

## ACCOUNTING SEPARATION 2013/14

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### PORTSMOUTH WATER LTD REGULATORY ACCOUNTS 2013/14

#### **Governance Process**

The Accounting Separation tables have been prepared by the Management Accountant and reviewed by the Chief Accountant. The allocation of direct costs between Wholesale and Retail has been reviewed by the Commercial Manager; this is mainly Inspectors, Distribution Administration and the Operations Centre. The allocation of Retail costs between the direct activities has been reviewed by the Customer Services Manager.

The Finance and Managing Directors have done a final review of the Accounting Separation allocations, and approved the data for inclusion in the Regulatory Accounts.

#### **Methodology Statement for Accounting Separation**

This statement details the systems in place and the sources of information used to populate the Accounting Separation Tables in the Regulatory Accounts.

The Company's detailed nominal ledger management information reports allow costs to be identified for each cost centre in the Company and therefore the direct costs of each business unit (e.g. Water Resources/Treatment) can be built up using the reports. The management reports allow for separate identification of direct costs relating to the Retail functions of the business. The general and support costs of the business are not allocated by business unit in the nominal ledger and it is therefore necessary to use methods of allocation to be able to provide this level of detail.

The Ofwat Accounting Separation guidance has been used and followed where appropriate, in the separating of costs for the reporting of figures in the Wholesale and Retail tables. Where it is felt the guidance does not offer the best solution, or is inappropriate for the allocation of costs, an alternative approach has been used. A line by line commentary as to how costs have been allocated is provided below.

The allocation of indirect costs between business unit areas is carried out using the Company's management information reports, detailed above. Some of the indirect costs are capable of being charged directly to business units; however with some indirect costs centres it is necessary to make either a pro-rata allocation between the areas or to base the allocation on an assumption of cost driver. (E.g. material costs for the allocation of stores department costs)

The Company has followed the guidance issued by Ofwat relating to the proportional allocation of assets & costs between business units. It has

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followed Ofwat's hierarchy of cost drivers when deciding upon the most appropriate basis for allocation of both assets & costs.

The Company has however opted to base the allocation of a number of assets and costs on a management estimate basis. Where it has chosen to do so the Company is satisfied that this was the only valid option given the time and costs involved in the other suggested alternatives. Senior departmental managers provided the allocation percentages for these items, using the Business Unit descriptions, and these percentages have been reviewed and updated to reflect any changes in the business in the current year.

### **Operating Cost Analysis (Wholesale Business only)**

The Wholesale Business of the Company consists of the following Business Units: Water Resources, Raw Water Distribution, Water Treatment and Treated Water Distribution.

### **Direct Costs**

**Employment Costs:** Employment costs are treated in two separate ways in terms of allocation to cost centres and activities. Costs of employment for employees who complete timesheets have been directly allocated to the relevant cost centre and work activity, and can then usually be allocated directly to a business unit. Employment costs of employees who do not complete timesheets have been split on the basis of a management estimate of time spent working for each business unit. The majority of employees carry out work in relation to a number of business units.

Direct employment costs coded to cost centres which are split between Wholesale and Retail functions have been allocated as follows:

#### **Inspectors**

These costs are allocated to either Treated Water Distribution or Retail. Costs of meter reading, debt recovery/disconnections consultations with customers, query/complaint investigations and customer-side leaks are directly allocated by timesheets and charged to Retail. All other direct costs, allocated by timesheets, relate to Treated Water Distribution. Office work and administration costs are allocated to Retail on the basis of a management estimate, which is 30%, and the rest is allocated to Treated Water Distribution.

#### **Distribution Administration**

These costs are allocated to either Treated Water Distribution or Retail. Management salaries are allocated to Retail on the basis of a management estimate, which is 20%, and the rest is allocated to Treated Water Distribution.

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Leakage and byelaw enforcement salaries are allocated 100% to Treated Water Distribution

The remaining costs relate to 4 office staff, of which 1 works 100% for Wholesale and the other 3 work 100% for Retail.

### Operations Centre

Costs are allocated to all business units on the basis of a management estimate, which includes a 30% allocation to Retail, and this represents the service that is provided to customers who call outside normal working hours.

### Mains & Services and Company Reinstatement

These costs are mainly allocated to Treated Water Distribution. However, the costs of any customer-side leaks are allocated to Retail.

