United Utilities Water Limited
Accounting Methodology Statement
2021/22

United Utilities

Water for the North West

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1. Introduction

The economic regulator of the water sector in England and Wales (Ofwat) requires companies to publish an annual performance report (APR) including the regulatory accounting standards. The APR is designed to provide customers and other stakeholders with a detailed and transparent commentary on our performance. The purpose of this methodology statement is to describe the systems and processes followed by United Utilities Water Limited (UUW, the company) to report disaggregated costs and asset data within the APR, including any changes year on year. More specifically, it covers the cost allocation within the following APR tables for the year ended 31 March 2022:

Section 2: Price review and other segmental reporting
- 2B – Totex analysis – wholesale
- 2C – Cost analysis – retail
- 2D – Historic cost analysis of tangible fixed assets
- 2I – Revenue analysis
- 2O – Historic cost analysis of intangible fixed assets

Section 4: Additional regulatory reporting – service level
- 4D – Totex analysis – water resources and water network+
- 4E – Totex analysis – wastewater network+ and bioresources
- 4J – Base expenditure – water resources and water network+
- 4K – Base expenditure – wastewater network+ and bioresources

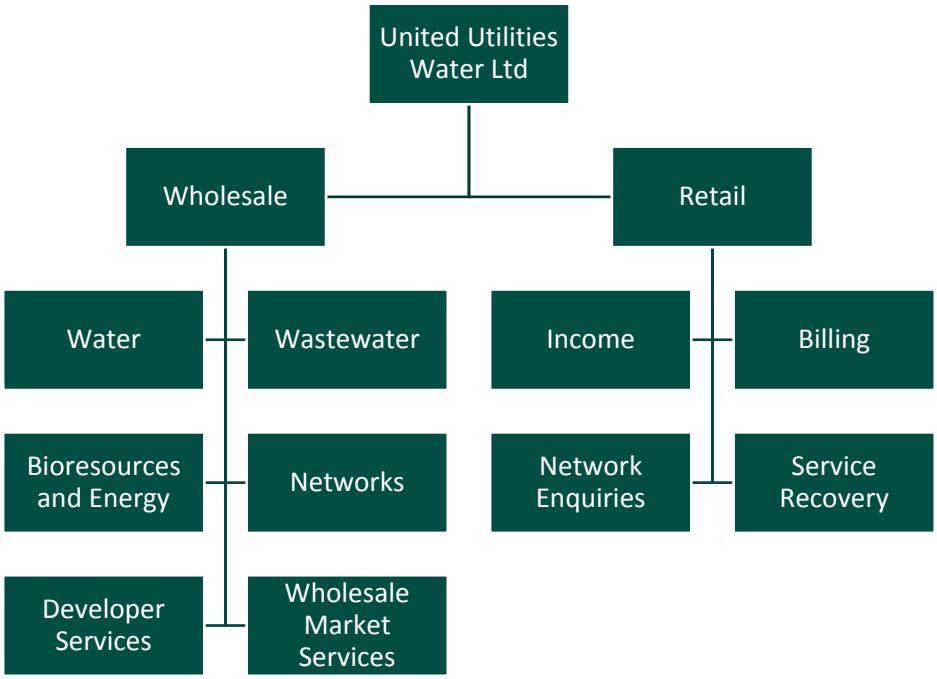
To meet the requirements of RAG 3.13, this methodology statement has been split into the following sections:
- Section 2: High level overview
- Section 3: Cost allocation process for both price controls and upstream services
- Section 4: Cost allocation performed – allocation bases used, with reference to the relevant APR tables.
- Section 5: Variance analysis of operating and capital costs year on year

2. High level overview

This section gives details of the company's structure and systems for producing disaggregated cost and asset data. It outlines the governance processes in place to ensure adherence to, and consistent application of, the RAGs, and also outlines how the company has responded to the cost allocation principles within RAG 2.08.

2.1 Business structure

United Utilities Water operates in two main business areas; wholesale and retail.



UUW's non-household retail operations were transferred to Water Plus Group Limited (Water Plus) in 2016.

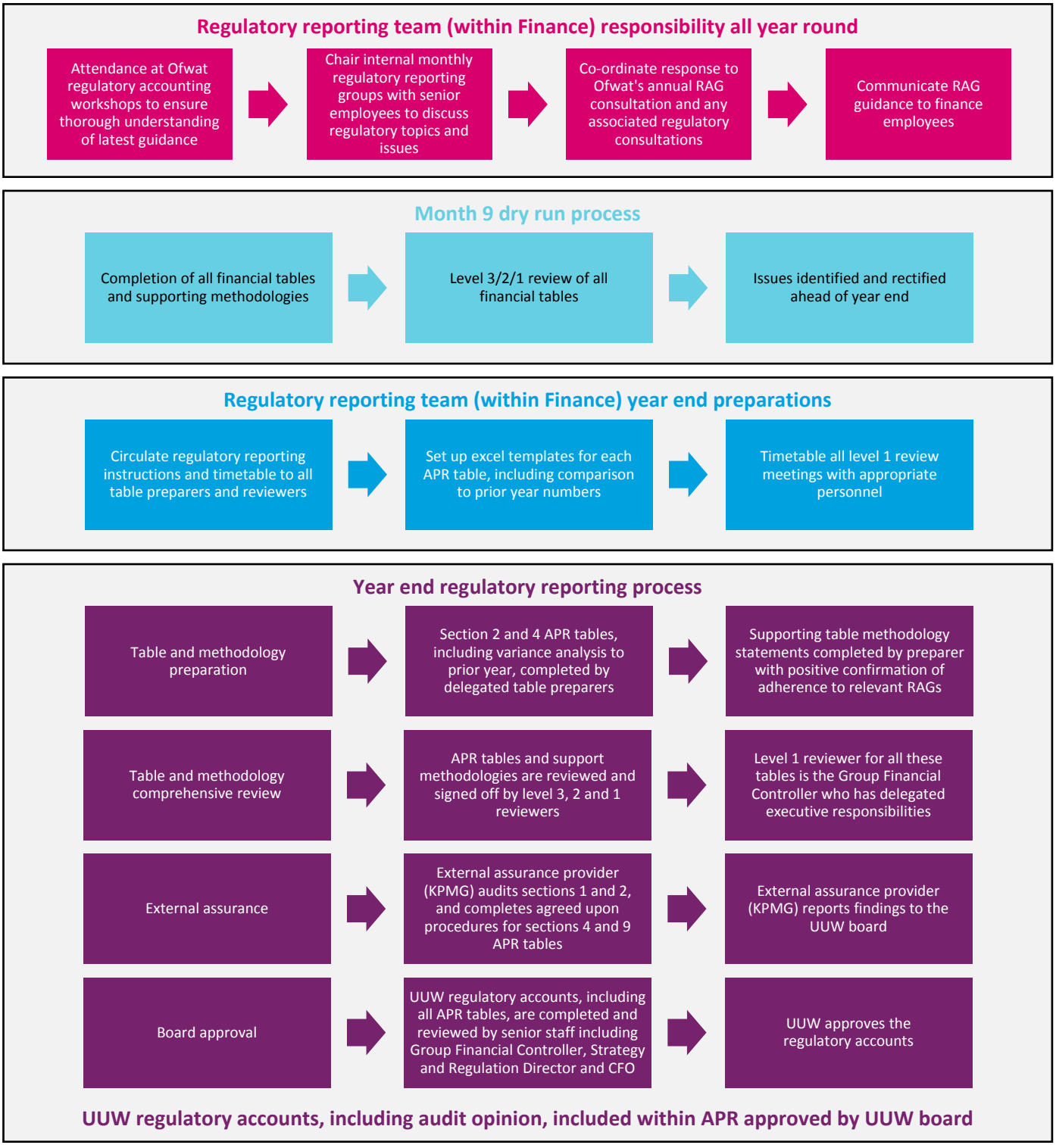
2.2 Outsourced functions

The company has not outsourced complete functions, but the following activities are performed by third parties (primarily in North West England):

- Bill printing and posting
- Retail cash processing
- Debt collection
- Billing and cash collection for wastewater service provision to cross boundary properties
- Capital programme construction
- Network repairs and maintenance
- Facilities management
- Capital programme estimating
- IT system support (partial)

2.3 Governance processes

We have a well-established, robust, governance structure underpinning the production of our APR.



