

M Tables – Regulatory Accounts Commentary

The sections in this document are:

1. General comments
 2. Results and reconciliations
 3. Assumptions
 - 4.1 Commentary – M tables 1-28
 - 4.2 Detailed Commentary – M tables 18 W & 18 WW
- Appendices

1. General Comments

There have been no disclosure changes to the 2008/09 M Tables by the WICS. Consequently there has been no requirement to restate any of the comparative figures for 2007/08.

SW's structure changed in 2008/09 when Scottish Water transferred the commercial, non regulated activities into separate legal entities. For this purpose, two wholly owned subsidiary companies were set up - Scottish Water Horizons Holdings Limited (SWHH) and Scottish Water Horizons Limited (SWH). SWH is the operating company, while SWHH is the intermediary holding company, owing 100% of the shares in SWH. The consolidation tables – M27 and M28 – include the results of SWH and SWHH along with Business Stream Holdings Limited (SWBSH) in the Non Core/Non Licensed column, while Business Stream is included in the Licensed column.

2. Results & Reconciliation

SW produces statutory consolidated accounts incorporating the results of SWBSH, SWHH, Business Stream and SWH. The consolidated statements also include the balance sheet (and relevant notes) for SW only ('company'). Detailed reconciliations between the statutory accounts and the regulatory tables have been attached in the appendix to this document.

M Table financial information is for SW only, i.e. excluding SWBSH, SWHH, Business Stream and SWH, and is analysed between Core (= Regulatory business) and the remaining Non Core (= Non regulatory activities) where required. The exceptions to this are:

- tables M18W and M18WW which include the costs of SWH; and
- tables M27 and M28 which provide reconciliations from the SW Core figures to the group consolidated income and expenditure statement and balance sheet respectively.

Due to some different descriptions and terminology between the regulatory M tables and the statutory accounts, Appendix 1.1 and 1.2 provide reconciliations from the Table M27 totals and M28 totals to the statutory consolidated income and expenditure account and consolidated balance sheet, respectively. Appendix 1.3 shows the reconciliation between Table M2 and the statutory "company" balance sheet.

Regulated / Non Regulated have been accounted for separately in SW's general ledger system enabling the production of regulated/non-regulated profit & loss accounts and balance sheets. These form the basis for the historical cost figures and analysis, in particular Tables M1, M2, M24, M27 & M28.

Cost analysis in Tables M18 W and M18 WW was prepared using reports from SW's Activity Based Management (ABM) systems. Detailed commentary on ABM methodology and cost allocation is provided in support of the E Tables and is not repeated in this document.

FRS17 entries in the statutory accounts have been included in the regulatory results, both HCA and CCA, but are excluded in Tables M18W and M18WW and the E Tables in the Annual Return. The impact of FRS 17 was a decrease to operating costs of £3.3m (2007/08: increase of £3.7m) and an increase to financing costs of £1.3m (2007/08: credit of £5.3m), giving a net increase to profit before tax in the income and expenditure account of £2.0m (2007/08: increase of £1.6m).

3. Assumptions

Non core tax charge

It has been assumed that there are no brought forward profits/losses or capital allowances for the non core element. The tax charge is based on the actual profit attributable to the non regulatory businesses in 2008/09. (Tables M1, M2)

CCA adjustments

RPI of -0.38% used in the relevant adjustments, being the rate as at March 2009.

CCA working capital adjustment

The working capital adjustment has been pro rated between water and waste water based on turnover values. (Table M7, line 7.14)

CCA fixed asset values

Opening and closing CCA fixed asset values have been taken from the H Tables for the relevant years. The H Tables for 2008/09 have been calculated on a MEAV basis. The movement in the fixed asset value due to the change in method is reflected through the 'Investment plan adjustment' lines. The RPI adjustment has been calculated on the opening balances as reported in the 2007/08 M Tables.

Tables M16 & M17 – 5 year rolling summaries

Figures for 2006/07 to 2008/09 have been entered (automatically). Figures for the previous years were not required.

4.1 Commentary – Tables M1 to M28

This section has comments on individual tables, where it is felt that such narrative will aid understanding, explain significant year-on-year movements or provide additional guidance on how the information was gathered or calculated. There are no comments on the tables which appear self explanatory.

Table M1 – HCA Income & Expenditure Account

The Core information is from the general ledger reports for the Regulated business. The non core information relates to the sundry non regulated activities which remain within Scottish Water. The 2007/08 comparatives figures for non core include the non regulated activities transferred to SWH on 1 April 2008.

Nominal operating costs (i.e. excluding depreciation, PFI charges, FRS 17 pension charges and costs associated with non regulated activities) increased by £31.2m to £290.2m compared to £259.0m in 2007/08. On a like-for-like basis regulated operating costs increased by £7.5m, a 2.9% nominal increase. The table below summarises this movement:

	2008/09	2007/08	Mvt fav/(adv)
	£m	£m	£m
Core operating expenditure – line M1.2	287.6	263.3	-24.3
Less: Internal PFI costs	-0.7	-0.6	0.1
Add/less: FRS 17 operating cost adjustment	3.3	-3.7	-7.0
SW Regulated operating costs	290.2	259.0	-31.2
CMA start-up / running costs	-0.6	-2.0	-1.4
A-typical bad debt credit	8.1	17.6	9.5
VR costs	-3.5	-3.4	0.1
Leakage reduction costs	-20.8	-8.3	12.5
Additional new opex	-3.0		3.0
Like-for-like nominal costs	270.4	262.9	-7.5
Average inflation (2.97%)		7.8	7.8
Like-for-like costs (real)	270.4	270.7	0.3

Like-for-like operating costs for 2008/09 of £270.4m include the absorption of increased local authority rates and SEPA costs of £4.9m. New opex released during 2008/09 to operational units relate to new operational activities associated with new assets which reached beneficial use during the year. The costs primarily relate to power, chemicals and rates costs. In real terms, like-for-like costs were £0.3m lower than in 2007/08.

The cost of the PFI schemes in the year was £132.0m (excluding PFI team costs), £5.0m higher than in 2007/08 due primarily to contract indexation which on one scheme was impacted significantly by gas prices.

