Dŵr Cymru
Welsh Water

PR14 Reconciliation Rulebook

Update

Supporting document

July 2019

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The proposed adjustment to the revenue requirement at PR19 and the midnight adjustment to the RCV is shown in Table 1 below. The high-level changes from the Reconciliation Rulebook early submission (July 2018) are shown in Table 1a.

Table 1: High level summary of submission (2017-18 prices)

	Water (£m)	Waste (£m)	Retail (£m)	Total (£m)
Revenue Adjustment				
Close out of PR09 (2014/15)	(11.2)	(1.0)	-	(12.2)
2015-20 Totex	29.4	(8.4)	-	21.0
Outcome Delivery Incentive	(11.7)	11.8	-	0.1
Wholesale Revenue	(13.0)	(11.0)	-	(23.9)
Retail Revenue	-	-	2.0	2.0
Water Trading	-	-	-	-
Total Revenue Adjustment	**(6.5)**	**(8.6)**	**2.0**	**(13.0)**
RCV Midnight Adjustment				
Close out of PR09 (2014/15)	36.9	8.4		45.3
PR09 CIS error correction	(34.3)	(38.4)		(72.8)
Outcome Delivery Incentive	-	-		0.0
2015-20 Totex	51.9	(25.4)		26.5
Land Sales	(0.5)	(0.1)		(0.5)
Total RCV Adjustment	**54.0**	**(55.5)**		**(1.5)**

Table 1a: Changes from "early submission" July 2018 (2017-18 prices)

	July 2018 (£m)	July 2019 (£m)	Difference (£m)
Revenue Adjustment			
Close out of PR09 (2014-15)	(12.3)	(12.2)	0.1
2015-20 Totex	15.2	21.0	5.8
Outcome Delivery Incentive	1.1	0.1	(1.0)
Wholesale Revenue	(0.6)	(23.9)	(23.3)
Retail Revenue	4.4	2.0	(2.4)
Water Trading	-	-	-
Total Revenue Adjustment	7.7	(13.0)	(20.7)
RCV Midnight Adjustment			
Close out of PR09 (2014-15)	45.9	45.3	(0.6)
PR09 CIS error correction	(73.5)	(72.8)	0.7
Outcome Delivery Incentive	-	-	-
2015-20 Totex	18.0	26.5	8.5
Land Sales	(0.5)	(0.5)	0.0
Total RCV Adjustment	(10.1)	(1.5)	8.6

*Any differences are due to rounding

Reasons for material change:

2015-20 Totex	Additional expenditure in 2019/20 from our early submission is due to reservoir safety, customer experience, IT systems and energy efficiency.
WRFIM	Over recovery of revenue in 2018/19 and the removal of the forecast abated revenue in 2019/20

Statement of Board Assurance

PR14 Reconciliation Rulebook for PR19 – July 2019 update

The Board has considered the Reconciliation Rulebook at its meeting held on 4 July 2019. The Board considered relevant supporting materials and made appropriate enquiries of the Executive Team, in particular the Regulation and Strategy Director and Jacobs who had been engaged to provide independent assurance, our approach and the information and data that supports the assumptions used in the submission.

Having made reasonable and relevant enquiries, the Board is able to confirm that it supports the submission.

We can confirm that appropriate steps have been taken to ensure that the information on which the document is based is accurate within reasonable levels of tolerance. The tables and the required additional information have been prepared and delivered under the direction of experienced staff, using appropriate processes and internal systems of control and has accordingly been prepared to a standard that could be reasonably expected of a diligent company. The assurance process was approved by the Audit Committee on 5 June 2019.

Having regard to the information requirements in the document 'Delivering Water 2020: Our final methodology for the 2019 price review' issued by the Water Services Regulation Authority on 15 December 2017 and subsequent PR19 queries and answers, the Board has satisfied itself that our submitted models and the information provided in this document have been compiled in accordance with these requirements.

This supporting document is published with the models and data tables and contains the proposed PR19 adjustments, information and commentary as required. It sets out the accuracy of the data tables and supporting information and exposes material assumptions.

