

Scottish Water Business Stream 2006-07

Section M Tables - Regulatory Accounts

General Comments

The Regulatory Accounts Tables M1 to M25 were prepared using reports from the corporate finance system in a format consistent with the Commission's (WIC) reporting requirements.

Scottish Water Business Stream (SWBS) did not use Scottish Water's (SW) Activity Based Management (ABM) software to allocate costs to WIC activities. Instead, information from the SWBS General Ledger, combined with non-financial information from the billing system has been used to apportion costs to WIC activities and to split costs between water and wastewater services. The coding structures in the General Ledger and the reporting capabilities of the billing systems are being continuously reviewed to ensure greater accuracy in cost allocation.

Table M1 - Historic Cost Income and Expenditure Account

This table was populated using information directly captured in the General Ledger.

The tables below reconcile the data in M1 to both the statutory accounts and the E tables.

| Per M Tables | 2006-07 |
|---|-----------------------|
| | £m |
| M1.1 Turnover | 140.9 |
| M1.1a Wholesale charge | -126.8 |
| M1.2 Other operating costs | -7 |
| M1.3 Depreciation | -0.3 |
| M1.8 Operating surplus | 6.8 |
| M1.10 Net interest receivable less payable | -0.7 |
| M1.12 Surplus on ordinary activities before taxation | 6.1 |
| M1.13 Taxation - current | -1.9 |
| M1.15 Surplus on ordinary activities after taxation | 4.2 |
| M1.17 Surplus for the year | 4.2 |
| M1.19 Retained surplus for year | <u><u>4.2</u></u> |
| | |
| Per Statutory Accounts | 2006-07 |
| | £m |
| Turnover | 140.9 |
| Cost of sales | (126.8) |
| Administrative expenses | (7.3) |
| Operating profit on ordinary activities before interest | 6.8 |
| Net interest payable | (0.7) |
| Profit on ordinary activities before taxation | 6.1 |
| Taxation | (1.9) |
| Retained profit for the period as stated in statutory accounts | <u><u>4.2</u></u> |
| | |
| Reconciliation to the E Tables | 2006-07 |
| | £m |
| M1.1a Wholesale charge | 126.831 |
| M1.2 Other operating costs | 6.963 |
| M1.3 Depreciation | 0.332 |
| Operating costs per M1 | <u><u>134.126</u></u> |
| | |
| E1.31 Total operating costs water | 49.067 |
| E2.31 Total operating costs wastewater | 85.059 |
| Costs per E tables | <u><u>134.126</u></u> |

Table M2 - Historic Cost Balance Sheet

This table was populated using information directly captured in the General Ledger.

The table below reconciles M2 to the statutory accounts.

| | 2006-07 |
|----------------------------------|-------------------|
| | £m |
| M2.4 Total fixed assets | 1.3 |
| M2.6 Debtors | 66.7 |
| M2.7 Cash at bank and in hand | 11.3 |
| M2.13 Creditors | -8.7 |
| M2.14 Borrowings | -64.5 |
| M2.15 Corporation tax payable | -1.9 |
| M2.27 Net assets employed | <u>4.2</u> |

| | 2006-07 |
|---|-------------------|
| | £m |
| Tangible fixed assets | 1.3 |
| Debtors | 90.8 |
| Cash at bank and in hand | 11.3 |
| Creditors: amounts falling due within one year | (75.1) |
| Provisions for liabilities and charges | (24.1) |
| Net assets as per statutory accounts | <u>4.2</u> |

Table M3 - Historic Cost Balance Sheet: Reconciliation to Statutory Accounts

Profit and Loss

There are no differences between the statutory accounts and the regulatory accounts for the profit and loss account.

Balance Sheet

M3.6 - Debtors

In the statutory accounts the credit note provision (£24.1m) is reported as a provision, whilst in the regulatory accounts it is reported as part of trade debtors, in order to ensure consistency with the information reported in Table M25.