The increase in depreciation year-on-year was primarily due to the higher infrastructure maintenance charge, reflecting the level of underlying and long term forecast infrastructure investment.

Other operating income of £1.5m (line 1.8) was the gain on disposal of fixed assets, £7.8m lower than in 2007/08.

The net interest charge of £150.8m (2007/08: £135.0m) (line 1.11) includes the FRS 17 financing charge of £1.3m (2007/08: £5.3m credit). The higher net charge was also due to

the timing of the drawdown of the new borrowings and lower interest received (see Table M23).

SW's total tax charge was £59.1m, an effective rate of 30.3% (2007/08: £38.1m, 17.1%). The effective rate was impacted by the requirement to revisit changes introduced by the Finance Act 2007 in relation to assets classed as industrial buildings. This required a cumulative catch-up in the 2008/09 deferred tax computation.

Table M2 – HCA Balance Sheet

Core / Non core information is from the general ledger reports. The non core information relates to the sundry non regulated activities which remain within Scottish Water following the transfer of the majority of the non regulated activities to SWH on 1 April 2008. The variances between the March 2008 and March 2009 non core balances relate to the transfer of the relevant assets and liabilities to SWH.

The main difference from the statutory HCA balance sheet is recognition of the Infrastructure Renewals accrual of £42.2m (line 2.14) and the corresponding increase to the fixed asset total (line 2.1; being £4,294.2m + £42.2m = £4,291.4m).

Investment – loan to group company (line 2.2) at 31 March 2008 was the intercompany loan of £58.5m to SWBSH. Following the repayment of this loan in December 2008 by SWBSH, there was no intercompany loan balance as at 31 March 2009.

Investment – other (line 2.3) is the investment in SWBSH of £34.6m and the investment in SWHH of £3.0m.

The £15.7m decrease in debtors (from £79.2m to £63.5m; line 2.6) is due to:

- lower household trade debtors (from £28.5m to £26.3m; Table M11, line 11.2);
- lower prepayments and other short term debtors (from £16.7m to £14.7m; Table M11, line 11.6) due to the utilisation of the advance purchase of materials for Glencorse WTW; and
- a reduction in non trade debtors (from £32.5m to £20.2m; Table M5, line 5.12) being lower VAT receivable outstanding from HMRC.

Cash at bank decreased by £11.2m to £15.9m. The balance at 31 March 2008 included £27.4m of out-performance monies. However, no transfers to the financial reserve have been made because all available financing will be required to finance delivery of the capital investment programme in 2009/10.

Deferred income of £21.1m (line 2.26) includes the proceeds from the sale of the masts and towers income stream.

Post employment liability (line 2.27) is the FRS 17 pension liability which has increased from £34.3m to £160.5m due mainly to an actuarial loss of £183.0m reflecting the lower than expected return on scheme assets.

Other provisions (line 2.28) have increased by £3.9m to £18.7m due primarily to net increases in the reorganisation (£2.8m) and wholesale income uncertainty provisions (£1.3m). The different elements within the total are detailed in Table M26 (lines 26.8-26.10).

Table M3 – HCA Balance Sheet – Reconciliation to Statutory Accounts

This provides a summary of the main reconciling items. The Profit and Loss section (lines 3.1-3.5) reconciles the statutory Group consolidated figures to Table M1 Core figures, because no profit and loss figures are provided for SW company in the statutory accounts.

However, more details have been given in the appendices – 1.1, 1.2 and 1.3. The balance sheet section (lines 3.8-3.15) reconciles SW Company figures from the statutory accounts to Table M2 Core figures.

Table M4 – CCA Income & Expenditure Account

The only differences between the HCA and CCA Income and Expenditure Accounts are due to the CCA adjustments.

- CCA depreciation is calculated based on the brought forward CCA net book values. The net/gross % per the H Tables at March 2009 indicates 50.9% of the average useful life remains. Therefore 50% has been used in the CCA depreciation calculation.
- The index applied is the RPI of -0.38%.
- Amortisation of deferred income (grants and contributions) is adjusted for the indexing.
- The working capital adjustment is the indexed of the opening (operating) working capital (as in Table M11).
- The financing adjustment is the index applied to the opening net finance amount for SW.

Table M5 – CCA Balance Sheet

Third party contributions (line 5.2) include the index-adjusted value of both grants and contributions.

Non trade debtors (line 5.12) is VAT receivable at March. The decrease of £12.3m compared to 2007/08 is due to the delayed receipt of VAT in 2008 being for two months whereas as the March 2009 balance represents one month only.

Non trade creditors (line 5.13) consist of the interest accrual (£34.2m), infrastructure income not yet invested (£9.7m), payments received in advance in relation to connections i.e. network, developers and inspection deposits (£21.7m) and other (£10.0m).

Other creditors due after one year (line 5.20) consist of infrastructure income not yet invested (£14.6m) and payments received in advance (£23.9m).

The income & expenditure reserve (line 5.28) is the total of the CCA reserve at 31 March 2008, the CCA profit for 2008/09 and the movements detailed in the STRGL (Table 19).

Table M6 – CCA Cash Flow

Interest received (line 6.4) includes the intercompany interest received from SWBSH of £2.5m. Interest paid (line 6.5) includes intercompany interest paid to Business Stream of £0.8m in relation to the settlement of wholesale billing and reconciliation process.

The gross cost of fixed assets purchased (line 6.9) relates to the additions within the 'Assets in the course of construction' (AUC) column of Table M8. All additions to fixed assets are entered in AUC before being reclassified to the appropriate fixed asset category when they come into beneficial use. As the exact categorisation of fixed assets (including the split between base and enhancement for infrastructure assets) is not determined until they come into beneficial use, it is not possible to analyse the cash payments relating to fixed assets between lines M6.9 and M6.11. Accordingly, all cash payments are shown in line M6.9 and reconcile to the additions to fixed assets in Table M8 (line 8.5) as follows:

	M Table / line ref	£m
Opening short term capital creditor	M11.10 (07/08)	71.558
Add: Additions to fixed assets	M 8.5	700.420
Less: Closing short term capital creditor	M11.10 (08/09)	<u>52.279</u>
=> Cash payments	M 6.9	<u>719.699</u>

The movement on loans to group companies (line 6.13) of £58.5m is the repayment of the intercompany loan by SWBSH. The non core figures include the transfer of the assets / liabilities to SWH, with the £3.0m acquisitions and disposals (line 6.15) being the investment made by SW (non regulated) in SWHH for the equivalent value of shares.

