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REC22: Ofwat Cost Benchmarking RFI Guidance – February 2022

Ofwat

Cost benchmarking – RFI Guidance

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1. Introduction

1.1 Background to the RFI

Since the opening of the business retail market in 2017, regulatory protections have been in place to protect the interests of business customers who have not engaged in the market¹. Regulatory safeguards in the form of price and non-price protections are set in place via the Retail Exit Code (REC). These were last revised in 2018-19, with revisions to both price and non-price protections taking effect from April 2020. We signalled at that time that we would look to review these terms in due course – particularly in the light of developing market conditions and the extent to which the market is functioning effectively.

We are now commencing our review, with the aim that any resulting revisions to price and/or non-price protections will take effect from April 2023. We set out our proposed approach to our review in our [December 2021 Consultation](#).

A fundamental part of our REC review will be to understand the efficient retail business costs of serving customers. A particular focus will be to better understand costs and cost drivers for Group One customers, with a view to understanding and assessing the costs, on a forward-looking basis, that an efficient Retailer might incur in serving them. We will also have regard to costs of serving customer Groups Two and Three.

We are therefore, through this RFI, seeking detailed cost and other data from Retailers. The data set we seek is intended to help us assess how costs have developed since market opening and in particular how the costs of serving Group One customers may develop in the future.

In our assessment of the costs, we are adopting a twin track approach to help determine an efficient level of the cost to serve Group One customers. First, we will take a 'top down' approach that uses overall retail cost data allocated into cost categories and cost drivers for cost categories to develop our understanding of an efficient cost to serve. Second, we are adopting a 'bottom up' approach that disaggregates costs by customer segments and cost categories.

We acknowledge that this RFI asks for relatively more complex and granular data, including the request to analyse costs and cost drivers by customer segment (ie. annual consumption by customer), tariff types and by Wholesale region. However, we view this a necessary

¹The REC protections also apply in the event that a negotiated contract expires.

requirement to help us better understand the cost bases, including costs that have developed since market opening, as well as if and how costs may vary regionally.

1.2 Purpose of this document

We are asking Retailers to complete an RFI Excel spreadsheet (provided separately to this document) with cost and other relevant data, and an additional narrative document (Word or .pdf format) containing where relevant descriptions and/or further explanation of assumptions and bases for the data and information provided. This guidance document provides a guide to completing the RFI spreadsheet, including definitions relating to costs and cost drivers, and tab by tab instructions. Where this guidance document or the RFI spreadsheet asks for further explanation or the bases for assumptions, these should be provided in the separate narrative document; ideally your narrative document would follow the same tab by tab structure of the RFI spreadsheet.

The guidance provides descriptions of the cost categories used for our 'top down' and 'bottom up' approach. Where segmentation of data has been requested, this guidance document details how relevant costs, revenue and other data are to be analysed. As part of our 'bottom up' approach to assessing retail costs, we have stated how costs are to be allocated/attributed to customer segments (see section 6 below).

Please note that there are also explanatory notes within each RFI spreadsheet tab, which, where relevant provide further explanation and clarification for specific questions, and supplement the guidance in this document. When completing the RFI spreadsheet, please refer both to guidance within this document as well as explanatory notes within the RFI spreadsheet.

We expect and require submissions relating to all information provided within the RFI to be as accurate as possible. Given the importance of accurate data in understanding Retailers' costs, we ask that you provide assurance at Board level concerning the quality and accuracy of the data submitted, including that the data have been subject to appropriate levels of verification. You should provide a description of assurance processes undertaken to verify that information and data submitted are accurate and ensure that any estimates are made within reasonable tolerances. Details of the assurance processes should be submitted in a word document or similar format at the same time as the data provision form. This document should also include a signed statement on behalf of your Company's Board.

Regarding forecasts of cost and revenue, we fully recognise that such forecasts will be subject to uncertainty and a range of assumptions and views about future circumstances.

We ask that you state the principal assumptions underlying your forecasts in the accompanying narrative document.

1.3 Structure of this document:

The guidance document includes specific descriptions of the cost categories and cost drivers we view as necessary to assess costs, particularly – at a more granular level – the cost of serving Group One customers. The document is structured as follows:

- Section 2: Methodology discussion
- Section 3: General RFI notes – all templates
- Section 4: Top-down approach tables
- Section 5: Bottom-up approach tables

2. Methodology discussion

2.1 Introduction

Our December 2021 consultation set out that we will consider if and to what extent the levels of REC price caps for Group One customers may need revision. With this in mind, we signalled that a more detailed analysis of the costs to serve Group One customers is warranted, and that it would include seeking granular data on costs and cost drivers for the different customer and tariff types comprising Group One customers. We also set out that we would look to understand if, where and how retail costs to serve might vary significantly by geography or wholesale region. As we noted above, this RFI is intended to collect relevant data at this granular, and where relevant, Wholesaler region, level.

We set out in the remainder of this section our broad approach for understanding and assessing efficient forward-looking costs, some challenges associated with that, and our consequent approach for the RFI with a view to collecting the data necessary to inform our view.

2.2 Broad approach

We are primarily looking to understand the costs to Retailers of serving Group One customers (0–0.5Ml)², by tariff type and where relevant by geography (i.e. Wholesaler region). We are seeking to identify the costs of serving these customers, through the data requested and the development of a methodology for allocating cost to different customer segments. We will look to establish an estimated forward-looking efficient view on costs using methods including, but not limited to, peer level cost comparisons and use of external benchmarks.

