



Northern Ireland Water Limited

**Auditors' Report and
Commentary on the Annual
Information Return
Year ended 31 March 2009**

Notice about this report

This report is made solely to the Board of Directors of Northern Ireland Water Limited and to the Northern Ireland Authority for Utility Regulation in accordance with our engagement letter dated 7 May 2009. Our work has been undertaken so that we might state to the Board of Directors of Northern Ireland Water Limited and the Northern Ireland Authority for Utility Regulation those matters we are required to state to them in this report and for no other purpose. To the fullest extent permissible by law we do not accept or assume responsibility to anyone other than the Board of Directors of Northern Ireland Water Limited and to the Northern Ireland Authority for Utility Regulation for our work, this report or for the opinions we have formed.

5 August 2009

This report contains 32 pages

NI Water Long Form Report - Final - 5 August 2009.doc

See Notice about this Report on page 1

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1 Notice about this report

- 1.1.1 Where no guidance has been given to auditors, we have assumed that comment is not required on these tables and have therefore not included these within the scope of our work.
- 1.1.2 This report is confidential and has been prepared solely for the purpose of Northern Ireland Water Limited ('NIWL') and The Northern Ireland Authority for Utility Regulation ('NIAUR') (the Beneficiaries), and has been released to the Beneficiaries on the basis that it will not be copied or disclosed to any third party or otherwise quoted or referred to, in whole or in part, without our written prior consent.
- 1.1.3 This report is not suitable to be relied on by any party wishing to acquire rights against KPMG (other than the Beneficiaries) for any purpose or in any context. Any party other than the Beneficiaries that obtain access to this report or a copy (under the Freedom of Information Act 2000 or otherwise) and chooses to rely on this report (or any part of it) does so at their own risk. To the fullest extent permitted by law, KPMG does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Beneficiaries.
- 1.1.4 The contents of the report should not be taken as reflecting the views of KPMG except where explicitly stated as being so.
- 1.1.5 To a certain extent the content of this report comprises general information that has been provided by, or is based on discussions with management and directors of the Company. Except to the extent necessary for the purposes of the audit, this information has not been independently verified.
- 1.1.6 [Section 1.1.6 has been redacted].
- 1.1.7 The Statutory Accounts for the year ended 31 March 2009 were approved by the Board of Directors and signed on 30 June 2009. The Regulatory Accounts for the year ended 31 March 2009 were approved by the Board of Directors and signed on 28 July 2009.
- 1.1.8 This report should be read in conjunction with the Annual Information Return prepared by NIWL for the year ended 31 March 2009.

This report is made to NIAUR in accordance with the terms of our engagement dated 7 May 2009.

2 **Report of the Independent Auditors to Northern Ireland Water Limited and the Northern Ireland Authority for Utility Regulation**

We have reviewed the Regulatory Accounts tables 6a, 18 to 31, 33, 34 and 39 set out in the Annual Information Return in respect of Northern Ireland Water Limited (“the Company”).

This report is made to the Company in accordance with the terms of our engagement letter dated 7 May 2009 (the “Contract”). This report is made also to the Northern Ireland Authority for Utility Regulation (the “Regulator”) in order to meet the requirements of the Instrument of Appointment by the Department for Regional Development of Northern Ireland Water Limited as a water and sewerage undertaker under the Water and Sewerage Services (Northern Ireland) Order 2006 (the “Regulatory Licence”) and to enable the NIAUR to verify that a report from independent auditors has been issued in connection with the Regulatory Accounts tables 6a, 18 to 31, 33, 34 and 39. Our work has been undertaken so that we might state to the Company and to the NIAUR those matters we have been engaged by the Company to state in this report and for no other purpose.

This report has been released to the Company and to the NIAUR on the basis that it shall not be copied, referred to or disclosed, in whole (save for the Company’s or the NIAUR’s own internal purposes) or in part, without our prior written consent. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company for our work, for this report, or for the opinions we have formed. We will accept such responsibility to the NIAUR on condition that the NIAUR agrees in writing to the Contract by signing the notice appended to the Contract.

Respective responsibilities of directors and auditors

The Company’s directors are responsible for the preparation of the Regulatory Accounts tables.

Our responsibilities, as independent auditors, are established in the United Kingdom by relevant legal and regulatory requirements and the Contract and the Accounting Guidelines and other relevant material issued by the NIAUR. It is our responsibility to form an independent opinion based on our review, on those tables and to report our opinion to the Company and (on the basis set out above) to the NIAUR.