2.4 Cost allocation principles

Within RAG 2.08 'Guideline for classification of costs across the price controls', Ofwat have set out the following principles which should underpin the attribution and allocation of costs. These principles have been adhered to during the preparation of the regulatory accounts.

Principle	RAG 2.08 guidance	UUW response
Transparency	The cost attribution and allocation methods applied to allocate costs within the APR need to be transparent. This means that the costs and revenues apportioned to each service or segment should be clearly identifiable. The cost and revenue drivers used within the system should be clearly explained to enable robust assurance against this guidance.	Transparency is provided by the production of this methodology statement.
Causality	Cost causality requires that costs (and revenues) are attributed or allocated to those activities and services that cause the cost (or revenue) to be incurred. This requires that the attribution or allocation of costs and revenues to activities and services should be performed at as granular a level as possible. Allocating costs in relation to the way resources are consumed provides a means of building up service and product costs. This approach views a business as a series of activities, each of which consumes resources and, therefore, generates costs. An activity based approach should result in the majority of the total costs being attributed or allocated on a meaningful basis. All operating and capital costs must ultimately be attributed or allocated.	Our costs are directly allocated, as far as practically possible, to activities that cause the cost to be incurred. Some costs (for example general and support costs) are more remote from the activities that cause the cost. The methods applied to allocating such costs are described in Section 4 of this methodology statement.
Non-discrimination	Companies should ensure that no undue preference or discrimination is shown by water undertakers and sewerage undertakers in relation to the provision of services by themselves or other service providers (this is consistent with the new duty in section 2 of the Water Industry Act 1991 that has been (or, in relation to Welsh water companies, will be) inserted by section 23 of the Water Act 2014). Therefore the attribution or allocation of costs and revenues should not favour any price control unit or appointed/non-appointed business and it should be possible to demonstrate that internal transfer charges are consistent with the prices charged to external third parties.	Objective cost allocation bases are utilised which meet the requirements of the Ofwat guidance and regulatory accounting principles, without any intention of discrimination.
No cross subsidy between price controls	Price reviews have separate binding price controls. Companies cannot transfer costs between the price control units in setting prices and preparing the APR. The revenue allowance for each price control is determined by the costs specific to that particular price control. Rules on transfer pricing are detailed in RAG 5.	The company has procedures in place to ensure that the relevant individuals are aware of the requirements of RAG 5, and that transactions between price controls are effected and recorded appropriately in compliance with RAG 5.

Principle	RAG 2.08 guidance	UUW response
Objectivity	The cost and revenue attribution criteria need to be objective and should not intend to benefit any price control unit or appointed/non-appointed business. Cost allocation must be fair, reasonable and consistent.	Objective cost allocation bases are utilised which meet the requirements of the Ofwat guidance and regulatory accounting principles, without any intention of benefitting either any price control or the non-appointed business.
Consistency	Costs should be allocated consistently by each company from year to year to ensure: • meaningful comparison of information across the sector and over time, • that regulatory incentives from comparative analysis apply fairly across companies, • to enable monitoring of companies' performance against price control assumptions; and, • any changes to the attribution and allocation methodology from year to year should be clearly justified and documented in the Accounting Separation Methodology Statement.	The company keeps the methodology as consistent as possible from year-to-year, with changes most likely to occur in order to comply with updated Ofwat guidance or utilising enhanced management information to provide improvements in allocation. Significant methodology changes from the prior year are explained in Section 3.7 of this document.
Principal use	Where possible, capital expenditures and associated depreciation should be directly attributed to one of the price control units. Where this is not possible as the asset is used by more than one service, it should be reported in the service of principal use with recharges made to the others services that use the asset reflecting the proportion of the asset used by the other services.	Capital expenditures and depreciation have been attributed or allocated in line with RAG 2.08 requirements, with particular reference to cost allocation to price control unit by principal use where expenditure cannot be directly attributed and recharges made. This is detailed in Section 4.4.

3. Cost allocation process

Cost allocation to price controls is performed in compliance with the Ofwat document 'RAG 2.08 – Guideline for classification of costs across the price controls', as outlined in the previous section. This section summarises the activities and processes to allocate costs and assets to each of the five price controls, and by upstream service. Methodology changes since 2020/21 are detailed within Section 3.7.

3.1 IT systems

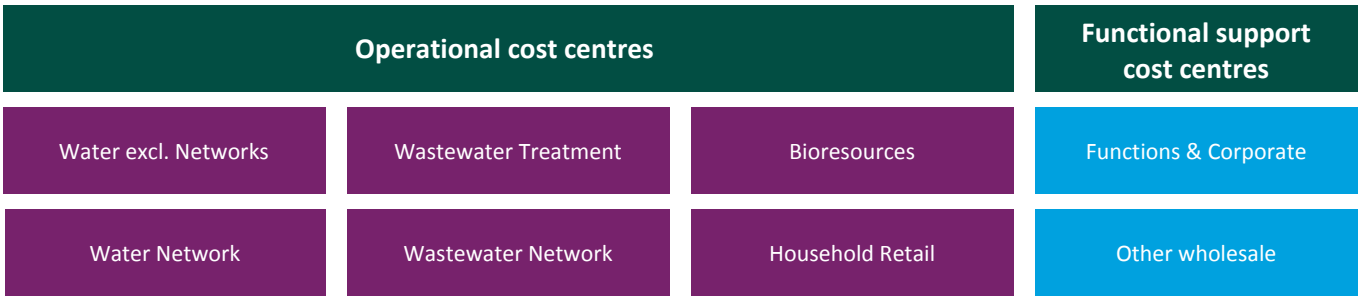
There are three key IT systems used to populate the Section 2 and Section 4 tables of the APR:

- SAP – Core financial accounting system
- CostPerform – Bespoke activity based costing software solution used to allocate operating expenditure to upstream service
- Capital Project Management System (CPMS) – Central repository for the project management of capital expenditure within UUW

3.2 Operating expenditure

The three key steps in allocating operating expenditure to price controls and upstream services are illustrated below.

Step 1: SAP captures data (IFRS basis) at a cost centre level. Costs centres within UUW are structured into the following areas:



The operational cost centres largely align with Ofwat's five price controls for 2020-25, although the water resources and water network plus price controls are both included within the 'Water excluding Networks' operational cost centres. Other wholesale includes business areas which predominately relate to the wholesale business, but have a more overarching remit than the more specific operational cost centres, for example Developer Services. See Section 4.3 for other areas included within Other wholesale. The functional support cost centres are mapped to the five relevant price controls using Cost Perform (see below).

The costs in each area are reviewed by the relevant budget managers.

Step 2: Some adjustments are required to the IFRS position to convert it to a regulatory accounting basis in accordance with RAG 3.13, for example:

- Renewable Obligation Certificate (ROC) income, reported in revenue on an IFRS basis is directed to 'Income treated as negative expense' within the Sludge Treatment upstream service

Some cost reallocations are required from operational cost centres to different price controls and upstream services, for example:

- The cost for the treatment of water sludges at wastewater treatment works are reallocated from the wastewater to the water price control