The management estimate percentages were reviewed for 2013/14 and remain unchanged from 2013/14.

**Power:** Power costs reported here mainly relate to treatment works & pumping stations, including borehole sites, and are 100% Wholesale. Power has been allocated on the basis of the assets that consume it. Each individual location is billed separately and bills provide the data of consumption and cost by location. Each of these costs is reported by location in the nominal ledger reports.

Where an asset consumes power for a dual purpose, then a split based on pumping head has been used to allocate the cost between the functions. These dual functions are mainly water resources abstraction and treated water distribution, but in some cases water treatment is a significant function and so consumes a proportion of the power. Where water treatment is a minor element of the asset function, then a management estimate has been used to allocate costs to this business unit.

An allocation of costs for the Bulk Supply of water to Southern Water has been based on the pumping head at Slindon for Whiteways Lodge reservoir. 48% of power costs have been allocated to the Bulk Supply.

**Hired and Contracted Services:** As per the guidance these costs have been allocated directly where possible and on the basis of direct allocation for costs relating to pumping and treatment.

**Materials & Consumables:** These costs have largely been identified as directly attributable to individual business units. However, management estimates of time spent carrying out the activities of the different business units were used to enable Inspectors, Distribution Administration and Operations Centre costs to be allocated to individual business units, and in particular between Wholesale and Retail. The exception to this is Assistant

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Inspectors who carry out meter reading, which is a Retail function, and 100% of their materials costs have been allocated to Retail.

Materials relating to customer-side leaks are all allocated to the Retail business unit.

**Service Charges:** This relates to abstraction charges and has therefore been allocated directly to Water Resources.

**Other direct costs:** These were largely attributable to individual business units. However, management estimates of time spent carrying out the activities of the different business units were used to enable Inspectors and Distribution Administration costs to be allocated to individual business units.

### **Operating Expenditure**

**General and Support Expenditure:** This covers a range of costs that have each been identified and allocated in the following ways.

**Land & Property:** The nominal ledger structure allows these costs to be largely directly identifiable by location. The costs that are directly attributable to individual business units have been identified and other associated costs not directly attributable have been allocated on a pro rata basis of those directly allocated.

Retail costs have been separately identified as a percentage of those costs relating to the Head Office only. The percentage allocated to Retail is based on the floor space occupied by the Retail function at the Head Office.

**Mechanical & Electrical:** The nominal ledger structure allows these costs to be largely directly identifiable by location. The costs that are directly attributable to individual business units have been identified and other associated costs not directly attributable have been allocated on the basis of the management estimate of time spent working for each business unit by the employees of that department.

Retail costs have been separately identified as a percentage of those costs relating to the Head Office only. The percentage allocated to Retail is based on the floor space occupied by the Retail function at the Head Office.

**Supply Engineer:** These represent the cost of the Supply Manager and related overheads. The costs have been split based on the same allocation as Mechanical & Electrical costs.

**Supply General:** The supply general costs were allocated directly where possible to individual business units. The remaining costs include the running costs of the Company's Telemetry system, and, in order to be consistent with

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the treatment of the fixed assets, were allocated on the basis of the Supply Manager's estimate between business units.

Distribution General: Costs here were allocated between Treated Water Distribution and Retail based on the management estimate of time spent carrying out associated activities by Distribution Administration staff.

Personnel Services: Personnel costs have been split on the basis of FTE's in each business unit, as per the issued table guidance. These costs include Staff Welfare. However, any costs relating to Water Efficiency have been directly allocated to Retail.

Legal & Property: A management estimate of time spent is used as a driver to split the costs for this area.

Financial Services: Financial Services costs have been split on the basis of a management estimate of time spent by the department working for each of the business units.

Data Processing: In previous years allocation of all these costs was based on the usage of the mainframe by system type. However, with the introduction of a new customer billing system, outside the mainframe, we have changed the allocation to be direct for mainframe costs, where the mainframe system time can be analysed, and then on the basis of number of computers in each Business Unit, for the remaining expenditure.

Operational & Technical support: Direct allocation of costs by business unit has taken place, as per the guidance.

