

ACCOUNTING SEPARATION METHODOLOGY STATEMENT

FINANCIAL YEAR 2017 / 18



South Staffs Water

incorporating



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DEFINITION OF TERMS

SSW – South Staffordshire Water, a group company of South Staffordshire PLC.

CAM – Cambridge Region

SST – South Staffordshire Region

SOCI – Statement of Comprehensive Income, previously known as the Profit and Loss Statement

SOFP – Statement of Financial Position, previously known as the Balance Sheet

Oracle – The Company’s Financial Management System

Maximo – The Company’s works management system

Measured – A water customer whose bill was calculated based on volumetric usage measured by a water meter

Unmeasured – A water customer whose bill was calculated based on a schedule of rates, regardless of usage

RAGS – Regulatory Accounting Guidelines issued by Ofwat.

Price Controls – Wholesale and Retail markets as defined by OFWAT. Retail price control splits into non-household (NHH) and Household (HH) business units while Wholesale price control splits into Treated Water Distribution (TWD), Raw Water Distribution (RWD), Water Resources (WR) and Water Treatment (WT) business units

Departments – functions of the business where costs are charged for management accounting purposes. A Full list of SSW’s business units with accompanying price controls can be found on page 4-5

Account Combination – At SSW our account structure is a combination of 5 codes creating a 15-digit account number. The 5 combinations are as follows:

Company Code	Location Code	Activity Code	Subjective Code	Spare Code
XX	XXX	XXX	XXXX	XXX

Company Code (CC) – 2 digit code which identifies the company in which the posting relates to

Location Code (LC) – 3 digit code which identifies the physical location where the cost / revenue was incurred / earned

Activity Code (AC) – 3 digit code which identifies the activity in which has generated such cost / revenue

Subjective Code (SC) - 4 digit code which identifies the type of cost / revenue and allows for SOCI categorization

Spare Code – A spare 3 digit code that allows for further enrichment of cost / revenue data.

DEPARTMENTAL LIST

Department Name	Price Control / Cost Allocation Methodology
Customer Services Retail	RETAIL
AIS Asset Management Planning-WHS Cambridge Depots Computer Development Customer Leakage Customer Services Developer Services Distribution Rechargeable DLS DMA DLS Mains DLS R&D DLS Rehab DLS Reinstatement Team DLS Running Costs Fradley Depot Leakage Operations Leakage Strategy Mains Rehab Major Capital Projects Network Engineering Network Modeling Network Performance Power generation Production Strategy Service Development Technical Department Tipton Department Water Quality Water Regulations	TREATED WATER DISTRIBUTION
Blithfield Education Centre Blithfield Project Operational Maintenance Water Resources Water Strategy	WATER RESOURCES
Appointed Crypto Chemicals Fluoride Water Supply Water Treatment	WATER TREATMENT

DEPARTMENTAL LIST

Department Name	Price Control / Cost Allocation Methodology
CLO Running Costs Customer Rechargeable Customer Operations Streetworks	Activity Allocation
Capital Investment Delivery Over ground Asset Management	Capital addition in the year
Building Health & Safety Training Site Maintenance Training & Development	Direct Allocation
Regulation	Equal Split Between All Water Only Company Price Controls
Estates	Equal Split Between WR and TWD
Site Central	Floor Space
Creative Studio Central Admin Childcare Finance Health & Safety HR Merlot Restaurant Security Social Club Unallocated Water Board	FTE
Procurement	Material Spend
Stores	Material Spend exclusive of Chemicals
Control, Automation & Development	Maximo Allocation
Fleet Services	Number of Vehicles
Hampton Loade Treatment Works Northern Treatment Works Pumping Group East Pumping Group North Pumping Group South	Pumping Groups Allocation

HIGH LEVEL OVERVIEW

PURPOSE

Each year, the Company publishes an Annual Performance Report (APR) which contains various tables of regulatory information across price control units (APR section 2) and Retail and Wholesale upstream services (APR section 4). This document sets out the Company's methodology for the allocation of costs contained within the following APR tables:

- 2A – Segmental income statement
- 2B – Totex analysis – Wholesale
- 2C – Operating cost analysis – Retail
- 2D – Historic analysis of fixed assets
- 4D – Wholesale Totex analysis
- 4F – Operating cost analysis – Household retail

The Company can confirm that it has followed the principles and guidance set out in Regulatory Accounting Guideline (RAG) 4.07. The Company believes that in preparing its Accounting Separation information, appropriate allocations and cost drivers have been used and where possible we used costs drivers suggested by Ofwat. The allocations and costs drivers are reviewed each year, and our accounting separation methodology has been enhanced to reflect these changes and systems have been modified to capture additional information.

ASSURANCE

As committed to in our assurance plan, we subjected our cost allocation methodology to external assurance for this reporting year, using our assurance partner, Jacobs U.K Limited (Jacobs). Their work checked that our methodology complies with Ofwat's Regulatory Accounting Guidelines (RAGs).

We also continued to use our statutory financial auditor, Deloitte LLP, to audit the cost allocation data back to source for the annual accounts.

Assurance comments from Jacobs and Deloitte LLP can be found in the External Assurance of Financial ODIs and the Independent Auditors Report sections respectively, within the company's Full Annual report.