We are therefore looking to collect both historical and forecast cost data disaggregated by principal cost categories and by customer segment. This is with a view to understanding how such costs have developed since market opening (historical costs) as well as a view on how they may develop in future (forward looking costs) and/or if some retail costs differ significantly by geography (i.e. Wholesaler region).

We are taking a twofold approach. First, we look to collect data on a 'top down' basis, (i.e. overall retail cost data) split into cost categories, but not differentiated by customer segment. We will complement this with data on the cost drivers for the cost categories, to assist our understanding of how costs vary by customer segment. Second, we look to collect

²As defined in the Retail Exit Code (REC)

data on a 'bottom up' basis, that is, costs disaggregated by both customer segment and cost category. Sections 3.4 and 3.5 below provide more detail here.

2.3 Practical issues

We note there are a number of practical challenges and issues in collecting such cost and other relevant data. Larger data sets, for example seeking to understand and reconcile Retailers' England and Wales business retail market in the context of their other activities, could increase our confidence in the quality of the data on costs attributed or allocated to the business retail market. On the other hand, greater scope and/or granularity of data increases the burdens on Retailers and may not greatly facilitate analysis of forward-looking costs for Group One customers. We have sought to balance our RFI, and paid particular regard to the following points:

1. Scotland / England

Some Retailers operate in the business retail market in Scotland as well as England & Wales, and prepare accounts across both markets rather than for each market. For such Retailers, we will want to understand how retail business costs are allocated and/or apportioned across their Scottish and English operations.

Our RFI therefore seeks 'top down' cost data for both Scotland and England & Wales, and for England & Wales separately to provide us with confidence that costs have been allocated between England and Scotland on a consistent basis. However, we do not seek Scottish data from a 'bottom up' – ie. customer segment – level.

2. Historical and forward-looking costs

We would like to understand how and why Retailer costs have developed and changed since market opening. Such historical data should help provide a richer picture of the costs to serve customers, including the effect of particular circumstances or costs, for example because of Covid-19 measures.

We would also like to understand Retailers' own views about how costs to serve might evolve on a forward-looking basis, including the reflection of views about how costs might change where a Retailer's operations are more streamlined and where the market itself operates more efficiently – particularly where market frictions such as poor quality market data are resolved.

3. Cost categories and cost drivers

As indicated above, we want to understand Retailer costs according to discrete costs and cost drivers. Our RFI sets out our view of the principal cost categories for Retailers, these being:

- Operating expenditure, comprising:
 - Customer contacts
 - Billing
 - MOSL, Ofwat and CCW fees
 - Customer acquisition
 - Customer retention
 - Debt management
 - Bad debt costs
 - Meter reading costs
 - MPF financial penalties
 - De-registrations
 - Other operating costs
- Non-attributable costs, comprising:
 - Exceptionals
 - Overheads
 - Depreciation
 - Amortisation
 - Other non-attributable costs
- Financing costs, comprising:
 - Interest costs
 - Other financing costs
- Wholesale costs
- Water efficiency

We also seek data on the potential drivers of operating expenditure costs, principally customer numbers, SPID numbers, number of multi-site customers, number of customers with payments in arrears, number of meter reads, number of bills, number of vacant premises.

4. Amortisation and depreciation

While we have sought to understand costs disaggregated by cost category, we appreciate that amortisation and depreciation costs may bridge a number of cost items. We have not however sought to give explicit guidance on amortisations or depreciation policy with a view to allocating aggregate amortisation costs to particular cost categories. Rather, **we will look to Retailers for a narrative description of the principal sources for amortisation and depreciation costs. Please provide such a description in your accompanying narrative document.**

5. Costs of market opening, other special or unique costs

We acknowledge that our cost categories as set out in our RFI will not always capture every cost, and that – particularly in respect of historical costs – some unique or special costs may have arisen – for example, in respect of measures to combat Covid-19. We therefore request separately data in respect of these, including costs of market opening, or other special or unique costs. **Where you enter data against such costs, you should also describe in your narrative document the source and basis of such costs.**

6. Costs relating to market frictions

Ofwat's [State of the market 2020-21: Review of the fourth year of the business retail water market](#) has highlighted three principal market frictions that impede effective market functioning: (1) Poor quality consumption, customer and asset data; (2) Cumbersome Wholesaler-Retailer interactions; (3) Inadequate Wholesaler performance. These frictions are also likely to have affected Retailers' costs to serve customers; for example, poor quality market data can make it more difficult or costly to understand a customer's consumption and potentially increase billing and customer contact costs.

We would like to understand where, and the extent to which, Retailers' costs, including on a historical basis, may be related to, or substantially caused by, the market frictions we have identified. We recognise that it may not always be straightforward to recognise and quantify costs related to market frictions. For example, poor market wide data quality could affect Retailers' billing costs, customer contacts, and other cost categories in ways that are not readily quantifiable.

Accordingly, **we ask Retailers to set out in their narrative document their views on how, and to what extent, relevant cost categories (as set out in RFI spreadsheet tabs TD1, TD2, BU1, BU2, BU6, BU7) may have been affected by market frictions.**

This should include views on if and how the Retailer has addressed or plans to address such costs, and forecasts (as per tab TD2 and BU2) of how these might change, and descriptions of the assumptions underlying your views.

7. (Potential for) Geographic variations in costs

The current REC price protections make regional variations in the cost to serve per customer. The RFI enables Retailers to set out and differentiate meter reading costs by Wholesaler region, if they consider this to be appropriate. We have not sought to collect other cost data on a regional or Wholesaler region basis.

