

March 2019

Trust in water

## **RAG 3.11 – Guideline for the format and disclosures for the annual performance report**

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## 1. Explanatory note

### 1.1 Introduction

- 1.1.1 On 18 December 2018 we modified Condition F of all companies' licences, with a replacement condition which comes into force on 1 March 2019. The old Condition F contained specific requirements about the construction and presentation of accounting data. The new condition F sets the purpose and framework for the RAGs and the checks and balances associated with them, but omits any specific detail as that detail was already contained in RAG 3.11.
- 1.1.2 The new Condition F makes it clear that the requirements in the RAGs must be complied with, albeit within the scope and purpose set by Condition F as a whole. Within the published RAGs there are some matters which are outside the framework of Condition F. One example of this is information required on outcomes performance. We are, however, able to require the provision of this information, with the form and content set out, under other conditions in the licence. In order to help people understand the basis on which we require information we include within RAG 3.11 a table at Appendix 3 setting out the licence or other provision to which the information relates.

### 1.2 Role of regulatory accounting guidelines

- 1.2.1 The accounting statements are the primary source of regular audited financial information about the business regulated by the Water Services Regulation Authority (Ofwat). It is intended that the RAGs should take precedence over UK accounting standards. Where the RAGs do not specifically address an accounting issue, then UK Generally Accepted Accounting Practice (UK GAAP) should be followed.
- 1.2.2 There are 3 areas where we will require companies to deviate from these accounting standards:
- **Revenue recognition.** Companies should not de-recognise turnover for amounts billed which they deem to be uncollectable. This means that IFRS 15 or FRS102 (23.3) should be disapplied in this respect.
  - **Grants and contributions.** Companies may recognise grants and contributions in the income statement as revenue under UKGAAP (either as a single transaction or through amortisation). We require that any such income be shown as 'other income' rather than revenue.

- **Borrowing costs.** IAS23.8 requires borrowing costs to be capitalised where they directly relate to the construction of an asset. We require this rule to be disapplied. Similarly the option to capitalise under FRS102 (25.2) should not be taken.

### **1.3 Annual information notice on the annual performance report**

- 1.3.1 Ofwat will publish an information notice annually. This will include any required amendments to RAG3. If any new accounting standards mean that a departure from UK GAAP is necessary it will be covered in this notice.

## **2. Accounting statements**

### **2.1 Accounting statements**

#### **Condition F requirements**

2.1.1 Under paragraph F2 of Condition F we require all appointees to prepare accounting information as set out in the regulatory accounting guidelines (RAGs). That requirement is set out in this guideline. This guideline also requires companies to provide information in addition to this. The basis of these additional requirements are set out in appendix 3.

#### **Pro forma tables**

2.1.2 We require that regulatory accounting statements should be prepared in accordance with the formats, accounting policies and principles which apply to the statutory annual accounts of the appointee.

2.1.3 The information in the regulatory accounting statements must be provided in a common format for all companies and with a 31 March year end. The pro forma tables for the submission of data are included in appendix 1.

2.1.4 The following pro-formas are not required to be included as part of the annual performance report but must still be prepared in accordance with these RAGs:

- table 3S; and
- tables 4J - 4W.

## **2.2 Publication of accounting statements**

#### **Reports to be delivered**

2.2.1 Appointees with a UK holding company (whether this is an ultimate holding company or an intermediate holding company as part of an overseas group of companies) should submit the following documents to Ofwat:

- ultimate UK holding company accounts;

- annual performance report including the regulatory accounting statements; and
- statutory accounts (if not bound with the annual performance report).

2.2.2 We require the appointee to deliver to Ofwat a copy of the annual performance report (including regulatory accounting statements and auditors reports prepared under Condition F) as soon as reasonably practicable and in any event **not later than 15 July** following the end of the financial year to which they relate. Appointees can submit electronic copies by email to Ofwat.

2.2.3 Companies may refer in the annual performance report to any relevant commentary provided as part of the latest available statutory accounts. A clear cross-reference and link needs to be provided.

## Website publications

2.2.4 Companies should publish their annual performance report on their websites at the same time as they are submitted to Ofwat.

2.2.5 Companies should publish the ‘accounting methodology statement’ on their websites. They may include these in the annual performance report but there is no specific obligation to do so. The required contents of the methodology statement are set out in appendix 2.

## 2.3 Audit

### Auditors’ reports

2.3.1 We require auditors to address reports to Ofwat concerning:

- accounting records; and
- accounting statements.

As a minimum the audit opinion should cover the pro forma tables in section one and section two of the annual performance report.

2.3.2 The required wording of the audit opinion will be set out in our annual information notice on the annual performance report.

## **Further information required from auditors**

- 2.3.3 The licence requires that the contract of appointment with the auditors contains a term ‘that the auditors will provide such further explanation or clarification of their reports, and such further information in respect of the matters which are the subject of their reports, as the Water Services Regulation Authority (Ofwat) may reasonably require.’

