Dŵr Cymru Cyfyngedig

Accounting Separation Methodology Statement

2013-14

Dŵr Cymru
Welsh Water

Overview

Each company must produce and publish an accounting separation methodology statement as part of its regulatory accounts submission. The purpose of this statement is to enable Ofwat and other stakeholders to understand the systems, processes and allocation methodologies used to populate the accounting separation tables.

This paper sets out the methodology adopted by Dŵr Cymru Cyfyngedig (DC) for the production, as required under RAG 3.07 of the operating and fixed asset analysis, within the regulatory accounts (proforma A7 to A10) and the supplementary accounting separation statements, as required under RAG 4.04. Ofwat during 2013-14 have issued further disclosure requirements to include in the methodology statement for 2013-14 so as to improve the usefulness and comparability of the data for users. In addition to this, further guidance was issued by Ofwat called 'Accounting Separation guidance clarification' which provides clarification for companies on the treatment of certain costs in the preparation of the 2013-14 regulatory accounts. This methodology statement and the regulatory accounts have been prepared in accordance with the requirements set out in these documents.

Background to the business

Business structure

DC is a 'not-for-profit' company which has been owned by Glas Cymru since 2001. Glas Cymru does not have shareholders, and any financial surpluses are reinvested in the business for the benefit of customers. DC is the group's principal trading company. Its principal activity is the supply of water and treatment and disposal of wastewater under the instrument of Appointment made by the Secretary of State for Wales under the Water Act 1989.

Dŵr Cymru Customer Services Limited (DCCS), another subsidiary of Glas Cymru, commenced trading in August 2012. Its principal activity is the provision of income collection and billing services to DC, which was previously outsourced.

Structure underlying core customer services activity

The structure is as follows:

- DCCS was set up as a subsidiary of Glas Cymru and commenced trading in August 2012. Its principal activity is the provision of income collection and billing services to DC, which was previously outsourced;
- DC has outsourced arrangements with local authorities and water companies for billing and collection;
- DC operates an operational call centre that takes all the operational calls which are then forwarded to schedulers to schedule in the first customer call (all these costs are included in retail).
    - For calls relating to the water network, inspectors go out and visit the site to see whether this is a network issue and if so will forward on the jobs to a team within DC. Once work has been completed the customer is contacted to advise that the issue has been resolved. The costs within retail include the inspector's time if the fault was not a network issue and the costs of the customer liaison team who call the customer advising that the issue has been resolved.

- For calls relating to the waste network, a team is sent out so that if this is a network issue it can be resolved as soon as possible. If, when attending the site, they find that this is not a network issue then the call is aborted. The costs included in retail relate to the costs of the aborted visits; also in retail are costs of the customer liaison teams who call the customer advising that the issue has been resolved.

- DC has inspectors who attend customer premises in relation to a billing query on their meters. The costs included in retail relate to the visits the inspector has made in relation to the following activities which are undertaken following a customer's request: final meter reading; check meter reading; customer billing meter query; meter reading work - abortive; determine property supplied by meter and site meeting to show location of meter. The latter two relate to billing and customer – facing activities hence we have treated them as retail costs;
- Support costs: all of DCCS costs are allocated to retail, along with a proportion of support costs which are incurred by DC. DC support costs are allocated to retail based on various costs drivers, as shown in Appendix 3;
- Other business activities include Ofwat fees, Water UK costs and regulation department costs. 1/9th of the costs have been allocated to retail by splitting the costs between business activities. The split between household and non household is based on customer numbers;

Related overheads included as direct costs or general and support costs

Our interpretation is that direct costs relate to employment costs, power, hire and contracted services, materials, EA service charges and other direct costs. All overheads are included as general and support costs rather than direct costs with the exception of 5% support costs that have been allocated to scientific services. However this is not shown within direct costs as per our interpretation above.

Outsourced arrangements:

DC has the following outsourced arrangements

Outsourced provider	Function	2013/14 status
Local authorities and water Companies	Billing and collection services	Remains outsourced
IT support DC[1]	IT support	Remains outsourced
IT support DCCS[2]	IT support	Remains outsourced
Appcon Consultancy Services	Payroll, payments and SAP access and authorisations service	Remains outsourced
Cost consultancy	Cost consultancy for capital programme	Remains outsourced

[1] 17% of the contract for IT support DC is carried out overseas
[2] 13% of contract for IT support DCCS is carried out overseas

Commentary

Significant changes in the company's costs in the year

Changes of costs compared to 2013 with commentary are included in Appendix 1 for wholesale and Appendix 2 for retail.

Details of the company's processes and systems and any changes year on year

Systems and structures

DC is split into three reporting areas: - Managing Director, Finance and Operations. Each one of these areas is headed up by a Board Director of the Company. The two primary business units which are included in Operations are water and waste water services. These are headed up by a Director of water and waste water respectively.

The finance team is set up to provide dedicated support to the operational and support teams that they look after. Every month management accounts are prepared which show variances against budget; these accounts are interrogated by the finance department and the budget holder to identify reasons for the movement and to highlight any costs that need to be transferred as they have not been charged to the correct area. Every month the head of department will hold a meeting to discuss performance which includes cost performance against budget. On a quarterly basis performance against budget is discussed at a senior level to understand all variances.
There is no change to this process from last year.

Sources of data and systems in place

Systems

- DC and DCCS use SAP as an integrated financial and business management system. SAP information is either downloaded into spreadsheets or extracted using Business Warehouse.
- The current customer accounting system (CAS) has successfully operated for 25 years; however it is now nearing the end of its life in terms of the technical platform it operates on, its ease of use for users and the increasing risks of maintaining this key legacy system into future years. DC will be ensuring this major change is managed carefully to ensure the transition to a new system is a smooth one and will not detrimentally impact our customers' experience of dealing with our business. After a comprehensive procurement process in 2012, DC selected Echo Managed Services' system, RapidXtra, to replace the current system. The Rapid system is a water billing system which currently operates successfully in a number of UK water companies. Our strategy has been to utilise as much of the existing tried and tested functionality the system offers as possible, in order to reduce implementation risk. Our users have recently commenced a comprehensive training programme, and we are pleased with the positive feedback from our staff. The delivery of our new system is planned for November 2014.
- In 2012 we upgraded our debt collection system, Tallyman, to version 3. Although a technical upgrade, moving to version 3 also provided us with greater functionality that will support our collection strategies in AMP6. Specifically it provides a platform to develop automated litigation

processes, greater variability in customer segmentation and interface with third parties to support data sharing.

- Electricity costs are allocated to assets via DC's electricity management system (ARIES) which receives electronic power bills from the energy providers and ,by reference to the supply point, charges the cost to the asset's cost centre via an interface with SAP. ARIES also records consumption and, based on historical data, generates accruals when actual bills are not received. Each Water and Sewerage service asset has a unique supply point allowing the actual power costs to be charged directly to the asset and its associated activity.
- SAP work management systems, such as Above Ground Asset (AGA) Water, Mechanical, Electrical and Instrument (ME&I) Planned Maintenance and Switch (below ground asset maintenance). The systems recognise which asset is being worked on, its geographical location and the type of work performed. Based on this information the system charges costs to predetermined revenue or capital cost collectors.

Process

- An alternate cost centre structure is used that aligns with Ofwat's accounting separation requirements. These contain specific cost centre groups for each of the business activities along with further groups capturing the cost of scientific services and general and support activities. This cost centre structure enables the costs to be collected in the same format as the tables.
- A number of 'work management systems' have been introduced in recent years resulting in greater accuracy of cost allocation and a reduced reliance of manual allocations across activities.
- The majority of our costs are coded at source. This includes payroll costs, purchase orders, service orders and power.
- An alternate cost element group is also used that reflects the requirements with the key cost element groups:
    - Employment costs
    - Power
    - Materials
    - Hired and bought-in services
    - Insurance
    - EA charges
    - Bad debt
    - Rates
    - General and support
- Each department is required to complete a table in the same format as the accounting separation tables. Where possible costs are allocated direct to service. For support service departments the costs that can be directly attributed will be shown against those business activities while the remaining costs will be allocated using the most appropriate cost driver, as shown in Appendix 5.
- DCCS (provider of income collection and billing services to DC) submits costs in the same format as the accounting separation tables and this facilitates consolidation of costs.

Governance procedures

DC has established appropriate processes and systems of control that provide assurance in respect of information contained within the regulatory accounting tables (which previously formed part of the 'June Return').

These systems have ISO9001:2008 accreditation and are reaffirmed by SGS Ltd as part of the company-wide IMS procedures rolling programme of audits. The company is now in its seventh year of holding this accreditation.

The company has documented key processes and internal controls and has assessed the quality of systems and processes used for generating regulatory information. These processes have been followed to produce this year's Performance Report.

Ownership and responsibility for each supplementary table have been clearly defined. Each individual is responsible for adhering to all appropriate guidance in the compilation of the data and associated commentary. This also involved formal 'sign-off' by the individual, verifying that the figures in each line had been obtained from a recognised data source and have been accurately compiled. In addition, confirmation was required that any material judgements or assumptions had been highlighted and documented, ensuring an accurate audit trail.

