

Information notice

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Expectations for company reporting 2013-14 – regulatory accounts, accounting separation and performance information

This information notice sets out the way in which we expect the companies to prepare their regulatory information for 2013-14. This includes their:

- regulatory accounts,
- accounting separation information; and
- performance reporting information.

Background

By law – and like any other private limited company in the United Kingdom – each licensed water company in England and Wales must prepare statutory accounts from its financial records every year.

To comply with its licence, each water company must also prepare a yearly financial statement about its regulated business. These are called regulatory accounts. The information that companies provide in their regulatory accounts is checked by independent auditors. In preparing their accounts, companies must

follow our [regulatory accounting guidelines \(RAGs\)](#).

As part of its regulatory accounts, each company has to report the accounts (costs, revenues, assets and liabilities) for the different activities it carries out in delivering services. This is known as accounting separation.

Alongside its regulatory accounts and accounting separation information, we require each company to set out in a yearly statement how it has managed its risks and complied with relevant statutory and regulatory obligations (a 'risk and compliance statement'). Each company also demonstrates how it has performed in the year by publishing a range of key indicators for its customers.

We use all of the information that companies publish – and other forms of intelligence – to consider where there are significant risks to customers and the environment, and whether we need to take any action. We call this our [risk-based approach to regulation](#).

Regulatory accounts

Reporting for 2013-14 and onwards

We will keep the current RAGs until the end of the 2014-15 reporting year. We will consult at the end of 2014 on changes to the RAGs for the 2015-16 reporting year. This includes amending the RAGs to reflect:

- changes to the UK's Generally Accepted Accounting Standards (UK GAAP) as they harmonise with international accounting standards (IFRS); and
- the approach we expect the companies to follow in recording transactions between different parts of their appointed business ('business units').

We have already started thinking about the transition to IFRS. We have met with Water UK – the representative body for water companies – and HM Revenue and Customs (HMRC). We also continue to meet with our [regulatory accounts working group](#) and Water UK. We will use these

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.

meetings to inform the development of our new RAGs.

We recognise that some water companies may wish to adopt the revised UK GAAP standards in their statutory accounts before 2015-16. Companies deciding to do this will adopt either:

- IFRS;
- the reduced disclosure requirements of Financial Reporting Standard 101 (FRS 101) (if they meet the qualifying criteria); or
- Financial Reporting Standard 102 (FRS 102).

Where a company does this, it will need to prepare its regulatory accounts based on the UK GAAP framework that existed previously.

Best practice guidance

In 2013, we published best practice guidance on revenue recognition accounting to help the companies to prepare their regulatory accounts. As a result we found there was a significant improvement in the standard of companies' reporting as part of our review of their 2012-13 regulatory accounts. But as part of our review, we also found that several companies did not include the following items in their regulatory accounts.

- A description of the variances between amounts of revenue assumed at the previous price determination and those recognised in the year.
- Any significant differences between a retrospective review

of the previous year's measured income accrual and amounts billed in the year.

Paragraph 3.6.2 of RAG 3.07 sets out that companies are required to provide these items.

So, we have updated '[Appendix 3: Best practice revenue recognition accounting policy note](#)' of RAG 3.07 to include these disclosures. We will incorporate the changes to the RAGs formally for the 2015-16 reporting year.

Also, as part of our review of companies' 2012-13 regulatory accounts, we looked at the extent to which they complied with the requirements of RAGs 3.07 and 4.04. Following this, we have developed:

- '[Best practice guidance – bad debt](#)'; and
- '[Best practice guidance – Directors' pay and standards of performance](#)'.

We have developed these documents using:

- RAG 3.07 paragraphs 3.2 and 3.8; and
- best practice we identified in our review of companies' regulatory accounts.

Both documents are for guidance only. It is for each company to use those parts that are appropriate to it and adapt them as necessary.

Following a consultation last year, we published '[Board leadership, transparency and governance –](#)

[principles](#)' for regulated companies in January 2014. This sets out the principles that we expect the companies' Boards to adopt as a minimum. We expect companies to transparently demonstrate how they meet these principles.

In '[Best practice guidance – Directors' pay and standards of performance](#)' we identify some examples of best practice in companies' 2012-13 regulatory accounts for presenting tables to show how remuneration linked to performance forms part of directors' overall remuneration. Companies should be aware that reproducing these tables alone will not be sufficient to meet all the requirements that apply for 2013-14.

Guidance to auditors

As part of companies' regulatory accounts, independent auditors give an opinion on the regulatory accounts. We set out the full wording of the opinion we require from auditors for 2013-14 in '[Wording of the regulatory accounts audit opinion 2013-14](#)'.

In '[Targeted review of accounting separation cost allocations](#)', which we published in June 2013, we set out the results of a review we commissioned of the accounting separation information that companies provided to us in 2011-12. Following this review we decided to ask the auditors to perform agreed audit procedures and submit a report to us on the companies':

- retail tables; and
- upstream services information.