## **2.4 Appointed business**

### **Definitions**

- 2.4.1 The licence separates the activities of an appointee into appointed and non-appointed activities.
- 2.4.2 Appointed activities are consequently those activities that are necessary in order for an appointee to fulfil the functions and duties of a water and sewerage undertaker. Please see Appendix 1 in RAG4 for more information on appointed and non-appointed activities. Companies should discuss areas of difficulty, in advance of preparing the accounts, with Ofwat.

## **3. Accounting disclosures**

### **3.1 Disclosures required in the annual performance report**

#### 3.1.1 Companies shall include:

- a statement which describes the link between directors' pay and standards of performance (as required by section 35A of the Water Industry Act 1991 (inserted into that Act by section 50 of the Water Act 2003));
- a statement as to disclosure of information to auditors;
- a statement on dividend policy for the appointed business;
- an accounting policy note for price control units;
- a note on revenue recognition;
- a note on capitalisation policy;
- a note on bad debt policy;
- a statement on sufficiency of non-financial resources;
- a statement on sufficiency of financial resources and facilities;
- the tax strategy for the appointed business;
- a statement on differences between statutory and RAG definitions;
- a long term viability statement; and
- a statement explaining out/under performance of the return on regulatory equity (RORE).

### **3.2 Statement of directors' remuneration and standards of performance**

3.2.1 In relation to transparency around the remuneration of directors, we expect companies to consider whether and how to take account of the requirements of the Large and Medium-sized Companies and Group (Accounts and Reporting) Regulations 2008 that apply to the Directors' Remuneration Report for a quoted company.

3.2.2 The Water Act 2003 introduced a requirement for companies to make a statement to Ofwat at the end of each financial year, regarding links between directors' pay and standards of performance. The annual performance report should contain this statement.

3.2.3 The statement should detail any arrangements linking the remuneration of the directors of the company to standards of performance in connection with the carrying out of functions of a relevant undertaker. It should comprehensively

explain the arrangements, including all information relevant to the users of the annual performance report.

3.2.4 Any person who has been a director of the company at any time and received remuneration during the financial year should be covered in this statement. Where the directors are also directors of another group or holding company they still need to be covered by this statement.

3.2.5 Remuneration means any form of payment, consideration or other benefit (including pension benefit). Standards of performance include any standards, which are set by condition of the company's appointment, any applicable regulations or any that are set or agreed to by the company, such as outcome delivery incentives (ODIs).

3.2.6 The statement must include in particular:

- the date the arrangements were made;
- a description of all the standards of performance in question;
- an explanation of the purpose of linking each particular standard of performance to remuneration;
- a description of the targets set for each standard;
- an explanation of how all the standards of performance are assessed and the source of the data; and
- an explanation of:
  - whether targets were achieved or not;
  - how the remuneration was calculated for each standard; and
  - details of the amounts paid to all individual directors.

3.2.7 Even if no remuneration has been paid under any arrangements in the financial year, the annual performance report must still disclose the details of any arrangements in force or any arrangements intended to be in force during the financial year. Commentary on future targets should also be provided as well as detail on any changes to previous arrangements such as targets, source of data and calculation method.

3.2.8 If no such arrangements are in place an explanatory paragraph should be provided detailing the reasons why no such arrangements are in place.

### **3.3 Statement as to disclosure of information to auditors**

3.3.1 The Companies (Audit, Investigations and Community Enterprise) Act 2004 includes sections dealing with the auditor's rights to information. Relevant

audit information is defined in s234ZA of the Companies Act 1985.

- 3.3.2 Previous legislation in this area (s389A of the Companies Act 1985) meant that auditors were entitled to require information and explanations for their duties from ‘officers’ of the company. Whilst it was a criminal offence to provide misleading, false or deceptive information it was not an offence if officers failed to provide any such required information. The revised legislation means it is now a criminal offence to fail to provide this information.
- 3.3.3 The new legislation requires each director to make a statement in the accounts that:
- a) so far as the director is aware, there is no relevant information of which the company’s auditors are unaware; and
  - b) he has taken all the steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the company’s auditors are aware of the information.
- 3.3.4 Typically this is included in the directors’ report for statutory purposes. Ofwat requires this statement to be made in companies’ annual performance reports.

## **3.4 Dividend policy**

- 3.4.1 Companies must report on the value of any dividend paid and provide a comprehensive explanation of the basis of the dividend.
- 3.4.2 Some companies pay dividends to parent companies which offset amounts of interest receivable under inter-company loan arrangements. Where such an arrangement exists, companies’ dividend policy note should describe both a description of the arrangement and the amounts paid and received in the year.

## **3.5 Accounting policy note for price control segments**

- 3.5.1 Companies must include an accounting policy note for price control units which are disclosed in section 2 of the annual performance report. This should summarise the basis of the allocation of operating costs and assets and any major changes in the year. Companies should state that the accounts have been drawn up in accordance with RAG2 – Guideline for classification of costs across the price controls. They should also refer to the accounting

methodology statement and provide a reference to this document.

