About this document

In 'Consultation on the final 2010-15 reconciliation' we invite comments on our proposals for reconciling the incentive arrangements for companies' performance and expenditure for the 2010-15 period now that actual information is available for the complete period, including 2014-15 the last year of the price review 2009 (PR09) price control.

To the extent that the adjustments we propose are different to the assumptions we made as part of the price review 2014, the differences will mainly be taken into account at the next price review in 2019, although one, in respect of the revenue correction mechanism, could be adjusted through revenue in the period 2015-2020.

In this appendix, we set out the proposals in respect of United Utilities. It shows how we have assessed the claims the company has made, and the basis for our proposals.

We are also publishing detailed spreadsheets containing calculations of the adjustments for each company alongside the consultation.

Contents

1. Introduction

At PR09 Ofwat included a number of incentive arrangements designed to protect customers by encouraging companies to improve and deliver their services more efficiently over the period 2010-2015. The mechanisms also were intended to help companies manage uncertainty.

Many of these mechanisms required data for the last year of the price control period, 2014-15 (the blind year) to assess the final outturn for the benefit of customers, or companies, as the case may be. When PR14 was completed in December 2014, this financial year had not finished. Consequently, companies provided forecast data, which Ofwat considered and adjusted as necessary, for inclusion in the PR14 final determination.

Companies have now provided complete information and final audited spend and performance data for the whole 2010-2015 period, which we have used to update our analysis.

In reaching our proposals on the 2010-15 reconciliation, we have applied an approach that follows that previously consulted on and set out in the PR14 Reconciliation Rulebook. In ‘Consultation on the final 2010-15 reconciliation’, we:

- Recap on the approach we used at PR14 to reconcile companies’ proposed adjustments to 2015-20 price controls given companies’ performance against incentive mechanisms put in place at the last price control review (PR09); and
- Explain how and why these adjustments differ from those we made in our PR14 final determinations, and those proposed by companies.

In this appendix, we set out our proposals of the blind year reconciliation adjustments for United Utilities resulting from the company’s actual performance during the period 2010-2015, reflecting actual data for 2014-15.

We have structured this appendix to begin in section 2 with a summary of the adjustments. In section 3 we explain each of the adjustments in turn:

- Revenue correction mechanism (RCM);
- Change protocol (logging up, logging down, shortfalls);
- Service standard outputs;
- Serviceability performance;
- 2009 agreed overlap programme; and
- Capital expenditure incentive scheme (CIS).

In addition to the incentive arrangements listed above, we also cover the 2014-15 transition mechanism in section 3.7. We summarise how and when our proposed adjustments will be implemented in section 4.

For each mechanism we outline:

- Our position as set out in PR14 final determination;
- How our proposals differ from decisions taken at PR14; and
- How our proposals differ from companies' proposals.

There are a number of other PR09 incentive mechanisms not listed above, in particular the service incentive mechanism (SIM), the opex incentive allowance (OIA) and other revenue adjustments. For these mechanisms we expected all information to be available at PR14 and so did not include these in the scope of this final reconciliation. In any case we are not aware of any reason to change these adjustments. This document makes no further reference to these.

In order to calculate the blind year adjustments, we have undertaken detailed calculations within our models for the RCM, CIS and serviceability shortfalls and the PR14 reconciliation rulebook legacy blind year model. While we provide an explanation of our interventions within this appendix, each model contains the detail of the specific calculation.

Populated models for the blind year update proposals are published alongside the consultation.

All monetary values stated in this document are in 2012-13 prices unless otherwise stated.

2. Summary of 2010-15 final reconciliation adjustments

Table A1 below sets out for each of the incentive tools for water and wastewater services a quantification of:

- PR14 final determination (FD) position;
- the company's view of the required adjustment (if stated in its blind year update submission); and
- our view resulting from the blind year reconciliation (BYR).

The main difference between the company and our view relates to the change protocol as set out in section 3.2 and the 2009 agreed overlap programme as set out in section 3.5.

The table shows adjustments made through revenue and those made through the RCV separately. This is because the PR09 incentive mechanisms are adjusted for in different ways. Mainly, they are adjusted through an adjustment to the RCV, however the RCM and the penalty / reward element of the CIS adjustment are both made through revenue.