OPERATING / CAPITAL EXPENDITURE

Costs were allocated between operating and capital expenditure in accordance with the company's accounting policies and applicable accounting standards.

The deminimis for capitalisation was:

Minor purchases (e.g. office equipment)	£1,000
Buildings Expenditure	£5,000

These limits are consistent with those applied in previous years.

PROVISIONS

The only provision included in operating costs was for the purposes of bad debts, where the debts identified as being irrecoverable had not yet been physically written off in the billing file. This was consistent with previous years.

The level of bad debt provision was calculated on a formula basis and reviewed by Deloitte LLP to ensure that it was appropriate.

PREPARING THE ANNUAL PERFORMANCE REPORT

The company used its financial system, Oracle, to download a Trial Balance (TB). The downloaded TB detailed all actual revenue and expenditure for the given time period, at an account combination level. Using the CC from the account combination, actuals relating to non-appointed business streams were excluded. Furthermore, using the AC, the company was able to identify the balance of direct Capital Expenditure (Capex), Operating Expenditure (Opex) and Infrastructure Renewal Expenditure (IRE). Finally, the TB was enriched with the company's departmental structure and reconciled back to the management accounts.

OWC DETAIL

Due to the nature of business, some costs were capitalised through the Statement of Comprehensive Income (SOI). For example, the Employment costs of salaried employees who undertook capital works. This allowed the company to report the gross costs in the SOI categories but the bottom line was reported net of capital expenditure.

As a result of this, the OWC balance had to be netted back against the original costs to show the appointed operating cost within in each cost category. This was completed using the subjective codes within OWC, as different cost categories are capitalised in distinct subjective codes within OWC. For example, within employment costs salaries and temporary staff costs are capitalised on different subjective codes but both roll into OWC in SOI.

DEPARTMENTAL COST RE-ALLOCATION

There were a number of adjustments that were required in order to bring the management accounting departmental structure in line with OFWAT RAG's. Many of these adjustments were as a result of costs being held centrally for a variety of reasons.

- Fluoridation Management Fee Adjustment – Costs from Procurement, Finance and Chemicals move into Fluoride Department to account for the management of the fluoride contract.
- Reorganisation costs– costs held central, taken back to relevant departments.
- Director and Heads off Bonus - costs held central, taken back to relevant departments.
- Reallocation of employees between departments due to change in activities undertaken in FY17/18. This was reflected by only one customer service team member being required to shift into regulation.
- Customer Engagement costs incurred within the year were coded to the customer services department which was classified as a directly retail department, however these costs were allocated on an FTE basis and thus an adjustment was required prior to allocation.

DIRECT ALLOCATION DEPARTMENTS

Once in the departmental structure and OWC had been netted back, we took values into each Price Control. The departments that wholly related to one price control were taken direct. The residual departments were those which required allocation over multiple price controls.

The remaining departments could be differentiated by how the costs were coded. Some departments, such as Training & Development, Site maintenance and Building Costs, were coded at a location level and activity level. The company describes these departments as Direct Allocation Departments because using the LC we could identify where the costs were incurred and return them to such location.

Using Training as an in-depth example, employees of the company attended an external training course on the new GDPR legislation. When coded into Oracle, a training AC was used along with the LCs of the course attendees. For management accounting purposes, the training activity code allowed the company to report all training costs within a

PREPARING THE ANNUAL PERFORMANCE REPORT

training and development budget. For APR purposes, this method of coding allowed Training and development costs to be returned to the departments which incurred them, where they would be treated under the individual department's allocation methodology.

Of the cost in these Direct Allocation Departments the majority was therefore allocated directly, however a small value of expenditure related to general running costs. Examples of the type of expenditure that would fall into this category included the cost of mobile phones, salaries of management and vehicle costs; as these could not be directly attributed to one LC or AC. As such, this expenditure was allocated back over the locations that had incurred the directly attributable costs.

Following on with the Training example above, the company's Training Officer was a salaried role that could not be directly attributed to one price control. As such, we allocated this cost over the LCs that incurred training costs. Simplistically, if Finance, HR and Operations all incurred £10,000 of training and the cost of the company's training officer was £30,000 – each department would have received a third of the salaried cost of the Training Officer, £10,000.

ACTIVITY ALLOCATION

CUSTOMER OPERATIONS AND RECHARGEABLES

Customer operations and rechargeable departments coded expenditure at a Location, Activity and Spare Code level on a job by job basis through the company's work management system, Maximo. In this situation, the spare code was used to identify who was completing the works; Direct Labour Operatives (DLO's), Customer Liaison officers (CLO's) or Contractors.

As with the direct department allocations, a small proportion of expenditure could not be directly attributed to one Spare and or Activity. For further detail on how this was allocated please refer to appendix 1.

Once all expenditure was on a Spare and Activity code, we combined both to identify the price control in which it related to. These Activity and Spare combinations were reviewed annually with operational employees to ensure the accuracy of cost allocation between price controls.

PLANNING & STREETWORKS

Planning and Streetworks can be seen as a support department specifically for our CLO's, DLO's and Contractors completing works on our behalf. The team structure in both regions means that there was an equal split of resources allocated to support CLOs, DLOs and Contractors. In the Cambridge region, the team only supported CLOs and Contractors due to the business not operating a DLO Team however the support split remained equal. This was reflected in the allocation methodology.

