

# Accounting Separation Methodology Statement

*Yorkshire Water 2014/15*

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Blueprint for Yorkshire



YorkshireWater

# Accounting Separation Methodology Statement

Yorkshire Water 2014/15

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# 1. Introduction

## 1.1 Purpose

- Ofwat requires water companies to report costs, revenues, assets and liabilities separately, for different activities they carry out in delivering services. This is known as accounting separation. There are four main activity areas which are water wholesale, waste water (or sewerage) wholesale, retail household and retail non-household.
- The purpose of this document is to set out the Yorkshire Water Services Limited (YW) approach on accounting separation. This document explains the methods that have been followed to ensure that the accounting separation is prepared in accordance with Ofwat's guidance.
- Ofwat require this document to be disclosed as supporting information to the regulatory accounting tables.

## 1.2 Scope

- This document is limited to the appointed business of YW.
- It has been prepared in accordance with the following documents published by Ofwat:
  - Information Notice (IN) 13/01 'Revised regulatory reporting requirements for 2012-13 and onwards' which includes:
    - i) RAG4.04 'Guideline for the definitions for the regulatory accounting tables'
  - IN 14/05 'Expectations for company reporting 2013-14 – regulatory accounts, accounting separation and performance information' which includes:
    - i) 'Disclosure requirements for companies' accounting separation and upstream services data methodology statements 2013-14'; and
    - ii) 'Accounting separation guidance clarifications'.
  - IN 15/01 'Future company performance reporting and assurance' in which Ofwat have set out that for the financial year 2015/16 and onwards the requirements for reporting will change.

## 1.3 Governance

YW operates a multi-layer approach in its control of the accounting separation process. The layers of control are as shown below:-

**Table 1 Layers of Control**

Control	Frequency	Responsibility
Board sign off	Annual	Yorkshire Water Board
External audit	Annual	PwC
High level sign off	Annual	Head of Account to Report
Business unit sign off	Annual	Senior Finance Business Partners
Version control of methodology / procedure notes	On going	Consolidation and Reporting Manager
Year on year analytical review	Bi-Annual	Consolidation and Reporting Manager
Reconciliation of accounting separation actuals to statutory annual financial statements	Monthly	Consolidation and Reporting Manager
Costing review using accounting separation alternate hierarchy	Monthly	Account to Report Team
Review of allocations	Monthly	Finance Business Partner / Budget Manager

## 2. Background to the business

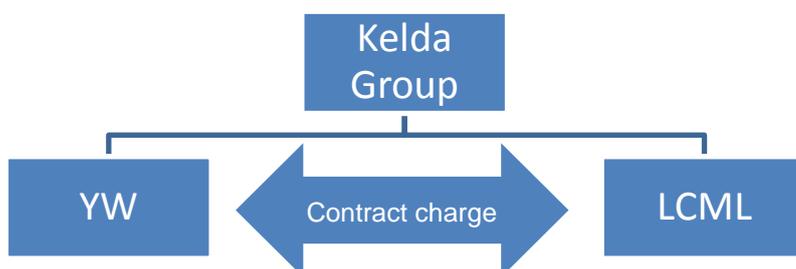
### 2.1 Background to the business

- YW and Loop Customer Management Limited (LCML) are both wholly owned subsidiaries of Kelda Group Limited..
- LCML is contracted by YW to provide Customer Services and Debt Management services.

### 2.2 Business structure

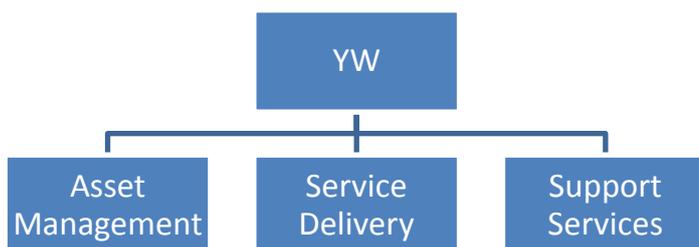
In respect of the appointed business figure 1 shows the business structure. YW carries out both wholesale and retail activities. LCML carries out exclusively retail activities for YW with a charge made via an annual contract fee.

Figure 1 Company structure



- Figure 2 shows how YW is currently organised into business units. Asset Management includes building and maintenance of wholesale assets. Service Delivery includes the operation of the wholesale assets and associated customer services. Support Services includes Business Support Group, Communications, Company Secretariat & Legal Services, Finance & Regulation, and Human Resources. During 2014/15 YW was reorganised into the existing structure. The changes had no impact on the methodology or allocation of costs as the process is set up in such a way to be resilient to business change.
- Related overheads are classed as General and Support and included in line 9 ‘other operating expenditure’ in the regulatory accounting tables A7 and A8 (as detailed in appendices 6.6 and 6.7 respectively).
- No overheads are included in direct costs.

Figure 2 YW business unit structure



## 2.3 Outsourced functions

- Ofwat requires companies to disclose outsourcing agreements as this could affect benchmarking comparisons.
- A significant proportion of the activities identified within retail are performed by a separate company, LCML, which is a UK based company, and are charged to YW via an annual contract fee.
- For some customers LCML outsources billing and collection to other water companies and local authorities.
- Where possible the costs are charged directly to the retail service activity that consumed the goods or service. The remainder of costs identified as retail are incurred by YW and, where possible, are allocated directly to an activity. Costs not allocated directly are allocated via management assessment.
- The table below shows the activities that were outsourced by YW and LCML for the year ended 31 March 2015.