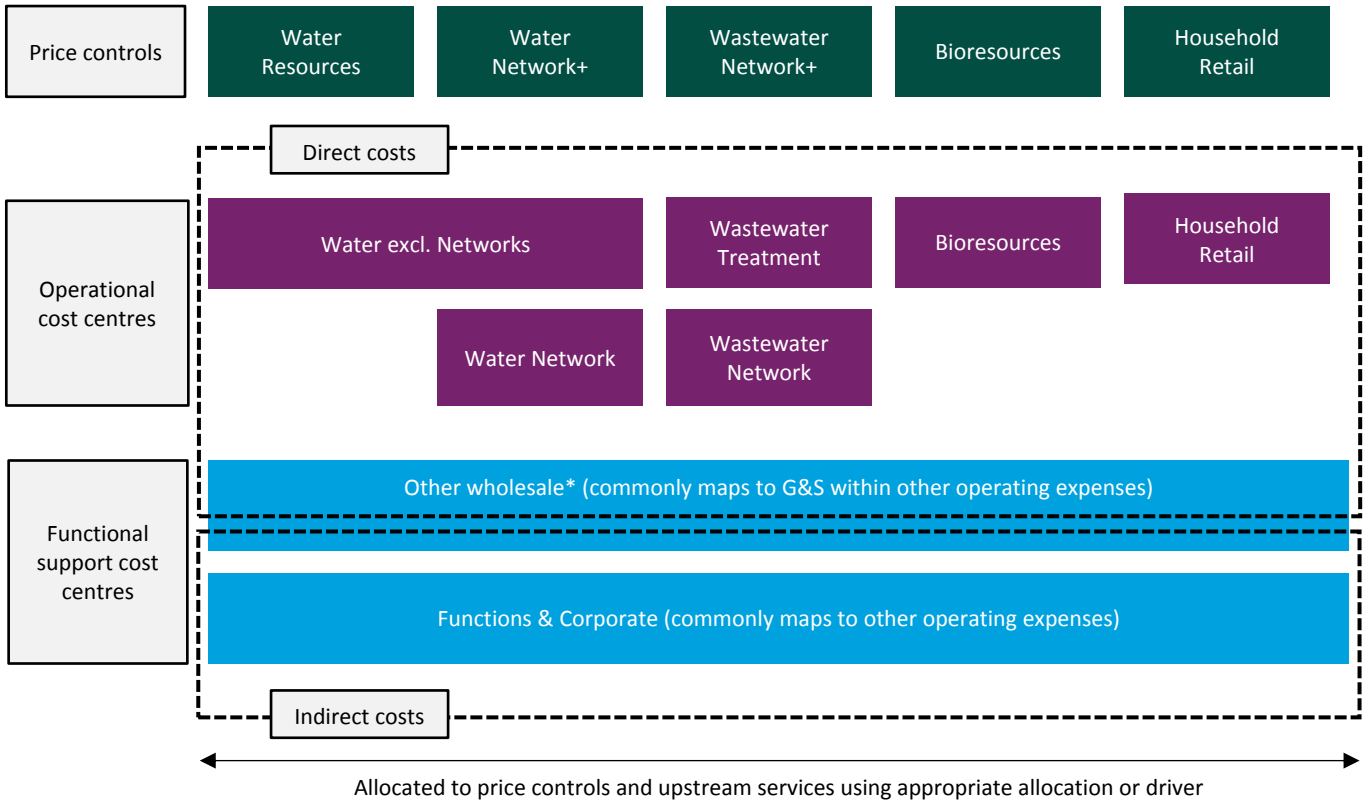
Non-appointed and third party costs recorded within UUW's cost centres are identified, with reference to the RAG 4.10 Appendix 1 Income Categorisation, and mapped accordingly.

Step 3: The CostPerform reporting solution takes the operating expenditure outputs from SAP, plus adjustments required within step 2, groups the costs of each cost centre by expense type e.g. employment, power, materials and consumables, etc. It then applies established allocation rules to attribute costs to price control, and ultimately, to upstream service within wholesale.

Where costs within a cost centre can be directly mapped to a specific upstream service (or price control for retail) and cost line, then no allocations are required and the costs will be mapped directly in CostPerform. Otherwise, costs are allocated across price controls, and to upstream services, using an appropriate driver or allocation rule.

Cost drivers and allocation rules are provided by the operational budget manager or finance representative responsible for those costs and are completed in accordance with RAG 2.08. These are also reviewed by the relevant budget managers and/or finance business partner. See Section 4 for details of how costs are allocated.

This process results in cost centres being principally allocated to the five price controls as below:



*Other wholesale also contains the abstraction charge which is mapped directly to the Abstraction Licence upstream service within Water Resources, making up the vast majority of costs within that upstream service.

A more detailed review of the cost allocation and allocation bases used in year is given within Section 4.

3.3 Capital expenditure

Data from the Capital Project Management System (CPMS) is used to attribute or allocate capital expenditure. CPMS is the central repository for the project management of capital expenditure within UUW. The data within the system includes spend, milestones and regulatory investment categories. Projects can be either assigned to one category or allocated across multiple categories which determine the project allocation across:

- regulatory price controls and/or upstream services;
- investment drivers (Maintenance, Quality, Supply & Demand and Enhanced Levels of Service); and
- asset classifications (e.g. infrastructure, civils and mechanical & electrical)

There is a defined relationship between the categories and the column and row position in the Regulatory Account tables. The relationship is held as a rule within CPMS and allows the analysis and allocation of project and programme level data in a consistent and comparable manner.

3.4 Grants and contributions

Data from SAP and CPMS is used to identify the following characteristics for each income project:

- infrastructure/non-infrastructure/infrastructure renewals (IRE) status;
- income type (connection charges, infrastructure charges, diversions, requisitioned mains, requisitioned sewers, other); and
- regulatory price control and/or upstream service

This information is then used to populate the grants and contributions lines, which is further explained in Section 4.1.

3.5 Fixed assets

The company maintains its fixed asset register in the SAP accounting system. All fixed asset and depreciation information in the APR is presented on an IFRS (historical cost) basis of reporting, adjusted for the removal of capitalisation of borrowing costs under IAS23, as required under RAG 1.09.

Each commissioned asset in the SAP register is assigned to a business unit which determines the price control unit that the asset/depreciation is allocated to in the Annual Performance Report (using the 'principal use' method). The business unit is assigned to the asset on commissioning in conjunction with the project team.

Additional processes are followed to allocate assets under construction, shared assets and year-end adjustments:

- **Fixed Asset Report** – A fixed asset report is run in SAP as at year end. For every commissioned asset it details the movements in the year from opening cost to closing net book value.
- **Assets Under Construction (AUC) allocation** – AUC are posted to summary AUC asset classes in SAP which cannot be used to allocate to asset types. The investment categorisation from CPMS is used to further allocate across price control units/upstream services and asset types.
- **Shared asset reallocation** – Shared assets are allocated to Management & General ("M&G") service areas. These M&G service areas determine the allocation percentages across the direct business units and therefore price control units and upstream services allocations as determined by operational management in conjunction with the Fixed Asset Accounting Team. Further information on these drivers is included in Section 4.4.
- **Year-end adjustments** – Allocations of year-end adjustments (opening and closing journal accruals) are individually reviewed to allocate across the price control and upstream services.

3.6 Revenue

A new requirement for AMP7, RAG 4.10 requires companies to split wholesale revenues by the four wholesale price controls. Our allowed revenue for each price control is set out in our final determination. We set wholesale tariffs each year with the intention to recover our allowed revenue for each price control. Our tariffs are set based on our latest view of forecast customer numbers and consumption. Every year, if each tariff therefore was to be multiplied by the forecast number of customers and consumption on that tariff, we would expect to recover our allowed revenue for each price control. The tariff split between price controls varies depending upon the characteristics of each individual tariff; the split is predominantly based on the underlying costs forecast to be incurred in providing that particular service to customers.

3.7 Methodology changes since 2020/21

A thorough review of operating cost allocations and processes is completed each year to ensure compliance with the RAGs. In the current year, the cost allocation of combined sewers between foul and surface water and highway drainage has been improved to achieve more accurate categorisation. Operating costs, excluding infrastructure renewals expenditure (IRE), are now allocated based on average volumes passing through the network, whereas IRE and capital costs are allocated based on peak volumes given that the assets are sized to provide extra capacity. This moves £12.3m of costs from surface water and highway drainage to foul.

In accordance with the information notice “IN 22/01 Expectations for monopoly company annual performance reporting 2021-22”, we have included a new statutory to regulatory adjustment to reverse the innovation fund provision. In 2020/21, the accrual of £6.2m was recorded in opex, whereas this year only actual spend incurred on innovation projects that we are leading are recorded in tables 4D and 4E.

Principal use of assets recharges are now reported within base operating expenditure in tables 4D and 4E, in accordance with updated RAG 4.10 guidance, and aligned with PR19 models and methodologies. Previously the recharge was recorded within depreciation (outside of totex) in Table 2A. See Section 5.4 for commentary on the movement in recharges compared to the prior year.

Demand-side water efficiency costs are now wholly allocated to wholesale. RAG 2.08 states expenditure should be in retail except where expenditure is to meet wholesale outcomes. We consider that water efficiency measures are designed to the meet the goals of our water resources management plan and protect both the short and long term resource requirements of our water resources. In 2020/21, costs were split £0.9m wholesale and £0.4m retail.

4. Cost allocation performed

The systems and processes used to perform cost allocations have been outlined in the previous sections. This section provides more granular detail of what this process actually means in practice, and with reference to the relevant APR tables.