Allocation of overall responsibility for individual tables and associated commentaries was assigned to the appropriate DC senior manager. Each was responsible for the review and 'sign-off' of his/her own tables and commentaries.

A rigorous process of internal due diligence meetings was undertaken by the Regulation Department between 13 May and 30 May 2014 to challenge information, judgements and assumptions made and to ensure compliance with the relevant guidance.

Capitalisation policy

Costs charged to capital follow the company's accounting policy. This states that capital expenditure includes the following categories of cost:

- Property, plant and equipment;
- Infrastructure assets (being mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls); and
- Other assets (including properties, overground operational structures and equipment, and fixtures and fittings).

Asset additions are recorded at cost together with any expenditure directly attributable to bringing the asset into use, including directly attributable internal costs.

The cost of property plant and equipment additions includes an accrual for incentive bonuses earned to date, relating to projects substantially completed at the year-end where the likelihood of making the incentive payment is considered probable. Amounts recoverable from contract partners relating to targets not being achieved are only recognised on completion of a project.

For accounting purposes, the water and waste water system is segmented into components representing categories of asset classes with similar characteristics and asset lives.

In accordance with RD 06/02, all leakage monitoring and reporting costs are treated as operating expenditure. The cost of maintaining leakage is also classified as such, unless it clearly falls in other areas e.g. replacement of capital items. The costs of detection and repairs in reducing leakage as initiatives to achieve the economic level of leakage are treated as capital expenditure.

Additions are recorded at cost, which reflects the purchase price together with any expenditure directly attributable to bringing the asset into use, including directly-attributable internal costs. Costs incurred on development projects are recognised as intangible assets when the relevant recognition criteria are met.

Capitalisation of salaries

The cost of employees working directly on capital projects is calculated using an hourly recharge rate which is reviewed by management annually. Each set of rates is broken down by bands based on average salary and includes national insurance, superannuation, bonus payments, overtime, car allowances, personal protective equipment, mobile phone and training costs.

A planned maintenance system integrated in SAP records mechanical and electrical maintenance, labour, materials and bought-in services costs at asset level. Craftsman time is recorded on handheld devices (“Toughbooks”) and job-types determine the classification of work as operating or capital expenditure.

Integrated work scheduling and cost systems record work scheduled on the system and allocate this to process operators and network teams via handheld devices. Details of time spent and materials used are allocated to jobs via these handheld devices. The final status of a job determines whether it is operating or capital expenditure (using the predefined settlement tables held within SAP).

Capitalisation of overheads

DC’s internal costs incurred in supporting the capital programme are capitalised as overheads using an appropriate recovery rate. The recovery rate is based on a review to identify costs which demonstrate a clear link to the capital programme. The assumptions and recovery rate used are reviewed every six months by the finance team.

Additional analysis or adjustment that the company made to the data from its systems

Fixed assets overview

Additions

The principal data source for the fixed assets tables is taken from our capital expenditure regulatory reporting database which is extracted from SAP. This information source provides sufficient information to directly allocate most costs to the accounting separation business units.

The regulatory reporting and accounting separation databases hold scheme information analysed by asset types. For the purposes of completing the regulatory accounts, they also identify whether the assets are 'infrastructure' or 'non infrastructure' and separately categorise 'retail assets'.

- Infrastructure assets include the following: underground systems of mains and sewers, impounding and pumped raw storage reservoirs, dams, sludge pipelines and sea outfalls. Some Information about infrastructure assets (general mapping and updating of networks records) is also regarded as an infrastructure asset.
- Operational assets include the following: intake works, pumping stations, treatment works, boreholes, operational land, offices, depots, workshops, residential properties directly connected with water and sewerage services. Land which is not currently in operational use but is expected to come in to use in the foreseeable future is included, as is plant, machinery and telemetry inherent in the nature of the works. Also included are non- operational plant, non-operational machinery, vehicles, surplus land and all other assets not previously listed.
- Retail operational assets include the following: buildings and offices, fixtures and fittings, IT systems and other operational assets directly involved in providing the retail service.

New expenditure incurred during the year is added to the base and is analysed as follows. Costs are recorded at a scheme level and are allocated to business type based on an analysis of the scheme design and target costs. This is the same principle for allocation of capital expenditure to business units that has been used for the preceding three years. The aim has been to map as much of the expenditure incurred on a one-to-one relationship, minimising the amount of subjective allocation. The analysis of each scheme is allocated to an eight digit coding structure based on the table structure of the former June return table (Table 32).

On the assumption that Quality, Base, Enhancement and Growth (QBEG) analysis continues to be a requirement, the asset categories are further extended to allow for the four possible descriptions of asset purpose. For the purpose of our systems, the above translates to an assets classification list of eight digit codes. The eight digit classification code comprises five pieces of data, which translate into the following information about the cost.

Example 0906Q13S

First two digits denote asset type and follows Table 32 line items

- 09 = Sewerage treatment works

Third and Fourth digits denote Infrastructure or Non-infrastructure depending upon whether asset relates to water or sewerage

- 01 = Infrastructure – water
- 02 = Non-infrastructure - water
- 05 = Infrastructure - sewerage
- 06 = Non-infrastructure - sewerage

The Fifth digit denotes the purpose

- M = Base/Maintenance
- E = Enhanced service Level

- N = New Development
- G = Growth
- Q = Quality

Fifth to Eighth denotes purpose type drivers

- Q13S = Habitats driver

The database queries use the data contained in the classification code to sort and group the year-end figures to allow grouping by asset type columns and QBEG classification as necessary. Some 90 per cent of expenditure in the year was suitable for this classification method. The remaining 10 per cent is for items of IT and management and general cost that cannot be directly allocated to a specific business unit. This expenditure has been proportionally allocated across the business activities by total programme costs.

Asset lives

ChandlerKBS have provided an asset life assessment service to DC for the past 20 years. The assessments are based on DC's accounting policy in relation to asset lives. Whist undertaking this service, ChandlerKBS has maintained a record of each individual assessment. The assessments are compiled on a regular basis into an overall summary database. The database can then be used to produce generic asset life assessment models where details of individual projects are not known.

For 2014, the following models were produced using the database. Each model relates to a specific project type as follows.

	Sample Size	**Sample Value**
Water Treatment Works	8 Projects	£71m
Waste Water Treatment Works	200 Projects	£191m
Combined Sewer Overflows (CSO) and Untreated Intermittent Discharges (UID)	225 Projects	£409m
Habitats Projects	19 Projects	£19m
Water Ultra Violet Treatment (UV) projects	12 Projects	£12m

ChandlerKBS also produce asset life assessments for several other water and sewerage companies. Using this knowledge and experience, the above models were checked and reviewed to ensure that they were consistent across the industry in general. They were then used to produce the generic fixed asset life assessments for 221 projects with a total value of £36m. This was used as the basis to calculate depreciation for additions in the year

Revaluation

For the PR14 submission the asset stock was revalued at 31st March 2013 and we have used this updated information to populate table A10. For the revaluation the PR09 MEAV was used as the base and then updated for:

- physical additions and subtractions from the asset base
- changes in construction costs
- data improvements for assets on the corporate system that were:

- not registered previously and have been identified during asset surveys.
- were recorded at a different level of granularity than previously identified.

Changes to the net valuation have occurred for the above reasons and because of a change in the assessed age profile of the asset base. Additionally the asset stock was categorised into the accounting separation business activities areas.

The updated model:

- does not include assets that are currently under construction
- private sewers
- includes assets that are now on corporate systems as a result of data improvements

Private sewers and assets under construction have been added to the revalued GMEAV in the fixed asset tables.

Infrastructure assets make up more than 75% of the total MEAV and we have revalued these using UCD8 cost equations to reflect changes to construction costs that have occurred since PR09. In turn, we have then made adjustments to account for additions and subtractions to the asset base using the total length of assets currently recorded.

For non -infrastructure assets, adjustments have been made for additions and subtractions from the physical asset base and we have then adjusted the total value using the Construction Output Price Index (COPI) to reflect changes to construction costs that have occurred since the PR09 valuation. The net value has been updated by adjusting the base year in the MEAV model from 2009.

Changes to methodology compared to 2012-13 and planned improvement

Changes to the methodology

We have restated the asset base using the valuations that were used for the PR14 business plan submission. This has resulted in an AMP adjustment of £1,563m credit.

We have changed the basis of allocation of some of the retail-wholesale costs to adopt the cost drivers reported in the guidance document "Chapter 21b Regulatory accounts Current cost accounting" where we feel that this is more appropriate. The changes in cost allocation relates to using FTE instead of direct costs and employment costs .These changes are not significant and amount to £50k.The cost driver used in 2013-14 is shown in Appendix 3.

The cost drivers for some general and support activities have also changed where we have used FTE instead of direct employment costs. These changes are not significant. Appendix 5 shows the cost drivers used for 2013-14.

The cost drivers for some household: non household activities have also changed and this shown in appendix 6.

We have not restated 2012-13 using the revised allocations as the prior year tables are not required to be disclosed in the regulatory accounts. Therefore there is no requirement to restate these values.

