performance commitment.
  - Section 5 explains the changes made to our performance commitment from September 2018
  - Section 6 explains why the changes are right for our customers.
  - Section 7 describes the design of the Outcome Delivery Incentives (ODI) and summarises the ODI in the format of the Ofwat tables. It then includes the detailed calculations for the incentive rates and their calibration.
  - Section 8 sets out our reporting and assurance framework.



## Section 2

# AMP7 SEMD Programme

- 2.1 Our September 2018 PR19 plan included REDACTED<sup>1</sup> of investment in our Security and Emergency Direction ('SEMD') programme over AMP7 (allocated REDACTED). This investment consisted of REDACTED<sup>2</sup>m for REDACTED.
- 2.2 We also included a performance commitment ('PC') and corresponding outcome delivery incentive ('ODI') mechanism in relation to our performance in this area.
- 2.3 At the time of our September submission, there was still much uncertainty in terms of the nature and extent of work to be included in our AMP7 SEMD programme. We recognise that agreeing the scope and prioritisation of work that is required to comply with Advice Notes ('AN') involves an iterative process with Defra, and is subject to change as risks and technologies change.
- 2.4 Efficient AMP7 investment towards securing our sites depends on the actual risks that exist at our sites and assets; the guidance specified in the Advice Notes/Protective Security Guidance; and the people and technology available to address the risks.
- 2.5 As a consequence of the uncertainty and iterative nature of our SEMD programme, we have retained spend for known activities, for example REDACTED, in our April PR19 re-submission. The remaining money that is needed to update some of our other sites and assets to comply with Advice Notes has been removed in our April 2019 Submission and instead we have amended our ODI to include an uncertainty mechanism to cater for changes in agreed scope, defined in greater detail in Section 7.
- 2.6 We need to invest more in security at sites where there is the greatest risk of interruption to supply as a result of malicious threats, while planned investment could be avoided/reduced where assets and sites are proven to be more resilient and/or exposed to lower risk. As such, there are merits for including a mechanism that varies investment in our SEMD programme as output requirements change.
- 2.7 Our proposed uncertainty mechanism involves investing more (and recovering monies from customers) as our requirements are agreed with Defra and become more clearly defined and quantifiable over AMP7.

---

<sup>1</sup> PR19 September Data tables REDACTED

<sup>2</sup> PR19 September PCS document: CSD005-DWS02-PR19 SEMD



### Section 3

## Background

- 3.1 The purpose of our SEMD programme is to secure our assets and sites from hazards such as terrorism and malicious threats. Security is a cornerstone of our long-term resilience strategy and plays a vital role in enabling us to deliver a consistent service to our customers.
- 3.2 We recognise our ongoing obligation to comply with the Security and Emergency Measures Direction: 1998 ('SEMD'). The SEMD guidance has, until recently, come in the form of Advice Notes issued by Defra. The Advice Notes ('AN') , while still relevant, are now accompanied by the Protective Security Guidance 2020 ('PSG') document, also issued by Defra, with additional and more technical information contained in the Water UK Standard for Security Arrangements for Operational Assets (WUK SSAOA) document.
- 3.3 We also expect that the security challenges we will face in the future are likely to vary significantly. New threats and emerging technologies have been seen to erode the protection provided by more traditional security measures. This is reinforced by the changing set of requirements we are required to respond to going forward.
- 3.4 Our SEMD programme provides targeted investment to meet this objective by complying with Defra and Water UK standards as required by the Security and Emergency Measures (Water and Sewage Undertakers) Direction 1998 (SEMD).
- 3.5 Our customers benefit from our continued investment in SEMD as we improve the security of their water supply through compliance with ANs and the implementation of PSG and WUK SSAOA. This includes measures that prevent loss of supply and contamination.
- 3.6 **REDACTED.** This business case sets out a strengthened commitment to prioritise security and make sure we are delivering the programme of work necessary to support our long-term resilience strategy.
- 3.7 Our updated SEMD programme, including the work to be delivered under our proposed uncertainty mechanism, is focussed on:
- Complying with all relevant Advice Notes, PSG and WUK SSAOA on sites that we update;
  - a risk based approach of implementing holistic solutions for sites which have the highest potential impact on customers;
  - ensuring that maintenance programmes maintain the required accreditation for electronic security systems;
  - improving customer satisfaction by improving our incident management and response to security incidents; and
  - improving the effectiveness of our security monitoring.