Table A1 Revenue and RCV adjustments 2015-20 (£ million)

	Water service			Wastewater service		
	FD position	Company BYR view	Ofwat BYR	FD position	Company BYR view	Ofwat BYR
Revenue adjustments						
RCM	41.121	n/a	32.400	68.575	n/a	66.698
CIS	-17.020	n/a	-25.525	-27.221	n/a	-37.021
Total revenue adjustments[2]	24.101	n/a	6.875	41.355	n/a	29.677

	Water service			Wastewater service		
	FD position	Company BYR view	Ofwat BYR	FD position	Company BYR view	Ofwat BYR
RCV adjustments						
Elements of CIS:						
Adjustment for actual expenditure 2010-15	-128.521	n/a	-190.630	23.773	n/a	-49.518
Adjustment for change protocol – logging up/down	0.000	0.000	0.000	71.968	94.589	62.713
Adjustment for change protocol – shortfalls	-9.451	-9.451	-9.451	-64.494	-72.765	-79.446
Adjustment to overlap	0.000	0.000	0.000	34.037	34.037	26.034
CIS total[2 3]	-137.972	n/a	-200.082	65.284	n/a	-40.217
Serviceability shortfall	0.000	0.000	0.000	0.000	0.000	0.000
Total RCV adjustments[2 3]	-137.972	n/a	-200.082	65.284	n/a	-40.217

Notes:
1. The revenue and RCV adjustments are added for comparison against the materiality threshold in the PR14 reconciliation rulebook blind year model.
2. Totals may not add up due to rounding.
3. The FD position has been updated for the RCV indexation correction that will be applied separately at PR19.

The adjustments for the Change protocol and 2009 agreed overlap programme are considered separately, but both are implemented through the CIS.

3. Adjustments by 2010-15 incentive mechanism

3.1 Revenue correction mechanism

Our view for the revenue correction mechanism (RCM) adjustment is detailed in table A2 below. This shows the components of the movement from the RCM adjustment included in the PR14 final determination.

Table A3 summarises our interventions in relation to the 2010-15 RCM adjustments.

For the RCM, we apply the PR14 vanilla wholesale WACC (real; pre-tax cost of debt, post-tax cost of equity) as the discount rate. As in the final determination, the PR14 discount rate is 3.6% for United Utilities.

Table A2 RCM total adjustments for 2015-20 (£ million)

	Water service	Wastewater service	Total
FD position	41.121	68.575	109.696
Impact of RPI changes[1]	-3.657	-4.718	-8.374
Impact of updated data from company	-5.064	2.841	-2.224
Impact of other adjustments	0.000	0.000	0.000
Impact of Ofwat intervention	0.000	0.000	0.000
Ofwat BYR	32.400	66.698	99.098
Change from FD position	-8.721	-1.877	-10.598

Note:

1. The calculated movement from the RCM adjustment included in the PR14 final determination relates to actual RPI being lower than forecast at PR14 for 2014-15.

The changes shown in table A2 above will be implemented in the PR14 reconciliation rulebook legacy blind year model as discussed in section 4.

Table A3 Interventions on proposed 2010-15 RCM adjustments

Area of intervention	What we did at FD	Why we did it at FD	What has changed in BYR	What we have done for BYR and why
Back-billing amounts	Our assumptions for the final determination did not include the back-billed amounts claimed by the company.	We had not received sufficient evidence that the back-billing amounts being claimed by the company are compliant with RAG4.04 and IN11/04. The company included an amount in 2010-11 that represents an under-accrual from the period 2005-10 that resulted in over-stated revenue in the previous price control period, 2010-15. The negative amounts included from 2012-15 represent a loss of revenue as a result of household customer data cleanse activity.	There has been no change from the final determination.	There has been no change from the final determination.
FD09 assumptions – Measured non-households' revenue for the measured non-household group immediately above and below the 50 megalitre (Ml)	The final determination included our view of the FD09 assumptions for the inputs to the RCM model. Our view of the company's revenue assumptions for the measured non-household group immediately below and above the 50 Ml tariff basket threshold originated from the	There were differences between the company's and our view of the FD09 assumptions used in the company's populated RCM model. The company applied different assumptions for 'FD09 Measured non-households' revenue for the measured non-household	There has been no change from the final determination.	There has been no change from the final determination.