M3.7 - Provisions for Liabilities and Charges

As detailed above, the credit note provision was reported as a provision rather than as part of trade debtors in the statutory accounts.

Table M6 - Cash Flow

This table was populated using information directly captured in the General Ledger.

SWBS inherited £35m of loans from SW as part of the transfer of assets on 1 November 2006. The new borrowings in the year were borrowed directly from SW; these were included as 'bank loans' in M6 in the absence of an alternative.

The table below reconciles Table M6 to the statutory accounts;

| | 2006-07 |
|---|---------------------|
| | £m |
| M6.1 Net cash flow from operating activities | -26.758 |
| M6.2 Interest received | 0.609 |
| M6.3 Interest paid | -0.957 |
| M6.16 Net cash flow before financing | -27.106 |
| M6.18 New bank loans | 39.500 |
| M6.20 Bank loans repayments | -10.000 |
| M6.23 Increase (decrease) in cash and cash equivalents | <u>2.394</u> |

| | 2006-07 |
|---|-------------------|
| | £m |
| Net cash outflow from operating activities | (26.7) |
| Net cash outflow from returns on investment and servicing of finance | (0.4) |
| Net cash outflow before management of liquid resources and financing | (27.1) |
| Net cash inflow from financing | 29.5 |
| Increase in cash as per statutory accounts | <u>2.4</u> |

Table M11 - Working Capital

This table was populated using information directly captured in the General Ledger.

The table below reconciles M11 to M2.

| | |
|---|----------------------|
| M11.1 Stocks | 0.000 |
| M11.3 Trade debtors - non-household | -0.623 |
| M11.5 Measured income accrual | 38.716 |
| M11.6 Prepayments and other short term debtors | 28.632 |
| M11.7 Trade creditors | -0.019 |
| M11.8 Deferred income - customer advance receipts | -0.142 |
| M11.10 Accruals and other creditors | -10.415 |
| M11.11 Total working capital | <u>56.149</u> |
| | |
| M2.6 Debtors | 66.725 |
| M2.13 Creditors | -8.689 |
| M2.15 Corporation tax payable | -1.887 |
| Total working capital as per M2 | <u>56.149</u> |

Table M13 - Reconciliation of Historic Cost Operating Surplus to Net Cash Flow from Operating Activities

This table was populated using information directly captured in the General Ledger.

The table below provides a detailed breakdown of M13.3 - Movement of Working Capital.

| | |
|---|------------------------------|
| Debtor balances at 1 November 06 | 30.619 |
| Creditor balances at 1 November 06 | -6.086 |
| Total working capital at 1 November 06 | 24.533 |
| M11.11 Total working capital at 31 March 07 | 56.149 |
| Movement in working capital | -31.616 |
| Add back non-cash items (closing accruals for interest and tax) | <u>-2.258</u> |
| Total movement in working capital | <u><u>-33.874</u></u> |
| | |
| M13.3 Movement in working capital | <u><u>-33.874</u></u> |

Tables M18W and M18WW - Activity Based Costing: Water / Wastewater Service

Allocation to Water and Wastewater

Costs were allocated to water and wastewater using the same methodology as in Tables E1 and E2.

The detailed commentary on the allocation of costs between water and wastewater provided for the E tables has not been repeated in this document.

The table below reconciles M18W and M18WW to the E tables:

| | 2006-07 |
|---|-----------------------|
| | £m |
| M18.57 Total operating costs water | 49.067 |
| M18.56 Total operating costs wastewater | 85.059 |
| | <u>134.126</u> |
| | |
| E1.31 Total operating costs water | 49.067 |
| E2.31 Total operating costs wastewater | 85.059 |
| | <u>134.126</u> |

Allocation of Costs Between Direct Operations, General and Support and Cost of Regulation

Peoplesoft 8.4, SWBS's General Ledger system, records information in chart fields. Chart fields are the individual fields in the accounting structure that hold financial information. SWBS predominantly uses two main chart fields: account and department ID. The department ID chart field is used to allocate costs to specific areas of the business.

