

RIIO-GD1

Regulatory Financial Performance Reporting (“RFPR”) Commentary

Year ended:
31 March 2021





Contents

Executive Summary	3
Key Financial Performance measures	4
Key Operational Performance measures	4
Overview of Regulatory Performance	5
Data Assurance Statement	10
Appendices	11





Executive Summary

The purpose of the Regulatory Financial Performance Reporting (“RFPR”) is to provide a framework to allow Ofgem to collect accurate and consistent information from licenced network operators (Licensees), in particular in the calculation of Return on Regulatory Equity (“RoRE”).

The RoRE calculation is presented on tab R1 of the RFPR. It should be noted that Wales & West Utilities Limited’s (“WWU”) RORE would be lower if it reflected only cash distributions to shareholders.

Enduring value adjustments have been entered into tab R4 – Totex. There has been a lack of detailed guidance in this area, which may impact the consistency of the enduring value calculations between each Licensee. WWU has included enduring value adjustments where the workload performed, as a proportion of the total workload performed over the eight years of the RIIO-GD1 price control, is materially different to the equivalent proportion of the workload upon which the allowances were set under the RIIO-GD1 price control.

The RFPR Submission can be located on the WWU website, as required by Ofgem by following the link below:

<https://wwutilities.co.uk/media/4187/2020-21-wales-west-utilities-rfpr-tables.xlsx>

For further information, please refer to the WWU RIIO-GD1 Eighth Year Annual Report, Strategic Performance Overview, which was submitted to Ofgem on 30 July 2021. The link to this report on the WWU website is as follows:

<https://wwutilities.co.uk/media/4185/2020-21-wales-west-utilities-rrp-strategic-performance-overview.pdf>





Key Financial Performance measures

Commentary on key financial performance measures can be found within the WWU RIIO-GD1 Eighth Year Annual Report, pages 8 – 18, which was submitted to Ofgem on 30 July 2021.

The link to this report on the WWU website is as follows:

<https://wwutilities.co.uk/media/4185/2020-21-wales-west-utilities-rrp-strategic-performance-overview.pdf>

Key Operational Performance measures

Key operational performance measures are discussed within the WWU RIIO-GD1 Eighth Year Annual Report, pages 24 - 31, which was submitted to Ofgem on 30 July 2021.

The link to this report on the WWU website is as follows:

<https://wwutilities.co.uk/media/4185/2020-21-wales-west-utilities-rrp-strategic-performance-overview.pdf>

Further detail can be found within the 2020/21 WWU Annual Stakeholder Report and draft WWU 2020/21 Statutory Accounts. The link to the Annual Stakeholder document is provided below.

<https://www.wwutilities.co.uk/media/4179/wales-west-utilities-annual-stakeholder-report-2020-21.pdf>





Overview of Regulatory Performance

R1 - RORE

The return on regulatory equity (“RORE”) involves two measures.

The first measure assumes notional gearing of 65%. On that basis, RORE was 8.5% for RIIO-GD1. This comprises operational RORE of 12.1%, reduced by a shortfall on debt performance, net of tax, of 3.6%. For the year 2020/21, RORE was 4.1% (8.7% for 2019/20), a reduction of 4.6% over 2019/20.

The main reasons for the decrease of 4.6% over 2019/20 are :-

- Lower Totex outperformance at 2.2% in 2020/21, a reduction of 2.0% compared to 2019/20
- Higher debt underperformance, net of tax, of 5.8% for RIIO GD1, and year on year increase of 2.6%

The second measure uses actual gearing. On that basis, RORE was also 8.5% for RIIO-GD1. This comprises operational RORE of 13.8%, reduced by a shortfall on debt performance, net of tax, of 5.3%. For the year 2020/21, RORE was 4.1% (8.5% for 2019/20), a reduction of 4.4% over 2019/20. Lower Totex outperformance and higher debt underperformance, net of tax, are the main factors for this reduction.

R2 – Revenue

This sheet reflects the data contained within the Revenue Return 2020/21, submitted to Ofgem on 30 July 2021 in line with Licence Condition SSC A40.

For commentary on these figures, please refer to the WWU RIIO-GD1 Eighth Year Annual Regulatory Reporting Pack (“RRP”) commentary, page 12, which was submitted to Ofgem on the 30 July 2021.

The link to this report on the WWU website is as follows:

<https://wwutilities.co.uk/media/4185/2020-21-wales-west-utilities-rrp-strategic-performance-overview.pdf>

R3 / R4 – Totex Performance

Data included within the R3 and R4 sheets on Totex performance was also included within the WWU RIIO-GD1 Eighth Year Annual Regulatory Reporting Pack (“RRP”) commentary, submitted to Ofgem on 30 July 2021 in line with Licence Condition SSC A40.

R3 - Rec to Totex reflects the data from the draft consolidated financial statements of Wales & West Utilities Limited reconciled to the Totex costs for the regulatory year.