Area of intervention	What we did at FD	Why we did it at FD	What has changed in BYR	What we have done for BYR and why
	company's FD09 revenue forecasts that came from the tariff basket model, which we used for PR09.	group immediately above and below the 50ML threshold' compared with our view of its FD09 assumptions. Our assumptions for the final determination included the FD09 revenue forecasts as contained in the PR09 tariff basket model in accordance with our published methodology 'Setting price controls for 2015-20 – further information on reconciling 2010-15 performance'.		

3.2 Change protocol (logging up, logging down and shortfalls)

Table A4 below summarises the company's view and our baseline view of total adjustments to capex included in the CIS reconciliation.

Table A5 summarises our interventions in relation to the company's proposed change protocol adjustments.

Table A4 Summary of post-efficiency capex for logging up, logging down and shortfalls included in the CIS reconciliation (£ million)

2009-10 to 2014-15 – post-efficiency capex	Water service			Wastewater service			Total service		
	FD position	Company BYR view	Ofwat BYR	FD position	Company BYR view	Ofwat BYR	FD position	Company BYR view	Ofwat BYR
Logging up (two-sided)[1, 2]	0.000	0.000	0.000	71.968	94.589	62.713	71.968	94.589	62.713
Logging down (two-sided)[1, 2]	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Shortfalls (one-sided)[1, 2]	-9.451	-9.451	-9.451	-64.494	-72.765	-79.446	-73.945	-82.216	-88.897

Notes:
1. We exclude serviceability shortfalls from the numbers above as they are not part of the CIS reconciliation. Instead we make direct adjustments to the RCV.
2. Changes relating to 2009-10 were implemented in full in the opening RCV at PR14 final determination.

The changes for the five years 2010-15 included in table A4 are implemented through the CIS.

Table A5 Interventions on proposed 2010-15 change protocol adjustments

Area of intervention	What we did at FD	Why we did it at FD	What has changed in BYR	What we have done for BYR and why
Habitats Directive – shortfall (water service)	We applied a shortfall adjustment (£8.4 million capex and £0.1 million opex) to reflect the delays to four schemes. These values were our post efficiency assessment.	Four schemes, which were not in the agreed AMP5/AMP6 overlap programme, were delayed into the 2015-20 price control period (Ennerdale Water, Yearl Intake, Deeside, Haweswater habitat phase 2). The company assessed the variance via the	This is an Ofwat initiated claim which the company has now reflected in its blind year submission table W13. The delivery dates for 3 of these projects are the	We have not intervened in this area. The company has accepted the shortfall claim we initiated for the final determination and reflected this in its blind year submission.

Area of intervention	What we did at FD	Why we did it at FD	What has changed in BYR	What we have done for BYR and why
		logging down mechanism and did not propose an adjustment because it was below the triviality threshold (2% of service turnover). However, the outputs were still to be delivered. It was therefore more appropriate to assess the variance to FD09 assumptions as a shortfall. Triviality does not apply in the case of the shortfalling mechanism. The capex variance was calculated by re-profiling the scheme costs against the new delivery timeline advised by the company.	same as assumed in the final determination. Ennerdale has been subject to further review by the EA but the required scope is still uncertain.	
Facility Flood Protection – shortfall (water service – service standard output)	We applied a shortfall adjustment (£1.0 million capex) to reflect the delays to the Heronbridge flood resilience scheme. This value was our post efficiency assessment.	The Heronbridge flood resilience scheme, which was not part of the agreed AMP5/AMP6 overlap programme, was delayed into the 2015-20 price control period. The company assessed the variance via the logging down mechanism and did not propose an adjustment because it was below the triviality threshold (2% of service turnover). However, the output was still to be delivered. It was therefore more appropriate to assess the variance to FD09 assumptions as a shortfall. Triviality does not apply in the case of the shortfalling mechanism. The	This is an Ofwat initiated claim which the company has now reflected in its blind year submission of table W13. There has been no change to the anticipated delivery date for this project, so the company is not proposing any revisions.	We have not intervened in this area. The company has accepted the shortfall claim we initiated for the final determination and reflected this in its blind year submission.