Alastair Lyons
Chairman
On behalf of the Board
4 July 2019

1 Methodology

1.1 Purpose

The PR14 Reconciliation Rulebook submission comprises of the following documents:

1. **PR19 Business plan tables** "PR19-Business-plan-data-tables-Past-Delivery WSH.xlsb" using the company specific tables uploaded on SharePoint 6th May 2019;
2. **Totex Reconciliation Model** "Totex-Menu-2016-05-17-change-log-removed WSH.xlsx";
3. **WRFIM Model** "WRFIM-June-2018-update WSH.xlsx";
4. **Retail Reconciliation** "pap_tec20160216hhrecon WSH.xlsx"
5. **Revenue Feeder Model** "PR19PD011-Revenue-adjustments-feeder-model-01l-for-publication WSH.xlsm"
6. **RCV Feeder model** "PR19-RCV-adjustment-feeder-model-June-2018-update WSH.xlsm"; and
7. This supporting document which contains the Board Assurance Statement, independent assurance report and outlines changes to the inputs.

1.2 Background

This document provides an update for each of the PR14 reconciliation mechanisms for 2018-19 actual performance and updated forecasts of 2019-20 performance. Ofwat sets out the requirement to update all of the PR14 reconciliations with 2018-19 actual performance and update the evidence for the forecast 2019-20 performance in action WSH.PD.A6 in their initial assessment of plans.

1.3 Structure

Section 2- ODI Reconciliation- This section provides an overview of our MOS performance including any rewards and penalties.

Section 3- Totex Menu Reconciliation- This section provides an update on the totex menu reconciliation model.

Section 4- Wholesale Revenue Forecasting Incentive Mechanism- This section provides an update of the Wholesale Revenue Forecasting Incentive Mechanism (WRFIM).

Section 5- Household Retail Reconciliation- This section provides an update of the Household Retail Reconciliation.

Section 6- Water Trading- This section provides an overview of the PR14 Water Trading incentive.

Section 7- Land Disposals- This section provides an update of Land Disposals.

Section 8 Inflation Forecasts- This section provides an overview of our inflation assumptions.

Appendix A- Independent Assurance Report- This section includes the Independent Assurance report and an overview of our assurance process.

2 MOS and ODI Reconciliation

Our performance for 2015-16 to 2019-20 is measured against 31 Measures of Success (MOS). Sixteen of our MOS have Outcome Delivery Incentives (ODIs) associated with them. The ODI reconciliation calculates the rewards and penalties based on companies' actual performance over the five years from 1 April 2015. The ODI model published with the PR14 Reconciliation Rulebook has not been used following the guidance in the Water2020 Final methodology. App5, App6 and App27 have been submitted for the ODIs.

- App5 reports the actual performance for 2018-19 and forecast performance for 2019-20 for the PR14 reconciliation performance commitments.
- App6 reports the actual performance for 2018-19 and forecast performance for 2019-20 for PR14 reconciliation- sub- measures.
- App27 reports the ODI revenue and RCV adjustments for 2015-16 to 2019-20.

Difference from Early Submission

App5, App6 and App27 have been updated to reflect actual performance for 2018-19 and forecast performance for 2019-20. Table 1 shows the difference between in the revenue adjustments due to updated ODI performance.

Table 1- ODI Revenue Adjustments

	Early Submission (£m)	Updated Submission (£m)	Difference (£m)
Water Resources	-	-	-
Water Network Plus	(10.9)	(11.7)	(0.8)
Wastewater Network Plus	12.0	11.8	(0.2)
Bioresources	-	-	-
Residential Retail	-	-	-
Business Retail	-	-	-
Total Net Revenue Adjustments	1.1	0.1	(1.0)

Water Network Plus

The ODI penalty for the AMP for water network plus is from two performance commitments; A2: Customer Acceptability and A3: Interruptions to supply.

Wastewater Network Plus

The ODI reward for the AMP for wastewater network plus is from two performance commitments; B3: Preventing Pollution and D3: Internal Sewer Flooding.

Our PR14 final determination performance commitment, current and forecast performance for each of the four performance commitments is summarised in tables 2.1- 2.4. The tables also reports the calculation of the ODI reward/penalty.

