Regulatory financial tables

Accounting separation methodology statement

For the year ended 31 March 2015

June 2015

Contents

1. Introduction

1.1 Purpose

The purpose of this document is to explain the systems, processes and allocation methods that the Company has used to produce:

- The Accounting Separation ("AS") tables;
    - wholesale water services,
    - wholesale sewerage services, and
    - retail household ("HH") and non-household ("NHH") operating costs.

These are referred to as the regulatory tables throughout this document.

This methodology statement should be read in conjunction with the Regulatory accounts as reported within the Company's 2014/15 Annual report and financial statements. This methodology statement forms part of our internal governance process and forms part of our control and reporting structure as shown in table 1 below.

Table 1

External guidance		Internal processes		Outputs
Regulatory Accounting Guidelines ("RAG")		Regulatory tables methodology statement		Regulatory accounts and appendix for wholesale upstream services
Information Notices		Anaplan methodology and process document		Internal verification pack
				Compliance document

1.2 Scope

This document relates to Thames Water Utilities Limited appointed business only, and should be read in conjunction with the following guidance:

- RAG 4.04 'Guideline for the definitions for the regulatory accounts tables'; and
- Information notice ("IN") 14/05 issued 7 February 2014 documents:
    - *'Disclosure requirements for companies AS and upstream services data methodology statements 2013-14'; and*
    - *'AS guidance clarifications'.*

In February 2015, Ofwat issued IN 15/01 confirming that there are no further changes to regulatory requirements other than those noted above. In March 2015, IN 15/02 was issued, which re-affirmed IN 15/01 and clarified the retail HH/NHH audit requirements.

Please refer section 3 below for more information.

1.3 Governance

The regulatory tables and methodology statement are externally reviewed and audited by KPMG as part of their audit of the Company's 2014/15 Annual report and financial statements including the regulatory accounts.

The final outputs of the regulatory tables are included in the Regulatory accounts of the Company's Annual report and financial statements ("AR&FS") which can be found on our website www.thameswater.co.uk/results.

2. Systems and structures

2.1 Systems

The management structure of our business is based on an Operating company ("OpCo") structure (see section 2.21 below). However, for the preparation and reporting of operating costs for the accounting separation regulatory tables, we need to use an alternative structure within our regulatory model.

In 2015 Thames Water has implemented Anaplan, a cloud based business modelling and planning application as a tool with which to produce our regulatory reporting. 2015 is the first year that Anaplan has been used to produce the regulatory tables.

Anaplan has replaced the use of assessment cycles in SAP and is also being used for the production of the Upstream Services ("US") information. SAP remains the primary financial accounting and management tool used by the business and is the source of the data used in Anaplan.

Anaplan was implemented to overcome certain shortcomings in the SAP assessment cycles processes, especially around the production of the US and Retail tables which previously required a significant level of manual adjustment and checking. A separate US methodology statement (which is also available on our website) has been produced and should be read in conjunction with this methodology statement.

2.2 Structures

2.2.1 Operating company structure

The Company is structured into a number of OpCos; against which the operational performance is monitored:

Table 2

Operating company	Description of activities
Water OpCo	Responsible for all aspects of water abstraction, treatment and distribution and some shared services with the other OpCo's.
Waste OpCo	Responsible for all aspects of wastewater collection and treatment and some shared services with the other OpCo's.
Retail OpCo	Customer facing activities.
Group Services	Responsible for shared services across the wider organisation.

The above OpCos do not fully align with the AS units as defined by Ofwat. Anaplan has been used to produce the regulatory tables using the data from the OpCo structure contained within SAP.

2.2.1.1 Outsourced contracts

Ofwat requires companies to disclose any outsourcing arrangements, including agreements with other water companies and local authorities. This is required as there could be differences in costs, which may be significant, for any industry comparison. Table 3 below lists the outsourced contracts, which the Company had in place for the year ending 31 March 2015.

Table 3

Outsourced contract	Nature of contract	Managing Operating company
IT support	Offshore and office based support from WIPRO	Support Services
Legal services	Legal services from BLP	Support Services
Facilities	Facilities and maintenance - Mitie	Support Services
Supply chain	Procurement services supplied by Efficio	Support Services
Payroll	Payroll services supplied by Capita, Logica (until July 2014) and ESOS (from July 2014)	Support Services
Metering	Meter reading by Vennsys (up to February 2015), MeterU (from March 2015)	Retail
Capital delivery *(note 1)*	Delivering the capital programme	Waste
Major projects *(note 2)*	Support for major projects	Waste
Local authorities and Housing Associations	Billing and cash collection	Retail
Other water companies	Billing and cash collection	Retail
Customer contacts (part)	Non-network contacts supplied by Capita, Steria and HCL	Retail

Note 1: There are various contractors involved in delivering the capital programme, including; Optimise, GBM, B&V and MGJV.

Note 2: These include; Tamesis for the Crossness and Beckton STW upgrades, MVBJV for the construction of the Lee tunnel, and AE Com and CH2M-Hill for Long Reach upgrade.

2.2.1.2 Cost categories

Each operating company categorises its cost between direct, indirect and overheads as defined below:

- Direct costs are defined as costs which can be clearly traced to a cost object. A cost object can be a product, contract, project or site. For example, the employment costs of a Site Manager associated with his/her site, chemicals, site maintenance and power.

- Indirect Costs are defined as costs which cannot be traced directly to one cost object or activity. For example, the employment costs of a Regional Manager who has several sites under his/her remit that relate to the Business Unit.

- Overhead costs are defined as costs not directly related to the operational element of the Operating company. For example Head Office costs, Senior Managerial costs, and administration. A WTW (Water treatment works)/STW (Sewage treatment works) may have zero overheads for these purposes.

2.2.2 Regulatory reporting structure

Table 4 below, reflects the regulatory reporting structure as defined by Ofwat, which is reflected in the Anaplan regulatory model:

Table 4

AS unit	US unit
Wholesale Upstream	
Water services	
Water resources	Abstraction licence Raw water abstraction
Raw water distribution	Raw water transport Raw water storage
Water treatment	Water treatment
Treated water distribution	Trunk treated water distribution Local treated water distribution
Sewerage services	
Sewage collection	Foul Surface water drainage Highway drainage
Sewage treatment and disposal	Sewage treatment and disposal
Sludge treatment	Sludge transport Sludge treatment Liquor treatment
Sludge disposal	Sludge disposal
Retail downstream	
Retail	Household Non-household

Where the activity of a cost centre (the lowest management accountable reporting level against which budgeted costs can be monitored and reviewed) within the management structure is 100% attributable to one of the units listed above, and allocation of costs is not required, the cost centre is mapped, within Anaplan, directly to that unit.