Area of intervention	What we did at FD	Why we did it at FD	What has changed in BYR	What we have done for BYR and why
		capex variance was calculated by re-profiling the scheme costs against the new delivery timeline advised by the company.		
Transfer of private sewers – logging up (sewerage service)	We applied a 29% challenge to the proposed capex associated with the logging up claim in relation to private sewers. We also applied a 55% challenge to the proposed opex associated with the claim. We transferred 8% of the proposed capex expenditure in the logging up claim to opex. Following adjustment, in post efficiency terms the values included for the logging up item were £72.0 million (capex) and £20.9 million (opex).	A transfer of 8% of capex to opex ensured that the company did not benefit from an accounting policy with a bias toward capitalising costs relative to other companies. We reduced the resulting capex by 29% to bring normalised capex/collapse to the industry unweighted average. The result was that of the £110.1 million capex claimed (pre-efficiency) only £79.4 million was accepted for logging up.	The company's capex claim for 2014-15 has reduced from £33.083m pre efficiency in its business plan to £27.265m in its blind year submission. In addition, its forecast of the number of collapses has reduced from 651 to 491 in its blind year submission. The company has restated its number of collapses in 2013-14 from 553 (in the August 2014 submission) to 467 in the blind year submission. This means that the number of collapses in AMP5 has reduced by 11.6% since the final determination. The company noted that “We have continued to successfully apply our active approach to the	The company has not provided evidence that its “active approach” to managing private sewers was in the interests of customers taking into account the higher costs that this approach involved compared to other companies. We note that the percentage reduction in sewer collapses from 12/13 or 11/12 levels is exceeded by several companies. We have intervened to reduce the company's claim, by applying the PR14 final determination methodology to firstly transferring 3.5% of the claimed capex to opex to counter any bias in the company’s accounting policy and secondly, bringing the capex / collapse ratio to the (updated) industry unweighted average. The company has now reported it had to repair significantly fewer sewer collapses than we assumed

Area of intervention	What we did at FD	Why we did it at FD	What has changed in BYR	What we have done for BYR and why
			management of private sewers, this has resulted in collapse rates being maintained at around 13/14 levels, rather than reverting back to 12/13 levels as had been assumed in our Business Plan."	when calculating our FD unit cost. The company is therefore judged as less efficient, leading to a greater percentage reduction of the 2014/15 capex. Our intervention for the previous four years remains unchanged. Overall we propose to log up £62.713m (post efficiency) which is £9.255m less than the PR14 final determination.
Bathing Water Directive – shortfall (sewerage service)	We applied a shortfall adjustment (£7.8 million capex and £0.1 million opex) to reflect the delays to the Manchester Square / Anchorsholme scheme. These values were our post efficiency assessment.	This scheme, which was not part of the agreed AMP5/AMP6 overlap programme, had been delayed into the 2015-20 price control period. The company assessed the variance via the logging down mechanism and did not propose an adjustment because it was below the triviality threshold. However, the output was still to be delivered. It was therefore more appropriate to assess the variance to FD09 assumptions as a shortfall. Triviality does not apply in the case of the shortfalling mechanism. The capex variance was calculated by re-profiling the scheme costs against the new delivery timeline advised by the company.	The company has reduced the capex value of the shortfall from -£8.656 million to -£8.225 million (pre efficiency) due to the company bringing forward the delivery date to 21 April 2016 compared with the 30 April at the time of the final determination.	We have not intervened in this area. We accept the company's revised value of this shortfall claim we initiated in the PR14 final determination.