Table M7 – Analysis of Turnover and Operating Income

Turnover from services supplied to household customers increased by 4.6% to £704.7m driven mainly by the tariff increase effective from 1 April 2008. Turnover from wholesale services provided to Licensed Providers increased by 4.7% to £319.9m. Turnover from other sales reduced by £2.4m to £5.1m reflecting the transfer of building water services to Business Stream during 2008/09.

Table M8 – CCA Analysis of Fixed Assets by Asset type (Core)

For Water Services and Sewerage Services columns, the opening (lines 8.1 & 8.14) and closing (8.7 & 8.15) values in Table M8, agree to the values in Table H1 as at 31 March 2008 and 31 March 2009 respectively. The additions in the year are at actual cost. The inflation adjustment figures (lines 8.3 & 8.10) are the indexing of the brought forward values, using RPI of -0.38%. The values shown for the investment plan adjustment (lines 8.2 & 8.9) are the revaluation adjustments bringing the closing values back into agreement with Table H1 values. H Table analysis generates a valuation of assets at a point in time and does not analyse year on year movements.

The H Tables categorise the assets into water / wastewater non infrastructure, water / wastewater infrastructure and support services. In Table M8 the support services have been allocated between water and wastewater based on their HCA values.

SW's additions to fixed assets are entered firstly to assets in the course of construction (AUC) then, on beneficial use, reclassified to the appropriate asset category. All values for AUC are HCA.

For the Business Plan 2010-2014, 2nd draft (2DBP) the fixed asset MEAVs as at 31 March 2008 were recalculated, with the revalued amounts used to calculate the CCA depreciation in that report. Therefore, for consistency, the revised MEAVs per the 2DBP have been used as the basis for the CCA depreciation calculations in the 2008/09 M Tables (not the CCA net book values submitted in the final H and M Tables as at 31 March 2008; i.e. lines M8.1 & M8.8 in the 2009 tables). The change in the 31 March 2008 MEAV balances between the H/M Tables and the 2DBP form part of the 'Revaluation – Investment plan adjustment' figures in lines M8.2 and M8.9. A full reconciliation of the MEAVs and the investment plan adjustment figures is provided in Appendix 2.

The CCA depreciation calculation assumes 50% of the relevant average useful life remains, based on the ratio of net to gross values per Table H1 at 31 March 2009. The index applied is the RPI of -0.38% (in 2DBP +2.5%). For additions during the year, half of the actual cost (i.e. assuming additions are in use for half of the year, on average) and the relevant average useful lives are the basis, with no indexing.

Table M11 – CCA Working capital

The decrease of £2.2m in Household trade debtors is predominantly due to higher bad debt provision requirements reflecting the current economic climate. Other trade debtors relate to sundry and non primary wholesale billing.

The increase in trade creditors of £5.1m to £25.0m was offset by a decrease in accruals of £6.6m to £76.5m.

The wholesale charge prepayment of £27.7m at March 2009 is the total of the provisional invoices for April 2009. The March 2009 balance was net of reconciliation amounts relating to prior months.

Capital creditors consist of the balance due to SW Solutions (£24.5m) and capital creditors and accruals relating to external parties (£27.7m). The lower total at March 2009 reflects the higher payments made towards the end of the year.

A separate reconciliation (Appendix 1.4) has been prepared showing reclassifications from statutory basis of debtors and creditors into regulatory CCA working capital (operating items) and non operating debtors and creditors. (Tables M11 & M5).

Table M12 – Movement on Current Cost Reserve

The investment plan adjustment (line 12.2) is the net opposite entry from Table M8 (line 8.2 £7,365.2m – line 8.9 £760.6m = £6,604.6m). The fixed asset inflation adjustment (line 12.3) represents the net of the cost and depreciation adjustments from Table M8 (lines 8.3 & 8.10). The other items are the opposite entries of the CCA adjustments described under Table M4. The detailed calculations for the financing adjustment and grants and third party contributions are provided in the tables below.

M Table line no.		2007/08 £m	RPI %	Financing adjustment £m	M Table line no.
5.26	Net assets employed	33,900.556			
5.8	Net operating assets	<u>34,162.337</u>			
		-261.781			
5.29	Deferred tax - add back	<u>241.965</u>			
	Net finance	<u><u>-19.816</u></u>	-0.38%	<u>0.075</u>	12.5/4.14
M Table line no.		2007/08 £m	RPI %	Grants & 3rd party contrib. adjustment £m	M Table line no.
5.2	Third party contributions	<u><u>-21.368</u></u>	-0.38%	<u>0.081</u>	12.6

Table M13 – Reconciliation of Current Cost operating surplus to net cash flow from operating activities

The working capital movement (line 13.3) is the movement in the working capital totals (Table M11) excluding the short term capital creditors – see table below:

	M Table Line ref	2007/08 £m	2008/09 £m	Mvmt £m
Total working capital	M11.13	-158.7	-153.4	-5.3
Short-term capital creditors	M11.10	71.6	52.3	19.3
Movement in working capital	M13.3			<u><u>13.9</u></u>

The actual movement of £13.9m reflects the higher level of net current liabilities.

For both years the amount in line 13.10 is the FRS17 adjustment in operating costs.

Table M14 – Analysis of net debt

Table M14 shows net debt for core activities of £2,778.6m. However, for the purposes of determining SW's out-performance of the Regulatory Contract, the net debt figure should be adjusted as follows:

	£m
Net Debt per M14, line 14.9	2,778.6
Less funding for Business Stream Group	<u>25.0</u>
Adjusted Net Debt	<u><u>2,753.6</u></u>

Table M16 – 5 year rolling summary: Current Cost Income & Expenditure Account for Core Business

As agreed with the WICS, this table has not been populated for the earlier years. The 2006/07 to 2008/09 figures are entered automatically from the other tables.

