PR19 final methodology queries and answers 15 May 2018

A price review is when water companies and their customers create plans for the future that will deliver customers' wants and needs. Our role is to:

- set the framework and methodology;
- check and challenge the plans; and
- set out our decisions on the five-year price, service and incentive package for each company.

We have published our final methodology for the 2019 price review (PR19), setting out:

- our expectations and requirements for companies preparing their business plans to meet the needs of their customers from 2020 to 2025 and beyond;
- how these expectations form the basis for how we assess company business plans;
- the approach that we will use if we need to intervene in those plans to ensure that companies deliver the step change required by customers; and
- how our assessment will flow through into companies' price limits, service commitments and the wider incentive framework.

In the PR19 final methodology we stated that we will run a queries process until 31 March 2018 for specific questions about the methodology. We stated that if a query was raised which we think is relevant to other stakeholders then we will publish the query and our response on our website. This document sets out our response to the seventh set of queries and covers all of the queries that we have received on the PR19 final methodology during the formal queries process. We will publish an update to the business plan data tables on 18 May 2018.

Ref No.	Topic	Query	Response
4	Cost assessment	In section 2.1 (basis of financial reporting) of the ‘Final guidance on business plan data tables’, companies are instructed to apply 2017-18 RAGs for 2017-18 and all subsequent years. However, from 1 April 2019 all companies will be required to comply with the new leasing standard IFRS16. This standard requires that all operating leases are treated as finance leases, which means replacing operating cost charges with depreciation and interest, and bringing lease assets and debt onto the balance sheet. Does Ofwat recommend that companies should ignore the impact of this new standard when preparing their business plan submission from 1 April 2019 onwards?	We will issue further guidance separately regarding the reporting of operating leases by the end of May.
47	Form of control	In the Final Methodology, appendix 5, section 4.3.2, references water resources selling water to both retailers and network plus, with the sale to network plus covering losses of water. The revenue allowance for network plus would need to include an additional company-specific item to allow for the costs of buying this lost water from water resources. The example provided in box 4 of the appendix shows the level of water resources revenue	The water resources control will include revenues from the network plus payments to compensate for losses and under-recorded consumption (in the example the £4 million). These can be seen as a recharge. However we have not yet set out how the revenues will be reflected/or not in the network plus water control and this will be something to be confirmed in the PR19 rulebook and companies final determinations.

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		allowing for the compensation from network plus, but doesn't set out in detail how the network plus revenue is grossed up for these losses. Based on the example, if the cost allowance for lost water is £4m in water resources (to cover the costs of supplying the water to the boundary) and £4m in network plus (for funding the purchase of losses not charged to customers through the notional water resources charge) i.e. the same £4m appears in both cost allowances, where then is the grossing up/netting down adjustment made so that overall wholesale revenue across the company is "net"? This has implications for cost assessment as part of PR19 and for the expected PR19 Rulebook in terms of reporting performance against the separate revenue controls	That said, our indicative view is that revenues falling within the scope of the network plus control would be defined to exclude the revenues attributable to the recharge from water resources to network plus. Under this approach there is no need to include any allowance for the recharge for network plus losses as part of the determination of the network plus control. This brings practical benefits for the determination of the controls through the PR19 process and avoids the complications that could arise from including the recharge in the network plus control.
53	Outcomes / Cost assessment / Risk and return	Should the cost adjustment mechanisms for unconfirmed environmental requirements be included in the RoRE range for ODIs?	The cost adjustment mechanisms for unconfirmed environmental requirements are not performance commitments / ODIs and should not be included in the RoRE range for ODIs.
58	Outcomes / Cost assessment	Regarding funding the NEP - the final methodology states the anticipated NEP programme will be funded, as long as companies propose an appropriate cost adjustment	<u>Response to second paragraph</u> Page 29 of appendix 2 to the methodology statement states: "Companies have the freedom to

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		mechanism to account for a potential discrepancy between the scale of the assumed and confirmed programmes. Companies will be required to link expenditure for unconfirmed requirements to an outcome and a unit cost. Please can you clarify whether you intend for companies to incorporate the NEP as a performance commitment itself and include this in APP1 of the business plan tables? One interpretation could be that we include performance commitments that cover each unconfirmed element of the NEP. We are also unclear as to where companies should propose details of the related cost adjustment mechanism. Should this be consistent with the previous change protocol methodology? There are now a number of reconciliation and adjustment mechanisms, and it would be important to specify how this new one would interact with the existing ones. Within APP1 there is a column to state whether the performance commitment relates to the NEP - in part or fully. The intention of this column is not clear to us. Would it be possible to explain the intention of this column, and how 'relating wholly or in part to the NEP' should be	engage widely with their customers and local stakeholders, to propose bespoke performance commitments that reflect their customers' particular preferences." The PR19 methodology does not require companies to include the NEP (or WINEP for England) as a performance commitment. The references to unit cost adjustments in the PR19 methodology relate specifically to the unconfirmed elements i.e. those lines within the spreadsheet that are coded 'Amber' and which represent a minority of the programme. Please see our response to query 17 (batch 4 of queries 15 March 2018 https://www.ofwat.gov.uk/publication/final-methodology-queries-answers-15-march-2018/) for further information on our expectations regarding unit cost adjustments. <u>Response to third paragraph</u> Companies are free to propose any performance commitments that they consider which reflect companies' commitments to deliver against their customers' preferences for service levels. However, with regard to the NEP (or WINEP for England) the references in the final methodology to outcomes and associated unit cost adjustments relate specifically to the unconfirmed elements i.e. those lines within the spreadsheet that are coded 'Amber' and which represent a minority of the

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		understood and interpreted? This may depend on the answer to the questions above.	programme (e.g. about 14% in England). Please see our response to query 17 batch 4 of queries 15 March 2018 https://www.ofwat.gov.uk/publication/final-methodology-queries-answers-15-march-2018/) for further information on our expectations regarding unit cost adjustments. We are not expecting companies to include details of their proposed cost adjustment mechanisms in their performance commitment information in Table App1. Instead they should set this out in a readily identifiable section in their business plan commentary or an appendix. <u>Response to fourth paragraph</u> The column on the NEP in table APP1 is one of five columns that help us classify performance commitments when analysing them. A company can propose a bespoke performance commitment that relates to delivering an improvement in the environment which is related to the NEP, but which is not a cost adjustment mechanism e.g. a commitment to customers to improve the length of rivers improved.
70	Form of control	Our query relates to the Final Methodology – specifically appendix 7, chapter 4, 4.1, page 29.	Developer services costs will form part of wholesale totex for the purposes of setting the relevant

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		In the final part of the worked example of the developer services (DS) revenue adjustment mechanism it states that, "We will not apply cost sharing rates to developer services activities. This provides a strong efficiency incentive to lower average costs of providing new connections." It would be helpful if Ofwat could confirm how allowed developer services costs (net of income) will be treated at PR19, including: Whether DS costs (net of income) are part of wholesale totex within the relevant wholesale price controls, and; If so, whether differences between actual and allowed totex which relate to DS activities are to be included in operation of the totex cost sharing mechanism for AMP7? If such costs sit outside totex, or outside the cost sharing mechanism, please confirm how they will be classified?	wholesale price control, but totex sharing rates will not apply to developer services activities. The methodology set out our proposed approach to apply a revenue reconciliation at the end of the period, for difference between actual and expected volumes of developer services activity. We will apply incremental revenue drivers for an incremental change in the volume of developer services activity. In broad terms, if volumes are greater than anticipated, the revenue adjustment will give additional revenues needed to fund the expected additional costs (through grants and contributions and other wholesale charges). However, if actual totex associated with providing developer services differs from the expected level given the volume of activity observed, we will not apply sharing rates to this difference. This is intended to preserve the efficiency incentive on companies. The detail of how we will apply this to different types of developer services provided is described in appendix 7 of the methodology.
76	Cost assessment	Given the tight definition of network reinforcement that we have applied through implementing the new charges, this will reduce	We intend to undertake totex efficiency modelling on gross basis (i.e. including developer

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		the amount of contribution received from developers to offset expenditure investment in our network. We are keen to understand how this will impact on the PR19 totex modelling. If the contributions from developers are deducted before the efficiency modelling then, any company which has followed a tight definition of network reinforcement, will look inefficient compared to other companies. We would therefore be keen for any totex efficiency modelling to be undertaken on gross totex and developer contributions deducted afterwards. On a separate note, when we discussed the new charges we talked about the increase in costs for new mains and it being related to the success of self-lay within our region. Ofwat asked us whether the price rise was just on contestable work rather than across both contestable and non-contestable work. I can confirm that our charges for non-contestable work are in fact coming down slightly and the increase is in the contestable elements, reflecting the fact that the work which we now deliver is generally more complicated and costly work, with self-lay providers completing a lot of the off-line new development mains.	contributions) and deduct developer contributions when setting an efficient allowance.

Ref No.	Topic	Query	Response
161	Cost assessment	We included new costs relating to an investment in a CRMB system in our PR14 retail business plan. Ofwat agreed to approve these new costs in its Final Determination, and, in doing so, it considered that we had demonstrated the need for this system and the robustness of cost estimates (implying that this investment was deemed efficient). Ofwat's retail HH model reports that we were allowed a depreciation figure (not included in RCV and based on a 10 year asset life, i.e. spanning more than one control) that was very close to the CRMB-related depreciation we had forecast for the same period. This strongly suggests Ofwat, in approving these new costs, had in mind that we should be allowed to recover our efficient CRMB depreciation to a very large extent. We have made good progress in delivering our CRMB system. It is currently being tested and our customers will be migrated to this system (in waves) over the next years. An implication of this on-plan investment is that we will continue to depreciate our efficient CRMB investment over AMP7. In fact, we plan to depreciate this investment to a very large extent over this period.	The PR14 retail control was set on a totex basis. Companies were allowed an efficient cost to serve, which included efficient depreciation on PR14 capex investments. We will not automatically allow costs in PR19 on grounds that it is depreciation of investments made at PR14. Companies will be able to fund efficient capital investment from the efficient allowance provided by our cost models. Companies can raise a cost adjustment claim for unique or atypical material costs that they consider are not reflected in our cost baselines (in line with guidance issued in our PR19 Final Methodology document, see section 9.4.5). Table R1 has been updated so that companies are required to separately report depreciation on assets acquired during the PR14 period (versus depreciation on assets planned for PR19).

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		We understand Ofwat's approval of these costs in PR14, and its confirmation of CRMB investment being efficient, to mean that we should be allowed to recover efficient CRMB depreciation over time, including in PR19. It would be consistent with this understanding if Ofwat were to add our efficient CRMB depreciation to the efficient retail cost allowance determined by Ofwat's benchmarking. It is not clear to us from reviewing the Final Methodology and the data tables how Ofwat intends to allow companies to recover costs that were approved for (full) recovery in PR14 and extend into PR19. One way to accomplish this would be for us to submit efficient CRMB depreciation over AMP7 as a cost adjustment claim (aka special factor case). Please could you clarify the mechanism that you have in mind to allow recovery of new costs that you approved in PR14 and that extend into PR19? If the intention is that we should provide a cost adjustment claim we need early clarification of this so that we can meet the 3 May 2018 deadline for providing outlines of such claims.	
163	Data tables	Would it be possible to clarify our interpretation of the calculation in table APP9:	The formula is correct. In the first year (2014-15) the calculation looks at the difference between the

Ref No.	Topic	Query	Response
		Lines 3 and 14 calculate the impact of 50% of the sales proceeds for the years, which are shown in lines 2 (water) and 13 (wastewater). However, for the first year on the table, the formula is calculating 50% of the total of actual and current forecast sales (lines 2/13), less the forecast at previous review (line 1/12). Is this correct? By doing this for the first year in question, we are effectively calculating 50% of the difference between the actual proceeds for the year and what we forecast for the year. This maybe what is required, but the guidance is not clear as it only states to calculate half of the proceeds from land sales, therefore implying 50% of line 2/13 only.	amount forecast at the last price review (already adjusted in the RCV) and the actual amount of proceeds. That way the RCV is corrected for the previous forecast-based adjustment.
180	Data tables	Exact duplicate of query 163 above.	See response to 163 above.
197	Data tables	Re table WS13: The ‘revenue forecast error’ calculated in line 20 does not compare ‘Allowed Revenue’ and ‘Revenue Recovered’ on a like for like basis. Revenue Recovered, as calculated in line 19, excludes revenue for non-potable water (reported as third party revenue in table 2I of the Regulatory Accounts) and also capital	We agree that the calculation is incorrect. The table should be fully aligned with the WRFIM model and table 2I of the APR. We have changed tables WS13 and WWS13 to: • align with the revenue recovered lines in block E with APR table 2I so that it includes third party revenue and grants and contributions; and

Ref No.	Topic	Query	Response
		contributions from connection charges and revenue from infrastructure charges covered by the price control. However, Allowed Revenue (line 12) implicitly includes both items. The Allowed Revenue used (line 12) does not include the adjustments made in respect of the RCM blind year adjustment and any applicable WRFIM adjustment. The RCM and WRFIM adjustments are incorporated when setting charges for any one year, and therefore are part of the actual/forecast revenue. This therefore leads to a comparison of actual and allowed revenue which is not on a like for like basis, and is not in line with the WRFIM calculation or the reporting in table 2I of the Annual Performance Report. We recommend that the comparison is amended in respect of the points above to ensure that forecast and actual revenues are compared on a like for like basis.	• remove the forecast error line from the table. We have included these changes in the updated version of tables WS13 and WWS13 issued in March 2018.
199	Data tables	Exact duplicate of query 197 above.	See response to 197 above.

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200	Data tables	Table App24a asks for two things in relation to residential retail depreciation: the input price pressure (line 23) and the assumed efficiency gains (line 47) for FY21-FY25. Both are requested as a percentage change relative to the year before. As historic cost depreciation is based on spend in previous years, it is unclear how this value could be affected by future input prices or future efficiency. Should these lines be removed from the table?	These lines should not be removed. The word 'depreciation' should be changed to 'capital expenditure'. We have amended this in table App24a. Input price pressure and ongoing efficiency could affect depreciation on future investment.
250	Cost assessment	In January, we raised with Ofwat the issue of principal business unit in the context of allocating capital costs. Ofwat responded on 15th January at query 12 of the methodology queries and answers (see link: https://www.ofwat.gov.uk/publication/pr19-final-methodology-queries-answers-15-january-2018/). The response was that the query we raised does not apply. However, we do not believe that the potential cost assessment issues that may arise from a principal unit methodology have been addressed, and to illustrate the point we have set out an example below: <u>Example</u> Assume that one of the WOCs is almost identical	As we have previously explained, in terms of charges between business units (e.g. water resources to network plus) RAG2 clearly states (in Section 4.1) the methods that companies should follow. This should ensure there is no cross subsidy between price controls. The revenues that we derive when we set prices will use, as a basis, cost information that is reported on the same principal use basis. We attach a worked example using your figures. This shows that from an accounting perspective the result is comparable. However we accept that, if you look at a 'line' in isolation and conduct any sort of efficiency analysis, then you could draw different conclusions. See worked example at the end of this document.

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		in scope/size/botex during AMP6 as the water services business unit of a WASC, but where the WASC in question has sewerage as its principal unit. Both organisations plan a new IT system from the beginning of 2024/25. The WOC's investment is planned at £20m and the WASC at £50m. The share of the WASC investment notionally attributable to its water services is £20m. Both systems depreciate over 5 years. The WOC's botex in year 5 of AMP7 will be £20m with depreciation of £4m. The WASC will have sewerage botex of £50m with depreciation in its water services unit of £4m. Water botex will be unaffected. The year 5 botex needs of the WOC and the WASC's water services BU will not be comparable (even though they are, in effect, the same). Depending on the cost models, the WOC will appear relatively inefficient compared to the WASC (for delivering its water service).	