Area of intervention	What we did at FD	Why we did it at FD	What has changed in BYR	What we have done for BYR and why
Sludge management – shortfall (sewerage service)	We applied a shortfall adjustment (£7.6 million capex and £1.8 million opex) to reflect the delays to three sludge management schemes. This was based on a value the company had calculated. These values were our post efficiency assessment.	Three sludge management schemes (Burnley, Leigh and Blackburn), which were not part of the agreed AMP5/AMP6 overlap programme, were delayed into the 2015-20 price control period. The company assessed the variance via the logging down mechanism and did not propose an adjustment because it was below the triviality threshold. However, these outputs were still to be delivered. It was therefore more appropriate to assess the variance to FD09 assumptions as a shortfall. Triviality does not apply in the case of the shortfalling mechanism.	The company has revised how it manages sludge which has led to further delays in a number of schemes, including those at Burnley, Leigh and Blackburn. The first two were completed in January 2016 and Blackburn "in the first couple of months of AMP6". Accordingly the company has increased the capex value of the shortfall from -£8.405 million to -£9.783 million (pre efficiency). The company also stated that it had experienced delays to 7 Pollution Prevention and Control (PPC) schemes, at Blackburn, Bury, Stockport, St Helens, Huyton, Crewe and Bolton. It stated that "If we were to use the standard approach to determining shortfall values then the additional delay relative to the position set out in RD208 would equate to a post efficiency shortfall of £1.184m. We consider that this movement is part of the overall re design of	We have intervened in this area to include the delays to the seven PPC schemes and to apply our own shortfall calculations in place of those of the company. We see no reason not to include shortfalls for these seven schemes that were not delivered in the 2010-15 period. We have used our standard approach to calculate the shortfall which differs from the company approach. Our shortfall assumes the annual expenditure included in the PR09 final determinations with the later revised completion date. We have applied a pre efficiency shortfall of £6.527 million for the 3 sludge management schemes at Burnley, Leigh and Blackburn and a pre efficiency shortfall £6.051 million for the 7 PPC schemes, making a pre efficiency shortfall of £12.578m (£11.350m post efficiency).

Area of intervention	What we did at FD	Why we did it at FD	What has changed in BYR	What we have done for BYR and why
			the sludge programme since PR09, which is dealt with through the shortfall adjustment described and updated in Table S13. As such we do not propose that any additional adjustment is made for the revisions to the PPC programme.”	At PR14 final determinations we used the figure that the company had calculated for the 3 sludge management schemes, rather than intervening and substituting our own calculation as this was to the benefit of customers. However, we have now used our standard calculation which results in a lower shortfall for these three specific schemes than the comparable company figure, but with the additional shortfall for the 7 delayed PPC schemes, a higher shortfall overall.
Unsatisfactory Intermittent Discharge (UID) Consolidated Programme – logging up (sewerage service overlap)	We revised the two-sided logging up adjustment we made in the draft determination from £18.4 million to £34.0 million in response to the company’s representation. This was based on the difference between the company’s revised total scheme estimate in 2010-15 (£80.0 million) with the apportioned outperformance (£8.2 million) less the FD09 assumption for 2010-15 post efficiency (£54.0 million). For 2015-20, we	The company forecast total scheme costs to be lower than the original FD09 assumptions (post efficiency), but reported an overspend in 2010-15 due to the early delivery of schemes. On that basis, we logged up in 2010-15, the difference between the company's revised total scheme estimate (£83.7 million) and the FD09 figures as provided by the company (post efficiency) so the company did not benefit from any reward or suffer any penalty in the CIS. For 2015-20, our view was to take	The company's actual capex in 2014-15 of £29.260 million is £8.9 million (23%) lower than forecast in its business plan giving a total of £71.004 million (post efficiency) for 2010-15 period. However, forecast capex in 2015-20 has increased from £3.865 million to £15.108 million which gives an overall scheme cost of £86.112 million. This is slightly higher than that forecast at the time of the final	The company has included in its claim, expenditure forecast to be incurred on activity not delivered in the period 2010-15. We have intervened to reduce the final determination adjustment to reflect only expenditure on activities in the 2010-15 period as set out in our main consultation document. Under our approach, we have applied a reduced logging up adjustment of £26.034 million which reflects the PR14 FD view amended by changes in

