

Information notice

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Changes to COPI

Introduction

In RD 11/10 'Changes to COPI' we notified you of the changes affecting the construction output price index (COPI) statistics introduced in July 2010. We confirmed that the changes in the COPI series did not have an impact on the way we use the output price index in regulatory processes, and we would adopt the new COPI (2010) series in our regulatory processes.

Further revisions to COPI were published in September 2011.

The purpose of this information notice is to reconfirm that we are using the new COPI (2010) series when comparing outturn 2010-15 capital expenditure with the 2009 price review assumptions.

Revisions

The September 2011 revisions reflect the changes to the COPI (2010) series made by ONS and improved output deflators developed by BCIS. The effect of these is to:

- revise values of the existing indices;

- provide index values to one decimal place (compares with no decimal place before);
- carry the latest four quarters as 'provisional' values (an increase from two quarters);
- provide index numbers back to 1955, except for infrastructure (IOPI) which goes back to 1980 only; and
- change a number of repair and maintenance indices (which do not have an impact on the all new construction index we use).

Discontinued COPI series

The revisions in September 2011 were not confined to the COPI (2010) series. There was also a change to when the discontinued COPI series closes down. It now closes later than had been announced last year. It closes with a value for the second quarter of 2010 and there are published values for 2009-10 in this series.

The extended coverage of the discontinued series helpfully allows us to continue assessing outturn 2005-10 capital expenditure with the 2004 price review assumptions on a continuous series across the 2005-10 period.

Impact of revised COPI (2010) indices

The revisions to the existing indices dampens the rate of deflation measured by the COPI (2010) series. For example, the annual rate of change for 2009-10 is now -3%, compared with -6.3% for the same period before the September 2011 revisions.

The cumulative movement in outturn COPI from 2007-08 is illustrated in figure 1, which also shows the assumptions we made in the 2009 price review.

Since the base year for the 2009 price review was 2007-08, this means we work the (ex ante and ex post) inflation on a cumulative basis from that year.

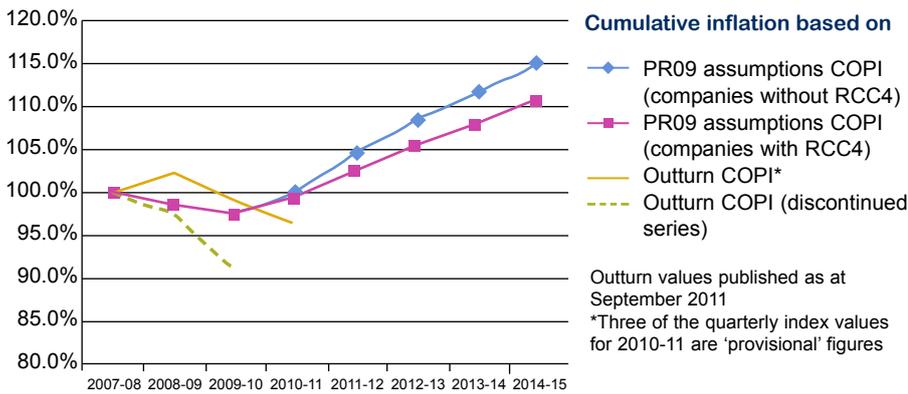
Using revised values

We are using the new COPI (2010) series to compare outturn 2010-15 capital expenditure with the 2009 price review assumptions.

Our approach is that we use the latest prevailing set of published values when we perform our regulatory calculations. This

This is a formal document that alerts our stakeholders to a change in the way that we regulate the water and sewerage sectors in England and Wales.

Figure 1 Cumulative COPI inflation



means that there can be changes in the outcome of the arithmetic, purely as a result of the revisions to the published indices.

Notified Index

The difference between COPI inflation and general RPI inflation forms the relative price effect, which is referred to as the Notified Index.

At the 2009 price review, we used the published values of RPI and COPI available at that time with assumptions on the rate of change thereafter. Details are set out in [chapter 5 of the FD report](#) at section 5.11. This gives the forward-looking year-on-year percent changes we assumed for the movement of COPI relative to RPI for 2009-10 onwards.

Our RPE assumption is the same for all companies; however we do not apply it to the years 2010-11 to 2014-15 in the price review for the companies with RCC4 in their licence.

Indexation in RCV and CIS

We receive enquiries on the impact the difference between our assumptions of COPI in the 2009 price review and the outturn position has on the RCV under CIS, and also the ex post true up of the CIS reward or penalty. We clarify how the indexation difference between forecast and outturn affects these below.

RCV

The fact that outturn COPI will inevitably be different to that assumed when we set price limits has **no direct impact** on any reconciliation of a company's RCV at the end of the price control period. This is because, at the end of the price control period, a company's outturn capital expenditure is included in its RCV, replacing that which we assumed when we set price limits.

CIS

The fact that outturn COPI will inevitably be different to that

assumed when we set price limits **will have an impact** on the CIS reward or penalty that will be calculated at the end of the price control period. This is because our CIS baseline will be adjusted for that difference.

To demonstrate this, we have produced a [simple illustration](#). The illustration represents the specific scenario where:

- expenditure forecast in the company final business plan and our assumption of capital expenditure for the CIS baseline are equal (that is, an ex ante CIS ratio of 100). Consequently, the capital expenditure assumed in price limits is equal to the company's final business plan; and
- the company outturns at the same level of capital expenditure to that included in its business plan and assumed in price limits.

In this scenario, there is no adjustment to the RCV because outturn capex is equal to that assumed when we set price limits. However, ex post, the CIS baseline changes from that assumed when we set price limits because it is adjusted to reflect outturn COPI. As a consequence of the adjustment to the CIS baseline, the ex post CIS ratio will be different to the ex ante ratio.

If you have any questions or want to know more about how we use COPI, please contact Dawn Harrison at dawn.harrison@ofwat.gsi.gov.uk.

More information

RD 11/10 Changes to COPI

The construction output price indices are owned by BIS and published via the BCIS online subscription service on <http://service.bcis.co.uk>. This service gives access to the new COPI (2010) series and the one that was prevailing at the time of the 2009 price review. The output price indices data are available on the [BIS website](#).

The Office for National Statistics (ONS) calculates the output indices. Values for the COPI (2010) series are available from the [ONS website](#). The only ONS releases that line up with the BCIS BIS releases are the releases made in March, June, September and December.

[Illustration](#)* of COPI indexation in RCV and CIS calculations.

*Amended since first publication



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