Where the activity of a cost centre within the management structure is not 100% attributable to any of the above, the operating costs of those cost centres are allocated based on the underlying activity of the cost centre across the units listed above.

Typically the costs that are required to be allocated are either:

- costs that are held at a water treatment or sewerage treatment site level, where the activity straddles more than one of the units; or
- support service costs requiring allocation using the most appropriate methodology outlined in section 5.3 of this methodology statement.

The allocation process is further described in section 4 below.

3. Guidance

3.1 Regulatory Accounting Guidelines ("RAG")

Ofwat issued revised RAG in February 2013, which RAG 4.04 'Guideline for the definitions for the regulatory accounts tables' is the primarily guidance used in producing the regulatory tables.

The following principles outlined in RAG 4.04 have been applied when allocating costs to the relevant AS unit.

- **Transparency:** the attribution methods applied within the AS system need to be transparent. This requires that the costs and revenues apportioned to each service and business unit should be clearly identifiable. The cost and revenue drivers used within the system should also be clearly explained to enable a review of their appropriateness.

  Management considers that the Company's financial system and allocation methodology outlined in section 5 provide transparency as required by this principle.

- **Causality:** cost causality requires that costs (and revenues) are allocated to those activities and services that cause the cost (or revenue) to be incurred. This requires that the attribution of costs and revenues to activities and services should be performed at as granular level as possible.

  Wherever possible, costs are attributed to the process that causes the cost to be incurred. Where costs cannot be directly attributed, the costs are allocated as detailed in section 5 of this methodology statement. Management considers that it is compliant with this principle.

- **Non-discrimination:** the attribution of costs and revenues should not favour any business unit within the regulated company and it should be possible to demonstrate that internal transfer charges are consistent with the prices charged to external third parties.

  Management consider that the cost allocation methodology detailed in section 5 are non-discriminatory and do not favour any one business unit to the detriment of others.

- **Objectivity:** the cost and revenue attribution criteria need to be objective and should not intend to benefit any business unit or service.

  Management considers that the cost allocation bases described in section 5 are objective and do not favour any one business unit to the detriment of others.

- **Consistency:** the cost and revenue attribution criteria should be consistent from year to year to enable meaningful comparison of information over time. Changes to the attribution methodology from year to year should be clearly justified and documented.

  Management consider that the methodology is consistent with the prior year. Where changes to the allocation methods are required, these are documented in this methodology statement, see section 3.3.

Section 4 below details the process and section 5 the allocation assumptions outlining how the above principles have been applied.

3.2 Information Notice ("IN")

Thames Water, through its methodology statement and the corresponding AS tables are compliant with all Information Notices issued by Ofwat including:

- IN 14/05, clarifying the requirements that companies should follow in preparing the 2014 AS tables, including additional disclosure requirements;
- IN 15/01, confirming that there are no further changes to the regulatory reporting requirements for the year ending 31 March 2015; and
- IN 15/02 was issued, which re-affirmed IN 15/01 and clarified the retail and upstream services audit requirements.

3.3 Changes to methodology

3.3.1 Changes to methodology as a result of management review

3.3.1.1. General and support activities

During the period, management have reviewed the basis of cost allocation for the following areas of expenditure as detailed in table 5 below.

Table 5

General and support activity	2014/15 methodology	2013/14 methodology
General management	FTE's	Pro-rata to total direct costs
Finance	FTE's	Pro-rata to total direct costs
Human resources	FTE's	Pro-rata to direct employment costs

Table 6 details the impact to operating expenditure resulting from the above changes in allocation methodology had these been applied to the 2013/14 regulatory outputs.

Table 6

Activity	Wholesale water £m	Wholesale sewerage £m	Retail £m
General management	0.1	0.1	(0.2)
Finance	(0.7)	1.1	(0.4)
Human resources	(0.1)	0.2	(0.1)
Total	**(0.7)**	**1.4**	**(0.7)**

The Company consider that the change in the basis of cost allocation more appropriately reflect the nature of the costs incurred and is consistent with the Company's methodology used in its Price Review ("PR") 14 business plan submission to Ofwat in June 2014.

3.3.1.2. Pumping stations

The Company has reviewed the cost allocation methodology for its pumping stations within sewerage services. Previously pumping station costs have been allocated to sewerage collection, irrespective of the location or classification of the pumping station. Following the review, the Company's classification of pumping stations is as follows:

- **Terminal pumping stations** – the last station on the network that pumps sewerage directly into a STW for treatment, which may be inside or outside the STW boundary. These terminal pumping stations have been classified as **sewage treatment**, consistent with the Company's compliance with Ofwat's PR14 guidance;

- **Network pumping stations** – stations that pump sewage along the sewer network. These pumping stations have been classified as **sewage collection**; and

- **Private pumping stations** – there are four private pumping stations that have been adopted early by the Company; these are classified as **sewage collection** as these pump directly into the sewer network.

Table 7 below details the impact on operating expenditure within sewerage services of this change to pumping station cost allocation, if these were applied to the 2013/14 regulatory outputs.

Table 7

Activity	Sewage collection £m	Sewage treatment £m
Terminal pumping stations	(3.8)	3.8
Total	**(3.8)**	**3.8**

3.3.2 Changes to the application of the capitalisation policy in 2013/14 applicable to 2014/15

Customer side leakage ("CSL")

In 2013/14 the Company had changed the application of its capitalisation policy in respect of replacement and relining of customer side pipes carried out as a result of CSL. Prior to 2013/14, all costs associated with CSL were charged to operating costs. In 2013/14, the Company started providing a free service to customers for any customer side leakage repairs including the replacement and relining of customer supply pipes. Accordingly, any costs associated with the replacement and relining of customer side pipes have been capitalised as Infrastructure Renewals Expenditure ("IRE"), as management considers that such expenditure meets the criteria of IRE as defined in RAG 1.01. In the year ending 31 March 2015 the amount capitalised as IRE was £5.5m (prior period: £3.3m).

In accordance with the guidance in RAG 1.01 in respect of the accounting for IRE, the Company has charged £6.6 (prior period: £2.2m) of the above IRE as an Infrastructure Renewals Charge ("IRC") in the year as depreciation within the statutory accounts. The IRC charge includes £1.1m of IRE not expensed from the prior period.

However, to comply with the guidance provided in RAG 4.04 and IN 14/05, the Company has reclassified the IRC as operating cost within the historical and current cost regulatory accounts.

There are no other changes to the methodology or to management judgements that the Company has used in the 2014/15 regulatory outputs within the regulatory accounts other than those noted above.