**Table 2 Outsourced functions**

Which company outsources	Function outsourced	Outsourced to
LCML	Cross water company boundary billing, payment handling and debt management	Other water companies
LCML	Some billing, payment handling and debt management	UK based local authorities and housing associations
YWSL	Capital delivery	UK based contract partners
YWSL	Below ground network repair and maintenance	UK based contract partners

## 3. Commentary

### 3.1 Commentary

The following section details changes in the year, an explanation of adjustments made to data and how RAG 4.04 principles have been applied.

### 3.2 Significant changes in costs in the year

The appendices show the movements in tables A7 and A8 from 2013/14 to 2014/15. The following section outlines any significant movements, i.e. those above 10%, with commentary.

**Table 3 Significant changes – Wholesale**

Income treated as negative expenditure	Water - 44.3% increase (£0.2 million) Waste Water - 35.5% increase (£0.5 million)
Infrastructure renewals charge	Water - 26.5% decrease (£12.8 million) Waste Water - 26.7% increase (£11.3 million)
Current cost depreciation	Waste Water - 15.6% decrease (£25.6 million)
Recharges from other business units	Water - 11.1% increase (£1.2 million)
Operating expenditure for Third Party Services	Water - 65.1% increase (£0.7 million)

**Table 4 Significant changes – Retail**

Customer Services	Non-household - 50% increase (£0.8 million)
Debt management	Household - 26.7% increase (£0.8 million)
	Non-household - 50% decrease (£0.4 million)
Services to developers	Non-household 33.3% decrease (£0.1 million)
Other operating expenditure	Non-household 40% decrease (£0.6 million)
Capital maint Recharges from other business units	Non-household 12.5% decrease (£0.1 million)

#### 3.2.1 Wholesale

##### Income treated as negative expenditure (£0.7 million net increase)

This is income received as a result of electricity self-generation. Costs are recorded as negative expenditure on a separate General Ledger (GL) code and are site specific. There are two main reasons for the movement:

- A change from ROCs (renewable obligation certificates) to FITs (feed in tariffs) at water treatment works giving an additional £0.4 million income.
- A decrease in energy generation at water treatment works of £0.2 million; and
- Increased energy generation of £0.5 million at waste water treatment sites with some changes in processes contributing to the change.

##### Infrastructure renewals charge – Water and Waste Water (£1.5 million net decrease)

- The methodology for apportioning the infrastructure renewals charge across the business units was revised so that the charge was apportioned across all categories based on the closing net book value of infrastructure assets. Previously it was apportioned specifically to raw water distribution, treated water distribution and sewage collection. It is considered that the new apportionment methodology is more appropriate as the previous

assumption used was that the infrastructure renewals charge applied only to assets in the raw water distribution, treated water distribution and sewage collection business units as this is where the largest value of infrastructure renewals expenditure is incurred, i.e. on water mains and sewers. However there is still some infrastructure renewals expenditure in other business units, for example relating to impounding reservoirs in the water resources business unit which has a significant infrastructure asset value. Therefore it was decided that this should be reflected in the allocation of the infrastructure renewals charge by allocation across all business units according to their infrastructure asset value.

- The effect of this was an increased allocation to water resources, which largely relates to impounding reservoirs.

#### Current Cost Depreciation – Waste Water (£25.6 million decrease)

- Current cost depreciation is lower in the sewage collection business unit in 2014-15 in comparison to 2013-14 because the 2013-14 figure contained a larger amount of accelerated depreciation on assets that had been written off in the year. This in itself was due to cross-checking the current cost asset register against the company's separate operational asset register and writing off any assets that had been physically disposed of. A significant element of these assets were in the sewage collection business unit. In comparison, there was less accelerated depreciation in 2014-15, however 'normal' depreciation increased slightly.

#### Recharges from other business units – Water (£1.2 million increase)

- The value of the recharges are broadly in line with previous years, however the relatively low value of these recharges still causes large percentage changes from year to year.
- The methodology for calculating recharges has not changed from previous years.

#### Third Party Services (£0.7 million increase)

- There has been an increase in the level of activity of £0.4 million and also an amount for bad debt of £0.2 million has been included here for the first time this year (previously under retail).

### 3.2.2 Retail

#### Customer Services (£0.8 million increase on non-household)

Although there is no overall significant variance, non-household has increased due to two factors.

- Adoption of new improved cost drivers under the existing guidelines.
- In 2013/2014 there was one off credit associated with a non-household income generation initiative.

#### Debt Management (£0.4 million net increase)

- The year on year increase equates to 10.5%. This is due to a reduction in court action during the year which was caused by delays in implementation of new HM Courts and Tribunal Services systems.
- There has been a movement between household and non-household due to two factors: An early adoption of the debt management cost driver which is debt over 30 days and more accurate allocation of costs which relate exclusively to household.

#### Services to Developers (£0.1 million decrease)

- There has been a reduction in salary costs in relation to managing developer queries and providing information to developers.

Other operating expenditure (£0.6 million decrease)

- The 40% reduction on non-household is mainly due to the change in allocation of regulation costs from a 50/50 split in 2013/2014 to a 94% household, 6% non-household split in 2014/2015 (see section 3.5).

Recharges from other business units – Water (£0.1 million decrease)

- The value of the recharges are broadly in line with previous years, however the relatively low value of these recharges still causes large percentage changes from year to year.
- The methodology for calculating recharges has not changed from previous years.