Using the department information held in SWBS's General Ledger, it is possible to separate costs between direct operations, general and support and regulation.

The allocation of costs-to-cost areas is, therefore, based on the information held directly in the General Ledger.

Direct Operations Costs

The costs of all departments that are directly involved in the provision of customer service were allocated to direct costs. The total costs allocated to this area were, therefore, derived directly from information held in the General Ledger. Information on how these costs were allocated to different activities is provided in the next section.

The table below shows all departments directly involved in SWBS operational activities:

- Billing
- Cash Collection
- Contact Centre
- Credit Control
- Head of Customer Experience
- External Debt Recovery Management

IT
Key Customer Management
Marketing

The Head of Customer Experience manages two support functions and five Customer Service departments. His costs were allocated evenly between each team, which resulted in £11k of his costs (30%) being allocated to general and support rather than direct costs.

The IT department's costs are primarily related to software maintenance and support of the customer service applications. These costs have, therefore, been treated as direct costs. All other IT costs have been classed as general and support; these were identified using the account codes in the General Ledger.

General and Support Costs

All support service departments were allocated to general and support costs. These costs were identified directly from the information held in the General Ledger.

In addition to these costs, a small proportion of the Head of Customer Experience's costs were also allocated to general and support, as detailed above. General and support costs also include £90k for IT contractor support, as detailed above.

The costs for Regulation and Procurement are held on one department ID within the General Ledger; therefore, these costs had to be split between support services (procurement) and the cost of regulation. The costs of the staff that work directly in Procurement were allocated to support services, together with 30% of the management costs of the team. The allocation of the management cost was based on an estimate of the proportion of managerial time spent on each activity provided by the team.

The table below shows all support services departments whose costs were classified as general and support:

Corporate Overheads
Finance and Business Performance Reporting
Procurement
Systems Support
Training, Audit, Policy and Procedures

Cost of Regulation

The Regulation department costs were split between general and support and cost of regulation, as explained above.

Allocation of Direct Costs to Activities

In some instances, costs could be allocated to activities using the information held within the General Ledger using the account and department ID. However, for a proportion of the direct costs, we do not capture costs in a way that enables direct allocations of cost to activities.

In this instance, event code information held in the billing system was used to allocate costs to each activity. Event codes are used to record all customer contact and any internal activity on customer accounts.

Each event code was allocated to a WIC activity as illustrated below:

| Event Code | Event Description | WIC Activity |
|-------------------|--------------------------|--------------------------------|
| PPLA | Payment Plan Request | Handle payment plan enquires |
| REFU | Refund Request | Remittance and cash processing |

The departments responsible for each activity were then identified and the costs of each department were then allocated to activities using the activity driver information.

An illustration of this is provided below for one event code

Event Code PPLA: Payment Plan Request

The event code was allocated to the remittance and cash processing activity. The initial contact from the customer will be handled by the Contact Centre team who then pass the task onto the Credit Management team. Clearly there are costs for both teams associated with this event and, therefore, with this activity.

There were 2,281 payment plan requests received in the 5 month period to 31 March 2007. The Credit Management team dealt with 40,167 events in total, so 5.6% of their costs were allocated against payment plan requests, which forms part of the remittance and cash processing activity.

The Contact Centre dealt with 135,430 events in the five months to 31 March 2007, therefore, only 1.6% of their costs were allocated to this event.

M18.11 - Contract Management

Not applicable, as this is a wholesale activity.

M18.12 - Manage Billing Data

Costs from the Contact Centre and the Billing team were allocated to this activity using the event code information held in the billing system. A portion of managerial costs were allocated to this activity on the same basis.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.13 - Generate and Issue Bills

Costs from the Billing department ID were allocated to this activity using the event code information held in the billing system. A portion of managerial costs were allocated to this activity on the same basis.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.14 - Handle Billing Enquiries

Costs from the Contact Centre, the Billing team and Credit Control were allocated to this activity using the event code information held in the billing system.