4. Process

4.1 Anaplan methodology and allocation process

4.1.1 Methodology

A regulatory model has been developed in Anaplan, which the Company is now using as the system solution to produce the accounting separation regulatory tables and the US appendix to the regulatory accounts (separate US methodology statement published on our website). There are a number of advantages in using Anaplan compared to SAP assessment cycle functionality as listed below:

- Granularity of information – detailed reports created in Anaplan showing costs attributable or allocated to each regulatory unit. SAP functionality did not provide the granularity of data in a user friendly manner;
- Drill down capability – straightforward reports with easy drill down facilities compared to restricted capability in SAP;
- Reports – user designed reports in Anaplan; SAP reports generated from business warehouse data cube extracted from SAP ECC core system;
- User friendly functionality – user driven and design for maximum transparency of process compared to SAP ‘black box’ approach;
- Processing – Quick and easy to use regulatory model compared to the processing timescale of SAP; and
- Manual adjustments – None required in Anaplan, many adjustments required to SAP output as part of the production of the regulatory tables.

Financial data is extracted from SAP for all general ledger codes containing a value for every cost centre used in the period and loaded into the regulatory model.

Within the regulatory model are a number of pre-defined lists, which Anaplan uses in performing the direct attribution and allocation of costs, via modules (the basic models that Anaplan uses to produce the regulatory tables). The main lists are shown in table 8 below:

Table 8

List title	Description
Accounting separation and upstream services	These are the units as defined in RAG 4.04
Organisation	The consolidated regulatory view
CC hierarchy	Basic cost centre hierarchy maintained and controlled by the Company’s Financial Systems team
Direct/indirect/overheads	Lists the cost categories used in the model
GL Hierarchy	List of the cost categories as defined by Ofwat in RAG 3.07
Price control	The regulatory units as defined by Ofwat in RAG 4.04
SAP GL codes	Detailed list of all GL codes and parent as defined by the GL Hierarchy within SAP
SAP Cost Centres	Detailed list of all CC codes (categorised as direct, indirect and overheads) and parent as defined by CC hierarchy

The modules use assumption tables, which are based on the cost allocation methodology outlined in section 5 of this document to allocate costs to the regulatory outputs.

4.1.2. Allocation process

Allocation tables form the basis of the attribution and allocation of costs to the regulatory outputs. There are 6 assumption tables that the regulatory model uses, which are detailed in table 9 below.

Table 9

Allocation tables	Description
Retail cost centre apportionment	Attribution and allocation of total costs in a cost centre to one or more of the cost categories defined in RAG 4.04 for populating the retail proforma A8 of RAG 3.07
Retail cost centre and general ledger apportionment	Attribution and allocation of specified general ledger codes within a cost centre to one or more of the cost categories defined in RAG 4.04 for populating the retail proforma A8 of RAG 3.07
Retail HH/NHH apportionment (see Note below)	Allocation of costs by RAG 4.04 cost category to HH/NHH based on Ofwat's guidance
Wholesale cost centre apportionment	Attribution and allocation of total costs in a cost centre to one or more of the cost categories defined in RAG 4.04 for populating the wholesale water and sewerage proforma A7 of RAG 3.07
Wholesale cost category apportionment	Attribution and allocation of costs by specific cost category as defined in RAG 4.04 for populating the wholesale water and sewerage proforma A7 of RAG 3.07
Wholesale cost centre and general ledger apportionment	Attribution and allocation of specified general ledger codes within a cost centre to one or more of the cost categories defined in RAG 4.04 for populating the retail proforma A7 of RAG 3.07

Note:
During the year, management undertook a detailed 'burden of proof' exercise of support system outputs, which form the basis of the retail HH/NHH apportionment within this allocation table. See section 5.2.5.1 for further information regarding the 'burden of proof' exercise and Table 14 for the allocation % to Household and Non-Household.

The allocation tables are reviewed by management at least annually to ensure that the cost attribution and allocation methodology remains appropriate and valid, taking into account any business unit reorganisation, any operational process changes and latest Ofwat guidance. As part of the Anaplan regulatory model development, the allocation percentages for all cost centres were reviewed by finance and operational management; the allocation tables were updated based on the outcome of this review.

A cost centre allocation control file is maintained by the Regulatory Reporting team, which details all relevant cost centres' regulatory information, including basis of cost allocation.

Since the development of the regulatory model, from 2015/16 the regulatory outputs are to be produced quarterly for management review and reconciled to the OpCo management structure.

5. Allocation assumptions – accounting separation operating costs

5.1 Wholesale tables

5.1.1 General assumption

The following sections describe the allocation assumptions used in the production of the wholesale AS tables reported in the regulatory accounts. Cost drivers are assigned to each type of cost incurred and these are shown below:

The following are the cost drivers used for all expenditure lines listed in section's 5.1.2 (Water services), and 5.1.3 (Sewerage services). For general and support expenditure, the appropriate allocation basis is provided in section 5.3.

Cost Driver - A
This is where direct costs can be attributed directly to the relevant AS process.

Cost Driver – B
In cases where the cost can be directly attributed to a service area (water, sewerage or retail) but a specific cost driver is then used to allocate the cost to the appropriate AS business unit within the service area.

Cost Driver – C
In cases where the mapping is not direct, allocations are worked out using appropriate estimates and judgements based on available data and management's understanding of the business.

The following tables set out by line item the basis of allocations used to populate the tables.

5.1.2 Water services

Most costs can be directly attributed at source to an AS process within water services or to water treatment sites and allocated to the relevant process. Table 10 below details the allocation basis and assumption for each expenditure line.

Table 10

Expenditure line	Cost driver	Allocation basis	Allocation assumption
Power	B	Direct cost to site	Allocated based on assessment by site management using pumping head data and power of equipment.
Service charges	A	Actual charge from the Environment Agency directly coded to process	N/A
Bulk supply imports	A	Directly coded to process	N/A
Other operating expenditure			
- **Employment costs**	A/C	Directly coded to process where possible, else allocated based on assessment of time spent	Based on split of maintenance activity
- **Hired and contracted**	A	Directly coded to process	N/A
- **Materials and consumables**	A	Directly coded to process	N/A
- **Other direct costs**	B	Direct cost to site	Management judgement
- **General and support**		See section 5.3	
- **Scientific services**	B	Allocated to wholesale AS unit	Based on samples
- **Other business activities**	A	Regulatory costs	Equally allocated across all units
Local authority rates	B/C	Floor space	Business unit FTE's of floor space occupied
Cumulo rates	C	Gross Modern Equivalent Asset Value	Based on AS values
Third party services	B	Allocated to AS unit	Based on activity analysis

Further assumptions

Power: High lift pumps at the end of the treatment process (on site) have been reported as water treatment, with an allocation to treated water distribution for dual pumping.

