Consultation questions and responses

We have published the responses to the consultation on our website. Below we summarise responses to consultation questions and our actions.

Questions relating to 2018-19 reporting

	Question	Consultation response	Our response
Q1	**Transparency of financial flows - Appendix 1 contains our new table 1F;**		
Q1.a	**Do you agree with the scope of the proposed information items in the new table?**	15 responses, 14 agreed. One respondent strongly disagrees **with reporting the cost of debt and hedging instruments separately**. Whilst the majority of the respondents were in favour of the proposals, there were a number of areas that respondents felt needed further considerations:	We have noted that in some instances the use of derivatives has **increased rather than mitigated** financial risk. As such in order to identify the use of derivatives we require, for transparency, that the cost of debt and the impact of hedging instruments **should be reported separately**.
		Three respondents commented that it would helpful to provide additional guidance on some of the line definitions.	We have reviewed the guidance and line definitions and provided further clarity as appropriate.

		Two respondents commented that the financial flows metric should be included in section 4 and as such not subject to full audit.	We disagree. This is a key metric to demonstrate the returns to shareholders and in order for wider stakeholders to have trust and confidence in the data, it should be subject to independent audit.
		One respondent commented that consideration should be given to the capital financial flows associated with a loan advance made to direct/indirect parent companies.	We agree that these types of transactions are relevant to financial flows and we will look into the impact of incorporating them into the metric in for the 2020-25 price review period.
		One respondent commented on how exceptional items should be reported, are they reported separately or removed from the analysis.	We have amended the table to include an additional line in section C for 'Other exceptional items'. With a line definition of exceptional items that are outside the normal operating activities i.e. the profit on disposal of the Retail Non-household part of the business. Note: if the line is used then the company must include an appropriate and clear supporting narrative of the associated transaction(s).
		One respondent requested confirmation that section 1F does not apply to Thames Tideway.	We can confirm that 1F does not apply to Thames Tideway.
		One respondent commented that they had concerns that the data would not be understood by the average customer.	Companies are required to provide an appropriate and clear supporting narrative, explaining their data in a manner that can be easily understood by all stakeholders.

		One respondent commented that they do not believe that a gearing adjustment should be applied to column “Actual returns and notional regulatory equity”, as the column refers to notional equity not actual equity.	We agree, that the “Actual returns and notional regulatory equity” column should not include a gearing adjustment. We have amended the table and line definitions to clearly indicate this.
Q1.b	**Is there any information missing from this table which you think should be included in order to achieve transparency and consistency for financial flows reporting?**	There were five responses to this question, with the majority suggesting the need for clarification or amendments to the components included. The areas identified were as follows:	
		For companies that have exited the Retail Non-Household market, have a methodology that is consistent, i.e. remove the Retail Non-Household margin from RoRE (notional return and equity)	We have amended the line definition for Line 1 to reflect that companies that have exited the Retail Non-household market should remove the associated margin from base RoRE from the year exit happened. We have also included an additional line in section C for 'Other exceptional items'. With a line definition of exceptional items that are outside the normal operating activities i.e. the profit on disposal of the Retail Non-household part of the business. Note: if the line is used then the company must include a detailed analysis and an appropriate and clear supporting narrative of the associated transaction(s).
		A number of respondents requested clarifications / amendments to some of the guidance notes and line definitions.	We have reviewed the guidance and line definitions and provided further clarity as appropriate.

		One respondent commented that it would be important to understand the audit opinion statement required, in particular where judgements are made on attributing reasons for Totex variances.	In our view we do not see that we should make any changes to the standard audit opinion statement as financial flows is no different to any other area within the financial statements requiring judgements to be made by companies in their preparation.
		One respondent commented that it would be useful for Ofwat to clarify what supporting narrative it expects companies to include with the table.	As we have previously stated, the onus is on companies to provide the additional commentary which is necessary to make the information presented clear and accessible.
Q1.c	**Do any of the line item definitions require further explanation?**	There were eight responses to this question, with the majority suggesting the need for clarification or queries relating to certain line item definitions. The areas identified were as follows:	
		Clarification of line definitions: • Variance in Corporation Tax • Cost of Debt (adjusted for hedging instruments) • Hedging Instruments • Interest received on intercompany loans • Return on Regulatory Equity • Gearing	We have reviewed the guidance and line definitions and provided further clarity as appropriate.

		One respondent requested clarity regarding the units required for reporting financial values in the tables.	The tables have been updated to clearly identify the reporting values required.
		One respondent requested guidance where values within the table are aligned with data reported elsewhere in the APR, Financial Determinations or other published data.	Where data is already reported elsewhere, we have incorporated the reference into the relevant line definition.
		One respondent requested clarity regarding the calculation of the Regulatory Capital Value (RCV).	To ensure consistency we have decided to publish the values for notional and historical actual regulatory equity on our website alongside the annual publication of the RCVs. This should improve consistency in reported data.
		One respondent commented that they felt that to ensure consistency on the calculation of regulatory equity, there should be no discretion on using the average of opening and closing values.	We have amended the line definition to reflect the answer in the above point.
		Two respondents suggested changes to some of the line headings.	We have considered the proposed changes and where the suggestions enhanced the understanding of the line in question we have incorporated the proposed change.
		One respondent suggested that it would be helpful if the APR tables' auto calculate the values where possible, as per the template issued for last year's submission.	It is our intention to auto calculate as much if the APR tables as possible, and we are working towards this.