Ref No.	Topic	Query	Response
		Attributing capital costs based on causality would remove this problem. Both botex and depreciation will be reflected in the appropriate business unit Our view remains that totex needs by price control may not be adequately reflected and that cross subsidy may result	
251	Data tables	Re data table R3, row 16. The notes ask for the following: “Forecast assumption to indicate the in-year collection rate i.e. the percentage revenue expected to be collected each year during the PR19 period. For consistency this should be based on the assumed level of revenue collected within the year as a percentage of total bad debt charges raised in the same year. Where companies do not hold revenue outstanding data for 2018-19 at the time of submission, an assumed percentage of revenue collected in 2018-19 can be entered.” What is the definition of revenue collected? Does this mean: • revenue collected only in relation to revenue raised during that year/total revenue in year; or,	We have clarified the definition in table R3. Line 16 should be, “Total revenue recovered in the year (including revenue in respect of bills raised in prior period) divided by total revenue allowed in the year”.

Ref No.	Topic	Query	Response
		• Is it total revenue collected in the year (including revenue that was billed in prior periods)/revenue in year? Further, we do not understand the definition for row 16, where it says, "………..as a percentage of total bad debt charges raised in the same year." If the bad debt charge is the denominator, the definition of revenue collected is still required.	
256	Risk and return	We have a query about price base of RCV in gearing calculations. The RCV used in the gearing calculations is calculated in year average prices, rather than at year end prices (see for example Analysis_Water_Resources row 162). This is therefore on an inconsistent price base with the net debt (which is in nominal prices at the end of the year, rather than year average prices), and is also inconsistent with how gearing is calculated for e.g. financial covenants, rating agencies, and the APR definitions: For example: APR definition for row 1E.7, Gearing: "Regulatory gearing calculated as net debt in 1E.6 divided by RCV in 4C.5". APR definition for 4C.5, RCV determined at FD at 31	This issue was raised in the July consultation. The current process mirrors the approach taken at PR14. As such we do not propose to amend the model. Please see query reference TMS-75 in the December 17 financial model.

Ref No.	Topic	Query	Response
		March: "RCV at 31 March per the 2014 price determination inflated using the March RPI – as published on the OFWAT website annually in April". Would it therefore be more appropriate to calculate gearing in line with the calculation used in the APR, using the RCV in year-end prices? When the model is notionalised, the level of debt is currently set using the gearing calculation using year average, rather than year-end prices. This could therefore distort the debt levels assumed in the notional structure, affecting all financial ratios.	
262	Data tables	In Table Wr1 (Wholesale Water Resources - Explanatory Variables), there does not appear to be a line to capture water reuse schemes. We have a new scheme where water is redirected from Water Recycling Centre discharge to Water Treatment for non-potable supply. We have currently not included it as a new water resources source, and instead captured it as an additional raw water pumping station. Please could Ofwat advise if this is assumption is correct, or if not, how and where these schemes should be captured?	We would not expect a scheme supplying non-potable water to be recorded as part of distribution input. We have added lines to table Wr1 to capture the amount of water supplied from reuse schemes and the number of reuse schemes in operation.

Ref No.	Topic	Query	Response
264	Performance commitments	In relation to the definition on Performance Commitments – we raised a query earlier about whether the PC definition should actually include the explanation of ODI types. Can you please confirm if rows 16, 17 and 18 need to be included in the May submission fully assured, or whether they should be subject to completion of assurance? We had assumed that ODI definitions were not within the scope of the May PC definitions submission.	Please see the response to query 34 published on 22 February 2018 (https://www.ofwat.gov.uk/publication/pr19-final-methodology-queries-answers-23-february-2018/).
265	Financial modelling	In June 2017 we completed a restructuring project regarding a number of our financial derivatives – being in relation to a proportion of the company's index linked (floating rate to RPI) swap portfolio (note that these swaps are not part of a designated hedging arrangement). One outcome of this restructuring project is that we will now receive a fixed amount of £19.4m per annum for the next 17 years from (and including) the 2017/18 financial year. However, the swaps to which the £19.4m is related to differ in both notional value and maturity date in each year that the £19.4m is receivable (not withstanding that in	Companies should report negative interest rates where income is receivable from financial instruments such as swaps. Where the notional amount which the interest rate depends on is not the same as the notional value, column L should be used to report what this notional amount is. As the swaps to which the £19.4m are related differ in notional value and maturity date over time, but always amount to £19.4m, the income should be reported as a separate instrument with a negative interest rate indicating its relationship to the portfolio of swaps. As the data is for year ending 31 March 2018, please report data as required by the reporting guidance as at 31 March 2018. Where

Ref No.	Topic	Query	Response
		total we will receive the same amount of £19.4m every year until 2032). Please could you provide guidance on how the above should be reflected in table App20?	appropriate, we would welcome commentary of this nature reported with the data.
266	Cost of debt / data tables	We have entered into two 364 day liquidity facilities which are forecast to remain undrawn during their term. Both facilities attract a fixed rate commitment fee based on the amount of the facility undrawn. For example: Debt Service Reserve facility of £189m with a commitment fee of 0.6% per annum equals an annual cash interest payment of £1.134m. Please can you provide guidance on how this should be shown within table App20 -cost of debt / analysis of debt table.	Companies should use column L of App20 ('Amount used...') to record undrawn amounts which inform fees for liquidity facilities, with the annual % fee applied to the undrawn amount used as the interest rate. They should add another line for the same instrument where drawdown has occurred, recording the drawn down amount in column K ('Principal sum'), and the relevant interest rate which applies.
270	Performance commitments	I was wondering if you could provide some more clarification and further explanation on what you are expecting to be included under the ‘mitigation / exceptions’ heading for the performance measures.	We are not providing any further information on what ‘mitigations' or 'exceptions’ mean.

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272	Data tables	Can you confirm the sign convention you want us to adopt for App19? Should the opening balances (lines 1-3) be entered as credits?	The opening balances should be entered as a positive, we will amend the table guidance to clarify this in the next publication of the data tables.
274	Performance commitments	Ofwat have set a challenge for companies to achieve industry upper quartile performance on a number of measures. On the enhancement tables WS2 and WWS2 there are no lines identified for the investment required to meet this, specifically in relation to interruptions to supply (customer minutes lost) and wastewater pollution. Can you clarify which lines this investment should be allocated to?	Please see response to query number 79 (https://www.ofwat.gov.uk/publication/pr19-final-methodology-queries-answers-23-february-2018/)
276	Retail	Please could you provide clarification of what revenue we need to include in the calculation of line 16 of the R3 table 'Percentage of revenue collected each year.' Should this be based on total revenue received in the current year (including the collection of revenue relating to prior years), or just total revenue received in the current year which relates to revenue billed in the current year?	See response to query number 251 published above.
277	Financial modelling	Our query is about the financial model: straight-line depreciation calculation for additions.	At PR14 companies had the option to choose either straight line or reducing balance depreciation of RCV balances.

Ref No.	Topic	Query	Response
		The calculation of RCV additions depreciation using the straight-line method (e.g. water resources row 1013) is based on the non-PAYG totex over the full forecast period (e.g. Water Resources F1010). When the model is also being used to consider AMP8, i.e. a 10 year forecast period, this makes the depreciation in AMP7 dependent on the AMP8 non-PAYG totex. Would it be more appropriate to just reflect the non-PAYG totex within each AMP for the depreciation of additions?	We have preserved these options, but have now moved to run-off rates that vary year-by-year that will allow users to calculate appropriate RCV run off. If run-off rates vary year-by-year then there becomes very little distinction between straight line and reducing balance depreciation. The model has been coded to try and preserve a distinction. Companies should consider which functionality in the financial model they wish to use for the depreciation of RCV (reducing balance or straight line). Regardless of which method they select, companies are expected to provide commentary on the run-off rates they use in their business plan.
278	Data tables	Our query is about data tables / financial model: run-off rate for additions. Data tables WN4 and WWN6 do not have a separate section for the run-off rate for post-2020 investment. This is inconsistent with the corresponding data tables for water resources (Wr4), bio resources (Bio5) and the dummy price control (Dmmy8), which all have an additional Section C "post 2020 investment run off rate".	As per the methodology the water network + and wastewater network + controls have a run-off rate that covers all CPIH based RCV (including post 2020 additions). The water resources, bio resources and dummy controls have separate run-off rates for post 2020 non-pay totex and opening CPIH indexed RCV. The model has been designed to replicate the structure of the business plan tables.

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		Should WN4 and WWN6 have a similar structure to e.g. Wr4? Similarly, the financial model does not currently use separate inputs for the run-off rate for additions (e.g. InpActive row 617 "run-off rate - RCV additions - active - WWN" and InpActive row 615 "Run-off rate - CPI(H) - active - WWN" both draw their inputs from F_Inputs row 181 "Total RCV run off rate to be applied ~ wastewater network plus CPI(H) linked").	Companies are expected to use a weighted run-off rate for the CPIH linked network + RCV balances. Companies are expected to provide commentary on the run-off rates they use in their business plan.
288	Company bid assessment framework	Re section 4.1.1 of the methodology – avoiding conflicts of interest. The guidance states that an incumbent's associated company should not participate in the bidding process for water resources. We would like clarification if this precludes associated appointed water companies from participating in the bidding process too? A strict interpretation could prevent two appointed water companies participating in a trade if they were related.	We have said in our final methodology, that we expect incumbents to take appropriate measures to prevent, identify and remedy any conflicts of interest arising from the procurement process, to avoid distortion of competition and ensure equal treatment of all bidders. In the final methodology we said that one important aspect of this is that an incumbent's associated company (as defined in condition A (interpretation and construction) of the incumbent's licence), if any, should not participate in the bidding process. However, in exceptional circumstances, such as this (where the associated company is another appointee), we may relax this rule, if the company concerned can justify this and explain what measures they will put in place to prevent and

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			remedy any conflict of interest issues which could arise as a consequence. We note that all appointees are under a licence obligation to ensure that every transaction between the Appointed Business and any Associated Company is at arm's length (so that neither gives to nor receives from the other any cross-subsidy).
290	Data tables	Re table: water resources and bio resources / row: 1019. The model assumes that additions are acquired at the end of the year rather than during the course of the year resulting in no depreciation being calculated in 2021. As companies are likely to acquire assets throughout the year we want to know if it would be appropriate to assume that at least half a year's depreciation will be incurred in year 1?	We agree that depreciation should have been calculated in the year of acquisition. We have subsequently amended this in the version of the model published in March 2018.
291	Data tables	Re table: water resources, water network, sewerage network and bio resources, retail_residential / row 104: The methodology states that for the reconciliation of the residential (household) retail revenues, the adjustment will apply to the residential retail control. The model is currently applying the adjustment to the wholesale price controls rather	There is functionality in the financial model to apply revenue adjustments to residential retail (see InpOverride'!$E$1272). Companies should use this to make the residential retail revenue adjustment from the PR14 reconciliation rulebook.

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		than residential retail. Can you confirm if this is right?	
293	Financial modelling	Re table: appointee / wholesale: As part of the 2016 budget, the Government announced that the start date for companies with annual taxable profits over £20m, to make payments four months earlier than currently, would be deferred to apply for accounting periods beginning on or after 1 April 2019. For a 12 month accounting period, these companies will have to make payments in months 3, 6, 9 and 12 of the accounting period to which the liability relates. This means that from 2021, the model should be assuming that corporation tax due in the year will be fully paid in the year. Can you please confirm if this is right?	We have developed the mode to run with tax fully paid in year, as such we do not propose to amend the model.
294	Data tables	Re table: residental_retail / row 54: The formulae currently calculates the residential proportion of wholesale revenue requirement less third party revenues. This means that the retail margin is being calculated on the correct base, but wholesale allowed revenue is not (as per our earlier query).	We agree that this was incorrect and has been amended in the third party revenue dedicated from both wholesale and retail. This has been amended in the version of the model published in March 2018.

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		It is not clear why third party revenues would be deducted for the purpose of the retail margin alone. Is this right or should the third party revenues be deducted from wholesale revenues?	
295	Data tables	Re table: residental_retail / row 93: While the SIM is being used in calculation of the retail net margin, it does not appear to be feeding through to residential retail service revenue. Residential revenue will therefore be understated if a SIM reward is assumed or overstated for a SIM penalty.	We agree that this is currently missing from the calculation and will be added to calculation block 'Residential retail service revenue - nominal' in the next version of the model.
296	Data tables	Re table: wholesale global / row 125: We think that the calculation at row 125 does not result in the correct value of wholesale charge being applied to retail residential because it is a simple average rather than a weighted average. To calculate the correct value, we think the percentage inputs in F_inputs would need to be applied to the revenue from each control, then the total retail portion summed up. The calculation at present means that the wholesale revenue used in retail residential is not equal to the sum of the parts.	We agree that the simple average should be amended to a weighted average calculation. This has not been amended in the March 2018 version of the financial model but will be amended in a future version.

Ref No.	Topic	Query	Response
297	Data tables	Re table: F_inputs / row 188: The line is unused and is a duplicate of row 186.	The formatting of F_inputs should reflect where companies are required to add inputs. Due to changes in the model some inputs are no longer required. The formatting will be amended in the model to reflect the latest structure.
298	Data tables	Re table: F_inputs / rows 183 to 188: 2025-30 column is highlighted for inputs but the cells are unused.	The formatting of F_inputs should reflect where companies are required to add inputs. Due to changes in the model some inputs are no longer required. The formatting will be amended in the model to reflect the latest structure.
299	Data tables	Re table: F_inputs / rows 220-233, 235-252, 256-266: The relevant cells requiring inputs have not been highlighted.	The formatting of F_inputs should reflect where companies are required to add inputs. Due to changes in the model some inputs are no longer required. The formatting will be amended in the model to reflect the latest structure.
300	Data tables	Re table: F_inputs mapping / row 63 - 66: Inputs are not required for years 2021 to 2025 as the debtor and creditor balances are calculated using the debtor and creditor days.	The formatting of F_inputs should reflect where companies are required to add inputs. Due to changes in the model some inputs are no longer required. The formatting will be amended in the model to reflect the latest structure.
301	Data tables	Re table: F_inputs mapping / row 115:	The formatting of F_inputs should reflect where companies are required to add inputs. Due to changes in the model some inputs are no longer

Ref No.	Topic	Query	Response
		For this line, only the closing cash balance for 2020 is required as an input, but the file shows inputs are required up to 2025.	required. The formatting will be amended in the model to reflect the latest structure.
302	Data tables	Re table: F_inputs mapping / row 115: For this line, only the closing cash balance for 2020 will be required as an input.	The formatting of F_inputs should reflect where companies are required to add inputs. Due to changes in the model some inputs are no longer required. The formatting will be amended in the model to reflect the latest structure.
304	Data tables	Re table: water resources, water network, sewerage network and bio resources / row 1542: Using the same logic as used at PR14, the tax adjustment for pensions is calculated as cash contributions excess over the charge (sourced from table App22) less pension deficit allowance. We think the current approach might be incorrect, as it results in removing the full tax benefit that a company would receive for paying the projected contributions, (which would include the deficit allowance) in table App22. This results in the tax allowance being higher than in reality it will be.	We have reviewed this query and as it is the same approach as taken in PR14 we do not propose to make any amendments to the model.
305	Data tables	Re table: sewerage network and bio resources / row 1403:	We agree that this is incorrect and have amended the formula to be consistent with the price controls in the version published in March 2018.