Area of intervention	What we did at FD	Why we did it at FD	What has changed in BYR	What we have done for BYR and why
	accepted the company's new, lower estimates to complete outstanding schemes.	the company's new, lower estimates to complete outstanding schemes. The company expected opex savings in the 2015-20 period so we accepted the company's latest estimates of opex in our adjustments to the basic totex cost threshold allowances. In its representation (paragraph 7.2.1 on page 13 of REP09 Legacy adjustments – 2010-15 performance), the company accepted the logging up included within the draft determination. However, the company noted that its total expected expenditure for the UID consolidated schemes across both 2010-15 and 2015-20 periods was significantly lower than that originally assumed at FD09. The company stated that it had made efficiencies within the programme that were not fully recognised by the logging up within the 2010-15 period. Having reviewed the basis of our draft determination assumption, we accepted that although our adjustment recognised the early delivery of the programme and ensured the company was not penalised for the overspend in	determination but remains significantly below the FD09 assumption. The company view is that "Applying a reduced AMP5 log up without an equivalent increase in the AMP6 totex baseline, feels inconsistent and as such maintaining the status quo and retaining the PR14 log up appears to the most equitable approach."	efficient actual expenditure in the 2010-15 period of £8.003 million (£8.870 million less FD09 capex infrastructure efficiency of 9.78%). We note that the company will be able to recover around 50% of any additional costs it incurs in the 2015-20 period in respect of this scheme, through the totex incentive mechanism.

Area of intervention	What we did at FD	Why we did it at FD	What has changed in BYR	What we have done for BYR and why
		the CIS reconciliation, it failed to recognise the outperformance the company achieved within the programme.		
Eccles WWTW - AMP3 NEP – shortfall (sewerage service)			This scheme was originally included within the AMP3 NEP but has been delayed from the position assumed within FD09 due to land access issues affecting the adjacent Manchester Ship Canal. Anticipated final delivery is now by 31/03/23, with the total cost expected to be £19.270 million in excess of that forecast in its 2009 Final Business Plan, but with an underspend in AMP5 of £12.762 million. The company states that the delays in AMP5 could lead to a shortfall of £4.159 million (post efficiency), but consider that no adjustment should be made because this would "not reflect the nature of the delay affecting this project and UUW will already be penalised through the totex menu incentives."	The company provided information on the progress it has made in delivering this scheme but did not submit a claim. We see no reason not to include a shortfall for this scheme that was not delivered in the 2010-15 period. We have applied a new pre efficiency shortfall of £4.609 million (£4.159 million post efficiency) based on the company's calculated value which we consider reasonable having checked against the PR09 Projects Database and consistent with our standard approach set out in the Change Protocol 2010-2015. We consider that this adjustment should be made to ensure that customers recover the costs they funded for the delivery of this scheme in the period 2010-2015. We also note that the company will be able to recover around 50% of any additional costs it

Area of intervention	What we did at FD	Why we did it at FD	What has changed in BYR	What we have done for BYR and why
			The company has calculated the shortfall based on moving the originally assumed annual expenditure at the 2009 final determinations back to reflect the new expected delivery date of 31/03/2023.	incurs 2015-20 period in respect of this scheme, through the totex incentive mechanism.

We have not intervened in the following shortfall claims:

- Freshwater Fish Directive (Shortfall – sewerage service);
- Bathing Waters Directive (Shortfall – sewerage service);
- Habitats and Bird Directive (Shortfall – water service); and
- Facility Flood Protection (Shortfall – water service).

3.3 Service standard outputs

Service standards are regulatory outputs that we set out in FD09 supplementary reports[1]. Where relevant companies reported their performance for 2014-15 on these service standards as part of their submissions for the blind year reconciliations.

In our PR14 final determination we were satisfied that the FD09 service standards had been met, except for those relating to the 'facility flood protection' scheme, hydropower generation schemes and the renewable energy research and development (R&D) programme.

- **Facility flood protection scheme**: in the PR14 final determination, we initiated a shortfall of £1.036 million due to delays in the Heronbridge flood protection scheme. In its blind year submission, the company reflected a shortfall claim for this amount (see table A5.2 above), and therefore we have not needed to intervene.
- **Hydropower generation schemes**: in the PR14 final determination, we accepted the company's reasons for non-delivery of four schemes on cost-benefit grounds and did not apply a shortfall adjustment. This remains our view for this final reconciliation.
- **Renewable energy R&D programme**: in the PR14 final determination, we noted that the R&D programme had not delivered the intended opex savings from reducing energy consumption and increasing energy generation and therefore the service

[1]In the 2009 final determination supplementary reports we said: "Both the project activity (as proposed in your final business plan) and the service standard are the defined output. You must demonstrate delivery of the stated service standard output through the June return. We recognise that companies may decide to prioritise activity differently in order to achieve the service output in a more efficient manner. All material changes to the project activity must be reported and explained through your June return."

standards had not been met. However, we did not apply a shortfall for the under-delivery of opex savings as this was reflected in any achieved OIAs.