Q2	**New connections - Appendix 1 contains our new table 2K;**		
Q2.a	**Do you agree with the scope of the proposed information items in the new table?**	13 responses, 13 agreed All of the respondents were in favour of the proposals, however there were some areas that respondents felt needed further consideration:	
		One respondent commented that it would be helpful to expand the definition of line 2K.4 – Variance brought forward.	Covered in 2c).
		One respondent commented that the table should be presented on a 5 year basis.	The table presents a cumulative view and as such will cover a 5 year period.
		One respondent disagreed with the definition of the revenue figures (line 2K.5) as this refers to being equal to the gross figure in tables 2B and 2J, as their infrastructure charges for 2018-19 and 2019-20 have been set after taking any discounted infrastructure charges into account.	In our view the infrastructure charges should be set at on a gross basis ie before taking any appropriate discounts into account.
Q2.b	**Is there any information missing from this table which you think should be included in order to achieve**	There were four responses to this question, all of which agreed with the proposals but raised areas that they felt required further considerations:	
		One respondent commented that the table does not include any data relating to New Connections, even though this in included in the table name.	We have changed the table name to remove “New Connections”, so as to remove any ambiguity.

	transparency and consistency for new connections reporting?	One respondent suggested that an additional line for 'prior period adjustment' be added and also the inclusion of additional columns to present the 5 year period / rolling performance.	We do not see the need for an additional line for 'prior period adjustments'. The table presents a cumulative view and as such will cover a 5 year period.
		One respondent suggested that the report will need to evolve in reporting year 2023-24 when there will be over 5 years of rolling cumulative data.	We recognise that there is a requirement to amend the reporting requirements from 2023-24 onwards to take account of the rolling 5 year reporting requirement. This will be incorporated into future consultations.
		One respondent commented that any cross references and data validation checks that could be incorporated would be very useful.	We checked that the line definitions already include cross references to other tables. We do not think that any further validation checks need to be included in the RAGs.
Q2.c	**Do any of the line item definitions require further explanation?**	There were eight responses to this question, with the majority suggesting the need for clarification of certain line item definitions. The areas identified were as follows:	
		One respondent queried as to whether Welsh companies are expected to complete the tables.	We can confirm that only the companies that are wholly or mainly in England are expected to complete the tables. (As per our decision document 'Charging rules for New Connection' published December 2016).
		Two respondents suggested that it would be helpful to expand the definition of line 2K.4 –	We have amended the definition of line 2K.4. Any changes or updates required as a

		Variance brought forward. Also, they commented that the definitions would need to be improved in light of the PR19 submissions.	consequence of PR19 will be considered for the 2020-21 reporting year.
		Two respondents requested clarification on: a. For line 2K.1 which column should it link from in table 2E? b. Line 2K.2, what is meant by discounts c. What period is covered by the data, all connections data or since 1 April 2018 when the new rules came into effect?	a. Line 2K.1 should link to lines 2E.2 and 2E.9 'total' column – this has been clarified in RAG4. b. Discounts are any efficiency incentives the company offers, for example the installation of water efficient devices. This was set out in the definition of 2K.3 in our consultation but has now been moved to 2K.2 c. The data in lines 1-3 covers infrastructure charges received in the 12 month period to 31 March 2019 and therefore lines 4-7 commence at the same point.
		One respondent asked for clarification that on line 2K.4 for 2018-19 the value is nil, and going forward should it be split between water and waste water.	For 2018-19 the value on line 2K.4 should be zero as per point 2). We suggest that any amendment to the table to show the variance brought forward to being split between water and wastewater should be deferred until the 2020-21 reporting year.
		One respondent commented that there needs to be more explanation of what is considered administration / providing information for new connections.	In our view this is not relevant to the information in this table.

Q3	**What are your views on the proposed changes to the existing tables in Appendix 1?**	There were 139 points made in the responses to this question, with several respondents suggesting the need for clarification or corrections to certain line item definitions. Many respondents raised the same, or similar points. The areas that attracted most discussion were: • Financial flows • New connections • Cost assessment • Outcomes • Impact of performance on RCV	56 of the 139 points raised led to amendments to the RAGs. These are included in the List of changes to the RAGs. There are 4 points made which we agree should be addressed. However we do not agree that these should be included in the 2018-19 RAGs. Our preference is to explore these more fully with a view to implementing them for the 2020-21 reporting year. The areas covered by these points are; • 'Principal use' recharges between price control areas, • Differences in presentations of bank overdrafts between the APR and the PR19 business plan tables, • Presentation of intangible assets; and, • Pension deficit recovery payments for companies who produce statutory accounts in the FRS102 basis. There were a further 78 points for which we did not amend the RAGs.

