

Meeting note

Friday 18 March 2016
10.30 am to 3.00 pm

Regulatory accounts working group (RAWG)

Water and Sewerage companies only

Attendees	
Phil Trussell	Anglian Water
Steve Riches	Anglian Water
Jean Thomas	Welsh Water
Sarah Heath	United Utilities
Richard Brindle	United Utilities
Mark Local	Northumbrian Water
James Maclean	Northumbrian Water
Rob McPheely	Severn Trent Water
Lee Musgrove	Severn Trent Water
Kim Williams	South West Water
Peter Hughes	Southern Water
Paul Kent	Southern Water
Lucy Aplin	Thames Water Utilities Ltd
Andrew Popple	Thames Water Utilities Ltd
Lee Derrick	Wessex Water
Ken Trussell	Wessex Water
Suzanne Carter	Yorkshire Water

Scope of meeting

In advance of Ofwat's next RAG consultation for 2016-17 being published we held a RAWG meeting for Water and Sewerage companies on 18 March 2016. We have scheduled another RAWG meeting for Water only companies on 23 March 2016.

We invited two representatives from each company, one attendee being our usual RAWG contact for each company, and another attendee from each company who is familiar with the practical/engineering processes around Boundary issues for sludge and water resources.

- Targeted review of sludge and water resources – background and scope
- Water resources: CEPA findings; Key changes to RAGs
- Sludge: CEPA findings; Key changes to RAGs
- Recharges between price control units: CEPA findings; Key changes to RAGs
- Other RAG changes: Transfer pricing disclosures; Arms length trading; Other changes
- Future RAG changes – Water 2020: Sludge; Water resources
- Future RAG changes – Water 2020: Other future reporting; Cost assessment

Key points from meeting to log for consultation document/ RAG amendments

- CEPA's report focused on companies' 2014-15 accounts.
- Ofwat's RAG consultation is for the 2016-17 reporting year (to be published end of March 2016). It will include proposed changes to RAGs, with a caveat that further changes may be applied to reflect Water 2020 decisions in the May document. A second RAGs consultation is possible if there are material changes from Water 2020.

Water resources

- Impounding reservoirs – A company asked if 'impounding reservoirs' referenced in the CEPA report should be all reservoirs. Ofwat confirms yes.
- Boreholes – A company asked if pumping heads is the right cost driver.
- Ofwat will include changes into RAG 2 and RAG 4 as per CEPA's report apart from a few items which Ofwat has rejected.
 - Labour and maintenance costs – this could be picked up through a 'Best practice guide' or in the 'methodology statement'
 - M&G asset allocation – choice of driver – Ofwat to do further work with RAWG in this area

- Definitions – Definitions that were defined in historic June return reporting requirements publications have been lost over time following the principles approach. We need to carry forward those definitions as a standalone document into future RAG publications.
 - Third party services - Definition of 'third party' in appendix 1 of RAG 4.
 - Bulk supply definition – of treated water, split between treatment and Water Resource cost.

Sludge

- Boundary issues - Ofwat will make changes to RAG 4 to clarify the boundary points. Note that this area is still in discussion for W2020. **Action: Ofwat to add a clarification in the RAGs.**
- Ofwat will include changes into RAG 2 and RAG 4 as per CEPA's report apart from a few items which Ofwat has rejected.
 - Treating waste from other WaSCs – this is a compliance issue. A company asked for clarification on this. Ofwat clarified that this is non-appointed as per RAG 1. It will only appear as appointed in one set of accounts i.e. the other WaSC would report it as appointed.
 - Co-located sites power costs allocation – Further work with RAWG. Ofwat states that we might need more robust wording on this.
 - Labour and maintenance costs – Further work with RAWG.
 - M&G allocation – principal user – this is a compliance issue.
 - M&G allocation – choice of driver - Further work with RAWG.
- Definitions – A company stated that the historic 'June return reporting requirements' definitions needs to be addressed in future RAGs.
- Liquor – not explicit how to allocate imported liquor between sludge and sewage. For imported sludge, 2014-15 → sludge; 2015-16 → sewage. Will require further work with RAWG for a consistent approach in the allocation between liquor and sewage.
 - ❖ A company raised several questions:
 - Liquor holding tanks/ balancing tanks (so that there is no spike in strength): unsure whether sludge, but majority of companies (& new entrants) would put this in sludge. Queried if can use the RAG 4 definitions on boundary points for sewage treatment and disposal, sludge, transport. Difficulties arise on co-located sites.
 - Metrics: liquor – BOD/COD/ammonia solids. does not think BODs is a reflective metric. Ammonia is what companies worry about – 50% of load at STWs.
 - Disposal boundaries - All assets related to disposal (e.g. dewatering, pumping stations) i.e. ready to leave the works to land or incinerators. Sludge disposal – transport to incineration, covered by disposal. Classification of incinerators could be to sludge treatment (for raw