4.1 Wholesale

The following tables show the cost drivers/allocations used to populate each line of the APR tables for wholesale Water by upstream service (4D) and wholesale Wastewater by upstream service (4E). Cost allocations to upstream services follow the boundary points and assets defined in RAG 4.10. The data in these tables is derived from the underlying financial records as follows:

- Cost Driver A = costs can be mapped directly from a cost centre (or service area for fixed assets) to the relevant upstream service
- Cost Driver B = costs can be mapped directly from a cost centre to water or wastewater and then costs are apportioned to an upstream service using a specific cost driver or in proportion to the level of direct costs
- Cost Driver C = costs are apportioned to water and wastewater using a specific cost driver and then apportioned to an upstream service using another specific cost driver or in proportion to the level of direct costs

The following tables describe how costs are split between Water, Wastewater and Household Retail, and subsequently to upstream services within wholesale, mirroring the operation of the CostPerform reporting solution. In explaining the allocations to individual upstream services, this is also effectively explaining the allocations to the four wholesale price controls reported in the Section 2 tables of the APR (i.e. Water resources, Water network+, Wastewater network+ and Bioresources), since these tables are created by summing the respective upstream service totals within each price control.

Additional Disclosures Required Under RAG 3.13, Appendix 2

Power costs are split between 63% directly coded to a price control and 37% involving some allocation between price controls (the equivalent split in 2020/21 was 61% directly coded, 39% involving some allocation). This split is derived from a complete mapping of every cost line from the SAP system download (described in Section 3.2) which feeds into the power reporting line.

Other operating costs are split between 64% directly coded to a price control and 36% involving some allocation between price controls (the equivalent split in 2020/21 was 67% directly coded, 33% involving some allocation). This split is derived from a complete mapping of every cost line from the SAP system download (described in Section 3.2) for all other operating costs excluding IRE. IRE is based on a direct mapping from the Capital Project Management System (CPMS) system (described in Section 3.3).

The method of disaggregating power costs consumed at sites that cover more than one price controls is described for water and wastewater in the following sections of this document.

4.1.1 Water (APR Tables 4D &4J)

Base operating expenditure (4J)

Expenditure line item	Cost driver	Allocation basis to price control and upstream service
Power	A/B/C	Power cost allocation is allocated on an MPAN meter basis to an upstream service applying asset classifications within RAG 4.10 and where necessary RAG 2.08 Appendix 2. Where this is not possible, for sites that include an element of power in relation to more than one business unit or upstream service the costs are apportioned based on management assessment at a site level. Power for support buildings are apportioned based on floor space. Fuel costs are split based upon the average electricity upstream services percentage split calculated from the above.
Income treated as negative expenditure	A	Direct cost
Bulk supply	B	Direct cost – Allocated to upstream service based on prior year cost allocations from the receiving company as shown in the annual performance report.
Renewals expensed in year (infrastructure)	A	Direct allocation to the business unit based on investment categories assigned to each project in the Capital Project Management System (CPMS), by the project manager.
Renewals expended in year (non-infrastructure)	n/a	Nil operating costs
Other operating expenditure excluding renewals		
– Employment costs	A	• Water network costs – Direct costs are charged to the individual sites and upstream service.
	A/B	• Water treatment works – Direct costs are charged to the individual sites against process level cost centres. These process level cost centres directly map to an upstream service. Where costs cannot be directly allocated to process level they are apportioned pro-rate to the level of directly allocated costs.
– Hired and contracted Services	B	• Water senior leadership and production managers – Cost are apportioned pro-rate to the level of directly allocated costs at Water Network and Water Treatment works.
– Materials and consumables	B	• Other water activities recorded in water profit centre hierarchy – Costs allocated to upstream service based upon the activity of individual teams workload and management estimate where necessary. These costs are not directly allocated to either upstream service or site level.
– Other Direct costs	B/C	• Non G&S costs recorded within the other wholesale profit centre hierarchy (e.g. operational technology, Wholesale market services) – Cost allocated to price control based on assessment of work undertaken or using an appropriate cost driver. Costs allocated to upstream service within water using specific cost driver or in proportion to the level of direct costs.
– General and support (G&S) expenditure	C	Indirect general and support costs are allocated across the relevant upstream service as analysed out in Section 4.3.
– Scientific services	C	Costs are allocated across water and sewerage based upon laboratory test numbers taken relevant to each business unit activity.
– Other business activities	C	8/9ths of the Regulatory costs (including Ofwat licence fees) are allocated to wholesale, 1/9th to retail, in line with Ofwat guidance. This is with the exception of DWI costs directly attributed to the water service. Where not directly allocated, costs are then allocated equally between water and wastewater. Regulation team time is split based on management's estimate of time spent on particular areas. Subsequent allocation to upstream service is done proportional to the level of direct costs for each upstream service.
– Meter maintenance/ installation non capex	A	Direct allocation of costs to wholesale treated water distribution.
– Principal use recharges	C	Based on the allocation of Management and General assets using the most appropriate driver as described in Section 4.4.
– Exceptional items	C	Exceptional items are allocated to price control and upstream service based upon the nature of expenditure and using an appropriate cost driver.
Local authority and cumulo rates	B/C	Rates are split proportionally based on the Gross Modern Equivalent Asset Value (GMEAV) of those assets attracting rates. Rates for support buildings are apportioned based on floor space.
Canal & River Trust abstraction charges/ discharge consents	A	Direct cost
Environmental Agency/ NRW abstraction charges / discharge consents	A	Direct cost
Other abstraction charges / discharge consents	A	Direct cost
Costs associated with Traffic Management Act	C	Cost allocated across Water Network+ and Wastewater Network + primarily based on the number of permits, and to treated water distribution for Water Network + specifically.
Costs associated with lane rental schemes	n/a	Nil costs associated with lane rental schemes
Statutory water softening	n/a	Nil costs associated with statutory water softening.
Base operating expenditure	n/a	Sum of above

Water Resources and Water Network+ totex analysis (4D)

Total operating expenditure

Expenditure line item	Cost driver	Allocation basis to price control and upstream service
Base operating expenditure	n/a	Detailed within Section 4.1.1 above.
Enhancement operating expenditure	n/a	Costs allocated on the same basis as those in base operating expenditure. Includes actual spend incurred on innovation fund projects allocated to price control based upon the natue of the project.
Developer services operating expenditure	A	Directly allocated to Treated Water Distribution (TWD) upstream service.
Third party services	A	Costs are directly allocated to upstream service based upon the nature of expenditure.
Total operating expenditure	n/a	Sum of above

Grants and contributions – operating expenditure

Expenditure line item	Cost driver	Allocation basis to price control and upstream service
Grants and contributions – operating expenditure	A	Direct allocation to upstream service based on the Capital Project Management System (CPMS).

Capital expenditure

Expenditure line item	Cost driver	Allocation basis to price control and upstream service
Maintaining long term capability of the assets – infrastructure	n/a	Nil capital expenditure, all expensed.
Maintaining long term capability of the assets – non infrastructure	A/C	Direct attribution to price control based on the Capital Project Management System (CPMS). Price control of principal use is used where assets cannot be directly attributed with recharges made to other price control services as appropriate to reflect the proportion of the asset used.
Base capital expenditure	n/a	Sum of above
Enhancement capital expenditure	n/a	Costs allocated on the same basis as those in base capital expenditure.
Developer services capital expenditure	A	Direct attribution to upstream service based on the Capital Project Management System (CPMS).
Third party services	A	Direct attribution to upstream service based on the Capital Project Management System (CPMS).
Total gross capex expenditure	n/a	Sum of above

Grants and contributions – capital expenditure

Expenditure line item	Cost driver	Allocation basis to price control and upstream service
Grants and contributions – capital expenditure	A	Direct allocation to upstream service based on the Capital Project Management System (CPMS).

Cash expenditure

Expenditure line item	Cost driver	Allocation basis to price control and upstream service
Pension deficit recovery payments	n/a	Nil pension deficit repair contributions. As of March 2022, the expectation is that the pension schemes will be fully funded on a low dependency basis without additional contributions from the company.
Other cash items	n/a	Nil other cash items.