## **3.6 Revenue recognition note**

3.6.1 The revenue recognition note should cover the following.

- A description of any adjustments between amounts recorded as turnover in the statutory accounts and amounts recorded as turnover in the regulatory accounting statements. This should be split between adjustments relating to IFRS15 deviation and any other adjustments.
- Whether or not the company bill void properties speculatively, that is to 'the occupier'. If so, it should confirm that this bill is then recorded in turnover.
- If the company does not speculatively bill, how it checks that the property is indeed unoccupied. It should also describe how it ascertains the identity of any occupier.
- A description of steps that the company takes to establish whether properties with no occupier information are void or occupied, e.g. visits to properties or searches using third party electronic data such as council tax/electoral roll records.
- Any changes in methodology in calculating the measured income accrual.
- Any significant differences between a retrospective review of the previous years measured income accrual and the amounts actually billed in the year.

## **3.7 Capitalisation policy note**

3.7.1 Companies should explain the basis for capitalising costs. Companies should also clearly state any general rules which have been used (e.g. a rule requiring the capitalisation of any expenditure on a physical asset greater than £100). Companies should also detail any changes in judgements, apportionments or adjustments since the prior year, including changes to their capitalisation policies.

### **3.8 Bad debt note**

- 3.8.1 Companies should set out details of their write-off policy and explain any changes from the prior year in their policies, procedures or practices in relation to write-offs along with the reasons for any changes.
- 3.8.2 Where a change in write-off policy (including ‘house-keeping’ exercises) results in a material change in the level of reported write-off, companies should explain whether this level is likely to continue in future years or is being reported as an atypical cost in this report year only.
- 3.8.3 Where a change in the bad debt provisioning policy results in a material change in the bad debt charge, companies should explain the reasons for the movement. The effect of any changes should be quantified.
- 3.8.4 Where there has been significant movement in the trade debtor balance companies should comment on the reasons for the movement. This should refer to outstanding customer debt and the bad debt provision.

### **3.9 Sufficiency of non-financial resources**

- 3.9.1 The annual performance report should also contain a statement as to whether the appointee was in compliance with paragraph 3.1 of Condition K 1 at the end of the financial year.

### **3.10 Sufficiency of financial resources and facilities**

- 3.10.1 The ring fencing provisions in the licence require companies to submit at the same time as the regulatory accounting information, a certificate from the directors stating that the company will have available to it sufficient financial resources and facilities to enable it to carry out, for at least twelve months, its regulated activities and sufficient management resources to enable it to carry out its functions. The requirement for the longer term viability statement is discussed further in section 3.13.
- 3.10.2 For most companies, the provisions in the licence have been extended. In addition to the requirements outlined above, these companies are required to:
- Confirm that in the opinion of the directors all contracts entered into

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<sup>1</sup> For some companies which have had licence modifications recently, this requirement may now be in Condition P of their licence.

with any associated company include all necessary provisions and requirements concerning the standard of service to the company, to ensure that it is able to meet all its obligations as a water and sewerage undertaker;

- submit with each certificate a statement of the main factors which the directors have taken into account in giving that certificate; and
- provide a report prepared by the companies' auditors and addressed to Ofwat, stating whether they are aware of any inconsistencies between the certificate and the financial statements or any information obtained in the course of their work.

### **3.11 Tax Strategy for appointed business**

3.11.1 The Finance Bill 2016 introduced the requirement for large companies to publish their tax strategy annually. We are also requiring all companies to publish details of their tax strategy (relating to the appointed business) within the annual performance report. The tax strategy should cover the following key areas:

- The approach to risk management and governance arrangements;
- The attitude of the company towards tax planning;
- The level of tax risk that the group is prepared to accept; and
- The approach of the company towards its dealings with HMRC.

References and links may be made to tax strategies published in the statutory or group accounts as appropriate.

### **3.12 Differences between statutory and RAG definitions**

3.12.1 Pro formas 1A, 1B, 1C and 1D all have a column to report any resulting differences between statutory and regulatory definitions on a line by line basis. Where any individual values recorded in these lines are considered material then a narrative explanation should be provided on what these differences relate to.

3.12.2 Companies should provide a reconciliation between the total borrowings figures included in the statutory accounts and the borrowings shown in the regulatory accounts with a brief explanation of the reasons for the differences.

### 3.13 Long term viability statement

3.13.1 Companies and their management are responsible for ensuring that they are financially resilient. We expect companies to include a statement<sup>2</sup> in their annual report which confirms that they are financially viable over the longer term. Companies' approach to doing this should comply fully with section C.2.2 of the UK Corporate Code. This requires that they should:

'explain in the annual report how they have assessed the prospects of the company, over what period they have done so and why they consider that period to be appropriate. The directors should state whether they have a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, drawing attention to any qualifications or assumptions as necessary.'

3.13.2 In meeting these requirements we expect companies to prepare and stress test a forward looking business plan in a robust manner and to consider the financial viability of the company over an appropriate forward looking period. Companies are responsible for determining the period over which they make their assessment, however justification for the choice will be required and companies should look beyond the end of the current price control period. We do not expect this to be a constraint. Companies are responsible for determining the appropriate level of stress testing they undertake. Companies are also responsible for determining the level of third party assurance that they believe to be appropriate.