Table 2.1- A2: Customer Acceptability

A2 - Customer Acceptability (Contacts per 1,000 Population)					
Forecast year	2015-16	2016-17	2017-18	2018-19	2019-20
Performance commitment level	2.54	1.89	1.23	1.23	1.23
Actual/Forecast performance level	3.08	3.2	3.19	3.28	2.64
Performance commitment level met	No	No	No	No	No
Penalty Deadband	3.2	3.2	1.23	1.23	1.23
Penalty Collar	3.4	3.4	1.43	1.43	1.43
ODI rate	£0.093m per 0.01 contacts per 1000 population (Max £1.86m in penalty or reward per annum)				
Underperformance Penalty	£0 (actual performance is better than the penalty deadband)	£0 (actual performance is better than the penalty deadband)	= 1.43 (Penalty collar) - 1.23 (Penalty Deadband) = 20 @ 0.093 = £1.8600m Maximum penalty as actual performance of 3.19 is above penalty collar)	= 1.43 (Penalty collar) - 1.23 (Penalty Deadband) = 20 @ 0.093 = £1.8600m Maximum penalty as actual performance of 3.28 is above penalty collar)	= 1.43 (Penalty collar) -1.23 (Penalty Deadband) = 20 @ 0.093 = £1.8600m Maximum penalty as forecast performance of 2.64 is above penalty collar)

Table 2.2- A3: Reliability of Supply

A3 - Reliability of Supply (Customer minutes lost)					
Forecast year	2015-16	2016-17	2017-18	2018-19	2019-20
Performance commitment level	36	24	12	12	12
Actual/Forecast performance level	21.7	12.2	43.3	16	12
Performance commitment level met	Yes	Yes	No	No	Yes
Penalty Deadband	48	48	12	12	12
Penalty Collar	68	68	32	32	32
Reward Deadband	12	12	12	12	12
Reward Cap	0	0	0	0	0
ODI rate	£0.195m per minute (Max Reward £2.34m pa "in the year". Max Penalty £3.9m pa "in the year")				
Penalty/Reward	£0	£0	= 32 (Penalty collar) - 12(Penalty Deadband) = 20 @ 0.195 = £3.9m Maximum penalty as actual performance of 43.3 is above penalty collar)	= 16 (Actual performance) - 12 (Penalty Deadband) = 4 @0.195 = £0.78m penalty	£0 (forecast performance sits at the reward and penalty deadband)

Table 2.3- B3: Preventing Pollution

B3 - Preventing Pollutions (Category 3)					
Forecast year	2015-16	2016-17	2017-18	2018-19	2019-20
Performance commitment level	161	154	131	131	131
Actual/Forecast performance level	110	111	112	118	112
Performance commitment level met	Yes	Yes	Yes	Yes	Yes
Reward Deadband	131	131	131	131	131
Reward Collar	106	106	106	106	106
ODI rate	Penalty - £0.400m per incident (Max 10m pa) Reward £0.047m per incident (Max of £1.175m pa)				
Outperformance payment	= 131 (deadband) - 110 (Actual performance) = 21 * 0.047 = £0.987m	= 131 (deadband) - 111 (Actual performance) = 20 * 0.047 = £0.94m	= 131 (deadband) - 112 (Actual performance) = 19 * 0.047 = £0.893m	= 131 (deadband) - 118 (Actual performance) = 13 * 0.047 = £0.6110m	= 131 (deadband) - 112 (forecast performance) = 19 * 0.047 = £0.8930m

Table 2.4- D3: Internal Sewer Flooding

D3 - Internal Sewer Flooding (Number of Properties)					
Forecast year	2015-16	2016-17	2017-18	2018-19	2019-20
Performance commitment level	310	300	292	282	269
Actual/Forecast performance level	223	242	221	221	222
Performance commitment level met	Yes	Yes	Yes	Yes	Yes
Reward Deadband	271	263	256	248	238
Reward Cap	232	226	221	215	207
ODI rate	Reward £0.062m per property, Penalty £0.161m per property (Average performance over two year period in order to smooth the effects of weather variability)				
Outperformance payment	£0 (No reward or Penalty applicable in the year as it is the average performance for two years)	= 263 (deadband) - (223 + 242)/2 = 233 (Actual performance) = 30 * 0.062 = £1.86m	= 256 (deadband) - (242+221)/2 = 232 (Actual performance) = 24 * 0.062 = £1.488m	= 248 (deadband) - (221 + 221)/2 = 221 (Actual performance) = 27 * 0.062 = £1.6740m	= 238 (deadband) - (222 + 221)/ 2 = 222 (Forecast performance) = 16 * 0.062 = £0.9920m

3. Total Expenditure (Totex)

The totex menu reconciliation calculates the adjustments to revenue and RCV for the next price control based on the totex performance of the company over the current price control period.