Using the CC we split the departmental costs by region. In SST the costs were equally split over CLOs, DLOs and Contractors. In Cambridge, the costs were split equally between CLO and CON. In the coding structure we allocated to the spare code in order to retain the remaining account combinations of costs.

Planning & Streetworks costs were not coded at an activity level and therefore required allocation to activity codes. Balances on CLO and DLO were allocated to activity codes by the Customer Operations and Rechargeable department Direct Wages spend. For the CON spare balance, we used contractor spend as the nature of contractors means they are not paid via the company's payroll system. Please see appendix 2 for a visual representation.

CLO RUNNING COSTS

Firstly, CLO running costs was reported within the management accounts as CLO Running Costs CAM and SST. Within both, some costs were wholly attributable to TWD. For a full list of these costs please refer to appendix 3.

PREPARING THE ANNUAL PERFORMANCE REPORT

The remaining costs required allocation. In SST, the costs were allocated to activity codes based on the percentage of direct wage spend of CLOs of the Customer Operations, Rechargeable and Planning and Streetworks departments. In Cambridge, a legacy system means that the time spent by CLOs was not recorded on activity basis. We therefore allocated to activities using the next best alternative, number of jobs in FY17/18 categorized job type. This was obtained from Water Works, the Cambridge Region Works Management System. These activities were wholly attributable to one price control meaning no further allocation was required. The resulting price control splits by region of the CLO running Costs department costs were as follows:

Region	Retail	Treated Water Distribution (TWD)
Cambridge	26%	74%
South Staffordshire	22%	78%

Prior year Methodology Change Note: in FY16/17 Cambridge Region CLO Running Costs were allocated to activities using the SST direct wage splits.

CONTROL, AUTOMATION & DEVELOPMENT (CAD)

Maximo captures the time spent by members of the CAD department on an asset by asset basis. As each asset within the company is directly attributable to one price control, the company directly allocated CAD departmental costs based on the actual level of activity within the year. Please refer to the cost driver table for details of the FY17/18 price control splits. This information was extracted from Maximo.

PUMPING GROUPS AND TREATMENT WORKS

Pumping Group East (PGE) served the Cambridge region of SSW via 86 supply sites. Each supply site had its individual location code which allowed costs to be coded at the location which they were incurred. General running costs however were not directly attributable to one supply site and therefore have a general location code (106). These costs required allocation back to the supply sites. Pumping Group north and south serve the South Staffordshire region and consists of 4 general running costs locations codes and 211 supply site locations codes. As with PGE, PGS and PGN coded costs to the individual locations codes, with general running costs coded centrally. Hampton Loade Treatment Works (HLTW) and Seedy Mill Treatment Works (SMTW – also referred to as Northern Treatment Works) served the South Staffs region and were allocated in line with the PGN and PGS Methodologies.

The general running costs were pro-rated over the total spend at each location within the respective pumping group, resulting in all costs sitting on a pumping group site. The power costs at each site were allocated to price controls based on the FY17/18 Average Pumping Head at each site. The remaining costs are allocated on FY16/17 Gross Modern Equivalent Asset (MEA) values on a per site basis.

Prior year Methodology Change Note: in FY16/17 after power costs had been allocated the remaining costs were allocated based on the % of yearly spend at site per price control, which was derived from the Spare code when costs are booked. In FY17/18 costs not captured at price control have had to be allocated at MEA values by site.

PREPARING THE ANNUAL PERFORMANCE REPORT

FINANCE

Billing costs were collected within the finance department and can be identified directly using the location code (Y05). These costs were wholly attributed to Treated Water Distribution. The residual balance in the finance department was allocated to price controls using the FY17/18 FTE percentage.

WATERBOARD

The Additional Superannuation pension payment in FY17/18 was charged to Water from the Group and therefore came into the accounts via a management fee on the water board department. This cost required a specific allocation methodology. Firstly, this cost was transferred within Waterboard from management fees to the correct cost line within employment costs, additional superannuation. Secondly, the element relating to the Retail Non-household market (3%) was charged out. Subsequently, the residual balance was allocated on the PR14 Ofwat Information Note Guidance of 17% into Retail Household with the remaining balance being allocated within the wholesale price controls on the FTEs per price control in FY11/12 when the scheme was closed.

The remaining adjustments are summarized in the table below.

Cost	Allocation methodology
Executive Team members and other Senior managers	Managing, Finance and HR Director – FTE Wholesale Director – 100% Distribution Customer Services Director –100% Retail
I/C Cross charges out	Echo Building – Retail
Water UK costs	Split equally over business units
Cumulo Rates	Split on Gross Modern Equivalent Asset (MEA) Valuation of business units. All rates costs are included within the Local authority rates lines.
Local rates	Allocated the same as Site Central. (Based on M ²). All rates costs are included within the Local authority rates lines.
Insurance Premiums	The insurance premium was allocated based on the individual elements as follows: Material Damage/Business Interruption – MEA per business unit MD/BI Terrorism – MEA per business unit Combined Liability - 100% Treated Water Distribution Employer’s Liability – based on FTE’s Excess Layer – 100% Treated Water Distribution Trustees Liability – WCPS members per business unit Crime – MEA per business unit Engineering Inspection – MEA per business unit Chlorine Leakage (SUD) – 100% Water Treatment Contract Works, Machinery Movement and Hired in Plant – Percentage of plant hire spend within each business unit Fish Farm – 100% Water Resources Motor Trade – No of vehicles per business unit Broker Fees – allocated to each business unit based on the total splits above plus Motor Fleet insurance split by number of vehicles per business unit. (The actual Motor Fleet insurance premium was charged to each individual department using the number of vehicles and was therefore allocated to the business units along with the other costs of the department).