Ref No.	Topic	Query	Response
		We think the formula is incorrectly referencing the positive version (line 1397) of the repayment line rather than the negative version (line 1398) as is being done in the water network and water resources worksheets. This results in the allocation of the repayment of floating rate debt to be inconsistently allocated between the price controls.	
306	Data tables	Re table: water resources, water network, sewerage network and bio resources / row 1213: The model requires the opening fixed rate debt assumption to be input in 2019, but the formula logic for this line requires a fixed rate debt input in 2020. Can you please clarify?	The formatting of F_inputs should reflect where companies are required to add inputs. Due to changes in the model some inputs are no longer required. The formatting will be amended in the model to reflect the latest structure.
307	Data tables	Re table: residential retail / rows 187 - 188 and 195 – 196: The weighted average days, used in the calculation of both the unmeasured and measured charge proportions, only references the % inputs for water resources and wastewater network. In addition, the % inputs being used in the calculations will result in allocating a higher proportion of the wholesale charge to the residential control because the % inputs are based on the % of the total wholesale charge.	We will amend the model in respect of the changes identified in query 296 above.

Ref No.	Topic	Query	Response
308	Data tables	Re table: residential retail / rows 189 and 197: The labels incorrectly state that these lines are nominal.	We agree that this is incorrect and we will amend the label name in the model.
309	Data tables	Re table: residential retail / rows 222, 223 and 229: We think weighted average debtor days are being overstated because they are calculated as debtor balance multiplied by revenue divided by revenue. We think the correct calculation for deriving debtor days is debtor balance divided by revenue multiplied by number of days as calculated in the FBP data table A13.	We agree with the comment and will amend the model to be calculated in the same approach as App13.
310	Data tables	Re table: wholesale / row 102: The model assumes that a half year dividend is paid in the year with the other half the following year. Although the model does allow for an input value for the 2019/20 dividend, the calculation logic does not bring forward the dividend resulting in the 2020/21 dividend not reflecting a full year's payment. This results in overstating the	The model allows for the % of ordinary dividend paid as interim dividend to be adjusted in InpOverride (row 883- '% of ordinary dividend paid as interim dividend (post override)'). In addition to this users can also input the ordinary dividend in as a £m input in InpOverride. As such we do not propose to make any amendments to the model in this instance.

Ref No.	Topic	Query	Response
		cashflow, understating debt and interest, thus affecting allowed revenue which will include an overstated tax allowance.	
313	Data tables	Re table: residential retail / row 462: The implied capital spend for retail is calculated by multiplying allowed depreciation by the average asset life for retail assets. As the allowed depreciation input includes depreciation on "assets post 2015" (i.e. including assets constructed between 2015 and 2020), simply multiplying by the average asset life will overstate the projected capital expenditure over AMP7. The overstated capital spend line is being used in cashflow as well as the calculation of the RCF to capex (worksheet 'Analysis_Appointee', row 275) metric. In addition, the use of an average asset life in this way will be materially inaccurate - using an average life for all capex in one year will tend to understate depreciation in the early years and overstate it in later years (when short life assets will be fully depreciated). This calculation does not simplify matters - it would be preferable to simply include an input for the relevant capex.	We will amend the model to use an inputted value for retail capex.

Ref No.	Topic	Query	Response
314	Data tables	Re table: analysis_appointee / row 276: The capex line flowing through cashflow and used in the calculation of the RCF to capex metric is not being adjusted for the movement in capital creditors. Instead the movement is being reflected through the change in trade creditors and other payables. The RCF to capex metric is currently returning a ratio lower than it otherwise would be.	This approach is similar to that used at PR14, and whilst the comment is technically correct, we do not feel it should have a material impact on the results. We therefore do not propose changing the model at this stage.
316	Form of control / design	Please provide further clarification on water company requirements regarding wastewater planning in PR19. Specifically: • The 25 Year Environment Plan states (p96): "We expect companies to provide robust and transparent plans for the 2019 price review using the available outputs from the Water UK-led 21st Century Drainage Programme and the emerging long-term planning methodology for drainage and wastewater management plans." How is this going to be translated into PR19 in practice? • Is Ofwat asking companies to follow the outputs of the 21st Century Drainage Board DWMP (Drainage & Wastewater Management Plan)	The 21st Century Drainage Programme is making its early conclusions available to the companies. This means that their approach in PR19 will be more consistent, and better informed, than previously. Because the 21st Century Drainage Programme work is ongoing, companies may make different use of the outputs to date. We will be looking to see which companies really stretch themselves to do the best for customers and the environment. In some cases, a company may have access to better information on risks and we would expect them to use that if it takes them beyond what is already possible with the 21st Century Drainage Programme work.

Ref No.	Topic	Query	Response
		project, or not necessarily – if they take a “risk-based approach” to wastewater planning? • What does a “risk-based approach to wastewater planning” actually mean? • The methodology mentions a system-wide approach, but what about a long-term approach, as advocated by the 25 Year Environment Plan?	
319	Past Delivery	I have been completing the totex menu legacy model, relating to PR14, in order to estimate the impacts for PR19. We currently are forecasting an underspend on our totex, which will result in a reward from the totex menu mechanism. However, the reward does not offset the underspend, so the impact for PR19 will be a reduction in the RCV and a reduction in the allowed revenue. (Split via PAYG) Intuitively, it seems as if we will be getting a revenue penalty for our totex underspend, which will be applied against the allowed revenue in PR19. Is this correct? Previously, the CIS mechanism meant that any capex underspend was applied to the RCV and the reward was applied to revenue.	The approach to totex reconciliation is set out in the PR14 reconciliation rulebook and associated spreadsheets. We will discuss the approach with the company in question.

Ref No.	Topic	Query	Response
		I might need to make sure that I have populated the totex menu model correctly, and to check that the output in 'totex menu adjustments' is before the customer share % has been applied. Could someone please call me, and I can talk this through with them.	
324	Data tables	Re App23 / rows 14 and 28: These rows ask for "financial year end assumed percentage increase" for RPI and CPIH. But this information is a duplicate of rows 13 and 27 (which are then used to calculate a % year-in-year change of year end inflation in rows 34 and 37). We would suggest deleting the rows?	We agree that the lines 14 and 28 can be deleted as these will be the same values as lines 34 and 37.
325	Data tables	Re App23 / row 39 and 40: These rows ask for the long term inflation rate. Are you asking for the assumed rate for years beyond 2030, or an annual assumption for years 2021 to 2030? If the latter is this information not already available in the rows above?	We agree that this information is already available in the rows above. These rows can be deleted.
328	External communications	Re table WS18 / row 4:	To clarify the basis of reporting, we have removed the reference to Discover Water for this line (and

Ref No.	Topic	Query	Response
		The definition refers to "in accordance with information provided for Discover Water", but I don't believe we supply information on number of customers receiving support with their bills for publication on Discover Water. To ensure consistent interpretation we suggest the definition refers to customers on a company's social tariff and on Water Sure (therefore excluding Water Direct or other payment support options).	the equivalent line in table WWS18) as this was slightly misleading in the context of this information.
329	Data tables	Re table R8 / row 2: For companies that have exited the retail market row 2 will be left blank and therefore the "validation flags" will always show up as "no, check table".	We have built in validation flags that are appropriate for those companies that have exited the retail market.

Ref No.	Topic	Query	Response
330	Data tables	Re PR19/YKY/020/ table: App19 - debt and interest costs / line block B / line name: interest rates and financing costs. We have a request for clarification on guidance and data definitions. The table guidance states that: “This table should reconcile to the borrowing figures entered in App12 and should exclude any amounts which have been reported as derivative financial instruments”. However the guidance goes on to say: “Companies should enter the cash interest rate that reflects what they pay on their debt”. Please can you clarify if block B – interest rates and financing costs, should exclude the effect of index linked swaps that are not part of a designated hedging arrangement?	Please see the response to query 421 published below.
334	Data tables	Re table R3 / line 16: Please could you clarify the comments on line 16 of the data table? Do you require us to forecast an overall annual collection rate as a % of annual revenue i.e. taking into account collection of aged	See response to query 251 published above.

Ref No.	Topic	Query	Response
		debt from prior years? Or should we report the collection rate for the first year of billing?	
337	Data tables	In the calculation of average of RCV post 2020 additions – WR - nominal (and likewise for WN, WWN and BR) on 'water resources' line 1114, the closing balance is subtracted from the opening balance. This results in a negative average RCV balance, which in turn gives a negative return on capital on RCV additions. It would seem reasonable that the calculation of the average of RCV post 2020 addition should work in the same way as the average of RCV - CPI(H) + RPI wedge bf - WR – nominal (line 982) and average of RCV - CPI(H) bf - WR – nominal (line 848), both of which take the average of the balance at the beginning of the year, plus indexation and the balance at the end of the year (after indexation and run-off). The formula in line 1114 could be corrected with = AVERAGE(SUM(J1045:J1046), J1049)	Please see response to query 370 published in batch 6 of queries and responses (https://www.ofwat.gov.uk/publication/pr19-final-methodology-queries-answers-24-april-2018/).

Ref No.	Topic	Query	Response
340	Data tables	Re table R8 and R7: Can Ofwat confirm whether R8, line 1, (required retail margin ~ residential customers) should reconcile to R7, line 2, (net margin (excl tax and interest)) or R7 line 5 (EBIT margin)?	The basis for submitting line 1 of R8 should be on an Earnings Before Interest and Taxation (EBIT) basis. Companies are not required to ensure a reconciliation between this figure and those reported in table R7, though we would not expect the figures to be materially different. Should they choose to do so, line 1 of R8 should reconcile to the EBIT margin (line 5 of R7)."
342	Data tables	Re App 13 and App 14: Is it correct to assume that the purpose of these tables is to assess the cash requirements of both retail and wholesale? If so, there are several issues: i. App14, line 4 – is this intended to show the notional balance due from retail to wholesale in respect of wholesale charge even though in reality, as they are the same company, there is no movement of cash? If so, would the offsetting wholesale receivable be reported on App13, line 11? This would cause a problem on App12 as both trade receivables and trade payables would be inflated. ii. App14, lines 1-2 – the guidance for these lines is the same. Should trade payables be the balance of invoices received and not paid only	You are correct to assume that the purpose of these tables is to model working capital and therefore cash requirements. i) App13 collects data on trade receivables. App14 collects data on trade and other payables. Where retail and wholesale are both within the appointee business, App 12 should show the net figure, after the trade receivables and payables for retail and wholesale have been cancelled out. ii) You are correct - there is an error in the guidance. We will amend the guidance to reflect how these items are used in the financial model. Trade payables relates to payables from opex. Other payables relates to any other accruals or creditors due within one year that are not trade creditors, borrowings, tax creditors, capex creditor or liabilities arising from derivative financial instruments.

Ref No.	Topic	Query	Response
		and other payables be all other items such as accruals? iii. App14, lines 13-17 – if trade payables is defined as per (ii) then the guidance calculation does not compare like-for-like and will therefore not produce a meaningful number. For example, employee costs are included in opex, but these will not be invoiced to the company so would sit in other payables. iv. App14, lines 23-24 – should this be calculated using a notional creditor as referred to in (i)? v. App14, lines 23-24 – the item references are the same as App13, lines 25-26. Should they be C00138 and C00139 as per the financial model mapping tool? vi. App14, line 3 – this formulated line will not be equal to the full retail trade and other payables as there are only lines for wholesale creditors and advance receipts. There should be lines for retail trade and retail other payables. vii. App13, lines 22-24 – the formula uses revenue from lines 17-18 and debtors from lines 3-4. However, in response to a previous query, wholesale debtors for business customers should	iii) In the financial model these trade payable day figures are applied to totex less capex. Given this usage in the financial model the definitions appear correct. iv) At PR14 Ofwat assumed credit terms of 1.5 months. In June 2016 we published a consultation on credit terms between wholesalers and retailers in the new retail market. Ofwat's expectation is that companies will use a figure consistent with 1.5 months. Companies should enter expected credit terms in these cells and provide commentary if they adopt an alternative assumption. v) We will update the codes in the mapping tool. vi) We will include lines for the additional retail items you suggest. vii) This relates to debtor balances from retail customers, so the formula appears to be correct. No change proposed at this stage.

Ref No.	Topic	Query	Response
		be on line 11 and not 3-4. Therefore, the debtor days will be zero whilst the revenue isn't, implying that cash is received immediately.	
344	Data tables	Re tables WS18 and WWS18: The guidance to WS18, line 10, and WWS18, line 12, "Amount of planned water investment improving services, maintaining the network and protecting the environment" refers to line 31 in tables WS1 / WWS1. We assume this reference should be to line 19 on the table 'total gross capital expenditure' (excel row 31)? If this assumption is correct then the formulae in WS18 line 10 and WWS18 line 12 are incorrect as they are using values from line 36 "total expenditure" which includes expenditure on pension deficit recovery payments, other cash items and atypical expenditure. Additionally, where the data tables pick up a value from elsewhere, they should also pick up the line title. WS18/WWS18 uses the values from WS1 / WWS1, line 31, but not the title. This could cause error or confusion.	We want to show overall totex in these tables and so disagree with your assumption that this should link to the capex expenditure lines 19 in tables WS1 and WWS1. However, we agree that the line descriptions / titles should be consistent. We have therefore amended the descriptions for line 31 in tables WS1 and WWS1 and reflected these in WS18 and WWS18.
345	Data tables	Re App 7:	We have amended the data tables to deflate the R7 figures from outturn to 1718 FYA CPIH Deflated.

Ref No.	Topic	Query	Response
		The formula in lines 26, 27 and 28 takes values from R7 in outturn. However, the values in App7 are in 1718 FYA CPIH Deflated, the formula in the cells on App7 does not convert between the two price bases.	
349	Data tables	Re App 12: As per the table guidance, App12, line 13, includes preference shares as the balance should equal App14, line 12, (which in turn includes preference shares from App18). However, in the APR, preference shares are reported in current borrowings. Do we report as per APR or as per table guidance? If it is to be reported as per table guidance, the formula in App14, line 8, needs to be amended to switch the signage of the balance copied from App18, line 15.	The tables should be reported as per table guidance. We will amend the data tables to switch the signage when copied from App18 line 15.
351	Data tables	Re App 24a: As per the guidance, the calculation of RPE is relative to the prior year. However, this will understate the RPE impact relative to the base year of 2017/18? Should the 2021 impact be amended to include the impact relative to the base year 2017/18?	As stated in our guidance document companies should calculate both RPE and efficiency gains relative to the prior year in percentage terms.

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		A similar query applies to the calculation of efficiency gains - i.e. should 2021 represent efficiency gains relative to 2017/18 (as a proxy for AMP6 on average) and future years just represent further gains thereafter, or should 2021 just represent efficiency gains relative to the final year of AMP6 alone?	
354	Cost Assessment	Our question is about allocation of water rates: PR19 guidance requires that we use RAGs for separating costs between price controls. The Regulatory Accounting Guidelines (RAGs) currently require rates to be allocated on the basis of GMEAV (absent a prior separation of RCV between water network, treatment and resources it has been reasonable to allocation rates based on GMEAV). However, we now consider it more appropriate to allocate rates based on our proposed allocation of RCV, rather than on GMEAV, as water resources will now have its own specific RCV allocation. For the PR19 business plan, we propose to	We consider that all companies should continue to allocate business rates on a GMEAV basis for consistency with the RAGs. If companies consider that this is no longer feasible or practical then they should put forward the case for an amendment to the RAGs which we will consider as we develop our draft and final determinations.