Vehicles & Plant: These costs, as per the table guidance, have been allocated pro rata via the allocation of the NBV of vehicle and plant fixed assets. Motor vehicle insurance is included in these costs.

Materials Storage: As per the guidance this has been split on the basis of the allocation of direct costs of materials and consumables.

FRS17 Pension Charge: The costs of this have been split based on the employment costs of each business unit.

National Insurance costs: This is allocated on the basis of employment costs. Employment costs of salaried employees were collated by department. The NI charge was then allocated to business units using the same methods as was used for the costs of each of the individual departments.

General Administration: The remaining general administration costs have been allocated directly to an individual business unit where possible. However

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there are a number of costs that cannot be allocated directly, the treatments of these are as follows:

- Head Office utilities: These have been split on the basis of floor area by business unit.
- Directors' salaries and related costs: Allocation based on the number of FTE's in each business unit.
- Secretaries' salaries and related costs: Allocation based on the number of FTE's in each business unit.
- Slow moving stock provision: Allocated on the basis of the direct allocation of materials and consumables.
- Professional fees, subscriptions & audit costs: This has been allocated on the basis of the direct costs of the business, excluding the abstraction charges, as it is felt that this would distort the % allocation towards the Water Resource business unit.
- Insurance costs: Allocation of insurance costs is directly to a business unit where possible, and based on FTE's by business unit for the policies relating to employee liability and directors' and officers liability. The remainder relates to building and contents insurance and is split on the floor space allocation between Retail and Wholesale.
- Promotional Strategy and Print Room costs: These costs are allocated entirely to Retail.

### **Scientific Services**

The costs of Scientific Services have been split based on a management estimate of time spent working for each business unit. The Water Quality Manager has prepared this estimation and it includes the number of water samples taken for each business unit. There is no allocation of costs to the Retail business unit., and this is a change from last year, where any direct sampling at customer taps was allocated to Retail.

### **Other Business Activities**

The costs of regulation have been allocated directly to Business Units where possible, and evenly across all 5 business units for any remaining costs, as per the table guidance.

### **Local Authority Rates**

As per the table guidance the costs of local authority rates are split on the GMEA of land and buildings. This information is sourced from the fixed asset tables in the Regulatory Accounts.

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### **Third Party Services Opex**

These costs relate directly to both the bulk supply of treated water to Southern Water Services and the costs of the distribution department for rechargeable works. These have therefore been directly allocated.

### **Infrastructure Renewals Charge**

This has been allocated directly to Treated Water Distribution.

### **Current Cost Depreciation**

This allocation comes directly from the fixed assets tables in the Regulatory Accounts.

The allocation bases above are considered the most appropriate treatment for each of the cost areas. Management has taken consideration of the cost, time and appropriateness of other possible allocation methods and has decided that the above treatments are the most appropriate for the Company to follow. The treatment of direct costs and operating expenditure is consistent with the treatment of the relevant fixed assets for allocation purposes.

### **Operating Cost Analysis (Retail Business only)**

The Retail Business is located at the Head Office of the Company in Havant and consists of the following functions:

Customer Services Department (including Debt Recovery and Postage)

Commercial Manager

Print Room

Bad Debts Provision

% of Inspectors (see Wholesale allocations)

% of Distribution Administration (see Wholesale allocations)

% of Operations Centre (see Wholesale allocations)

Customer-side leaks

% of Other Business Activities (Regulation)

% of Head Office costs (Land, Property and Mechanical & Electrical)

% of General and Support costs

### **Direct Costs**

The methodology above for the Wholesale business identifies the direct costs of employment, materials and consumables and other direct costs which have been allocated between Wholesale and Retail. These relate to the costs of Inspectors, Distribution Administration and Operations Centre, as well as customer-side leaks.

In addition, there are costs which are direct Retail costs and can be identified from the company nominal ledger reports. These are as follows:

Customer Services Department (including Debt Recovery and Postage)

Commercial Manager

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Print Room

Bad Debts Provision

Below is a line by line description as to how the direct costs have been allocated to the Retail activities and then allocated between Household & Non-Household for each activity.

In the Regulatory Accounts the operating expenditure for Retail is in a less detailed format, with one line for 'Customer Services' and another for 'Other Operating Expenditure'. The definition of these line items is in RAG 4.04 and has been followed.