## Section 4

# Updated PC Definition

- 4.1 In AMP5 and AMP6 we have encountered difficulty in defining the technological solutions for improving site security several years in advance of the works. In particular, the electronic systems for intruder detection, alarm sensors, and integration to our core systems. This has resulted in extensive discussions with Defra to reprioritise the various programmes and subsequent changes to them.
- 4.2 We want to make sure we protect customers while also ensuring we have the funds available for essential security enhancements.
- 4.3 Our performance commitment definition for SEMD remains consistent with what we said in September 2018 i.e. to ensure all sites in the list as agreed with Defra are 100% compliant with SEMD measures.
- 4.4 Performance against our commitment to make these specific sites fully compliant with Security and Emergency Measures Direction (SEMD) requirements will be assessed against a set of criteria agreed with Defra.
- 4.5 We recognise the nature of work required to be fully compliant with SEMD Advice Notes varies greatly by site and asset, is complex and has an element of uncertainty as the risks faced and technology available can change quickly.
- 4.6 We therefore propose to split the ODI for this performance commitment into two (as detailed in Section 7):
- Part A) Performance based – measures delivery of outputs against a list of agreed outputs over AMP7, with an underperformance penalty; and
  - Part B) Uncertainty mechanism – to take account of the cost of the yet to be defined and agreed scope of work needed to secure our sites and assets during AMP7.
- 4.7 Our commitment is to ensure all the sites in the agreed list are 100% compliant with SEMD measures (Table 1). The performance related ODI penalty will be based on the number of sites made compliant by the end of AMP7, relative to the number of sites on our final deliverable list, as agreed during the AMP with Defra.
- 4.8 At present, we have defined and agreed a total of **REDACTED** that we are committing to make compliant by the end of AMP7. As additional outputs are defined and agreed, they will be added to the list of committed outputs, and our performance in their delivery measured as part of this performance commitment.



**Table 1: Forecast profile of our level of performance**

AMP6 Target (Outputs)	AMP7 Targets (outputs)				
Yr5	Yr1	Yr2	Yr3	Yr4	Yr5
Agreed outputs					REDACTED
100%					100%

Source: Thames Water, APP1 data table

4.9 The REDACTED outputs currently presented relate to the REDACTED described in Table 2. This table will be updated annually as additional outputs are agreed with Defra.

**Table 2: Our proposed AMP7 investment**

Activities - Description	Price control	Type of asset	TOTEX (£m; 17-18 CPI-H price base)
This programme will provide new security to REDACTED and integrate that security with the existing security already in place <sup>1</sup> . This is a cost efficient approach.	REDACTED	REDACTED	REDACTED
Changes on this site mean additional measures are now required.	REDACTED	REDACTED	REDACTED
REDACTED	REDACTED	REDACTED	REDACTED
REDACTED	REDACTED	REDACTED	REDACTED
Opex	REDACTED	REDACTED	REDACTED
<b>Total investment included and allowed in PR19 Business Plan for SEMD (Water and Waste)</b>	REDACTED	REDACTED	REDACTED

Source: Thames Water PR19 Consolidated data tables; April 2019 submission; REDACTED