Basis of opinion

We conducted our review in accordance with the Regulatory Accounting Guidelines, the Annual Information Return reporting requirements dated March 2009 and other relevant material issued by the NIAUR and the Contract. A review includes examination, on a test basis, of evidence relating to the amounts and disclosures in the Regulatory Accounts tables. It also includes an assessment of the significant estimates and judgments made by the Company’s directors in the preparation of the Regulatory Accounts tables, and of whether the accounting policies are appropriate to the Company’s circumstances, consistently applied and adequately disclosed.

We planned and performed our review so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Regulatory Accounts tables are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the Regulatory Accounts tables in terms of UK Generally Accepted Accounting Principles and the Regulatory Accounting Guidelines.



Opinion

Based upon our view, in our opinion, the Regulatory Accounts tables contain the information for the year to 31 March 2009 required to be submitted to the NIAUR by the Company to comply with Condition F of the Regulatory Licence and are materially consistent with the information submitted to NIAUR in the Regulatory Accounts.

A handwritten signature in black ink, appearing to read 'KPMG'.

KPMG
Chartered Accountants
Belfast
5 August 2009

3 Part A – General Procedures

Requirement (followed by our commentary for each procedure listed)

3.1 **From discussions with management and sight of underlying documentation, describe the NI Water's sign off procedures. Describe the nature of the underlying documentation observed.**

3.1.1 We note that system and processes for the production and review of information of the Annual Information Return ('AIR') are still under development. In particular there is a general point to note that in terms of apportioning costs, empirical and historical evidence to support the apportionment needs to be further developed by the Company over time. We do note however, in section 4.3.1 of this report that the methodology in respect of allocating general support expenditure has been refined in the current year allowing a more accurate allocation of costs than in the prior year.

Each table was allocated an owner within the Finance and Regulation Directorate (FRD), who was responsible for populating the table with the relevant data in line with the AIR Reporting Requirements and Definitions Manual 2009. A separate member of the FRD was then required to review each table and ensure completeness and accuracy of the information contained within.

Ongoing briefings were made to the Executive Team, Audit Committee and Board to update them on progress being made.

Final tables and commentaries were approved (in conjunction with the Regulatory Accounts) by the Director of Finance and Regulation and then by the Audit Committee and Board, which met on 27 July 2009. This ensured consistency of approach.

3.2 **For each Regulatory Table*, check that NI Water has complied with Definitions Manual or has included a commentary as to why the guidance has not been followed. (*we have considered only those tables on which we are required to report – as set out in the pro-forma Auditors' report on page 2).**

3.2.1 For each of the tables/elements of tables where the Auditors' had specific responsibilities (as referred to in Sections B-G of the Auditors' guidance, and reported on in our Auditors' Report (tables 6a, 18 to 31, 33, 34 and 39)), we carried out procedures to satisfy ourselves that the requirements of the guidance had been complied with. We noted that management have reported the following exceptions:

3.2.2 **Part A General Procedures**

No significant issues noted.

3.2.3 **Part B Activity Cost Analysis**

NIAUR has requested sub-analysis of tables 21 (Activity Costing Analysis – Water) and 22 (Activity Costing Analysis – Sewerage) for the year ended 31 March 2009. This sub-analysis requires separate disclosure of NIW only costs and PPP only costs. In the prior year, NIW total costs only were submitted.

[Section 3.2.3 paragraphs 2, 3, 4 and 5 have been redacted].

3.2.4 **Part C Pensions**

The Company has not carried out an exercise to separately analyse staff members included in the Pension Scheme between those involved in Appointed and Non-

Appointed activities, and consequently have not analysed the pension asset or the associated net interest cost between Appointed and Non-Appointed. Management have provided full explanation in their commentary to Tables 21 and 22 and believe the cost of calculating the impact for these members in isolation to be unjustified. Management note in their commentary that in the process of apportioning costs (including total wages, salaries and pensions) to unappointed activities it is assumed that an element of this apportionment will cover pension costs. An exact split between appointed and unappointed pension costs cannot be determined as all operating costs in aggregate (including pension costs) are allocated to unappointed activities based on unappointed activity turnover.

3.2.5 **Part D Income**

Management have been unable to assess the accuracy of accrued income or show 'the actual income billed compared to the amount accrued in the previous year', as the required information is not yet available from the Rapid Xtra billing system to compare year end provisions to actual bills raised post year end.

The company has to date experienced delays in issuing bills. Management are taking steps to rectify this and expect to be up to date by the end of September 2009. At this point management will implement a process to compare accrued income at the period end to subsequent billed income.

We note that significant steps have been taken in the current year by management to improve the billing and accounts receivable process however there remain a number of issues in this regard which need to be resolved by management. We note that management are taking active steps to address the remaining issues. These issues include, inter alia, the following:

- Reconciliation of meters read to bills issued in terms of both number of meters and consumption measured;
- Data cleansing in respect of legacy data from the Water Service; and
- Timely issue of bills.

