

## Commentary

### Accounting separation

**1** In order to produce regulatory accounts, and in addition to the accounting structure used for internal management reporting, we have created a separate, regulatory cost structure in our financial system. This means that directly coded water and sewerage operational costs can largely be assigned to the appropriate regulatory service and cost heading. Further re-allocation of costs to service type is required in order to comply with reporting guidelines. Where costs are not directly coded to a specific service, management have assessed the appropriate allocation.

**2** The allocation of support costs to Wholesale is carried out using a central consolidation model. Each support business unit provides a summary of its costs by cost driver in line with RAG 4.04 definitions and business unit management determine the appropriate allocation of costs between services. The allocation between services is reviewed annually to ensure that the basis of allocation is still appropriate.

**3** For Retail reporting, the reporting structure of our customer services business unit is closely aligned to the cost drivers on the retail cost analysis shown in note 2 of the current cost financial statements. The vast majority of costs reported in customer services, and therefore retail, are coded at source with the allocation of costs between household and non-household based either on the cost drivers proposed by Ofwat or through management review of an appropriate allocation. We allocate an appropriate share of all support overheads to the retail function (for example Human Resources, IT and Finance). We review annually the basis of our cost allocation to Retail.

**4** Our accounts have been drawn up in accordance with the accounting separation methodology statement published on our website.

### Upstream services

**5** Our starting point for the assessment of upstream services are our wholesale totals reported in the regulatory accounts

**6** Some costs for upstream services can be readily identified and allocated directly to service, whereas others rely on management estimate or a pro-rata allocation.

**7** Our full upstream services methodology is included in our full accounting separation methodology statement (appendix 9).

# Accounting Separation and Upstream Services Commentary