Loughor Expenditure

In line with our early submission of the PR14 reconciliation rulebook we have removed expenditure for Loughor from the total expenditure for the totex true-up model. The table below reconciles the APR expenditure and the Loughor expenditure.

The total expenditure excluded for Loughor from the APR up until 2018-19 is £41m.

Table 3.1 Loughor Totex excluded from APR published expenditure (Table 2B)

	2015-16 (£m)	2016-17 (£m)	2017-18 (£m)	2018-19 (£m)
APR Total Including Cash Items	232.4	289.3	315.8	355.7
Loughor Expenditure	-	4.3	18.2	18.8
Totex Inc Cash Items for the reconciliation rulebook	232.4	285.1	297.6	336.9

(Outturn Prices)

Updated Reconciliation Rulebook Input

The table shows the changes to the inputs from the early reconciliation rulebook submission. The changes reflect actual 2018/19 performance and updated forecasts for 2019/20.

		Updated Submission		Early Submission		Difference	
		2018/19	2019/20	2018/19	2019/20	2018/19	2019/20
Water: Actual Totex	£m	359.7	328.3	344.2	310.1	15.5	18.2
Water: Third party services (opex)	£m	6.1	9.5	9.5	9.5	(3.4)	-
Water: Third party services (capex)	£m	4.3	0.6	0.6	0.6	3.7	-
Water: Pension deficit recovery costs	£m	3.5	1.8	3.5	1.8	-	-
Water: Other cash items	£m	-	-	-	-	-	-
Water: Disallowables		-	-	-	-	-	-

		Updated Submission		Early Submission		Difference	
		2018/19	2019/20	2018/19	2019/20	2018/19	2019/20
Sewerage: Actual Totex	£m	336.8	342.6	336.9	350.3	(0.0)	(7.7)
Sewerage: Third party services (opex)	£m	0.7	0.2	0.2	0.2	0.6	-
Sewerage: Third party services (capex)	£m	0.4	0.0	0.0	0.0	0.4	-
Sewerage: Pension deficit recovery costs	£m	2.5	1.3	2.5	1.3	-	-
Sewerage: Other cash items	£m	-	-	-	-	-	-
Sewerage: Disallowables	£m	-	-	-	-	-	-

The difference between the allowed and actual totex is explained in the commentary for table 4B in the APR19.

4. Wholesale Revenue Forecasting Incentive Mechanism (WRFIM)

The Wholesale Revenue Forecasting Incentive Mechanism (WRFIM) incentivises companies to accurately forecast revenue by applying a penalty to variations that fall outside the set revenue flexibility threshold. The model also adjusts companies' allowed revenue for each year to take account of any over/under-recovery in previous years which has been returned to customers within the period. Due to the two year time-lag set out within the mechanism, the difference between the allowed revenues and recovered revenues in the final two years of AMP6 (2018-19 and 2019-20) and any resulting penalty will be applied at PR19.

The table shows the changes to the inputs from the early reconciliation rulebook submission. The changes reflect actual 2018/19 performance and updated forecasts for 2019/20.