### 3.3 Processes and systems

- Financial and management accounts are prepared using an accounting system, SAP. SAP is set up to provide both management information and accounting separation information.
- An alternate hierarchy is maintained with cost centres attached to wholesale and retail services in accordance with accounting separation guidelines.
- Reconciliation is carried out to the regulatory accounts to ensure that all relevant costs are included.
- Information from SAP is downloaded onto spreadsheets and manual changes are made as required – see section 3.4.
- Overheads are allocated in line with cost drivers detailed in this statement.
- Validation checks are completed and year on year comparisons completed.
- There are various stages of sign off which are detailed in section 1.3.
- There have been no significant changes to SAP during the year.

### 3.4 Additional analysis

- Once the data from SAP has been extracted some adjustments are made to ensure increased accuracy.
- The following table shows what adjustments have been made and the reason for the change.

**Table 5 Adjustments**

Adjustment	Reason
Cost centres (Salaries and V&P) omitted from assessment cycles	Small values on old salaries home cost centres cleared at year end
Miscellaneous year end coding corrections	The period 12 accounting separation review exercise
Whole site costs	Large waste sites have a site specific code which is cleared to service at year end based upon information provided by operations
Engineering reliability - clearance of centralised costs and statutory maintenance	Centralised costs (e.g. consumables) are moved to service pro rata to actuals. Statutory maintenance costs are moved to service dependent upon the type of contract and information provided by operations
Service charges	Costs not booked to correct service for Environment Agency charges. Manual adjustment made based on information provided by operations
Internal recharges	Accounting separation return is completed using primary costs on salaries. All secondary postings are ignored
Power	Data taken from SAP onto a spreadsheet in order to allocate multi service sites and to allocate carbon reduction commitment costs
Non-appointed	Year end review carried out in order to ensure figures align with the reporting of non-appointed activity within the regulatory accounts
Laboratory costs	Moved to service at year end based upon sampling information provided by water quality
Doubtful debts	Amount in respect of sundry debt moved to wholesale at year end

Severance	Centrally held costs not put to service as part of assessments. Analysis by person carried out and costs moved to appropriate service
IT system maintenance	Costs relating to IT system maintenance on retail systems not separately coded so manual adjustment required
Customer supply pipes	Work management system not set up to cost work on customer supply pipes to retail. Report by job type run to identify costs and manual transfer made

## 3.5 Changes in methodology

### 3.5.1 Changes to methodology compared to previous year

During 2014/15 the following improvements have been carried out:

- Insurance costs are now allocated directly to service via a database system.
- Use of assessments in SAP for salary allocations has been extended to include support services.

The following changes have been made to categorisation of costs between the 2014 and 2015 accounting separation return:

- Amounts paid to the Canals and Rivers Trust were shown under water abstraction in the 2014 submission. It has been established that part of the cost is in relation to highways drainage, so this year an amount of £0.3 million has been moved to Sewage Collection.
- There has been a change in the allocation of salaries on scientific services, with the individual water and waste water teams being allocated separately rather than as a combined team as was the case in the 2014 submission.
- The element of doubtful debts associated with sundry debt has been put to third party services. This was included under retail in the 2014 submission.
- A change has been made to the allocation of court costs income between household and non-household. The revised split recognises that the majority of income (99%) is in respect of household.
- There have been a number of changes to cost drivers in this year's submission in order to align more closely with Ofwat guidelines. Tables detailing cost drivers used with comparatives are shown in appendix 6.1.
- There has been a change in the cost driver for number of customers. In previous years the number of customers has been used, whilst this year weighted customer numbers has been used. This treats customers who receive a single service as one customer and customers who receive both water and sewerage services as 1.3 customers.
- General and support costs in LCML have been broken down into the individual components and shown separately whereas last year these were allocated to retail activity by FTE and not shown as an overhead. This change is consistent with Ofwat's preferred disclosure of costs.

### 3.5.2 Planned improvements to methodology

- In IN 15/01 Future company performance reporting and assurance, the Ofwat laid out new regulatory guidelines it expects water companies to adopt, including detailed requirements for the use of cost drivers.
- A review has been undertaken of the new requirements and a plan is place to deliver the changes required.
- In the 2014/15 submission YW has, where possible, adopted the cost drivers laid out in the new regulatory guidelines referred to in IN 15/01.
- During 2015/16 YW is planning to internally report accounting separation figures on a monthly basis. This will allow costs to be regularly monitored, validated and challenged.

## 3.6 Applying RAG 4.04

In RAG 4.04 Ofwat laid out general principles for accounting separation. The following details the principles which Ofwat have laid out, followed by the company's response and approach taken.

**Transparency:** the attribution methods applied within the accounting separation system need to be transparent. This requires that the costs and revenues apportioned to each service and business unit should be clearly identifiable. The cost and revenue drivers used within the system should also be clearly explained to enable a review of their appropriateness.

- Costs are allocated in a clearly transparent way via cost centres within the company's accounting system (SAP).
- Where adjustments are made to the costs in SAP this is to improve the accuracy of reporting and the reasons for the adjustments are disclosed in a table above.
- Cost drivers used are consistent with Ofwat guidance and are shown in the appendices.

**Causality:** cost causality requires that costs (and revenues) are allocated to those activities and services that cause the cost (or revenue) to be incurred. This requires that the attribution of costs and revenues to activities and services should be performed at as granular level as possible.

- An alternate cost centre hierarchy is maintained within the SAP system. This assigns every cost centre to a 'service level' node allowing reports to be run in the required format for the tables in accordance with Ofwat's Regulatory Accounting Guidelines. Checks are made to ensure all codes are included and that the balances reconcile to the financial statements.
- Where possible costs are allocated directly to service (e.g. Water Treatment). If allocation of costs is required the allocation methods used were chosen from the suggested methods in the guidelines. See section 5 for more details.