Customer Services is the sum of the following activities:

Billing

Payment Handling, Remittance and Cash Handling

Non-network Customer Enquiries and Complaints

Network Customer Enquiries and Complaints

Other Operating Expenditure is the sum of the following activities:

Disconnections (customer contact only and not the physical disconnection)

Demand Side Water Efficiency Initiatives

Customer Side Leaks

General and Support expenditure

Other Business Activities

**Billing:** Direct employment costs of Customer Services staff are allocated to Billing, as well as 75% of Print Room staff costs. Customer Services stationery is allocated 100% to Billing activities and Postage is allocated to Billing on the basis of number of bills sent. 33% of General Management costs are allocated to Billing. An allocation of stationery is made from the Print Room and the Photocopy Room, as well as 25% of the software licence costs.

The total Billing cost has been allocated between household and non-household on the basis of the number of bills issued in these areas, as per the table guidance.

**Payment Handling, Remittance and Cash Handling:** Direct employment costs of Customer Services staff are allocated to this activity, as well as a proportion of Finance Services staff. Retail Bank Charges are allocated 100% here, as well as contract repairs & maintenance and 25% of the software licence costs.

These costs have been allocated to household and non-household on the basis of the number of payments made for each area, as per the table guidance.

**Debt Management:** Employment costs of the Customer Services Debt Recovery staff have been allocated to this activity, as well as Debt Recovery



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Commission from third parties. Postage costs have been allocated to this activity and represent the remaining costs after the allocation to Billing. 25% of the software licence costs have been allocated here, as well as 33% of Management salaries.

The allocation between household and non-household is based on the debt outstanding > 30 days for each, at the end of March 2013.

**Doubtful Debts:** Costs are allocated directly to this activity.

The allocation between household and non-household is based on direct allocation where possible, with the remainder, which is all measured debt provision, allocated on the basis of measured debt outstanding > 30 days at the end of March 2013.

For 2013/14 the total amount of Doubtful Debts is £665k. This is split as follows:

Unmeasured Doubtful Debts	£529k	> 99% household
Measured Doubtful Debts	£136k	household and non-household

Of the £136k for Measured Doubtful Debts, £44k relates to former tenants, who are all household customers.

The remaining £92k relates to a 15% provision for current outstanding debt (£40k) and an allowance for the movement in total debt written off (£52k). These 2 categories are both allocated between household and non-household customers on the basis of current debt outstanding >30 days.

**Vulnerable Customer Scheme:** There is no material cost associated with the administration of the vulnerable group scheme.

**Non-network Customer Enquiries and Complaints:** Direct employment costs of Customer Services staff are allocated to this activity, as well as 33% of General Management and 100% of the Commercial Manager. 25% of the software licence costs are allocated to this activity and a proportion of telephone costs from General and Administration.

The allocation between household and non-household is based on the number of non-network customer contacts recorded for each business unit, as per the table guidance.

**Meter Reading:** Direct employment costs of Inspectors and Assistant Inspectors are allocated to this activity, as detailed in the Wholesale commentary above, as well as Distribution Administration meter reading supervision. Associated motor transport costs are also allocated here.

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The allocation between household and non-household is based on the number of meter reads in each business unit, as per the table guidance.

**Network Customer Enquiries and Complaints:** Direct employment costs of Inspectors, Distribution Administration and the Operations Centre are allocated to this activity as well as other associated direct costs.

The allocation between household and non-household is based on the number of network customer contacts recorded for each business unit, as per the table guidance.

**Disconnections:** Direct employment costs of Inspectors carrying out customer consultations for this activity are allocated here.

These costs are allocated directly to non-household.

**Demand Side Water Efficiency Initiatives:** These costs are directly identifiable and allocated to this Retail activity. The costs include Water Efficiency and Promotional Strategy.

They are allocated to household and non-household efficiency measures.

**Services to Developers:** These costs are chargeable work supervision costs by Distribution Administration and the salary costs of staff who deal directly with developers with regard to new services. They are allocated directly to this Retail activity. Last year only the Distribution Administration supervision costs were allocated to Retail.

All costs only relate to non-household customers.

**Customer Side Leaks:** These costs are directly identifiable and allocated to this Retail activity as described in the Wholesale commentary above.

All costs only relate to household customers.