		Updated Submission		Early Submission		Difference	
		2018/19	2019/20	2018/19	2019/20	2018/19	2019/20
Water: Unmeasured ~ household	£m	143.4	148.8	142.6	143.2	0.8	5.6
Water: Unmeasured ~ non-household	£m	2.1	2.0	2.1	2.2	-	(0.2)
Water: Measured ~ household	£m	67.7	70.5	62.3	66.0	5.4	4.5
Water: Measured ~ non-household	£m	80.6	75.1	79.8	81.5	0.8	(6.4)
Water: Third party revenue ~ household	£m	-	-	-	-	-	-
Water: Third party revenue ~ non-household	£m	7.3	6.1	7.9	8.1	(0.6)	(2.0)
Water: Revenue collected from household and non-household	£m	301.1	302.5	294.8	300.9	6.3	1.6
Water: Grants and contributions	£m	9.7	9.3	8.4	9.3	1.3	0.0
Water: Revenue recovered	£m	**310.8**	**311.8**	**303.2**	**310.3**	**7.6**	**1.6**

		Updated Submission		Early Submission		Difference	
		2018/19	2019/20	2018/19	2019/20	2018/19	2019/20
Wastewater: Unmeasured ~ household	£m	207.9	207.5	207.9	206.9	0.0	0.6
Wastewater: Unmeasured ~ non-household	£m	2.8	2.6	2.7	2.7	0.1	(0.2)
Wastewater: Measured ~ household	£m	110.0	112.3	104.4	108.0	5.6	4.3
Wastewater: Measured ~ non-household	£m	76.9	72.4	73.6	74.3	3.3	(1.8)
Wastewater: Third party revenue ~ household	£m	-	-	-	-	-	-
Wastewater: Third party revenue ~ non-household	£m	-	-	-	-	-	-
Wastewater: Revenue collected from household and non-household	£m	397.6	394.8	388.6	391.9	9.0	2.9
Wastewater: Grants and contributions	£m	7.7	9.1	8.2	9.1	(0.5)	-
Wastewater: Revenue recovered	£m	**405.2**	**403.8**	**396.8**	**401.0**	**8.5**	**2.9**

5. Retail Reconciliation

The household retail control is an average revenue control based on the efficient cost of retail activities and projected customer numbers. There is an automatic annual modification to the allowed household retail service revenue in each year of the price control to account for the difference between actual and forecast customer numbers and meter penetration. The retail reconciliation model sets out how differences in the forecast and actual customers' numbers in a given year will be reconciled. The model also reconciles any over or under recovery of household retail revenue per customer type.

Updated Reconciliation Rulebook Input

The table shows the changes to the inputs from the early reconciliation rulebook submission. The changes reflect actual 2018/19 performance and updated forecasts for 2019/20. In line with the Reconciliation Rulebook submission in July 2018 and the request from Query WSX-DD-PD-001 (sic) the forecast "Actual customer numbers" have been calculated using the latest available numbers as published in the Annual Performance Report, i.e. March 2019 actuals.

Actual revenue collected (£m)

	Updated Submission		Early Submission		Difference	
	2018/19	2019/20	2018/19	2019/20	2018/19	2019/20
Unmetered water-only customer	0.7	1.3	1.4	1.3	(0.7)	0.0
Unmetered wastewater-only customer	0.6	1.3	1.3	1.3	(0.7)	0.0
Unmetered water and wastewater customer	17.2	13.6	18.0	14.2	(0.8)	(0.6)
Metered water-only customer	0.7	1.1	1.0	1.1	(0.3)	(0.0)
Metered wastewater-only customer	2.2	2.8	2.7	2.8	(0.5)	(0.0)
Metered water and wastewater customer	27.3	21.0	21.4	21.5	5.9	(0.5)
Total Revenue	**48.7**	**41.0**	**45.9**	**42.1**	**2.8**	**(1.1)**

Revenue sacrifice (£m)

	Updated Submission		Early Submission		Difference	
	2018/19	2019/20	2018/19	2019/20	2018/19	2019/20
Unmetered water-only customer	0.1	0.1	0.1	0.1	(0.0)	(0.0)
Unmetered wastewater-only customer	0.0	0.0	0.0	0.0	(0.0)	(0.0)
Unmetered water and wastewater customer	5.6	9.8	6.1	9.4	(0.5)	0.5
Metered water-only customer	0.0	0.0	0.0	0.0	0.0	0.0
Metered wastewater-only customer	0.0	0.0	0.0	0.0	0.0	(0.0)
Metered water and wastewater customer	1.4	2.4	1.1	1.7	0.3	0.7
Total Revenue Sacrifice	**7.1**	**12.4**	**7.3**	**11.2**	**(0.2)**	**1.2**