Details of other changes

- Sampling at customer taps – following IN 13/10 sampling of drinking water at customers taps is now reported as a wholesale activity.
- Network customer enquiries and complaints - in 2013 the costs reported as network customer enquiries and complaints included operational call centre (unchanged) and aborted calls (unchanged). As a result of the recent accounting separation guidance clarification document additional costs are shown as retail as follows:-
- scheduling jobs where they are triggered by a customer call (transfer from retail to wholesale);
    - For waste services there are specific teams set up who carry out this task. This was not included in retail previously as our interpretation of the guidance was that the 'scheduling' of calls related only to passing the calls on to the network, but as a result of the additional clarification by Ofwat we recognise that the costs of scheduling the initial call with the customer needs to be included within retail and are now reporting as such.
    - For water the costs relate to scheduling the initial jobs with the customer where they are triggered by a customer call. There are carried out by a centralised team in Cardiff as well as employees at the regional depots. For these employees, each manager has provided an estimated time taken to schedule the initial call after this has been passed to them by the operational call centre following a customer contact. This was not included in retail previously as our interpretation of the guidance was that the 'scheduling' of calls only related to passing the calls on to the network, but as a result of the additional clarification by Ofwat, we recognise that the costs of scheduling the initial call with the customer need to be included within retail and are now reporting as such.
- visiting the customer to investigate the problem where it is found that it is not a network issue;and
    - This relates to inspectors visiting the customer to establish whether the problem is a network issue. A list of these visits was extracted from SAP and then filtered by cause types which showed whether the job was a network issue. Time taken for these 'non-network' visits was calculated using a standard job hourly rate (which was prepared in December 2013) and a standard hourly rate. This has been included in retail following the additional clarification issued by Ofwat which states that costs of inspectors' time should be included in retail where it is found not to be a network issue.
- calls to customer to enable the customer call to be resolved
    - This relates to the 'close the loop' and customer liaison officers contacting the customer after work has been completed to enable the customer call to be resolved. This was previously included as wholesale costs, but as a result of the guidance clarification and discussions with the business these costs are now included as retail.
- Disconnections- the requirements state that it is only the decision and administration that should be included in retail. The actual cost of the physical disconnection should be included in wholesale. In 2013 physical disconnections costs were reported in retail and this has been corrected for 2014.

Planned improvements

Replacement of billing system

We are in the process of implementing our new billing system 'RapidXTra' which is a largely preconfigured system, and is designed specifically for the water sector. The reason for the change is that our current billing system, CAS, is not sufficiently flexible for the future, the skills to support it are becoming increasingly hard to source and the mainframe technology it sits on is expensive to run. The new system will be an enabler for our retail 'cost to serve' and competition challenges through opening up further opportunities for automation (through integration with our telephony system for example), customer self-service and multiskilling of staff. The main benefits of the new system are:

- Staff will be able to focus better on what customers are telling them as the system is easier to use;
- Currently CAS requires employees to update a number of screens during and after a call, while RapidXtra leads the member of staff through a process and has a series of in-built 'drop down' lists with mandatory fields to be completed. This will ultimately lead to fewer staff errors as it is easier to use;
- Improvement to our current consolidated bill service for non- household customers in that we will be able to make electronic billing available to household and non-household customers at 'go live' – something that we have tried but failed to deliver through CAS;
- We will be able to introduce other developments so as to enhance services to customers and will include web based 'my account' functionality with live integration to our systems, allowing customers to check their balances, update their own meter reading and change their payment option; and
- Improve ability to classify customer contacts as resolved or unresolved through coding that sits behind the classification attributed by our employees. This will facilitate and simplify the process of gathering regulatory information and generating reports.

Other changes

While there are no other planned changes to be looked at in the coming year, the accounting separation process is reviewed on an ongoing basis, making changes and improvements as required to ensure that we comply with the principles as set out in RAG 4.04. Any changes in treatment of costs will be disclosed in the commentary.

How the company has applied the principles set out in RAG 4.04

RAG 4.04 covers the form, content and principles of the analysis of operating costs and assets to be produced as part of the current cost accounts, and includes a list of definitions of terms.
The objective of the guideline is to facilitate:

- transparency and comparability of costs across the water and sewerage value chain;
- informed regulatory decisions; and
- demonstrate costs and assets employed in providing water and sewerage services.

The guidelines states that the cost allocation principles need to comply with the following general principles (in order of priority):

- **Transparency**: the attribution methods applied within the accounting separation 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.

- Alternative cost centre structures have been created (as part of DC's overall accounting separation cost centre group) in SAP in a format that facilitates the completion of accounting separation tables. These contain specific cost centre groups for the business activities along with further groups capturing the cost of scientific services and general and support activities. A number of 'work management systems' have been introduced in recent years resulting in greater accuracy of cost allocation and a reduced reliance on manual allocations across activities. Asset-related cost centres and most operational support staff can be attributed directly to a business activity. Non-operational staff costs are allocated directly to activities where possible; where this has not been possible cost drivers have been used to apportion departmental costs in line with Ofwat's previous hierarchy of cost drivers.
- Each business area have to submit their costs in the accounting separation format and forward to the Regulatory Accountant for consolidation. The consolidated spreadsheet details the costs for each business area which can be traced back to SAP. As part of the submission to the Regulatory accountant an analysis is required for all costs that have changed significantly from previous year.
- The costs drivers used are shown in the following appendices:
  - Retail – wholesale split — Appendix 3
  - Retail – household: non household split — Appendix 6
  - Wholesale cost allocation — Appendix 4
  - General and support allocation — Appendix 5

- **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 a level as possible.
  - In respect of costs that are directly attributable to a business activity are allocated to these activities.
  - Any costs that are not directly attributable then the most appropriate cost drivers are used relating to that specific cost.
- **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.
  - We do not have any internal transfer charges
- **Objectivity**: the cost and revenue attribution criteria need to be objective and should not intend to benefit any business unit or service.
  - The allocation methods that we have used are not intended to benefit any business unit or service and have been applied objectively
- **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.
  - We aim to be as consistent as possible however, if we believe that there is another cost driver that is more appropriate then we will use this and will include our rationale for the change in the methodology statement

Billing and collection

- DC has outsourced arrangements with local authorities and water companies for billing and collection.
  - Local authorities and registered social landlords:
    DC has two types of agreement:
    - Under the terms of the "old-style" arrangements the third party bears the risk of bad debts above the agreed level of commission. This amounts to 3% of total income in 2013/14.
    - Under newer arrangements DC bears the bad debt risk. This amounts to 1% of total income in 2013/14.
  - Water companies:
    - DC has agreements with Severn Trent, United Utilities and Dee Valley to collect on its behalf. This amounts to 5% of total income in 2013/14. DC bears all collection risks.

In all cases, income is shown gross (excluding any void element), with commission and bad debt elements reported separately.

- DC issues bills to 'the occupier' for metered customers only if we see consumption on the meter and cannot get a name at the time. Very few premises are billed in this way and no bills are sent out speculatively in this manner, only where there is evidence suggesting an actual occupier (e.g. a visit, finance check or Land Registry search). We are unable to provide the turnover and consequently the doubtful debt for income billed in the name of the occupier at this time without uploading and reconfiguring the 2013-14 data to extract this information, however the value is not significant (considerably less than 1% of turnover). We are in the process of changing our billing system and we have been advised that this information will be readily available in future periods.
- DC's policy on treatment of bad debt is to write off debt when it is shown that a debt is not collectible. A debt is regarded as not being collectible when one of the following conditions has been satisfied:
  - the debtor has been declared bankrupt;
  - the debtor cannot be traced;
  - the debtor has died without an estate;
  - all reasonable legal remedies have been exhausted and two collection agencies have failed to recover the debt; or
  - the debt is too small to pursue beyond specified recovery action.

- All debt that has completed the full recovery process is held in an "end of line bucket" pending write-off. Write offs are scheduled as part of a routine procedure however initiatives continue to be undertaken in respect of the "end of line" debt to review collectability and debts are currently only written off post completion of these initiatives. Generally when debt reaches the "end of line bucket" the majority will have been provided for in the bad debt provision. As a result the timing of the write-offs has little impact on the overall charge for bad debts in any year. As a consequence, the level of write-offs throughout the year is not monitored in isolation but as a component of the overall movement in collections as part of the bad debt provision calculation. DC believes it is important to look at the overall trend in collections when determining bad debt provisioning rates rather than reacting to isolated write-offs. No changes have been made to the write off policy or procedure during the year. We are unable at this time to quantify the value of any charges cancelled or credited in a year against live and leaver debt. Once a leaver has followed our debt collection route the amount is written off.

Cost allocation

Disclosure requirements

The disclosure requirements issued by Ofwat have asked for the following items to be disclosed within the methodology statement:

Explanation of how costs have been allocated for each line of the table

- Where costs explicitly relate to a specific business unit, the expenditure has been coded directly to the business unit that consumed the good or the service. Where direct coding is not possible, an appropriate allocation has been made using specific cost drivers. In most cases these cost drivers are applied consistently.
  - The retail and wholesale cost allocation table (appendix 3) provides explanation of how operating costs have been allocated to retail for each line of the table.
  - Retail household: non household table (appendix6) provides detail of cost drivers used to allocate costs
  - Wholesale cost allocation is included in appendix 4.
  - General and support costs allocation is included in appendix 5.