PREPARING THE ANNUAL PERFORMANCE REPORT

Cost	Allocation methodology
Insurance Excess	100% Distribution
Group Management Fee's and Non Exec Director Fee's	This has been apportioned based on the splits for the Water Board Directors. (Supply Director, Managing Director, Network Management Director, and Customer Operations Director)
All other costs	Split on number of FTE's per business unit.

SITE CENTRAL

Site Central was composed of costs for Green Lane offices (SSW) and Fulbourn Road offices (CAM), which could be identified using the location code. Green Lane was split into the following areas using the approximate m2:

- o Childcare facilities– 86 m2
- o Echo – 2,574 m2 (Note 1)
- o Fleet – 853 m2
- o Group – 650 m2
- o IWS – 1,858 m2 (Note 2)
- o Restaurant – 347 m2
- o Stores – 1,821 m2
- o Water Company – 3,044 m2

Echo provides customer contact, billing and debt collection for South Staffs Water. IWS (Integrated Water Services provide pump refurbishment activity for South Staffs Water).

Based on the actual running costs for Green Lane a cost per m2 was calculated. The costs for Site Central were allocated to these areas using floor space multiplied by the m2 unit rate. The cost in each area was then allocated to the business units based on the following cost drivers:

- o Busy Bees – FTE
- o Echo – 100% Retail
- o Fleet – No of vehicles in each unit
- o Group – FTE's in each unit
- o IWS - Percentage of spend with IWS in each business unit
- o Restaurant – FTE at Green Lane in each business unit
- o Stores – Material Spend without chemicals in each business unit
- o Water Company – FTE in each unit

PREPARING THE ANNUAL PERFORMANCE REPORT

Rates for the Echo building and Fleet Services building were charged direct, therefore no rates allocation had been made to Echo (100% Retail) or Fleet (allocated on the number of vehicles in each unit)

Site Central Fulbourn Road was allocated by the FTE per price control at Fulbourn Road offices.

FULL TIME EQUIVALENT (FTE) ALLOCATION

Central Admin, Childcare, Creative Studio, Health & Safety, Human Resources (HR), Merlot, Security and Social Club are departments which were allocated using the FY17/18 FTE Cost Driver. In addition, an element of cost from the Finance and Waterboard departments was allocated using the FTE Cost Driver, however adjustments were required first. Please refer to the Finance and Waterboard sections within 'Preparing the Annual Performance Report' Chapter for further explanation.

The FTE cost driver was calculated using payroll data and the company's departmental structure. This allowed the direct FTE to be taken to each price control, and the indirect departments that require allocation to be allocated in line with the cost allocation methodology.

Where department costs were allocated by FTE, their FTE's were excluded from the calculations. As noted from the OWC notes above, some departments cost were capitalised through OWC and where this was the case, the company adjusted the costs to reflect only the operating element. For consistency this approach was replicated in the FTE calculation. In addition, where employment costs were recharged to non-appointed activities in the cost allocation model, this was replicated in the FTE calculations for those individuals.

This result was an Appointed Operating FTE % per price control.

Prior year Methodology Change Note: This was important change from the methodology used in prior years and arose as a result of SSW's APR Assurance Audit. Previously, the FTE base used was not adjusted for capital employees. The resulting impact of this change was the Retail FTE percentage increased, ceteris paribus. Please note: in real terms Retail FTE percentage has fallen from the prior year due to the outsourcing of retail activities and further cost efficiencies. Please see 'Analysis of Significant Movements' for further clarification.

TABLE 4D – WHOLESALE TOTEX ANALYSIS WATER

At this stage all costs were allocated to price controls, however they still remain in SSW's SOCI cost categories. The below table identifies how costs have been directly allocated to Ofwat Table 4D table.

SOCI Category	Table 4D Category
Associated Companies	Other operating expenditure - excluding renewals
Employment Costs	Other operating expenditure - excluding renewals
Hired and Contracted Services	Other operating expenditure - excluding renewals
Infrastructure Renewals	Other operating expenditure - renewals expensed in year (Infrastructure)
Infrastructure Renewals	Other operating expenditure - renewals expensed in year (Non-Infrastructure)
Intercompany Costs	Other operating expenditure - excluding renewals
Local Authority Rates	Local authority and Cumulo rates
Materials and Consumables	Other operating expenditure - excluding renewals
Other Direct Costs	Other operating expenditure - excluding renewals
Power	Power
Provisions and Charges	Other operating expenditure - excluding renewals

In addition to the Table 4D categories listed above, there are Abstraction Charges/ Discharge Consents, Bulk Supplies and Third Party Services.