Managerial costs were allocated to this activity on the same basis.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.15 - Handle Billing Exceptions

Costs from the Billing team were allocated to this activity using the event code information held in the billing system.

A portion of managerial costs were allocated to this activity on the same basis.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.16 - Handle Billing Complaints

Costs from the Billing team were allocated to this activity using the event code information held in the billing system. Managerial costs were allocated to this activity on the same basis.

Costs captured directly in the General Ledger for compensation payments were also allocated to this activity, as these costs arise as a direct consequence of customer complaints.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.17 - Meter Reading

Costs captured directly in the General Ledger for meter reading (performed by SW under SLA) were allocated to this activity.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.18 - Cost of Meter Maintenance and Installation

Not applicable, as this is a wholesale activity.

M18.19 - Handle Metering Enquires

Costs from the Contact Centre and the Billing team were allocated to this activity using the event code information held in the billing system.

A portion of managerial costs were allocated to this activity on the same basis.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.20 - Handle Metering Complaints

Costs from the Contact Centre were allocated to this activity using the event code information held in the billing system.

A portion of managerial costs were allocated to this activity on the same basis.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.21 - Remittance and Cash Processing

Costs from the Contact Centre, the Cash team and Credit Control were allocated to this activity using the event code information held in the billing system.

A portion of managerial costs were allocated to this activity on the same basis.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.22 - Debt Management, Excluding Bad Debt Recovery

Costs from the Contact Centre and Credit Control were allocated to this activity using the event code information held in the billing system.

Managerial costs were allocated to this activity on the same basis.

£18k of costs captured directly in the General Ledger for debt management activities were also allocated to this activity.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.23 - External Debt Recovery

All of the costs captured in the General Ledger for the Third Party Debt Management team and contract were allocated to this activity. In addition, costs from the Credit Control departments and managerial costs were allocated to this activity using the event code information held in the billing system.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.24 - Disconnections

All of the costs captured in the General Ledger for disconnections were allocated to this activity. In addition, an element of costs from the Contact Centre and managerial costs were allocated to this activity using the event code information held in the billing system.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.25 - Handle Payment Plan Enquiries

Costs from the Credit Control department and the Contact Centre were allocated to this activity using the event code information held in the billing system. A portion of managerial costs were allocated to this activity on the same basis.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.26 - Advertising / Marketing

All of the costs captured in the General Ledger for the Marketing team were allocated to this activity.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.27 - Account Management

All of the costs captured in the General Ledger for the Key Customer Management team were allocated to this activity.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.28 - Manage GSS Payments

All of the costs captured in the General Ledger for GSS Payments were allocated to this activity. In addition, an element of costs from the Contact Centre and managerial costs were allocated to this activity using the event code information held in the billing system.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.29 - Handle Customer Operational Calls

All of the costs captured in the General Ledger for operational contacts recharged from SW under SLA were allocated to this activity.

Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.30 - Other Direct Costs

Wholesale charges captured directly in the General Ledger for water and wastewater were classified as other direct costs.

Other direct costs also includes the property and IT related costs for all staff directly involved in customer operations.

The IT application support and software maintenance costs and the insurance costs for the business, recharged from SW, were also classified as other direct costs.

All other direct costs were identified directly from the General Ledger. However, where they were not allocated specifically to water and wastewater, the allocation of water and wastewater, measured and unmeasured, is based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.34 - General and Support Costs

The allocation of total costs to line M18.34 is explained above. Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.37 - Cost of Regulation General and Support Costs

The allocation of total costs to line M18.37 is explained above. Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.40 - Bad Debt Charge

The allocation of total costs to line M18.40 was directly obtained from the information held in the General Ledger. Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

M18.52 - Business Activities Depreciation Charge

The allocation of total costs to line M18.52 was directly obtained from the information held in the General Ledger. Costs were allocated to water and wastewater, measured and unmeasured, based on the number of bills issued. This approach is consistent with the method of cost allocation used in the E tables.