## Section 5

# Explanation of Changes to our September Performance commitment

- 5.1 When amending our performance commitment we considered:
- protecting the interests of our customers;
  - protecting our assets and sites from malicious threat; and
  - addressing needs efficiently and effectively.
- 5.2 We recognise this performance commitment is driven predominantly by Defra and the Security and Emergency Direction (SEMD), which sets out what water and wastewater companies must do to meet their security obligations.
- 5.3 Given companies have varying security related requirements, and many have already completed a significant portion of their SEMD programme, we have no direct comparative data.
- 5.4 The SEMD programme is a statutory requirement, with an objective of bringing all critical national infrastructure, national infrastructure and other important sites and assets up to a secure status, where this is consistent with Defra's risk based approach to prioritisation.
- 5.5 We recognise that the burden of proof will fall to us to justify the scope and cost of any proposed SEMD programme additions, beyond the initial REDACTED spend, over AMP7 which will result in changes to customer bills.
- 5.6 When we submitted our business plan in September we included REDACTED<sup>3</sup> of totex for our SEMD programme. This was our best estimate at the time of what an economical and efficient SEMD programme would look like over the AMP.
- 5.7 Since September we have improved our understanding of the challenges experienced in delivering SEMD requirements at our sites and assets. The most significant of which is the level of uncertainty inherent in our AMP7 programme of work, which has been materially affected by the increased scope and complexity of the work needed to comply with guidance during AMP6.
- 5.8 In light of this uncertainty we have decided to include SEMD investment that is attributable to a specific and quantifiable activity. The activities we have defined, as agreed with Defra, are shown in Table 2.

---

<sup>3</sup> PR19 September Data tables REDACTED





- 5.9 Note the investment reflected in Table 2 only covers AMP7 related security enhancement work. It does not include the maintenance of existing assets.
- 5.10 We will update customers on our progress against the current year programme, and plans for the following year(s), as agreed with Defra.
- 5.11 We have included two ODI mechanisms for SEMD:
- Part A) Performance based – measures delivery of outputs against the list of agreed outputs over AMP7, with an underperformance penalty; and
  - Part B) Uncertainty mechanism – to take account of the cost of the yet to be defined and agreed scope of work needed to secure our sites and assets during AMP7.



## Section 6

# Why this PC is right for our customers

- 6.1 This incentive arrangement is designed to protect customers in two ways:
- the performance based ODI (part A) incentivises us to deliver our committed outputs on time; and
  - the uncertainty mechanism (part B) provides a way of mitigating the impact of uncertainty for customers.
- 6.2 With respect to the performance based ODI, we believe the penalty is sufficiently incentivising because:
- a failure to secure our sites appropriately can lead to malicious actions causing disruption to services REDACTED;
  - penalty ODIs exist on all measures which may fail as a result of failure to deliver SEMD compliance. REDACTED
  - The reputational risk and poor publicity that would result from any of the above failures in service delivery.
- 6.3 With respect to our uncertainty mechanism, the reasons why it is appropriate to fully recover the cost incurred in delivering the SEMD programme include:
- SEMD is a legislative requirement, outside management control;
  - limited flexibility for solutions exists at a site level. The available range of compliant solutions is considered and the appropriate one for a specific site selected as part of the Security & Resilience Appraisal process. This process has been approved by Defra and Centre for the Protection of National Infrastructure (CPNI); and
  - funding allocation to SEMD is “ring-fenced”, with any financial efficiency resulting in additional spending for further SEMD initiatives.
- 6.4 The uncertainty mechanism is designed to provide an incentive for us to deliver a risk-based SEMD programme over AMP7, by enabling us to recover the efficient costs of the programme, beyond the amount included in our April submission.
- 6.5 The uncertainty mechanism will also deliver better outcomes for customers by providing a targeted tool to manage uncertainty. We have used the ODI framework to be consistent with the PR19 framework and also for simplicity.
- 6.6 The decision to use an uncertainty mechanism for SEMD has been considered carefully, balancing the need to include totex for SEMD in our base plan against the risk of customers bearing the cost of investments that do not transpire, or are materially different in nature and cost when delivered.