Table M17 – 5 year rolling summary: Current Cost Balance Sheet for Core Business

As agreed with the WICS, this table has not been populated for the earlier years. The 2006/07 to 2008/09 figures are entered automatically from the other tables.

Table M18B W – Analysis of fixed assets – Water Service

The information presented here is a more detailed analysis of the non infrastructure and infrastructure water assets provided in Table M8. The opening (lines 18b.1 & 18b.16) and closing (lines 18b.6 & 18b.15) balances agree to the values in Table H1 at 31 March 2008 and 31 March 2009 respectively. The Table H1 figures for water storage (H1.2) and water resources (H1.4) are combined under "Sourcing"; water treatment works (H1.1) is "Treatment"; water pumping (H1.3) and water mains (H1.5) are "Water distribution". Support service assets are not included in Table M18b. Their inclusion, which could only be by means of allocation across the current category headings, would distort the clear tie between Tables H1 and M18B.

Additions/reclassifications from AUC are at actual cost. As in Table M8, the RPI of -0.38% was applied to the opening balances to calculate the RPI adjustment (lines 18b.3 & 18b.11). The revaluation adjustments to bring the closing figures back to the H1 values are shown in the investment plan adjustment (lines 18b.2 & 18b.8). H Table analysis generates a valuation of assets at a point in time and does not analyse year-on-year movements.

Table M18B WW – Analysis of fixed assets – Waste water Service

The information presented here is a more detailed analysis of the non infrastructure and infrastructure waste water assets provided in Table M8. The opening (lines 18b.1 & 18b.16) and closing (lines 18b.6 & 18b.15) balances agree to the values in Table H1 at 31 March 2008 and 31 March 2009 respectively. The Table H1 figures for wastewater infrastructure (H1.6, H1.7 & H1.8) and sewage pumping (H1.9) are combined under “Sewerage”; sewage treatment works (H1.10) is “Sewage treatment”; sludge treatment facilities (H1.11) is “Sludge treatment & disposal”. Support service assets are not included in Table M18b. Their inclusion, which could only be by means of allocation across the current category headings, would distort the clear tie between Tables H1 and M18B.

Additions/reclassifications from AUC are at actual cost. As in Table M8, the RPI of -0.38% was applied to the opening balances to calculate the RPI adjustment (lines 18b.3 & 18b.11). The revaluation adjustments to bring the closing figures back to the H1 values are shown in the investment plan adjustment (lines 18b.2 & 18b.8). H Table analysis generates a valuation of assets at a point in time and does not analyse year on year movements.

Table M19 – Statement of total recognised gains and losses (core)

Although the table title states ‘Core’, line 19.1 is actually referenced to the total column of Table M1, i.e. total of Core and Non Core.

The actuarial gain is calculated as part of the FRS 17 statutory adjustments. In 2007/08, the ‘other’ gain of £9.6m was SW’s gain on the value of the investment in Business Stream following Business Stream’s capitalisation of £9.6m of reserves through a bonus share issue. SWBSH acquired SW’s investment in Business Stream for £9.6m by issuing share capital to the same value.

Table M21 – Taxation analysis

The amended 2007/08 tables reflect the position as per the submitted 2007/08 tax computation which was submitted to HMRC in March 2009. The 2007/08 annual return is populated using estimated values in some circumstances.

In addition the 2007/08 tax computation includes capital allowances claimed on £304.2m of work in progress capital spend. This is as a result of an agreement with HMRC that Scottish Water could claim capital allowances on WIP for all projects commencing after 1 April 2006 in the Q&S3 capital programme.

Current tax charge relates to capital gains which cannot be offset with trading losses brought forward. The 2007/08 amount has been submitted but has not been reviewed to date by HMRC. The 2008/09 value is an estimate at this stage.

Table M22 – Fixed asset additions and expected depreciation (CCA)

The non infrastructure additions (line 22.8) are the amounts reclassified from AUC, as described above. These figures agree to the reclassifications in Table M8 (line 8.6) for non-infrastructure assets and support services, as split between water and sewerage services. The following table provides the reconciliation of the reclassifications in Table M8 (line 8.6) to the ‘additions’ in Table M22:

	Line ref	Col ref	Water £m	Wastewater £m	Total £m
Non infrastructure assets	M8.6	F / J	105.034	200.873	
Support services	M8.6	H / L	2.082	3.594	
Additions per Table M22	M22.8	I / J	107.116	204.467	311.583
Infrastructure assets - enhancement	M8.6	G / K	43.639	65.400	
Total	M8.6	I / M	150.755	269.867	420.622
Infrastructure assets - base	M22.20				57.156
Total reclassifications from AUC	M8.6	N			477.778

The figures in the section “Infrastructure renewals charges, expenditure and provision”, (lines 22.20 – 22.22), are the movements during 2007/08 and 2008/09. Therefore the resulting total is not the closing balance as given in the balance sheets at 31 March 2009. The table below shows the full reconciliation:

Infrastructure renewals:	31 March 2008	2008/09 movements	M22 refs	31 March 2009	M2 / M5 refs
- Expenditure	720.818	57.156	22.20	777.974	
- Charges	-716.000	-104.200	22.21	-820.200	
Prepayment/(accrual)	4.818	-47.044	22.22	-44.226	2.14 / 5.7

In the section “Expected depreciation on closing assets as of 31 March 2009”, (lines 22.23 – 22.28), the gross book values and net book values are taken from Table H1. The forecast depreciation charges are calculated using the relevant NBV at 31 March 2009 and 50% of the average useful lives remaining. The H tables indicate 50.9%.

Note: CCA depreciation charges for 2010/11 to 2013/14 per the 2DBP are based on MEAV as at 31 March **2008**, plus additions for each these years. Table M22 shows the CCA depreciation charges relating to only the existing assets MEAV as at 31 March **2009** (i.e. excluding all subsequent additions). Therefore the CCA depreciation in Table M22 is not the same as in the 2DBP.

Table M23 – Interest analysis

Intercompany interest receivable/payable (line 23.1) is made up of £2.5m received from SWBSH and net payable of £0.8m to Business Stream in relation to wholesale settlements.

