

South East Water's
Response to
Consultation on
regulatory reporting

June 2016

1 INTRODUCTION

This document provides South East Water's response to the consultation on the review of regulatory reporting published in March 2016.

Overall we welcome the approach set out by Ofwat to clarify the guidance for reporting to ensure a consistent and comparable approach across the industry. In addition to the consultation questions we also look forward to contributing to defining, and confirming, the boundary between the proposed price controls: water resources and network plus, with latter commencing with the raw water network distribution. We have a number of boundary complexities involving our water resource network interacting with impounding reservoirs that differ from case to case and we welcome further clarification to how these should be handled.

Whilst we welcome the approach to ensure guidance evolves into a consistent submission from all companies we are wary that price controls in place have been set on guidance relevant for PR14. Significant guidance change at this time could therefore alter the allocation of expenditure driven to each price control, which may lead to actual returns being inconsistently reported against FD expectations.

Given this outcome we would suggest that Ofwat should confirm how they could deal with this issue at PR19.

2 ANSWERS TO SPECIFIC CONSULTATION QUESTIONS

Below are responses to the specific questions raised.

Q1. What are your views on the content and format of the proposed tables in Appendix 1

There seems to be little variation in table format and requirement from the 2015/16 period, with the exception of 3B, which we are not required to complete. We believe this to be sensible since this allows us to build up a process for producing the information and provides a point of reference to the information produced. We do question the need for the statutory accounts primary statements to be reproduced in section 1. We believe reporting the regulatory accounts, split between appointed and non-appointed, would be enough in the return without having to show the workings in getting from statutory accounting to regulatory accounting in the report.

Q2. Do you have any views on the revised guidance in RAG1 which is intended to assist completion of pro-forma table 4G

We have no comment to make on this issue.

Q3. RAG2 consists of a mixture of high level principles and detailed guidance for cost reporting;

- Q3a is the balance of principles and rules appropriate?

We believe the proposed principles are adequate. We consider guidance rules for allocation of expenditure between wholesale and retail, and household and non-household are generally sensible. However, we believe companies should be able to vary from the guidance if there is suitable reason to do so – where this is the case companies should clearly state their reasons and altered approach in the methodology statement. We use debt management as a unique example to South East Water, where debt greater than 30 days old should be used as a driver. At South East Water we have been unable to use this as an appropriate driver since debt remains linked to the original customer type – hence unmeasured debt remains unmeasured debt (until written off or cleared). Issues have arisen as properties have become a measured property (particularly given our metering programme. Allocation using Ofwat guidance therefore inappropriately allocates associated cost to unmeasured customers that is no longer relevant. Ultimately this may therefore skew cost to serve values, which are based upon the current customer type base. We offer this example to support our view that prescribed guidance should be adaptable to unique circumstances.

- Q3b Are there areas where more principles should be provided?

We believe current stated principles are sufficient.

- Q3c Are there areas where more guidance should be provided?

There is no guidance regarding allocation of pension deficit payments. The last guidance regarding this subject was issued within IN 13/17 (Treatment of companies' pension deficit repair costs at 2014 price review). We have outlined our approach for 2015/16 within our methodology statement, which is different to rules set out in IN 13/17. Further clarity regarding the treatment of pensions maybe useful given the value involved.

Detailed clarification of business unit for impounding reservoirs would be useful with RAG4.06. Following the CEPA review we have a number of impounding reservoirs that potentially could be allocated either water resources or raw water storage. We are aware this is an area of continuing review and look forward to assisting with the debate to secure a conclusion.

We consider there should be a level of materiality attached to the raw water transport and storage business units. Following the definitions strictly we clearly have an element of a raw water network that links water resources to water treatment. However the majority of sites physically have a small footprint that encompass both abstraction (water resources) and water treatment. We currently assume a common sense approach and assume no raw water network when considering allocation of cost, since we do not believe these business units were created to capture this type of inter-site activity. We would therefore seek

improved clarification in the RAG guidance to include a de minimus value (e.g. length of main) regarding the raw water network link between water resources and water treatment.

Q4. RAG2 suggests that a common method for calculating returned sludge liquors should be implemented. Do you have any observations on the approach suggested and any suggestions for a common formula?

No view offered for sewerage activity.

Q5. In RAG2 we have set out how energy costs and savings from sludge processes should be treated – do you have any views on this approach?

No view offered for sewerage activity.

Q6. In RAG2 we have set out how imported potable bulk supplies should be treated – do you have any views on this approach?

Further clarification on the allocation guidance would be useful – for allocating paragraph 2.14 of RAG2 seems to begin by offering two options before just outlining one options based upon the costs of the exporting company. We infer this to mean a pro-rata basis on total expenditure for either water resources or water treatment. It should be noted that companies of receiving supplies will not have access to supplying companies' tables until after submission, and therefore would rely on the previous period submission which could be out of date. Furthermore it is not clear whether an aggregated pro-rata of total cost would be reflective of specific bulk exports.

It is not clear what the objective of moving to this level of detail is, particularly if detail is lightly assumed and out of date. Indeed, the current level of reporting makes it clear what bulk supply transfer is delivered untreated and what is received treated. An alternative would be for the exporting company to supply the relevant detail in sufficient time for submission, however for this level of detail we would be dependent on other companies managing this process. We would therefore favour retention of the current guidelines given the unclear advantages of changing.

Q7. In RAG3 we have clarified our expectations for reporting transactions with associates and the non-appointed business. Do you have any comments on these?

The guidance on transactions with associates is clear and simple.

Q8. Our intention is to include the metrics for the Financial monitoring framework and site data for the Abstraction Incentive Mechanism (AIM) in the Annual Performance Report. Do you agree with this approach?

Yes, we agree in principle the approach.

Q9. Should the Annual Performance Report contain more transparency over metering assets and installation and maintenance costs from 2017?

We do not feel it is currently necessary to introduce this additional information in the Annual Performance Report. We believe this area should be reviewed after market opening once the use of accredited entities is better understood.

Q10. Ofwat is working with the sector to develop new charging rules covering activities such as connection charges, infrastructure charges and other contributions from third parties. Should the Annual Performance Report contain more detailed cost information on new connections and other costs associated with these charges?

Whilst it may be useful to have additional reporting information for new connections, it would be difficult to define what these should be, and whether they are necessary, when the new charging rules are yet to be defined.