- 6.7 We have challenged ourselves to use our uncertainty mechanism to provide additional benefits for customers. We have achieved this by including a complimentary performance related commitment with a financial underperformance payment against the same SEMD programme.



## Section 7

# Design of the Outcome Delivery Incentives

## A Introduction

- 7.1 In our September 2018 Business Plan we:
- introduced a performance commitment to ensure all our sites in the list agreed with Defra are 100% compliant with SEMD measures; and
  - included an under performance only ODI based on the percentage delivered against our agreed list of outputs (Part A of our SEMD ODI).
- 7.2 To mitigate the risk of uncertainty we have developed an uncertainty mechanism (Part B of our SEMD ODI). The risks associated with SEMD cost are likely to be material over AMP7.
- 7.3 The two mechanisms (both the performance based ODI and the uncertainty mechanism) are designed to operate jointly, with one ensuring we continue to invest in the crucial area of security and the other to incentivise us to deliver on time. There is a clear and tangible benefit to customers in keeping their money until such time as the need for investment is known, defined and quantifiable.

## B Part A: Performance based ODI

- 7.4 We recognise that the ODI in its September 2018 format is beneficial to customers as it penalises us financially, and compensates customers, for any delay to delivery of our agreed SEMD programme.
- 7.5 We provide further clarity to how our programme of committed outputs will be defined and how the performance commitment will be measured, including the calculation of any underperformance payments.

## C Performance based ODI definition

- 7.6 The performance ODI has an under-performance payment for late delivery based on an agreed programme of work for which funding has been allowed.
- 7.7 The Outcome delivery incentive is an end of AMP7 revenue adjustment based on the annualised revenue for expenditure that has been delayed.
- 7.8 We have not followed Ofwat's standard formula to set under performance rates as the variation in costs between different types of projects means this could inadvertently drive behaviour that is not in customers' interests.



7.9 Our performance in delivering our agreed list of outputs will be based upon the summation of annual assessments for years 1-4 of AMP7 and forecast position for the final year of AMP7 and the assessment will be subject to independent scrutiny and assurance.

7.10 We have not applied a deadband and the penalty collar is set at the size of the programme, meaning the ODI is likely to apply in practice for any level of underperformance.

## D Incentive description

7.11 The penalty component of our SEMD performance commitment will ensure that customers are compensated for any outputs we fail to deliver, and for which customers have paid.

## E ODI Calculation

7.12 At the time of our April PR19 Plan submission, we have a defined list of REDACTED to be delivered by the end of AMP7 (2024-2025) for REDACTED.

7.13 As we progress through AMP7 and the programme scope becomes defined and agreed with Defra, we will add the additional agreed outputs to the list of deliverables covered by this PC.

7.14 Performance, expressed as progress as a percentage against the target of 100% will be measured and reported on an annual basis for any outputs agreed and included in our list of deliverables.

7.15 An output is a defined programme of work to deliver compliance with Advice Notes. It often takes the form of an asset or site.

7.16 Percent completion is measured by individual output on an annual basis. The percent completion is then used to calculate the penalty (where applicable).

7.17 The commitment is 100% delivery of outputs included on an agreed list by the end of AMP7 (with progress updated annually).

7.18 The list of agreed outputs will be maintained and updated not less than annually, as part of our annual performance reporting process.

7.19 Delivery of less than 100% by the committed delivery date will result in a penalty being calculated based on the annualised revenue attributable to the cost of the undelivered output.

7.20 Underperformance penalty

$$Revenue\ impact_t = \sum_{i=1}^1 \frac{Capital\ enhancement\ expenditure}{asset\ life_i} \left[ 1 + \left( asset\ life_i - \left[ \frac{2t+1}{2} \right] * WACC \right) \right]$$

Where 'i' indexes the asset type in the solution and 't' indexes the time period.

7.21 In the calculation of the return on capital we have used a wholesale weighted average cost of capital (WACC) as defined in the Final Determination. The depreciation charge is calculated by reference to asset lives by asset category maintained in our reporting system.