We shared draft versions of the procedures with the audit firms for discussion and comment. We set out the final versions in:

- ‘[Audit procedures for retail cost analysis 2013-14](#)’; and
- ‘[Audit procedures for upstream services cost analysis 2013-14](#)’.

Companies and auditors need to make sure that this additional work is included in engagement letters for the audit work for 2013-14.

Small company regulatory accounts information requirements

Small companies are those with a turnover of less than £6.5 million in 2013-14.

We have incorporated the relevant information requirements for small companies into section 4 of RAG 3.07. Small companies should also refer to RAG 4.04 for guidance on line definitions.

Small companies should submit statutory accounts containing associated statements as required. For example:

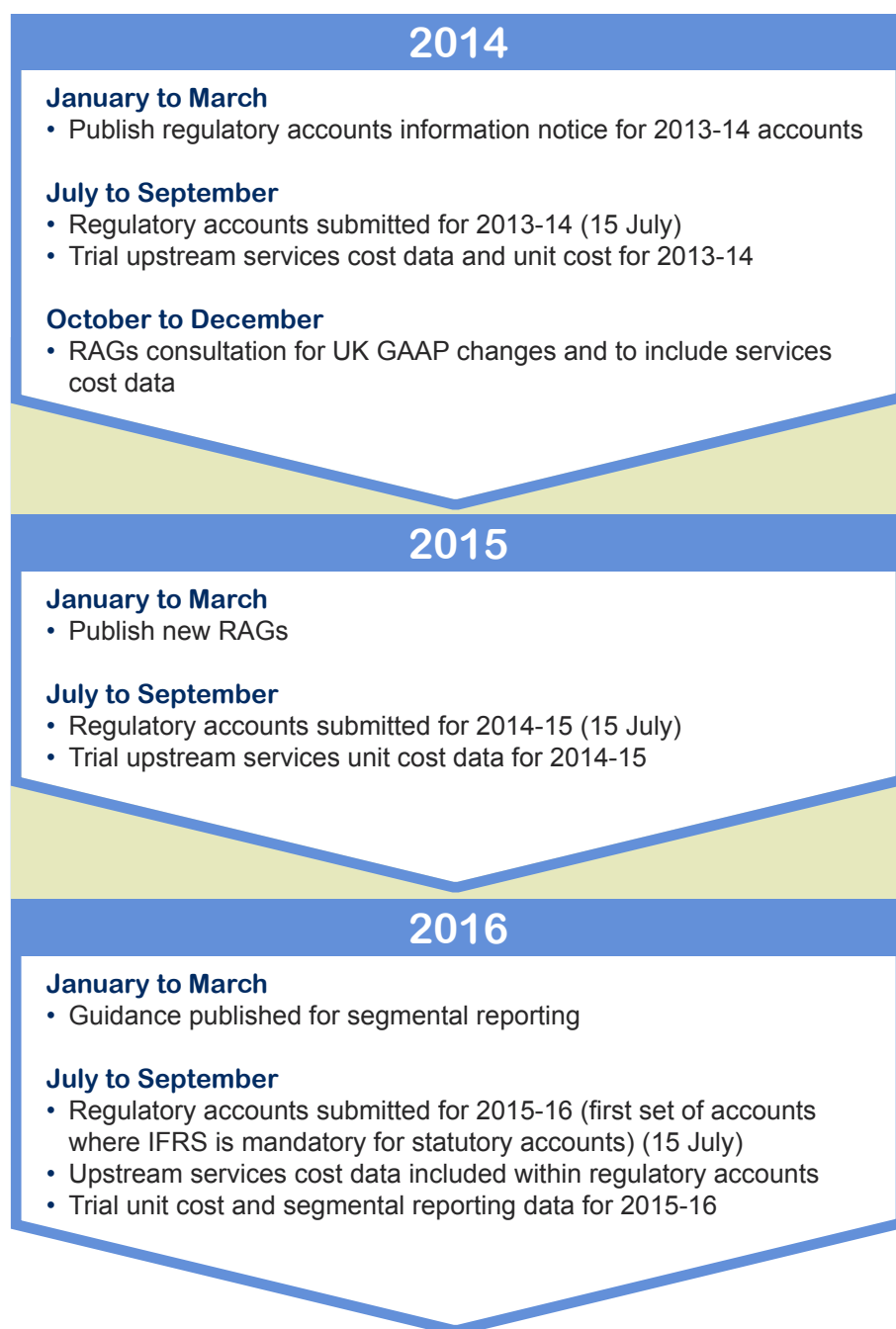
- a F6A certificate of financial resources; and
- a statement on links between directors’ pay and standards of performance.

For small companies that wish to submit their return using our Excel template, please use ‘[RAG 3 Small company return](#)’.

Developing new RAGs for 2015-16 and beyond

The timeline in figure 1 shows the

Figure 1: Future reporting requirements



key milestones for developing and introducing RAGs that are aligned with revised UK GAAP.