Scientific services: All tap sampling at water customers premises are allocated to treated water distribution.

5.1.3 Sewerage services

Most costs can be directly attributed at source to an AS process within sewerage services or to sewage treatment sites and allocated to the relevant process. Table 11 below details the allocation basis and assumption for each expenditure line.

Table 11

Expenditure line	Cost driver	Allocation basis	Allocation assumption
Power	A/B	Direct cost to process by sub metering where it exists, else allocated	Allocated based on assessment of site activity by site management
Income treated as negative expenditure *	A	All income reported in Sludge treatment	N/A
Service charges	A	Actual charge from the Environment Agency for discharge consents directly coded to process	N/A
Bulk supply imports	A	N/A	N/A
Other operating expenditure			
- **Employment costs**	A/C	Directly coded to process where possible, else allocated based on assessment of time spent	Estimate based on time spent on process
- **Hired and contracted**	A/C	Directly coded to process where possible, else allocation. Sludge disposal costs fully allocated with exception of ash disposal which is directly coded	Allocated based on assessment of site activity by site management
- **Materials and consumables**	A/C	Directly coded to process, else coded to site and allocated between sewage and sludge treatment	Allocated based on assessment of site activity by site management
- **Other direct costs**	A/B	Direct cost to site, else allocated	Management judgement depending on the type the cost reported in this category
- **General and support**		See section 5.3	
- **Scientific services**	B	Allocated to wholesale AS units	Based on samples
- **Other business activities**	A	Regulatory costs	Equally allocated across all units
Local authority rates	B/C	Floor space	Business unit FTE's of floor space occupied
Cumulo rates	C	Gross Modern Equivalent Asset Value	Based on AS values
Third party services	B	Allocated to AS unit	Based on activity analysis

* Income treated as negative expenditure; includes income from Renewable Obligation Certificates, levy exemption certificates and the national grid reserve, in line with guidance provided in RAG 4.04. All internal power generation is used in the sludge treatment process; therefore all income is shown within this AS unit.

5.2 Retail

The retail business unit reports the customer facing costs of water and sewerage services.

5.2.1 General assumption

The assumptions, allocations and management judgements used for the collection, allocation and apportionment of the retail cost data are reviewed at least annually, to ensure that the methodology is still appropriate and updated to the current OpCo structure in the allocation of costs to the various retail activities in accordance with Ofwat guidance.

For this year's tables the production of the retail table split between HH and NHH is an automated process through the Anaplan regulatory model.

The following sections provide further guidance in support of the Company's retail cost table within the regulatory accounts.

5.2.2 Customer services managed activities within the Retail OpCo

The majority of costs reported within the Retail table are directly attributable and reported within the Customer services managed function of the Company.

Direct costs which are not included within the current Customer service function are allocated from Wholesale and are reported within Retail costs.

Table 12 below shows the activities and costs that are not reported within the Customer service managed function but are allocated from the Wholesale and Support Services OpCos to be reported within Retail costs:

Table 12

Cost Type	Allocated Cost £m
Services to developers – managed by the Wholesale team, the cost of supporting Developers in administration function is allocated to Retail	1.6
Network customer enquiries and complaints where it is found that it is not a network issue – this cost is managed by the Wholesale team	1.8
Disconnections	0.1
Customer side leakage *(see note below)*	9.9
Demand side water efficiency – measures to improve efficiency of water use, managed by Wholesale and support costs allocated to Retail	1.4
Other business activities	0.4
General and support costs	23.1

Note
Customer side leakage costs of £9.9m include £6.6m of IRC, see section 3.3.2 for further information.

Table 13 below details the Customer Services managed activities by cost centre and the cost allocation basis, used for each activity listed:

Table 13

Customer Services activities by cost centre	Basis of allocation	Billing	Payment, remittance and cash handling	Vulnerable customer schemes	Non-network customer enquiries & complaints	Network customer enquiries and complaints	Debt management	Doubtful debts	Meter reading	Services to developers	Other operating expenditure
Revenue Contact Centre Agents	Based on average Full Time Equivalent ("FTE") requirements for Work Baskets/Work streams as per Agents Workload Planning (Long Term Plan)	•	•	•	•		•				
Operational Contact Centre Agents	Specific to Netw ork /Operational Enquiries & Complaints					•					
Operational contact centre	Specific to Netw ork /Operational Enquiries & Complaints					•					
Office agents	Pro-rata to FTE split betw een Revenue and Operational Contact Centre	•	•	•	•		•				
Outsourced Office Agents	Based on Analysis of Calls Taken, and Work streams / Workbaskets for Outsource providers.	•	•		•		•				
Mail house	Based on volumes of type of bills/mail	•	•				•				
Key Accounts (all NHH)	Based on Managers Activity Summary for key accounts agents	•	•		•	•	•				
Head of Revenue *	Based on FTE allocation relating to Manager's roles/duties	•	•				•				
Billing & Sales	Specific to Billing	•									
Revenue Agents (debt recovery)	Specific to Debt Management						•				
Cash & Debt Staff & Other Operating costs	Specific to Payment Handling & Debt Management, allocation based on managers FTE assessment.		•				•				
Cash & Debt - Payment Commissions	Specific to Payment Handling		•								
Cash & Debt - DCA commissions	Specific to Debt Management						•				
LA/HA Commissions (all HH)	Management judgement based on TW relative costs for the activities covered, and historical discussions w ith LA/HA's.	•	•		•		•				
Meter reading	Specific to meter reading								•		
WOC Bad Debt	Specific to Doubtful Debts							•			
WOC Commissions	Allocation across activities covered by WOCs pro-rata to their Retail Costs submissions	•	•		•		•		•		
Bad Debt Provision & Excess Credits	Specific to Doubtful Debts							•			
Customer Insight & Resolution - RCC	Specific to Non-Netw ork Customer Enquiries & Complaints				•						
Customer Insight & Resolution Ops	Specific to Netw ork Customer Enquiries & Complaints, including GSS payments allocated to other operating expenditure					•					•
Customer experience and engagement - Staff costs	Based on Managers assessment of FTE's supporting customer non-netw ork and netw ork activities				•	•					
Customer experience and engagement - Non-Staff costs	Specific costs relating to customer non-netw ork, netw ork activities and billing w ith some costs shared across these activities (based on managers assessment)	•	•		•	•					
IT & Change -Transformation	General and support cost										•
Senior Management Team	General and support cost										•
Developer Services	Specific to Developer services									•	

5.2.4 General and support cost assumptions

The General and support allocation is addressed in section 5.3 below for all AS units. General and support costs represent overheads that are allocated to Wholesale and Retail AS units.