**Non-discrimination:** the attribution of costs and revenues should not favour any business unit within the regulated company and it should be possible to demonstrate that internal transfer charges are consistent with the prices charged to external third parties.

- The attribution of costs and revenues do not favour any business unit and all internal transfers are at cost.

**Objectivity:** the cost and revenue attribution criteria need to be objective and should not intend to benefit any business unit or service.

- To ensure no favour is given to any business unit, costs are directly allocated where possible and where this is not possible an objective measure is used to allocate costs.
- Objective cost allocation measures used are measures which are reported internally or externally, e.g. number of customer contacts, number of FTEs and are in some cases subject to external assurance.

**Consistency:** the cost and revenue attribution criteria should be consistent from year to year to enable meaningful comparison of information over time. Changes to the attribution methodology from year to year should be clearly justified and documented.

- The accounting separation tables are prepared in a consistent way each year in order to enable meaningful comparison of information over time.
- Any changes as detailed in Information Notices issued by Ofwat are implemented.
- Other changes which are implemented are done so to improve the accuracy of reporting and these changes are explained in section 3.5.1.

## 4. Billing and Collection

### 4.1 Billing and Collection

The following section provides more details about YW's arrangements for billing and collection activity.

### 4.2 Third party billing and collection

- YW currently has billing and collection agreements with Local Authorities and Housing Associations for collection of water and sewerage charges in tenant's rent.
- YW also has reciprocal cross boundary billing agreements with Severn Trent and United Utilities for billing and collection of sewerage charges.

**Table 6 Third party billing and collection**

	2014/15	
	£(m)	% split
Main Charges Revenue	991.432	
Local Authorities/Housing Associations	31.222	3.1%
Sewerage Charges billed by STW/UU	27.116	2.7%

- Commissions are included within the LCML contract price. All commissions are costed to the retail activity to which they relate.
- For Local Authority, Housing Association and Water Company cross boundary commissions a management estimate has been made of the allocation of costs between billing and debt collection.

### 4.3 Bills to 'the occupier'

YW does not issue bills to 'the occupier' and all bills are raised to a named customer. The company employs an effective vacancy management process to identify where unoccupied premises have become occupied.

### 4.4 Treatment of doubtful debt where a customer has vacated a property

The company's policy for treatment of doubtful debt where the customer has vacated a property leaving amounts unpaid is as follows:

- Where the customer has absconded without paying, and strategies to trace their whereabouts and collect outstanding monies have been fully exhausted, the debt may be written off.
- The bad debt provision is charged to operating costs to reflect the assessment of the risk of non-recoverability of debtors, including debt relating to absconding customers.
- Credit notes would only be applied if YW were made aware that the date of vacation was different to the one previously held on the customer's account. Due to data restraints YW is unable to identify the value of credit notes in such cases.

### 4.5 Approach to provisioning

- Higher provisioning percentages are applied to categories of debt which are considered to be of greater risk, including those with a poor payment history as well as to those of greater age.
- Bad debt provisioning rates are updated annually to reflect the latest collection performance data from the company's billing system.
- For unmeasured customers, all debt greater than three years old is fully provided for. For measured customers, all debt greater than four years is fully provided for.

## 5 Cost allocations

### 5.1 Cost allocations

Tables detailing explanations of cost allocations are shown in the appendices

### 5.2 Other direct costs

For other direct costs the following tables give a breakdown of cost categories and values included within wholesale and retail as part of other operating expenditure.

**Table 7a Wholesale**

	£m
General & Support	32.440
Scientific Services	3.078
Other Business Activities	5.010
Other Direct Costs	
- Employment costs	57.839
- Hired & Contracted Services	71.453
- Materials	26.822
- Other	4.929
	161.043
Other operating expenditure	201.571

**Table 7b Retail**

	£m
General & Support	8.341
Scientific Services	0.000
Other Business Activities	0.685
Other Direct Costs	
- Disconnections	0.060
- Demand side water efficiency initiatives	0.287
- Customer Side Leaks	1.432
- Other (external comms)	0.365
	2.144
Other operating expenditure	11.170

### 5.3 Local authority rates

A large proportion of the rates cost for retail is the rates cost for the LCML contact centre building which is charged directly from the local authority to LCML. A proportion of the YW rates overhead costs are allocated to retail based on floor area / FTE based on colleagues carrying out retail activity. Currently a number of YW colleagues carry out both retail and wholesale activities.

### 5.4 Breakdown of cost categories and values – exceptional items

There were no exceptional items in 2014/15.

## 5.5 Analysis of assets allocated to the retail table

The assets included in the retail table A8 are allocated to the following categories:

**Table 8 Analysis of assets**

Category	Retail household £m	Retail Non-household £m	Retail Total £m
<b>Current Cost Depreciation</b>			
Billing System	2.0	0.1	<b>2.1</b>
Other assets specifically allocated to the Retail table	3.0	-	<b>3.0</b>
<b>Total</b>	<b>5.0</b>	<b>0.1</b>	<b>5.1</b>
<b>Closing Net Book Value</b>			
Billing System	6.3	0.7	<b>7.0</b>
Other assets specifically allocated to the retail table	14.0	1.6	<b>15.6</b>
<b>Total</b>	<b>20.3</b>	<b>2.3</b>	<b>22.6</b>

'Other assets specifically allocated to the retail table' includes telephony systems, as well as buildings and equipment used solely by the retail business.

## 5.6 Method of allocating assets between wholesale and retail

No shared assets were allocated directly to the retail table. Each asset is allocated to the business unit of principal use and a recharge is made for use of such assets by the other business units.