Table M19 - Regulatory Accounts (Historical Cost Accounting) Statement of Total Recognised Gains and Losses

There are no gains and losses, other than the profit for the year.

Table M20 - Analysis of Borrowing by Interest Rate and Date of Maturity (Licensed)

This table was populated using information held in the SWBS Debt Book and was reconciled to the balances held in the General Ledger.

All loans outstanding at 31 March 2007 are due to be repaid by 31 March 2008. Any new loans from this date forward will be borrowed at commercial interest rates.

Table M21 - Taxation Analysis

This table was populated using information directly captured in the General Ledger combined with the information from the SWBS corporation tax return.

M21.7 - Assets to be Included in the General (25%) Pool

Additions in the period totalled £57k.

M21.19 - Opening Pool of Capital Allowances: Asset Life < 25 Years

The Hi Affinity billing system was transferred to SWBS on 1 November 2006 for a NBV of £1.587m

M21.35 - Capital Allowances: Asset Life >=25 Years

Capital allowances were claimed on fixed assets at 25%. As the company had only been trading for 5 months, only 5/12^{ths} of the annual capital allowance was claimed.

The table below illustrates how capital allowances were calculated:

| | |
|---|---------------------|
| Hi Affinity transferred to SWBS at 1 November 06 | 1.587 |
| Capital additions in the year | 0.057 |
| Total | 1.644 |
| Full year capital allowances at 25% | 0.411 |
| 5/12 of full year capital allowances | <u>0.171</u> |
| M 21.34 Capital allowances - asset life <25 years | <u>0.171</u> |

Table M21 reconciles to M1

Table M23 - Interest Analysis

This table was populated using information directly captured in the General Ledger.

Table M21 reconciles to Table M1 as shown:

| | |
|--|----------------------|
| M23.7 Total net interest | <u><u>-0.662</u></u> |
| M1.10 Net interest receivable less payable | <u><u>-0.662</u></u> |

M23.6 - Other Finance Charges

These costs are for bank charges incurred in the period.

Table M24 - Analysis of Primary and Secondary Income (Licensed Activities)

This table was populated primarily using information captured directly in the General Ledger, although some extrapolation was required to allocate sundry income (excluding field troughs) to water or wastewater services.

Table M24 reconciles to Table M1 as shown below:

| | 2006- 07 £m |
|--|----------------------------|
| M24.13 Total turnover - primary income | 140.131 |
| M24.32 Total turnover - other sources | <u>0.779</u> |
| | <u>140.910</u> |
| | |
| M1.1 Turnover | <u>140.910</u> |

M24.15 - Secondary Income Other

This income is for meter changes, meter installations and new connections.

This income is not classified as water or wastewater in the General Ledger, therefore, the income was allocated 32% to water and 62% to wastewater, in proportion to the total number of bills issued per service.

This approach is consistent with the cost allocation method used in populating the E tables.

Table M25 - Bad Debt

This table was populated using information directly captured in the General Ledger.

Table M25 reconciles to Table M11 as shown below;

| | 2006-07 |
|-------------------------------------|----------------------|
| | £m |
| M25.8 Non-household trade debtors | <u>-0.623</u> |
| M11.3 Trade debtors - non-household | <u>-0.623</u> |

M25.1 - Bad Debt Provision in the Year

SWBS inherited a bad debt provision from SW at 1 November of £9.7m. This reduced by £1.1m to £8.6m in the period as detailed below:

| | 2006-07 |
|--------------------------------|----------------------|
| | £m |
| Bad debt charge for the period | 2.083 |
| Bad debt write-off | <u>-3.218</u> |
| Reduction in the period | <u>-1.135</u> |