Actual customer numbers (,000)

	Updated Submission		Early Submission		Difference	
	2018/19	2019/20	2018/19	2019/20	2018/19	2019/20
Unmetered water-only customer	52.6	51.8	52.3	51.5	0.3	0.3
Unmetered wastewater-only customer	48.7	47.1	48.6	47.0	0.0	0.0
Unmetered water and wastewater customer	662.8	652.1	666.5	655.8	(3.7)	(3.7)
Metered water-only customer	29.2	31.6	29.8	32.1	(0.6)	(0.6)
Metered wastewater-only customer	83.2	86.3	84.6	87.6	(1.4)	(1.4)
Metered water and wastewater customer	525.5	543.9	519.9	538.4	5.5	5.5
Total Customer Numbers	1,401.9	1,412.7	1,401.7	1,412.5	0.2	0.2

6. Water Trading

The water trading incentive was introduced at PR14 to encourage companies to trade water where it is beneficial to do so. We published our trading and procurement code on 25th November 2015 and it was approved by Ofwat in February 2016. We do not anticipate entering into any new trades before March 2020.

7. Land Disposal

The 2018/19 actuals are reported in table 2E of the APR and have been included in the updated submission.

Updated Reconciliation Rulebook Input

	Updated Submission		Early Submission		Difference	
	2018/19	2019/20	2018/19	2019/20	2018/19	2019/20
Water: Actual and current forecast sales (£,000)	360	100	100	100	260	-
Waste: Actual and current forecast sales (£,000)	24	100	100	100	(76)	-

8. Service Incentive Mechanism

R10- Service Incentive Mechanism of the PR19 business plan table provides actual and forecast SIM scores.

Updated Reconciliation Rulebook Input

The table shows the changes to the inputs from the early reconciliation rulebook submission. The changes reflect actual 2018/19 performance and updated forecasts for 2019/20.

	Updated Submission		Early Submission		Difference	
	2018/19	2019/20	2018/19	2019/20	2018/19	2019/20
Qualitative performance						
1st survey score	4.5	4.6	4.5	4.6	-	-
2nd survey score	4.4	4.5	4.5	4.6	(0.1)	(0.1)
3rd survey score	4.6	4.6	4.6	4.7	(0.1)	(0.1)
4th survey score	4.7	4.8	4.5	4.5	0.2	0.2
Qualitative SIM score (out of 75)	66.6	67.6	66.6	67.6	-	-
Quantitative performance						
Quantitative composite score	94.5	93.1	85.1	84.5	9.4	8.5
Quantitative SIM score (out of 25)	20.3	20.3	20.7	20.8	(0.5)	(0.4)

9. Inflation Forecasts

Table App23 includes our forecast of the Retail Price Index (RPI) and the Consumer Price Index including housing (CPIH). Table 10.1 outlines our inflation assumptions.

Table 10.1- Inflation forecasts

	2019-20	2021-22 onwards	Long Term
RPI annual increase	3.0%	3.0%	3.0%
CPIH annual increase	2.3%	2.0%	2.0%

Appendix Assurance process and independent assurance report

The flowchart below shows the process undertaken for production and assurance of the submission.