3.2.6 **Part E Bad Debt**

No exceptions noted.

3.2.7 **Part F Taxation**

[Section 3.2.7 has been redacted].

3.2.8 **Part G Accounting Charges**

No exceptions noted but attention is drawn to limitations in estimation of IRC and IRE. See 9.3.1 for further comment.

3.2.9 **Part H Land Sales**

[Section 3.2.9 has been redacted].

3.2.10 **Part I Borrowings**

No exceptions noted.

3.3 **Check that management has included a commentary including an explanation for reporting requirements that do not apply to a particular company.**

3.3.1 For all tables reviewed, management has included a commentary (if applicable) including an explanation for reporting requirements that do not apply to the Company, as outlined in 3.4.1 below.

3.4 **Read NI Water's explanation of reporting requirements that do not apply and check details set out in the commentary to the underlying accounting records or other supporting documentation. Describe the nature of the underlying accounting records or other supporting documentation.**

3.4.1 [Section 3.4.1 has been redacted].

3.5 **Check that the figures reported in the Regulatory Accounts tables 6A, 18 to 31, 33, 34 and 39 in the Annual Information Return agree to the underlying accounting records and the final Regulatory Accounts.**

3.5.1 We have reviewed the tables as follows:

NB. references to the 08/09 accounts relate to the audited statutory and regulated accounts for the year ended 31/03/09.

Table	Description	Comment
Table 6A	Outstanding revenue and breakdown of customer services operating expenditure	Lines 1-28 have no figures as there was no household billing in 08/09. We have agreed lines 29, 31, 33, 43, 45, 47, 57a and 58a (for 08/09) to the Oracle nominal ledger. Lines 29, 31, 33, 43, 45 and 47 have also been agreed to the Aged Debt Listing at 31 March 2009. Household numbers in lines 30, 32 and 34 have been provided by the Rapid Xtra billing System. Comparatives (for 07/08) have been agreed to the 2008 Annual Information Return.
Table 18	Profit and Loss Account (Historical Cost Accounting)	We have agreed lines 1 to 15 (for 08/09) to the 08/09 Regulatory Accounts, to the Oracle nominal ledger and client schedules detailing adjustments made for regulatory purposes. Comparatives (for 07/08) have been agreed to the 2008 Annual Information Return.
Table 18A	[Redacted]	[Redacted]
Table 18B	[Redacted]	[Redacted]
Table 18C	Statement of total recognised gains and losses	We have agreed lines 1 to 4 (for 08/09) to the 08/09 Regulatory Accounts. The actuarial gain reported in line 2 has been agreed to the Statutory Accounts. Comparatives (for 07/08) have been agreed to the 2008 Annual Information Return.
Table 18D	Analysis of dividends and interest charges for year	Lines 1 to 3 have no figures as there were no dividends in 08/09. Lines 4 to 12 (interest analysis) could not be agreed to the Regulatory Accounts as this disclosure is not required. However the total in line 12 agrees to 'net interest payable' in the Regulatory Accounts. We have agreed lines 4 to 12 to the Oracle nominal ledger and client supporting schedules detailing adjustments made for regulatory purposes. All comparatives (for 07/08) have been agreed to the 2008 Annual Information Return.
Table 19	Balance Sheet (Historical Cost Accounting)	We have agreed lines 1 to 33 (for 08/09) to the 08/09 Regulatory Accounts except for lines 18, 19, 21, 22 and 24. This is due to specific disclosure requirements in Table 19 relating to the presentation of deferred income. However the net assets employed total in line 28 agrees to the Regulatory Accounts as it is merely a reclassification within liabilities. We have agreed all lines to the Oracle nominal ledger and client supporting schedules detailing adjustments made for regulatory purposes. Comparatives (for 07/08) have been agreed to the 2008 Annual Information Return.