The allocation of General and support costs between HH and NHH is allocated based on the number of customer accounts, which is in accordance with the guidance received for PR14.

5.2.5 Definition of household and non-household properties used in this methodology statement

The Companies allocation of costs into HH and NHH is compliant with the definitions below as clarified by Ofwat in IN 14/05.

Households: These are properties used as single domestic dwellings (normally occupied), receiving water for domestic purposes which are not factories, offices or commercial premises. These include cases where a single aggregate bill is issued to cover separate dwellings having individual standing charges. (In some instances the standing charge may be zero). The number of dwellings attracting an individual standing charge and not the number of bills should be counted. Exclude mixed/commercial properties and multiple HH properties, e.g. blocks of flats having only one standing charge.

Examples of households:
• typical family dwelling, i.e. terraced, semi-detached, detached house or flat having individual standing charges; or

• Local authority family dwellings which each have individual standing charges but may be included in an aggregate water bill.

Non-households: These are properties receiving water for domestic purposes, but which are not occupied as domestic premises, or where domestic dwellings are combined with other properties, or where properties are in multiple occupations, but only have one standing charge. The number of bills should be counted in this case.

Examples of non-households:
• industrial/commercial properties (e.g. institutions, farms, public houses, offices);

• combined premises with a single standing charge, such as a flat above a shop; or

• block of flats, or caravan site (consisting of multiple dwellings), but only having one standing charge. These must be counted as one NHH property."

5.2.5.1 Allocation of costs to HH/NHH

During the year, a 'burden of proof' exercise was performed to ensure that the outputs from the underlying source systems, which are used as the basis of the HH/NHH allocation, complied with the HH/NHH definition above, and PR14 basis of cost allocation guidance. The result of this exercise provided the basis of cost allocation to HH/NHH.

Table 14 below details for each activity the methodology used to allocate costs to HH and NHH cost driver and the rationale used. This table also provides the percentage allocation for each activity to HH/NHH.

Where a cost has been allocated from the wholesale business, information supporting the allocation method used is also provided in the table or within section 5.2.8 below.

Table 14

Expenditure line and activity	Directly retail or allocated	Driver	Rationale	HH allocation %	NHH allocation %
Customer services					
- Billing	Direct	Number of bills issued to HH/NHH customers	Ofwat guidance	87.20	12.80
- Payment handling, remittance and cash handling	Direct	Level of payment transaction processed and commissions paid by HH/NHH customer	Transaction analysis	85.76	14.24
- Charitable trust donations	Allocated from External Affairs	Costs separately identified and allocated 100% to HH	All HH	100.00	-
- Vulnerable customer schemes	Direct	All HH	All HH	100.00	-
- Non-network customer enquiries and complaints	Direct	Pro rata to number of customer network HH/NHH contacts received	Ofwat guidance	86.78	13.22
- Network customer enquiries and complaints	Direct	Pro rata to number of customer operational HH/NHH contacts	Ofwat guidance	89.24	10.76
- Network customer enquiries and complaints where it is found that it is not a network issue	Allocated from Wholesale	Based on number of engineer customer visits at a fixed call out rate	Ofwat guidance	94.69	5.31
Debt management	Direct	Pro-rata to HH/NHH Outstanding Debt with DCA commissions specific to HH/NHH.	Ofwat guidance	81.99	18.01
Doubtful debts	Direct	Pro-rata to average HH/NHH % for cost of 5 years debt write-offs.	Based on actual history of debt write-offs by HH/NHH	91.06	8.94
Meter reading	Direct	Allocation to HH/NHH based on time taken for Meter Reads.	Ofwat guidance	65.85	34.15
Services to developers	Allocated from Wholesale	Customer facing enquiries allocated 100% to NHH	Costs identified within a wholesale cost centre used wholly in this activity	-	100.00
Other operating expenditure					
- Disconnections	Allocated from Wholesale	No of disconnections managed - all NHH	Ofwat guidance	-	100.00
- Demand side water efficiency	Allocated from Wholesale	HH/NHH Activity cost analysis.	Ofwat guidance	70.30	29.70
- Customer side leaks	Allocated from Wholesale	Analysis of number of jobs split HH/NHH	Ofwat guidance	99.35	0.65
- Other direct costs	Direct	Pro rata to billing	Small value costs	87.20	12.80
- General and support		See section 5.3		94.21	5.79
- Other business activities	Allocated from Regulation	Costs allocated equally across 9 AS units	Pro rata to number of customers billed into HH/NHH	94.21	5.79
Local authority rates	Direct	Floor space occupied	Staff based at Walnut Court and Kemble Court	94.21	5.79
Third party services	N/A	N/A	N/A	N/A	N/A

IN 14/05 document '*Disclosure requirements for companies AS and upstream services data methodology statements 2013-14'* issued by Ofwat on 7 February 2014, require the following information to be disclosed within companies' methodology statements.

5.2.6 Billing and collection

5.2.6.1 Percentage of income

The percentage of income that the Company outsourced for billing and collection is based on the revenue billed on behalf of the company by Local Authorities/ Housing Associations (LA/HA), who bear the risk of any non-collection of any outstanding debt. Billed value taken from year-end LA/HA Commissions Report. During the year ended 31 March 2015, LA/HA billing percentage of turnover billed was 6.7%.

5.2.6.2 Bills to occupier policy

The Company only raises bills in the name of the "occupier" when it has evidence that the property is occupied but cannot confirm the name of the occupier. When the occupant is identified the bill is cancelled and rebilled in the customer's name. If the Company has not identified an occupant within 6 months the bill is cancelled and the property is classified as empty. The value of bills issued in the name of the occupier included in turnover is obtained from the 'Occupier Billing report' run by our Billing Analysts. No specific doubtful debt provision is provided for bills issued in the name of the occupier at the year-end. A bad debt provision is applied to all outstanding debt, at the year-end a provision of 14.6% is applied to all debt less than one year old, which would include any debt in the name of the occupier.

5.2.6.3 Doubtful debt policy where the customer has vacated a property

Where a customer has vacated a property leaving unpaid debt, this is handled within our debt management process, credit notes are not issued to cancel any such uncollectable debt, it is written-off as bad debt.