- 7.22 Any penalty will be assessed at PR24 and will be subject to independent scrutiny and assurance. There is no scope to outperform this performance commitment; therefore the form of the ODI is penalty only.
- 7.23 This is an appropriate penalty rate as the output will still need to be delivered, with any costs arising from late delivery at our expense.

## F Summary of Performance based Performance Commitment

- 7.24 The following tables summarise the parameters of the ODI package for this performance measure.

**Table 3: Additional details**

Necessary detail on measurement units	<p>The performance commitment is defined as the percentage of a number of Outputs, as agreed with Defra, that are compliant with Security and Emergency Measures Direction (SEMD) requirements as prescribed through Advice Notes and Protective Security Guidance.</p> <p>Outputs may include sites, assets or specific activities undertaken in complying with SEMD requirements.</p>
Frequency of performance commitment measurement and any use of averaging	<p>The penalty applies to performance at the end of 2024/25. This will be calculated at PR24 based on actual programme delivery for years 1 to 4 and forecast programme delivery for year 5 of AMP7.</p> <p>Penalties will be calculated at PR24, to be applied in PR24.</p>
Timing and frequency of rewards/penalties	End of period revenue adjustment
Form of reward/penalty	<p>Revenue Adjustment</p> <p>A penalty for undelivered scope will be calculated based on annualised revenue attributable to expenditure for agreed outputs.</p>
Any other information or clarifications relevant to correct application of incentive	There are no exclusions.

Source: Thames Water



## G Part B: Uncertainty mechanism ODI definition

- 7.25 In our April submission we have included a financial ODI in the form of an uncertainty mechanism. This incentive arrangement is designed to protect customers by helping us to manage uncertainty.
- 7.26 Where there is additional SEMD work required and it is specific and quantifiable, this uncertainty mechanism will allow us to recover the efficient cost of an agreed SEMD programme. We recognise that part of any additional spend will be recovered through the totex sharing mechanism at the rate specified in the Final Determination. This uncertainty mechanism will facilitate recovery of the remainder, for 100% recovery of efficient costs.
- 7.27 In order to maximise cost-effectiveness, wherever possible we have and will continue to:
- look for options that can adequately protect sites and assets by applying the risk-based approach to prioritisation, consistent with Defra guidance;
  - seek lowest whole-life cost options, considering opex only and systems based solutions;
  - include only efficient costs that one would expect a prudently managed company to incur; and
  - seek synergies with other investment drivers to lower overall investment costs (for example, co-ordinating SEMD work with other site upgrade/maintenance activities).
- 7.28 A financial ODI is appropriate for this performance commitment because it:
- is supported by customers;
  - protects customers' interests;
  - promotes efficiency in scope;
  - is fair;
  - is transparent; and
  - customers want us to ensure that the benefits of a secure and resilient supply of water are delivered.
- 7.29 Any changes that increase bills for customers are agreed with Ofwat and Defra and are cost beneficial.
- 7.30 The Totex allowance for this performance commitment, including any additional agreed allowance recoverable through our uncertainty mechanism, is ring fenced in our business plan. This means that the programme may be re-prioritised but the Allowed Totex will be spent on prioritised security advice notes in line with this performance commitment.
- 7.31 We will provide, to Defra, credible evidence in a timely manner, so that they can endorse our SEMD programme scope as it emerges through this iterative process. Where too much uncertainty remains, we do not propose to request any additional money from customers.



7.32 Summary of parameters linked to uncertainty:

**Table 4 SEMD ODI Part B: Uncertainty mechanism explanation of parameters**

Parameter	SEMD programme uncertainty
Outcome	Enhanced security at sites and assets, following risk-based approach to prioritisation and with agreement from Defra
Cost rate	Costs vary considerably from site to site; this overall variability is a key driver in our need for an uncertainty mechanism
Trigger	PR19 annual performance report; in calculating the SEMD performance commitment, the list of agreed outputs will need to be updated annually. As part of this annual update process, a corresponding efficient amount will be added to our ODI uncertainty mechanism.
Cost recovery	100% adjustment through RCV at PR24

Source: Thames Water

7.33 We anticipate the maximum value of the programme would be no more than REDACTED. The final sum will be subject to the methodology proposed through the uncertainty mechanism.