8. Customer segmentation

As noted above, a principal task for the REC review will be to understand efficient cost to serve Group One customers (0-0.5MI), including by tariff type. We therefore need to seek cost data allocated or apportioned to relevant customer segment.

2.4 Our 'top down' approach

We are looking to collect data on a 'top down' basis, ie. aggregate costs for a Retailer business, with costs allocated or apportioned to cost category. We look to collect data on a historical, annual basis since market opening, plus forecast costs for the years 2022-23 and 2026-27.

We will also request data on relevant cost drivers. This aims among other things at enabling our own cross checks of the allocation or apportionment of costs to the categories we have listed, including by relevant customer segment.

2.5 Our 'bottom up' approach

With a view to understanding costs disaggregated by customer segment, we have set out a 'bottom up' approach to collect this data set, including by cost category. We will look to understand and where necessary reconcile 'top down' costs, allied with cost driver data, against 'bottom up' reported costs.

This will be particularly relevant and useful for our understanding of the cost to serve Group One customers, where our cost driver analysis should facilitate understanding of how and where costs have been allocated or apportioned between customer Groups One, Two and Three.

3. General notes – all templates

The information in this section is relevant to all templates for this RFI.

3.1 Scope of request: Your business retail water market activities

We are principally interested in the costs to Retailers of serving eligible business customers in the England and Wales business retail market. For customers or customer premises in Wales, this will necessarily mean businesses or premises consuming more than 50MI/year.

Nevertheless, we are aware that some Retailers serve customers in other regions, including Scotland. As such, in addition to requesting cost and cost driver information for eligible business customers in England and Wales, for our top-down analysis we are also requesting cost data that combines the business customers in England, Wales and Scotland.

Where you have customers or business in areas outside the scope of eligible business customers for water and waste water services in England and Wales, please state in your accompanying narrative document the basis for any apportionment or allocation of information or data to the England and Wales market.

3.2 Customer

For the purposes of this RFI and consistent with the approach taken previously, we have decided to use a **customer billing account** as the equivalent to a water and/or sewerage customer. When asking for customer numbers, these should be the number as at 31 March in each reporting period or the Retailers accounting year end if different. Unique customer numbers should be identified by the unique number of customer billing accounts.

Where an account is part of a group and does not receive a bill and instead the bill is transacted as part of an overall parent account, it **should not** be counted as a separate customer from the parent account.

Where an account is part of a group and does receive a bill instead of it being managed by an overall parent account, it **should** be counted as a separate customer from the parent account.

3.3 Units for pounds £m

Numbers entered for £ inputs should be entered as units of £million.

3.4 Price base

We seek historical cost and revenue data expressed in nominal terms. This means that, in respect of historical data for 2017-18 to 2021-22, we seek actual (outturn) expenditure, cost data and income without any adjustments for inflation. For forecast data on expenditure, cost data and income – ie. for years 2022-23 and 2026-27, we ask Retailers to report forecast data in 2021-22 prices, without any forecasts of inflation included. **For any costs that a Retailer views as being affected differently to inflation (e.g. wage inflation) we ask that Retailers state these views in a supporting narrative.**

3.5 Cost categories and apportionment

We are asking Retailers to allocate/apportion costs into the following cost categories, as set out in Table 1. We have set out descriptions and definitions of these categories below in section 4.1.

Table 3 – Cost categories

	Cost category
Operating expenditure	Customer contacts
	Billing
	MOSL, Ofwat and CCW fees
	Customer acquisition
	Customer retention
	Debt management
	Bad debt costs
	Meter reading costs
	MPF financial penalties
	De-registrations
Other operating costs	
Non-attributable costs	Exceptionals
	Overheads
	Depreciation
	Amortisation
	Other non-attributable costs
Financing costs	Interest costs
	Other financing costs
Wholesale costs	Wholesale charges
Water efficiency costs	Demand-side water efficiency expenditure

3.6 Time period covered

We seek both historical and forecast data. All data should be based on the financial year ending 31 March, or the Retailers accounting year end if different.

Historical data sets are requested for the years ending 31 March 2018, 2019, 2020, 2021 and 2022.

All information given up to the financial year ending 31 March 2022 should be actual outturn. If any data for the year ended 31 March 2022 is based on a best estimate, this should be clearly stated, and the basis of the estimate fully explained.

For the purposes of this RFI, we are also requesting forecast data for the financial years ending 31 March 2023 and 31 March 2027. Any assumptions made in determining forecasts should be clearly stated, and the basis of the assumptions fully explained.

As a general rule, data concerning the segmentation of customers by tariff type and size should be based on the last day of the time period covered or referred to. For example, if a Retailer acquired a customer in July 2020, under the year heading 2020–21 that customer should be classified as having been 'Acquired' and the related indicators for that customer – billed volumes, wholesale charges, revenues etc. – should only relate to the period for which they have been on this tariff.

3.7 Merger and acquisition

Where a Retailer has engaged in merger and acquisition activity, we request:

- In the year of acquisition, Retailers should provide the date from which the new company was acquired and incorporated into their business, including financial and customer details of the acquired company.
- For periods prior to the acquisition, Retailers are requested to include the activities of the combined entities providing the data is robust and reliable. If this is not the case the historical data for the acquired entity prior to acquisition should be excluded.

Retailers must provide a supporting narrative as to how any mergers or acquisitions have been accounted for, in each reporting period as appropriate, in the RFI.

3.8 Customer segmentation

Where required, we ask for Retailers to provide information segmented by customer size to understand how costs may vary for different customer groups.

Data should be segmented by annual consumption, as set out in table 2 below.