ABSTRACTION CHARGES / DISCHARGE CONSENTS

These costs were identified using the coding in the final TB as a result of these activities having their own specific subjective Codes (1700 and 3190 respectively). Abstraction Charges were wholly attributed to Abstraction Licences within Water Resources. Discharge Contents were wholly attributed to Water Treatment.

BULK SUPPLIES

Costs relating to Bulk Supplies could also be directly identified using the coding in the final TB. As SSW imports potable water only, an allocation between WR and WT was required. The company used the FY16/17 Table 4D Water Resources and Water Treatment cost splits for the respective water companies who supplied SSW with Bulks in FY17/18 to allocate the cost.

THIRD PARTY SERVICES

Costs attributable to this category were derived from multiple activities at SSW, which could be identified using the account combinations in the final TB. This includes the following:

TABLE 4D – WHOLESALE TOTEX ANALYSIS WATER

- Fluoridation
- Customer Rechargeable
- Distribution Rechargeable
- Supply Pipe Repairs
- Leakage Operations work on Supply Pipes
- Customer Liaison Officers work on Supply Pipes
- Direct Labour Operatives work on Supply Pipes
- Bulk Supplies

These costs have been removed from the expenditure lines and classified as 3rd Party operating expenditure, as per the Ofwat Table. Where salaried employees work on 3rd party operating expenditure, their proportion of time is reallocated to third party operating expenditure.

INFRASTRUCTURE RENEWALS

Infrastructure Renewals (IRE) was reported gross within the tables and was directly allocated between Infrastructure and Non-infrastructure. Using Ofwat Guidance, IRE expenditure was directly classified between the two categories allowing for direct allocation.

COST DRIVERS

Cost Drivers FY17/18	WR	RWD	WT	TWD	Retail
Full Business FTE	5.23%	0.72%	13.48%	73.90%	6.68%
FTE at Fulborn Road	7.59%	0.31%	13.72%	73.24%	5.14%
Number of Vehicles	5.3%	0.4%	11.9%	76.7%	5.7%
Directors Time	11.53%	4.38%	15.92%	48.02%	20.15%
Gross Modern Equivalent Asset (MEA) Values	2.99%	3.80%	6.83%	85.15%	1.23%
Total Material Spend	2.02%	0.13%	69.47%	27.68%	0.70%
Total Material Spend excluding Chemicals	5.97%	0.37%	11.11%	80.00%	2.05%
Capital Additions	8.45%	0.00%	27.44%	63.57%	0.54%
Control, Automation & Development	50.22%	0.15%	25.25%	24.38%	0.00%
Wholesale WCPS Members in FY11/12	8.53%	0.04%	13.92%	77.51%	0.00%
% of Spend with IWS	0.00%	0.00%	0.00%	98.80%	1.20%

WHOLESALE UPSTREAM SERVICES

This section sets out how the company allocated costs between Water resources and Network+. The company's methodology statement above has been used as a basis for separating these costs.

WATER RESOURCES

- Abstraction Licence - Abstraction Licence was directly coded to this activity and had been identified in the final TB and moved to this Price Control.
- Raw Water Abstraction - This was the total Water Resources Costs from the company's Accounting Separation less Abstraction Licence costs as outlined above.

RAW WATER TRANSPORT AND STORAGE

- Raw water storage - This was the cost of operating and maintaining the company's Reservoirs. The two main reservoirs that hold raw water are Blithfield and Chelmarsh. These costs were identified using the location code in the final TB for these reservoirs.
- Raw Water Transport - This was the total Raw Water costs taken from the company's Accounting Separation tables less the costs of raw water storage

WATER TREATMENT

- This was the total Water Treatment costs taken from the company's Accounting Separation.

TABLE 4F – COST ANALYSIS HOUSEHOLD RETAIL

INTRODUCTION

Following SSW's exit from the eligible (Non-Household) market, the company's retail costs relate to only Household Customers. No allocation is made between NHH and HH customers as in prior years.

For Tables 2C and 4F, the retail price control must be allocated from SOCI categories into Ofwat defined lines and from a Retail total into Measured HH and Unmeasured HH Elements. The retail costs mainly comprised of: The Echo Contract, Bad Debt Provision, Customer Services Retail Departmental costs and Retail related activity costs derived from retail activities undertaken by CLO's, DLOs or Contractors.

COST CATEGORY ALLOCATION

Echo provides a detailed breakdown of the contract costs, allowing the direct allocation into OFWATs defined categories. The bad debt provision was by nature wholly attributable to Doubtful Debts. Based upon the responsibilities of the Customer Service Retail Team, this cost was wholly attributed to General and Support Expenditure apart from Enghouse costs which relates to Debt Management, Charitable Trust Donations which was wholly attributed to Charitable Trust Donations and Rapid Licences which was allocated over users of the RAPID system.

Finally, the activity driven element of retail costs was directly allocated to the relevant lines dependent upon the activity code. This balance was derived from the Retail elements of CLO Running Costs, Customer Operations and planning & Streetworks. This was feasible due to the company's work management system mapping specific activities to specific activity codes which in turn map into Ofwat defined categories.