3.13.3 Companies need to include a clear and unambiguous statement in their annual performance report which sets out the steps that company Boards have taken to assess the long term financial viability of the company. We do not expect companies to publish information that is commercially sensitive, but we do expect the statement that they make to clearly set out the approach that they have taken and to provide a suitably robust justification for the selection of the sensitivities that they have undertaken, the forward looking period that has been considered and the extent to which (if any) they have used third party assurance.

3.13.4 If companies publish the same statement in the statutory accounts and this is published simultaneously with the annual performance report then it need only be included in the statutory accounts with a suitable cross reference in the annual performance report.

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<sup>2</sup> [IN 18/04 Expectations for companies in issuing long term viability statements](#)

## **3.14 RORE**

3.14.1 We expect companies to include a statement which explains the movements in RORE compared to the base RORE set at the last price review. Companies should identify and quantify the key components of the out/under performance. RORE should be calculated on an average basis for the period from the start of the AMP.

## **4. Narrative disclosures on performance**

### **4.1 Outcomes**

- 4.1.1 Companies should provide narrative commentary explaining how the information reported in pro forma 3A relates to the information on outcome performance it has published and reported to its customer challenge group or similar body and customers more generally.
- 4.1.2 Companies should provide narrative commentary where it thinks forecasting a reward or penalty in column 3A.6 would be inappropriate for a particular performance commitment. The commentary should explain why a forecast would be inappropriate.

### **4.2 Totex**

- 4.2.1 Narrative commentary should be provided on any difference between the actual and allowed totex values in pro forma 4B. Separate commentary should be provided for both water and wastewater.
- 4.2.2 Commentaries should make reference to the following areas (this is not an exhaustive list):
- efficiency savings;
  - changes resulting from expenditure being delayed or brought forward;
  - expenditure on outputs which are not included in the PR14 baseline; and
  - other changes.
- 4.2.3 Where actual totex includes costs which the company believes to be exceptional or atypical, these should be disclosed separately in the commentary. The commentary should highlight clearly relevant links between the narrative on outcome performance and delivery and the totex costs reported in the year.

### **4.3 Retail**

- 4.3.1 Narrative commentary should be provided on any material difference between the values reported in lines 2C.12 (total operating costs) of pro forma 2C and the retail revenues allowed in price limits for 2015-20. Separate commentary should be provided for household and non-household retail.

4.3.2 Commentaries should make reference to the following areas (this is not an exhaustive list):

- efficiency savings;
- changes in customer numbers;
- changes in metering levels;
- material one-off / atypical items of expenditure; and
- other changes.

## **4.4 Wholesale revenue control reconciliation**

4.4.1 Narrative commentary should be provided on the difference reported in line 2I.26 (difference between allowed and actual revenue under the wholesale control) of pro forma 2I. Companies should explain any subsequent consequences of any variations in revenue for future periods.

4.4.2 Commentaries should make reference to the following areas (this is not an exhaustive list):

- Changes in metering levels;
- Changes in customer demand;
- Numbers of customers;
- Number of new connections; and
- Number of void properties.

4.4.3 Following the commencement of the competitive retail market (on 1 April 2017), companies should disclose both the income and the payments relating to 'performance charges'. It is not sufficient for companies to disclose the net set-off position.

## **4.5 Current tax reconciliation**

4.5.1 A reconciliation is required of the appointed current tax charge or credit reported in line 1A.12 to that resulting from applying the standard corporation tax rate to the profit or loss on ordinary activities for the appointed business before tax and any fair value movements as shown in table 1A. There should be no netting off of material positive or negative amounts.

4.5.2 A reconciliation is also required to explain any significant variations between the appointed current tax charge or credit reported in line 1A.12 for the appointed business to the total current tax charge allowed in price limits. The

reconciliation should quantify the £m difference relating to each particular area and narrative should be provided to explain at a high level the circumstances which led to the difference arising. E.g. If the value of capital allowances claimed is significantly different to that assumed at price limits, has this arisen due to changes in the level or type of expenditure or uncertainty/change around what expenditure would qualify for a particular allowance etc?

4.5.3 The reconciliation should make reference to the following areas (this is not an exhaustive list):

- Prior year adjustments
- Impact of group relief; including any amounts paid for these – these transactions should also be disclosed in the transfer pricing table template (see sections 6.2 and 6.3)
- Effect of corporation tax rate changes

4.5.4 Details of factors affecting future tax charges should be given.

## **4.6 Financial flows**

4.6.1 We are working towards improving the transparency concerning financial flows to the company's investors. This requires a clear comparison between the actual financial flows to investors under the actual capital structures that companies have adopted and what they would have been under the structure we have used for setting the prices that customers pay.

4.6.2 We expect companies to provide a supporting narrative to fully explain and highlight the key features of the analysis. This narrative should aid the understanding and interpretation of the data and is a key element in improving transparency.

## **4.7 New connections**

4.7.1 We expect companies to include a statement which explains the variance between revenues and costs arising from providing infrastructure network reinforcement for developers, which is proportionate to its value. The variance is calculated over a rolling five-year period, as set out in the definition of terms in RAG4.