Other finance charges (line 23.5) is the FRS 17 statutory adjustment.

Table M24 - Turnover

Primary income (lines 24.1 – 24.13): The majority of the income types are directly identifiable with specific accounts in the SW general ledger. There is no income in any of the Non-Household categories (lines 24.3-24.10) as these categories relate to Business Stream’s activities following business separation in November 2006.

Other sources (line 24.14 onwards): Each income source representing > 3% of the other sources total has been separately identified. The balance (around 6% of the total) has been shown as “Sundry” (line 24.20). The reduction in building water supplies reflects the transfer of these services to Business Stream during 2008/09.

Table M25 – Bad Debts (Trade debtors)

This table shows the gross receivable less bad debt provision. The net receivable amounts here are taken to Table M11 (lines 11.2 & 11.4).

The amounts shown in the Wholesale/non-household trade debtors section relate to non primary wholesale revenue and sundry / other regulated income.

Bad debt provision in the year: The Household charge to the profit and loss account (line 25.7) is net of an a-typical credit of £8.1m. The movement on the sundry bad debt was a net credit to the profit and loss account.

The table below provides a breakdown of the household gross balances and bad debt provisions by age:

	96/04	04/05	05/06	06/07	07/08	08/09	Total
	£m	£m	£m	£m	£m	£m	£m
Gross Debt	128.4	24.9	27.4	29.7	34.2	52.6	297.2
Bad Debt Provision	(125.5)	(24.0)	(26.3)	(28.4)	(31.1)	(35.6)	(270.9)
Net Debt	2.9	0.9	1.1	1.3	3.1	17.0	26.3

Table M26 – Provisions analysis

The reorganisation provision (line 26.8) has increased by £2.8m because of additional VR charges for pension costs and extra staff redundancies due to restructuring of the business, particularly in Supply Chain Services, Customer Services and the rationalisation of the contracting business.

The income uncertainty provision – wholesale (line 26.9) was created in 2007/08 and relates to uncertainty around wholesale non-domestic income. This provision has increased by a net £1.3m in 2008/09. The provision reflects ongoing data quality issues associated with the operation of the wholesale market. The main areas of concern are associated with the treatment of vacant properties, the basis of calculating estimated weighted average unit rates and the impact of meter roll-overs on consumption volumes.

The other provision (line 26.10) relates to onerous leases and decreased during the year following settlement of some of the leases.

Table M27 – Consolidated HCA Income & Expenditure Account

The intercompany items being visibly eliminated (in col 3) on this table are the intercompany wholesale income in SW and the intercompany cost of sales in Business Stream. Due to an adjustment to Business Stream's cost of sales relating to the reconciliation process, there is an intercompany profit elimination along with the related tax impact. The intercompany interest between SW and Business Stream already eliminates across line 27.11.

Non core / non licensed includes the remaining non regulatory business within SW (as per table M1), the results for the 2 holdings companies (SWBSH & SWHH - interest and taxation) and SWH.

The intercompany item being visibly eliminated in col 6 relates to reversal of the write off of an investment by Business Stream. This 'investment' value was the intercompany profit on the transfer of the Business Solutions division to Business Stream and had previously been

eliminated as part of the consolidation process. All remaining intercompany interest already eliminates across line 27.11.

Appendix 1.1 provides a reconciliation between Table M27 and the statutory consolidated income and expenditure account. The differences are due to the terminology and descriptions being used.

Table M28 – Consolidated HCA Balance Sheet

The intercompany items being visibly eliminated are:

- intercompany debtor and creditor balances (lines 2.6 & 2.15);
- intercompany profit elimination and related tax impact; and
- investments in subsidiary companies and the relevant share capitals (lines 2.3 & 2.30).

The intercompany loans eliminate across line 2.2.

Non core / non licensed includes the remaining non regulatory business within SW (as per table M2), the balance sheets for the 2 holdings companies (SWBSH & SWHH – intercompany loans, investment in subsidiary, intercompany debtors and creditors, taxation, share capital and reserves) and SWH.

Appendix 1.2 provides a reconciliation between Table M28 and the statutory consolidated balance sheet. The differences are primarily due to reclassifications and grouping of various items.

4.2 M Table 18W & 18WW detailed commentary

Methodology & Cost Allocation

Cost analysis in M Tables (M18W, M18WW) was prepared using reports from Scottish Water's Activity Based Management (ABM) systems.

Detailed commentary on ABM methodology and cost allocation is provided in support of table E and is not repeated in this document.

Trading Results & Reconciliation

Scottish Water Horizons Holdings Limited (SWHH) and Scottish Water Horizons Limited (SWH), were established and commenced trading on 1 April 2008. SWHH is the intermediate holding company and owns 100% of the shares in SWH which is the operating company. SWH is responsible for the majority of the Scottish Water Group's Non Regulated activities.

Business Stream is a fully owned subsidiary of Scottish Water. Scottish Water produces group consolidated accounts incorporating the results of Business Stream. E & M18 Table financials are produced for Scottish Water Regulated and Non Regulated activity, excluding Business Stream.

To aid comparison, the table below summarises Scottish Water consolidated results, Scottish Water company and Scottish Water Horizons results.

SW Group Statutory Accounts

	£m	£m
Cost of Sales	632.7	
Admin Expenses	<u>101.8</u>	
SW Group Expenditure		734.5
Less Business Stream		(22.0)
FRS 17 adjustment		<u>3.4</u>
Total Expenditure (excluding Business Stream and FRS 17)		<u>715.9</u>
Represented by		
SW Regulated		687.9
SW Non Regulated		3.8
Horizons		24.2

E & M18W & WW Tables include the costs of Scottish Water (Core / Regulated), Scottish Water (Non Regulated) and Scottish Water Horizons (Non Regulated). The costs of business retail activity undertaken by Business Stream are not reported in Scottish Water's E or M tables.

Scottish Water company and Scottish Water Horizons combined results are summarised and reconciled below, to E tables and the regulatory account tables M18 (W & WW).