Table 2 – Customer segmentation and consumption thresholds

Customer segment classification	Water consumption thresholds (megalitres per year)
CS1	0 – 0.5MI
CS2	0.5 – 5MI
CS3	5 – 50MI
CS4	>50MI
CS5	unmetered

The annual consumption attributed to each customer billing account will determine the consumption category within which it falls. For each reporting period, customers should be assigned to the consumption category based on their annual consumption in that period. For the avoidance of doubt, we expect acquired customers to be assigned to the relevant consumption category based on their consumption from the date that they were acquired to the end of the reporting period. We also expect similar treatment of a customer, where separate bills are generated and sent to a single customer billing account, who is ultimately responsible for settling the bill.

The calculation of annual consumption may be based on actual usage, estimated annual consumption or on historical consumption. If you have used a method which deviates from these please explain your methodology in detail and provide an indication of any margin of error associated with your methodology.

Any subsequent data items (e.g. number of SPIDs, billed volumes, charges and revenues, etc.) should therefore correspond to the customer billing accounts in each segment respectively. For the avoidance of doubt, we expect a customer with consolidated bills to be treated as a single customer. We also expect similar treatment of a customer, where separate bills are generated and sent to a single customer billing account, who is ultimately responsible for settling the bill.

Where any Retailer requires further guidance regarding the treatment of metered and unmetered accounts, we suggest the following approach:

Concerning whether or not the customer's data should be recorded as 'metered' or 'unmetered':

- For the purposes of this RFI, we can define customers whose charges are all based on measured quantities of volume as 'metered'. We can define customers who have the majority of their charges based on other metrics as 'unmetered' (e.g. rateable values, assessed charges, etc.).

- In instances where a customer has both metered and unmetered connections, we would like you to record such a customer as 'metered' if the majority (>50%) of revenue received is derived from the metered connections of that customer. If the majority of the relevant revenue is derived from the 'unmetered' connections, then please categorise that customer as unmetered.

For the bottom-up tables, where data needs to be assigned to customer segment (for example tab BU1 which seeks data on Customer Group One (0-0.5Ml)), we ask that data relating to unmetered customers be assigned as follows:

- For the purposes of this RFI, we can define customers whose charges are all based on measured quantities of volume as 'metered'. We can define customers who have the majority of their charges based on other metrics as 'unmetered' (e.g. rateable values, assessed charges, etc.).
- For customers who are wholly unmetered, we ask Retailers to attempt, as far as they can, to assign the customer and hence the consumption to an appropriate consumption band, for example on the basis of any known customer characteristics or the size of any assessed charges. Where this is not possible or very uncertain, customers and associated data should be categorised as unattributed.
- Concerning a customer who has a mix of unmetered and metered SPIDS, we again suggest Retailers attempt, as far as they can, to assign the customer to an appropriate consumption band, for example on the basis of the metered consumption and any known customer characteristics or the size of any assessed charges. Where categorised, all the customer revenue should be assigned to that category; i.e. we do not expect a split for a customer with some portion to be 'unattributed' and the remainder in one of the customer consumption categories.

Where necessary, please provide in your accompanying narrative document an explanation of the basis for assigning customers to an appropriate consumption category.

4. Top-down approach Tables

There are 7 data tables associated with the top-down methodology for the cost benchmarking.

Table Number	Contents
TD1	Historical Retail Costs
TD2	Forecasting Retail Costs
TD3	Customer Volume Data
TD4	Special Cost Factors
TD5	Debtors
TD6	Regional Cost Data
TD7	Cost Totals – Companies that operate in England & Scotland

4.1 TD1 Historical cost data

This tab TD1 asks for historical actual cost information from Retailers for non-household market for the period 2017-18 to 2021-22, inclusive.

Data, information and assumptions should relate only to eligible business customers in England and Wales.

We seek cost data according to the following five cost categories.

4.1.1 Block A: Operating expenditure

We seek data on costs here which are broadly scalable or change in line with cost drivers such as customer numbers or other metrics.

Customer contacts

The costs associated with providing customer contact services, including those related to enquiries and complaints.

Note contact costs exclude customer contact costs related to debt management, and customer acquisition and retention. We seek these costs separately, as set out below.

Billing

The costs associated with providing the following service to non-household customers:

- Billing.
- Payment handling, remittance, and cash handling.

Note billing costs exclude the costs of debt management, which we seek separately below.

MOSL, Ofwat and CCW fees

Please include here:

- All fee payments to the Market Operator MOSL in accordance with the Market Arrangement Codes. Please exclude any monies related to Market Performance Standard charges; Additional services & Market Services charges, and/or any financial penalties paid under the Market Performance Framework.
- Fees paid to Ofwat and CCW.

Note we expect all MOSL, Ofwat and CCW fees that accrues in the relevant time period to be attributed to that time period.

Customer acquisition

All costs relating to acquiring business customers that have switched to you from another Retailer in the market.

This includes the cost of acquiring new customers through the use of third-party intermediaries (TPIs). This should include fees and/or commission payments made to relevant TPIs. **We are requesting that Retailers provide a written commentary in their accompanying narrative document in support to indicate how costs differ between the use of TPIs and internal customer acquisition processes.**

Customer retention

All costs relating to the retention of existing business customers who have negotiated (including negotiated for the first time), or renegotiated, a deal with their existing Retailer or customers who have received financial incentives (e.g. cashbacks) or additional services to renew or sign a new contract with the existing Retailer.