## 5. Small company accounting information requirements

### 5.1 Small company requirements

- 5.1.1 For new and existing small companies it may not be appropriate to request the full regulatory accounting information that we receive from larger companies, but we still require some regulatory accounting information to a 31 March year end.
- 5.1.2 The information requirements should be proportionate to the size of the company, but sufficient to enable us to effectively regulate these companies. **We define a company with an annual turnover of less than £10.2m as small in terms of regulatory accounting information requirements<sup>3</sup>.** This threshold only applies to regulatory accounting information required under Condition F and no other types of information.
- 5.1.3 In some circumstances, we may ask some small companies for more information than is set out below, to address certain company specific issues. If required, we will discuss this with the company to explain what information we require and when it should be submitted.
- 5.1.4 Table 2 below sets out the requirements for companies that fall below the **Small company** threshold. These should all be prepared by 15 July following the year end.

**Table 2 Small company requirements**

Requirement	Where
Accounts prepared to a 31 March year end. These should also be available on your website at the same time they are submitted to us	Paragraph 2.1.1
Certificate of adequacy of financial resources	Licence condition I 17
Two pro forma tables S1. Split of turnover, operating costs and depreciation S2. Volumes and connections	Appendix 1 See RAG4 for line definitions
Statement on links between Directors' pay and standards of performance published in the accounts	paragraphs 3.2, 3.2.8, and 3.2.9
Statement of dividend policy published in the accounts	paragraph 3.4

<sup>3</sup> This is also the turnover threshold below which the government allows limited companies to file abridged accounts with Companies House.

## **6. Transactions with associates and the non-appointed business**

### **6.1 RAG5 Principles**

- 6.1.1 Appointees are under a duty to trade at arm's length and to ensure that there is no cross-subsidy with respect to transactions between the appointed business and both associated companies and the non-appointed business.
- 6.1.2 In addition following the introduction of separate binding price controls at the 2014 price review, companies need to attribute or allocate costs between the controls. The revenue allowance for each price control is determined by the estimated costs specific to that particular price control and comparable information on actual costs will be needed for future price reviews. Therefore companies should also ensure that there is no cross subsidy between price control units.
- 6.1.3 Appointees are required to demonstrate, through the application of the principles set out in RAG5, the basis of arm's length trading and that there is no cross- subsidy.

### **6.2 Transactions to be disclosed**

- 6.2.1 The licence requires that all transactions between the appointee and its associated companies must be disclosed and if any single transaction exceeds 0.5% of the turnover of the appointed business (or £100,000 if greater) it should not be aggregated. In particular, the following transactions, with related data, must be disclosed if over the materiality limit:
- loans by or to the appointee;
  - dividends paid to any associated company;
  - guarantees or other forms of security by the appointee;
  - transfer of any asset or liability by or to the appointee;
  - transfer of any corporation tax group losses by or to the appointee;
  - supply of any service by or to the appointee;
  - omission by the appointee or any associated company to exercise a right as a result of which the value of the net assets of the appointee is decreased; and
  - waiver of any consideration, remuneration or other payment by the appointee.

- 6.2.2 The licence also specifies the information to be disclosed for each of these categories of transactions. Where appropriate, formulae may be disclosed in place of figures, for example for interest rates.
- 6.2.3 Transactions in the last three categories may be aggregated with any other similar transaction in the same category with the same associated company (unless prohibited by the ‘single transaction’ rule in 6.2.1). This aggregation does not include netting off transactions to the appointee against transactions by the appointee or vice versa.
- 6.2.4 Additionally where more than one associated company has transactions which are below the threshold then these should not be amalgamated such that there becomes a disclosure between the appointee and ‘various’ associates, even for common transaction types.
- 6.2.5 If a company is an associated company of an appointee for only part of a financial year then transactions with that associated company will only need to be disclosed whilst they were an associated company.
- 6.2.6 Amounts disclosed should not be rounded below the £1,000 level e.g. £0.652m rather than £0.7m.

### 6.3 Transfer pricing table templates

- 6.3.1 The disclosures required should be included in the published annual performance report in three separate tables:

Service	Company	Turnover of associate	Terms of supply	Value
Service received by regulated business.	Associate providing the service.		A statement of the means by which the price charged by the associates has been established, e.g., competitive tendering.	Value of service received by regulated business.
Corporation tax group relief received by regulated business	Associate surrendering the group relief.		A statement of the means by which the payment for the group relief has been established (including the amount paid).	Value of group relief.

<b>Service</b>	<b>Company</b>	<b>Turnover of associate</b>	<b>Terms of supply</b>	<b>Value</b>
Service provided by regulated business.	Associate to whom the service is provided.		A statement of the means by which the price charged to the associates has been established, e.g., competitive tendering.	Value of service provided by regulated business.
Corporation tax group relief surrendered by regulated business	Associate receiving the group relief.		A statement of the means by which the payment for the group relief has been established (including the amount received).	Value of group relief.