## 5.7 Breakdown of recharges

### **Cost drivers used for shared assets & breakdown of recharges**

Assets which are used by more than one business unit are allocated to a single business unit of principal use and recharged to the relevant business units using an appropriate cost driver, as in table 9

**Table 9 Shared asset cost drivers**

Assets used by	Allocated to	Recharged to	Recharge basis	Total recharged in the year (£m)
Whole business	Treated Water Distribution	All business units	Full-time equivalent employees, headcount or vehicle recharges as appropriate	9.0
Wholesale only	Treated Water Distribution	Wholesale business units	Full-time equivalent employees, headcount or telemetry as appropriate	16.8
Water business	Treated Water Distribution	Water business units	Full-time equivalent employees in water business units	0.3
Sewerage business	Sewage collection	Sewerage business units	Full-time equivalent employees in sewerage business units	0.6
Above ground sites	Water Treatment	Water Resources, Water Treatment, Sewage Treatment, Sludge Treatment	Full-time equivalent employees in relevant business units	0.3
Below ground assets	Treated Water Distribution	Raw Water Distribution, Treated Water Distribution, Sewage Collection	Full-time equivalent employees in relevant business units	0.2
Retail business units	Retail (household)	Retail (household) and Retail (non-household)	Number of billed customers (household and non-household)	4.9

## 5.8 CCA register

The company maintains a Current Cost asset register (CCA) as well as a Historical Cost asset register (HCA). The existing CCA register was set up in 2010 with the assets valued at current cost at that time. From then on, all new asset additions have been automatically set up in both HCA and CCA registers. At the end of each financial year, the asset values in the CCA register are inflated by the appropriate Retail Prices Index figure used in the regulatory accounts.

## 5.9 Retail cost allocation household and non-household

For each row within the retail table the cost driver that has been used to allocate costs between household and non-household customers is shown in appendix 6.2.

## 6 Appendices

## 6.1 Wholesale / retail cost drivers

Activity	2014/15	2013/14
<b>Wholesale / Retail</b>		
Customer Services - Billing	Wholly in retail	Wholly in retail
Customer Services - Payment handling	Wholly in retail	Wholly in retail
Customer Services - Charitable trust donations	N/A	N/A
Customer Services - Vulnerable customer schemes	Wholly in retail	Wholly in retail
Customer Services Non-network customer enquiries and complaints	Wholly in retail	Wholly in retail
Customer Services- Network customer enquiries and complaints	Wholly in retail	Wholly in retail
Customer Services - Investigatory visits / first visit to customer	First time investigatory visits charged to retail only where not a network problem (including water stop tap)	All first time investigatory visits charged to retail
Customer Services Other customer services	Wholly in retail	Wholly in retail
Debt management	Wholly in retail	Wholly in retail
Doubtful debts	All put to retail with the exception of wholesale sundry billing debt	All put to retail
Meter reading	Wholly in retail	Wholly in retail
Services to developers	Providing information and administration for new connections in retail everything else in wholesale	Providing information and administration for new connections in retail everything else in wholesale
Disconnections and reconnections	Administration retail, doing is wholesale	Administration retail, doing is wholesale
Demand side water initiatives	All expenditure is retail except where expenditure is to meet wholesale outcomes	Cost of devices was retail, salaries were wholesale
Customer side leaks	All expenditure is retail except where expenditure is to meet wholesale outcomes	Costs are separated based on whether wholesale or retail driven
OOE - Other direct costs	Other direct costs which are wholesale in nature	Other direct costs which are wholesale in nature
OOE - General and Support - IT costs	Split based on headcount - proxy to number of computers	Split based on headcount
OOE - General and Support - motor vehicles	N/A	N/A
OOE - General and Support - Finance, HR, payroll, general management	HR on headcount, everything else FTEs	HR done on headcount, everything else FTE
OOE - Executive directors remuneration	FTEs	FTEs
OOE - Non-executive director's remuneration	FTEs	FTEs
OOE - General and support - Facilities, building / grounds maintenance	Floor area & FTE	Split out facilities cost based on number of FTEs
OOE - General and support - insurance	FTEs for staff related insurance, GMA values for asset insurance	FTEs for staff related insurance, GMA values for asset insurance
OOE - Other general and support costs	FTEs	FTEs
OOE - Regulation costs	One ninth to retail, eight ninths to wholesale	One ninth to retail, eight ninths to wholesale
OOE - Local Authority Rates	Floor space & FTE	Split out facilities cost based on number of FTE
Third party services, e.g. rechargeable works	All wholesale	All wholesale