MEASURED/UNMEASURED ALLOCATION

The cost drivers used to split Ofwat defined categories between Measured and Unmeasured customers are compiled below:

OLD TABLE 4F CATEGORIES	ALLOCATION METHODOLOGY	NEW TABLE 4F CATEGORIES
Billing	Number of Bills	Customer services
Payment handling, remittance and cash handling	Number of Payments	Customer services
Debt management	HH Debt > 90 Days Split Measured / Unmeasured	Debt management
Doubtful debts	Actual Measured / Unmeasured Debt Charge	Doubtful debts
Charitable trust donations	Number of Customer given Grant in FY17/18	Customer services
Vulnerable customer schemes	Number of Social Tariff Customers	Customer services
Non network customer enquiries and complaints	Number of Contacts	Customer services
Meter reading	Wholly Attributable to Measured	Meter reading
Meter maintenance/installation non capex	Wholly Attributable to Measured	Other operating expenditure

TABLE 4F – COST ANALYSIS HOUSEHOLD RETAIL

OLD TABLE 4F CATEGORIES	ALLOCATION METHODOLOGY	NEW TABLE 4F CATEGORIES
Network customer enquiries and complaints	Number of Contacts	Customer services
Other direct costs	Number of Customers	Other Operating Expenditure
General and support expenditure	Number of Customers	Other Operating Expenditure
Other business activities	Number of Customers	Other Operating Expenditure
Local Authority rates	Number of Customers	Other Operating Expenditure
Third party services	Number of Customers	Third party services operating expenditure

DEMAND SIDE WATER EFFICIENCY

In addition to our normal demand side efficiency schemes, our Education Outreach Officer implemented demand side water efficiency initiatives within local schools to promote water efficiency and water awareness. A proportion of this employee's time, as well as an element of management time, was allocated to Demand side water efficiency using time based drivers.

CUSTOMER SIDE LEAK REPAIRS

Customer Side leak repairs were collected in our Customer Leakage Department allowing SSW to easily identify expenditure relating to Customer Side Leak Repairs. As a result, the departmental cost was wholly attributed to this cost category. The expenditure is 100% funded by the Wholesale price controls due to a business decision to target Leakage as one of the company's ODIs.

FIXED ASSET TABLES

The fixed assets and depreciation in the cost allocation tables used historical cost information. With all fixed asset information taken directly from the fixed asset register within Oracle. Each asset was coded directly to a department which identified the price control it was used in, with the exception of Water Resources. Water Resources assets were identified by taking the balance sheet figures for boreholes and assets for Blithfield. These were identified from the fixed asset register for South Staffs Region. For the Cambridge Region all assets with the description "Boreholes" were extracted from the fixed asset register.

All retail fixed assets were coded directly to one department and therefore could be identified separately to wholesale assets. These assets were then allocated between households and non-household based on the number of customers.

The Company confirms that it followed the principle use rules set out in RAG 4.06. Shared assets between wholesale and retail were wholly recorded in the business unit of principal use. All shared assets identified were principally used by wholesale and a proportion of the depreciation cost was recharged between wholesale and retail.

The recharge from wholesale to retail in the year of £0.035m related to the use by retail of the Company's Works Management System. Around 10% of the system use was in relation to customer contact, customer appointments and updating the Company's billing system, RAPID.

ANALYSIS OF SIGNIFICANT MOVEMENTS

Movements Greater than 10% on FY16/17 costs have been discussed below

WHOLESALE

- Power - £1.4m increase
 - Predominately driven by higher pass through charge rates and volumes pumped
- Bulk Supply – £0.009m increase in bulk supply costs
- Other Operating Expenditure - £7.6m increase
 - £6.9m relates to the increase in Infrastructure Renewals Expenditure (IRE).