## H Incentive rates (uncertainty mechanism)

7.34 The Totex sharing rate was assumed to be 50%<sup>4</sup> during the April submission development. There may be a difference between our assumption and the Company sharing rate formally established by the Final Determination. This will be updated when the final rate becomes known.

7.35 We do not have direct WTP valuations for compliance with environmental regulations. However, our research does show that customers expect a safe and reliable water and wastewater service.

7.36 Due to the wide variation in costs between solutions required to achieve this performance commitment, there is a risk that setting rates using the standard Ofwat formula could result in unintended consequences. We have therefore specified an outperformance payment mechanism, which is based on an end of AMP7 RCV adjustment. Outperformance payment

7.37 An outperformance payment will apply for increases in scope due to a change in the number of agreed outputs to be delivered, from those which were included in the allowed Totex in our final business plan.

7.38 This equates to the net increase in scope after schemes have been re-prioritised or swapped following final agreement of the SEMD programme and delivery in AMP7.

7.39 Any adjustments will only be made after challenge from Defra to ensure that customers are protected from additional investment costs that do not deliver tangible benefits. Customers will be further protected from bill volatility with our proposed bill smoothing mechanism.

<sup>4</sup> 150116 - TW - Menu choice and ODI re-calibration letter.pdf





7.40 We have therefore specified an ODI mechanism to recover:

$$\text{for agreed outputs which increase scope in our plan} = (1 - p) * (\sum_{T=0}^{T=5} \text{Increased net SEMD totex after programme agreement})$$

Where

$p$  = *The final plan Company totex sharing ratio per the Final Determination*

7.41 This adjustment will be assessed in year four for the years 2020 to 2024 and forecast for 2025. It will be subject to independent scrutiny and assurance.

7.42 These changes will be required as a function of an agreed regulatory requirement, and will be made as an RCV adjustment.

7.43 This performance commitment relates to the schemes and benefits delivered.

7.44 For clarity, this only applies to scope increases. It does not apply to scope or cost reductions as all money allowed for SEMD is ring-fenced and can only be spent on additional SEMD activities.



## I Summary of the performance commitment

7.45 The following tables summarise the parameters of the ODI package for this performance measure.

**Table 5: Our performance commitment**

		Starting level	Committed performance levels				
	Unit	2019-2020	2020-2021	2021-2022	2022-2023	2023-2024	2024-2025
Performance commitments	£m	0					TBD
Outperformance rate	As per PCS Annex 1						
Penalty collar			N/A	N/A	N/A	N/A	N/A
Penalty deadband			N/A	N/A	N/A	N/A	N/A
Payment deadband			N/A	N/A	N/A	N/A	N/A
Payment cap			N/A	N/A	N/A	N/A	N/A

Source: Thames Water, APP1 data table

**Table 6: Incentive rates**

Incentive type	Performance levels		Incentive rate
	Lower	Upper	
Payment	£0m	TBD	$(1-p) * \text{totex increased as a function of net agreed scope increase}$

Source: Thames Water internal data

7.46 With respect to the upper limit, we anticipate the maximum value of the programme would be no more than REDACTED. The final sum will be subject to the methodology proposed through the uncertainty mechanism.

