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TO: OfwatPandO@ofwat.gov.uk
Sent by email only

Monday 2nd August 2021

Dear Ofwat,

Overhead cost reporting – revising RAG2 (consultation)

We are pleased to offer our comments on the proposals set out in this consultation. We respond to the proposals of the consultation, including the specific questions.

Question 1: Do you agree with the guidance that we propose adding to RAG2?

The extra guidance is welcomed but the earlier it can be finalised the better, as this will allow us sufficient time to build any changes into our reporting systems.

Question 2 Are the 'general and support' categories carried over from RAG 2.08 still appropriate? If not then what should we use instead?

The categories in RAG 2.08 are still appropriate but we would like to suggest a disaggregation of reporting between general and support costs within business streams and genuine corporate level overhead such as IT, Finance and HR. This would allow a more useful benchmarking between companies, especially if this was accompanied by clear assumptions in the methodology statements. Consistent and transparent treatment of overhead allocation, which can be significant contributors to total costs, could avoid companies appearing as more efficient in certain price controls, simply because of inconsistent allocations.

Question 3 Are there any areas that we have not covered by these proposals that we should?

We request a clearer boundary for smart metering activities and the associated data recovery systems between water network plus and retail. These data recovery systems provide benefits to both water network+ (e.g. for leakage calculation) and retail price controls (provision of consumption data to customers), and we therefore believe costs should be allocated consistently between the two.

Question 4 For 2021-22 we are considering asking companies to report costs on both their existing approach and the new approach so that we can understand the impact that this has on the allocation of costs across controls. Would you agree with this approach? If not then how could we assess the impact of this in advance of the PR24 business plan submissions?

This depends on the extent of the changes. If the new RAGs fundamentally change how our reporting systems need to work (e.g. new Developer Services price control) it is going to be very difficult to produce two sets of reporting tables. Regardless of whether there are significant changes or not, two sets of reporting tables will cause a significant amount of extra work as there are multiple levels of control, reconciliation and assurance that will need to be performed.

If general and support costs need to be allocated to Developer Services separately then the APR data tables should reflect this i.e. an “Other operating expenditure” line within tables 4N &O. We don’t want to be in the position of producing two versions of the APR. A shadow reporting table could be a viable option and preferable to just reporting in the commentary.

We also believe that it is unhelpful to have RAG guidance now that reflect possible future changes in price controls. Developer Services is not a price control this AMP so should not appear in the RAGs until it is. The RAGs should be the “rulebook” to the APR not the future rulebook.

Yours Sincerely,

[redacted]

Alex Plant
Director of Strategy & Regulation