(£m)	SW	Diff	M18W/WW Tables			Diff	E1/2/3a
	Group*	Board - M18	Total	M18 W	M18 WW	M18 - E1/2/3a	Tables Total
Employment	148.1						
Other	170.2		316.3	183.3	133.0		288.9
Opex	318.2	2.0	316.3	183.3	133.0	27.4	288.9
PFI	132.6	(3.4)	136.1	0.0	136.1	0.0	136.1
IMC	104.2	0.2	104.0	76.6	27.5	0.1	104.0
Depreciation	161.7		162.0	74.5	87.5		161.3
Grant Amortisation	(1.1)	(0.2)	(1.1)	(0.7)	(0.4)	0.6	(0.9)
Amort PFI	1.6		0.0				0.0
Gain on assets	(1.5)		0.0				0.0
Expenditure	715.9	(1.5)	717.3	333.7	383.6	28.0	689.4
Explained by							
Charges to SWBS for support		1.5					

* Excludes Business Stream & FRS 17

The line differences above are explained as follows:

- £3.4m difference between our Board report and M18 Tables re PFI costs, is due to transfer of costs from Customer Operations for Intersite Sludge Tankering from Scottish Water wastewater treatment works to PFI works (£2.8m), terminal pumping station costs pumping to PFI works (£0.5m) and support costs for the PFI team (£0.1m).
- £1.5m of Scottish Water expenditure has been charged to Business Stream under Service Agreements. This cost has been netted off Scottish Water's expenditure in line with group inter-company transaction reporting. However, for the purposes of regulatory reporting this expenditure has been added back to report the full costs of providing these third party services.
- £28.0m Non Regulated expenditure is not reported in table E1 and E2.

Commentary

Total operating costs excluding PFI costs and exceptional items increased by £(51.0)m to £581.3m.

	2008/09 £m	2007/08 £m	Variance £m
Functional costs - Water M18w.34	132.406	117.716	(14.690)
Operating costs - Water M18w.43	50.866	42.736	(8.130)
Capital maintenance - Water M18w.54	150.436	123.752	(26.684)
Functional costs - Waste M18ww.35	240.235	231.849	(8.386)
Operating costs - Waste M18ww.44	28.837	26.238	(2.599)
Capital maintenance - Waste M18ww.55	114.568	118.347	+3.779
	717.348	660.638	(56.710)
exclude PFI included in M18ww.35	136.065	130.320	(5.745)
	581.283	530.318	(50.965)
Remove Exceptional costs	0.000	0.000	+0.000
	581.283	530.318	(50.965)

Detailed commentary on wholesale operating costs and efficiencies is provided in support of Annual Return Table E and is not repeated in this document.

More detailed commentary on Non Regulated and Retail activities is provided in this document.

Activity Analysis

	2008/09 £m	2007/08 £m	Variance £m
Non Regulated	27.996	27.740	(0.256)
Wholesale (excluding PFI)	508.582	465.440	(43.142)
Retail	44.705	37.138	(7.567)
	581.283	530.318	(50.965)

Non Regulated activity costs have increased by £0.3m from 2007/08 to £28.0m (£3.8m Scottish Water, £24.2m Horizons). However, cost increases were offset by an increase in total Non Regulated turnover of £0.7m from £30.7m in 2007/8 to £31.4m in 2008/9.

Direct costs have increased by £1.1m, General & Support by £0.4m and other operating expenditure has reduced by £1.2m.

The key movements in Non Regulated Operating Costs from 2007/08 were:

- External consultancy work has increased by £1.4m, due to increased hired and contracted costs (£1.8m), partly offset by the transfer of Business Solutions to Business Stream, which reduced employment costs by £0.4m. The overall cost increase was offset by increased income.
- £0.2m increase in level of recoverable works, again offset by additional income.

- There has been a decrease in the bad debt provision on non regulated services of £1.5m. This is due to an improvement in sundry billing and credit management activities since the initial transfer of sundry billing from Business Stream to Scottish Water.

Wholesale activity cost movements are explained in support of E Tables and are not repeated in this document.

Retail activity costs have increased by £7.6m.

The key movements in Retail Costs from 2007/08 were:

- In 2007/08 there was an atypical release of household bad debt provision of £17.6m, and £8.1m in 2008/09, which accounts for the majority of the increase of £9.2m in Regulated doubtful debt;
- Increase in council domestic billing and collection service of £0.2m offset by small reduction in internal costs £0.1m;
- Retail Non-infrastructure Depreciation has increased mainly due to the commissioning of wholesale/retail interface assets of £2.7m.
- Reduction in the cost of services provided to Business Stream under service agreements. This cost has been netted off Scottish Water's expenditure for the purposes of group reporting. However, for the purposes of regulatory reporting this expenditure has been added back to report the full costs of providing these third party services. This is split £1.0m operating expenditure and £0.5m capital maintenance. In 2007/08 the figure was £4.1m, split £2.6m operating cost, £1.5m capital maintenance. Core Third Party retail costs have therefore decreased by £1.6m operating expenditure and £1.0m capital maintenance;
- Reduction in retail separation, market set up and vacant property survey activity from prior year of £0.8m, partly offset by increased wholesale billing activity of £0.2m;
- Costs of Regulations have decreased by £1.1m due to a decrease in CMA costs of £1.5m, which included set-up costs in 2007/08. This decrease was partly offset by increased WICS fees of £0.3m and increased internal regulation activity of £0.1m to meet new regulatory requirements;

Retail costs by segment

	2008/09	2007/08	Variance
	£m	£m	£m
Domestic	38.274	28.360	(9.914)
Non Domestic - Measured	3.670	5.051	+1.381
Non Domestic - Non Measured	2.761	3.727	+0.966
	44.705	37.138	(7.567)

Domestic customer retail total functional and operating expenditure has increased by £9.9m. The main movements from 2007/08 were:

- In 2007/08 there was an atypical release of household bad debt provision of £17.6m, and £8.1m in 2008/09, which explains the increase of £9.2m on Regulated doubtful debt;
- Increase in council domestic billing and collection service of £0.2m offset by small reduction in internal costs £0.1m;
- Increase in WICS fees of £0.3m and in costs of internal regulation of £0.1m to meet new regulatory requirements.