**Other Direct Costs:** No costs have been allocated on this line.

**General and Support expenditure:** These costs represent the remaining costs not identified as being direct costs for the purposes of this table and mainly relate to the General and Support costs described above and allocated between the Wholesale and Retail business units.

They have been allocated between household and non household in two ways, the direct Customer Service employment costs for each and on the basis of customer numbers. The guidance advocates the usage of the number of FTE's. However employment costs should represent an allocation that would be similar to that of the FTE basis. As staff work for both business units in reality it would have been difficult to split these costs on the basis of FTE's.

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All general and support costs relating to employment have been allocated on the basis of the direct employment costs in each activity, as identified in the calculation of the direct cost figures.

The remainder of the general and support costs have been allocated by customer numbers as this represents the best estimate of how costs actually relate to the general and support activities performed.

### **Scientific Services**

There is no allocation of costs to the Retail business unit. Last year all costs relating to the sampling at customer taps was allocated to Retail.

### **Other Business Activities**

The costs of regulation have been split evenly across all 5 business units, as per the table guidance. The 20% of cost allocated the Retail is split between household and non-household on the basis of customer numbers in each.

### **Local Authority Rates**

As per the table guidance the costs of local authority rates are split on the GMEA of land and buildings. This information is sourced from the fixed asset tables in the Regulatory Accounts.

### **Third Party Services**

There are no identified third party services for Retail.

### **Current Cost Depreciation**

This allocation comes directly from the fixed assets tables in the Regulatory Accounts.

The Company's management is satisfied that the costs and allocation methods used in the Retail Operating Cost are the most appropriate. The guidance has largely been followed and on occasions where this is not the case, the Company has used its judgement to produce the most appropriate methods of cost allocation in order to give accurate cost allocations.

### **Changes in Retail Costs > 10%**

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

	<u>Change 2013 vs 2014</u>
Customer Services	+25%
Debt Management	-12%
Doubtful Debts	+42%
Meter Reading	-14%
Services to Developers	+108%
Local Authority Rates	-85%

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Customer Services has increased by 25% due mainly to the increase in headcount in the department. Also, postage costs have increased by 12% in the year.

Debt Management has decreased by 12% due to less staff in this area.

Doubtful Debts increased by 42% due mainly to the write-off of additional debt in the year.

Meter Reading costs fell by 14% due to an increase in commission costs received from a third party of 12%.

Services to Developers costs that relate to the direct contact with the customer have now all been allocated to Retail, as per the Ofwat clarification notice. This was not the case in the previous year.

Local Authority rates have been allocated to Retail on the basis of floor space occupied by that Business Unit, which gives an 85% lower cost than in the previous year. Previously, costs were allocated on the basis of NBV of assets.

Scientific Services costs are all allocated to Wholesale, as stated above.

### **Current Cost Analysis of Fixed Assets (Wholesale and Retail)**

Portsmouth Water keeps current cost fixed asset ledgers for all categories of fixed assets. The assets contained within these ledgers are separately identified and are updated on a regular basis.

Capital expenditure comprises expenditure on overground assets plus new mains expenditure and the purchase of vehicles, computers and small plant items (including meters).

The disaggregated fixed asset tables require the separation of assets into each of the 5 business units, with a further separation of the retail assets between household and non-household categories.

The current cost fixed asset registers have now been arranged in order to classify the existing assets into the relevant business units for Accounting Separation reporting purposes. The asset additions are assessed prior to addition to the ledger, to determine which business unit they belong to. The Ofwat business unit definitions have been used as a guide for the asset allocations.

The current cost fixed asset ledgers are maintained on Excel spreadsheets and the data is therefore flexible to the specific adjustments required to Accounting Separation tables. Look up functions and 'if' statements have been used in order to produce, within Excel, a version of tables for each of the

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asset types maintained in the current cost fixed asset ledgers. Each line in the fixed asset registers are linked into a formula that looks up the asset values, depreciation and the business unit classification. The individual tables created in Excel are then amalgamated to produce the required inputs for the Accounting Separation tables.

In previous years, the Company has followed the guidance issued by Ofwat relating to the proportional allocation of assets between business units. It has followed Ofwat's hierarchy of cost drivers when deciding upon the most appropriate basis for allocation of assets. The Company has opted to base the allocation of a number of assets on a management estimate basis. Where it has opted to do so the Company is satisfied that this was the only valid option given the time & costs involved in the other suggested alternatives.