5.2.6.4 Bad debt provision policy

The bad debt provision is charged to operating costs to reflect the company's assessment of the risk of non-recoverability of debtors. It is calculated by applying expected erosion rates to debts outstanding at the end of the accounting period. These collection rates take into account the age of the debt and type of debt. Higher provisioning percentages are applied to older categories of debt. Bad debt provisioning rates are updated annually to reflect the latest collection performance data from the company's billing system. All debt greater than 4 years old are fully provided for.

The bad debt provision also takes into account the recoverability of debts which will ultimately be cancelled and may or may not be rebilled, and of debts which have not yet been billed, but are part of the metered sales accrual.

Future expected performance (taking into account historic trends) is also used to validate our bad debt provisions to ensure that use of historic performance will not result in a material misstatement.

We also provide for debts from Water Only Companies (WOCs), who bill for our sewage service on our behalf. Since detailed information about the debt is unavailable to us, we provide for the debt based on the historical write-offs.

5.2.7 Contact centre and outsourced costs

Contact Centre Agents' costs and Outsourced costs are allocated to activities on the basis of the FTE requirement planning and the work packs and work streams issued to outsource partners.

WOC commissions are allocated across activities in accordance with the previous year's Retail submission.

LA/HA commissions are allocated across the activities they undertake, i.e. billing, payment handling, debt management and customer (non-network) queries based on the relevant weighting of those activities within the Customer Service Operating costs, factored for the relative costs for the LA/HAs based on management discussions.

5.2.8 Further assumptions

The following assumptions have been applied consistently with the prior period.

Customer services expenditure in the retail table includes payment handling, remittance and cash received from developers.

Network customer enquiries and complaints include costs:

- associated with the scheduling of jobs where they are triggered by a customer call,
- visiting the customer to investigate the problem where it is found that it is not a network issue, and
- internally generated calls to enable the customer call to be resolved.

These costs are reported in the Operations contact centre, a separately identified cost centre within the Customer service operating company.

Doubtful debts split into HH/NHH are based on 5 year history of the debt write-offs. Ofwat's latest PR14 guidance proposes that companies should directly attribute costs on a customer specific basis, however, our systems do not currently enable us to report on this basis.

Demand side water efficiency initiatives within Retail refer to the Base Line Programme ("BSWE") costs identified and allocated to retail from wholesale.

Customer side leakage costs are reported within a separately identified cost centre in the Operations operating company, the costs being transferred to retail for AS reporting. Operating costs include £6.6m of IRC to comply with RAG 4.04 and IN 14/05.

Local authority rates are allocated to Retail based on office occupancy of the Customer Services operating company; Walnut Court in Swindon, and Kemble Court in Reading where the Operations contact centre is based. These costs are shown within the Local authority rates caption in the Retail table within the Regulatory accounts.

Key accounts retail team costs are allocated to retail from the Commercial business unit within Wholesale. This represents the cost of managing key commercial NHH accounts.

Third party costs – there are no costs incurred within Retail that are classed as third party costs, therefore no costs have been reported within this line.

5.3 General and support expenditure

These costs reflect the support services functions within the Company, which are detailed below in Table 15 with an explanation of the appropriate allocation method used. The costs allocated to the AS units are net of any recharges of costs that the support services functions provide to associate companies of the group and recharges to the non-appointed business of the Company. All General and support costs are shown within the 'Other operating expenditure' line category of the AS tables; none are shown as direct expenditure.

The allocation methodology has been updated to reflect management's review of cost allocation, outlined in section 3.3.1.1 above. Management considers that the allocation assumptions and methodology detailed in section 5 are reasonable and are compliant with the cost allocation principles contained in RAG 4.04.

Table 15

Support Service function	Activity and type of expenditure incurred	Allocation Basis Used
General Management	Employment costs and consultancy costs managed within the Chairman's and CEO's offices	After recharging a proportion of costs to other associated companies of the Kemble Group, remaining costs are allocated based on the level of the FTE's of each of the AS units.
Finance	Internal audit, taxation, financial control and treasury functions. Costs include employment , audit fees and subscription fees	Costs are allocated based on the level of the FTE's of each of the AS units.
Supply Chain	Management of outsourced supply chain provider	Management and third party contractor costs are allocated pro-rata to the level of bought in services of each AS unit.
Vehicles and Plant	Fleet management costs and fuel costs	Management of the Company's vehicles are allocated based on the relevant AS unit in which the vehicle is used.
Legal & secretariat	Management of outsourced legal service provider, management of board and related committees	Allocation applied to all legal requests in the managed legal service database based on work undertaken. All other costs pro-rata to direct costs.
Human Resources costs	Employment costs, training costs and other HR business support costs	Costs are allocated based on the level of the FTE's of each of the AS units.
IT	Employment and telephony costs All other costs including management of outsourced IT support costs	These costs are allocated pro-rata to direct employment costs incurred. These costs are allocated pro-rata to direct hired and contracted costs incurred.
External Affairs (excluding Customer Assistant Fund)	This activity includes corporate communications, shareholder engagement and corporate responsibility.	Due to the nature of the costs incurred it is considered appropriate to allocate these costs pro rata to direct costs incurred.
Facilities and Maintenance	This function includes office supplies, security, facilities and building maintenance costs.	Costs are allocated based on the level of the FTE's of each of the AS units
Health and safety	Cost of the advisors providing support to Company employees and contractors	All costs relating to the management of Health and safety are allocated pro-rata to direct employment costs.
Insurance premiums	Costs include public liability, employers' liability, construction and property damage	Allocation based on the type of insurance premium incurred and claims history

6 Allocation assumptions - fixed assets

6.1 General assumptions

The following documents the process adopted by the Company to comply with Ofwat's guidance for the AS fixed asset tables. The methodology detailed in this section covers the assumptions, adjustments and method of analysis applied to populate the fixed asset tables.

The Company maintains a current cost asset register that is based on the 2008 modern equivalent asset value (MEAV) revaluation adjusted to include fixed assets commissioned from 2009 to date.

Assets are commissioned to sites and are at present exclusively utilised by the service carried out at that facility. Consequentially, at present, there are no recharges between business units relating to asset use.

Asset data is mapped to AS categories using a combination of asset class, purpose code and location code. Any assets that do not fall into the Ofwat categories are consolidated into service specific overheads (water or sewerage). This approach enables the majority of asset data to be analysed to match the Ofwat AS categories. The water and sewerage overhead depreciation charges are then absorbed into the appropriate Ofwat categories on a percentage uplift basis.

The Company's AS fixed asset tables methodology remains unchanged compared to the prior year.

The following section tabulates the allocation assumptions used in the production of the AS tables reported in the regulatory accounts. Cost drivers are assigned to each asset classification and these are shown below:

The following are the cost driver's used for populating the asset related expenditure and depreciation lines.