4.1.2 Wastewater (APR Tables 4E &4K)

Base operating expenditure (4K)

Expenditure line item	Cost driver	Allocation basis to price control and upstream service
Power	A/B/C	• Wastewater – Direct costs at co-located sites are allocated based on either sub metering (where available) or engineering's assessment of power usage by asset, which are then apportioned across upstream services. All other costs are allocated directly to the individual sites. Power for support buildings are apportioned based on floor space. An adjustment is made to give the full benefit of CHP generation to sludge treatment. • Liquor treatment – a proportion of the sewage treatment business unit power costs were classified as liquor treatment based on engineering assessments at each co-located site. • Sewage collection – allocated to upstream service based on GMEAV of network assets.
Income treated as negative expenditure	A	Direct cost
Bulk supply	A	Direct cost
Renewals expensed in year (infrastructure)	A	Direct allocation to the business unit based on investment categories assigned to each project by the project manager in the Capital Project Management System (CPMS).
Renewals expended in year (non-infrastructure)	n/a	Nil operating costs
Other operating expenditure excluding renewals		
– Employment costs	B	• Wastewater treatment works (Co-located sites) - Direct costs are charged to the individual sites against process level cost centres. These process level cost centres directly map to an upstream service. Where costs cannot be directly allocated to process level they are apportioned pro-rate to the level of directly allocated costs.
– Hired and contracted Services	A/B	• Wastewater treatment works (Sewage Treatment only) - Direct costs are charged to the individual sites and upstream service. Where costs cannot be directly allocated to site they are apportioned pro-rate to the level of directly allocated costs.
– Materials and consumables – Other Direct costs	B	• Sewage collection – Direct costs are allocated based on number of incidents in the Wastewater Incident Recording System database which identifies if they relate to Foul, Surface Water Highway Drainage (SWHD) or combined. SWHD is split between SW and HD based on the split of the total UU area which drains to UU sewers between SW and HD, based on information from UU Geographical Information Systems (GIS) for land use / type and hydrology models for the area drained.
	B	• Wastewater senior leadership, area business managers and production managers – Costs are apportioned pro-rate to the level of directly allocated costs at Sewerage treatment works and Co-located sites.
	B	• Other wastewater activities within wastewater profit centre hierarchy – Costs are allocated to upstream services based on the activity of the individual teams workload and management estimate where necessary. These costs are not directly allocated to individual Sewerage treatment works.
	B/C	• Non-G&S costs recorded within the other wholesale profit centre hierarchy (e.g. operational technology, Wholesale market services) – Cost allocated to price control based on assessment of work undertaken or using an appropriate cost driver. Costs allocated to upstream service within wastewater using specific cost driver or in proportion to the level of direct costs.
– General and support expenditure	C	Indirect general and support costs are allocated across the relevant upstream service as analysed out in Section 4.3.
– Scientific services	C	Costs are allocated across water and sewerage based upon laboratory test numbers taken relevant to each business unit activity.
– Other business activities	C	8/9ths of the Regulatory costs (including Ofwat licence fees) are allocated to wholesale, 1/9th to retail, in line with Ofwat guidance. This is with the exception of DWI costs directly attributed to the water service. Where not directly allocated, costs are then allocated equally between water and wastewater. Regulation team time is split based on management's estimate of time spent on particular areas. Subsequent allocation to upstream service is done proportional to the level of direct costs for each upstream service.
– Support for trade effluent compliance	B	Direct costs are charged to specific cost centres and allocated to upstream services based on the activity of the individual teams workload and management estimate where necessary.
– Principal use recharges	C	Based on the allocation of Management and General assets using the most appropriate driver as described in Section 4.4.
– Exceptional items	C	Exceptional items are allocated to price control and upstream service based upon the nature of expenditure and using an appropriate cost driver.
Local authority and cumulo rates	B/C	Rates are split proportionally based on the Gross Modern Equivalent Asset Value (GMEAV) of those assets attracting rates. Rates for support buildings are apportioned based on floor space.
Canal & River Trust discharge consents	B	Canals & Rivers trust payment allocated based on the split of non marine outfalls.
Environment Agency / NRW discharge consents	A	Direct from a cost centre to an upstream service.
Other discharge consents	A	Direct from a cost centre to an upstream service.

Costs associated with Traffic Management Act	C	Cost allocated across Water Network+ and Wastewater Network+ primarily based on the number of permits, and to upstream within Wastewater Network+ based on a specific cost driver.
Costs associated with lane rental schemes	n/a	Nil costs associated with lane rental schemes
Costs associated with Industrial Emissions Directive	A	Costs are specifically identifiable at site level, and allocated to upstream service on that basis.
Base operating expenditure	n/a	Sum of above

Note that we have continued to use the same methodology as AMP6 for the reporting cost of imported sludge liquors in table 4K (applying marginal cost approach). Separately, we have applied Jacob's methodology for the shadow reporting of the sludge liquor recharge in APR table 8C in line with RAG 4.10 guidance.

Wastewater Network+ and Bioresources totex analysis (4E)

Total operating expenditure

Expenditure line item	Cost driver	Allocation basis to price control and upstream service
Base operating expenditure	n/a	Detailed in Section 4.1.2 above.
Enhancement operating expenditure	n/a	Costs allocated on the same basis as those in base operating expenditure. Includes actual spend incurred on innovation fund projects allocated to price control based upon the natue of the project.
Developer services operating expenditure	B	Directly allocated to sewerage collection and then to upstream by the appropriate driver.
Third party services	A	Costs relating to the repair of damages caused to the wastewater network (Sewage Collection) by a third party. Costs offset by income from 3rd party damages.
Total Operating expenditure	n/a	Sum of above

Grants and contributions – operating expenditure

Expenditure line item	Cost driver	Allocation basis to price control and upstream service
Grants and contributions – operating expenditure	A/B	Income directly allocated to sewerage collection and then by upstream service by GMEAV.

Capital expenditure

Expenditure line item	Cost driver	Allocation basis to price control and upstream service
Maintaining long term capability of the assets – infrastructure	n/a	Nil capital expenditure, all expensed.
Maintaining long term capability of the assets – non infrastructure	A/C	Direct attribution to price control based on the Capital Project Management System (CPMS). Price control of principal use is used where assets cannot be directly attributed with recharges made to other price control services as appropriate to reflect the proportion of the asset used.
Base capital expenditure	n/a	Sum of above
Enhancement capital expenditure	n/a	Costs allocated on the same basis as those in base capital expenditure.
Developer services capital expenditure	A	Direct attribution to upstream service based on the Capital Project Management System (CPMS).
Third party services	A	Direct attribution to upstream service based on the Capital Project Management System (CPMS).
Total gross capex expenditure	n/a	Sum of above

Grants and contributions – capital expenditure

Expenditure line item	Cost driver	Allocation basis to price control and upstream service
Grants and contributions – capital expenditure	A/B	Directly allocated to sewerage collection and then by upstream service by GMEAV.

Cash expenditure

Expenditure line item	Cost driver	Allocation basis to price control and upstream service
Pension deficit recover payments	n/a	Nil pension deficit repair contributions. As of March 2022, the expectation is that the pension schemes will be fully funded on a low dependency basis without additional contributions from the company.
Other cash items	n/a	Nil other cash items.

4.2 Household Retail

Operating expenditure (APR Table 2C)

The below table shows how costs are attributed to Household Retail operating cost lines which form the basis for APR table 2C. As the below table shows, the majority of costs are directly mapped from specific cost centres within the household retail cost centre hierarchy to a specific cost line in accordance with line definitions specified in RAG 4.10.

Certain costs, such investigatory visits, are mapped from wholesale cost centres, where the costs are initially recorded. Other centrally recorded costs, such as general and support expenditure, have an apportionment to Household Retail. These mappings and apportionments are completed in accordance with cost categorisation per price control, as specified in RAG 2.08.