The purpose of the R3 Rec to Totex schedule is to show a reconciliation of the statutory financial statements to Totex, (WWU has used audited regulatory accounts where the statutory year ends were not coterminous with the regulatory year – for the years ended 31 March 2013, 2014, 2015 and 2016 – which can be reconciled back to the statutory accounts after adjusting for timing). From 1 April 2016 onwards the statutory and regulatory year ends are coterminous. From 1 April 2018 the consolidated statutory financial statements of Wales & West Utilities Limited have been used as the basis for the reconciliation to Totex, following Ofgem’s consent to withdraw the requirement for Consolidated Regulatory Accounts.

WWU has made no further adjustments to Totex to achieve the reconciliation to the PCFM.

The draft consolidated statutory financial statements of Wales & West Utilities Limited for the current year are the starting point for the R3 Rec to Totex.

The link below is to the Consolidated statutory financial statements for the year ended 31 March 2020. The year ended 31 March 2021 financial statements will be submitted in August 2021.

<https://beta.companieshouse.gov.uk/company/05046791/filing-history>

R4 – Totex reflects the data contained within table 2.2 Totex costs summary: Summary tables, see link below

<https://wwutilities.co.uk/media/4190/2020-21-wales-west-utilities-rrp-cost-and-volumes-tables.xlsx>

For commentary on the totex figures, please refer to the WWU RIIO-GD1 Eighth Year Annual Report, which was submitted to Ofgem on 30 July 2021.

The link to this report on the WWU website is as follows:

<https://wwutilities.co.uk/media/4185/2020-21-wales-west-utilities-rrp-strategic-performance-overview.pdf>

R5 – Output Incentive Performance

Data within this tab mirrors the data contained within the Revenue Return 2020/21, submitted to Ofgem on 30 July 2021 in line with Licence Condition SSC A40.

Please refer to the WWU RIIO-GD1 Eighth Year Annual Report, which was submitted to Ofgem on the 30 July 2021.

The link to this report on the WWU website is as follows:

<https://wwutilities.co.uk/media/4185/2020-21-wales-west-utilities-rrp-strategic-performance-overview.pdf>





R6 – Innovation

Please refer to the WWU RIIO-GD1 Eighth Year Annual Report, pages 19 - 23, which was submitted to Ofgem on the 30 July 2021.

The link to this report on the WWU website is as follows:

<https://wwutilities.co.uk/media/4185/2020-21-wales-west-utilities-rrp-strategic-performance-overview.pdf>

Further information on innovation at WWU can be found in our 2020/21 WWU Innovation Report. The link to this report on the WWU website is as follows:

[Energy Innovation | Wales and West Utilities \(wwutilities.co.uk\)](#)

R7 / R8 – Finance and Net Debt Position

Cost of Debt (excluding derivatives)

WWU continues to have a significant shortfall against the Cost of Debt allowance for GD1. WWU's cost of debt has been efficiently incurred but is not fully compensated for by the rolling 10-year iBoxx index used by Ofgem for calculating Allowed Cost of Debt.

R9 - RAV

Data reported within tab R9 reflects the 2020 Price Control Financial Model ("PCFM") agreed with Ofgem through the informal AIP process in November 2020 which calculated LMOD1 using actual results up to 2019/20.

R10 – Taxation

Reconciliation to the Regulatory Year

For years prior to 2017, Wales & West Utilities Limited's statutory reporting periods were not coterminous with the Regulatory Year. Accordingly, in preparing the R10-Tax submission the tax liability per latest submitted CT600 has been taken as the CT600 tax liability per the Regulatory Accounts for 2014 to 2016 inclusive. No CT600 tax liability arises under either the statutory reporting periods or regulatory years for 2014 to 2016 inclusive (as a result of the utilisation of brought forward tax trading losses) and accordingly no reconciliation of these amounts is provided.

Regulatory performance in respect of taxation

Prior to 2017, Wales & West Utilities had no regulatory tax liability, and accordingly no net tax allowance, as a result of the utilisation of brought forward regulatory tax losses.

The brought forward regulatory tax losses were utilised in full during 2017, resulting in regulatory tax liabilities and associated forecast net tax allowances arising in 2017 to 2021 inclusive. Wales & West Utilities forecast net tax allowances for 2017 and subsequent years are reduced by tax





clawback as a result of actual gearing being in excess of notional gearing; except in 2021 where actual gearing is below notional.

The RFPR submission is based on the latest PCFM of November 2019. Therefore row 63 of the R10 – Tax tab does not include tax clawback for actual 2020 because the figure would have been a forecast, thus nil, at that time.

As per the 2012 Final Proposals document the total tax allowance for Wales & West Utilities was £81.2m (09/10). Based on the RFPR submission, the total tax allowance for GD1 is forecast as £103.7m (09/10) (or a net forecast tax allowance of £82.9m after tax clawbacks of £20.8m).

The tax performance in the RoRE calculation (in line with section 1.14 of the [Regulatory financial performance annex to RIIO-1 Annual Reports - 2017-18](#)) compares Wales & West Utilities actual/forecast CT600 tax liability against the tax allowance set as part of the RIIO-1 price control including the impact of deviating from notional levels of gearing in the form of tax clawback.