Non domestic customer retail total functional and operating expenditure has reduced by £2.3m to £6.4m (£3.7m measured and £2.8m unmeasured). The main movements from 2007/08 were:

- £0.8m reduction in retail separation activities, most notably reduction in vacant property surveys £0.4m, partly offset by increase in wholesale billing activity of £0.2m;
- Costs of Regulation have decreased by £1.6m due mainly to a decrease in CMA costs;
- Reduction in the cost of services provided to Business Stream under service agreements £1.6m opex, £0.9m depreciation;
- Retail Non-infrastructure Depreciation has increased mainly due to the commissioning of wholesale/retail interface assets of £2.7m.

Since the transfer of business retail activity to Business Stream, the majority of Non Domestic costs are incurred in 3 main areas:

- Scottish Water's Wholesale Revenue Management team responsible for wholesale billing and account management, and interface with Licensed Providers and the Central Market Agency (CMA);
- The CMA costs charged to Scottish Water for set up and operation of the CMA systems and processes;
- The cost of providing services to Business Stream under service agreements.

Scottish Water does not have access to business customer details. However, Scottish Water does have knowledge of properties and services. Therefore the costs of activities are allocated to customer and service, primarily on the basis of properties and services volumes, except where activities are clearly attributable to one service, e.g. trade effluent billing service.

The cost of handling customer calls has been split by service based on the number of calls. Licensed Providers are now responsible for handling calls from business customers. The cost of initial customer contact related to wholesale activities will be incurred by Licensed Providers. However, where Licensed Providers require information or action from the wholesaler, this is the responsibility of the wholesaler. In this case the costs of calls are included under wholesale activities, e.g. water distribution includes the cost of all customer contact on this type of activity, e.g. low pressure calls, water rising calls. Therefore, no cost is shown in line M18WW.29 and M18W.30 under retail.

Retail	2008/09	2008/09	2007/08	2007/08
	£m	%	£m	%
Water - Domestic	18.884	42%	14.123	38%
Water - Non Domestic	3.404	8%	4.616	12%
Wastewater - Domestic	19.390	43%	14.237	38%
Wastewater - Non Domestic	3.027	7%	4.162	12%
	44.705		37.138	

The split of Retail operating costs between water and wastewater level has remained consistent with 2007/08 (50% water, 2008/09 versus 50%, 2007/08).

Scottish Water
Year ended 31 March 2009
Reconciliation of Regulatory Accounts / M Tables to Consolidated Statutory Accounts

Table M27			Statutory Accounts		
Line	Description	Consolidated £m (3dp)	Consolidated £m (1dp)		
27.1	Turnover	1094.619	1094.6	Turnover	
27.2	Operating costs	-336.924			
27.3	PPP costs	-131.972			
27.4	Historical Cost Depreciation	-162.401	-632.7	Cost of sales	
27.5	Infrastructure Renewals charge	-104.200			
27.6	Amortisation of PFI assets	-1.634	-101.8	Administrative expenses	
27.7	Amortisation of deferred income	1.067			
27.8	Operating income	1.507			
		-734.557	-734.5		
27.9	Operating profit	360.062	360.1	Operating surplus on ordinary activities before interest	
			-149.9	Net interest payable	
			-1.4	Other finance income	
27.11	Net interest receivable less payable	-151.319	-151.3		
27.12	Profit on ordinary activities before taxation	208.743	208.8	Surplus on ordinary activities before taxation	
27.13	Taxation - current	-5.406			
27.14	Taxation - deferred	-58.505			
		-63.911	-63.9	Taxation	
27.19	Retained profit for year	144.832	144.9	Retained surplus for the financial year	

Scottish Water
Year ended 31 March 2009
Reconciliation of Regulatory Accounts / M Tables to Consolidated Statutory Accounts

Table M28		Reallocations / Reclassifications:						Statutory Accounts	
Line	Description	Consolidated £m (3dp)	Infra Ren Ppyt	PFI assets	CT debtor	Def Inc <> 1yr	roundings	Consolidated £m (1dp)	
	Fixed Assets								
2.1	Tangible Assets	4,296.018	-42.2					4,253.8	Tangible fixed assets
2.2	Investment - loan to group company	0.000							
2.3	Investment - Other	0.053							
2.4	Total fixed assets	4,296.071						4,253.8	
	Current Assets								
2.5	Stocks	3.153						3.2	Stock
2.6	Debtors	135.891		32.2	0.5			168.6	Debtors
2.7	Cash at bank and in hand	75.237						75.2	Cash at bank and in hand
2.8	Short term deposits	0.000							
2.9	Gilts reserve	0.000							
2.10	Assets transferred to PPP contractors	32.233		-32.2					
2.11	Infrastructure Renewals prepayment	0.000							
2.12	Total current assets	246.514						247.0	
	Creditors: amounts falling due within one year								
2.13	Overdrafts	0.000							
2.14	Infrastructure Renewals accrual	-42.226	42.2						
2.15	Creditors	-288.171				-5.3		-293.5	
2.16	Borrowings (excl. Govt. loans)	-2.934						-2.9	
2.17	Corporation tax payable	-2.163			-0.5			-2.6	
2.18	Customer retained earnings payable	0.000							
2.19	Total creditors	-335.494						-299.0	Creditors: amounts falling due < 1 year
2.20	Net current assets	-88.980						-52.0	Net current liabilities
2.21	Total assets less current liabilities	4,207.091						4,201.8	Total assets less current liabilities
	Creditors: amounts falling due after one year								
2.22	Borrowings (excl. Govt. loans)	-7.130						-7.2	
2.23	Other creditors	-39.002				-24.6		-63.6	
2.24	Total creditors	-46.132						-70.8	Creditors: amount falling due > 1 year
	Provision for liabilities & charges								
2.25	Deferred tax provision	-300.795						-300.8	Deferred taxation
2.26	Deferred income - grants and contributions	-29.935				29.9			
2.27	Post employment assets / (liabilities)	-160.804					-0.1	-160.9	Pension liability
2.28	Other provisions	-19.181					0.1	-19.1	Other provisions
2.29	Net Assets employed	3,650.244	0.0	0.0	0.0	0.0	0.0	3,650.2	
	Capital and reserves								
2.30	Govt. loans	2,842.929						2,842.9	Government loans
2.31	Income and Expenditure account	673.885						673.9	Income & expenditure account reserve
2.32	Other reserves	133.430						133.4	Other reserves
2.33	Capital & reserves	3,650.244	0.0	0.0	0.0	0.0	0.0	3,650.2	