<b>Service provided to the non- appointed business</b>	<b>Basis of recharge made by the appointed business</b>	<b>Value of the recharge made by the appointed business</b>
Treatment of imported sludge	Where appointed business assets have been used to carry out non-appointed activities, then the basis of the recharge should be explained. This should include an explanation as to the contribution to depreciation and finance costs of the assets as well as the incremental operating expenditure and any rental for land or buildings.	Value of the recharge made by the appointed business.
Treatment of tankered waste	Where appointed business assets have been used to carry out non-appointed activities, then the basis of the recharge should be explained. This should include an explanation as to the contribution to depreciation and finance costs of the assets as well as the incremental operating expenditure and any rental for land or buildings.	Value of the recharge made by the appointed business.
Other	Where appointed business assets have been used to carry out non-appointed activities, then the basis of the recharge should be explained. This should include an explanation as to the contribution to depreciation and finance costs of the assets as well as the incremental operating expenditure and any rental for land or buildings.	Value of the recharge made by the appointed business.

## Appendix 1: Pro forma tables

<b>Section 1 Regulatory financial reporting</b>	
Pro forma 1A	Income statement
Pro forma 1B	Statement of comprehensive income
Pro forma 1C	Statement of financial position
Pro forma 1D	Statement of cash flows
Pro forma 1E	Net debt analysis at 31 March 20xx
Pro forma 1F	Financial flows for the 12 months ended 31 March 20xx and for the AMP to date (2012-13 financial year average RPI)
<b>Section 2 Price review and other segmental reporting</b>	
Pro forma 2A	Segmental income statement for the 12 months ended 31 March 20xx
Pro forma 2B	Totex analysis for the 12 months ended 31 March 20xx - wholesale water & wastewater
Pro forma 2C	Operating cost analysis for the 12 months ended 31 March 20xx - retail
Pro forma 2D	Historic cost analysis of tangible fixed assets - wholesale & retail
Pro forma 2E	Analysis of 'grants and contributions' and land sales for the 12 months ended 31 March 20xx - wholesale
Pro forma 2F	Household - revenues by customer type
Pro forma 2G	Non-household water - revenues by tariff type
Pro forma 2H	Non-household wastewater - revenues by tariff type
Pro forma 2I	Revenue analysis for the 12 months ended 31 March 20xx
Pro forma 2J	Infrastructure network reinforcement costs for the 12 months ended 31 March 20xx
Pro forma 2K	Infrastructure charges reconciliation for the 12 months ended 31 March 20xx
<b>Section 3 Performance summary</b>	
Pro forma 3A	Outcome performance table
Pro forma 3B	Sub-measure performance table
Pro forma 3C	AIM (Abstraction Incentive Mechanism)
Pro forma 3D	SIM (Service Incentive Mechanism)
Pro forma 3S	Shadow reporting of new definition data

<b>Section 4 Additional regulatory information</b>	
Pro forma 4A	Non-financial information for the 12 months ended 31 March 20xx
Pro forma 4B	Totex analysis
Pro forma 4C	Impact of AMP performance to date on RCV
Pro forma 4D	Totex analysis for the 12 months ended 31 March 20xx - wholesale water
Pro forma 4E	Totex analysis for the 12 months ended 31 March 20xx - wholesale wastewater
Pro forma 4F	Cost analysis for the 12 months ended 31 March 20xx – household retail
Pro forma 4G	Wholesale current cost financial performance for the 12 months ended 31 March 20xx
Pro forma 4H	Financial metrics for the 12 months ended 31 March 20xx
Pro forma 4I	Financial derivatives
Pro forma 4J	Atypical expenditure by business unit for the 12 months ended 31 March 20xx - wholesale water
Pro forma 4K	Atypical expenditure by business unit for the 12 months ended 31 March 20xx - wholesale wastewater
Pro forma 4L	Enhancement capital expenditure by purpose for the 12 months ended 31st March 20xx - wholesale water
Pro forma 4M	Enhancement capital expenditure by purpose for the 12 months ended 31st March 20xx - wholesale wastewater
Pro forma 4N	<b>Sewage treatment - Functional expenditure for the 12 months ended 31st March 20xx</b>
Pro forma 4O	Wholesale wastewater service - Large sewage treatment works for the 12 months ended 31 March 20xx
Pro forma 4P	Non-financial data for WR, WT and WD for the 12 months ended 31st March 20xx - wholesale water
Pro forma 4Q	Non-financial data - Properties, population and other for the 12 months ended 31st March 20xx - wholesale water
Pro forma 4R	Non-financial data - Wastewater network and sludge for the 12 months ended 31st March 20xx - wholesale wastewater
Pro forma 4S	Non-financial data - Sewage treatment for the 12 months ended 31st March 20xx - wholesale wastewater
Pro forma 4T	Non-financial data - Sludge treatment for the 12 months ended 31st March 20xx - wholesale wastewater
Pro forma 4U	Non-financial data - Properties, population and other for the 12 months ended 31st March 20xx - wholesale wastewater
Pro forma 4V	Operating cost analysis for the 12 months ended 31 March 20xx - water resources
Pro forma 4W	<b>Operating cost analysis for the 12 months ended 31 March 20xx - sludge transport, treatment and disposal</b>
<b>Small company return</b>	
Pro forma S1	Analysis of turnover and operating costs
Pro forma S2	Number of connections and site consumption

Follow this link for the [Pro forma tables 2018-19](#)

## Appendix 2: Accounting methodology statement

This appendix sets out our requirements for the disclosures to be included in companies' accounting methodology statements. Each company must publish their statement either on their website or in the annual performance report.