			We will update the common reporting definitions in line with the proposals that companies have made to increase clarity.
Q4	**What are your views on the issues highlighted in section 3 'Future developments in performance reporting'?**		
Q4.1	**New accounting standard; IFRS 16 - Leasing**	8 responses, 7 agreed that the RAGs should not diverge from UKGAAP in 2019-20 when the new accounting standard will become mandatory. One company suggested that the RAGs should retain the existing UKGAAP treatment for an additional year and only allow IFRS 16 treatment from 2020-21.	We do not agree to the suggestion to diverge from UKGAAP – for 2019-20 companies should be able to explain and quantify the operating costs that would have been recorded as expenditure in the income statement under the previous reporting regime so that the difference can be explained and compared with the forecasts included in the business plan.
Q4.2	**Table 2A - Impact of additional price control units**	14 responses, 14 agreed. All respondents who gave a view were in favour of the proposals. However there were areas that respondents felt needed further consideration;	In our PR19 final methodologies for Water resources and Bioresources we set out some expectations with respect to development and publication of notional charges for water resources, bioresources, and separate charges for network plus.

		• Three respondents raised concerns about splitting revenues; – How should revenue be split? – Would wholesale charging rules provide more clarity? – Could the tariff model be used? – Should RAG4 appendix 1 be expanded to cover price control units? • Two respondents had concerns about 'principal user'. • Recharges were identified by 5 respondents as requiring further clarification as to how these should be disclosed. • Other costs noted as requiring further clarification for reporting were highlighted; – recharges for sludge liquors treated by Network+, – Borehole pumping for both water resources and Network+.	We agree that we should seek to change the way recharges are presented in the APR in tables 2B, 4D and 4E. We will work with companies in order to introduce revised disclosure requirements for 2020-25. We will meet with companies who have raised specific points and discuss any revised proposals at a RAWG meeting later in 2019.
Q4.3	**Bioresources trading**	7 responses, 6 agreed. • Three respondents stated that further general guidance was needed in this area. • One respondent thought that specific areas to be addressed included;	We agree that further agreed guidance may help reporting in this area. The suggestion to report volumes would help to make information comparable between companies. Companies would have the option of including narrative to explain any regional variations that may exist.

		– Imported sludge volumes should be recorded to add value to the financial information, – recharges for sludge liquors treated by Network+, – temporary use of portable assets to cover asset breakdowns, – Recognition that there could be local variability hidden behind the company wide position.	We will address the detailed points on recharges and breakdown mitigation costs with companies on an individual basis and at a future RAWG meeting.
Q4.4	**Impact of Retail non-household exit**	There were eight responses to this question, with all suggesting the need for clarification or reclassification of certain activities. Activities which the RAGs, and therefore price control, states are retail activities but which respondents disagree on are as follows: – Customer side leakage costs, – Developer services in relation to new connections, – Investigatory visits (where the cause of the investigation is not a network issue). Three respondents were clear that there should not be costs recorded in retail where they had exited	We are aware that this has been an area of confusion for many respondents. It appears that the cost burden for some of the activities which were defined at PR14 have not precisely matched the practical boundaries which were in place either before or after retail exit for some companies. Taking developer services as an example, the PR14 assumption was that most of the developer contact would be via a retailer, with wholesale retaining a smaller function which would then interact with only a small number of retailers. In reality it appears that developers have by-passed the retailer route and contacted wholesalers directly.

		the market but one thought that it should remain in wholesale as there was associated income. One respondent thought that administration of developer services should be moved to wholesale or to non-appointed activities.	We do not anticipate that the costs in question are significant in respect of the wholesale business. We would agree with the principle that where a company has exited retail, then we would not ordinarily expect to see any costs being reported by the exiting company under retail. All of those relevant costs should fall to the exiting entity according to the boundaries defined in the price control.
Q4.5	**Income from 'diversions' activity**	10 responses; 6 agreed , 4 disagreed Of those that disagreed, three respondents thought that there was more uncertainty associated with forecasting diversions activity and as such there were likely to be significant true-up adjustments.	Our overriding principle is that all revenues should be considered as being part of the price control **unless** they are defined as excluded charges by licence condition B. We will clearly set out our approach in the PR19 draft and final determinations. Reporting over 2020-25 will need to be consistent with this.
Q5	**What are your views on our preference to require all costs associated with the 'Traffic management act' to be reported?**	15 responses; 6 agreed with collecting all costs, 8 were in favour of collecting direct costs only and one disagreed with collecting cost information. The respondent that disagreed questioned the use of such information.	We agree that collecting direct costs and the associated administration costs only would result in the highest level of consistency of reporting and we have amended RAG4 to confirm this.

Q6	**What are your views on our additional asset type descriptions for Water resources which recognise ‘desalination’ and ‘effluent reuse’ abstraction assets?**	10 responses; 9 agreed with the new definitions although one of these suggested some schematic guidance would assist the interpretation of this. One respondent stated that more technical guidance was needed over and above our proposals.	We would be happy to work with the industry to enhance our RAG guidance in this area. We could discuss this at the next RAWG meeting.