Expenditure line item	Allocation basis
Customer services:	
– Billing	Largely directly attributed within Household cost centre hierarchy. In addition, allocations of: • Internally generated correspondence based on FTE • Local authority commission based on associated direct costs • Postage, printing and cash management costs based on cost type and volumes of bill types/letters to correct activity line • Senior leadership team costs per individual based on associated direct costs of activities they are involved in
– Payment handling, remittance and cash handling	Largely directly attributed within household cost centre hierarchy plus an allocation of: local authority commission; postage, printing and cash management costs; and senior leadership team costs (allocation basis for all these as described above).
– Vulnerable customer schemes	Vast majority directly attributed within household cost centre hierarchy plus an allocation of senior leadership team costs based on associated direct costs of activities they are involved in.
– Non-network customer enquiries and complaints	Vast majority directly attributed within household cost centre hierarchy plus an allocation of senior leadership team costs based on associated direct costs of activities they are involved in less internal generated correspondence allocation moved to Billing.
– Network customer enquiries and complaints	Vast majority directly attributed within household cost centre hierarchy plus an allocation of senior leadership team costs based on associated direct costs of activities they are involved in.
– Investigatory visits	Direct cost transfer of activity related costs from wholesale water and wastewater to household retail.
Debt management	Largely directly attributed within household cost centre hierarchy plus an allocation of: local authority commission; postage, printing and cash management costs; and senior leadership team costs (allocation basis for all these as described above).
Doubtful debts	Directly attributed within household cost centre hierarchy plus an IFRS to regulatory accounts adjustment for bad debt associated with revenue recognition.
Meter reading	Directly attributed within household cost centre hierarchy, plus an allocation of senior leadership team costs.
Service to developers	Nil costs.
Other operating expenditure	
– Demand side water efficiency initiatives	Nil cost. All expenditure recorded in wholesale as incurred to meet wholesale outcomes.
– Customer side leaks	Nil costs – fully funded by wholesale.
– General and support expenditure	There are no direct general and support costs within the household price control. Indirect general and support costs are allocated across the relevant price controls as shown in Section 4.3.
– Other business activities	Where not directly attributable, 8/9ths of the regulatory costs (including Ofwat licence fees) are allocated to wholesale, 1/9th to household retail, in line with Ofwat guidance. Regulation team time is split based on management's estimate of time spent on particular areas.

– Exceptional items	Price control exceptional items are attributed to water, sewerage or retail household. If the exceptional item relates to functional support, the cost is apportioned across water, wastewater and retail household using an appropriate driver.
– Other direct costs	Direct mapping from Household cost centres less specific management employment costs which are allocated to other lines.
Local authority and Cumulo rates	Rates for sites specifically used by retail household are directly attributed. Shared central office rates allocated based on floor space occupied.
Depreciation and amortisation	100% attributable to household retail where price control of principal use, as per service area field in the SAP fixed asset register.
Recharges and income from wholesale assets	100% attributable to household retail where price control of principal use, as per service area field in the SAP fixed asset register.
Third party services operating expenditure	Nil costs.
Pension deficit repair costs	Nil pension deficit repair contributions. As of March 2022, the expectation is that the pension schemes will be fully funded on a low dependency basis without additional contributions from the company.
Debt written off	Derived from bad debt control account.
Capital expenditure	100% attributable to household retail as per business unit asset commissioned to within SAP fixed asset register.

Billing and collection

The company outsources a small amount of debt collection where the risk is transferred to third parties. In 2021/22 the outsourced amount equated to 0.4% of the total 2021/22 appointed revenue.

The company does not issue bills addressed to “the occupier”.

Where a customer has vacated a property, leaving amounts unpaid, the UUW policy is that the customer will be charged up to the date of the change of tenancy. This debt is then placed with debt collection agencies for trace and collection. If new information is obtained by the agencies, advising us of a more accurate date of vacation, the account will be amended accordingly. If debt collection is ultimately unsuccessful, the debt will subsequently be written off.

Bad debt is written off when all economically viable efforts to recover outstanding amounts have been fully exhausted or, alternatively, when the write-off of such amounts forms part of customer rehabilitation processes (subject to acceptance criteria and customer “matching” payments). The company’s bad debt write-off policy has remained unchanged and has been consistently applied in the current year compared with the previous year.

A new requirement for AMP7, RAG 4.10 requires companies to split wholesale revenues by the four wholesale price controls. Our allowed revenue for each price control is set out in our final determination. We set wholesale tariffs each year with the intention to recover our allowed revenue for each price control. Our tariffs are set based on our latest view of forecast customer numbers and consumption. Every year, if each tariff therefore was to be multiplied by the forecast number of customers and consumption on that tariff, we would expect to recover our allowed revenue for each price control. The tariff split between price controls varies depending upon the characteristics of each individual tariff; the split is predominantly based on the underlying costs forecast to be incurred in providing that particular service to customers.

4.3 General and Support expenditure

General & Support (G&S) costs are all recorded within UUW’s functional support cost centres, split by ‘Functions & Corporate’ and ‘Other wholesale’. CostPerform apportions these G&S costs across the five relevant price controls; water resources, water network+, wastewater resources, bioresources and household retail price controls, in accordance with RAG 2.08 cost classification guidelines, and subsequently to upstream service within the wholesale price controls.

The tables below show the basis of allocation per cost type along with the resulting %’s by price control. Full-Time Equivalents (FTEs), including all full-time staff and contractors/temporary staff directly employed, is the most commonly used cost driver.

Functions and corporate profit centres

Expenditure line item	Allocation to price control and subsequent upstream service (where wholesale)	Water Res	Water Net+	WW Net+	Biores-ources	HH Retail	Non-app
Finance	Costs in relation to treasury and tax are allocated based on the regulatory capital spend profile for water, wastewater and household retail. Remaining costs split by team allocated by management assessment of most appropriate split/driver (predominantly FTE). Upstream service allocation pro-rate to the level of direct employment costs with the exception of tax and treasury which are split pro-rate to total direct costs.	3.2%	36.2%	37.7%	8.3%	13.9%	0.7%
HR	Costs allocated to price control using default FTE driver. Upstream service allocation pro-rate to direct employment costs.	2.8%	35.8%	35.3%	8.9%	16.4%	0.8%
Learning & Development	Allocation to price control based on a management assessment of time spent. Upstream service allocation pro-rate to direct employment costs.	2.7%	35.7%	35.3%	8.9%	17.4%	0.0%
General Counsel	Directly attributable to price control where possible. Remaining costs allocated to price control by FTE. Upstream service allocation pro-rate to direct employment costs	2.6%	34.1%	33.6%	8.5%	20.4%	0.8%
Corporate Affairs	Costs allocated to price control using default FTE driver. Upstream service allocation pro-rate to direct employment costs.	2.8%	35.8%	35.3%	8.9%	16.4%	0.8%
Commercial	Costs allocated to price control primarily using default FTE driver. Upstream service allocation pro-rate to direct employment costs.	3.0%	36.7%	36.0%	8.6%	15.0%	0.7%
Executive directors remuneration	Allocated to price control based on a management estimate of time spent. Upstream service allocation pro-rate to total direct costs.	4.2%	32.0%	47.8%	5.6%	10.0%	0.4%
Non-executive directors remuneration	Allocated to price control based on a management estimate of time spent. Upstream service allocation pro-rate to direct employment costs.	4.2%	32.0%	47.8%	5.6%	10.0%	0.4%
Reward and pensions	Allocated to price control either based on an ongoing number of pensions members or FTE by price control. Upstream service allocation pro-rate to direct employment costs.	2.8%	35.9%	35.2%	8.9%	16.4%	0.8%
Other central costs	Allocated direct to price control where possible. All remaining costs are allocated based on the proportion of FTEs. Upstream service allocation pro-rate to total direct costs or to the level of direct employment costs, depending on cost type.	3.1%	40.3%	39.3%	9.9%	6.9%	0.5%

Other wholesale profit centres

Expenditure line item	Allocation to price control and subsequent upstream service (where wholesale)	Water Res	Water Net+	WW Net+	Biores-ources	HH Retail	Non-app
Fleet management costs	Allocated to price control and upstream service based on fleet servicing cost breakdown.	3.4%	29.3%	31.1%	33.7%	2.1%	0.4%
Facilities management and Accom.	Allocated to business area based on floor space occupied. Other wholesale business area subsequent price control and upstream service allocations follow cost allocations each sub-area.	7.4%	31.6%	31.0%	11.3%	17.3%	1.4%
Grounds maintenance	Vast majority of costs are directly attributed to specific water/wastewater sites. Where not directly attributable, allocated pro-rate to the level of employment costs for each upstream service.	0.0%	50.4%	44.6%	5.0%	0.0%	0.0%
Insurance	Claim costs directly attributed where possible. Insurance premium costs allocated using cost drivers reflective of the basis of the insurance charge per area e.g.: - Asset values used for property insurance - Turnover used for Public Liability and Professional Indemnity insurance Costs not directly attributable to an upstream service are subsequently allocated by total direct costs.	7.6%	64.7%	24.3%	2.4%	1.0%	0.0%
Innovation	Existing innovation costs within UUW, and not those incurred under the PR19 Ofwat Innovation Competition. Allocated to price control based on an assessment of the portfolio of projects in the year. Upstream service allocation pro-rate to total direct costs.	13.2%	28.5%	35.0%	23.3%	0.0%	0.0%
IT costs	IT software support costs are directly allocated where possible. Where span more than one area allocated based on the most appropriate driver for each system e.g. FTE, capital spend. Employment costs and other IT costs are allocated by FTE. Subsequent upstream service allocations pro-rate to direct employment costs.	1.7%	41.9%	39.5%	5.1%	11.2%	0.6%

Asset Management	Directly attributed where possible. Otherwise allocated based on management assessment using the most appropriate driver. General costs most commonly split by reference to FTEs or capital expenditure. Where not directly attributed, allocated to upstream service pro-rate to employment costs or total direct costs depending on the nature of the costs.	30.4%	27.6%	34.9%	7.1%	0.0%	0.0%
Remaining indirect other wholesale costs e.g. legal, tech support		7.8%	39.2%	34.9%	6.2%	6.8%	5.1%

4.4 Fixed assets

Allocation of tangible and intangible fixed assets between price controls (Table 2D and Table 2O)

All fixed assets recorded in UUW's SAP register are allocated to price control, as defined in RAG 4.10. All mappings are direct to price control, with the exception of Management & General (M&G) assets, for which the mapping is described below.