Table	Description	Comment
Table 19A	Analysis of borrowings due after more than one year (Historical Cost Accounting)	<p>We have agreed the principal sum, nominal interest rate and the carrying value to the 08/09 Statutory Accounts and the carrying value to the Oracle nominal ledger.</p> <p>The principal sum and carrying value has also been agreed to the Regulatory Accounts but the nominal interest rate is not included in the Regulatory Accounts.</p> <p>The years to maturity has been agreed as the number of years from 31 March 2009 to the maturity date of 31 March 2027 per the loan note agreement. As this is a fixed rate instrument, the real coupon rate is agreed as the nominal interest rate adjusted for the RPI assumption.</p>
Table 20	Profit and Loss Account (Current Cost Accounting)	<p>We have agreed lines 1 to 16 (for 08/09) to the 08/09 Regulatory Accounts, to the Oracle nominal ledger and to client supporting schedules detailing adjustment made for regulatory purposes. Comparatives (for 07/08) have been agreed to the 2008 Annual Information Return.</p>
Table 21	Activity Cost Analysis – Water Services	<p>We have agreed lines 1 to 34 (for 08/09) to the 08/09 Regulatory Accounts except for lines 16, 23 and 24 as the Regulatory Accounting Guidelines do not specifically require this disclosure within the Regulatory Accounts.</p> <p>We have agreed the total of line 22 in table 21 and line 21 in table 22 to the Oracle nominal ledger less unappointed costs supported by client schedules. The apportionment of costs to water and sewerage has been agreed to client allocation/apportioning model.</p> <p>The sum of the total of lines 24-26 in table 22 and lines 25, 26 and 27 in table 21 have been agreed to the Oracle nominal ledger and current cost fixed asset register.</p> <p>We have confirmed the arithmetic accuracy of line 16, total business costs which is the sum of lines 13, 14 and 15. Lines 23 and 24 classify certain elements of operating expenditure included in lines 1 to 22 between infrastructure and non-infrastructure reactive and planned maintenance. This is for disclosure purposes only as lines 23 and 24 are excluded from the overall total to avoid duplication.</p> <p>[Redacted]</p>
Table 22	Activity Cost Analysis – Sewerage Services	<p>We have agreed lines 1 to 33 (for 08/09) to the 08/09 Regulatory Accounts except for lines 15, 22 and 23 as the Regulatory Accounting Guidelines do not specifically require this disclosure within the Regulatory Accounts.</p>

Table	Description	Comment
		<p>We have agreed the total of line 22 in table 21 and line 21 in table 22 to the Oracle nominal ledger less unappointed costs supported by client schedules. The apportionment of costs to water and sewerage has been agreed to client allocation/apportioning model.</p> <p>The sum of the total of lines 24-26 in table 22 and lines 25, 26 and 27 in table 21 have been agreed to the Oracle nominal ledger and current cost fixed asset register.</p> <p>We have confirmed the arithmetic accuracy of line 15, total business costs which is the sum of lines 12, 13 and 14. Lines 22 and 23 classify certain items of operating expenditure included in lines 1 to 21 between infrastructure and non-infrastructure reactive and planned maintenance. This is for disclosure purposes only as lines 22 and 23 are excluded from the overall total to avoid duplication.</p> <p>[Redacted]</p>
Table 23	Analysis of Turnover and Operating Income	We have agreed lines 1 to 21 (for 08/09) to the 08/09 Regulatory Accounts, the Oracle nominal ledger and client supporting schedules detailing adjustments made for regulatory purposes. Comparatives (for 07/08) have been agreed to the 2008 Annual Information Return.
Table 24	Balance Sheet (Current Cost Accounting)	We have agreed lines 1 to 29 (for 08/09) to the 08/09 Regulatory Accounts, the Oracle nominal ledger and client supporting schedules detailing adjustments made for regulatory purposes. Comparatives (for 07/08) have been agreed to the 2008 Annual Information Return.
Table 25	Analysis of Fixed Assets by Asset type	We have agreed lines 1 to 16 in columns 4, 8 and 9 (for 08/09) to the 08/09 Regulatory Accounts. Lines 1-16 have also been agreed to the Current Cost Fixed Asset Register plus client schedules of adjustments made for regulatory purposes. Comparatives (for 07/08) have been agreed to the 2008 Annual Information Return.
Table 26	Working Capital	We have agreed lines 1 to 13 (for 08/09) to the 08/09 Regulatory Accounts and supporting mapping schedules from the Oracle nominal ledger. Comparatives (for 07/08) have been agreed to the 2008 Annual Information Return.
Table 27	Movement on Current Cost Reserve	We have agreed lines 1 to 7 (for 08/09) to the 08/09 Regulatory Accounts except for line 3 which is the sum of £23,582k and (£144k) featured in the Regulatory Accounts. Comparatives (for 07/08) have been agreed to the 2008 Annual Information Return.
Table 28	Cash Flow Statement	We have agreed lines 1 to 23 (for 08/09) to the 08/09 Regulatory Accounts and client workings