Cost Driver - A
Is where direct costs can be attributed directly to the relevant AS business units.

Cost Driver – B
In cases where the cost can be directly attributed to a service area (water, sewerage or retail) but a specific cost driver is then used to allocate the cost to the appropriate AS business unit within the service area.

Cost Driver – C
In cases where the mapping is not direct, allocations are worked out using appropriate estimates and judgements based on available data and an understanding of the business.

Table 16 below set out by line item the basis of allocations used to populate the tables.

Table 16

	Cost Driver	Allocation Basis Used
Water and Sewerage Service assets	A	**Direct using project purpose code and asset class/category.**
Land	A	**Direct using project purpose code and asset class/category.**
Buildings and offices	A	**Direct using project purpose code and asset class/category.**
Plant	A	**Direct using project purpose code and asset class/category.**
Fixtures and fittings	A	**Direct using project purpose code and asset class/category.**
Retail IT systems	A	**Direct using project purpose code and asset class/category.**
Meters	A	**Direct using project purpose code and asset class/category.**
General and support	**C**	**Indirect as an uplift applied separately to water and sewerage.**

6.2 Calculation of Current Cost Depreciation (“CCD”).

The CCD is based on Modern Equivalent Asset (“MEA”) commissioned asset data.

Current year commissioning data is based on asset records downloaded from SAP ECC Asset Management and General Ledger into Microsoft Excel. This data is consolidated with project level detail from SAP Project Systems to create an enhanced data set. The MEA commissioning data set includes commission date; gross book value; annual depreciation charge, asset class and AS analysis which is not available in Asset Management.

This current year data is then incorporated with the prior year’s MEA commissioned data.

This final data set is uploaded into Business Objects and analysed as detailed below, see ‘section 7.4’.

6.3 Analysis of Current Cost Fixed Asset Additions

The current year fixed asset additions data is based on SAP Project Systems data downloaded into Microsoft Excel. This is then reconciled to SAP ECC to ensure the fixed asset spend for the year is accurate.

This final data set is uploaded into Business Objects and analysed as detailed below, see ‘section 7.4’.

6.4 Business Objects Analysis

The two data sets are analysed independently within Business Objects to enable the allocations to the AS units on the following basis:

Wholesale

The data is analysed in table 17 below:

Table 17

Classification	Asset field used	Source
Water or Sewerage	Purpose code	SAP PS
Infrastructure or Non-Infrastructure	Asset class	SAP Asset Module
Base or Enhancement	Asset category	SAP PS

A second tier allocation to exact AS business unit is then performed based on Purpose Code (SAP PS).

Retail

The Location Code field is used to extract data relating to Customer Services which is then allocated to Retail. The additions and depreciation figures for Retail are derived from the sum of all assets with a "location code" e.g., for Walnut Court i.e. "WALNO1ZZ" plus a proportional allocation of the overhead.

Retail assets that are not directly assignable to either HH or NHH are allocated based on the numbers of customer accounts.

Table 18 below provides details of the assets reported within retail showing the closing net book value and current cost depreciation charged in the year.

Table 18

Asset	Net book value £m	Depreciation charged in the year £m
Billing system	6.2	6.2
Customer Relationship management Billing (CRMB) system	2.4	-
Other computer hardware and software assets under construction	9.1	-
Land and buildings, fixtures and fittings, plant and machinery and other assets *(see note below)*	41.8	2.8
Total	59.5	8.0

Note
Total assets with a NBV of £41.8m include £38.4m of shared assets with Wholesale, who are the principal users of these assets.

Retail assets do not have any amortisation of deferred credits arising from third party contributions on any of the assets reported in the above table.

Additionally, Retail does not have any intangible assets and therefore there is no amortisation reported within retail.

Overheads

Assets that do not fall into the AS business units are consolidated into service specific overheads. The overhead data is then allocated across the AS business units on a percentage uplift basis.

Non-Infra Base Additions

As Non-Infrastructure Base expenditure is reported against "Additions" under "Gross replacement cost" for the year, their value is replicated in the disposals line on the assumption that they represent "like for like" replacements of existing non infrastructure assets.

These costs do not represent an enhancement to the asset base so a corresponding and off-setting disposal is deemed to exist, i.e. this spend represents a "like for like" replacement of existing assets.

7. Capitalisation Policy

7.1 General principles

The Company's Capitalisation Policy details the framework, principles and specific treatment for all capital expenditure within the Company.

This policy contains specific guidance on a number of areas. Where there is no guidance on a particular type of expenditure, the principles contained within the policy are to be used when ascertaining the appropriate accounting treatment.

There has been no change in the policy in the reporting period.

In addition, a number of local policies exist, which are consistent with the overall policy and provide further guidance to the business.

The company adopts the following principles in relation to its capitalisation policy:

- Adherence to Accounting Standards, particularly FRS 15 'Tangible Fixed Assets';
- Adherence to Regulatory Standards, particularly RAG 2 04 'Guideline for classification of Expenditure',
- Where practicable, capital costs are directly attributed to projects;
- Where capital costs cannot be directly attributed to projects, these need to be allocated via a capital overhead mechanism;
- All capital expenditure is formally approved by an appropriate level of management as defined in the Company's Schedule of Delegated Authorities policy.

7.2 General overheads

The Company recognises that elements of its Support services costs, whilst not directly attributable to individual projects, are actually incurred to sustain capital delivery. These costs can be characterised as expenditure that would have been avoided if the capital programme did not exist. Such costs are known internally as Design and Procurement General (D&PG). These costs are absorbed as a percentage of total capital cost.

Exclusions are identified for those support costs where it is clear that the expenditure is of a specific nature that does not qualify for capitalisation, i.e. operational costs which are excluded from the D&PG percentage as detailed in the policy document.

7.3 Employee overheads

Certain salary related costs attributable to the delivery of the capital programme are charged directly to capital projects through a time sheeting process. Such costs are primarily employee costs and associated indirect costs that arise as a result of having a pool of engineering resource. The timesheet activity rates are reviewed annually.

7.4 Internal verification

The existence and completeness of capital expenditure is verified through robust reviews on a project basis at the Company's Investment Committee. Investment papers are checked by the Capital Investment Team prior to their submission.

The level of capital expenditure by business unit is reviewed at a monthly meeting chaired by the Asset Investment Director.

There is regular monitoring of overheads recharged to capital and monthly reviews of capital spend.

Specific Internal Audit reviews are performed as agreed with the Audit Committee to supplement the capital controls.

7.5 Processes and procedures in place to assess the continued appropriateness of the accounting policies.

The capitalisation policy is reviewed on an annual basis. A refresh of the percentage of capitalisation of overheads by department has been performed in the current year.