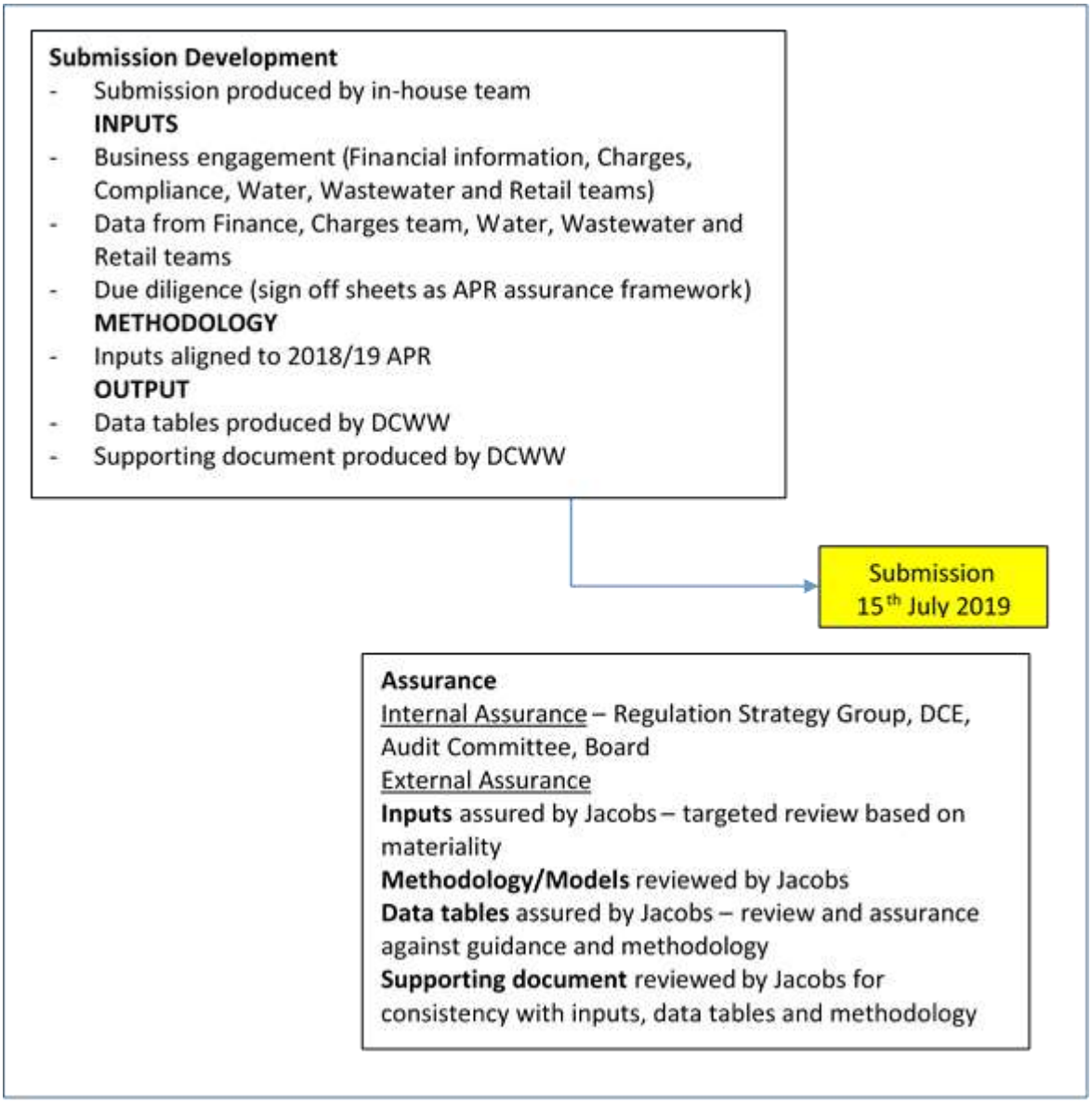

Figure A-1 Flowchart of process for production and assurance of the PR14 Reconciliation rulebook

There is a statement from the Board setting out the factors and the assurance information they considered in support of the PR14 Reconciliation rulebook.

An independent review and assurance of the submission was undertaken by Jacobs reflecting the targeted assurance requirements. Jacobs were asked to review, in particular:

- The data used for PR14 Reconciliation rulebook
- The use of the PR14 Reconciliation rulebook models
- Output of the feeder models for the PR19 Business Plan Tables

The report from Jacobs is included below.

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25 June 2019

Attention: The Board
DCWW
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Road Nelson
Treharris
Mid Glamorgan
CF46 6LY

Project Name: Dŵr Cymru Welsh Water (DCWW) non-financial assurance
Project Number: B2271301

Subject: Price Review 2014 PR14 reconciliation - assurance letter

To the Board

DCWW has been promoted to self-assured status by Ofwat through its recent Company Monitoring Framework assessment. We are pleased your good work on assurance has been recognised and earned you this promotion. We look forward to continuing to work with you to retain the trust and confidence of your customers and stakeholders and to maintain and further enhance your assurance status.

