

Annex A to PR09/04

Calculation of the operating expenditure incentive allowance with addition of extra year

This is an annotated example of the calculation of the operating expenditure incentive allowance with the addition of the extra year (shown in bold in rows 13 to 16). Outperformance in 2008-09 is **lower** than prior years, so the outperformance constraint is applied. This calculation is used for either water or sewerage service expenditure.

Operating Expenditure		AMP4 period					AMP5 period				
		2005 -06 £m	2006 -07 £m	2007 -08 £m	2008 -09 £m	2009 -10 £m	2010 -11 £m	2011 -12 £m	2012 -13 £m	2013 -14 £m	2014- 15 £m
1	Initial regulatory assumption	270	265	265	260	255					
2	+/- IDoK adjustments										
3	+/- logging-up or down	-	-	-	-	-					
4	Less shortfalls	-	-	-	-	-					
5	Revised regulatory expectation	270	265	265	260	255					
6	Actual Expenditure	255	250	240	238	?					
7	Less atypical & exceptional costs	-	-	-	-	-					
8	Less any cross-subsidy adjustment	-	-	-	-	-					
9	Adjusted actual expenditure	255	250	240	238	?					
10	Outperformance	15	15	25	22	?					
11	Outperformance (setting negatives to zero)	15	15	25	22	?					
12	Outperformance constrained at 2008-09 level	15	15	22	22						
13	Incremental outperformance in 2005-06	15	15	15	15	15	15				
14	Incremental outperformance in 2006-07	0	0	0	0	0	0	0			
15	Incremental outperformance in 2007-08		7	7	7	7	7	7			
16	Incremental outperformance in 2008-09			0	0	0	0	0	0	0	
17	Incremental outperformance in 2009-10				?	?	?	?	?	?	?
18	FINAL INCENTIVE ALLOWANCE						22	7	7	0	

Notes

Line	
1	This is the operating expenditure assumed at the 2004 periodic review.
2	Adjustment to reported operating expenditure for IDoKs.
3	This line includes operating expenditure associated with agreed logging up and down of outputs.
4	Adjustment to reported operating expenditure for shortfalls.
5	Sum of lines 1 to 4.
6	Actual operating expenditure including exceptional costs reported in June Returns.
7	Exceptional and atypical costs.
8	Adjustments made to reported operating expenditure to reflect trade with associates.
9	Sum of lines 6, 7 and 8.
10	Outperformance in each given year (line 5 minus line 9).
11	As line 10 but with negative outperformance set to zero.
12	Outperformance in any year cannot be higher than outperformance in the final year 2008-09. Any outperformance higher than the 2008-09 outperformance is constrained at the 2008-09 level.
13	Incremental outperformance in 2005-06. Since 2004-05 is not used in the calculation, this line is the total outperformance for 2005-06. Outperformance in this year has already been kept for 5 years, so the first 5 years' outperformance is not included in the calculation of the opex incentive allowance.
14	Incremental outperformance in 2006-07. This is the constrained outperformance for 2006 in line 12, minus the sum of the incremental outperformance for the preceding years (line 13).
15	Incremental outperformance in 2007-08. This is the constrained outperformance for 2007 in line 12, minus the sum of the incremental outperformance for the preceding years (lines 13 + 14).
16	Incremental outperformance in 2008-09. This is the constrained outperformance for 2008 in line 12, minus the sum of the incremental outperformance for the preceding years (lines 13 + 14 + 15)
17	Incremental outperformance in 2009-10. Not known at PR09
18	Final incentive allowance: the sum of lines 13, 14, 15 and 16