8 Year on year comparison of operating expenditure

8.1 Wholesale water

Table 19

	£m
2013/14 reported values	607.0
Impact of change in methodology of certain general and support activities	(0.7)
Impact of inflation	5.5
2013/14 inflated to 2014/15 prices	611.8
Year on year movements:	
Lower abstraction licence costs	(15.7)
Increased treated water distribution direct costs	15.2
Increased general and support costs	5.3
Lower rates	(1.3)
Lower IRC	(4.5)
Other operating cost movements	0.1
2014/15 reported values	**610.9**

Commentary

The lower abstraction licence costs include a one off refund of Environmental Improvement Unit Charges paid to the Environment Agency in prior periods.

The increase in treated water distribution direct costs principally reflecting higher contractor rates partially offset by lower employment costs.

The increase in general and support costs include one-off redundancy and reorganisation costs incurred as a result of the organisational design of the Company's operations in readiness for the 2015 to 2020 regulatory period.

8.2 Wholesale sewerage

Table 20

	£m
2013/14 reported values	622.4
Impact of change in methodology of certain general and support activities	1.4
Impact of inflation	5.6
2013/14 inflated to 2014/15 prices	629.4
Year on year movements:	
Lower waste network costs (2014 included wet weather event costs)	(11.5)
Higher general and support costs	6.7
Increase in sludge treatment costs	5.5
Increase in current cost depreciation	18.5
Other operating cost movements	4.3
2014/15 reported values	**652.9**

Commentary

The lower waste network costs is principally due to a reduction in sewage collection costs. The exceptional rainfall during the second half of 2013/14 led to an increase in the sewage collection costs for that period, which has not been repeated in 2014/15.

The increase in general and support costs include redundancy and reorganisation costs incurred as a result of the organisational design of the Company's operations in readiness for the 2015 to 2020 regulatory period.

Sludge treatment costs increased in the year primarily as a result of higher intersite tankering costs. The prior year's tankering costs were lower than normal due to increased tanking requirements required for sewage collection as a result of the exceptional rainfall.

The increase in current cost depreciation of £20.6m is principally within sewage treatment (£18.0m) as the Company continually improves the operation of its treatment works.

8.3 Retail

Table 21

	£m
2013/14 reported values	175.5
Impact of change in methodology of certain general and support activities	(0.7)
Impact of inflation	1.6
2013/14 inflated to 2014/15 prices	176.4
Year on year movements:	
Customer services expenditure:	
➢ Reduced network and non-network customer enquiry activity	(3.4)
➢ Increased charitable trust fund donation for vulnerable customers	2.6
➢ Lower billing, payment handling, remittance and cash handling activity	2.6
Increased bad debt charge	11.1
Lower debt management costs	(1.7)
Increased Customer Side Leakage costs	5.1
Increased general and support activity	5.1
Lower current cost depreciation	(1.1)
Other operating cost movements	(0.8)
2014/15 reported values	**195.9**

Commentary

The reduced level of network and non-network customer enquiry activity is principally due to the higher than normal level of activity in the prior period, as a result of the exceptionally high winter rainfall.

There has been an increase in the level of contributions to the customer assistance fund to support those customers with financial difficulties in paying their water bills. The increase has been funded by the tax refund received in the year and not by customers, reflecting shareholders commitment in assisting customers with payment difficulties.

Lower billing, payment handling and remittance and cash handling activity reflecting lower bill volumes compared to the prior period.

The increase in bad debt charge of £11.1m principally reflects an increase in the value of younger aged debt written off that had not been fully provided. The increase has been partially offset by lower debt management costs due to lower commission costs to LA/HA.

Customer side leakage costs have increased reflecting the increased level of replacement and relining of customer side pipes, undertaken at no cost to the customer. This reflects the change in policy in 2013/14 outlined in section 3.4 above.

The general and support increase of £5.1m include redundancy and reorganisation costs incurred as a result of the organisational design of the Company's operations in readiness for the 2015 to 2020 regulatory period.

The reduction in current cost depreciation reflects an increase in assets that are yet to be depreciated.

The following table details those cost included within the other operating expenditure caption within the retail table on page 148 of the AR&A.

Table 22

	Retail £m
Disconnections	0.1
Demand side water efficiency costs (see note 1 below)	1.4
Customer side leakage costs (see note 2 below)	9.9
General and support costs	23.1
Streetwork customer facing activity costs	2.0
Regulation costs	0.4
2014/15 reported values	**36.9**

Note 1:

Demand side water efficiency costs of £1.4m reflect the baseline expenditure transferred to retail from wholesale as outlined in table 22 above. In addition, a further £1.0m of enhanced expenditure was incurred, and in accordance with Ofwat's PR14 guidance, this cost has been reported within treated water distribution within wholesale.

Note 2

The total cost of £9.9m includes expenditure required to meet wholesale delivery of its leakage outcomes. RAG 2.05 - guideline for classification of costs across price controls, effective for the 2015 to 2020 regulatory period, state that expenditure required meeting the delivery of wholesale outcomes should be reported within Wholesale. If the Company had retrospectively applied RAG 2.05 for the year ended 31 March 2015, the £9.9m costs would have been split between wholesale and retail as detailed in table 23 below.

Table 23

	£m
Wholesale outcome delivery of leakage target expenditure	7.4
Retail CSL related expenditure	2.5
2014/15 reported values	**9.9**

9 Comparison of actual operating expenditure with Final Determination

Table 23

	Water £m	Sewerage £m	Total £m
Final determination allowance *	404.6	387.3	791.9
Less deficit repair payment included in above	(10.7)	(10.3)	(21.0)
Final determination excluding deficit repair payment	393.9	377.0	770.9
Actual expenditure	409.9	413.7	823.6
Variance – net increase above FD	(16.0)	(36.7)	(52.7)
Analysis of variance			
Bad debt above the amount in the Final Determination	(13.1)	(13.2)	(26.3)
Traffic Management Act	2.0	0.3	2.3
Lower accrued pension costs	1.3	1.3	2.6
Rates	1.6	1.1	2.7
Carbon reduction commitment costs	(5.1)	(2.5)	(7.6)
Private sewers	-	(4.6)	(4.6)
STID costs not in FD	(5.4)	(5.1)	(10.5)
Organisational Design restructuring costs	(7.0)	(6.2)	(13.2)
Other net cost movements	9.7	(7.8)	1.9
	(16.0)	(36.7)	(52.7)

*Final determination includes cash pension costs, whereas the AS tables within the regulatory accounts include accrued pension costs in accordance with FRS 17.