However, as required by Ofwat from 2012/13, all assets have been allocated to either a Wholesale business unit or Retail, depending on the business unit of principal use. Consequently, the Retail Fixed Asset table in the Regulatory Accounts now only contains assets that are directly allocated to the Retail business unit, and any shared assets have been identified and it was decided that Treated Water Distribution in Wholesale was the most appropriate business unit to be the one of principal use.

Where an asset has been allocated entirely to Wholesale, but provides a tangible benefit to Retail, a recharge has been calculated and is included in the total Retail operating costs, while reducing the Wholesale operating costs.

*An analysis of the assets allocated to Retail, and associated depreciation costs are in Appendix 1.*

### **Asset Allocations between Business Units**

#### **Infrastructure Assets**

Infrastructure Assets have been allocated directly to either Raw Water Distribution or Treated Water Distribution. The assets as at 31<sup>st</sup> March 2008 had already been categorised as either Raw Water aqueducts or as Potable Water Mains as part of the PR09 process in table B7.13 of the Company's Final Business Plan submission. Infrastructure asset additions beyond this date have been assessed as to the business unit that they belong in. All additions are directly allocated.

#### **Other Tangible Assets, Vehicles**

The Fixed Asset Schedules used in the preparation of these tables itemise each vehicle by registration reference. This enables the drivers and users of these vehicles to be identified. Where applicable, the vehicles have been allocated to one single business unit. Where direct allocation of vehicles to single units was not possible then a consistent approach to allocation has been taken to that of the relevant operating costs.

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Where the activities associated with the use of a single vehicle covered a number of business units, a management estimate was produced detailing the time spent carrying out activities for each business unit. This estimate was produced by the Senior Departmental Manager and the Management Accountant. The management estimate was then used as the bases to allocate the value of the vehicle proportionally between business units.

### **Other Tangible Assets, Small Plant & Meters**

The Small Plant Current Cost Fixed Asset ledger has been analysed and those plant items that were directly identifiable as being used for the purpose of only one business unit have been allocated directly to that business unit. There are a number of small plant asset types that related to company departments whose activities straddle the business units. These assets have been allocated on the same basis as the related operating costs.

### **Operational Assets**

Operational assets have been directly allocated to a single business unit where possible. Where this was not possible assets have been allocated on bases consistent with the guidance document:

#### Offices & Depots

Where business activities straddle the business units the assets have been allocated on a consistent basis with that of other assets that are utilised by the same department.

The Head Office has been allocated on the basis of floor area & then sub allocated either directly to a single business unit or has been proportionally allocated based on management estimates for shared service areas. For example, the Laboratory office space has been proportionally allocated between business units on the same bases that the Laboratory equipment has been allocated by. All other offices and depots have been allocated either directly or on the basis of management estimates (as above).

#### Land

Land values have largely been identified as attributable to one business unit. Ofwat's Knowledge Management Team has provided advice regarding a number of sites and as to how they should be allocated for the purposes of asset separation. Portsmouth Water has followed this guidance.

Where land is utilised for the purposes of more than one business unit, the land has been allocated accordingly. Technical drawings of the sites have been provided by the Company's Drawing Office and these have been used to allocate the land to each business unit necessary on the bases of floor area.

#### Service Reservoirs and Treatment Works

These assets have been allocated directly to individual business units.

### Pumping Stations

Pumping station assets have been allocated directly to individual business units, where possible, using the asset inventory category mapping tables supplied by Ofwat. These allocations have been verified by the Supply Manager. There are only a small number of assets that required allocation to more than one business unit, due to the fact that they carry out activities that are for the benefit of multiple business units.

### Telemetry Assets

These have been allocated to a number of business units on the basis of a Management estimate produced by the Supply Manager and the Management Accountant.

### Retail Household and Non-Household Allocation

The allocation of asset values between Retail Household & Retail Non-Household business units is on the basis of the number of properties in the financial year. This basis for allocation ensures that assets have been allocated in a manner consistent with the associated operating cost.

### Capitalisation Policy

The Company classifies costs as either capital expenditure or operating expenditure based on a number of factors. These include the value, nature and purpose of the expenditure.