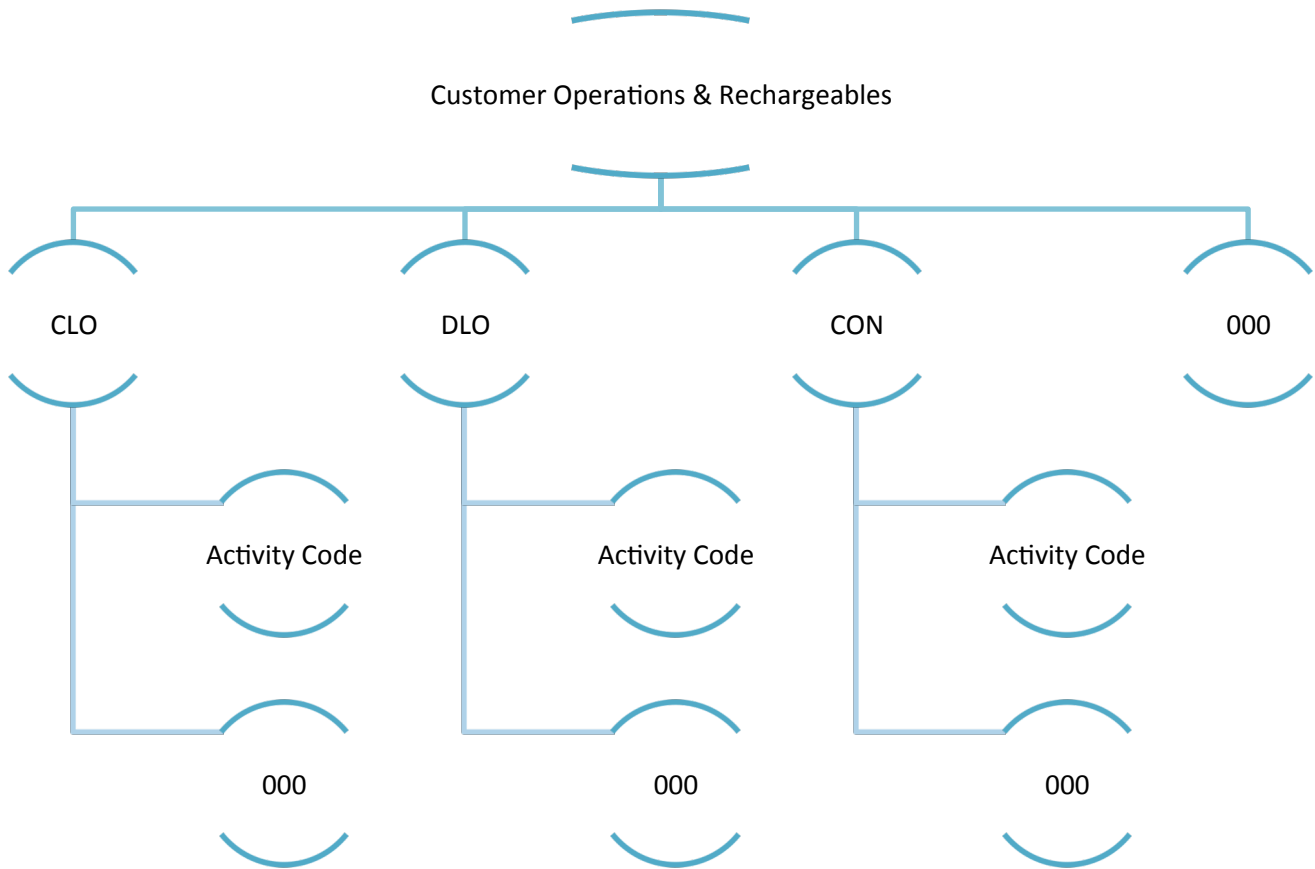
	FY16/17	FY17/18
Reported Infrastructure Renewals Expenditure	£8.7m	£15.6m
Comments	Reported Net of Contributions. Contributions - £1.5m	Reported Gross of Contributions. Contributions - £5.6m

- The remaining variance is attributable to the increase in general and support expenditure allocated to wholesale resulting from FTE changes. The Retail price control shows the corresponding saving.
- Third Party Services – (£0.27m) decrease
 - In the previous year, SSW experienced two large bursts in the Cambridge region for which the incident costs were rechargeable (£0.130m) and have not re-occurred.
 - In addition, bulk supply exports have reduced along with Fluoridation costs.

RETAIL

- Customer services - £0.63m increase
 - This movement was due to £0.22m increase in network customer enquiries, which was driven by additional resources obtained to respond to enquiries and an increased number of customer enquiries resolved by Customer Liaison Officers.
 - Furthermore, £0.25m uplift in Non-network customer enquiries resulting from additional resources taken on to improve the service offered to customers.
- Debt Management – (£0.11m) decrease
 - As a result of lower Paypoint costs driven by lower activity.
- Other Operating Expenditure – (£0.99m) decrease
 - Due to the full year efficiency savings of transferring metering to Echo and restructuring the company's retail operations. This reduced the number of retail FTE's and so the level of general and support costs allocated to retail on a FTE basis by £0.82m.
 - Echo's cross charge of their General and Support costs fell by £0.17m in the year.
 - The allocation of the company's communications department was previously a direct retail cost. A review of the work undertaken by the department led to SSW treating the department as a general and support department; which was allocated by FTE's, leading to a £0.120m retail saving.

APPENDIX 1



Expenditure is split by the Spare Code. In the South Staffordshire Region, any balance on 000 is allocated back across CLO, DLO and CON based on Spend as follows:

$$000 \times (CLO / (CLO + DLO + CON))$$

$$000 \times (DLO / (CLO + DLO + CON))$$

$$000 \times (CON / (CLO + DLO + CON))$$

In the Cambridge Region however, it is only prorated over CLO and CON due to the company not operating a DLO team in Cambridge.