Ref No.	Topic	Query	Response
		allocate rates on the basis of RCV allocation, and we consider that the PR19 guidance and RAGs should be modified to reflect the creation of a separate Water Resources RCV. This issue is also material to our wholesale charges (particularly for non-potable supplies) and network access prices.	
355	Bioresources	We have a query about the transfer of pricing of liquor returns between bio resources and wastewater network+. Companies need to provide new transfer prices for the cost of sludge liquor returns (due to be implemented from 2020). This could materially differ between companies depending if they use a full Mogden, or if modified, or some other separate cost based transfer price. As Ofwat has no data collection to interrogate the reasons for differences, it will be difficult to judge if these differences represent differences in efficient costs, or differences in transfer pricing methodology. We consider it would be helpful if companies provided those charges on a consistent basis. Also, it is unclear if the charges proposed by companies will be a “passed through” ex post	We will be modifying the RAGs to collect additional information to support the separate price controls after 2020. We are not proposing to add to any business plan table to collect information about company proposals for internal charging for bio resources. We would expect companies to include commentary about their approach to internal charging, including for liquor treatment, across price control boundaries in their bio resources strategy. We will consider these approaches in setting bio resources totex allowances. As set out in RAG5.07, the principle of transfer pricing is that the charge for any activity needs to be cost-reflective. It will be up to companies to consider their internal charging approaches in the light of competition law and satisfy themselves that their internal and external charging approaches are transparent, appropriate and non-discriminatory.

Ref No.	Topic	Query	Response
		adjustment the totex assessed from totex models (which are based on historic costs and hence do not include this recharge). If not, and Ofwat perform an "efficient comparative cost" assessment based on company proposals, then we may receive an assumptions based on another company's low cost methodology (which could be close to marginal cost), whilst our "actual cost" proposed is based on Mogden charges (which reflect fully allocated average costs). Such an approach would be particularly punitive to companies due to there not being a cost sharing mechanism for bio resources. It seems that it would also be more helpful for the future competitive market for these charges to be incurred by all incumbent bio resources companies on the same basis.	We note that the subject of liquor treatment charges was discussed at the sludge working group meeting in June 2016 and a note of the meeting on our website logged attendee opinion that the industry (via UKWIR) should research liquor charging. It also noted the range of discussion about charging approaches.
356	Retail	We have a question about residual non-household retail operating costs: Following retail exit, we still incur some costs associated with business retail activities – we propose that these activities should be moved for AMP7 to sit in wholesale.	We consider that these costs should still be associated with business retail activities. It is important that the retailer takes a proactive approach towards customers.

Ref No.	Topic	Query	Response
		There are certain activities which, under the existing RAGs, we will continue to report as part of our non-household retail activities despite having exited the non-household retail market. The main area is 'providing developer information and administration for new connections' (under RAG2.07 table 2.4.1) which did not migrate to our Water Plus joint venture. Another additional residual non-household activity is investigatory visits. In line with the current RAGs, we will included these residual costs in the PR19 non-household table for all years through to 2024/25. Those companies who have separated their retail activities are unable to pass costs across to the appropriate retailer via the market code that is in operation. This indicates that the current RAG cost categorisations are not in line with the competitive market in following an approach where customer contact drives whether the cost is the retailers. Given that those companies who have separated have effectively derived their own cost base by the activities they undertake, the RAGs should be amended to follow the precedent set by the real-life situation rather than the company incurring stranded costs. Whilst we acknowledge the costs classifications have been set for AMP6, our recommendation is	

Ref No.	Topic	Query	Response
		to reclassify the activity ''providing developer information and administration for new connection" to sit entirely within wholesale for AMP7. We would also suggest similarly that "investigatory visits" in relation to non-household customers should also be reclassified as a wholesale activity. These costs should therefore be recorded as Water and Wastewater Network+ cost (as appropriate) from 2020/21 onwards and hence be recovered from wholesale price controls.	
357	Retail	We are seeking further clarification regarding section 8.5 of the Final Methodology, 'Gap sites and voids'. The Methodology says: "Accordingly, we expect water companies to come forward with bespoke performance commitments to manage their voids and gap sites for the residential market and business market or explain why they have not." As this performance commitment falls in the retail controls section, and we do not manage our business retail customers, are we correct in	In our December Methodology document, we said that we expect water companies to come forward with bespoke performance commitments (BPCs) to manage their voids and gap sites for the residential market and business market or explain why they have not. This requirement also applies to water companies that have exited the business retail market. Separately, we have provided additional guidance on this issue (see query 62 – batch 5, 9 April 2018

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		assuming that there is not an expectation to come forward with a bespoke performance commitment for the business market?	https://www.ofwat.gov.uk/publication/pr19-final-methodology-queries-answers-9-april-2018/). The following guidance we provided in answer to that issue may be helpful: “In our December Methodology document we said that water companies should consider providing a financial incentive to retailers in the business market to identify gap sites and occupied voids, if they have not already done so. If a water company chose to introduce such a financial incentive, it might decide that a BPC covering voids and gap sites in the business market would not be required. This would then leave them needing to consider just one or two BPCs for voids and gap sites in the residential market."
363	Data tables	Re table App14: You have added two new rows (4&5) for wholesale creditors with residential retail and business retail respectively. Can you provide some example scenarios of when you expect there to be creditors between these parties, in particular wholesale and residential retail?	An example of this would be a building which is used primarily for housing the retail contact centre, and so is a retail asset, but is also used by some wholesale staff. In this case retail would charge the relevant wholesale business unit for their share of the use of the building.

Ref No.	Topic	Query	Response
364	Cost assessment	Further to the RAWG meeting on 8th February 2018, we wanted to enquire about when we might expect to see further guidance on treatment of leases from a regulatory perspective? As IFRS 16 becomes effective for water companies on 1 April 2019, we are conscious that the regulatory treatment is applicable for both the current AMP period and our PR19 plan. As we finalise our PR19 plan, we wish to ensure that our treatment of leasing costs is consistent with Ofwat guidance. We note that there may be benefits in accounting for such leases for regulatory purposes in AMP6 and AMP7 in line with the current accounting treatment (a 'frozen GAAP' approach), to avoid inconsistencies in how the regulatory mechanisms deal with such totex. This would avoid any unintended consequences due to, for example: • Changes in AMP6 totex (in 2019/20) arising due to the change in accounting standard, changing the totex incentive adjustment. • Econometric models estimating the efficient AMP7 totex using input data on the current	We will issue further guidance separately regarding the reporting of operating leases by the end of May

Ref No.	Topic	Query	Response
		GAAP, may therefore generate out/underperformance in AMP7 solely due to the accounting change. Whichever approach is finally preferred, we would value clarity, particularly as we continue developing our business plan.	
367	Data tables	Our query relates to table Wn1, lines 1 to 14: We note that the size banding proportions by treatment complexity are to be based on total DI. Total DI includes bulk imports and the guidance states that bulk imports should be included in the proportions of water from different treatment types. Therefore we assume that bulk imports should also be included in the numbers / size bands for WTWs, lines 16 to 48. In our case we do not have any bulk imports of raw water; all our bulk imports are treated water. Please confirm that we have interpreted this correctly.	No, we wouldn't expect bulk imports to be in the numbers / size bands for WTWs where the import is already of potable standard.
368	Data tables	Re table Wn1 and Table Wr1, lines 1 to 4: We note that Table Wn1 treatment guidance states that companies should include in lines 15 - 29 treatment works that have not been used in the year. However in Wr1, lines 1 – 4, it states that operational sources from which no water has	No - please follow the guidance and line definitions in Wr1 and Wn1. In this example, where a site has not been used, continue to report WTW in Wn1 and do not count in Wr1 lines 7 -12.

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		been obtained in the year should not be included in the number of sources, and line 13 states that standby or mothballed sources from which no water has been obtained in the year should not be included. For us the majority of sources and water treatment works are co-located. Therefore, where a water treatment works is included in Wn1 we propose to also include its sources in Wr1. Please confirm that we have interpreted this correctly.	
369	Financial modelling	My query is about indexation of the RCV: The input for the RCV in your latest model is the closing AMP6 value indexed back to 17-18 average year prices using CPIH. The closing AMP6 value has got RPI growth implicitly included. The model then splits the closing value between the CPIH and RPI portions and indexes each one forwards using the respective index. This appears to double count the RPI / CPIH wedge between 2017-18 and 2020. Can you confirm if our interpretation of the inputs required is correct and if so whether this calculation is correct?	The model assumes a wedge of zero prior to 2020. Similar queries have been raised by other companies (see query 257 published in batch 6 of queries and replies - https://www.ofwat.gov.uk/publication/pr19-final-methodology-queries-answers-24-april-2018/). We will amend the indexation in the model to ensure there is no double count on indexation in the model.

Ref No.	Topic	Query	Response
373	Business planning	There is uncertainty in the next AMP relating to our head office site. Our current site is in need of significant refurbishment and there are a number of different opportunities including the disposal of the existing site and development of a new site, or disposal of the existing site and rental of a new site. There is significant uncertainty at present in relation to which options would be most effective for the business. This is impacted, amongst others, by planning uncertainty, availability of suitable rental properties and uncertainty as to the possible disposal of the existing site. We should like to seek guidance as to how best to approach an item of this nature, where there is significant uncertainty as to the final approach to be taken.	We think that our baseline allowance should cover an expenditure of this nature. If you consider that it doesn't, and it passes the materiality threshold for cost adjustment claims, you may choose to raise a cost claim with a suitable protection for customers in the event that the investment does not go ahead or changes scope.
375	Form of control	Re table WR6 / line 1 / water resources: We are not certain how we should estimate the pre 2020 capacity i.e. line 1 in WR6. For example, should we report the same value from 2019-20 until 2045, or do we need to apply reductions to it due to climate change, sustainability reductions and other factors that	Reductions should be applied to capacity (water resources yield) based on the same drivers and assumptions used for developing your water resources management plan (WRMP). This includes any changes over time due to climate change and licence reductions. Further detail on the approach to changes in capacity was outlined in Annex 1, section 1.4, of

Ref No.	Topic	Query	Response
		will change the hydrology and/ or abstraction licences?	Appendix 5 of the draft methodology. An updated version of this guidance will be available in RAG 4.08. You will find Appendix 5 here: https://www.ofwat.gov.uk/publication/delivering-water-2020-final-methodology-2019-price-review-appendix-5-water-resources-control/
376	Form of control	Re table WR6 / line 1 / water resources: We can see in the definition that the forecast forwards should "*account for any changes*" but we are not clear whether this means changes due to climate change (which we have modelled and reported in terms of DO impact in our WRMP tables). Can you clarify what changes you want us to account for? Assuming that we do need to adjust for factors such as climate change over the planning period, would a single central estimate scenario be acceptable?	Reductions should be applied to capacity (water resources yield) based on the same drivers and assumptions used for developing your water resources management plan (WRMP). This includes any changes over time due to climate change and licence reductions. The climate change assumptions, factors and scaling approaches should be consistent with the scenario used for your WRMP and represented in the planning tables. Further detail on the approach to changes in capacity was outlined in Annex 1, section 1.4, of Appendix 5 of the draft methodology. An updated version of this guidance will be available in RAG 4.08. You will find Appendix 5 here: https://www.ofwat.gov.uk/publication/delivering-water-2020-final-methodology-2019-price-review-appendix-5-water-resources-control/

Ref No.	Topic	Query	Response
377	Form of control	Re table WR6 / line 1 / water resources: For the WRZs that we have Aquator models for, should we use a flat or a seasonal demand profile to derive the WR capacity?	The approach used to calculate capacity (water resources yield) should be consistent with guidance used to calculate deployable output and the assumptions made in those calculations for your water resources management plan (WRMP). We expect the demand profile to be consistent with the approach taken for calculating deployable output in the planning scenario, represented in the WRMP planning tables.
378	Data tables	Re table WR6 / line 1 / water resources: Should we follow the methodology set out in Appendix 5 which Ofwat published on 11 July 2017, or is there more recent guidance on how to derive our WR capacity / yields?	Annex 1 of Appendix 5 of the draft methodology is the most recent guidance published on how to derive water resources yield (as of April 2018). As stated in the final methodology an updated version of this guidance, with minor changes, will be available in RAG 4.08. You will find Appendix 5 here: https://www.ofwat.gov.uk/publication/delivering-water-2020-final-methodology-2019-price-review-appendix-5-water-resources-control/
381	Cost assessment	We should like to enquire as to the suitability of these [water resource scheme] costs for the transition programme and to further understand	As we set out in the PR19 methodology, the transition programme allows companies to bring forward planned investment from 2020-25 to 2019-20. We said we would allow transition expenditure

Ref No.	Topic	Query	Response
		what additional information Ofwat would require in order to advise on this matter.	in water resources in exceptional circumstances only. The transition programme in water resources could be appropriate, in certain circumstances, for large investment schemes with long lead-in and delivery periods. Where companies propose transition expenditure, we expect them to make the case for why it is efficient to bring the investment forward, and why it was not part of its outcomes and long-term planning from PR14. Our methodology does not allow for a transition programme to start in 2018-19. This is because we will not have been able to assess any case made to us for bringing investment forward in the context of the whole of a company's business plan.
382	Cost assessment	Given the exceptional circumstances and materiality of costs in 2018/19, relative to normal totex activities, we should like to enquire as to the extent to which it may be permissible to treat these as transitional expenditure in the 2018/19 period.	Please see response to query 381 above.
384	Data tables	Re App 3: The guidelines/definition states that we should be able to select 'surface water' or 'ground water'. When accessing the drop down box there are no	We cannot reproduce this issue. We will contact the company directly to discuss.

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		values to select from. Cells are blank and unable to free type into the cell.	
388	Data tables	Re App 2: Is it correct that for E.43 we are being asked for the performance commitment number? Please confirm whether this is correct, or whether the data being requested is our performance (number of flooded properties) per year against the PR14 definition.	Table App2 is collecting information on old definitions of metrics so that we can understand the relationship between the new consistent reporting data and the previous definitions. Therefore we expect you to report the PR14 definition of internal sewer flooding incidents in line Block E, line 43. Further clarification on what we are expecting in particular columns is: Column C: enter the PR14 reference and performance commitment name, e.g. S-A9: Internal sewer flooding incidents. This will allow us to identify the PR14 performance commitment. Column E: enter the measurement units of the PR14 performance commitment, e.g. number of properties or number of incidents Column F: enter the number of decimal places used for measuring the PR14 performance commitment. This is usually, but not always, 0 (zero) for sewer flooding PCs. Columns H-Q: enter the actual / forecast performance levels for 2015-16 to 2024-25. This is

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			the company's performance (e.g. number of properties flooded internally) per reporting year against the PR14 definition.
389	Financial modelling	Request for clarification on financial model: Average RCV calculation - tab water resources, water network, waste water network and bio resources. The calculation for average RCV on lines 848 and 942 does not appear to be in line with the methodology used in the Annual Performance Report, table 4H, line 4, post tax return on equity. The APR calculation for the average RCV is that it is the average of the opening RCV (before indexation) and the closing RCV (including indexation). The model is calculating the average as the opening RCV (including indexation) and the closing RCV (including indexation). Please could you clarify whether the model calculation will be brought in line with the APR or if the APR calculation has changed?	The PR19 model mirrors the approach taken in PR14. We therefore do not propose to amend the model. We will review the APRs.