This includes the cost of retaining customers through the use of third-party intermediaries (TPIs). **We are requesting that Retailers provide a written commentary in their accompanying narrative document in support to indicate how costs differ between the use of TPIs and internal customer retention processes.**

Debt management

All costs relating to the management of debt recovery for non-household customers and monitoring of outstanding debt, including:

- issue of reminders and follow up telephone calls, managing and monitoring field recovery of debt
 - includes costs of customer visits;
- managing and monitoring external debt collection routes
 - including debt collection agencies and legal;
- notification and carrying out of disconnections to non-household customers (where disconnections relate to debt recovery and/or non-payment)

Bad debt costs

Bad or doubtful debt costs, in relation to consumption in the reporting period or prior periods comprised of:

- Movement in provisions
- Bad debts written off

Meter reading costs

The costs associated with meter reading for non-household customers – including ad hoc read requests, cyclical reading, scheduling, transport, physical reading, reading queries and read processing costs, managing meter data plus supervision and management of meter readers. We are requesting this data for the 12 months ended 31 March for each reporting period.

Any income from meter reading commission should be netted off these costs.

Figures should exclude costs associated with meter reading for third parties.

Market Performance Framework financial penalties

Please record any and all MPF financial penalty payments made by you in respect of any relevant underperformance against the Market Performance Framework. Any such amounts recorded should be net of any received reimbursements from the fund.

Note we expect all MPF financial penalties fees that accrues in the relevant time period to be attributed to that time period.

De-registrations

Costs incurred by Retailers involved in the de-registration of Supply Points or removal of one or more Service Components. **Please describe in your narrative document the bases for any such costs entered here.**

Other operating costs

Any other operating costs (ie, excluding interest and taxation) incurred serving non-household customers, on an aggregated basis. Please include the costs of (among other costs):

- insurance premiums;
- customer side leaks;
- other direct costs;
- general and support expenditure;
- other business activities

Please describe in your narrative document the bases for any such costs entered here.

4.1.2 Block B Non-attributable costs

We seek here costs that do not have, or do not appear to have, direct cost drivers associated with them, such as customer numbers, number of bills sent etc.

Exceptionals

Exceptional cost items that are outside normal business operating activities.

Exceptionals include one-off items of expenditure – these should be supported by a written commentary in your narrative document that provides details of the exceptional cost items.

Overheads

Any costs incurred in the provision of retail services to business customers that are not directly attributable to cost drivers (eg. customer numbers). Include the costs of (among other costs):

- Property costs
- IT expenditure

Depreciation

Depreciation of tangible fixed assets used in the provision of services to business retail customers.

Depreciation excludes amortisation of deferred credits and intangible fixed assets.

We request that Retailers provide in your narrative document written details of their accounting policy relating to the depreciation of tangible fixed assets.

Amortisation

Amortisation of intangible assets wholly or principally used for the provision of non-household retail services to business customers.

We request that Retailers provide in your narrative document written details of their accounting policy relating to the amortisation of intangible assets.

Other non-attributable costs

Please include any other items of non-attributable costs which you consider have not been included above. **Please provide in your narrative document a detailed description of cost items entered here, if any.**

4.1.3 Block C: Financing Costs

We seek data here on costs of financing the retail business in terms of interest payments on bank loans and any relevant bond facilities.

For the costs of financing outside of bank loans and bond facilities, Retailers should include a description of the bases of these costs in your narrative document.

We seek data under two headings:

Interest costs

Total net interest expenses defined as interest income less interest expense.

Interest income includes interest received on cash deposits, loans to group companies,

Interest expense includes interest paid on loans, finance leases, debenture, floating rate debt, overdrafts, preference shares and all other borrowings

Please note that payments relating to equity arrangements, eg. ordinary shares (e.g. dividends) are to be excluded.

Other financing costs

Please record other financing costs related to interest payments or bond arrangements not included above. Please note that, as above, payments relating to equity arrangements, eg. ordinary shares (eg. dividends), are to be excluded.

4.1.4 Block D: Wholesale cost

Wholesale charges

The Wholesale charge paid by Retailers to Wholesalers for the water and wastewater services provided to eligible non-household customers.

4.1.5 Block E: Water efficiency costs

Demand-side water efficiency expenditure

The total retail operating costs of providing water efficiency services to non-household customers, including:

- Promotion of water saving initiatives
 - Production of customer literature and customer awareness campaigns;
- Retro-fitting of water saving devices
 - Provision of advice and devices to customers;
- Water efficiency audits
 - Water and energy conservation, optimisation of systems, advice and investigations into usage;
- Data logging

4.2 TD2 Forecast cost data

This table asks for forecasting cost information from Retailers for non-household market for the two years 2022–23 and 2026–27. Note you should provide such data in constant price terms, in terms of 2021–22 constant prices.

Data, information and assumptions should relate only to eligible business customers in England and Wales.

We fully recognise that forecasts will be subject to uncertainty and a range of assumptions and views about future circumstances. We ask that you state the principal assumptions underlying your forecasts.

For a description of the cost categories, please refer to section 5.1.

4.3 TD3 Customer Volume Data

This tab asks for historical and forecast customer volume data for business retail market for the period 2017-18 to 2026-27.

Data, information and assumptions should relate only to eligible business customers in England and Wales.

We ask that Retailers state any principal assumptions made in determining forecasts in the relevant commentary box.

Note this tab requests information for two customer types:

Block A – Actual customer volumes

Actual customers are defined as all eligible business customers in England and Wales that a Retailer serves.

Block B – Acquired customer volumes

Cost data for acquired customers relates to business customers that have switched.

Switched customers are defined as those that have actively chosen an offer that is different from the statutory terms and conditions and have switched to a Retailer from another Retailer in the market.