Why these allocations are considered appropriate

- We consider that the allocations are appropriate as we have used , in most cases , the cost drivers mentioned in the accounting separation guidance documents issued in January 2011 for:
  - Chapter 21a Regulatory Accounts Current Cost accounting Water Services
  - Chapter 21b Regulatory Accounts Current Cost accounting Retail Services
  - Chapter 22a Regulatory Accounts Current Cost accounting Waste Services

  Other costs drivers are used if we feel that this is more appropriate. Where we have previously used other cost drivers, we have changed the allocation so that we are using the preferred cost drivers as set out in the above guidance documents. This will ensure a consistent approach in the industry and will make the reports more comparable.
- A higher proportion of employment costs is being allocated directly to business units, however some costs are cycled using assessment cycles. In the majority of cases these are cycled to the same business unit, however there is a small amount that is transferred to other business activities. These cost assessment cycles are monitored on a regular basis, and a thorough review of these takes place every six months.
- We have discussed the accounting separation guidance clarification document with the business to ensure that we are adhering to the guidance with regard to network customer enquiries and complaints. We have used reports from SAP which shows the split of household and non-household contacts and have used this for allocation. For inspectors' non network visits, we have devised a

report that shows the cause code for the jobs after the inspector has attended the premises. This is used to determine the costs for the visits that are not network related.

- We have confirmed that the customer numbers that we are using in the household/ non-household split is in line with the definition set out in the accounting separation clarification guidance.
- Where management judgment has been used we have examined the rationale used to ensure that it looks reasonable.
- In allocating the bad debt charge (households 91%: non- households 9%) we have undertaken the following sampling:
    - We have calculated the movement in “true” debt for each household and non-household account, as reported by EXIS (in-house legacy system reporting capability). It excludes accounts billed through other companies, trade effluent billing and scheduled accounts. It also excludes the impact of any occupation changes between Annual Billing (7 February 2014) and the end of the year.
    - The movement for each account was calculated as follows:
        - Debt at 01/04/13
        - Add billing during the year
        - Deduct payments during the year
        - Deduct debt outstanding at 31/03/14
        - The overall movement for each price control is used as the basis for allocation of the bad debt charge.

How the company’s management is satisfied that they are reasonable

- In the main the cost driver are applied on a consistent basis, however where there have been changes this is discussed with the relevant department to ensure that this is reasonable. Any changes are disclosed in the methodology statement.
- Managers are rewarded on their performance which includes financial performance. Monthly reports are produced by the finance team which they and the budget manager interrogate to highlight any cost variances and to identify any costs that should not be included in that area. This will include any cost assessment cycles that they do not recognise. Any costs that should not be included within this area will be transferred out. Therefore, due to this rigorous system management is satisfied that the costs are being reported in the correct area.
- For the retail / wholesale split and household/ non-household split the finance team at DCCS have to agree that the costs being transferred from wholesale to retail by DC and the cost drivers used for household/ non household are reasonable

The breakdown of the cost categories and values that is included within other direct costs.

Other operating expenditure as reported in the Accounting Separation tables consists of the following cost elements:-

- Employment costs
- Hired and bought-in services
- Materials and consumables
- **Other Direct cost**
- General and support

- Scientific Services
- Other business activities

The disclosure requirement asks for details of the breakdown of the cost categories and values that the company has included within Other Direct cost. This is shown below:-

	Water					Sewerage					
Other Direct cost	Resources	Raw water distribution	Treatment	Treated distribution		Sewage collection	Sewage treatment	Sludge treatment	Sludge disposal		
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Insurance costs	**0.4**	**0.1**	**0.7**	**0.7**	**1.9**	**0.7**	**0.8**	**0.3**	**0.1**	**1.9**	**3.8**
customer side leaks (funded by wholesale)	-	-	-	1.1	1.1	-	-	-	-	-	1.1
Customer compensation payments	-	-	-	0.3	0.3	-	-	-	-	-	0.3
Other Direct costs 13/14	**0.4**	**0.1**	**0.7**	**2.1**	**3.3**	**0.7**	**0.8**	**0.3**	**0.1**	**1.9**	**5.2**

Within retail activities other direct costs relate to the following:

	Household	Non household	Total
	£m	£m	£m
Customer services - DC team	1.0	0.1	1.1
Pension actuarial costs	(1.6)	(0.3)	(1.9)
Total	(0.6)	(0.2)	(0.8)

The customer services team within DC carries out the following activities: managing online services for across all electronic channels, (Website, Web chat, eContact, eforms, emails and text messaging) as well as social media channels such as Facebook, Twitter, Linkedin and YouTube; ensuring defined governance processes for all channels are followed and the business understands how change can be initiated and managed moving forward. In addition to this they arrange the customer focus groups. These costs have always been included in other direct costs.

Pension actuarial accounting credit (FRS17 and IAS19 adjustments) is included within other direct costs for retail (which differs from the treatment in wholesale). The reason for this is that this credit can be easily identified in retail.

Local authority rates allocated to retail

The local authority rates that have been included within the retail table relate to the offices occupied by DCCS staff and the staff working on network customer and enquiries. There has been a detailed measurement of the office space at Linea and the split is based on the floor space occupied by those

working on retail activities. In addition to this there are some retail employees working in the other offices and the rates have been allocated using direct labour as the cost driver. These costs are shown in table A8 as Local authority rates.
There are no cumulo rates allocated to retail.

There are no costs reported as exceptional items

Analysis of assets allocated to the retail table

The analysis of the assets allocated to retail is as follows:

Retail assets	Billing system	Other assets specifically allocated to the retail table	Shared assets allocated to the retail table	Total
Net book value	£m	£m	£m	£m
At 31 March 2014	**17.8**	**5.2**	**13.2**	**36.2**
household	15.2	4.8	13.2	**33.2**
non household	2.6	0.4	-	**3.0**
Depreciation charge	**0.8**	**0.9**	**0.3**	**2.0**
household	0.7	0.6	0.3	1.6
non-household	0.1	0.3	-	0.4

Other assets include telephony assets, Demand side water efficiency schemes, and other IT systems specifically allocated to retail.
Shared assets include a proportion of the property costs where the Customer services department is located. Floor space occupied is the cost driver that was used to allocate these costs .
Other shared assets are IT additions and these have been allocated based on headcount.

£8.9m of assets were reclassified as retail assets in 2013-14 which were previously included in wholesale activities. These are as follows:

	£m
Billing system replacement costs included within wholesale in 2012-13	4.1
Billing and income contract extention (tallysman etc) included in wholesale	3.7
IT enhancements not previously allocated to retail	1.1
Reclassification of assets	8.9

Customer numbers is the cost driver used to split depreciation between household and non household for retail assets apart from demand side water efficiency schemes which is allocated according to type of scheme.

The method or cost driver that the company has used to allocate shared assets between its wholesale and retail business units

- The assets that are directly allocated or shared between wholesale and retail is as follows:
  - Linea – this is where predominantly DCCS and those carrying out network customer and complaints activity is based. The split is based on square footage occupied.
  - Billing – all to retail.
  - Telephony- retail telephony identified and allocated accordingly.

- Demand side water efficiency – specific schemes identified and included as retail.
- Other IT schemes – these relate to specific IT schemes relating to retail together with IT enhancements of the system (including SAP) that have been split to retail based on FTE.

A breakdown of the recharges the company paid to and received from other business units for the use of fixed assets

There have been no recharges paid to or from other business units for the use of fixed assets. The only recharges are for facilities and insurance recharges. All assets used for retail activities are allocated directly to retail.

Whether the company maintains a CCA register, the extent to which it is reconciled to the HCA fixed asset register and the methodology or assumptions undertaken to compile CCA data.

We do not maintain a CCA register or reconcile this to the HCA fixed asset register.
We use the additions that are reported for HCA and adjust for IRE. The reconciliation is as follows:

	£m
Fixed asset additions (excluding income) per Historic Costs	353
IRE expenditure (excluding income)	(99)
Current Cost additions	**254**
	£m
Water	111
Waste	126
Retail	17
Current cost additions	**254**

The Current Costs tables are prepared as follows:

Opening balances - Gross Replacement cost and depreciation

- The opening balances were carried forward from the accounting separation tables submitted in 2013.

AMP adjustment

- For PR14 the asset base was revalued. This adjustment in gross replacement section relates to the difference between the PR14 GMEAV and the brought forward gross replacement cost. The AMP adjustment is reported as £(3,060)m: water £(1,459)m and sewerage £(1,601)m. For private sewers this is revalued every year based on RAG1.10.9 and the AMP adjustment relating to this is reported as £(164)m
- The AMP adjustment for depreciation is the difference between the opening depreciation and the depreciation derived from the PR14 revaluation (opening depreciation from the PR14 revaluation is calculated as GMEAV less NMEAV).

RPI adjustment for gross replacement cost and depreciation

- This has been calculated by applying the inflation to the opening balances and the AMP adjustment above to reflect 13/14 prices.

Additions

- As in previous years, fixed asset additions are allocated across business areas using the project coding structure. Assets that do not fall into the Accounting Separation categories are firstly coded to service areas (water or waste) and then further allocated to the Accounting Separation areas on a percentage uplift basis.