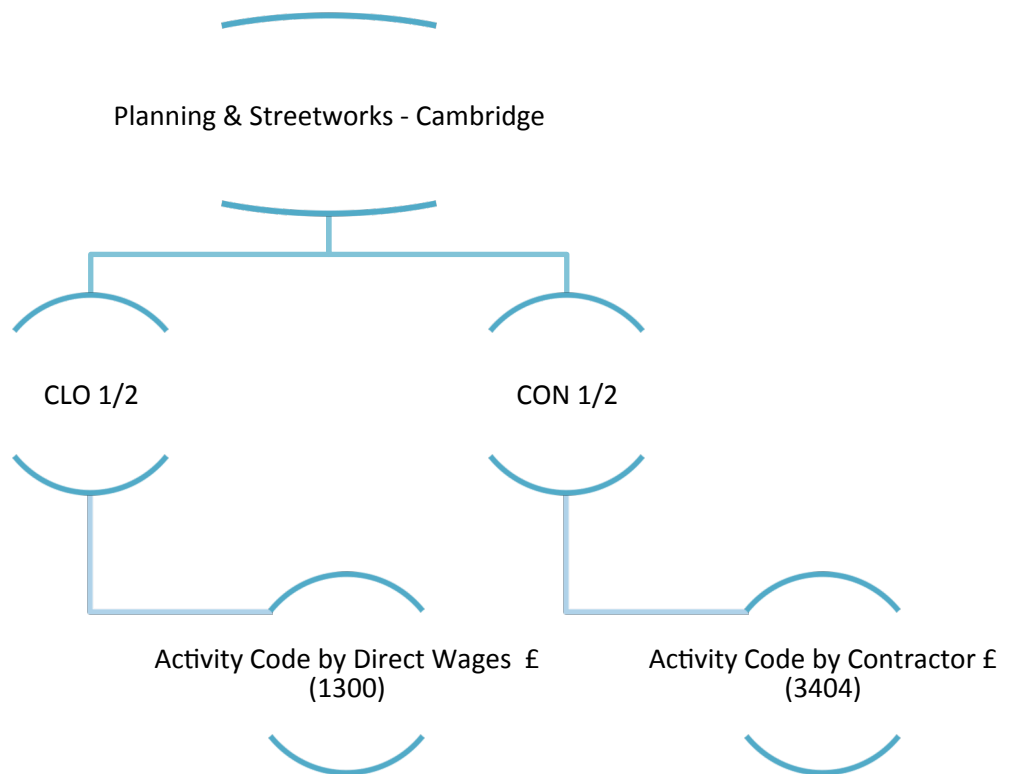
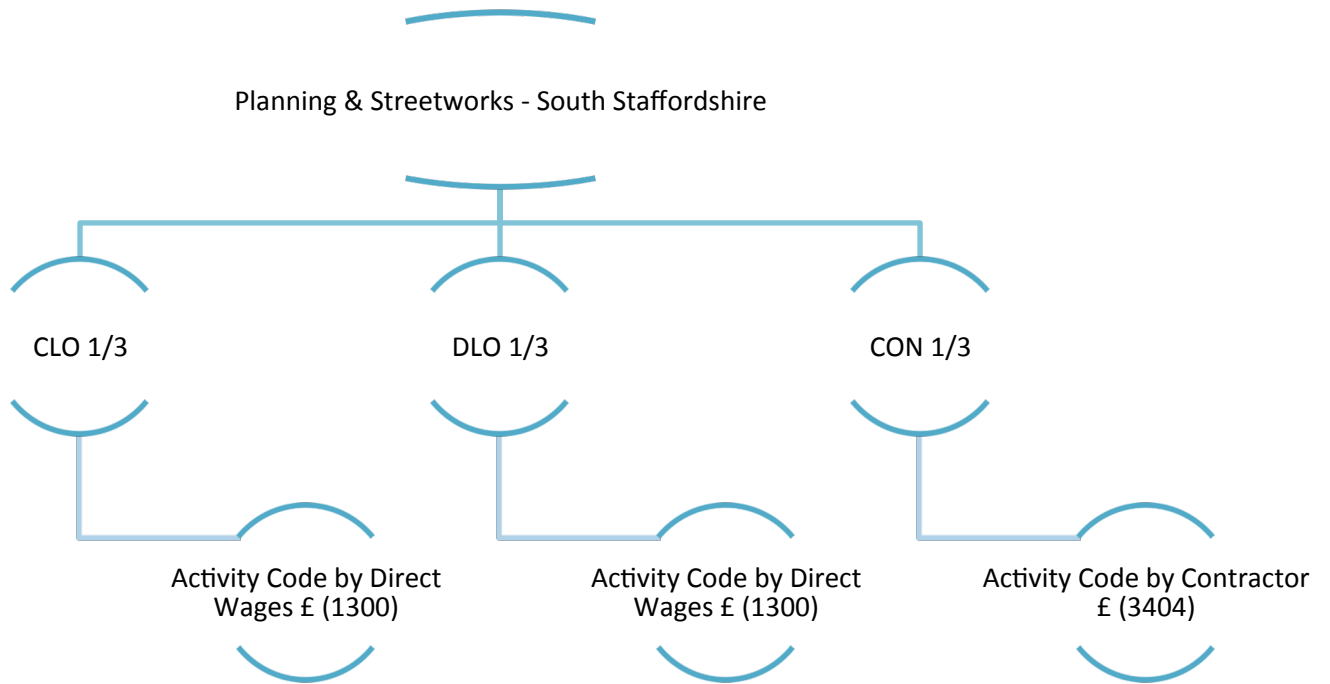
Secondly, CLO, DLO and CON balances are split out by the Activity Codes. Any Balance on 000 is allocated over the Activities based on Spend.

$$000 \times (Activity\ 1 / (Sum\ of\ All\ Activities\ excl.\ 000))$$

$$000 \times (Activity\ 2 / (Sum\ of\ All\ Activities\ excl.\ 000))$$

$$000 \times (Activity\ 3 / (Sum\ of\ All\ Activities\ excl.\ 000))$$

APPENDIX 2



APPENDIX 3