Scottish Water
Year ended 31 March 2009
Reconciliation of Regulatory Accounts / M Tables to Consolidated Statutory Accounts (Company only)

Table M2		Reallocations / Reclassifications:					Company	Statutory Accounts
Line	Description	Total	IRA	PFI assets	CT debtor	Def Inc <> 1yr	Company	
		£m (3dp)					£m (1dp)	
	Fixed Assets							
2.1	Tangible Assets	4,291.375	-42.2				4,249.2	Tangible fixed assets
2.2	Investment - loan to group company	0.000						
2.3	Investment - Other	37.652					37.6	
2.4	Total fixed assets	4,329.027					4,286.8	
	Current Assets							
2.5	Stocks	2.904					2.9	Stock
2.6	Debtors	64.288		32.2		0.5	97.1	Debtors
2.7	Cash at bank and in hand	15.917					15.9	Cash at bank and in hand
2.8	Short term deposits	0.000						
2.9	Gilts reserve	0.000						
2.10	Assets transferred to PPP contractors	32.233		-32.2				
2.11	Infrastructure Renewals prepayment	0.000						
2.12	Total current assets	115.342					115.9	
	Creditors: amounts falling due within one year							
2.13	Overdrafts	0.000						
2.14	Infrastructure Renewals accrual	-42.226	42.2					
2.15	Creditors	-274.479				-1.8	-276.3	
2.16	Borrowings (excl. Govt. loans)	-2.934					-2.9	
2.17	Corporation tax payable	0.522			-0.5		0.0	
2.18	Customer retained earnings payable	0.000						
2.19	Total creditors	-319.117					-279.2	Creditors: amounts falling due < 1 year
2.20	Net current assets	-203.775					-163.3	Net current liabilities
2.21	Total assets less current liabilities	4,125.252					4,123.5	Total assets less current liabilities
	Creditors: amounts falling due after one year							
2.22	Borrowings (excl. Govt. loans)	-7.130					-7.2	
2.23	Other creditors	-38.502				-19.3	-57.8	
2.24	Total creditors	-45.632					-65.0	Creditors: amount falling due > 1 year
	Provision for liabilities & charges							
2.25	Deferred tax provision	-301.631					-301.6	Deferred taxation
2.26	Deferred income - grants and contributions	-21.124				21.1		
2.27	Post employment assets / (liabilities)	-160.450					-160.5	Pension liability
2.28	Other provisions	-18.731					-18.7	Other provisions
2.29	Net Assets employed	3,577.684	0.0	0.0	0.0	0.0	3,577.7	
	Capital and reserves							
2.30	Govt. loans	2,784.429					2,784.4	Government loans
2.31	Income and Expenditure account	659.825					659.9	Income & expenditure account reserve
2.32	Other reserves	133.430					133.4	Other reserves
2.33	Capital & reserves	3,577.684	0.0	0.0	0.0	0.0	3,577.7	

Scottish Water
Year ended 31 March 2009
Reconciliation of Regulatory Accounts / M Tables to Consolidated Statutory Accounts (Company only)

Statutory Accounts Company	Expand detail	Reallocations / Reclassifications:				CCA Adj	Less - Non Reg	Regulatory Tables			
		categories	<> 1 year	Interco				M 11	M 5	Line	Description
£m	£m	£m	£m	£m	£m	£m	£m	£m	£m		
Note 12											
Stocks	2.9						0.0	2.9		11.1	Stocks
Note 13 Debtors											
<i>Amounts falling due < 1 year</i>											
Trade debtors	29.5	-29.5									
Other debtors	22.6	-22.6									
Prepayments & accrued income	13.2		0.8		0.7		0.0	14.7		11.6	Prepayments & other short term debtors
Corporation tax	0.5										
Amounts due from subsidiaries	0.7				-0.7						
Loans to subsidiaries	0.0								0.0	5.14	Investment - loan to group company
Trade debtors - household		26.3						26.3		11.2	Trade debtors - household
Other trade debtors		3.2					-0.9	2.3		11.4	Other trade debtors
Other debtors - operating		2.4	-0.8	-1.6							
Other debtors - non operating		20.2							20.2	5.12	Non trade debtors
	66.5										
<i>Amounts falling due > 1 year</i>											
PFI assets	30.6			1.6					32.2	5.11	Assets transferred to PPP contractors
Total debtors	97.1										
Note 14 Creditors											
<i>Amounts falling due < 1 year</i>											
Non-government loans	-2.9								-2.9	5.9	Borrowings (excl Govt loans) (<1year)
Trade creditors	-23.9				-1.1			-25.0		11.7	Trade creditors
Capital creditors and accruals	-27.7				-24.5			-52.2		11.10	Short-term capital creditors
Accruals	-126.1	126.1									
Payments received in advance	-31.2		31.2								
Other creditors	-10.0		10.0								
Deferred income	-1.8			1.8							
Other taxes & social security	-2.7		2.7								
Amounts due to subsidiaries	-28.4				28.7		-0.3				
Amounts due to SWS	-24.5				24.5						
Wholesale charge prepayment			-0.1		-27.6			-27.7		11.8	
Credit note provision		-18.1						-18.1		11.11	
Accruals - operating		-73.9	-2.7					-76.6		11.12	Accruals & other creditors
Other creditors - non operating		-34.1	-41.1				-0.4		-75.6	5.13	Non trade creditors due < 1 year
	-279.2										
<i>Amounts falling due > 1 year</i>											
Non-government loans	-7.2								-7.2	5.19	Borrowings (excl Govt loans) (>1year)
Other creditors	-38.5								-38.5	5.20	Other creditors
Deferred income	-19.3			-1.8		-1.6			-22.7	5.2	Third party contributions
	-65.0										
Total creditors	-344.2										
Check total	-244.2	0.0	0.0	0.0	0.0	-1.6	-1.6	-153.4	-94.5		