## 6.2 Retail household / non-household cost drivers

Activity	Company	2014/15	2013/14
<b>Retail household / non-household</b>			
Customer Services - Billing	LCML	Number of bills	Number of bills
Customer Services - Payment	LCML	Number of payments	Number of payments
Customer Services - Charitable trust donations	YW	N/A	100% household
Customer Services - Vulnerable customer schemes	LCML	100% non-household	100% non-household
Customer Services - Non-network enquiries and complaints	YW / LCML	Volume of contacts	Split on number of customers
Customer Services - Network enquiries and complaints	YW / LCML	Volume of contacts	Split on number of customers
Customer Services First time investigatory visits - Retail	YW	Volume of visits	Number of customers
Customer Services - Other customer services	YW / LCML	N/A	N/A
Debt management	YW / LCML	Debt o/s over 30 days	Total debt o/s
Doubtful debts	YW	Direct allocation	Direct allocation
Meter reading	YW	Number of meter reads	Number of meter reads
Services to developers	YW	100% non-household	100% non-household
OOE - Disconnections and reconnections	YW/LCML	100% non-household	100% non-household
OOE - Demand side water efficiency initiatives	YW	100% household	100% household
OOE - Customer side leaks	YW	100% household	100% household
OOE - Other direct costs	YW / LCML	Various	Various
OOE - General and support - IT	YW	FTEs used to allocate to retail activity then activity cost driver used.	Pro-rata based on retail expenditure
OOE - General and support - IT	LCML	Customer numbers	FTE
OOE - General and Support - motor vehicles	YW/LCML	N/A	N/A
General and support, Finance, HR etc	YW	FTEs used to allocate to retail activity then activity cost driver used	Pro-rata based on retail expenditure
General and support, Finance, HR etc	LCML	Customer numbers	FTEs used to allocate to retail activity then activity cost driver used
General and support - Executive director's remuneration	YW	FTEs used to allocate to retail activity then activity cost driver used	FTEs used to allocate to retail activity then activity cost driver used
General and support - Executive director's remuneration	LCML	Customer numbers	FTEs used to allocate to retail activity then activity cost driver used
General and support - Non- Executive director's remuneration	YW	FTEs used to allocate to retail activity then activity cost driver used	FTEs used to allocate to retail activity then activity cost driver used
General and support - facilities	YW	FTEs used to allocate to retail activity then activity cost driver used	Pro-rata based on retail expenditure
General and support - facilities	LCML	Customer numbers	FTEs used to allocate to retail activity then activity cost driver used
General and support - insurance	YW	FTEs used to allocate to retail activity then activity cost driver used	FTEs used to allocate to retail activity then activity cost driver used
General and support - insurance	LCML	Customer numbers	FTEs used to allocate to retail activity then activity cost driver used
General and support - other	YW	FTEs used to allocate to retail activity then activity cost driver used	Pro-rata based on retail expenditure
General and support - other	LCML	Customer numbers	FTEs used to allocate to retail activity then activity cost driver used
Regulation and licence fee	YW	Customer numbers	50% household and 50% non-household
Local Authority Rates	YW	FTEs used to allocate to retail activity then activity cost driver used	Customer numbers
Local Authority Rates	LCML	FTEs	FTEs used to allocate to retail activity then activity cost driver used
Third party services	YW	N/A	N/A

### 6.3 Wholesale Water cost allocations

Expenditure line	Method of allocation	Why considered appropriate	How satisfied
Power	Optima system collects costs at meter level and this costed directly to the service where possible. Where site meters supply more than one service the account is split based upon estimated power usage of equipment on site	No sub metering at large sites so the only way that this is possible.	Management estimates are reviewed by finance business partners with operational colleagues
Income treated as negative expenditure	Allocated to main service, sub split to individual service using the same allocations as power above	No sub metering at large sites so the only way that this is possible.	Management estimates are reviewed by finance business partners with operational colleagues
Service charges - Abstraction	Directly allocated	Directly allocated	Directly allocated
Service charges - Other	Directly allocated	Directly allocated	Directly allocated
Service charges - Discharge	Directly allocated	Directly allocated	Directly allocated
Bulk Supply	Directly allocated	Directly allocated	Directly allocated
Other operating expenditure - Employment costs	Where costs can be directly allocated this is done so. For other costs these are allocated based on a management assessment. For overhead costs these are allocated based on number of FTEs, e.g. pension deficit	All employment costs charged to capital are booked based on timesheets. For remaining operating costs, management assessments are based, where possible, on operational data. Where this is not possible estimates have been made	Finance Business Partners are trained in accounting separation guidelines and meet with all operational budget managers. A peer review is also undertaken
Other operating expenditure - Hired and contracted services	These costs are allocated direct to service through our procurement system (SRM) and work management system (WMS)	Directly allocated	A review is undertaken monthly and at the end of the year to ensure all costs have been allocated correctly
Other operating expenditure - Other direct costs - Telephone	Landlines are directly allocated. Mobile phones are allocated in the same way as employment costs	Directly allocated, where possible, and the rest in line with cost of employment	In line with employment allocation process
Other operating expenditure - Other direct costs - Insurance	Insurance payments are allocated directly to service and premiums are allocated using an appropriate cost driver based on the type of insurance	Directly allocated where possible, and the balance is based on appropriate cost driver	Insurance database categorises insurance claims and the allocations for the premium are based on the type of cover
Other operating expenditure - Other direct costs - Leases / rents	Operational leases and rents are allocated directly to service.	Directly allocated	Monthly costs review to ensure directly allocated costs are correct
Other operating expenditure - Other direct costs - Contract cars	Allocated in the same way as employment costs	Directly allocated, where possible and the rest in line with cost of employment	In line with employment allocation process
Other operating expenditure - Other direct costs - Professional subscriptions	One ninth to each service	Based on Ofwat guidelines	Agrees with guidelines
Other operating expenditure - Other direct costs - GSS & Ex gratia	Directly allocated	Directly allocated	Monthly Guarantee Standards Scheme & ex-gratia review to ensure directly allocated costs are correct
General and support - IT	Allocated using headcount	Each colleague has a PC or handheld device even if part time	Proxy for number of PCs and handheld devices
General and support - HR	Allocated using headcount	Each colleague drives an HR cost even if part time	Proxy to how HR costs are driven
General and support - Facilities	Floor space and FTE	Based on Ofwat guidelines	Agrees with guidelines
General and support - Other	FTE	Based on Ofwat guidelines	Agrees with guidelines
Scientific services	Allocated on costs of sampling	Costs are driven by complexity of sampling, for which cost is a proxy	Monitor sampling for DWI purposes
Other business activities	Four ninths to water. Four ninths to waste, one ninth to retail	All of this cost is regulation costs. The cost allocation used is per the Ofwat guidance	Complies with guidelines
Local authority rates - Cumulo rates (water)	Use Gross Modern Equivalent Asset values (GMEA) to allocate costs	Based on value of assets assigned to the business unit which are reported in supplementary fixed assets tables	Complies with guidelines
Exceptional items	No items in 2014/15	N/A	N/A