The 2 areas that should form the focus of the statement will be to describe how costs are reported across:

- Price control units (annual performance report section 2); and
- Wholesale upstream services (annual performance report section 4).

### High level overview

Details of the company's systems for producing disaggregated cost and asset data (eg spreadsheets or integrated accounting systems), including any changes year on year.

### Price control units

We expect that companies will apply the principles and guidance set out in RAG 4.

Companies should:

- Confirm they have followed the principles and guidance set out in RAG 4;
- Describe the method or cost driver that the company has used to calculate allocations between the price control units (where specific guidance has not been prescribed);
- Where there has been a change to the methodology compared to the previous year give reasons for the change and quantify the impact;
- Describe significant changes in reported costs at the price control unit level compared to the previous year;
- Where there has been a significant movement in a particular cost type (e.g. power or local authority rates) between the price control units then reasons for this should be included;
- For both 'power' costs and 'other operating expenditure' quantify the percentage split between directly coded and allocated costs;
- Describe how power costs are disaggregated when it is consumed at sites that cover more than one price control unit;
- Quantify the percentage split of M&G costs across the price control units; and

- Describe any planned improvements for future years.

For assets companies should adopt the 'principal use' rules whereby the asset is recorded in a single price control unit which then makes recharges.

Companies should:

- Confirm they have followed the principal use rules set out in RAG 4;
- Describe the method used to calculate the appropriate recharge. This should have reference to the depreciation and the finance costs of maintaining the asset; and
- Describe any significant movements in the amounts recharged between the price control units.

Companies should also refer to the equivalent recharges to the non-appointed business for activities set out in appendix 1 of RAG4 such as tankered waste.

## **Wholesale upstream services**

Companies should provide an explanation of:

- how the company has disaggregated the operating costs across the upstream services for each cost type, specifying cost drivers where necessary;
- Describe how power costs are disaggregated when it is consumed at sites that cover more than one upstream service;
- how treated bulk supply imports have been allocated between water resources and water treatment;
- the derivation of the quantities used to calculate the unit cost information,
- Significant changes in reported costs at the upstream services level compared to the previous year;
- Where there has been a significant movement in a particular cost type (eg power or local authority rates) between the upstream services then reasons for this should be included; and
- Where there has been a significant movement in a particular unit cost then reasons for this should be included.

Where companies encounter difficulties in completing tables 4D and 4E, they should describe how they have completed the table and suggest how alternative methods could be used.

## Appendix 3: Basis for requesting information

OFWAT has the power to request information in licence conditions B, F, I, K, M and P. This appendix sets out our requirements along with the relevant licence condition under which it is requested.

### Pro forma tables

Section 1 Regulatory financial reporting		Accounting - information - licence condition F	Other information - licence condition M
Pro forma 1A	Income statement	✓	
Pro forma 1B	Statement of comprehensive income	✓	
Pro forma 1C	Statement of financial position	✓	
Pro forma 1D	Statement of cash flows	✓	
Pro forma 1E	Net debt analysis at 31 March 20xx	✓	
Pro forma 1F	Financial flows for the 12 months ended 31 March 20xx and for the AMP to date (2012-13 financial year average RPI)	✓	
Section 2 Price review and other segmental reporting			
Pro forma 2A	Segmental income statement for the 12 months ended 31 March 20xx	✓	
Pro forma 2B	Totex analysis for the 12 months ended 31 March 20xx - wholesale water & wastewater	✓	
Pro forma 2C	Operating cost analysis for the 12 months ended 31 March 20xx - retail	✓	
Pro forma 2D	Historic cost analysis of tangible fixed assets - wholesale & retail	✓	
Pro forma 2E	Analysis of 'grants and contributions' and land sales for the 12 months ended 31 March 20xx - wholesale	✓	
Pro forma 2F	Household - revenues by customer type	✓	✓
Pro forma 2G	Non-household water - revenues by tariff type	✓	✓
Pro forma 2H	Non-household wastewater - revenues by tariff type	✓	✓
Pro forma 2I	Revenue analysis for the 12 months ended 31 March 20xx	✓	
Pro forma 2J	Infrastructure network reinforcement costs for the 12 months ended 31 March 20xx	✓	
Pro forma 2K	New connections reconciliation for the 12 months ended 31 March 20xx	✓	
Section 3 Performance summary			
Pro forma 3A	Outcome performance table	✓	✓
Pro forma 3B	Sub-measure performance table	✓	✓
Pro forma 3C	AIM (Abstraction Incentive Mechanism)		✓
Pro forma 3D	SIM (Service Incentive Mechanism)		✓
Pro forma 3S	Shadow reporting of new definition data		✓