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390	Financial modelling	Request for clarification on financial model: Run off for additions to RCV calculation - tab water resources, water network, waste water network, bio resources. The calculation for the run off for additions writing down value does not appear to take into account any part year impact, therefore the run off rate does not apply in the year of the expenditure as we would have expected. This appears to be a change from previous price reviews. Will this calculation be amended?	The model published in March 2018 time apportions the RCV depreciation for additions in the year of acquisition, with full depreciation occurring in subsequent year. We therefore believe this issue has been addressed and do not propose to make any further amendments to the model.
393	Cost assessment	We have a query about the Final Methodology – specifically section 9.5.2 – Our approach to business retail – page 154 final paragraph. Would you be able to provide further clarity on the statement, “we would set a revenue cap, based on previously allowed levels of costs”. Does this mean: 1. When we submit our business plan for the retail non household we should bridge the 2020-25 expenditure levels to the 2015-20 allowance,	This statement refers to English water companies that have not exited the business retail market. For non-exited business retailers, we will set a revenue cap based on previously allowed levels of costs in PR16. We expect non-exited business retailers to provide robust evidence to demonstrate that their costs are efficient.

Ref No.	Topic	Query	Response
		however present the anticipated costs for 2020-25 within the new market? 2. We are limited to the 2015-20 levels of costs which were allowed in PR16? 3. An alternative approach to forecasting the costs for 2020-25?	
395	Outcomes	We have a query about table APP2: Please would you be able to provide further clarification on the following point: Ofwat and the EA have stated that SELL is no longer a useful tool for deriving leakage targets as it does not drive either ambition or efficiency, so why are we required to submit upper, central and lower limits of SELL through until 2045? Are companies expected to be able to forecast using the new method of leakage reporting to 2045, when the final guidance has only been issued this week so companies have not had the opportunity to understand the impacts of these changes? Long run SELL is mainly determined by supply demand balance overlaid by assumptions on growth, asset deterioration and efficiency of	The aim of providing SELL forecasts until 2045 is to allow us to understand how ambitious companies' proposed leakage performance commitments are over the long-term. We would expect all companies to calculate the SELL using the new consistent definition of leakage and to set out any assumptions and uncertainties associated with the impact of the new definition leakage has on the calculation of the SELL. The upper and lower limits enable us to understand the certainty of a company's SELL calculation. We consider that companies are best placed to consider what the main uncertainties and assumptions are based on the calculation of the SELL and we are therefore not prescribing a detailed approach to how it is calculated. We expect companies to set out what assumptions they have made in their commentaries.

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		leakage management. Is the central forecast for SELL aimed at understanding the impacts of our supply demand balance on SELL? It is impossible for any company to predict the impacts of efficiency of leakage management to 2045 when embarking on a leakage reduction plan greater than previously achieved within the industry. We accept that calculation of SELL has a high degree of uncertainty, but request clarification on what basis we should estimate upper and lower limits for SELL and what these will be used for? Are we correct in assuming that this is our WRMP target measured in litres/property/day and cubic metres/kilometre/day?	We are expecting companies to calculate the SELL in the units that their performance commitments are in so that we can compare the performance commitment with the SELL estimates. We expect the company's performance commitment to be consistent with its WRMP or for the company to explain why this is not the case. Separately from the SELL, you ask about whether you should report your WRMP target measured in litres/property/day and cubic metres/kilometre/day. We are expecting the leakage data companies report in the table on litres/property/day and cubic metres/kilometre/day to reflect companies' proposed leakage performance commitments based on the new consistent reporting guidance for leakage, which we would expect to be consistent with the WRMP projections.
396	Outcomes	Within the adapted worksheet, which follows the format for the PR19 business plan table App1, and which has been provided as part of the requirement to submit early information on our bespoke performance commitment definitions, we note the specific guidance for AIM. Where a company does not have any suitable sites for inclusion within AIM, the final PR19 methodology statement expects us to include a	The PR19 methodology appendix 2 (page 31) says: "The table below sets out the five areas that performance commitments must cover [which includes the Abstraction incentive mechanism] and our rationale for companies having to cover each area with bespoke performance commitments. If a company chooses not to cover one of these areas with its bespoke performance commitments it will need to provide justification for its approach."

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		bespoke performance commitment in line with the AIM guidelines (originally published in February 2016). This requires identifying suitable sites in liaison with the Environmental Agency (EA), if there are no existing AIM sites. The EA has asked us to check with Ofwat the situation where there are no current AIM sites and no currently suitable sites, but there are investigations that may identify if there are abstraction changes required in the future. In this situation, we assume a company would create an alternative bespoke performance commitment to reflect the investigations or abstraction protection work it was doing, but would not label this on App1 as "AIM", as it does not meet the methodology description of an AIM bespoke performance commitment. We would be grateful if you could confirm whether our assumption is accurate?	The PR19 methodology appendix 2 (page 36) says: "If, following the application of well-justified checks, a company does not have any suitable sites for AIM, a company should consider sites not identified in the WINEP lists for inclusion in the AIM. For example, companies could consider sites where there is evidence that current abstraction rates are causing harm and that reductions in abstraction at low flows will provide environmental benefit. Companies should also engage with their local stakeholders on such sites."
397	Data tables	Feeder Model - could you please confirm what the PV base date should be in the profiling inputs section of the revenue feeder model (column F, row 130)?	We confirm the PV base date in the profiling inputs section of the revenue feeder model (column F, row 130) is 31-March-2021 as shown in the model published on our website. Setting the PV base date as year ending 31-March-2021 produces a PV discount factor of unity in 2020-21 when values do not require a discounting adjustment. This adopts

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			the same discounting approach used in PR14 for profiling the CIS revenue adjustments.
398	Past delivery	Feeder Model - could you please confirm what is meant by “discount rate” inputs in profiling section of the revenue feeder model (column F, row 132-137)? Does this refer to the WACC? If so, what is the appropriate input for the “residential retail” and “business retail” components?	We confirm the “discount rate” inputs in profiling section of the Revenue feeder model (column F, row 132-137) refer to the appointee WACC for PR19, because the model is profiling over the 2020-25 period. We consider the appropriate discount rate value for all the inputs, including those for “residential retail” and “business retail”, would be the appointee cost of capital. We have future-proofed the revenue adjustments feeder model by building in flexibility for different discount rates to be specified if needed.
400	Financial modelling	In the FM release of the financial model we noted that there did not appear to be an input for the retail residential revenue adjustment (PR14 reconciliation adjustment relating to customer numbers and allowed cost by customer type), although there were clear entries (F_Inputs! 449, flowing to Residential_Retail! 56) for the SIM penalty. We note in the 16 March 2018 update to the financial model, that the F_Inputs! 449 and Residential_Retail! 56 entries have been relabelled as 'retail residential revenue	The input in row 449 of F_inputs comes from the revenue feeder model. This takes into account several revenue adjustments including SIM, the labelling in the financial model F_inputs was updated to reflect the feeder model. This labelling will be updated in Residential retail.

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		adjustment', but still end up as a 'SIM' entry in the calculation. As these are 2 separately-identifiable adjustments, is your intent that we should combine these as a single input for the financial modelling? We also note that the wholesale calculations include entries labelled 'water resources - residential retail mechanism (+ or -) value chosen - active - real' (e.g. see Water Resources! 105), with associated entries on the F_inputs sheet. Inclusion of retail adjustments in wholesale controls appears counter-intuitive. Could you please confirm the adjustment we should include here?	
402	Financial modelling	The Trade Receivables (row 184 onwards) section of Retail_Residential! includes some unusual logic. Retail residential apportionment of the wholesale charges only includes water resources and wastewater network plus. In addition, the percentage apportionment entries in F_Inputs! (e.g. for water resources see rows 212-215) appear to be used in different ways in different parts of the model.	Please see response to query 307 above.

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		For example: The sum of percentage for each wholesale control should 100% (per data table guidance for block C of WR3, WN3, WWN5, Bio4). Assume 69%, 11% (residential measured, unmeasured) and 19%, 1% (business measured, unmeasured), populated on F_Inputs! for the four wholesale controls. This yield an 80% residential apportionment on wholesale_global! 112, but on retail_residential! 197 shows a retail residential measured apportionment of 138%.	
403	Data tables	Re data tables: Further to query ref no 221, in Q&A (15 March 2018 https://www.ofwat.gov.uk/publication/final-methodology-queries-answers-15-march-2018/), consider a situation where each wholesale price control has the same percentage splits across residential/business and measured/unmeasured. Could the formulas in App17, C 13-16, not generate percentage allocations, at combined wholesale level, in excess of 100%?	We agree that the lines 13-16 in App17 could generate allocations in excess of 100%. We are amending App17 block C to calculate a £m charge (see query 477 below).

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404	Financial modelling	Re financial models - Water_Resources! 986: Return on RCV is calculated by applying a nominal WACC to nominal RCV. This flows into the revenue building blocks (nominal) at row 127. Does this approach not double-count inflation? This appears to be because the deflator in row 973 (for CPIH + wedge) requires manual inputs in Sensi!, which feed the deflator for the chosen scenario at Sensi! 74. Core inflation, imported to F_Inputs! from data tables appears irrelevant and does not feed the Base Case inflation. The same holds true for deflation using CPIH (trace from Water_Resources! 838). Should we link these base case inflation assumptions to relevant active inflation assumptions on index?	The nominal WACC is deflated into real WACC on the wholesale control sheets. Please see Post-tax return on regulatory capital value calculation block for this calculation. This is deflated by long term inflation when calculating a real WACC. The long term inflation is different to the monthly inflation which may be more volatile.
405	Financial modelling	Further to query 404, the model appears to adopt a similar approach in other areas too, with some inputs in the Inp_Active! sheet, rather than being primary inputs on F_Inputs! or embedded model parameters. Examples include: TDS for Bio (Inp_Active! 902), RCV splits for CPIH (AMP7) and RPI (AMP8) (Inp_Active! 236,237,432,433,623,6324,809,810).	Some inputs are located on other sheets e.g. proportion of RCV to CPIH for each wholesale control is found on InpActive. We expect companies to input into these sheets and provide a fully populated financial model when submitting their business plans.

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		Do we understand correctly that we should populate such primary inputs in this manner?	
409	Confidence and assurance	We have a query relating to the pre-populated data sheet ‘F-inputs’. Your response to our previous query indicated that we need to submit 3 versions of the data tables- one for Bournemouth Water (reconciliation tables) one for South West Water (reconciliation tables) and one for the two companies’ combined (all data tables excluding reconciliations). The query is that the pre-populated cells in the data tables reference the F-inputs sheet which we assume will be completed by Ofwat (based on guidance documents) and re-issued with the final tables on 3rd May. Can you confirm that there will be two versions of the table provided to enable the reconciliation tables to be completed, or is the expectation that we complete the F-inputs table with the relevant data from the two companies?	We will produce 3 sets of the BP tables – one each for South West Water (SWT), Bournemouth Water (BWH) and the combined company (SWB). We will include an F_Input sheet in each set, but only the sheets for SWT and BWH will be populated by Ofwat. The F_Input sheet for SWB will be left blank and the company will need to complete this. The PR14 reconciliation data for SWB should be the combined total of adjustments for the pre merged companies. The company should submit all 3 sets of the BP tables.
410	Cost assessment	Re uncertain environmental obligations: Ofwat has specified that a unit cost based ODI mechanism should be put in place to accompany uncertain environmental obligations. We have	We agree with this approach in principle. We will require good quality evidence behind the choice of those unit costs for the different consents to be able to understand how well the proposal will protect

Ref No.	Topic	Query	Response
		analysed the relationship between costs and PE, kg/P removed and river length improved and have not been able to generate a single unit cost that would enable us to reconcile actual requirements and performance appropriately. We would like to propose a table of unit costs (£/PE) but with different rates depending on STW size band and the new permit limits. Would Ofwat consider this to be in line with the guidance on a unit-cost based ODI to cover uncertain environmental obligations?	customers when investment requirements turn out to be different to those we see in business plans
413	Water resources	Re table WR6 / lines 3-4 and 5-6: Capacity Company Forecasts, “The post-2020 capacity is based on the incremental water resources yield funded through the water resources control after 1 April 2020”. Definitions for WR6, lines 3-4, 5-6, 10-11 and 12-13 has the sentence: “The post-2020 capacity is based on the incremental water resources yield funded through the water resources control after 1 April 2020”. We are not clear on what ‘incremental water resources’ means. Is this referring to additional	We have updated the line definitions for Wr6 in relation to another PR19 query (number 120). This now includes an example for what should be reported. For example for A3: ‘This is the company total available post-2020 capacity, as available in all WRZs, and measured using water resources yield. The post-2020 capacity is based on the incremental water resources yield funded through the water resources control after 1 April 2020. This will be the total post-2020 capacity available up to and including the year being reported for. For example, if 20Ml/d of new capacity was available in 2020-21, then the

Ref No.	Topic	Query	Response
		resource (Future Planning – Baseline) or year on increase (either row 13FP or 18FP) on WRMP?	reported post-2020 capacity for that year would be 20Ml/d. If a further 10Ml/d is made available in 2021-22, then that years reported post-2020 capacity would be 30Ml/d. These forecasts should be provided for the DYAA planning period.’
421	Risk and return	Re App19 (debt and interest costs): If App19 is to be used to calculate interest costs then section A should be completed using nominal values, as this is the value we will actually pay interest on. In the guidance to App19 it states that this table should reconcile to the borrowings in App12. This will only reconcile if both use the carrying value of debt. However, if App19 uses the carrying value of debt rather than the nominal value, then the interest cost calculated from it will not be correct. The carrying value of borrowings shown on App12 will, for example, include the effects of the movement in interest rates and exchange rates in the value of the bond since it was traded. The nominal value however will be what we are required to pay back at the maturity of the bond and is what we are charged interest on. We suggest that a formal reconciliation from App19 to App12 should be included as a	We will amend App19 by adding a separate block for companies to add reconciling items to demonstrate how App19 reconciles to the values in App12. We will also amend the guidance in App19 to provide further clarification of the data companies should input.

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		separate block in App19. This will show how the nominal values in App19 reconcile to the carrying values in App12. App19 guidance should also clearly state that it should be completed using nominal values. If App19 is not to be used to calculate interest costs then it can be completed with carrying values and no such reconciliation will be required; App12 borrowings and App19 debt will agree.	
422	DPC	Re App21 (direct procurement for customers): App21 commences from 2020/21. We may propose that (if possible) some early costs could be included in 2019/20 and considered as “transitional investment”. It would therefore help if App21 was amended to include 2019/20 as an additional year.	In reviewing this query we have further considered the data requirements for DPC schemes for PR19. In doing so, we have identified the need to update the business plan guidance for DPC and the wholesale cost tables to ensure that the cost tables reflect appointee total totex requirements in the transitional year (2019-20) and PR19. In the DPC table guidance we said that we did not expect companies to include any costs for DPC projects in other data tables on PR19 costs. We have now amended this guidance to confirm that appointee costs should also be included in the relevant cost assessment tables for PR19 and transitional costs. This change has also been reflected in the relevant wholesale water and wastewater cost tables guidance.