Table	Description	Comment
		based on the Statutory Accounts. Comparatives (for 07/08) have been agreed to the 2008 Annual Information Return.
Table 29	Reconciliation of Operating Profit to Net Cash Flow	We have agreed lines 1 to 9 (for 08/09) to the 08/09 Regulatory Accounts and client workings based on the Statutory Accounts. Comparatives (for 07/08) have been agreed to the 2008 Annual Information Return.
Table 30	[Redacted]	[Redacted]
Table 31	[Redacted]	[Redacted]
Table 33	Depreciation charge by asset type	We have agreed lines 3-6 (for 08/09) to the Regulatory Accounts. We are unable to agree lines 1 and 2 to the Regulatory Accounts as the Regulatory Accounting Guidelines do not specifically require this disclosure within the Regulatory Accounts. We have agreed lines 1-2 to client supporting schedules, 3 and 6 to the Oracle nominal ledger adjusted for regulatory purposes, 5 to the Oracle nominal ledger and 4 to the CIDA system. Comparatives (for 07/08) have been agreed to the 2008 Annual Information Return.
Table 34	Analysis of non-infrastructure fixed asset additions by life categories	We have agreed lines 1-7, 9-13 and 15-19 to the CIDA system. We have reconciled lines 8 and 14 to the Regulatory Accounts and table 32.
Table 39	[Redacted]	[Redacted]

- 3.6 **Where there are subsequent changes to the Regulatory Accounts, compared to the submitted Regulatory Tables, NI Water should write to NIAUR setting out any differences between the submitted Regulatory Tables and the finalised Regulatory Accounts and the reasons for the changes. Read NI Water's explanation and agree details set out in the commentary to the underlying accounting records or other supporting documentation. Describe the nature of the underlying accounting records or other supporting documentation.**
- 3.6.1 Regulatory Accounts were signed on 28 July 2009, pre-submission of the Annual Information Return – there are no differences between the signed Regulatory Accounts and the Annual Information Return.
- 3.7 **Read NI Water's response to the Regulator's queries and check that NI Water's commentary is consistent with the Regulatory Accounts and the underlying accounting records.**
- 3.7.1 We have reviewed NIW's log of queries received from NIAUR in respect of AIR 08 and the responses provided by NIW in respect of financial tables only. All issues raised have been addressed in full and where applicable further clarification has been provided in AIR 09 commentaries.
- 3.8 **The full wording of the opinion NIAUR require for the Regulatory Accounts for 2008/09 is set out in Annex A. Where NI Water submits a set of Regulatory Accounts that does not contain this wording, NIAUR will not consider it to be compliant with licence condition F. The wording of the opinion NIAUR require for the Annual Information Return is set out in Annex B.**

3.8.1 The wording of the opinion on the Regulatory Accounts is consistent with that set out in Annex A of the Auditors Guidance. The wording of the opinion on the regulatory tables as presented on page 2 and 3 differs from that in the auditor's guidance but is consistent with that agreed between NIAUR, NIWL and KPMG in the engagement letter. The report differs due to the fact that as the Regulatory Accounts are submitted to NIAUR prior to submission of the Annual Information Return, we have removed the reference in the opinion paragraph to any expected differences between the Regulatory Accounts and the Annual Information Return, and state that these are consistent.

3.9 **NIAUR expect, given the timescales of submission for the Annual Information Return 2009, that information in the Annual Information Return submission and the Regulatory Accounts will be consistent and that auditors will be able to agree the Annual Information Return figures to the Regulatory Accounts. Where this is the case, we would expect auditors to issue an opinion confirming consistency of the information in the Annual Information Return and the Regulatory Accounts as set out in Annex B.**

If there are any material differences between the Annual Information Return submission and the Regulatory Accounts, these should be detailed and explained in a covering letter by the auditors.

3.9.1 **There are no material differences between the AIR and the Regulatory Accounts.**

4 Part B – Activity Cost Analysis (Table 21 & 22)

In line with the NIAUR guidance the following materiality has been used for Part B:

- All items excluding bad debt charge & atypicals (1% of OPEX) - £3.2m
- Bad debt charge (10% of £3.225m) - £323k
- Atypicals – all items reviewed

4.1 Read NI Water's explanation of the procedures used to allocate costs, starting from the point where such data is extracted from the general ledger. Check that this explanation is consistent with the preparation basis of the Regulatory Table and the underlying accounting records.

4.1.1 The Company's explanation of the procedures used to allocate costs is consistent with our understanding and our review and walkthrough of the allocation and apportionment model designed and implemented by the company.

We selected five expenses from Table 21 and five expenses from Table 22, obtained a breakdown by service activity for each expense selected and traced the balance back to the statutory nominal ledger to ensure that the balance was (i) complete, and (ii) accurately allocated in accordance with the company methodology as detailed in the management commentary.

Each balance could be traced from the Oracle nominal ledger through to the Regulatory Accounts and relevant tables from the Annual Information Return, and had been allocated correctly as detailed in the management commentary.