<b>Section 4 Additional regulatory information</b>		<b>Accounting information - licence condition F</b>	<b>Other information - licence condition M</b>
Pro forma 4A	Non-financial information for the 12 months ended 31 March 20xx		✓
Pro forma 4B	Totex analysis	✓	
Pro forma 4C	Impact of AMP performance to date on RCV	✓	
Pro forma 4D	Totex analysis for the 12 months ended 31 March 20xx - wholesale water	✓	✓
Pro forma 4E	Totex analysis for the 12 months ended 31 March 20xx - wholesale wastewater	✓	✓
Pro forma 4F	Cost analysis for the 12 months ended 31 March 20xx – household retail	✓	
Pro forma 4G	Wholesale current cost financial performance for the 12 months ended 31 March 20xx	✓	
Pro forma 4H	Financial metrics for the 12 months ended 31 March 20xx	✓	
Pro forma 4I	Financial derivatives	✓	
Pro forma 4J	Atypical expenditure by business unit for the 12 months ended 31 March 20xx - wholesale water	✓	
Pro forma 4K	Atypical expenditure by business unit for the 12 months ended 31 March 20xx - wholesale wastewater	✓	
Pro forma 4L	Enhancement capital expenditure by purpose for the 12 months ended 31st March 20xx - wholesale water	✓	
Pro forma 4M	Enhancement capital expenditure by purpose for the 12 months ended 31st March 20xx - wholesale wastewater	✓	
Pro forma 4N	Sewage treatment - Functional expenditure for the 12 months ended 31st March 20xx	✓	
Pro forma 4O	Wholesale wastewater service - Large sewage treatment works for the 12 months ended 31 March 20xx	✓	✓
Pro forma 4P	Non-financial data for WR, WT and WD for the 12 months ended 31st March 20xx - wholesale water		✓
Pro forma 4Q	Non-financial data - Properties, population and other for the 12 months ended 31st March 20xx - wholesale water		✓
Pro forma 4R	Non-financial data - Wastewater network and sludge for the 12 months ended 31st March 20xx - wholesale wastewater		✓
Pro forma 4S	Non-financial data - Sewage treatment for the 12 months ended 31st March 20xx - wholesale wastewater		✓
Pro forma 4T	Non-financial data - Sludge treatment for the 12 months ended 31st March 20xx - wholesale wastewater		✓
Pro forma 4U	Non-financial data - Properties, population and other for the 12 months ended 31st March 20xx - wholesale wastewater		✓
Pro forma 4V	Operating cost analysis for the 12 months ended 31 March 20xx - water resources	✓	
Pro forma 4W	Operating cost analysis for the 12 months ended 31 March 20xx - sludge transport, treatment and disposal	✓	
<b>Small company return</b>			
Pro forma S1	Analysis of turnover and operating costs	✓	
Pro forma S2	Number of connections and site consumption		✓

## RAG3 disclosure requirements

RAG3 Accounting disclosures requirements		Accounting information - licence condition F	Other information - licence condition M	Other information - licence condition B	Other information - licence condition K	Ring fencing provisions - licence conditions I or P	Other information - statutory
3.1.1 3.2	Note which describes the link between directors' pay and standards of performance						✓
3.1.1 3.3	Statement as to disclosure of information to auditors	✓					
3.1.1 3.4	Statement on dividend policy for the appointed business	✓	✓				
3.1.1 3.5	Accounting policy note for price control units	✓					
3.1.1 3.6	Note on revenue recognition	✓					
3.1.1 3.7	Note on capitalisation policy	✓					
3.1.1 3.8	Note on bad debt policy	✓					
3.1.1 3.9	Sufficiency of non-financial resources		●		■	■	
3.1.1 3.10	Sufficiency of financial resources and facilities				●	◆	
3.1.1 3.11	Tax strategy for the appointed business,	✓					
3.1.1 3.12	Statement on differences between statutory and RAG definitions,	✓					
3.1.1 3.13	Long term viability statement,	✓					
3.1.1 3.14	Statement explaining out/under performance of the return on regulatory equity (RORE)	✓					
RAG3 Narrative disclosure requirements							
4.1	Outcomes		✓	✓			
4.2	Totex	✓	✓				
4.3	Retail	✓	✓				
4.4	Wholesale revenue control	✓	✓				
4.5	Current tax reconciliation	✓	✓				
4.6	Financial flows	✓	✓				
4.7	New connections	✓	✓				
RAG3 Small company disclosure requirements							
5.1.4	Sufficiency of financial resources					◆	
5.1.4	Statement on links between Directors' pay and standards of performance published in the accounts						✓
5.1.4	Statement of dividend policy published in the accounts	✓	✓				
RAG3 Transfer pricing disclosure requirements							
6.2	Transactions with associates			✓			
6.3	Services received and provided by the regulated business from/to an associate			✓			
6.3	Corporation tax group relief received and surrendered by the regulated business from/to an associate			✓			
6.3	Services provided by the non-appointed business			✓			

### Key

●	For Tideway
◆	Authorisation is contained in either condition I or condition P, depending on when a company's licence was last updated.
■	Authorisation is contained in either condition K or condition P, depending on when a company's licence was last updated.

Ofwat (The Water Services Regulation Authority) is a non-ministerial government department. We regulate the water sector in England and Wales. Our vision is to be a trusted and respected regulator, working at the leading edge, challenging ourselves and others to build trust and confidence in water.

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