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			We have also amended APP21 to include a column for 2019-20 transitional investment to reflect possible transitional investment in 2019-20 for appointee DPC development costs. In line with the updated guidance, transitional investment should also be included in tables WS10 and WWS10 and must meet the criteria and requirements set out for these tables. As set out in the final methodology, the cost of developing projects is included in totex allowances. We only expect to fund transitional expenditure for appointee development costs for DPC schemes by exception. In addition to the requirements for transitional expenditure under tables WS10, and WWS10, companies will also have to provide evidence that this cost has not already been funded and justify why it requires accelerated expenditure for the delivery of the DPC scheme. Companies must also provide details on what this expenditure will be used for and what impact it will have if this expenditure is not provided in 2019-20.
423	Risk and return	The financeability section of the Final Methodology notes the working assumption that companies will hold 33% of index linked debt.	Appendix 12 of our methodology stated that we consider 33% of the notional company's debt to be index linked as a prudent assumption for financeability testing. Our approach will be to assume 33% of the opening balance sheet is index

Ref No.	Topic	Query	Response
		However, this looks to raise an inconsistency with the approach taken to indexing the cost of new debt to the iBoxx index. In particular, that indexation approach takes no account of the costs of new index linked debt, and appears to effectively assume that companies will raise no new index linked debt (at least from a notional company perspective). While the assumption that companies will hold 33% of index linked debt is not new, the approach of setting a fixed allowance for new costs meant that its implications to be taken into account implicitly. Is Ofwat planning to take account of the costs of companies securing new index linked debt in its final assessment of new debt costs? This issue has particular relevance given the transition from RPI to CPIH, as this changes the inflation risk exposure that companies will need to manage. Has Ofwat taken account of the effect that this can be expected to have on debt issuance costs, given the new arrangements that companies are likely to have to put in place to manage the transition?	linked in the financial model; we assume no new index linked debt is raised by the notional structure in either our financeability assessment or the cost of debt reconciliation model. On CPI-linked debt, we have previously commissioned a report by Oxera examining the impacts of a switch to CPI indexation (https://www.oxera.com/getmedia/151823cd-c92c-4394-be5e-ea97312df1a5/Oxera_Indexation-of-future-price-controls-in-the-water-sector.pdf.aspx?ext=.pdfif). This report concluded that there is no evidence that financing costs will increase as a result of a switch to a different inflation measure such as CPIH. Of course, companies can submit further evidence in their business plans where this is relevant to the assessment of the efficient cost of debt for a company with a notional financial structure.
424	Risk and return	Our query relates to the cost of debt true-up:	We recognise that RCV adjustments could smooth bill impacts for customers relative to revenue

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		The final methodology sets out that Ofwat's policy on how the cost of new debt true-up will be reflected in company revenues will be decided as part of the next price control, PR24. We recognise the attractions of this approach, including that it allows positive and negative adjustments to be netted off at that point. Our query is whether Ofwat intends to develop any further policies at this stage to address the possibility that the required true-up could be 'large'? Our analysis suggests that under some relatively extreme, but clearly plausible scenarios, the required true-up could be substantial. The need for a 'large' true-up could make its treatment a material factor in terms of company financeability, while at the same time posing significant issues for PR24 customer bills (as if interest rates rise much more rapidly than had been expected, customers in PR24 may need to face both the higher prevailing rates at that time and a 'large' true-up cost from PR19). While this type of situation may not arise, there is a reasonable possibility of it doing so. Experience at many previous price controls has highlighted	adjustments. We have not, however, made a final decision on the form the revenue true up for the cost of new debt should take (i.e. revenues or RCV). We will decide this as part of our methodology for PR24.

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		the difficulty of accurately predicting interest rates, and the scale of observed differences between forecast and 'actual' levels underpinned the movement to the new indexation approach. We would be very happy to share our analysis of the potential scale of the true-up effect. There looks to be a good case for committing to a policy of addressing true-ups through an RCV adjustment. This would reflect that over time, the average level of true-up would be expected to be zero (with forecasts sometime higher than outturn levels, and sometime lower). The alternative of making a true-up adjustment to revenues each period could introduce an unnecessary source of bill volatility, in a context where those adjustments would in any case be expected to net out over time.	
428	Past delivery	Re data table - PV effect of 50% of proceeds from disposals of interest in land (APP9 - Currently Line 9 and 21): Currently these are positive numbers and therefore are added to the RCV. However, it should be deducted and should therefore be a negative number.	We agree the adjustment should be deducted from the RCV. We have reversed the signage in the calculation of lines 10 and 21 in table App9.

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429	Financial modelling	Re Financial Model _ Return on RCV Additions (Row 1122 Water resources, water network, Wastewater network and Bio resources): Currently the model calculates negative returns on RCV additions as the calculation of average of RCV post 2020 additions (Row 1114 WR, WN, WWN, BR) appears to be incorrect.	Please see response to query 370 published in batch 6 of queries and replies on 24 April 2018 (https://www.ofwat.gov.uk/publication/pr19-final-methodology-queries-answers-24-april-2018/).
430	Financial modelling	Residential retail revenue adjustment does not feed through to allowed revenue. This adjustment is applied to the calculation of the margin (Retail_Residential row 88), however the adjustment is not included in the final revenue calculation (appointee row 12) as the final revenue calculation uses the Residential retail service revenue - nominal calculation (Retail_Residential row 176) that does not included this adjustment.	Please see response to query 295 above.
432	Financial modelling	The debt adjustment calculation (Appointee F244, F274, F304, F340) only uses the wholesale opening cash balances. As it does not take into account the opening retail cash balance, this results in the initial gearing levels and debt adjustments being calculated incorrectly.	We are basing the adjustment on wholesale cash as it is a wholesale gearing adjustment and where the RCV sits. We are not expecting retail net debt to be significant enough to have a material effect on appointee gearing, if this is the case we will take this into account if it is required. We therefore do not propose to amend the model.

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433	Financial modelling	With regard to the financial model - direct procurement (e.g. InpActive row 210); although these costs feed through to each price control sheet (water resources row 52) and the financial statements, they do not appear to feed through to the final allowed revenue calculation which are based upon rows 194 in each wholesale price control, that does not include direct procurement costs.	DPC costs (apart from company's own development costs) and DPC revenue are excluded from final allowed revenue calculations because they fall outside of price controls. It would therefore not be appropriate to include them in k calculations. The costs and revenue are included in the model to enable the bill impact on customers of schemes to be estimated. No change to the model proposed.
437	Outcomes and customer engagement	We have a generic query on lines A2, A5, A9, B12 and B20 of customer metrics. We will complete these lines for the submission of our Business Plan including forecasts. Lines A2 and A5 (affordability and acceptability) in particular will be explored in the testing of our Business Plan over the next few months. We are also intending on monitoring performance on an ongoing basis for each of these metrics by including relevant questions in our annual image tracking survey. Can Ofwat confirm that companies will be required to monitor and report these on an ongoing basis?	We are not currently requiring companies to monitor and report on the customer metrics in Table App4 on an ongoing basis after PR19. We say in Appendix 1 (Addressing affordability and vulnerability) of the PR19 methodology statement in relation to the vulnerability common metrics that: "We are also considering the use of a third party expert panel and the further development of common metrics to assess and advise companies' approaches to vulnerability across all companies during 2020-25. We will discuss this with the sector after the PR19 final determinations." (Page 15).
438	Outcomes and customer engagement	Our query is about line A2 customer metrics - customers finding the level of their combined bills affordable: (b) for companies who charge for both water and wastewater (WaSCs).	We do not consider it is appropriate for Ofwat to pre-approve individual survey questions undertaken by companies. It is companies' responsibility to ensure that the approach they have taken is

Ref No.	Topic	Query	Response
		We are proposing to collect this information on an ongoing basis by inserting a question into our annual image tracker survey which is a telephone survey of 1,000 randomly selected customers across our region. The question would be the same as that used in the annual CCWater 'water matters survey' as follows: How much do you agree or disagree that the total water and sewerage charges that you pay are affordable to you? The scale would be 'strongly agree' through to 'strongly disagree' along with a 'don't know' option. Can Ofwat confirm this question wording is appropriate for Line A2?	consistent with the definition of Table App 4, line A2 and the PR19 final methodology.
439	Outcomes and customer engagement	Exact duplication of query 438.	See response to query 438.
440	Outcomes and customer engagement	Query regarding line A9 - customers aware of affordability assistance measures. We are proposing to collect this information on an ongoing basis by inserting two questions into our annual image tracker survey which is a telephone survey of 1,000 randomly selected customers across our region. The questions would be as follows:	We do not consider it is appropriate for Ofwat to pre-approve individual survey questions undertaken by companies. It is companies' responsibility to ensure that the approach they have taken is consistent with the definition of Table App 4, line A9 and the PR19 final methodology.

Ref No.	Topic	Query	Response
		Are you aware of any kind of assistance that (name of water company) offers for customers who struggle to afford their water bill? (If 'yes' do you receive any kind of assistance?) 1. Yes – aware but do not receive any assistance 2. Yes – aware and receive some form of assistance 3. No – not aware 4. Don't know (not prompted) For those who answer 1 or 2 they will then be asked: Which, if any, of these are you aware of that (name of water company) offers for customers who struggle to afford their water bill? (The list is read out and it is multi-code) 1. Flexible payment plans 2. Ability to pay bill directly from benefits 3. Reduced bills for customers in certain circumstances, such as low income or with certain medical conditions 4. Debt repayment plans 5. Free water saving packs 6. Free water meters, so you only pay for what you use 7. Something else	

Ref No.	Topic	Query	Response
		8. One of these 9. Don't know Can Ofwat confirm this question wording is acceptable for line A9?	
441	Outcomes and customer engagement	Re line B12 customers aware of the non-financial vulnerability assistance measures offered: We are proposing to collect this information on an ongoing basis by inserting a question into our annual image tracker survey which is a telephone survey of 1,000 randomly selected customers across our region. The question would be the same as that used in the annual CCWater 'water matters survey' as follows: Are you aware of any additional services offered by your water company, such as large print or braille for people who need them, passwords to check that company callers are genuine, or liaison with customers on dialysis who need a constant supply of water? These are also known as priority services. (If yes, are you registered for priority services?) 1. Yes – but I am not registered 2. Yes – and I am registered 3. No	We do not consider it is appropriate for Ofwat to pre-approve individual survey questions undertaken by companies. It is companies' responsibility to ensure that the approach they have taken is consistent with the definition of Table App 4, line B12 and the PR19 final methodology.

Ref No.	Topic	Query	Response
		4. Don't know (not prompted) Can Ofwat confirm this question wording is acceptable for line B12?	
442	Outcomes and customer engagement	Line B20 customers satisfied that the services are easy to access: The line definition provided by Ofwat is customers satisfied that the services provided by their company are easy to access, as a percentage of all customers. This may include, but is not limited to, satisfaction of customers in relation to the range of methods they can use to contact their supplier and satisfaction that the information provided is clear and easy to understand. We believe this line is covering two different issues, namely ease of access and information provision. We are proposing to collect this information on an ongoing basis by inserting two questions into our annual image tracker survey which is a telephone survey of 1,000 randomly selected customers across our region. The answers to the two questions would need to be combined. The questions would be as follows: How would you rate our performance in the following areas? For each one please tell me if	We do not consider it is appropriate for Ofwat to pre-approve individual survey questions undertaken by companies. It is companies' responsibility to ensure that the approach they have taken is consistent with the definition of Table App 4, line B20 and the PR19 final methodology.

Ref No.	Topic	Query	Response
		you are very satisfied, fairly satisfied, neither satisfied nor dissatisfied, fairly dissatisfied or very dissatisfied? Read out each statement, randomise order, single code for each. Randomise order: Very dissatisfied, fairly dissatisfied, neither/nor fairly satisfied very satisfied, DK /no opinion. The range of methods through which you can contact them. They make information about their services clear and easy to understand. Can Ofwat confirm this question wording is acceptable for Line B20?	
443	Outcomes and customer engagement	Line B20 customers satisfied that the services are easy to access: The line definition suggests this question should be asked of all customers and not just those who contact you, the latter having more direct experience of ease of access and information. Should this question therefore be aimed at contactors only?	The line definition for App4, Line B20 specifies that it relates to all customers.

Ref No.	Topic	Query	Response
446	Financial modelling	Interest on existing or new debt: The interest rates in F_Inputs 137 and F_Inputs 141 appear to link to the total debt balance (rather than just the existing debt balance). Given this, would it make sense to make the data table App19 consistent with the financial model. Currently it includes a split between new debt (App19 rows 12 and 14) and existing debt (App19 rows 11 and 13). Alternatively, the financial model could be adjusted to be consistent with the data table.	The financial model has debt balances that reflect interest rate type (fixed, floating, index-linked) rather than by age (existing, new). This means that interest rate inputs are applied to the total debt balance rather than just the existing debt or just the new debt. We will amend App19 to include interest rates for all debt of a particular type (e.g. nominal debt), that will be a weighted rate of both for new and existing debt. This new interest rate will then be the input into the financial model.
447	Financial modelling	Interest on index-linked debt: The interest calculation on index-linked debt (for example water resources row 1362 - 1370), does not include interest on the indexation accrued in the year (e.g. assuming indexation occurs on average midway through year). This appears to be inconsistent with the approach for new drawdowns (where the proportion of debt applicable for accounting in year is included in the interest calculation), and with the approach for opening index-linked debt balance, where the opening balance including indexation is used as the basis for the interest calculation.	The approach we use is consistent with the PR14 model. At this stage we do not propose changing the model calculation approach.

Ref No.	Topic	Query	Response
448	Financial modelling	Pension deficit repair modelling: There may be a difference in AMP7 between the revenue allowance for pension deficit repair, per IN13/17 (e.g. F_Inputs row 252), and the company's expected pension deficit repair costs (e.g. F_Inputs row 256). Would it be worth including functionality as part of the 'Notionalisation' of the model to allow the expected pension deficit repair payments so they are in line with the allowance?	The notionalisation process is similar to that at PR14. At this stage we do not propose adding further steps for pension deficit repair allowances.
449	Financial modelling	Post-2020 RCV additions: Calculation of average post-2020 additions balance for return on RCV calculation (e.g. Water Resources row 1114): Should this formula reflect the average of the previous two rows, rather than the opening RCV less the closing RCV? Also need the opening RCV to include indexation (i.e. row 1112 should be the sum of 1045+1046).	Please see response to query 370 published in batch 6 of queries and replies on 24 April 2018: https://www.ofwat.gov.uk/publication/pr19-final-methodology-queries-answers-24-april-2018/
450	Financial modelling	Intercompany loan interest income: Where companies have intercompany loan interest income, where should this be included in the model? One option would be to include it as 'Interest receivable (other)' (i.e. data table App19, row 17, feeding into the financial model F_Inputs	For the notional company this is not an issue. Under the actual company structure, then companies may need to include both the interest received in respect of the intergroup loans and the round trip dividends. Within the model, if the interest received is recorded in other interest then the model will net off the interest received from the

Ref No.	Topic	Query	Response
		row 105. This looks to generate the correct cashflows, but as this interest income is included in the financial ratio calculations, these ratios may be distorted. Potentially a switch could be added to exclude such interest income from the ratio calculations, such that they just reflect external debt (in line with, for example, ratio calculations as defined in Table 4H of the APR). An alternative approach could be to completely exclude such intercompany loans (both the principal balance and the income) from the model.	interest paid and that will impact on the interest metrics. If the amounts involved are material and the company considers that they are significantly distorting the metrics then the company can present alternative calculations of the metrics in their business plans.
451	Financial modelling	Retail bill calculation: The calculation of the average retail revenue per customer (summary_calc, rows 1081 and 1091) does not reflect potential differences in revenue for single service and dual service customers. Given that the model already calculates separately revenue per customer for the different customer categories (for example in retail_residential rows 125 - 128) could the model give a more accurate view of household bills by using in the bill calculation for single service and dual service revenue per customer already calculated in retail_residential?	We have amended the cost to serve categories in the model to provide greater granularity and will ensure that the bill calculations reflect this.