Disposals

- The disposals reported in the year relate to maintenance expenditure included within infrastructure additions, which, it is judged, do not enhance the intrinsic replacement value of the asset derived for the MEAV.

Charge for year

- We have used the CCD charge included in the MEAV valuation which shows for each class of asset the depreciation based on the remaining asset life using NMEAV.
- For additions in the year the charge is calculated by splitting the spend into asset life categories by applying the asset lives % as calculated by Chandler KBS.

Reclassification adjustments

- We have reclassified some retail assets as they were previously included in wholesale. This amounts to £9m which is shown in the table above.

For each row within the retail table, the cost driver the company has used to allocate costs between its household and non-household customers

- The table in appendix 6 shows the cost drivers used to allocate costs between household and non household customers

Operating expenditure

Operating expenditure (excluding Capital maintenance and third party services) have decreased by only 1%.

Total operating costs (which include capital maintenance) have increased by 4% since last year; water services have remained in line with last year and waste services increased by 9%.

The movements compared to last year are as follows:

Year on year comparison of costs	Water	Waste	Total	Water	Waste	Total
	£m	£m	£m	%	%	%
Operating expenditure						
Power	2.3	1.2	3.5	14%	5%	9%
Income treated as negative expenditure	(0.0)	(0.1)	(0.2)	30%	6%	8%
Service charges	0.4	0.0	0.5	4%	1%	3%
Bulk supply imports	(0.1)	0.0	(0.1)	(7%)	-	(7%)
Other operating expenditure	(1.8)	(3.6)	(5.4)	(3%)	(5%)	(4%)
Local authority rates	(0.2)	0.0	(0.2)	(1%)	0%	(1%)
Total operating expenditure excluding third party services	**0.5**	**(2.4)**	**(1.9)**	**0%**	**(2%)**	**(1%)**
Capital maintenance						
Infrastructure renewals charge	1.5	0.7	2.3	4%	2%	3%
Current cost depreciation	2.9	19.4	22.3	5%	26%	17%
Amortisation of deferred credits	0.0	(0.0)	(0.0)	0%	6%	3%
Total capital maintenance excluding third party services	**4.4**	**20.1**	**24.5**	**5%**	**19%**	**12%**
Third party services						
Operating expenditure	(3.3)	0.0	(3.3)	(28%)	-	(28%)
Infrastructure renewals charge	(0.6)	0.0	(0.6)	(52%)	-	(52%)
Current cost depreciation	0.0	0.0	0.0	1%	-	1%
Total operating costs	**1.0**	**17.7**	**18.7**	**0%**	**9%**	**4%**

Cost movement	Water	Waste	Total
	£m	£m	£m
Pension actuarial charge	(5.9)	(4.2)	(10.2)
Third party costs	(3.3)	0.0	(3.3)
Transport maintenance reclassified as depreciation	(0.9)	(1.4)	(2.3)
Insurance	(0.7)	(0.6)	(1.3)
Network customer enquires and complaints	(0.5)	(0.8)	(1.3)
Sampling costs	(0.3)	0.2	(0.1)
Customer compensation	0.3	0.0	0.3
IT costs	0.6	(0.2)	0.4
Sampling at customer taps	0.4	0.0	0.4
Facilities increase	0.2	0.4	0.6
Employer superannuation increases	0.5	0.4	0.9
Private sewers	0.0	1.0	1.0
Customer side leaks	1.2	0.0	1.2
Increase in leakage activity and inclement weather costs	2.4	(0.0)	2.4
Bonus payments	1.5	1.1	2.6

Dŵr Cymru Cyfyngedig

Appendix 1

Operating Cost Analysis for the 12 month ended 31 March 2014 (wholesale business)

Power	2.3	1.2	3.5
Infrastructure Renewals charge	0.9	0.7	1.7
Current cost depreciation	2.9	19.4	22.3
Others	(0.6)	0.5	(0.1)
Total operating cost movement	**1.0**	**17.7**	**18.7**

Movements compared to last year are as follows:-

- Pension actuarial movement in the year as a result of the IAS19 and FRS17 adjustment .
- Third party opex costs lower compared to last year. The Competition Appeal Tribunal costs have decreased which consists of costs and damages. These costs have been split equally between water resources and raw water distribution. This has been offset by increased rates recharged to the Environment Agency in relation to the reservoir agreements and increase in operating costs for non potable supplies mainly relating to increase in power.
- Higher proportion of transport maintenance costs being included as depreciation as a result of replacing the older fully written down fleet.
- Insurance costs have decreased in the year reflecting lower uninsured loss provision following a review of all the outstanding claims.
- Network customer enquiries and complaints costs included as retail activity in 2013-14, following the clarification document issued by Ofwat. This cost was previously included in wholesale and relates to costs of schedulers and customer liaison officers as well as costs of visits where it was found not to be a network issue.
- Sampling costs reflect a saving in total over wholesale activities reflecting the insourcing saving. Movement between water and sewerage activities reflect that in 2012-13 costs were included as raw water distribution and are now reported in treated water distribution and sewage treatment.
- Customer compensation relating to wholesale activities was previously included in retail. This has been amended for 2013-14.
- IT costs have increased. The movement between services reflect that costs are allocated on a headcount basis (in 2012-13 direct labour costs were used to apportion costs) and on equipment supported. The increase reflects increase in licence costs offset by increase in costs transferred to retail to support those employees that are working on the network enquiries and complaints area.
- Sampling at Customer taps . This was previously included as retail activity but after IN 13/10 is now reported as wholesale activity and is shown within treated water distribution
- Facilities increase reflects lower capitalisation, less allocated to retail activities and increase in facilities costs.
- Increase in employers' contribution reflecting auto enrolment and increase in Defined Benefit scheme contributions.
- Private sewers increase relates to increased activity compared to last year
- Customer side leaks included within treated water distribution. This was previously reported as non appointed. We have changed the treatment of these costs in line with Ofwat guidance.
- Increase in leakage activity and inclement weather costs have increased costs which relate to treated water distribution.
- Bonus payments increased due primarily to salary inflation and insourcing.

- Power has increased in total by 9% and this reflects the following movements:
    - 14% increase in water services .Consumption for water increased by 4% with power price increase of 10%.
    - 5% increase in sewerage services. The increase in Sewage treatment reflects the higher power price 11% compared to last year) offset with lower consumption (7%)
- Infrastructure renewals charge has increased which includes third party services. The increase in water reflects higher charge in water resources in the year offset by lower treated water distribution costs. In sewerage areas this all relates to sewerage collection. Infrastructure renewals charge for third parties have decreased compared to last year as there was a misallocation in previous years which has since been corrected.
- Current Cost Depreciation has increased reflecting that the MEAV values prepared for PR14 were used to update the gross and net replacement costs. As part of the MEAV exercise, current costs forecast were prepared for each class of assets taking into account the age of the asset stock, expected life and condition of the assets .A Current Cost Depreciation forecast was prepared up to 2030 based on this information. By using this forecast, current cost depreciation within water has remained stable. Within services, however, there are movements as the revaluation has allocated the assets into the correct accounting separation areas, whereas previously this was based on management's judgement. Current cost depreciation within sewerage activities have increased which mainly relates to sewage treatment. This increase relates to the CCD forecast prepared as part of the MEAV revaluation which takes into account the age and condition of the asset.

Dŵr Cymru Cyfyngedig
Appendix 2
Operating Cost Analysis for the 12 month ended 31 March 2014 (retail business only)

Operating expenditure

Total operating expenditure excluding third party services has increased since last year by 4% . Household costs have increased by 4% and non household costs are in line with last year. The split between household and non households have also changed from 89%:11% to 90%:10% which is mainly due to the change in allocation of bad debt.

The increase in costs has arisen because bad debt , customer service activity and debt management costs have increased offset by a reduction in other operating expenditure .

Year on year comparison of costs	Household	Non household	Total	Household	Non household	Total
Operating expenditure	£m	£m	£m	%	%	%
Customer services	1.8	0.5	2.3	21%	71%	24%
Debt management	0.7	0.1	0.8	12%	42%	13%
Doubtful debts	2.0	(0.9)	1.1	8%	(27%)	4%
Meter reading	(0.2)	0.1	(0.1)	(10%)	31%	(5%)
Services to developers	0.0	(0.1)	(0.1)	-	(49%)	(49%)
Other operating expenditure	(2.1)	0.3	(1.9)	(19%)	22%	(15%)
Local authority rates	(0.0)	0.0	0.0	(%)	19%	2%
Total operating expenditure	**2.1**	**(0.0)**	**2.1**	**4%**	**-**	**4%**
Capital maintenance						
Current cost depreciation	1.0	0.4	1.4	184%	1002%	236%
Total capital maintenance	**1.0**	**0.4**	**1.4**	**181%**	**992%**	**233%**
Total operating costs movements	**3.1**	**0.4**	**3.5**	**6%**	**6%**	**6%**

Movements compared to last year are as follows:-

- Network customer enquiries and complaints, within customer services have increased. This reflects a change in our treatment of costs following the clarification notice issued by Ofwat. As a result costs of schedulers , customer 'close the loop' teams and costs for customer visits where it was found not to be a network issue are included in retail.
- Debt management costs have increased reflecting the increase in cost of external debt collection agency commission. In addition the key customer team which was reported previously in 2012-13 as admin costs is now in Debt management.
- Doubtful debts are 4% higher than last year which is due to the continued recession in Wales. As well as the increase in charge since last year , the bad debt split has also changed from the previous H:NH split of 87%:13% to 91%:9% . This has meant that the amount included within household has increased with a corresponding decrease in non households. In allocating the bad debt charge we have undertaken the following sampling on all debtors' accounts excluding accounts billed through other companies and local authorities, trade effluent billing and scheduled accounts. It also excludes

the impact of any occupation changes between Annual Billing (7th February 2014) and the end of the year.