Management and General assets

In accordance with RAG 2.08, where an asset is utilised in more than one price control, the asset and its associated depreciation is recorded in the price control of principal use.

As at 31 March 2022, there are approximately 125 live M&G allocations which require an assessment, based on the most appropriate driver, to identify percentage allocations which determine the price control of principal use. Examples of these allocations are as follows:

Service area	Key assets	Drivers
Head office allocation	Head office buildings	Floor space occupation
Corporate systems	SAP system/Workforce Management systems	Number and type of licence/users
Billing systems	Alto billing system	System utilisation
Capital/Project related assets	Project/Investment/Treasury/Tax systems	Total AMP capex
IT assets used by all employees	Microsoft, printer, internet, video conferencing	FTE allocation
IT assets supporting all systems	Infrastructure, servers, data centre, IT networks	Weighted average based on the specifically allocated MG codes

Where the principal use changes during the year, to ensure consistency of reporting, we will continue to record the shared asset as being 'owned' by the original 'principal use' price control unit for the AMP period rather than transferring these assets across price controls.

Overall c.13% of depreciation relates to assets used by more than one price control (all M&G assets). This depreciation is charged on a principal use basis to the following price controls:

Price Control	Water Resources	Water Network+	Wastewater Network+	Bioresources	Retail Household	Total
Depreciation (%)	-	21.6%	72.2%	2.1%	4.1%	**100.0%**
Depreciation (£m)	-	11.1	37.2	1.1	2.1	**51.5**

Principal use recharge impact to price control for use of fixed assets (Table 2A)

As noted above, the depreciation charge for each asset is recorded in the price control of principal use. Separately, APR table 2A (Segmental income statement) also shows principal use recharges impact to each price control for the shared use of that asset. In accordance with RAG 4.10 and the revised proforma tables published by Ofwat in November 2021, the principal use recharges are now included in base operating expenditure within the detailed cost tables (4D, 4E, 4J and 4K), and disclosed on line 4 'PU opex recharge' of table 2A. The recharge amount per asset is equal to the amount of depreciation which would have been recorded by that price control on a proportional allocation basis. These are the same allocation percentages used to determine the price control of principal use as detailed above.

See Section 5.4 for commentary on the movement in recharges compared to the prior year.

4.5 Planned improvements for future years

UUW will continue to make further enhancements to its cost allocation processes in the future and the methodology for preparing these tables will be reviewed again as part of Regulatory Accounting Guidelines published for 2022/23.

There is an ongoing exercise to increasingly book more costs to site level cost centres in SAP, to reduce proportional allocations required.

Our continued participation in Ofwat's Regulatory Accounts Working Group may also help us to identify methodologies or allocation methods which are an improvement or which provide greater consistency across water companies.

5. Commentary on cost variances 2021/22

5.1 Wholesale Water

Operating expenditure

Wholesale Water year on year movements in operating expenditure (£m)	Water Resources	Water Network+				Water Services Total
		Raw water transport	Raw water storage	Water treatment	Treated water distribution	
RR21 total operating expenditure	**61.5**	**13.4**	**1.1**	**90.7**	**210.0**	**376.8**
Power price increases	1.0	0.7	0.0	3.0	1.9	**6.6**
Power volume movements	0.7	0.1	0.0	0.1	0.7	**1.5**
Increased infrastructure renewal expenditure to deliver Impounding Reservoir projects (water resources) and mains cleaning activity (treated water distribution)	5.1	-0.3	0.0	0.0	3.0	**7.9**
Increase in unit cost of chemicals	0.0	0.0	0.0	1.1	0.4	**1.5**
Water resources incidents in FY22	0.6	0.0	0.0	0.3	0.7	**1.7**
Expenditure to meet improved levels of customer service and leakage	0.0	0.0	0.0	-0.1	1.4	**1.3**
Early removal of solar array to facilitate capital programme in FY21	0.0	0.0	0.0	-1.5	-1.2	**-2.7**
Wholesale market services - Increase in cost due to Vacancy/Gap sites	0.2	0.1	0.0	0.4	0.4	**1.1**
Water efficiency - engagement to influence customer behaviour	0.1	0.1	0.0	0.5	0.4	**1.0**
Change in mix of provisions and insurance	-1.5	0.0	0.0	-0.1	3.2	**1.7**
Software as a service (previously accounted for within capex)	0.0	0.0	0.0	0.1	2.6	**2.7**
Principal use recharges (previously reported in depreciation)	0.2	2.2	0.0	9.3	0.4	**12.2**
Enhancement - reversal of the innovation fund provision, offset by increased spend to meet lead standards	0.2	-0.2	0.0	-1.0	2.0	**1.0**
Other year on year movements	0.5	0.7	0.2	0.7	-0.7	**1.4**
RR22 total operating expenditure	**68.7**	**16.9**	**1.3**	**103.6**	**225.2**	**415.7**

Capital expenditure

	Water resources		Water Network+				Total
Line description	**Abstraction licences**	**Raw water abstraction**	**Raw water transport**	**Raw water storage**	**Water treatment**	**Treated water distribution**	
2020/21 total capital expenditure	**0.0**	**11.3**	**3.6**	**0.0**	**121.0**	**119.1**	**255.0**
Base variance	0.0	0.0	0.1	0.0	-29.6	12.7	-16.8
Enhancement variance	0.0	1.7	10.2	0.0	-22.1	5.5	-4.8
Developer services variance	0.0	0.1	0.0	0.0	0.0	-1.0	-0.9
2021/22 total capital expenditure	**0.0**	**13.1**	**13.9**	**0.0**	**69.3**	**136.3**	**232.6**
Movement £m	**0.0**	**1.8**	**10.3**	**0.0**	**-51.7**	**17.2**	**-22.4**
Movement %	**n/a**	**16%**	**74%**	**n/a**	**-75%**	**13%**	**-9%**

In general, capital expenditure varies from year due to the different mix and levels of maturity of projects being delivered. As such there are multiple movements increasing and decreasing expenditure each year. The below explanations detail the major reasons for growth or reductions in expenditure, however there are multiple other movements that offset each other.

The Raw water abstraction unit saw increases in enhancement costs in the reported year primarily due to increases in expenditure on the Eels Regulations programme (£1.7m).

The increase in raw water transport unit can be mainly attributed to expenditure in the year on the Alston Spade Mill project (£11.9m).

The Water treatment unit saw a decrease in base expenditure of £29.6m, significant contributions to this is reduced expenditure at Oswestry water treatment works (-£20m), and a reduction in expenditure to resolve dry weather event risks (-£6m). There was a further £22.1m reduction in enhancement expenditure in this business unit, this includes reduced expenditure as part of the West Cumbria project (-£11.7m), the enhancement component of the Oswestry project (-£7.7m) and a reduction in SEMD activity in the year (-£4.3m).

The increases observed in the base expenditure for the treated water distribution unit are primarily due to increased expenditure on the Service Reservoir programme (£11m). Enhancement expenditure has seen a net increase in expenditure of £5.5m, however there are a number of increases and decreases contributing to this, including increased investment in West Cumbria (£26m), Free Meter Optants (£2.4m), partially offset by less expenditure on resilience projects (-£26m) including at Hallbank and HARP.