Please note where a Retailer has acquired the entire customer base of another company such as through an acquisition, merger or the Interim Supply Process, these customers should maintain their 'status' as it was with the previous Retailer. For example, a customer on a REC default tariff that was acquired through an acquisition or merger should still be classified as being on a default tariff. Only customers who actively chose to transfer services to the incoming Retailer should be included in the "Acquired customer volumes" table.

In this tab, we are also requesting data segmented by customers' annual consumption – consumption thresholds are listed in table 2 of this guidance document.

We also request that Retailers separate customer volume metrics by tariff type into the following categories, according to whether a customer is:

- Water only;
- Wastewater only;

- Trade effluent only;
- Water and wastewater;
- Water and trade effluent;
- Waste water and trade effluent;
- Water, waste water and trade effluent.

We expect Retailers to apply the relevant segmentation by size and tariff type as of the last day of the reporting period (31 March). If a customer is no longer with you on that day, we expect that the relevant segmentation is applied on the last day the customer was served by the Retailer.

If a customer is no longer with you on the last day of the reporting period, we do not expect customer numbers, SPIDs, multisite customers, and customers in arrears data to be reported for that customer.

We expect Retailers to allocate to acquired customers from the date that they were acquired to the end of the reporting period. For example, if a Retailer acquired a customer in July 2020, that customer should be classified as having been 'acquired' and the related indicators for that customer – wholesale charges, revenues, billing for the period July 2020 to March 2021 for that customer – should be included within the report for the financial year 2020-21. If a customer which had previously been acquired leaves during the year, related data for that customer – wholesale charges and billing revenue – should relate to the point that customer left. For example if a previously acquired customer leaves in August 2020, then data for that customer relating to April 2020 to August 2020 should be included against the 2020-21 financial year.

We request that Retailers provide

- The number of customer billing accounts at 31 March for each historical and forecast period.
- The number of SPIDs at 31 March for each historical and forecast period.
- The number of multisite customers at 31 March for each historical and forecast period.
 - Multisite customers are defined as the number of business customer accounts that have more than one **site** associated with the customer.
- The total number of bills for each historical and forecast period.
 - Note we expect all bills issued in relevant time period to be attributed to that time period, including any bills issued to customers that subsequently switched away from your company.
- Revenue figures for each historical and forecast period.
 - Revenue data should reflect the revenues in respect of acquired customers for the 12 months ending 31 March for reporting period.
 - Note we expect all revenue that accrues in the relevant time period to be attributed to that time period, including any revenue that accrued from

customers that subsequently switched away from your company. Revenue should exclude any VAT amounts.

For example, if a Retailer acquired a customer in July 2020, that customer should be classified as having been 'acquired' and the associated revenue data for the period July 2020 to March 2021 for that customer – should be included against the financial year 2020–21. If a previously acquired customer leaves in August 2020, then the associated revenue data for that customer relating to April 2020 to August 2020 should be included against the 2020–21 financial year.

- Regarding forecasts of revenue, we fully recognise that such forecasts will be subject to uncertainty and a range of assumptions and views about future circumstances. We ask that you state the principal assumptions underlying your forecasts in the relevant commentary box.
- Wholesale charge
 - We request that Retailers provide total Wholesale charges for each historical and forecast period.
 - Wholesale charges should reflect charges in respect of acquired customers for the 12 months ending 31 March for reporting period.
 - Note we expect all Wholesale charges in the relevant time period to be attributed to that time period, including any Wholesale charges for customers that subsequently switched away from your company.

For example, if a Retailer acquired a customer in July 2020, that customer should be classified as having been 'acquired' and the associated wholesale charge data for the period July 2020 to March 2021 for that customer – should be included against the financial year 2020–21. If a previously acquired customer leaves in August 2020, then the associated wholesale charge data for that customer relating to April 2020 to August 2020 should be included against the 2020–21 financial year.

- Number of customers in arrears at 31 March for each historical and forecast period.
 - Business customer accounts in arrears are defined as any account that have fallen behind agreed or scheduled payment timelines.

Block C – Vacant properties

We are requesting data on vacant properties in two sections:

'Business as usual' vacant premises

We request that Retailers provide:

- The number of metered vacant properties by each consumption category for each tariff type at 31 March for each historical and forecast period (excluding premises listed as vacant under the temporary Covid-19 vacancy flag policy).
- The number of unmetered properties for each tariff type at 31 March for each historical and forecast period. (excluding premises listed as vacant under the temporary Covid-19 vacancy flag policy).

Covid-19 vacancy flag premises

Please note, for the historical periods 2019–20 and 2020–21 should include premises that were flagged as temporarily vacant during the first national lockdown due to the Covid-19 pandemic. The temporary vacancy flag policy expired on 31 July 2020 and Retailers were required to remove these flags from the Central Market Operating System (CMOS) by end September 2020. As such, we request that Retailers provide

- The number of metered vacant premises listed as vacant under the temporary Covid-19 vacancy flag policy by each consumption category for each tariff type at 31 March for each historical and forecast period.
- The number of unmetered premises listed as vacant under the temporary Covid-19 vacancy flag policy for each tariff type at 31 March for each historical and forecast period.

4.4 TD4 Special Cost Factors

This tab TD4 asks you to submit special or one-off cost claims that you believe should be considered in our assessment of business retail costs, either on a backward looking, historical basis over any of the years 2017–18 to 2021–22 or an anticipated basis for 2022–23 and/or 2026–27.