Furthermore, a reconciliation was carried out on the Oracle nominal ledger in order to ensure that all statutory operating costs less any un-appointed costs were accounted for correctly within tables 21 and 22. This reconciled and all relevant costs had been included.

4.2 For any judgements, apportionments or adjustments identified by management in (1), agree that these are consistent with the basis of preparation of the Regulatory Table and, where relevant, the underlying accounting records.

4.2.1 Operating costs are downloaded from Oracle by nominal ledger code into an excel spreadsheet where they are allocated to services (i.e. Water or Sewerage) and then service areas (i.e. Resources and Treatment, Distribution). As some general support expenditure can not be directly mapped to service areas, a basis of apportionment is used to attribute a fair proportion of overhead costs to each area. The allocations and apportionments are identified by management within the commentary to tables 21 and 22. Based on our testing, we noted that these were consistent with the basis of preparation of the Regulatory Table and, as appropriate, with the underlying accounting records. The cost allocation methodology is consistent with the prior year.

- 4.3 **Obtain management's commentary for changes in judgements, apportionments or adjustments when compared with the prior year. Read NI Water's commentary and, where relevant, agree details set out in the commentary to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.**
- 4.3.1 The methodology in respect of allocating general support expenditure for tables 21 and 22 has been refined in the current year, as outlined in the management commentary, allowing a more accurate allocation of costs. This has reduced the amount of "indirect" general support expenditure apportioned on the basis of total direct costs in the absence of specific cost drivers from approximately £51m in 2008 to £12m in 2009. The approach adopted is in line with our understanding of the key cost drivers within the business. However, we understand that a cost allocation project is currently underway to refine the process and provide increased granularity of information.
- 4.4 **Obtain management's commentary on all items noted as being 'exceptional' or 'atypical'. Read NI Water's commentary and, where relevant, agree details set out in the commentary to the underlying accounting records or other supporting documentation. For atypical item, compare costs in the report year with historic actual costs for that item. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.**
- 4.4.1 Management has identified one item (£0.2m decrease in flooding provision no longer required) in the year that they consider atypical for AIR reporting purposes. No exceptional items have been identified. The commentary provided is consistent with our understanding of the basis for the provision. The movement in the provision has been supported by management assessment and reconciled to the Oracle nominal ledger.
- We note that classification of atypical and reorganisation costs for AIR purposes are not consistent with the Statutory Accounts. Management have identified a £0.2m decrease in one environmental provision as atypical in nature for AIR purposes; however the Statutory Accounts show a net increase in environmental, public liability and contractual provisions of £0.9m.
- 4.5 **Obtain management's capitalisation policy which should also highlight any changes from the prior year. Read NI Water's commentary and check that it is consistent with the policies applied in the Regulatory Accounts and the underlying accounting records.**
- 4.5.1 There has been no change in management's capitalisation policy which is detailed in the commentary to tables 21 and 22. The commentary is consistent with the policies applied in the Regulatory Accounts and the underlying accounting records and agrees to the capitalisation guidance published by NIWL. Project sampling performed during the statutory audit fieldwork confirmed that this is the policy being applied.
- 4.6 **Trace the costs relating to 'movements in provisions' (including legal provisions) to the Regulatory Accounts and the underlying accounting records.**
- 4.6.1 All material movements in provisions have been agreed to the Regulatory Accounts, statutory nominal ledger and client schedules based on legal advice and management assessment.

4.7 Obtain management's commentary in relation to reorganisation costs which should include a brief description of what costs have been included (split between redundancy costs and pension strain etc.) along with details of when the expenditure is expected to be incurred. Read NI Water's commentary and, where relevant, agree details set out in the commentary to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.

4.7.1 The Company have noted three reorganisation costs in their commentary. The Business Improvement Programme ('BIP') consists of a series of major projects set up with an aim to meet or exceed performance levels of similar English and Welsh water companies. These costs have no redundancy or pension element. Costs in respect of the Voluntary Early Retirement (VER) programme have been split into pension and non-pension elements and the Company have noted how much has been paid and accrued at the year end.

The provision for contract termination costs represents management's best estimate of costs to be incurred in respect of the early termination of a supplier contract.

All three costs have been agreed as included in operating expenditure in the Regulatory Accounts and reconciled to the Oracle nominal ledger. The expected timing of expenditure has been disclosed in the commentary to tables 21 and 22, if known.

4.8 To the extent not covered by Ofwat's RAG 5.04 work on transfer pricing, check if any adjustment has been made to exclude non-appointed business costs from the Regulatory Accounts Table. Agree the adjustment to the underlying accounting records and/or the Regulatory Accounts.