There are no formal procedures for the classification of costs to either operating expenditure or capital expenditure, due to the size of the company, the number of staff involved in the accounting process and the operating procedures that the company follows.

A detailed capital programme is drawn up each October for the coming financial year. This is approved by the Company's Board and incorporated into the Company's Budget. Following Board approval individual schemes are programmed for the coming year by Project Managers responsible for delivering the schemes. The Project Managers are responsible for the control of expenditure on the schemes and authorise each individual item of expenditure incurred. The Chief Accountant reviews the scheme expenditure in order to ensure that the correct accounting treatment has been applied.

On a monthly basis the capital expenditure relating to the board approved capital schemes is reviewed by the Chief Accountant, prior to submission to the Board of a monthly capital statement which shows authorised amounts. This report details the expenditure by scheme. Any material variances are investigated and resolved.

For small plant, equipment and vehicles a list is drawn up and approved by the Company's Board. Purchases made are reviewed for correctness of

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treatment and to ensure that these are all capital items. The policy adopted by the company is that only items above £500 are capitalised.

The Chief Accountant reviews the small plant and vehicle additions on a monthly basis prior to entering the additions onto the asset records.

Capitalised costs include contractor invoices, stores issues, direct labour charged to schemes plus on-cost recovery and the design and supervision staff costs related to project management.

The Executive Directors ensure that the capitalisation policies and procedures adopted by the business are being operated correctly and that they are fit for purpose by regular review of the business processes and by the reviewing of the capital scheme expenditure totals on a monthly basis. The Finance Director and Chief Accountant ensure that the company complies with the current accounting standards applicable to the Company.

The treatment of Infrastructure renewals varies between the Regulatory Accounts and the Statutory Accounts of the Company. In the Statutory Accounts the Company has followed common industry practice and adopted the infrastructure renewals accounting policy as set out in FRS 15. This has not been applied in the Regulatory Accounts at the request of Ofwat.

**Date:** 10.05.2014  
**Prepared By:** C Jemphrey



**Appendix 1: Allocation of Assets to Retail**

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**Table of Retail Fixed Assets**

	Total Value NBV £'000	Retail NBV £'000	Household NBV £'000	Non-household NBV £'000	Total Value Depreciation £'000	Retail Depreciation £'000	Household Depreciation £'000	Non-household Depreciation £'000	Cost Driver Household/Non-Household
<u>Assets Directly Coded to Retail</u>									
Billing System	617	617	584	33	75	75	71	4	No of Customers HH/Non-HH
Vehicles	4	4	3	1	2	2	2	-	No of Customers HH/Non-HH
Other Assets	275	275	260	15	40	40	38	2	No of Customers HH/Non-HH
<b>TOTAL DIRECT RETAIL</b>	<b>896</b>	<b>896</b>	<b>847</b>	<b>49</b>	<b>117</b>	<b>117</b>	<b>111</b>	<b>6</b>	
<u>Assets with a recharge to Retail</u>									
Telephony Equipment	43	20	19	1	9	4	4	-	
<u>Buildings -</u>									
Head Office (Main Building)	3,200	1,507	1,427	80	62	29	27	2	No of Customers HH/Non-HH
Other Buildings (Stores, Garage, Car Park at Havant, % to Retail)	2,826	240	227	13	60	5	5	-	No of Customers HH/Non-HH
Vehicles	79	25	24	1	47	15	14	1	No of Customers HH/Non-HH
<u>Land -</u>									
Head Office	834	158	150	8	-	-	-	-	No of Customers HH/Non-HH
Other Plant	1,248	437	414	23	189	77	73	4	No of Customers HH/Non-HH
Other Operational Assets	468	93	88	5	18	5	5	-	No of Customers HH/Non-HH
<b>TOTAL RECHARGE</b>	<b>8,698</b>	<b>2,480</b>	<b>2,349</b>	<b>131</b>	<b>385</b>	<b>135</b>	<b>128</b>	<b>7</b>	
<b>TOTAL RETAIL ASSETS</b>	<b>9,594</b>	<b>3,376</b>	<b>3,196</b>	<b>180</b>	<b>502</b>	<b>252</b>	<b>239</b>	<b>13</b>	