Such costs should be those that you consider fall outside 'business as usual' activity. Such costs could include any special cost claims relating to the effects of measures to combat Covid-19 and/or market opening costs in these tables. Data, information and assumptions entered into tab TD4 should relate only to eligible business customers in England and Wales.

Where such costs involve one-off investments or up-front expenditure where benefits or services are realised in subsequent years, please explain such effects and time profiles in your accompanying narrative document.

When completing tab TD4, each table block should relate to a separate identified cost that is being put forward for special treatment (adjustment / exclusion).

Description of special cost claim

Description of costs being put forward for a special cost claim. A separate table block should be filled in for each cost type that has been identified as requiring special treatment (adjustment / exclusion).

Cost category claim refers to (from list)

Please select in the box what cost category the cost adjustment claim refers to from the cost categories available in the drop-down list in Column G. If more than one cost category is applicable or Other (specify) is selected, provide explanation in the description box above (line 1) for the respective cost claim.

Forecast expenditure

Forecast total expenditure related to the proposed special cost claim.

Historical total expenditure

Historical total expenditure related to the proposed special cost claim.

Please note that any cost entry items in tab TD4 should already be reflected in your cost breakdowns given in tabs TD1 and TD2. That is, special or one-off costs listed in tab TD4 are sub-sets, and a further refinement, of cost breakdown data already provided for tabs TD1 and/or TD2.

4.5 TD5 Debtors

This table requests historical and forecast customer debtor and bad debt provision information for the periods 2017-18 to 2021-22 and forecasts 2022-23 and for 2026-27.

Data, information and assumptions should relate only to eligible business customers in England and Wales.

The period end refers to the Retailers' accounting year end; where this is not the 31st March, this should be indicated in the accompanying narrative document.

The table is split into two sections:

Block A - Debtor Information

For the end of each financial year, please provide the debtor balance outstanding for each of the aged debtor time periods indicated (the number of days outstanding refers to calendar days not working days). Note: credit balances held by Retailers, including deposits paid,

prepayments or any other monies paid by customers in advance of consumption should be excluded.

Detailed aged analysis is only required for the historical data (2017-18 to 2021-22).

Block B – Bad Debt provision by customer segment

For each year and consumption segment, please provide:

- the increase / decrease in the provision that has been charged to the profit and loss account for that reporting period; and
- the actual value of customers debts written off in the reporting period.

Note: where possible we ask that Retailers refrain from using the 'Unattributed' category, as this reduces the quantity and quality data available to input into the analysis.

4.6 TD6 Regional cost data

This table asks for historical and forecast cost driver information from the period 2017-18 to 2021-22.

Data, information and assumptions should relate only to eligible business customers in England and Wales.

This tab separates the required regional cost data into two categories:

- Meter reading cost by Wholesale region
- Bad debt cost by Wholesale region

Meter reading costs by Wholesale region

We are asking Retailers to provide meter reading costs separated by Wholesale region to consider if and where meter reading costs vary by geography or Wholesaler region.

Meter reading costs

The costs associated with meter reading for non-household customers – including ad hoc read requests, cyclical reading, scheduling, transport, physical reading, reading queries and read processing costs, managing meter data plus supervision and management of meter readers. We are requesting this data for the 12 months ended 31 March for each reporting period.

Any income from meter reading commission should be netted off these costs.

Figures should exclude costs associated with meter reading for third parties.

We also request that Retailers provide in their narrative document a written commentary to supplement this data, including their view on what are the drivers of regional variation in meter reading costs.

Number of SPIDs

To help determine an average meter reading cost per SPID, we also request that Retailers provide the total number of SPIDs for each Wholesale region at 31 March for each historical period.

Bad debt costs by Wholesale region

We request that Retailers indicate whether they believe bad or doubtful debt costs, normalised by customer numbers, customer bill size or other relevant metrics, vary significantly by geography or wholesale region.

Where Retailers believe that such bad or doubtful debt costs vary significantly by geography or Wholesale region exist, **we ask that Retailers provide in their narrative document a written commentary that sets out the basis and for their view, including their views on what are the drivers of any regional differences and any relevant evidence to support their views.**

4.7 TD7 Cost totals – Retailers that operate in England & Scotland

As part of this RFI, we are asking Retailers that operate in both England and Scotland to provide high-level cost data.

Data, information and assumptions entered into tab TD7 should relate to both business customers in Scotland and eligible business customers in England and Wales. Please note, for Retailers that do not operate in the business retail market in Scotland as well as England, there is no requirement to complete this tab.

This table requests historical and forecast cost and cost driver information for the periods 2017-18 to 2022-23, and for 2026-27.

We ask that you state any principal assumptions made in determining forecasts in the relevant commentary box.

i) Historical and forecast cost data

For guidance on completing this table, please refer to section 4.1 and 4.2.

ii) Historical & forecast customer volume data

For guidance on completing this table, please refer to section 4.3.

iii) Special cost factors

For guidance on completing this table, please refer to section 4.4. Data entered here may relate to special costs factors arising or having arisen in Scotland and/or England; please specify.

iv) Debtors

For guidance on completing this table, please refer to section 4.5.

v) Regional cost factors

We are asking Retailers to provide average meter reading costs across all regions in England and Scotland.

For guidance on completing this table, please refer to section 4.6.

Note, we ask Retailers with water retail business operations in Scotland as well as England and Wales to allocate or attribute costs to the England and Wales business retail market for the purposes of tab TD1 (and other tabs). We consider that Retailers are best placed to understand how their costs might be so allocated or attributed, for example on the basis of customer numbers and/or revenue.