3.4 Serviceability performance

Table A6 quantifies the value and impact of any serviceability shortfall on the RCV. Table A7 summarises our interventions in relation to the company's proposed adjustments for serviceability.

There are no changes from our final determination and there are no interventions in this area.

Table A6 post-efficiency serviceability shortfall value (£ million)

Post-efficiency shortfall		2010-15
Water service	FD position	0.000
	Company view	0.000
	Ofwat BYR	0.000
Wastewater service	FD position	0.000
	Company view	0.000
	Ofwat BYR	0.000

Any change between our PR14 final determination and our proposals shown in table A6 above will be implemented in the PR14 reconciliation rulebook legacy blind year model at PR19, discussed in section 4.

Table A7 Impact of serviceability shortfalls on the RCV

Area of intervention	What we did at FD	Why we did it at FD	What has changed in BYR	What we have done for BYR and why
There are no interventions in this area.				

3.5 The 2009 agreed overlap programme

Table A8 below confirms the 2009 agreed overlap programme assumptions.

As in the final determination, we are not making any adjustments to the baseline in 2010-15 for Vyrnwy large diameter trunk main cleaning, Sandon Dock or Stockport nitrate vulnerable zone designation overlap schemes. However, there are changes from our final determination in relation to the logging up adjustment we have made for the company's Unsatisfactory Intermittent Discharge (UID) consolidated overlap programme. This is summarised below and explained in table A5.

Table A8 PR09 agreed overlap programme adjustments and assumptions (£ million)

		2010-15
		Two-sided adjustments for inclusion in the CIS
Water service	FD position	0.000
	Company BYR view	0.000
	Ofwat BYR	0.000
Wastewater service	FD position	34.037

		2010-15
		Two-sided adjustments for inclusion in the CIS
	Company BYR view	34.037
	Ofwat BYR	26.034

Any changes between our PR14 final determination and our final reconciliation shown in table A8 are implemented through the CIS.

3.6 CIS

Table A9 provides details of the CIS ratios and performance incentive. It also gives the monetary amounts of the CIS performance reward or penalty and true-up adjustments to allowed revenues.

Table A10 provides details of the RCV adjustments and quantifies the impact of this final 2010-15 reconciliation compared to the PR14 final determination position (updated for the indexation correction we decided to implement in February 2016).

In table A11 we summarise our interventions in relation to the company's CIS adjustments.

Table A9 CIS true-up adjustments

		Water service	Wastewater service	Total service
Restated FD09 CIS bid ratio[1]	FD position	94.138	110.042	n/a
	Ofwat BYR	94.138	112.584	n/a
Out-turn CIS ratio	FD position	92.221	105.975	n/a

		Water service	Wastewater service	Total service
	Ofwat BYR	93.888	108.804	n/a
Incentive reward/penalty (%)[2]	FD position	2.655	-1.535	n/a
	Ofwat BYR	2.082	-2.011	n/a
Reward/penalty (£m)	FD position	38.169	-34.408	3.762
	Ofwat BYR	29.986	-44.617	-14.631
Adjustments to 2015-20 revenue (£m)[3]	FD position	-17.020	-27.221	-44.241
	Ofwat BYR	-25.525	-37.021	-62.546

Notes:

1. The restated FD09 CIS bid ratio takes account of the adjustments for the change protocol (table A4) and the 2009 agreed overlap programme (Table A8).
2. The reward/(penalty) is adjusted for the additional income included in the 2010-15 determination and the financing cost on the difference between actual spend and capital expenditure assumed in the 2010-15 determination to derive the value of the adjustment to 2015-20 revenue.
3. The adjustment to 2015-20 revenue values shown in this table assumes a single year adjustment in the first year, and does not include the NPV profiling used for the final determination.