Ref No.	Topic	Query	Response
455	Financial modelling	Retail SIM adjustment: retail_residential, row 79: The SIM adjustment doesn't currently look like it has any impact on the retail revenue calculation. Is this intentional?	Please see response to query 295 above.
456	Financial modelling	Retail working capital: retail_residential, row 189: This currently takes the sum of the percentage of wholesale revenue collected from unmeasured residential customers, from two of the five wholesale price controls. (a) Would it be more appropriate to consider all five of the wholesale price controls? (b) Would it be more appropriate to take a weighted average, rather than the sum? For example: Suppose each wholesale price control collected 70% of its revenue from unmeasured households, then row 189 would currently show 140% of the wholesale revenue collected from unmeasured households, thus setting off the alert in row 193 that the percentage should be less than 100%. Similarly for row 197.	We agree that should show all price controls and be calculated as weighted average of controls in use based on revenue from customer type. Linked to query 309 above.

Ref No.	Topic	Query	Response
		This also affects working capital calculations that depend on these rows, for example the Measured income accrual calculation in rows 334 - 343.	
458	Financial modelling	Retail capex and depreciation: The calculation of implied capex based on the allowed depreciation appears to assume that there is a full year's depreciation in the year of capex spend (retail_residential row 435). Would it be sensible to add flexibility to allow depreciation to reflect capex incurred part way through a year?	Please see response to query 313 above. This should mean that this flexibility is not required.
459	Financial modelling	Retail allowed depreciation: The check calculation in retail_residential, row 558, compares the input allowed depreciation (row 556) with the depreciation as calculated based on the implied new capex in AMP7 (row 557). If there is any depreciation associated with the brought forward retail asset balance, this will therefore give rise to a check. Would it therefore make sense to adjust the check calculation so the allowed depreciation can	We are amending the capex calculation to be an input line from the data tables (see query 313 above). The checks will then be updated to reflect the changes to the model.

Ref No.	Topic	Query	Response
		include depreciation on brought forward retail assets? Similarly, as the calculation in row 557 is just based on the implied capex in years 1-5, then if the model is being used to estimate impacts beyond AMP7, then the calculation in row 558 will show a check, as row 556 may include depreciation on AMP8 capex, but row 557 will not. Note that the depreciation, excluding depreciation on brought forward assets, is currently used elsewhere in the model. For example, retail_residential, row 552, is used in appointee row 188 and analysis_appointee row 142. retail_residential, row 553, is used in row 282, and also in FinStat_Residential, row 13. These rows, and subsequent calculations will therefore be distorted from not including the full retail depreciation.	
462	Financial modelling	Accounting for grants and contributions: The model does not appear to be correctly accounting for grants and contributions. Currently these appear to be accounted for in the model as negative capex (e.g. water network, row 420).	We recognise that grants and contributions can be accounted for in several ways and table 2E in the APR looks to collect total grants and contributions regardless of accounting treatment to eliminate any possible mismatch. If a company does account for any grants and contributions as revenue, these should not be reflected as revenue in their APR

Ref No.	Topic	Query	Response
		While this approach should generate the correct revenue requirement (before tax - see below), this does not reflect how grants and contributions are accounted for (grants and contributions recognised as income on the income statement, either in the year of receipt, or deferred over a period). If the expectation is to use the model to populate data tables (for example App11) in line with the Regulatory Accounting Guidelines, does the model need to be able to recognise grants and contributions within the income statement, rather than as negative capex? Where the grants and contributions tax treatment follows the accounting, the model may not therefore currently be calculating the appropriate tax charge.	(shown as a difference to stat accounts in table 1A). The model does not need to be able to recognise grants and contributions within the income statement.
471	Financial modelling	Dividend calculation: The recommended dividend calculation for AMP7 uses the final year AMP6 as the base year (i.e. for using the RCV and net debt to determine the equity value on which the dividend yield is applied). Would it be more appropriate for base year of the AMP7 dividend calculation to be the first year of AMP7?	The financial model mirrors the PR14 approach in taking the prior year RCV, post-midnight adjustments, less debt multiplied by dividend yield and grows using the balances from the final pre-forecast period (the final year of the prior AMP). We therefore do not believe the financial model requires amending.

Ref No.	Topic	Query	Response
472	Risk and return	Re App 12, Section J: We have some queries concerning the new section J in App 12. In order to avoid fundamental differences in how companies allocate balances, please can you clarify the following two points: 1. Definition of what is meant by wholesale, residential retail and business retail. 2. How you would like us to treat retained earnings prior to the introduction of these price controls? Our assumption is that ‘wholesale’ refers to the wholesale element across all customers and retail residential and business refers to the retail margin. Therefore, for companies that exited the market, business retail will be nil from 1 April 2017. We propose that for retained earnings, all balances prior to AMP 6, i.e. before the price control was in existence are treated as wholesale and only profits in this AMP and going forward are allocated to these price controls. Non-operating costs, which are not specific to price controls, such as interest and tax, are to be allocated to wholesale.	RAG 4, chapter 3, gives details of classification between residential and non-residential. We would expect companies will have to set out their assumptions for any split in their business plans based on how they manage the businesses.

Ref No.	Topic	Query	Response
		Cash is to be allocated 100% to wholesale as we do not hold any specific cash relating to the residential retail business. Capex creditors are to be allocated based on capex spend allocations in the year, unless there are any specific reasons to suggest payment terms have varied between price controls. Please can you confirm that these are acceptable assumptions for the completion of section J.	
473	Cost assessment	I have a query in relation to APP22, Pensions, the whole table. Please could you clarify your expectations for APP22, Pensions? In particular, please would you be able to provide further clarification on the following point: • Could you please clarify whether you need us to include both employer's contributions to employee's pension and employers pension deficit contributions, and if so which parts of the table should cover each?	Please see response to query number 394 published in batch 6 of queries and replies on 24 April 2018: - https://www.ofwat.gov.uk/publication/pr19-final-methodology-queries-answers-24-april-2018/
475	Retail	We have a question about household retail - revenue sacrifice in AMP7 and historic values:	We do not consider that it is necessary to separately report costs associated with the

Ref No.	Topic	Query	Response
		Table R9 allows for the reporting of “revenue sacrifice” in block E and is used to report lost revenues through schemes such as company funded social tariff reductions and other company volunteered tariff discounts to customers that cannot be rebalanced onto other customers. However, R9 only covers AMP6. There is currently nowhere to report household retail revenue sacrificed in the historic years 2012/13, 2013/14, 2014/15 or (more importantly) forecast revenue sacrifice in AMP7. Voluntary tariff discounts form an important part of household retail company costs. As set out on table App4, lines 7-8, these costs are often balanced by benefits to bad debt or other elements of cost. To ensure that companies can present a full picture of household retail operating cost plans (and therefore required revenues) we believe an additional line to table R1 should be included, seeking to capture “revenue sacrificed” for the full period 2012/13 to 2024/25, and that this also be represented in the financial model for the assessment of required revenues over and above company proposed costs (which naturally exclude revenue sacrifice values).	household retail revenue sacrifice. The costs of voluntary tariff discounts are included in customers service costs, which also include billing and customer care costs. The customer service costs are defined in our Regulatory Accounting Guidelines 4.07, Table 2C line 1. Any analysis we do, for example cost benchmarking, will be done at an aggregate customer service level and therefore would not identify separate components, such as costs for revenue sacrifice.

Ref No.	Topic	Query	Response
476	Risk and return	Is App 20 an early submission table with APR? In Ofwat's meeting notes of the Regulatory Accounts Working Group (RAWG) on 8 February, it states that Ofwat proposed that for the 2017-18 APRs, companies should submit Table 1E together with App20. Can Ofwat confirm whether App20 is required to be submitted early with the APR, and what (if any) other tables are required for early submission with the APR?	Given the identical date and similar data coverage, our expectation is that the key summary statistics from App20 - and in particular 'Indicative weighted average nominal/cash interest rate' will be the same as the corresponding figures provided in APR Table 1E. Where there are differences between these figures we will expect companies to provide a reconciliation explaining them. Companies should submit App20 with their business plans, but are welcome to submit App20 early if they so wish.
477	Risk and return	Re App17, lines 13-16 – proposed amendments to table set to resolve issues: The calculation and units for the wholesale charges by price control in App17, lines 13-16, in the March 2018 table set lead to errors in table App13. App13 lines, 15-18, calculates the appointed revenue by adding the wholesale charges from App17, lines 13-16, which is a % to the retail revenue from R7 in £m. We propose that the calculations in App17, lines 13-16, and the guidance are amended. The amendments sum the price control charges in lines 13-16 in £m,	We agree that this is an error in the data tables. We will amend the wholesale charges lines in App17 to be a calculated £m figure. This will resolve the error in App13.

Ref No.	Topic	Query	Response
		and will correct the appointed revenues calculation in App13. Alternatively, if Ofwat wants to retain APP17, lines 13-16, to be represented as percentages, then the current calculation is incorrect, as one cannot simply add the percentages from the sub-control tables. Instead, a weighted average calculation should be used (weighted by the revenues in each control). This would then require a change to APP13 to multiply the percentages in APP17 by total revenues to obtain the values required in £m.	
484	Financial modelling	Re Financial model (Dec '17 edition) / F_Inputs / 'F_Inputs!$H$142: This name needs to specify whether it relates to indexation on existing index linked debt or existing plus new index linked debt.	Please see response to query 446 published above.

Ref No.	Topic	Query	Response
485	Financial modelling	Re Financial model (Dec '17 edition) / F_Inputs / 'F_Inputs!$H$147: Is this requesting an indexation rate to apply to new indexed linked debt? For example, if new index linked debt was all RPI linked, then the values in this cell would be FYA RPI.	This input allows companies to demonstrate a blended rate if not all debt is RPI linked. However if all RPI linked then yes would be FYA RPI.
490	Financial modelling	Re financial model (Mar '18 edition) / "Retail_Residential" / 'Line 552: Allowed depreciation and capital expenditure is back calculated from an input allowed depreciation value on F_Inputs. Given that ongoing capex must be known in order to calculate and then input the F_Inputs allowed depreciation, then perhaps it might be more straightforward to request an input for this HH Retail capex. The current calculation method means that no (or insufficient) allowed depreciation is calculated for the period 2025/26 - 2029/30.	Please see response to query 313 above.

Ref No.	Topic	Query	Response
492	Financial modelling	Re financial model (Mar '18 edition) / InpActive / InpActive!F$433 - "Target level of RCV linked to CPI(H) _ RPI wedge at beginning of AMP 8". I think this is an input that Ofwat needs to provide, much as they gave the 50% input in cell F432 above in other PR19 documentation. In cells F236:237, the cells are pre-populated with the values of AMP7 "50% and AMP8 "25%" for the Water Resources price control. No other main price controls (except DMMY in cells F997:998) have pre-populated values; should they? (N.B. this appears to be a value decided by Ofwat for both AMPs, as such, companies are therefore probably not best placed to have the knowledge to populate both cells).	We expect companies to provide a fully populated financial model when submitting their business plans. As detailed in the methodology, companies are also expected to explain bill profiles from 2025 onwards and while this can be done using the financial model however, it is not mandated that they use the financial model to demonstrate this. We will, however, amend the model and remove the 25% in AMP8 in the Water Resources price control to be consistent with the other wholesale price controls.
494	Water resources	Re company bid assessment frameworks, specifically section 4.1.1 – avoiding conflicts of interest: The guidance states that an incumbent’s associated company should not participate in the bidding process for water resources. We would like clarification if this precludes associated appointed water companies from participating in the bidding process too.	Please see response to query 288 above.

Ref No.	Topic	Query	Response
495	Cost assessment	Lines 23 & 25 of table App24a require annual 'Input Price Pressures' to be calculated on Retail depreciation. The total depreciation figure in each year represents a proportion of capital costs incurred in previous years, and so are not impacted by current year prices. This means there will always be zero input price pressures on depreciation in any given year. Can Ofwat advise whether this is the correct interpretation?	See response to query number 200 above.
500	Data tables	Re data table / R5 / Validation: There is a validation check for row 13 in the table which is currently a blank row. We think this check should be removed.	We agree and have removed his validation.
501	Data tables	Re data tables / Wr5, Wn5, WWn7, Bio6 & Dmmy9 / Validation: The formulae in cell V27 in the tables is referencing the incorrect cell in table App32. We think the formulae should be referencing cell G47.	The cell references for this validation rule have been changed and now pull from the correct cells - we are grateful for pointing this out.
502	Data tables	Re data tables WS1, WWS1, R1, R4: The response to query ref 131 in the 'queries and answers 22 February 2018' publication states	In App22 companies report actual pension contribution – split between prices controls. Ofwat will use the proportions to allocate the outstanding PR19 allowances. The pension deficit recovery

Ref No.	Topic	Query	Response
		that AMP7 spend for pension deficit recovery payments should be based on actual spend costs rather than the costs that will be allowed as per IN13/17. We think that this is incorrect as companies plans will reflect the pension costs that will be funded by Ofwat rather than what they actually intend to spend. Actual amounts that companies intend to spend on their defined benefit schemes will be reported in table App22.	costs in line 22 WS1/WWS1 are "total" deficit costs i.e. include what Ofwat allowed and any further payments companies are required to make in agreements with the pension trustees.
507	Water resources	What is the definition of "increasing water resources capacity"? Should we be including company inter-zonal and intra-zonal transfer options as individual options with a capacity in the same way that we would treat a resource option?	Water resources yield used to measure water resources capacity is only applied to raw water. For transfers of raw water the capacity should be reported by the company (or zone for internal transfers) that benefits from the capacity (importer). Treated water transfers are considered network plus water activities and do not contribute to water resources capacity. Further guidance on water transfers will be included in RAG 4.08.
508	Financial modelling	Re water resources / water network etc / #1672: The calculation of notionalised tax seems to be incorrect. It is missing the item 'interest on change in net debt - WN - nominal' to adjust the 'Adjusted taxable profit loss'.	You are correct to state that when notional gearing is below actual gearing the interest change from the change in net debt is excluded from the tax calculations. This is intentional. By excluding this item from the tax calculation the interest shield from debt is based on the actual gearing level, which is higher. This means that customers benefit from the

Ref No.	Topic	Query	Response
			interest shield from higher than notional gearing. Where notional gearing is above actual gearing the interest change from change in net debt is included in the tax calculations. The approach we have adopted is consistent with that used at PR14.
509	Financial modelling	Re water resources / water network etc. / #1672: The indexation of IL debt is an important input to the tax calculation. This also needs to be adjusted for if the notionalised tax is to match the actual tax for revenue requirement.	Our testing indicates that the ILD behaves as expected, and we do not propose amending the model. Changing the percentage of total debt that is index linked debt will not result in a material movement in tax charge if the index linked debt inputs (i.e. interest rate and inflation assumption) and nominal debt inputs are consistent. Our approach is therefore similar to PR14, where a macro was used to set the tax adjustment consistent with the level of tax prior to adjusting the index linked debt.
510	Financial modelling	Re water resources / water network etc. and analysis water resources / analysis water network etc / WR/WN etc #393 / analysis_water network'!#104: Notional interest on notional debt is being adjusted incorrectly for the CF and PL. Interest is then being used incorrectly in the notional financial ratios. All occurrences of 'interest on change in net debt	Thank you for your query. We have reviewed the financial model in light of your query, and our testing indicates that the model is consistent with the approach we took at PR14 (where we allowed interest movement to flow to financial statements). We believe that changes in interest as a result of gearing changes should flow into the CF and PL. This ensures that when Ofwat is consistent when reviewing notional financial indicators from different companies. No changes to the model are therefore proposed.