**Table 7: Additional details**

Necessary detail on measurement units	The performance commitment is defined as the totex of SEMD programme in AMP7, as agreed with Defra.
Frequency of performance commitment measurement and any use of averaging	<p>The out or under performance applies to performance at the end of 2020 to 2025. This will be calculated at PR24 based on actuals for years 1 to 4 and forecasts for year 5 of 2020 to 2025.</p> <p>Performance against the commitment will be reported annually and assessed at the end of the AMP.</p> <p>Out or underperformance payments will be calculated at PR24, to be applied in 2025 Adjustment to RCV</p>
Timing and frequency of payments/penalties	End of AMP RCV adjustment.
Form of payment/penalty	<p>This incentive will provide the appropriate Totex (net of the Totex sharing factors) of any additional totex as a result of changes in scope related to the finalisation of the SEMD programme and corresponding changes in cost compared with Thames Water's April 2019 submission.</p> <p>For the avoidance of doubt, this does not apply to cost reductions as a result of efficiencies.</p> <p>Incentives will be applied in AMP8.</p>
Any other information or clarifications relevant to correct application of incentive	There are no exclusions.

Source: Thames Water internal data



## Section 8

# Reporting and assurance

- 8.1 This section sets out our reporting and assurance framework. Our company-wide approach and process for all regulatory assurance and reporting is detailed in CSD010 AMP7 performance reporting framework.

## Track record

- 8.2 Investment to protect our assets to ensure that they are compliant with the SEMD and associated guidance notes has been ongoing since AMP5. Our track record for completion and compliance has improved.
- 8.3 The requirements, issued by Defra and written by the CPNI (Centre for the Protection of National Infrastructure) are interpreted by the Business Resilience and Security Team and supplied to the business as a suite of security documents which define compliance (which is stated in terms of people, processes and technology). Any proposed solution which does not meet these standards is referred as a derogation request to the Security Programme Lead for agreement, and a record maintained of the agreed solution and associated derogation. Projects are subject to the Technical Governance Process which includes a review of testing evidence and the acceptability / compliance of the individual projects is audited in depth annually by an independent SEMD certifier as part of the annual SEMD Audit, with reporting submitted to both Defra and Ofwat.

## Measurement Audit and Assurance

- 8.4 For this Performance Commitment, the company will set out a methodology statement which will outline the processes and procedures for collecting data and calculating the metric to ensure consistency in the approach to reporting performance.

## Audit and Reporting

- 8.5 Progress is tracked on a monthly basis by the SEMD Programme Manager within our Business Resilience & Security team.
- 8.6 High level reporting is provided to the Security Board and the operational performance reporting teams and escalated as necessary through the Strategic Planning & Investment Director. For AMP6 our delivery teams report to the Chief Delivery Officer for Thames Water, a level of oversight that is expected to continue in AMP7. Both roles report to Thames Water at an Executive level.
- 8.7 Thames Water's SEMD Programme Manager holds progress reviews quarterly with Defra, in addition to the annual external independent examination as part of the business-wide SEMD Audit. This annual audit by an independent SEMD certifier reports on the quantitative & qualitative progress. They conduct reviews of compliance, derogations and report on the "quantity of sites" completed and the financial spend against the pre-agreed profiles. This audit is provided to Defra and Ofwat by a Defra approved auditor (SEMD certifier).



## **Audit and Assurance**

- 8.8 The Security Board is chaired by the Chief of Health, Safety and Security, and any issues are escalated through the Strategic Planning and Investment Director.
- 8.9 Quarterly progress reviews with Defra ensure that they are aware of progress, and any issues impacting performance or deliverables promptly. For this performance commitment the information that we publish on our performance will be assured to maintain and build a high level of trust and confidence from our customers and stakeholders. Our policy continues a risk based approach to assurance, using internal and external review to provide robust challenge and scrutiny of our performance.
- 8.10 Our existing risk based assurance process examines our end to end outcomes reporting process for each measure to identify the risks, strengths and weaknesses that may arise in providing the quality of information that customers and stakeholders trust. We conduct individual measure reviews that examine the probability of these risks materialising, and the potential impact that they may have. This ensures that we focus on the areas which may have impact on our reported performance which allows us to take action to monitor and actively manage any risks.
-