The movement for each account was calculated as follows:

- Debt at 01/04/13
- Add billing during the year
- Deduct payments during the year
- Deduct debt outstanding at 31/03/14

The overall movement for each price control was used as the basis for allocation of the bad debt charge. The effect of this is that the household: non household split amounts to 91%:9%.

This is different to the approach taken during 2013 where the bad debt split was prepared by taking the split of outstanding debt greater than one year. The split between household: non household as a result came to 87%:13%.

- Meter reading costs are similar to last year although the allocation of costs has changed between household and non household. The reason for this movement is that the household: non household cost driver has changed to use number of meter as reported in table 7 of the June return. This cost driver is the one included in table 21b as Ofwat's preferred cost driver.
- Services to developers (all reported as non-household) have reduced reflecting lower activity.
- Other operating expenditure has decreased:
  - Pension actuarial charge due to the IAS19 and FRS17 accounting adjustment.
  - Wholesale compensation payments previously reported as retail but now shown in wholesale.
  - Customer side leaks relate to the cost of repairing leaks on the customer's side of the stop-tap that have originated from a request by the customer. We allocated all costs to household in 2012-13, however for this report year we were able to extract the job type information from SAP and the household: non household split came to 85%:15%.
  - Facilities costs have decreased as we had not taken into account the direct recharge to DCCS in 2012-13 and therefore had double counted this charge last year.
  - Scientific services have decreased - costs of sampling at customer taps which were previously reported as retail activities are now shown as wholesale following IN13/10 guidance.
  - General and support costs have increased of which the majority relates to IT costs. This reflects the IT support cost for the employees that were previously classed as wholesale together with the IT support for the operational call centre.
  - Other Business activities relate to the cost of the Economic Regulation department, the Ofwat licence fee, Water UK. And the economic regulation team. These costs are allocated equally across 9 business units (4 for water services, 4 for sewerage services, and 1 for retail services, which is split

equally between household and non-household). The increase in the year reflects increase in Ofwat fees and economic team activity.

- Communication costs have increased reflecting the increased team and higher retail activity.

- Capital maintenance costs have increased in the year. These costs reflect the current cost depreciation charge for the year and are consistent with the retail fixed asset table in the regulatory accounts. The reason for the increase in depreciation relates to demand side water efficiency schemes included in depreciation and being fully written off in the year; depreciation on the replacement billing system and increase in depreciation in telephony. The depreciation has been split between household and non household using customer numbers.

Appendix 3 Retail- wholesale cost allocation

	Cost driver used 2013-14
Customer Services	
Billing	Wholly in retail
Payment handling and remittance	Wholly in retail
Non - Network customer enquiries and complaints	Wholly in retail
Network customer enquiries and complaints	
Dwr Cymru Operational call centre	Wholly in retail
Dwr Cymru Waste	
Scheduling jobs	Team within waste who schedule the first job after they have been triggered by a customer call
Aborted jobs	Report from SAP to show cost of all aborted jobs as a result of customer contact
Call to customer for call to be resolved	Direct allocation as unique cost centre for this team
Dwr Cymru Water	
Scheduling jobs	Managers estimate of time spent on scheduling the intial job after a customer contact.
Inspectors first visit	Number of jobs depatched from OAC that require visit and then filtered by cause types to establish the costs of non network visits
Call to customer for call to be resolved	Managers estimate of time spent on calling customer to advise that work has been completed
Other customer services	
Debt management	
Dwr Cymru Customer Services Ltd	Wholly in retail
Dwr Cymru Council Commissions	Wholly in retail
Customer doubtful debt	
Local authority bad debt	Wholly in retail
Dwr Cymru doubtful debt	Wholly in retail
Meter reading	
Dwr Cymru Customer Services Ltd	Wholly in retail
Dwr Cymru water inspectors	Customer liaison for meter queries - extracted all the jobs that the inspector went out to visit following a customer contact which related to a billing query
Other operating costs	
Disconnections and reconnections	Decision and administration costs only
Demand- side water efficiency initiatives	
Dwr Cymru Customer Services Ltd	Wholly in retail
Dwr Cymru water efficiency	Wholly in retail
Customer side leaks	
jobs raised after customer call	Type of jobs raised as result of a customer contact
Other direct costs	
Dwr Cymru Customer Services	Wholly in retail (apart from some compensation payments)
Dwr Cymru insurance costs	Recharged direct to DCCS
Dwr Cymru Actuarial costs	Scheme numbers
General and support expenditure	
IT costs	
Dwr Cymru Customer Services Ltd	Wholly in retail
Dwr Cymru IT dept	Allocated using headcount , number of computers and system type
Motor vehicle costs	Wholly in retail
Finance	
Dwr Cymru Customer Services Ltd	Wholly in retail
Dwr Cymru Finance	FTE
Dwr Cymru Audit fees	FTE
Dwr Cymru income and tarriff team	Wholly in retail
HR	
Dwr Cymru Customer Services Ltd	Wholly in retail
Dwr Cymru HR	FTE
Executive team	
Dwr Cymru MD and FD	FTE
Dwr Cymru - Co Sec	FTE
general management	
Dwr Cymru Customer Services Ltd	Wholly in retail
Facilities	
Dwr Cymru Customer Services Ltd	Wholly in retail
Dwr Cymru	Floor space and FTE
Other general and support costs	
Dwr Cymru Customer Services Ltd	
Meter reading	Wholly in retail
Training and quality	Wholly in retail
Web	Wholly in retail
Business change	Wholly in retail
compliance	Wholly in retail
Key and business customers	Wholly in retail
Dwr Cymru	
Finance business customer	included in DCCS charge
Communication team directly allocated	Directly allocated due to type of spend and management allocation of time spent for employment cost
Comminication team indirect costs	FTE
Quality and assurance	Management time spent on audit work
Health and safety	FTE
Tax and capital markets	FTE
Finance planning	FTE
Scientific Services	No costs in retail following IN 13/10
Other business activities (regulation costs)	1/9th to retail
Developers services	Cost apportionment by manager
Local Authority rates	
Local Authority rates	Floor space

Appendix 4: Wholesale cost allocation

Allocation bases

cost Driver A- direct costs can be mapped directly from a cost centre to the relevant Accounting separation business unit.

Cost Driver B-In cases where the mapping is not direct but a specific cost driver is used to allocated the cost to the Appropriate Accounting separation business unit

