

**PORTSMOUTH WATER LTD
UPSTREAM SERVICES (Wholesale Business)**

Governance Process

The Upstream Accounting Separation table has been prepared by the Management Accountant and reviewed by the Chief Accountant. The allocation of operating expenditure between Trunk and Local Treated Water Distribution Business Units has been advised by the Commercial Manager.

The Engineering Director has done a final review of the Accounting Separation allocations, and approved the data for submission to Ofwat.

Methodology Statement for Accounting Separation

The Methodology Statement details the systems in place and the sources of information used to populate the Accounting Separation Tables in the Regulatory Accounts. (See main Accounting Separation Methodology Statement for details.)

This guidance details the methods used to allocate the total operating costs from the existing split of Wholesale Business Units, to the lower level split of Services, as follows:

| | |
|-----------------------------------|--|
| <u>Water Resources</u> | Abstraction Licence Raw Water Abstraction |
| <u>Raw Water Distribution</u> | Raw Water Transport Raw Water Storage |
| <u>Water Treatment</u> | No further split |
| <u>Treated Water Distribution</u> | Trunk Treated Water Distribution Local Treated Water Distribution |

See Appendix 1 for Operating Cost Allocation

Operating Expenditure

Water Resources

The Abstraction Licence costs are taken from the invoice paid to the Environment Agency, relating to 2013/14. The remaining expenditure is all Raw Water Abstraction.

Raw Water Distribution

Raw Water Storage relates to Highwood Reservoir at the Itchen site. The costs allocated include power and associated direct employment costs. The remaining expenditure is all Raw Water Transport.

Treated Water Distribution

The split of operating costs between Trunk and Local Treated Water Distribution has been done with a series of allocations, depending on the type of expenditure, as follows:

Power

This is allocated mainly to Trunk Treated Water Distribution, and reflects the pumping costs of moving water from Water Treatment into the distribution network. There are a few booster stations along the length of the Local distribution network and the power associated with these is included in Local Treated Water Distribution. These booster stations include Madehurst, Shedfield and Titchfield.

Other Pumping Costs

These are allocated on the same proportion as the power costs, and include employment costs, contractor costs and materials.

Mains & Services

Employment costs are allocated on a management estimate, and this reflects the fact that it is not usually internal labour which is used to repair trunk mains, but contract labour.

Materials and other direct costs are allocated on total length of mains for each of Trunk and Local mains.

Inspectors

One senior inspector works solely on Trunk mains and there is an assistant inspector who is working alongside him. This means that there are 2 FTE's working on Trunk mains. Costs of inspectors are allocated on the proportion of FTE's working on Trunk mains.

Contractors

Contract labour which is used on Trunk mains is directly coded to 'Other Contractor's Charges' and can be allocated to Trunk Treated Water Distribution.

Other Direct Costs

Other costs include Company Reinstatement, Distribution Administration, Cleaning and Operations Centre, and are allocated on the basis of total length of mains for each of Trunk and Local mains.

Overheads

Overheads are split on the same proportion as the total direct costs.

Infrastructure Renewals Charge

This charge is allocated in total to Treated Water Distribution.

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The split of the charge between Trunk and Local Treated Water Distribution is based on the value of the assets. This is a current valuation, based on the actual assets that are held in the GIS system.

Current Cost Depreciation

Water Resources

All the depreciation is allocated to Raw Water Abstraction.

Raw Water Distribution

Depreciation for Highwood Reservoir is allocated to Raw Water Storage and all other depreciation is allocated to Raw Water Transport.

Treated Water Distribution

Service Reservoirs' depreciation is allocated directly to Trunk Treated Water Distribution and the remaining depreciation is allocated between Trunk and Local Treated Water Distribution on the basis of the value of the associated mains.

Changes in Upstream Costs > 10%

As per the Ofwat guidance, below is a summary of the Upstream costs which have changed by >10% since last year, and an explanation of the differences.

| | <u>Change 2013 vs 2014</u> |
|----------------------------------|----------------------------|
| <u>Operating Expenditure</u> | |
| Raw Water Storage | +31% |
| <u>Current Cost Depreciation</u> | |
| Trunk Treated Water Distribution | +28% |
| Local Treated Water Distribution | +158% |

Raw Water Storage operating expenditure relates to Highwood Reservoir and only amounts to £38k in 2014. This compares to a cost £29k in 2013.

Current Cost Depreciation in the upstream analysis for 2013 did not reflect the allocation of all meter assets to the Wholesale Business. This change in 2013 was reflected in the Regulatory Accounts and is now included in the Upstream Services numbers. This accounts for the large increase in Local Treated Water Distribution depreciation.

The 2014 asset additions in the year account for the remaining increase in both Trunk and Local Treated Water Distribution depreciation.

Date: 30.05.2014
Prepared By: C Jemphrey

ACCOUNTING SEPARATION 2013/14

Appendix 1

**UPSTREAM SERVICES
2013/14**

WHOLESALE WATER

| Business Unit | NETWORK PLUS | | | | | | | | | | TOTAL |
|------------------------------------|---------------------|-----------------------|------------------------|-------------------|-----------------|----------------------------------|----------------------------------|----------------------------------|----------------------------------|--------|-------|
| | Water Resources | | Raw Water Distribution | | Water Treatment | Treated Water Distribution | | Treated Water Distribution | | TOTAL | |
| Service | Abstraction Licence | Raw Water Abstraction | Raw Water Transport | Raw Water Storage | Water Treatment | Trunk Treated Water Distribution | Local Treated Water Distribution | Trunk Treated Water Distribution | Local Treated Water Distribution | TOTAL | |
| Total Operating Expenditure | 1.327 | 1.246 | 0.611 | 0.038 | 3.061 | 4.096 | 6.296 | 4.096 | 6.296 | 16.675 | |
| IRC | - | - | - | - | - | 1.191 | 3.986 | 1.191 | 3.986 | 5.177 | |
| CCD | - | 0.367 | 0.106 | 0.144 | 2.449 | 1.290 | 1.420 | 1.290 | 1.420 | 5.776 | |
| Total Operating Costs | 1.327 | 1.613 | 0.717 | 0.182 | 5.510 | 6.577 | 11.702 | 6.577 | 11.702 | 27.628 | |
| Total Business Unit Operating Cost | 2.940 | | 0.899 | | 5.510 | 18.279 | | 18.279 | | 27.628 | |
| Volumes/Drivers | | | | | | | | | | | |
| Length of Mains | | | | | | | 490 | | 2,773 | | |
| Unit Costs | | | | | | | 13.4 | | 4.2 | | |