Ref No.	Topic	Query	Response
		- WN - nominal' should be removed from any calculation other than that for modifying the tax for the revenue requirement and tax in the notional financial statements.	
511	Financial modelling	Re residential retail / #451: I don't understand the logic being used here. I have entered five years of 'allowed depreciation' in F_Inputs# 72. There is also an opening balance of retail assets from F_Inputs #455. The current calculation of implied capex in retail residential #451 returns zero for the first year of the period if there is an opening balance given. I would suggest revising the formula to ignore the first period test. The second half of the formula is sufficient and gives the correct answer for capex and the correct answer for fixed asset balance.	Please see response to query 313 above.
512	Past delivery	We have ODIs which have a shareholder funded underperformance penalty. However, there is nowhere in App27 to record these penalties, as the existing table allows for revenue adjustment or RCV adjustment only. How should we report on these penalties? Should we leave them out of App27 completely? Should we record them in one of the existing	The shareholder funded penalty should not be included in table App27.

Ref No.	Topic	Query	Response
		sections with comments explaining that they are shareholder funded, or should we add extra sections to the table for us to record these penalties?	
518	Direct procurement for customers	Our query is about the TTT pass-through revenue to Bazalgette Tunnel Ltd: The data table guidance requires the use of RAGs when populating the data tables. The pass-through revenue associated with the TTT to Bazalgette Tunnel Ltd is treated as non-appointed revenue in the APR, and as such may not get included in the data tables, if following the RAGs. This approach may therefore give a distorted view of the overall customer bill. Is it therefore appropriate instead to include such TTT pass-through revenue as if it were DPC revenue (i.e. in the "expected CAP revenue stream" of table App21)?	We do not consider that it is appropriate to collect Thames Tideway pass-through revenue in App21 as it not a DPC revenue stream. However, for the purposes of completing the financial model these pass through costs should be entered in the inpActive worksheet in the 'direct procurement for customers - infrastructure cost' lines for the relevant wholesale control. We have already provided specific guidance on the how Thames should report information on the Thames Tideway scheme in section 2.5 of the 'PR19 table guidance for business plan data tables'. This guidance sets out the data that we will require in order to take into account the Thames Tideway scheme in the financial model.
519	Direct procurement for customers	Re DPC appointee costs: The guidance for Table App21 (direct procurement for customers) indicates that "we do not expect companies to include any costs for DPC projects in other data tables on PR19 costs". What is the mechanism for allowing the	We have reviewed the treatment of appointee costs relating to DPC schemes at PR19. We note that in the DPC table guidance we said that we did not expect companies to include any costs for DPC projects in other data tables on PR19 costs. We have now amended this guidance to confirm that appointee costs should also be included in the

Ref No.	Topic	Query	Response
		appointee to recover its costs in relation to setting up DPC projects (i.e. row A5, "Total appointee costs" of App21)? This does not appear to form part of the totex that is used in the financial model, which uses data from WS1 and WWS1.	relevant cost tables. This is to ensure that the cost tables reflect appointee total totex requirements at PR19. This change has also been reflected in the relevant wholesale water and wastewater cost tables guidance.
520	Outcomes	For the common measure - Internal sewer flooding incidents (including severe weather) please can you clarify whether this needs any normalisation (per 10,000 connected properties? As stated in the December 2017 appendix 2 document) as this is inconsistent with the final reporting guidance march 2018 which does not mention any normalisation.	We will use internal sewer flooding incidents (including severe weather) normalised per 10,000 connected properties to compare company performance during PR19. This is also the metric used on Discover Water. We are not requiring companies to express their performance commitments on sewer flooding incidents normalised by "per 10,000 connected properties" in case they want to use the number of incidents instead, which some companies might consider is easier for customers to understand.
521	Outcomes	I have a query regarding how AIM is completed on the PR19 App1 table that is due to be submitted by 3rd May. Ofwat's PR19 final methodology guidance, and the query response to query 315 in the 9th April query response set, indicate that companies can develop a bespoke performance commitment for AIM.	We provided the information on the Abstraction Incentive Mechanism (AIM) in the Table App1 guide to help companies translate the information they entered into table App3 into table App1. We have amended the guidance on AIM in Table App1 to say that the direction is "Down" i.e. a lower number represents better performance on AIM (i.e. lower abstraction at times of low flow) in keeping with the approach in the February 2016 AIM

Ref No.	Topic	Query	Response
		However the App1 table has guidance covering AIM which stipulates how the data line should be completed, including the units of measure, number of decimal places and the direction of performance. We were intending our AIM calculation to follow the existing method as used currently in the annual performance report table 3C. This gives a normalised output which is dimensionless, so the final units are not Megalitres, and also the direction of improving performance is down, not up as stipulated above. We are not clear on why Ofwat has stipulated the above requirements for AIM in this 3rd May submission? Can we confirm please, that we can complete the data line in table App1 as per our intended methodology, i.e. the current methodology used in APR table 3C?	guidance. We have amended the guidance on AIM in Table App1 to say that the "PC unit" can be Megalitres or percentage, which are the two units used in table App3.
522	Retail	We would appreciate confirmation that our interpretation (given the two examples below) that Initial Assessment of Business Plans is not intended to apply in respect of the non-household retail control of non-exited retailers in England. Chapter 8, section 8.6, “Initial assessment of business plans – retail controls” - the last	We recognise that competition will help to drive positive outcomes for eligible customers and that exited retailers are not covered by PR19. Therefore, in line with our approach to targeted and proportionate regulation, water companies’ business plans should, in general, focus on retail services not open to competition.

Ref No.	Topic	Query	Response
		paragraph of this section clearly states: " … business plans to focus on retail services which are not open to competition …". Can you please confirm our interpretation that the non-household retail control for non-exited retailers in England is not subject to IAP? Chapter 14, Page 237 "Retail Costs" - the methodology states that "only" retail costs for customers using less than 50 megalitres in Wales (i.e. not subject to competition) will be subject to cost assessments as set out in Chapter 9. Can you please confirm our interpretation, that by exception, retail costs for those non-household customers in the 50 megalitre plus market, customers of exited English retailers and non-exited retailers whose customers are subject to competition are not subject to IAP.	That said, for water companies that have not exited the business retail market, there are some things we will consider as part of our Initial Assessment of Business Plans. These fall into the following categories: **1. Issues that are relevant at the appointee level and consequently cover companies' business retail functions too.** This covers IAP questions related to: • Securing confidence and assurance. This is because, for example, we expect board assurance to cover all of an appointees' regulated activities; and, • Risk and return (other than those questions specifically targeted at wholesale controls). This is because, for example, companies' financeability assessment is considered at appointee level. **2. Issues that are specific to business retailer functions.** This covers the key building blocks for setting a business retail control, that is: • Securing cost efficiency, where we will take into account companies' cost forecasts related to business retail, and,

Ref No.	Topic	Query	Response
			• Risk and return issues specific to business retail. That is, we will take into account companies' proposed net and gross margins related to business retail tariffs.
523	General	We wanted to check to what extent Ofwat sees catchment management playing a role in company business plans for PR19? Is there any relevant guidance companies should be considering?	Catchment management is highlighted in several sections of our final methodology for PR19, including 1.6, 4.2.3, 5.8 and 14.4. There is further detail in our 'Resilience in the Round' publication. We have highlighted catchment management as an area where companies should progress options if they represent best value to deliver outcomes for customers.
524	Outcomes	We are considering a penalty only ODI for vulnerable customers where the penalty would be paid to a relevant charity (for vulnerable customers) rather than to customers as a whole through lower allowed revenues. Would this still be classed as a financial incentive?	From the information provided because the ODI underperformance penalty reduces your revenue it appears appropriate to classify it as a financial ODI.
525	Outcomes	Exact duplicate of query 521 above.	See response to query 521 above.
526	Cost assessment	We have a query regarding allocation of capex costs for pumping assets between price controls for pumped surface water abstractions.	Yes – we can confirm that on the information provided the allocations presented in the example is correct. Correct terminology is Raw Water Transport (not distribution).

Ref No.	Topic	Query	Response
		For pumped surface water abstractions where the pumps are located at the abstraction site and the WTW or raw water tank is some distance away from the abstraction site, Ofwat has already confirmed that average pumping head should be allocated between water resources and raw water distribution based on the relative total pumping head. We are seeking clarification regarding how to allocate capex and opex costs for pumping assets for these types of abstractions, as follows (set out over next two queries): <u>Abstraction type 1</u> A river abstraction to a WTW or raw water tank where the pumps are located at the abstraction site and the WTW or raw water tank is some distance away from the abstraction site. The abstraction itself is by gravity from the river to the pump sump. The pumps then pump the abstracted water to a WTW or raw water tank some distance away from the abstraction site. Our assumption is that all capex and opex costs for this pumping (i.e. including the purchase and installation of new pumps) will be raw water distribution. Is this correct?	

Ref No.	Topic	Query	Response
527	Cost assessment	We have a query regarding allocation of capex costs for pumping assets between price controls for pumped surface water abstractions. For pumped surface water abstractions where the pumps are located at the abstraction site and the WTW or raw water tank is some distance away from the abstraction site, Ofwat has already confirmed that average pumping head should be allocated between water resources and raw water distribution based on the relative total pumping head. We are seeking clarification regarding how to allocate capex and opex costs for pumping assets for these types of abstractions, as follows: <u>Abstraction type 2</u> An abstraction from an impounding reservoir to a WTW some distance from the abstraction site. The water is abstracted by gravity from draw-off points in the reservoir to pumps that are located on the reservoir site below the dam. These pumps then pump the abstracted water to the WTW which is some distance away from the abstraction site. Our assumption is that all capex and opex costs for this pumping will be raw water distribution. Is this correct?	Yes – we can confirm that on the information provided the allocations presented in the example is correct. Correct terminology is Raw Water Transport (not distribution).

Ref No.	Topic	Query	Response
528	Cost assessment	We have a query regarding allocation of capex costs for pumping assets between price controls for pumped surface water abstractions. For pumped surface water abstractions where the pumps are located at the abstraction site and the WTW or raw water tank is some distance away from the abstraction site, Ofwat has already confirmed that average pumping head should be allocated between water resources and raw water distribution based on the relative total pumping head. We are seeking clarification regarding how to allocate capex and opex costs for pumping assets for these types of abstractions, as follows: <u>Abstraction type 3</u> A river abstraction to a WTW or raw water tank where the pumps are located at the abstraction site and the WTW or raw water tank is some distance away from the abstraction site. There is only one set of pumps and they are located at the abstraction site at the same elevation as the intake. In order to abstract the required quantity of water, some of the pumping head is needed to abstract the water from the river and make it	Yes – we can confirm that on the information provided the allocations presented in the example is correct. Correct terminology is Raw Water Transport (not distribution).

Ref No.	Topic	Query	Response
		available at the abstraction site for transport, and the rest of the pumping head is needed to pump the abstracted water to the WTW or raw water tank. Our assumption is that all capex and opex costs for this pumping will be allocated between water resources and raw water distribution based on the relative total pumping head. Is this correct? Unfortunately neither of these examples are in the RAG schematics so it would helpful to confirm if our understanding is correct.	
529	Outcomes / past delivery	I would be so grateful if you could please confirm for me whether my understanding is correct regarding the following: For table App5, column 4: the allocation by PR19 price control is only needed for those performance commitments with a financial ODI. Column reference definition 4 PR19 price control allocation: enter the allocation for each price control (as a percentage, to 1 decimal place). This is based on the understanding that there would be nothing to allocate to PR19 price controls for reputational (NFI) commitments.	Within table App5 (PR14 reconciliation - performance commitments), companies are not required to complete the PR19 price control allocations for performance commitments with reputational (i.e. non-financial) ODIs.

Ref No.	Topic	Query	Response
530	Outcomes	There is a potential issue and inconsistency with the drought resilience metric performance commitment. The drought resilience metric calculation is based on the supply-demand balance (SDB) and whether a company is in surplus or deficit based on this calculation. This is specified in the guidance document “Drought resilience metric – Risk of severe restrictions in a drought”. In the supply-demand balance calculation, only deployable output (supply) is considered on the supply side, which is normally considered as the output from a company’s own sources. Should the supply-demand balance calculation also include imports and exports? The supply-demand balance calculation using deployable output only ignores the net benefit of imports and exports, which are included in the supply-demand balance calculations in company Water Resource Management Plans, and therefore in the assessment of drought risk in those plans. This could lead to inconsistencies between WRMP stated drought risk, and as calculated in	The example supply-demand balance shown in the metric definition is simplified for ease of understanding. Based on the metric definition the supply-demand balance as used for WRMPs should be applied for this metric. The main difference between the company calculations used for WRMP19 and the metric should be the inclusion of data appropriate for the 1-in-200 year scenario. Based on this, all supply demand balance allowances used for WRMP19 should be included in the metrics calculation, including imports and exports and other components of the supply demand balance not mentioned in the simplified example, such as operational losses. In terms of the confidence score, given the long term nature of the metric, it will be best if this is reflective of the reported risk value, which is calculated over the 25 year forecast.

Ref No.	Topic	Query	Response
		the performance commitment. This means that if a company is a net importer, it loses the benefit of the import in its calculation of drought risk (and likewise, a net exporter would benefit from no exports). Furthermore, if a company has selected a new import to solve a supply-demand balance deficit as part of its WRMP, then this scheme would show no impact on the company performance commitment. The performance commitment would not incentivise them for early delivery of this scheme. The uncertainty in the reliability of imports and exports is dealt with elsewhere in the calculation in two places. In the supporting technical document on the certainty grade method, from the Water UK Long Term Planning Framework project (produced by Atkins), the calculation guide proposes that the risk score is derived based on the WAFU – e.g. including imports and exports. The risk score proposes that the certainty of imports and exports is included in the risk score, yet the supply-demand calculation method to which it is applied, does not actually consider them. Furthermore, the uncertainty in imports and exports is also accounted for in our target headroom analysis, which is included in the	

Ref No.	Topic	Query	Response
		supply-demand balance calculation, which technically means we would be accounting for uncertainty in a component of the calculation that is not actually in the equation itself. On that basis, it seems that the SDB calculation on which the metric is based should consider imports and exports. An additional uncertainty is how the confidence score is meant to be specifically calculated. The risk metric aspect is based on a supply-demand balance calculation to derive a risk label. On which year through the planning period should this metric be based? The base year figure – reflecting the tightness and reliability of the supply-demand balance – might be very different to the final year figure if, for example, supplies from other sources mean growing surplus improves the risk label value. Should it be the average risk label score over the planning period, given it is meant to provide a confidence score to a number that is, in itself, calculated as an average over the period?	
531	Data tables	Re table Retail_ResidentialL63, L88: Currently SIM financial incentive seems to be added to the total cost to serve, and then a 1%	We have amended the financial model so that that residential retail revenue includes the full value of SIM.

Ref No.	Topic	Query	Response
		margin of the incentive is included in the residential retail revenue, rather than taking the total incentive amount. Please could you check if SIM incentive is being incorporated correctly?	
532	Outcomes	Ofwat's "Putting the sector back into balance" consultation says that C-MeX and D-MeX will be reconciled at PR24, but the PR19 final methodology says that C-MeX and D-MeX will be reconciled each year in the next price control period. Which is correct please?	The final PR19 methodology states (page 66): "We will apply the C-MeX financial incentives in-period (reconciled for each year individually) to strengthen the incentive for companies to improve their customers' overall experience more quickly." And for D-MeX on page 67 we say: "We will apply these performance payments and penalties annually, in keeping with the approach for the other common performance commitments." It is the PR19 final methodology that is correct.