## 6.4 Wholesale Waste Water cost allocations

Expenditure line	How allocated costs	Why considered appropriate	How satisfied
Power	Optima system collects costs at meter level and this costed directly to the service where possible. Where site meters supply more than one service the account is split based upon estimated power usage of equipment on site	No sub metering at large sites so the only way that this is possible	Management estimates are reviewed by finance business partners with operational colleagues
Income treated as negative expenditure	Directly allocated to sludge treatment	Directly allocated	Directly allocated
Service charges - Abstraction	Directly allocated	Directly allocated	Directly allocated
Service charges - Other	Directly allocated	Directly allocated	Directly allocated
Service charges - Discharge	Directly allocated	Directly allocated	Directly allocated
Bulk Supply	Directly allocated	Directly allocated	Directly allocated
Other operating expenditure - Employment costs	Where costs can be directly allocated this is done so. For other costs these are allocated based on a management assessment. For overhead costs these are allocated based on number of FTEs, e.g. pension deficit	All employment costs charged to capital are booked based on timesheets. For remaining operating costs, management assessments are based, where possible, on operational data. Where this is not possible estimates have been made	Finance Business Partners are trained in accounting separation guidelines and meet with all operational budget managers. A peer review is also undertaken
Other operating expenditure - Hired and contracted services	These costs are allocated direct to service through our procurement system (SRM) and work management system (WMS)	Directly allocated	A review is undertaken monthly and at the end of the year to ensure all costs have been allocated correctly
Other operating expenditure - Other direct costs - Telephone	Landlines are directly allocated. Mobile phones are allocated in the same way+ as employment costs	Directly allocated, where possible, and the rest in line with cost of employment	In line with employment allocation process
Other operating expenditure - Other direct costs - Insurance	Insurance payments are allocated directly to service and premiums are allocated using an appropriate cost driver based on the type of insurance	Directly allocated where possible, and the balance is based on appropriate cost driver	Insurance database categorises insurance claims and the allocations for the premium are based on the type of cover
Other operating expenditure - Other direct costs - Leases / rents	Operational leases and rents are allocated directly to service.	Directly allocated	Monthly costs review to ensure directly allocated costs are correct
Other operating expenditure - Other direct costs - Contract cars	Allocated in the same way as employment costs	Directly allocated, where possible and the rest in line with cost of employment	In line with employment allocation process
Other operating expenditure - Other direct costs - Professional subscriptions	Directly allocated	Directly allocated	Directly allocated
Other operating expenditure - Other direct costs - GSS & Ex gratia	Directly allocated	Directly allocated	Monthly Guarantee Standards Scheme & ex-gratia review to ensure directly allocated costs are correct
General and support - IT	Allocated using headcount	Each colleague has a PC or handheld device even if part time	Proxy for number of PCs and handheld devices
General and support - HR	Allocated using headcount	Each colleague drives an HR cost even if part time	Proxy to how HR costs are driven
General and support - Facilities	Floor space and FTE	Based on Ofwat guidelines	Agrees with guidelines
General and support - Other	FTE	Based on Ofwat guidelines	Agrees with guidelines
Scientific services	Allocated on costs of sampling	Costs are driven by complexity of sampling, for which cost is a proxy	Monitor sampling for DWI purposes
Other business activities	Four ninths to water. Four ninths to waste, one ninth to retail	All of this cost is regulation costs. The cost allocation used is per the Ofwat guidance	Complies with guidelines
Local authority rates - Non-domestic (waste)	Use Gross Modern Equivalent Asset values (GMEA) to allocate costs	Based on value of assets assigned to the business unit which are reported in supplementary fixed assets tables	All operational
Exceptional items	No items in 2014/15	N/A	N/A