5.2 Wholesale Wastewater

Operating expenditure

Wholesale Wastewater year on year movements in operating expenditure (£m)	Sewage collection			Sewage treatment		Bioresources			Waste-water Services Total
	Foul	Surface water drainage	Highway drainage	Sewage treatment and disposal	Imported sludge liquor treatment	Sludge trans-port	Sludge treatment	Sludge disposal	
RR21 total operating expenditure	**46.0**	**46.5**	**18.6**	**144.1**	**2.5**	**9.7**	**21.5**	**8.5**	**283.5**
Increased power price	1.8	0.9	0.3	8.4	0.0	0.0	-1.6	0.0	**9.7**
Power volume movements	-0.2	-0.1	0.0	-0.7	0.0	0.0	-0.6	0.0	**-1.7**
Increased power income from gas and electricity export	0.0	0.0	0.0	0.0	0.0	0.0	-3.4	0.0	**-3.4**
Reduced infrastructure renewals expenditure on our sewer repair and maintenance programme	-1.4	-2.9	-1.3	0.0	0.0	1.0	1.4	0.0	**-3.1**
Increase in materials, principally due to the unit cost of chemicals	0.2	0.1	0.0	1.3	0.0	0.4	-0.2	0.4	**2.1**
Improved allocation of combined sewer costs	12.3	-8.6	-3.7	0.0	0.0	0.0	0.0	0.0	**0.0**
Wholesale market services - Increase in cost due to Vacancy/Gap sites	0.6	0.2	0.1	0.7	0.0	0.0	0.0	0.0	**1.6**
Increase in provisions	0.0	0.0	0.0	2.7	0.0	0.0	1.3	0.0	**4.0**
Spend required for compliance with Farming Rules for Water	0.0	0.0	0.0	0.0	0.0	0.0	1.1	0.7	**1.8**
Software as a service ((previously accounted for within capex)	0.5	0.2	0.1	1.9	0.0	0.0	0.0	0.0	**2.6**
Principal use recharges (previously reported in depreciation)	2.0	2.1	0.8	-23.6	0.0	0.3	2.9	0.3	**-15.1**
Business rates reflecting refund in FY21	0.0	0.0	0.0	0.7	0.0	0.0	0.2	0.0	**0.9**
Enhancement - the reversal of the innovation fund provision	-0.4	-0.5	-0.2	-2.1	0.0	0.1	0.0	0.1	**-2.9**
Other year on year movements	2.2	1.0	0.3	3.7	0.3	1.2	0.8	-1.0	**8.4**
RR22 total operating expenditure	**63.6**	**38.8**	**14.9**	**137.0**	**2.8**	**12.8**	**23.4**	**8.9**	**302.2**

Capital expenditure

	Network+ Sewage collection			Network+ Sewage treatment		Bioresources			Total
Line description	**Foul**	**Surface water drainage**	**Highway drainage**	**Sewage treatment and disposal**	**Sludge liquor treatment**	**Sludge transport**	**Sludge treatment**	**Sludge disposal**	
2020/21 total capital expenditure	**41.2**	**45.5**	**18.2**	**218.8**	**0.0**	**0.0**	**28.2**	**2.3**	**354.2**
Base variance	-2.2	-2.6	-1.1	1.3	0.0	0.0	-4.1	-1.8	-10.5
Enhancement variance	-0.3	-2.7	-1.4	66.8	0.0	0.0	-0.6	0.0	61.8
Developer services variance	0.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.3
2021/22 total capital expenditure	**38.9**	**40.2**	**15.7**	**286.9**	**0.0**	**0.0**	**23.5**	**0.6**	**405.7**
Movement £m	**-2.3**	**-5.3**	**-2.4**	**68.1**	**0.0**	**0.0**	**-4.7**	**-1.8**	**51.6**
Movement %	**-6%**	**-13%**	**-15%**	**24%**	**n/a**	**n/a**	**-20%**	**-320%**	**13%**

In general capital expenditure varies from year due to the different mix and levels of maturity of projects being delivered. As such there are multiple movements increasing and decreasing expenditure each year. The below explanations detail the major reasons for growth or reductions in expenditure, however there are multiple other movements that offset each other.

The Sewage collection units saw reduced base expenditure costs of £6m this is primarily related to less maintenance activity at pumping stations. There was also a decrease in enhancement expenditure of £4.4m related to less expenditure on sewer flooding projects.

The Sewage treatment and disposal unit saw increases in expenditure, including an overall increase in enhancement activity at wastewater treatment works of £66.8m. This increase is due to the delivery of projects in the AMP7 WINEP programme.

The Sludge treatment unit saw a minor decrease compared to last year, the majority due to reduced base maintenance at the Manchester Bioresource Centre (£3m).

The decrease in spend in the sludge disposal unit is due to a small decrease in spend on the biosolids fleet.

5.3 Household Retail

Table 2C Cost line	2021/22 (£m)	2020/21 (£m)	Movement (£m)	Movement (%)	Explanation
Customer services	22.1	21.2	0.9	4%	Customer services cost increase is predominantly due to an increase in head count to maintain service levels and therefore maintain C-Mex performance levels.
Debt management	15.9	12.7	3.2	25%	Increase in Debt Collection Agency activity in FY22. Activity was lower in the previous year due to Covid-19 restriuctions which prevented field staff from visiting customer premises.
Doubtful debts	43.0	47.6	(4.6)	(10)%	Reduction of £5m due to ECL overlay in FY21 due to Covid-19. Provision c/f'wd deemed adequate to cover future risk of deteroration in cash collection against debt raised due to cost of living increase.
Meter reading	2.6	3.4	(0.8)	(24)%	Meter reading costs were higher in FY21 due to legacy payments to third party service provider following contract termination. Costs have reduced in FY22 as efficiencies associated with insourcing have been realised and a higher proportion of cost allocated to non-appointed as contracts with retailers have been let.
Other operating expenditure	12.6	13.4	(0.8)	(6)%	Other operating costs have reduced by £(0.4)m due to a reduction in water efficiency expenditure as this is now allocated to wholesale on the basis that expenditure is incurred to meet wholesale outcomes. Other operating costs have reduced by a further £(0.4)m due to a reduction in severance costs.
Total opex excluding third party services	**96.2**	**98.3**	**(2.1)**	**(2)%**	
Depreciation - tangible fixed assets	1.7	1.0	0.7	70%	Depreciation and amortisation has increased, mainly due to commissioning of new assets as expected.
Amortisation - intangible fixed assets	5.1	4.6	0.5	11%	
Recharges from wholesale	3.5	4.0	(0.5)	(13)%	Recharges to and from wholesale are materially consistent with the prior year, with a slight reduction due to assets being fully written down.
Income from wholesale	(0.5)	(0.1)	(0.4)	(400)%	
Total retail costs excluding third party and pension deficit repair costs*	**106.1**	**107.8**	**(1.7)**	**(1.6)%**	
Debt written off	37.2	37.0	0.2	0.5%	Debt write offs consistent with the previous year
Capital expenditure	5.4	12.3	(6.9)	(56)%	Capital expenditure has decreased in the year as planned.

**Third party and pension deficit repair costs for 2021/22 were £nil.*

5.4 Principal use recharges

2021/22

Price control	Water Resources £m	Water Network+ £m	Wastewater Network+ £m	Sludge £m	Retail Household £m	Total £m
Recharge from other segments	(0.2)	(16.2)	(3.2)	(3.6)	(3.5)	(26.7)
Recharge to other segments	0.0	4.3	21.8	0.1	0.5	26.7
Net recharge	**(0.2)**	**(12.0)**	**18.6**	**(3.5)**	**(3.0)**	-

2020/21

Price control	Water Resources £m	Water Network+ £m	Wastewater Network+ £m	Sludge £m	Retail Household £m	Total £m
Recharge from other segments	(1.9)	(17.6)	(3.2)	(3.9)	(4.0)	(30.6)
Recharge to other segments	1.3	4.8	24.3	0.1	0.1	30.6
Net recharge	(0.6)	(12.8)	21.1	(3.8)	(3.9)	-

Overall net recharges of £26.7m for 2021/22 have decreased by £3.9m compared to the net recharges in 2020/21. The majority of this reduction relates to shared use assets coming out of life since the prior year including a large IT hardware refresh project commissioned in 2016 with a 5 year life.

Recharges are also made from the appointed business to the non-appointed business and non-regulated businesses for the use of appointed assets by these businesses, e.g. for the use of IT assets by non-appointed staff.

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Water for the North West