sewage) or disposal (for sludge/treated sewage) . **Action: Ofwat to add a clarification in the RAGs.**

- ❖ A company raised several questions:
 - Power savings – requires consistency in the definitions in calculating this. It is the 'avoided cost' to use for the cost savings calculations. Use actual rates, actual weighted averages of sites/ regional rates.
 - Treating waste from other WaSCs – what about Mutual aid agreements (re: Water UK)? This is not mentioned in the Act. Appointed? This company charges it at the incremental cost, not considered material. **Action: Legal input required. RAGs principle – appointed asset for non-appointed business.**
 - Tankering (re: CEPA report) – vehicles transporting between holding tanks/ STW/ sludge. Clarity needed here. Sludge vs sewage – debatable, much simpler for accounting purposes.

Other RAG changes

Further guidance on Current cost reporting – Table 4G

- Table 4G line 3 – Capital maintenance charges

A company stated that the red text that had been added to the definition did not clarify the guidance enough. Another company provided an alternative way to explain it which was better understood by companies.

... the difference between IRE and IRC put into the capital maintenance charge. A proxy for previous CCD. Where CCD was IRC & IRE, but for IFRS, we are now expensing IRE (opex).

Action: Ofwat to work with SRN to produce an illustrative example to include in the RAGs. We will draft something for SRN to review and then test on TMS to check if it makes sense to them.

Further changes recommended by CEPA to be discussed

- Allocation of M&G CCD recharges – need to review materiality. One of the companies showed agreement re: cost drivers for land and buildings (L&B), perhaps allocate by FTE(?). Focus on the bigger asset groups and what's material to concentrate on what needs consistency.
- Co located site labour costs – One of the companies suggested to use 'management estimate' rather than the 'centralised robust process' wording.

However, there would be no consistency here. Ofwat suggests that a time-based approach is more appropriate.

- Co located sites power costs – Information is not available at the sub metering levels for some co located sites. Those who don't have them metered needs more information on this – working group level discussions required to work out the materiality of this. The long term view is to have meters in place once the boundaries are known. **Action: We need to pick this up with David Black/ Justine. RL to feedback to Alison rather than include this in the consultation document.**

Defining the Market: The boundaries around sludge and water resources

- A separate Sludge working group exists for further debates on boundaries.
- The potential boundary change options did not have the 'Return liquors' between STWs and Sludge thickening centres (STC).
- Not all companies have a STC.
- Measurement points have increased.
- Welcome company comments (re: definitions) for us to consider whether to include in RAGs, and can be forwarded to the sludge working group.

Other future reporting

- Data for cost assessment – not part of 2015-16, but intended for 2016-17 as part of the APR in the long-term. There will be Board sign-off for 2016-17.
- Metering – A company stated that there is an inconsistency between RAG 3 and RAG 4 re: metering (TWD). **Action: RAG 3 Tables are ok, but we need to update RAG 4.**

AOBs

- A company raised an inconsistency between the 2015-16 APR and the Data capture system re: calculation error in Table 4D and 4E. The F&G (Info) project team are aware of this and confirm that the error resides in the excel file only. The underlying files for Fountain are correct.