R11 – Dividends

WWU has not paid dividends since its formation in 2005 and is not forecasting to pay dividends in future years due to negative reserves. However, shareholder loan note interest payments are made instead, and are treated as distributions for RFPR purposes.

WWU made no shareholder loan interest payments in 2020/21 (2019/20 £40m) and deferred the interest payment due in 2020/21 to April 2021 as a result of Covid-19 uncertainty and to support financeability. The future forecast distributions for shareholder loan interest payments assume the RIIO-GD2 Ofgem modelled distribution rate of 3% of equity RAV.

Details of shareholder loan notes are included on page 60 of the WWU statutory accounts for the year ended 31 March 2021 within Note 13 (iv) – External Borrowings, which will be filed in August 2021.

R12 – Pensions

Please refer to section 9.2 starting on page 100 of the RRP Commentary (submitted to Ofgem - 30 July 2021) and the PDAM (submitted to Mick Watson, Ofgem – by email 28 August 2020).

Please refer to these submissions for explanations.





R13 – Other activities

WWU has not incurred any Ofgem penalties or fines throughout RIIO-GD1.

Guaranteed Standards of Service payments (“GSOP”) are statutory payments at rates set by Ofgem.

WWU incurred £26k of additional compensation for the year ended 31 March 2021 (2020: £27k) following the decision to double the Ofgem compensation rates from July 2017. This has been included within the return together with other discretionary payments.

The data to 31 March 2021 has been extracted from table 8.3 Guaranteed Standards of Service within the 2020/21 Regulatory Reporting Pack (RRP), submitted to Ofgem on 30 July 2021 in line with Licence Condition SSC A40.

The table 8.3 is also published on the WWU website – see link below

<https://wwutilities.co.uk/media/4190/2020-21-wales-west-utilities-rrp-cost-and-volumes-tables.xlsx>

The GSOP payments have been adjusted for tax within the return to show the net effect of the amount to be disallowed.

As per the instruction extract from Ofgem letter to GDN regulatory managers dated 22 October 2018, WWU resubmitted all RIIO-GD1 RRP in 2019 for the period of 2013/14 to 2017/18 removing all associated discretionary payments.





Data Assurance Statement

This is the third year that WWU has submitted Ofgem's RFPR return and Commentary. Ofgem require that the 2020/21 submission be uploaded on the Company's website.

The 2020/21 RFPR has been completed in line with the RIGs and on this basis a full DAG process has been conducted.

Management prepared methodology statements and completed risk assessments for each RFPR table and these were provided to Internal Audit for review. All tables were subject to the requisite first line assurance i.e. data preparer, second person review, business lead sign-off and executive sign-off, and these review stages included the following checks:

- Agreeing data to already published information where possible, including the RRP, Regulatory Accounts and Consolidated statutory financial statements, where such information has already been subject to varying levels of validation and data assurance;
- Agreeing data to the underlying workbooks;
- Reperforming calculations to ensure the correct results within the tables; and
- Ensuring the commentary is aligned with the tables.

A final review has been undertaken by members of the WWU Executive team including the Director of Regulation & Asset Strategy and the Director of Finance.

Additionally, following review of the risk assessments and discussion with management a sample of submission tables were selected for review by Internal Audit. Independent data and process audits were performed which involved detailed reviews to agree the submissions details to source data on a sample basis and reperforming calculations where required to ensure correct results were recorded.





Appendices

- 1 Reconciliation where licensees have a different statutory reporting year to the Regulatory Year
- 2 Enduring Value Adjustments





Appendix 1

Reconciliation where licensees have a different statutory reporting year to the Regulatory Year

For the past data where the statutory and regulatory year ends were not co-terminus WWU has referenced the audited Regulatory accounts for the years ended 31 March 2013, 2014, 2015 and 2016, such Regulatory accounts having been subject to review by WWU's auditors. From 31 March 2016 onwards the statutory and regulatory year end are coterminous.





Appendix 2

Enduring Value Adjustments

Enduring value adjustments have been entered within tab R4 – Totex and tab R9 - RAV. These adjustments have sought to apply a re-phased allowance to items within Totex, for the calculation of outperformance and to calculate the impact these adjustments would have in RAV.

The re-phased allowance is based on actual workload over RIIO-GD1. The re-phasing has been applied to Capex, Repex and gas holder demolition within Opex. The purpose of the rephrasing is to account for timing differences between workload delivery forecast in final proposals compared with actual workload data.

Overall, WWU has meet or exceeded its RIIO-GD1 targets and therefore the net adjustment over the whole of the RIIO-GD1 period is nil.

Although enduring value adjustments have been entered, a caveat should be applied given the lack of detailed guidance in this area. In addition, no enduring value adjustments have been calculated in respect of non-controllable costs and incentives which are trued up within allowed revenue on a two-year lag basis.

WWU has not applied any enduring values in relation to close out mechanisms, such as NARMs (currently NOMs for RIIO-GD1). We are not expecting to submit any further reopener claims and do not currently forecast any significant impact as a result of NARMs.