## 6.5 Retail cost allocations

Expenditure line	How costs are allocated	Why considered appropriate	How satisfied
Customer services - billing	Where separately costed teams work solely on billing activity they are coded directly to billing. Where teams work for a proportion of their time on billing an appropriate cost driver is used. Where teams work solely on household or non-household they are allocated accordingly.	Where costs are separately identified on SAP these are charged direct. For costs which are allocated, e.g. postage, an appropriate cost driver is used, e.g. number of bills issued as a proportion of total items of mail dispatched.	Cost allocation methods are reviewed with a finance business partner and an operational colleague to ensure appropriate.
Customer services - payment handling	Payment commissions and the cost of the Payments team are held separately in SAP. Other costs allocated to payment handling are small and based on an appropriate cost driver	The majority of costs are separately identifiable	The majority of costs are separately identifiable
Customer services - charitable trust donations	No costs	N/A	N/A
Customer services - vulnerable customer schemes	Costs are allocated directly.	Direct cost allocation	Cost allocation methods are reviewed with a finance business partner and an operational colleague to ensure appropriate.
Customer services - non-network enquiries and complaints	For the contact centre costs are allocated between network and non-network using the number of contacts as a cost driver. The number of contacts agrees to numbers reported for the Company Compliance Certificate and SIM. Other teams costs are allocated based on management estimate	Costs are apportioned on the number of calls which is what drives the costs	The number of contacts used to apportion costs are assured through existing processes
Customer services - network enquiries and complaints	For the contact centre costs are allocated between network and non-network using the number of contacts as a cost driver. The number of contacts agrees to numbers reported for the Company Compliance Certificate and SIM. Other teams costs are allocated based on management estimate	Costs are apportioned on the number of calls which is what drives the costs	The number of contacts used to apportion costs are assured through existing processes
Customer services - first time investigatory visits - retail	An analysis is prepared of customer visits which are not due to a network failure	This is compliant with Ofwat's guidance that first time investigatory visits that are not due to a network failure are classed as retail activities	Cost allocation methods are reviewed with a finance business partner and an operational colleague to ensure appropriate.
Customer services - other customer services	No costs	N/A	N/A
Debt management	Most is done by separate household and non-household teams who are allocated directly. Some other teams are allocated to this activity by management estimate but the costs are much smaller.	The majority of costs are separately identifiable	The majority of costs are separately identifiable
Doubtful debts	Costs are allocated directly.	Costs are allocated directly.	Costs are allocated directly.
Meter reading	Costs are allocated directly.	Costs are allocated directly.	Costs are allocated directly.
Services to developers	Costs are allocated directly.	Costs are allocated directly.	Costs are allocated directly.
Other operating expenditure			
General and support - IT	LCML costs are allocated directly. For YWSL costs are allocated based on headcount.	Assumed each person employed has a PC, Laptop or handheld	Headcount from Payroll by section
General and support - HR	LCML costs are allocated directly. For YWSL costs are allocated based on headcount.	Assumed each person employed has a call upon HR services	FTE from Payroll by section
General and support - Facilities	LCML costs are allocated directly. For YWSL costs are allocated based on floor space and FTE.	Floor space alone is not valid as some staff carry out both wholesale and retail activities	Done on a facilities site specific basis
General and support - Other	LCML costs are allocated directly. For YWSL costs are one ninth of regulation costs	YWSL is regulation costs. The cost allocation used is per the Ofwat guidance	Complies with guidelines

## 6.6 Table A7 Wholesale 2014/15 to 2013/14 variances

WHOLESALE	Water		Waste Water	
	£m	%	£m	%
<b>Operating expenditure</b>				
Power	1.1	4.4%	(1.9)	(5.8%)
Income treated as negative expenditure	(0.2)	44.3%	(0.5)	35.5%
Service charges	(0.1)	(2.1%)	(0.0)	(0.9%)
Bulk supply imports	0.1	2.6%	0.0	0.0%
Other operating expenditure	3.6	3.9%	(4.2)	(3.8%)
Local authority rates	0.8	2.1%	1.1	6.0%
Exceptional items	0.0	0.0%	0.0	0.0%
<b>Total operating expenditure excluding third party services</b>	5.2	3.2%	(5.5)	(3.3%)
<b>Capital maintenance</b>				
Infrastructure renewals charge	(12.8)	(26.5%)	11.3	26.7%
Current cost depreciation	(0.9)	(0.9%)	(25.6)	(15.6%)
Recharges to other business units	(0.1)	0.4%	0.0	0.0%
Recharges from other business units	1.2	11.1%	(1.3)	(8.3%)
Amortisation of deferred credits	0.1	(7.7%)	0.0	(0.0%)
Amortisation of intangible assets	0.0	0.0%	0.0	0.0%
<b>Total capital maintenance excluding third party services</b>	(12.5)	(9.5%)	(15.6)	(7.1%)
<b>Third party services</b>				
Operating expenditure	0.7	65.1%	0.0	0.0%
Infrastructure renewals charge	0.0	0.0%	0.0	0.0%
Current cost depreciation	0.0	0.0%	0.0	0.0%
<b>Total operating costs</b>	(6.6)	(2.3%)	(21.1)	(5.5%)

## 6.7 Table A8 Retail 2014/15 to 2013/14 variances

RETAIL	Household		Non-Household	
	£m	%	£m	%
<b>Operating expenditure</b>				
Customer Services	(0.8)	(4.4%)	0.8	50.0%
Debt management	0.8	26.7%	(0.4)	(50.0%)
Doubtful debts	1.2	7.1%	0.1	6.7%
Meter reading	0.0	0.0%	0.0	0.0%
Services to developers	0.0	0.0%	(0.1)	(33.3%)
Other operating expenditure	0.3	3.0%	(0.6)	(40.0%)
Local authority rates	0.1	0.0%	0.0	0.0%
Exceptional items	0.0	0.0%	0.0	0.0%
<b>Total operating expenditure excluding third party services</b>	<b>1.6</b>	<b>3.2%</b>	<b>(0.2)</b>	<b>(3.3%)</b>
Third party services operating expenditure	0.0	0.0%	0.0	0.0%
<b>Total operating expenditure</b>	<b>1.6</b>	<b>3.2%</b>	<b>(0.2)</b>	<b>(3.3%)</b>
<b>Capital maintenance</b>				
Current cost depreciation	(0.1)	(2.0%)	0.1	0.0%
Recharges to other business units	0.1	(2.0%)	0.0	0.0%
Recharges from other business units	0.2	4.2%	(0.1)	(12.5%)
Amortisation of deferred credits	0.0	0.0%	0.0	0.0%
Amortisation of intangible assets	0.0	0.0%	0.0	0.0%
<b>Total capital maintenance</b>	<b>0.2</b>	<b>4.1%</b>	<b>0.0</b>	<b>(0.0%)</b>
<b>Total operating costs</b>	<b>1.8</b>	<b>3.3%</b>	<b>(0.2)</b>	<b>(2.9%)</b>
<b>Debt Written off</b>	<b>0.9</b>	<b>5.8%</b>	<b>0.1</b>	<b>6.7%</b>

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