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

	Resource (Water Processes)	Raw Water Distribution	Treatment (Water Processes)	Water Distribution (Networks)	Sewerage	Sewage Treatment	Sludge Treatment	Sludge Disposal
	£m	£m	£m	£m	£m	£m	£m	£m
Power	A/B	A/B	A/B	A/B	A/B	A/B	A/B	
	This cost includes all energy costs (including climatechange levy costs) and income from energy generation .The cost consists of electricity costs £38.9m, income received £2.1m, gas £0.5m and climate change levy £3.1m. Electricity costs are allocated to assets via DC's electricity management system (ARIES) which receives electronic power bills from the energy providers and by reference to the supply point, charges the cost to the asset's cost centre via an interface with SAP.Each Water and Sewerage service asset has a unique supply point allowing the actual power costs to be charged directly to the asset and its associated activity. Where a supply point provides power for more than one activity,(e.g a sewage treatment works which also contains a sludge treatment facility) sub-meter data is used where possible. Where sub-meter data is not available, the amount attributable to each activity is determined by reference to the location of equipment, the output of that item, it's frequency of use and the pumping head involved.							
EA Service Charges	A	-	A	-	A	A	-	-
	Abstraction charge received from the Environment Agency is allocated to water resources. Discharge consent payments to the Environmental Agency are supported by a site-by-site breakdown and this is used to allocate the cost to the appropriate activities and processes.							
Bulk Supply Imports	A	-	-	A	-	-	-	-
	Bulk supply imports relate to the purchase of potable water and non-potable water . The non-potable element is allocated to water resources. The potable element is allocated to water distribution.							
Other operating expenditure								
Emploment costs	A/B	A/B	A/B	A/B	A/B	A/B	A/B	A/B
	Following the introduction of the above SAP work management systems, the majority of operational staff's workload and the related allocation of cost is automated. As a consequence, the need for manual allocations of people's time is minimised. Furthermore, many operational staff and their associated cost centres can be attributed to one particular activity and instances of staff working across more than one activity are relatively low. For example, Water Distribution employees rarely work on Water Resources, Raw Water Distribution or Water Treatment assets., while Water Treatment operatives rarely carry out any work within Water Distribution. The situation is similar within the sewage business, where sewerage operatives, rarely work on sewage treatment and sludge treatment activites. Managers' estimates are used to allocate any under or over-recoveries in operatives' home cost centres. In 2013/14, £27.0m of water services operational labour costs were allocated across opex and capex activities. This comprised £13.8m of work management systems allocations, £1.6m of authorised timesheet allocations, and £11.6m of labour costs allocated on the basis of managers' estimates. £7.2m of the managers estimated transfers were to opex, of which £0.4m (or 1.6% of total allocated salaries) was allocated outside of the home cost centre's activity. Like wise for waste :In 2013/14, £18.5m of waste services operational labour costs were allocated across opex and capex activities. This comprised £13.6m of work management systems allocations, £1.9m of authorised timesheet allocations, and £3m of labour costs allocated on the basis of managers' estimates. £1.2m of the managers estimated transfers were to opex, of which £0.3m (or 2% of total allocated salaries) was allocated outside of the home cost centre's activity. Non-operational staff generally support one activity. Where they support more than one activity, their costs are allocated on the basis of staff costs or managers' estimates.							
Hired and Contracted Services	A	A	A	A	A	A	A	A
	Hire and contracted services are charged directly to business units by procurers who are generally dedicated to that activity. Where the costs relate to Switch, AGA or ME&I generated work, they are charged directly to a works order which is a unique cost collector for a specific job. These works orders settle costs to the cost centres or capital internal orders associated with the asset, job type and location.							
Chemicals	A	A	A	A	A	A	A	A
	Chemicals are charged directly to assets and activities by procurers who are generally dedicated to those activities. Where the costs relate to Switch, AGA or ME&I generated work, they are charged directly to a works order which is a unique cost collector for a specific job. These works orders settle to the cost centres or capital internal orders associated with the asset, job type and location.							
Materials & Consumeables	A	A	A	A	A	A	A	A
	Materials and consumables are charged directly to assets and activities by procurers who are generally dedicated to those activities. Where the costs relate to Switch, AGA or ME&I generated work, they are charged directly to a works order which is a unique cost collector for a specific job. These works orders settle to the cost centres or capital internal orders associated with the asset, job type and location.							
Other	C	C	C	C	C	C	C	C
	Other costs include insurance costs £3.9m, customer side leaks funded by wholesale £1.1m and customer compensation payments relating to wholesale activities. Insurance costs have been allocated over business activities using direct cost in line with the treatment last year. Customer side leaks (£1.1m) and customer compensation (£0.3m) have all been allocated to water distribution as this is directly attributable. In 2013 Customer side leaks was treated as non appointed activity , however following Ofwat's risk and compliance feedback in which it is mentioned that customer side leaks is a wholesale activity we are now treating customerside leaks as a wholesale cost. Compensation payments relate to payments to customer for water distribution activity issues .							
General and support expenditure	C	C	C	C	C	C	C	C
	The cost allocation for General and support is shown in Appendix 5							
Scientific services	B	B	B	B	B	B	B	B
	The laboratory services costs are allocated across the various activities on the basis of volume of samples. The cost of taking samples at the customer tap (£491k in 2012/13) is included in wholesale in accordance with Ofwat's information notice IN 13/10.							
Other business activities	B	B	B	B	B	B	B	B
	This includes the cost of regulation, including all incremental managerial costs of regulation associated with a periodic review, licence fees payable to Ofwat in respect of regulation, certification fees associated with the Licence requirements and staff and associated costs incurred in the preparation of submissions to, and liaison with, regulators.Costs are allocated equally across nine activities (four for water services, four for sewerage services and one for retail services. In 2013 these costs were split over 10 business units with retail being classed as two.However we have changed the allocation following Ofwat's Accounting Separation guidance clarification and allocated the costs over nine areas							
Local Authority rates	B	B	B	B	B	A/B	B	B
	This relates to the cost of local authority rates and includes both local authority rates and cumulo rates Cumulo (water-only) rates are allocated across activities in proportion to the gross MEA value of assets assigned to the business. Cumulo rates associated with the Environment Agency operating agreement are charged to third party services. Non-domestic rates relating to sewerage sites are allocated primarily to the sewage treatment activity. Where there is a sludge treatment activity at a sewage treatment site, a percentage (based on direct employment costs) is charged to the sludge treatment activity. Non-domestic rates relating to offices are allocated to activities where possible. Where this is not possible, the costs are allocated to activities on the basis of employment costs or floor space.							
Infrastructure renewals charge (excludin	B	B	B	B	B	B		
	This infrastructure charge is taken from Table 33 which we still prepare as part of the June return process. This amounts to £69.5m charge in the year -£39.3m water and £30.3m sewerage. If we take out third party costs the remaining charge amounts to £69m (£39m water and £30m sewerage).This methodology has not changed from last year and is consistent with the previous June return guidance.For Accounting separation,the water and waste costs are allocated to the seperate business activities on the basis of the IRE spend							
Current cost depreciation	B	B	B	B	B	B	B	B
	Current cost depreciation has increased by £30.3m from £126.3m for wholesale activities to £156.6m in 13/14.The reason for this is that we have restated the fixed asset costs to reflect the revised MEAV valuation that was carried out for PR14. The depreciation has been calculated on the MEAV reavalued assets for 2012/13 and the additions in 2013/14.							
Amortisation of deferred credits	B	B	B	B	B	B	B	B
	The allocation across activities is based on the current cost depreciation figures quoted in the analysis of fixed assets, This treatment is consistent with last year.							
Third party services - opex	C	C	C	C				
	Third party services includes costs associated with the supply of non-potable water, the supply of standpipes, ships water, bulk supply and reservoir agreements. Rechargeable works are treated as non appointed costs							
Third party services - current cost depre				A				
	The costs are calculated by taking the CCD figures for Raw and treated water distribution, as quoted in analysis of fixed assets (Water) table, reducing it by the CCD value of short life assets and applying the percentage associated with non-potable. The non-potable percentage is calculated by comparing the MEA values from the 2009 revaluation exercise for DCWW assets, less short life assets, and the MEA values from revaluation exercise for non pots pipelines and asset values, less the CCD associated with impounding reservoirs which is transferred to IRE.This treatment is consistent with last year,							
Third party services - infrastructure rene			A	A	-	-	-	-
	The costs are calculated by taking the Infrastructure renewals charge and applying the percentage associated with non-potable. The non-potable percentage is calculated by comparing the MEA values from 2009 revaluation exercise for DCWW assets, less short life assets, and the MEA values from revaluation exercise for non pots pipelines and asset values, plus the CCD associated with impounding reservoirs which is transferred to IRE. This treatment is consistent with last year.							