We request that Retailers with water retail business operations in Scotland as well as England and Wales describe in their narrative document the approach they have taken to allocating or attributing data to their England and Wales water retail business (eg. for the purposes of completing tab TD1, and other relevant tabs).

5. Bottom-Up approach Tables

There are 7 data tables associated with the bottom-up methodology for the cost benchmarking.

Table Number	Contents
BU1	Historical Cost Data ~ Customer Group One
BU2	Forecast Cost Data ~ Customer Group One
BU3	Special Cost Factors ~ Customer Group One
BU4	Debtors ~ Customer Group One
BU5	Regional Cost Data ~ Customer Group One
BU6	High-level Cost & Volumes ~ Customer Group Two
BU7	High-level Cost & Volumes ~ Customer Group Three

5.1 BU1 Historical Retail Costs – Group One Customers

This tab BU1 asks for historical cost information from Retailers for the Customer Group One for the period 2017-18 to 2021-22, inclusive.

For the purposes of formulating our bottom-up approach to assessing Retailer costs, in this tab, we provide guidance of the cost allocation method to be used by Retailers when allocating costs to Group One customers. **The method of allocation to Group One customer for each cost category is listed in table 3.**

As a purely illustrative example in the case of billing costs, allocation and cost drivers would enable allocation of billing costs to Group One customers as follows:

- Assume total billing costs for year across your England and Wales business retail business are £1 million.
- The billing cost driver is the number of bills. Assume the number of bills sent in year divides between customer groups as follows:

Customer Groups	Number bills sent in year	Proportion of Total
Customer Group One	65,000	0.65
Customer Group Two	30,000	0.30
Customer Group Three	5,000	0.05
Total	100,000	1

- In this case, you should be looking to allocate to customer Group One billing costs of £650,000, i.e. £1million x (65,000 ÷ 100,000).

Table 3 – Cost allocation methods

Cost category	Allocation method
Contacts	Unique customer numbers
Billing	Number of bills
MOSL, Ofwat and CCW fees	Customer wholesale charge
Customer acquisition	Number of customer acquisitions
Customer retention	Number of customer acquisitions
Debt management	Number of customer accounts in arrears
Bad debt costs	Number of customer accounts in arrears
Meter reading costs	Number of SPIDs
MPF financial penalties	Number of SPIDs
De-registrations	Number of SPIDs
Other operating costs	Sum of above operating costs (ie. contacts to meter reading costs)
Exceptionals	Operating costs
Overheads	Operating costs
Depreciation	Operating costs
Amortisation	Operating costs
Interest	Wholesale charge
Wholesale charges	Directly attributable
Demand side water efficiency expenditure	Unique customer numbers

For descriptions of the cost categories, please refer to section 4.1.

To the extent a Retailer considers that an additional cost should be directly attributable to customer groups, in ways significantly different to that implied by Ofwat's approach set out here, please provide your reasoning and where relevant, quantitative estimates and/or evidence, in your narrative document. You should nevertheless, for the purposes of completing the RFI spreadsheet, follow Ofwat's approach.

5.2 BU2 Forecasting Retail Costs – Group One Customers

This tab BU2 asks for forecast cost information for the Group One customers for the periods 2022–23 and 2026–27.

We request that Retailers provide in your narrative document a written commentary in support of forecast information for Group One customers that states any underlying assumptions and overall drivers of forecasts.

We ask that Retailers follow the cost allocation method as set out in table 3.

For descriptions of cost categories, please refer to section 4.1.

5.3 BU3 Special Cost Factors – Group One Customers

This tab BU3 asks for historical and forecast cost information for the Group One customers from 2017-18 to 2022-23 and for 2026-27. This table asks Retailers to submit special cost claims that they believe should be considered in our assessment of business retail costs.

Retailers should include in their description of the special cost claim how this relates to Group One customers.

For the bottom-up tables, we are asking Retailers to allocate special cost factors to customer groups. Retailers should allocate special cost factors to customer groups using the relevant cost category's cost driver, as listed in table 3.

For guidance on special cost factors and completing the table, please refer to section 4.4.

Please note that any cost entry items in tab BU3 should already be reflected in your cost breakdowns given in tabs BU1 and BU2. That is, special or one-off costs listed in tab TD4 are sub-sets, and a further refinement, of cost breakdown data already provided for tabs TD1 and/or TD2.

5.4 BU4 Debtors – Group One Customers

This tab BU4 asks for historical and forecast customer debtor information for Group One customers from the period 2017-18 to 2022-23 and for 2026-27.

For guidance on completing the table, please refer to section 4.5.

5.5 BU5 Regional Cost Data – Group One Customers

Table A in this tab asks for historical meter reading information Group One customers by Wholesale region from the period 2017-18 to 2021-22. Table B asks Retailers to provide their views if and how bad debt costs vary by Wholesale region.

For guidance on completing the tables, please refer to section 4.6.

5.6 BU6 High-level Cost & Volumes – Customer Group Two

This tab BU6 asks for high-level historical and forecast cost information for the Group Two customers from the period 2017-18 to 2021-22 and for 2022-23 and 2026-27.

For guidance on completing the tables, please refer to sections: 4.1, 4.2, 4.3, 4.4, and 4.5.

5.7 BU7 High-level Cost & Volumes – Customer Group Three

This tab BU7 asks for high-level historic and forecast cost information for the Group Three customers from the period 2017-18 to 2021-22 and for 2022-23 and 2026-27.

For guidance on completing the tables, please refer to sections: 4.1, 4.2, 4.3, 4.4, and 4.5.

**Ofwat (The Water Services Regulation Authority)
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