4.8.1 The Company excludes non-appointed operating costs (£3,037k) from the activity cost tables in the Regulatory Accounts. The activity costs reported in the AIR have been reconciled and agreed to both Statutory and Regulatory Accounts. The amount deemed non-appointed has been agreed to client apportioning schedules.

5 Part C – Pensions (Table 18, 18d, 19, 21, 22 & 24)

In line with the NIAUR guidance, 5% of the FRS17 operating profit charge (5% of £11,626k = £581k) has been used as materiality for Part C.

- 5.1 **Obtain an explanation of the procedures used to allocate costs, starting from the point where such data is extracted from the general ledger. Check that NI Water's explanations and, in particular the apportionments of the FRS17 charge across several lines in tables 21 and 22, is consistent with the Regulatory Accounts and the underlying accounting records.**
 - 5.1.1 An explanation of the procedures used to allocate costs including pension costs, is included in the commentary for tables 21 and 22. Tables 21 and 22 have been agreed to the Regulatory Accounts as detailed in section 3.5.1 and reconciled to NIWL's Oracle nominal ledger. Pension costs for those employees who can be directly attributed to service or business activities are directly mapped to these areas via the wages and salaries codes. However pension costs that relate to either employees not engaged directly on service/business activities or that relate to past service costs have been apportioned to activities in line with the treatment of general and support expenditure. We have not identified any inconsistencies between the Company's explanations, the Regulatory Accounts and underlying information.
- 5.2 **Check that an adjustment has been made for employees who are outside of the appointed business.**
 - 5.2.1 Management have been unable to separate out the FRS17 charge or the pension asset relating to those employees in the non-appointed business. However, these employees represent a small minority of the total number in the scheme and any allocation is not expected to be material. The commentary to tables 21 and 22 notes this departure from reporting requirements.
- 5.3 **Check that the amounts included for the interest cost in table 18d and the balance sheet position in tables 19 and 24 can be agreed to the Regulatory Accounts, and where relevant the pension disclosure notes provided by NI Water's actuary.**
 - 5.3.1 Tables 18d, 19 and 24 have been agreed to the Regulatory Accounts and pension disclosure notes provided by the Company's actuary where applicable.
- 5.4 **Where any apportionments are identified in 5.1 and 5.3, obtain from management a commentary identifying any changes in apportionment policy from the prior year. Agree the new basis to the basis of preparation of the Regulatory Accounts.**
 - 5.4.1 Pension costs have not been split between Appointed and Non-Appointed business, as set out in 5.1 above – therefore no apportionments have been made in relation to pension costs.

- 5.5 **Obtain NI Water's commentary on the comparison of actual contributions to those set out in the final determination. Read NI Water's explanation and agree details set out in the commentary to the underlying accounting records or other supporting documentation. Describe the nature of the underlying accounting records or other supporting documentation.**
- 5.5.1 The Company's commentary to tables 21 and 22 states an employer's contribution rate of 29.3% (2008: 29.3%). We have tested and confirm that this is the rate at which contributions are being paid. This is the contribution rate specified in the Schedule of Contributions as agreed by the company, scheme trustees and actuary.
- 5.6 **Through discussions with management, comment on any changes to future contribution levels that have been agreed with the pension scheme trustees which will commence after the year-end. If changes are noted, provide details and the details of supporting documentation that was made available.**
- 5.6.1 Future levels of contributions have yet to be agreed. However note 26 of the statutory accounts indicates that management anticipate 2009/2010 contribution levels to remain in line with 2008/2009 (£11.5m) which is based on the Schedule of Contributions agreed by the actuary.
- 5.7 **For defined benefit schemes, trace the level of cash contributions stated by NI Water to the underlying accounting records.**
- 5.7.1 Cash contributions for the defined benefit scheme have been agreed to bank statements, as having been paid.
- 5.8 **Where NI Water contributes to both a defined benefit and a defined contribution scheme, check the split to the underlying accounting records.**
- 5.8.1 The Company does not have a defined contribution scheme.
- 5.9 **Trace any lump sum contribution to the underlying accounting records and NI Water's commentary.**
- 5.9.1 Additional lump sum contributions totalling £3.7m were paid into the Company Pension Scheme during the year. These contributions covered the costs of augmenting pensions in line with the Voluntary Early Retirement (VER) Scheme, as calculated by the scheme actuary. Such contributions have been agreed to bank statements as paid in the year and reconciled to the Oracle nominal ledger.
- 5.10 **Obtain from NI Water, detail of changes in actuarial assumptions underpinning the FRS17 valuation that have occurred since the previous year-end. Agree these assumptions to the FRS17 report provided by NI Water's actuary.**
- 5.10.1 We note that, as disclosed in Note 26 to the statutory accounts, prior to February 2009 members had the option of transferring their past service benefits from the Principal Civil Service Pension Scheme (NI) to the new NIWL pension scheme. The company had assumed in 07/08 that 50% of employees would transfer past service benefits and the actuary had therefore presented the sensitivities of the pension liability to a variation in the assumed level of transfer. However, the actual take up rate was significantly lower (approximately 20%). The 08/09 disclosures have reflected this outcome by recognising the obligation to take on members' PCSPS (NI) accrued rights and making provision for the expected amount of bulk transfer payments in