Table A10 CIS RCV adjustments (£ million)

	Water service	Wastewater service
FD position	-137.972	65.284
Impact of indexation correction	-88.784	-143.982
Corrected FD position	-226.756	-78.697
Impact of updated actuals	26.674	38.481
Ofwat BYR	-200.082	-40.217

The changes to revenue shown in table A9 and the impact of updated actuals for the RCV shown in table A10 above will be implemented through the PR14 reconciliation rulebook legacy blind year model at PR19, discussed in section 4. The indexation correction will be applied separately at PR19.

Table A11 Interventions on proposed CIS adjustments

Area of intervention	What we did at FD	Why we did it at FD	What has changed in BYR	What we have done for BYR and why
Methodology	We used the post-tax basis of the PR09 cost of capital for the discount rate when calculating the future value of the revenue adjustment in the 2010-15 period. We used our assumption of the cost of capital as the discount rate when profiling the revenue adjustment in 2015-20.	As explained in policy chapter A4 (PR14 FD), we changed the methodology in the CIS model to use the PR09 post-tax cost of capital as the discount rate. The company used its view of the discount rate (3.36%) when profiling the revenue adjustment over 2015-20.	Updated to reflect 2014-15 actual expenditure, RPI and COPI. The company's commentary repeats the June 2014 business plan erratum (ie there were inconsistencies with the 2013-14 regulatory accounts). We did not use the erratum details in the CIS calculations in the final determination. We considered the blind year update would be the appropriate time to take account of the erratum details when audited figures for both 2013-14 and 2014-15 would be available which we have now done. In response to a query, the company revised 2013-14 to reflect the required treatment of expenditure in the CIS and 2014-15 transition mechanisms.	We have used the company's revised data and have therefore not intervened.

Area of intervention	What we did at FD	Why we did it at FD	What has changed in BYR	What we have done for BYR and why
Change protocol adjustments	In carrying out our assessment, we included our view of the applicable change protocol amounts for water and wastewater.	We applied Ofwat's published methodology.	See section 3.2 and section 3.5 above.	See section 3.2 and section 3.5 above.
Data inconsistencies	We used the correct signage for the input PR09 bid grants and contributions.	The company had broadly applied the published Ofwat methodology. However, the company had input the PR09 bid grants and contribution values with negative signage. The model requires these to be input as positives. This signage error affected the RCV adjustment and revenue adjustment.	There has been no change since the PR14 final determination.	There has been no change since the PR14 final determination.

3.7 The 2014-15 transition programme

Table A12 confirms the company's proposed transition programme. There are no interventions in this area.

Table A12 Transition programme in 2014-15 (£ million)

Net capital expenditure	FD position	Company BYR view	Ofwat BYR
Water service	9.570	10.095	10.095
Wastewater service	28.056	15.874	15.874

4. Implementing the changes

Our PR14 reconciliation rulebook describes how we will implement the changes between our PR14 final determination and our proposals. This includes the application of the £10,000 materiality threshold to the aggregate of the revenue and RCM adjustments.

The PR14 reconciliation rulebook legacy blind year model draws together the RCM, CIS and serviceability shortfall adjustments applied in the final determination and from the blind year update, calculates the differences, performs the materiality test and preserves the present value of the blind year adjustments for those that will be implemented at PR19. Table A13 shows the output values from the legacy blind year adjustment model.

Table A13 adjustments to be implemented (£ million)

	Water service	Wastewater service
RCM revenue adjustment[1]	-8.721	-1.877
Total adjustment revenue carry forward to PR19	-10.150	-11.696
Total adjustment RCV carry forward to PR19	31.834	45.924

Note:
1. To allow companies to manage potential volatility in customer bills, we have given them the option of implementing the RCM revenue adjustment through WRFIM in either 2017-18, 2018-19, 2019-20 or in PR19. We expect companies' responses to this consultation to propose how they want RCM adjustments to apply taking account of customer interests.

The CIS RCV indexation correction is not included in the RCV carry forward in table A13 above because it will be applied separately at PR19 in accordance with the PR14 reconciliation rulebook (section 7.2 process for adjusting CIS for both indexation and the blind year).