Appendix 5: General and support		13/14 basis of allocation				
Department	**Directly attributed**	**direct to business units**	**Apportioned**	**Apportionment basis**	**G & S included in wholesale**	**G & S included in retail**
Managing Director	11%	Any costs directy attributed have gone direct to the relevant business activity	89%	Water UK costs and PR14 Financing costs are included in other business activities and are allocated over each business activity equally with retail counting as one business unit. The remaining costs are apportioned on the basis FTE.	70%	30%
Company Secretary	0%	no costs directly attributable	100%	Regulatory Compliance team are included in other business activities and are allocated over each business activity equally with retail counting as one business unit.The remaining costs between wholesale and retails are apportioned on the basis of FTE.	79%	21%
Human Resources department -DC	2%	Training costs directly attributable to waste or waste water business activities	98%	wholesale: retail split based on FTE. Wholesale business activity split based on headcount.	93%	7%
Quality & Assurance department	0%	no costs directly attributable	100%	Managers allocation based on nature of work	95%	5%
Communications department excluding Education	57%	Communication team allocated to retail by going through each line of spend to identify retail costs	43%	For the remaining costs, wholesale: retail split is based on FTE. For those costs apportioned to wholesale this is further split between business activities based on headcount.	34%	66%
Education department	-	Cost captured in unique cost centre which is shown as non appointed	-	All non appointed	-	-
Environment department	59%	Costs allocated direct to waste and waste water. For allocation between business units managers assessment is used based on nature of work that that have carried out in the year.	41%	For the remaining costs , managers allocation of time spent within wholesale activities only. No retail activity.	100%	0%
Waste Water	73%	All wholesale activites no retail activity . These costs have been directly allocated to business units	27%	Business efficiency team;head of waste ;planning and scheduling team and Sludge disposal G & S are allocated to other business activities based on direct costs and management judgement	100%	0%
Energy Manager	0%		100%	Allocated on basis of direct power costs to wholesale activities	100%	0%
Finance Director	0%		100%	Costs apportioned between wholesale and retail based on FTE . Allocated to wholesale business activities based on heacount.	79%	21%
Finance Business Services department	-	Transferred to DCCS	-	Transferred to DCCS	-	-
Income & Billing- DC	100%	All these costs are allocated to retail	0%		0%	100%
Finance treasury, tax & capital markets department	0%		100%	Costs apportioned beween wholesale and retail based on FTE . Allocated to wholesale business activities based on heacount.	93%	7%
Financial Accounting Department excluding Income Accounting department & Audit Fees	0%		100%	Costs apportioned beween wholesale and retail based on FTE . Allocated to wholesale business activities based on heacount.	93%	7%
DC income accounting	100%	All these costs are allocated to retail	-		0%	100%
DCCS IT costs	100%	All these costs are allocated to retail	-		0%	100%
DCCS motor vehicle costs	100%	All these costs are allocated to retail	-		0%	100%
DCCS finance	100%	All these costs are allocated to retail	-		0%	100%
DCCS HR	100%	All these costs are allocated to retail	-		0%	100%
DCCS general management	100%	All these costs are allocated to retail	-		0%	100%
DCCS facilities	100%	All these costs are allocated to retail	-		0%	100%
DCCS other general and support	100%	All these costs are allocated to retail	-		0%	100%
Financial Accounting Audit Fees	0%		100%	Costs apportioned beween wholesale and retail based on FTE . Allocated to wholesale business activities based on heacount.	93%	7%
Planning & Regulation Director	0%		100%	Costs apportioned beween wholesale and retail based on FTE . Allocated to wholesale business activities based on heacount.	93%	7%
Legal Services - DC	61%	All costs relate to wholesale activities as DCCS has own legal department. These costs that have been directly attributed relate to employment costs for those working on water or waste water activities .	39%	Costs apportioned based on direct costs	100%	0%
Insurance costs	0%	Insurance costs relating to retail are recharged to DCCS	100%	The insurance costs included in general and support is based on total insurance costs * total cost of general and support in proportion to total costs for wholesale activities. This is further allocated to business units based on total cost of that unit in proportion to total cost	100%	0%
Operations IT costs	0%		100%	Apportionement method used to allocate to water , waste and retail is dependant on the nature of the spend and varies from headcount , no of laptops and headcount within specific offices. Allocation to business activites within water , waste and retail based on headcount . Allocation of support service IT costs included in the split	90%	10%
Operations director	0%		100%	Costs apportioned to beween wholesale and retail based on FTE . Allocated to wholesale business activities based on heacount.	100%	0%
Health & Safety	0%		100%	Costs apportioned to beween wholesale and retail based on FTE . Allocated to wholesale business activities based on heacount.	93%	7%
Operations...New Developements	0%		100%	Managers allocation.	100%	0%
Water services	84%		16%	The following costs within DC's water department are apportioned over different business units as follows: general and support allocated over wholesale business units based on managers assessments;production costs allocated over direct costs of the water department;water assets costs allocated over water activities based on the work carried out in different areas ; ops control costs allocated using managers assessment	100%	0%
Procurement & Commercial	0%		100%	Costs allocated to wholesale only and apportioned using hired and BIS costs	100%	0%
Facilities & Property	0%		100%	Costs apportioned using analysis provided by the Facilities team identifying the numbers of people, by department, at each non-operational site. Facilities costs for DC are recharged directly to DCCS. Other Facility costs included in retail relate to employees employed by DC who carry out retail activities.	89%	11%
	30%		70%		79%	21%

Appendix 6: household:non household split	Cost driver used for Regulatory 2014 Accounts H:NH split	H : NH split	
		H	NH
Customer services		%	%
Billing		93%	7%
Dwr Cymru Customer Services Ltd	Customer numbers	92%	8%
Dwr Cymru Council Commissions	Customer base relating to Council Commission	96%	4%
Payment handling and remittance		92%	8%
Dwr Cymru Customer Services Ltd	Customer numbers	92%	8%
Vulnerable customer schemes			
Non - Network customer enquiries and complaints		92%	8%
Dwr Cymru Customer Services Ltd	Customer numbers	92%	8%
Network customer enquiries and complaints		84%	16%
Dwr Cymru Operational call centre	Based on call data (in 2012-13 this was allocated using management judgement resulting in H91%:NH 9%)	83%	17%
Dwr Cymru Waste			
Schedulers	Volume and type of network customer enquiries passed to scheduler	85%	15%
Aborted jobs	Based on call data (in 2012-13 this was allocated using management judgement resulting in H91%:NH 9%)	85%	15%
Call to customer for call to be resolved	Volume and type of network customer enquiries passed to scheduler	85%	15%
Dwr Cymru Water			
Scheduling jobs	Volume and type of network customer enquiries passed to scheduler	83%	17%
Investigation of problem	This is based on actual Household: Non household activity	83%	17%
Call to customer for call to be resolved	Volume and type of network customer enquiries passed to scheduler	83%	17%
Debt management		94%	6%
Dwr Cymru Customer Services Ltd	Household and non household debt outstanding data from table 6a of June return ((in 2012-13 this was allocated using customer numbers resulting in H92%:NH 8%)	90%	10%
Dwr Cymru Council Commissions	Customer base relating to Council Commission	98%	2%
Customer doubtful debt		91%	9%
Local authority bad debt	All household	100%	0%
Dwr Cymru doubtful debt	Customer numbers based on a sample of customers . Methodology applied is included in the methodology statement (in 2012-13 this was allocated using Debt >1 year resulting in H 87%:NH 13%)	91%	9%
Meter reading		83%	17%
Dwr Cymru Customer Services Ltd	Number of metered customers (in 2012-13 this was allocated using customer numbers resulting in H98%:NH 8%)	84%	16%
Dwr Cymru water inspectors	Volume and type of calls raised	82%	18%
Other operating expenditure			
Disconnections and reconnections	All non-household	0%	100%
Demand- side water efficiency initiatives		0%	100%
Dwr Cymru Customer Services Ltd	Directly attributable	0%	100%
Customer side leaks		85%	15%
jobs raised after customer call	Job types from SAP and Business Warehouse report (in 2012-13 this was allocated using management judgement resulting in H100%:NH 0%)	85%	15%
Other direct costs		74%	26%
Dwr Cymru Customer services team	Cost identified that could be directly attributed and remaing costs split using customer numbers (in 2012-13 this was allocated using management judgement resulting in H100%:NH 0%)	91%	9%
Dwr Cymru insurance costs	Costs recharged to DCCS and included in admin charge		
Dwr Cymru Actuarial costs	Unchanged from 2013 basis used	84%	16%
General and support expenditure		88%	12%
IT costs		89%	11%
Dwr Cymru Customer Services Ltd	Customer numbers	92%	8%
Dwr Cymru IT dept	Headcount and nature of support	82%	18%
Motor vehicle costs	Customer numbers	92%	8%
Finance		89%	11%
Dwr Cymru Customer Services Ltd	Customer numbers	92%	8%
Dwr Cymru Finance	Customer numbers and water save initative credit direct to household	78%	22%
Dwr Cymru Audit fees	Customer numbers (in 2012-13 this was allocated using direct cost resulting in H99%:NH 1%)	92%	8%
Dwr Cymru income and tarriff team	Customer numbers (in 2012-13 this was allocated using management judgement resulting in H75%:NH 25%)	92%	8%
HR		87%	13%
Dwr Cymru Customer Services Ltd	Customer numbers	92%	8%
Dwr Cymru HR	Employment costs	84%	16%
Executive team		92%	8%
Dwr Cymru MD and FD	Customer numbers (in 2012-13 this was allocated using employment costs resulting in H96%:NH 4%)	92%	8%
Dwr Cymru - Co Sec	Customer numbers (in 2012-13 this was split equally H50%:NH 50%)	92%	8%
general management		92%	8%
Dwr Cymru Customer Services Ltd	Customer numbers	92%	8%
Facilities		84%	16%
Dwr Cymru Customer Services Ltd	Customer numbers	92%	8%
Dwr Cymru	Headcount and includes share of support services facilities costs allocated to retail	79%	21%
Other general and support costs		80%	20%
Dwr Cymru Customer Services Ltd		72%	28%
Meter reading	Customer numbers		
Training and quality	Customer numbers	92%	8%
Web	Customer numbers	92%	8%
Business change	Customer numbers	92%	8%
compliance	Customer numbers	92%	8%
Business customers	Non household only	0%	100%
Dwr Cymru		90%	10%
Finance business customer	This activity has now been transferred to DCCS		
Comminication team directly allocated	Customer numbers (in 2012-13 this was allocated using management judgement resulting in H100%:NH 0%)	92%	8%
Communication team indirect costs	Customer numbers (in 2012-13 this was allocated using management judgement resulting in H90%:NH 10%)	92%	8%
Quality and assurance	Managers assessment of time spent on audit work	60%	40%
Health and safety	Employment costs (in 2012-13 this was allocated using management judgement resulting in H100%:NH 0%)	84%	16%
Tax and capital markets	Employment costs (in 2012-13 this was allocated using direct costs resulting in H99%:NH 1%)	84%	16%
Finance planning	Customer numbers (in 2012-13 this was allocated using direct costs resulting in H99%:NH 1%)	92%	8%
Scientific Services	Not included in retail due to information notice IN 13/10	0%	0%
Other business activities (regulation costs)	Customer numbers (in 2012-13 this was allocated equally H50%:NH 50%)	92%	8%
Developers services	Non household only	0%	100%
Local Authority rates			
Local Authority rates	Linea - DCCS ooccupied split using customer numbers , remaining allocation based on salaries	90%	10%
Regulatory Accounts 2013-14		90%	10%