Accounting separation information

Guidance clarifications

Our targeted review of accounting

separation cost allocations last year highlighted that companies were interpreting the definitions of data they need to provide about customer services and other operating expenditure in different ways. So, to help all users to compare companies’ retail cost information, we have provided

clarification for companies on the definitions they should use in preparing their 2013-14 accounting separation information. [‘Accounting separation guidance clarifications’](#) is available on our website.

Methodology statement

Each company must publish on its website an accounting methodology statement and accompanying commentary at the same time as its regulatory accounts. The targeted review of companies’ accounting separation cost allocations identified wide variation in the level of transparency provided in the companies’ methodology statements for 2011-12. The review recommended that we require companies to make additional disclosures as part of their methodology statement to improve the usefulness and comparability of the data for users. So we have added them to [‘Disclosure requirements for companies’ accounting separation and upstream services data methodology statements 2013-14’](#), which is available on our website.

Trial of cost allocation to upstream services

We are currently conducting a trial by asking companies to publish extra information about their costs in delivering their ‘upstream’ services, such as transporting and treating water and sewage. For 2013-14, we require companies to:

- complete a form with their upstream services data and publish it along with a methodology statement and

commentary on their website; and

- report the main factors causing changes to their costs (‘cost drivers’) for each of the upstream services they provide. Each company has the flexibility to choose the cost driver it decides is the most appropriate for each service. They should also explain in their commentaries why the cost drivers they have chosen are the most appropriate. Where the most appropriate cost driver information is not available, we expect companies to use the next most appropriate and explain their reasoning.

The upstream services form can be found in [‘Upstream services definitions and form for providing data 2013-14’](#), which is available on our website. The definitions for each data item are the same as in 2012-13.

Performance information

This year we have made no changes to our guidance for companies on:

- [preparing their risk and compliance statement](#); and
- [reporting their performance against their indicators](#).

As they did last year, the companies can choose how they explain their performance to their customers and other stakeholders. We expect each company to clearly set out:

- how it has performed;
- its risks; and
- how it has dealt with them.

We expect companies to bring to our attention risk and performance issues that they identify as they arise. Where we find issues that they have not made us aware of, we will take action. This may include taking formal action, in line with our [approach to enforcement](#).

Where we find that companies have failed customers, they can expect us to take strong action. This guidance also applies to small companies.

Publication and submission

Performance information

By 15 July 2014 each company will need to send us its risk and compliance statement and publish it on its website, as well as publish its key performance information. Companies should send the website links to these documents and one signed copy of their risk and compliance statements to riskandcompliance@ofwat.gsi.gov.uk. We will then update the relevant information on our website.

Regulatory accounts and accounting separation information

As soon as possible after the end of the financial year, and at the latest by 15 July 2014, each company will need to publish its regulatory accounts information on its website. This includes its:

- regulatory accounts;
- accounting separation methodology statement and accompanying commentary; and
- upstream services form, methodology statement and accompanying commentary.

As soon as it is published, we expect each company to:

- provide us with an electronic link to where this information is held on its website so that we can publish a link to it on our website; and
- send us electronic copies of its:
 - regulatory accounts;
 - statutory accounts (if not bound with the regulatory accounts); and
 - UK holding company accounts (where the ultimate owner is an overseas company).

Please send electronic copies to regulatory.accounts@ofwat.gsi.gov.uk. Small companies should also submit their statutory accounts and associated statements to this address.

Where a company has a statutory year-end that is different from 31 March 2014, please remember to send us links to your statutory accounts when these are available.

Enquiries

If you have any questions about this information notice or any of our requirements, please send them to regulatory.accounts@ofwat.gsi.gov.uk.

More information

[Regulatory accounting guidelines \(RAGs\) web pages](#)

[Regulatory accounts working group web page](#)

[Risk-based approach to regulation web page](#)

[‘RAG 3.07 – Appendix 3: Best practice revenue recognition accounting policy note’, updated February 2014](#)

[‘Best practice guidance – bad debt’, February 2014](#)

[‘Best practice guidance – Directors’ pay and standards of performance’, February 2014](#)

[‘Board Leadership, transparency and governance – principles’, January 2014](#)

[‘RAG 3 Small company return’, Excel template](#)

[‘Targeted review of accounting separation cost allocations’, June 2013](#)

[‘Wording of the regulatory accounts audit opinion 2013-14’, January 2014](#)

[‘Audit procedures for retail cost analysis’, February 2014](#)

[‘Audit procedures for upstream services cost analysis’, February 2014](#)

[‘Accounting separation guidance clarifications’, February 2014](#)

[‘Disclosure requirements for companies’ accounting separation and upstream services data methodology statements 2013-14’, February 2014](#)

[‘Upstream services definitions and form for providing data 2013-14’, February 2014](#)

[Key indicators – guidance web page](#)

[Risk and compliance statement guidance web page](#)

[Our approach to enforcement web page](#)



Ofwat (The Water Services Regulation Authority) is a non-ministerial government department. We are responsible for making sure that the water sector in England and Wales provides consumers with a good quality and efficient service at a fair price.

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