Part of the 2019 Price Review (PR19) will be the calculation of adjustments to take account of AMP6 performance and incentive mechanisms. This is particularly important given the potential materiality of the adjustments and the fact that the way adjustments are calculated can be complex and open to different possible interpretations.

Ofwat has produced the Price Review 2014 (PR14) reconciliation rulebook which describes the way that it will reconcile companies' 2015-2020 performance against the PR14 Final Determinations at PR19, through the following mechanisms:

- Outcome Delivery Incentives (ODIs), which provide companies with rewards for achieving stretching performance targets and compensate customers if performance is below performance targets;
- Wholesale Total Expenditure (Totex) sharing, where company over- and underperformance is shared with customers;
- Wholesale Revenue Forecasting Incentive Mechanism (WRFIM), which provides financial incentives for companies to provide accurate forecasts, and ensures under- and over-recovery is reconciled;
- PR14 Service Incentive Mechanism (SIM);
- Household retail, where the total revenue allowance is adjusted for actual customer numbers;
- Land sales, where the company shares the proceeds with customers.

In July 2018, prior to your initial Business Plan submission, you engaged us to conduct a risk-based review of your submissions relating to the Reconciliation Rule Book – Feeder Models. Our assurance focused on your interpretation of the guidance for the PR14 reconciliation rulebook and subsequent application via the feeder

models. The risks identified do not reflect the robustness of the data relating to actual costs that input to the feeder models as these are subject to separate assurance.

Our review included the aggregated Totex forecasts for 2018/19 and 2019/20 that input to the feeder models. We also reviewed performance for 2018/19 and forecasts for 2019/20, and the calculation of ODI rewards and penalties.

On 13th July 2018, we provided a letter summarising the outcome of that assurance. We also provided your team with detailed feedback that explained our assessment of the risk associated with the reported data and set out any actions. When reviewing your models, our risk-based sampling approach assessed the completeness, reliability and accuracy of the data and your interpretation of the process. We found no material issues.

Subsequently, Ofwat has required companies to resubmit the PR14 reconciliation to capture companies' actual data for 2018-19 and its impact on the 2019-20 forecasts. Companies must submit this data at the same time as the 2018-19 APR submission. Consequently, you asked us to assure your revised data and how the outputs of the feeder models provide data required for Ofwat's financial model and any relevant PR19 tables. Further detail on our approach is set out in Appendix A.

Observations

We note that during our reviews relating to the use of actual 2018-19 data and the 2019-20 forecasts we identified a limited number of instances, where the latest/final data had not been flushed through all of its relevant models and tables. During the audit on 15th May 2019, your team updated the models to ensure the final data was being used and this was completed during the audit.

Recommendations

We did not identify any recommendations for improvement.

Conclusions

Overall, for the Reconciliation Rule Book – Feeder Models we consider:

- your team has good understanding of the data required to populate the feeder models, in line, where appropriate, with other PR19 tables;
- your team has good understanding of your processes required to populate the feeder models, in line with Ofwat guidance; and,
- your team has good understanding of how the outputs of the feeder models provide data required for the Ofwat financial model and any relevant PR19 tables.

Yours sincerely

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Appendix A. Summary of assessment framework

As we note in the letter above, our assurance approach focuses on the level of risk associated with the data/forecast. The result of our approach is a score of A, B, C or D for each PR19 table, line or group of lines. In assessing your data, we used a standard scoring framework to produce results that are comparable across the measures. Table A.1 below summarises this framework.

Table A.1 Summary of scoring framework for the data stage of our assurance approach

Score	Meaning
A	Low risk – no weaknesses in production of data/forecast
B	Low to medium risk - no material weaknesses in production of data/forecast
C	Medium to high risk - material weakness (or number of minor ones with material effect)
D	High risk – multiple material weaknesses or data missing/not provided

Table A.2 Scores for the PR14 reconciliation models and business plan data tables we reviewed

Tables and line descriptions	Data score
PR14 reconciliation models and associated PR19 tables	B
We note that during our reviews we identified a limited number of instances, where the latest data had not been flushed through all its relevant models and tables. This was corrected during the face to face audit 15th May 2019.	