assets. All other changes in actuarial assumptions have been agreed to the FRS 17 report provided by NIW's actuary.

5.11 Where there has been a change in the level of contributions within the year, check that management has included a commentary on the difference in the relative amount of contributions being used to fund any deficit. If changes are noted, provide details and the details of supporting documentation that was made available.

5.11.1 There has been no change in the level of contributions within the year.

6 Part D – Income (Tables 23 and 26)

In line with the NIAUR guidance 0.1% of turnover (i.e. £327k) has been used as materiality for Part D.

6.1 **Read management's reconciliation and commentary of the amounts billed to the reported turnover. Where there are adjustments, (other than for the measured income accrual) management's commentary should set out whether these are one-offs for the current year or repeated. Where the adjustments occur annually, management should comment on the size of the adjustment compared to the previous year. Read NI Water's commentary and agree details set out in the commentary to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.**

6.1.1 [Section 6.1.1 paragraph 1 has been redacted].

Management have made specific reference to three balances within their commentary to Table 23, which required further explanation to the user. Firstly, £219,028k is included as 'unmeasured household income' – this relates entirely to subsidy income from DRD provided in lieu of domestic charging in 2008/09. Secondly, the £76,733k included as 'measured non-household income' comprises £47,233k non-domestic billed income and a further £29,500k of subsidy income received from DRD in lieu of phased charges. Finally, £17,150k subsidy income from DRD in respect of road drainage is included in the total balance of £17,850k shown as 'other sources'.

6.2 **Based on discussion with management and sight of underlying documentation, describe NI Water's procedures for monitoring revenue, including who reviews the revenues against the SBP and forecasts, the process for identification of variances and whether any sensitivity analysis takes place. Describe the nature of the underlying documentation observed.**

6.2.1 Measured and unmeasured water and sewerage revenue are monitored against the budgetary position on a monthly basis and variances investigated. This process is undertaken by representatives from Financial Accounts, Management Accounts and Customer Services. Monthly variances are also reviewed by the Finance Director and Customer Services Director, who subsequently prepare a report for submission to the Board. The annual budget is based on the SBP, after adjusting for a change in revenue mix given the deferral of domestic charges, not anticipated when the original plan was set in 2007. No formal sensitivity analysis is performed. However, as noted in the commentary to Table 23, the monitoring process has improved in 2008/09 with the use of the Dynamic Consumption Report and quarterly re-forecasting. This report allows underlying trends in consumption to be compared to the volumetrics underpinning the budgeted information and can provide logical explanations for under/over achievement in revenue targets. Management reviewed the Dynamic Consumption Report in conjunction with usage records for the company's top customers on a weekly basis during Quarter 3. This resulted in a £6m reduction in forecast revenue for 2008/09. These reforecast revenue levels were presented to the Board of Directors at the end of Quarter 3 to highlight the impact of the decline in customer consumption.

- 6.3 **Obtain the commentary given by NI Water on both revenue reported and to explain variances between the actual and forecasted revenue in the SBP. Read NI Water's explanation and agree details set out in the commentary to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.**
- 6.3.1 The Company have noted in their commentary that total revenue for 2008/09 was £7.9m (2.3%) below budget. The majority of this movement may be attributed to the measured water and sewerage (excluding subsidy income) category where customer numbers and average consumption have both fallen against budget, primarily as a result of the downturn in the economy. Customers in general have reduced their usage, while certain businesses have also ceased trading. Actual revenue figures have been agreed to the Oracle nominal ledger. Budget figures are those set by the tariff group and explanations in respect of turnover variances are those provided by the Customer Service Team.
- 6.4 **Obtain management's commentary on the basis of the measured income accrual. Read NI Water's commentary and agree the accrual and supporting details set out in the commentary to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.**
- 6.4.1 The commentary on the basis of the measured income accrual was reviewed and is consistent with our understanding established during the statutory audit. The level of measured income accrual noted for 08/09 has been agreed to the Oracle nominal ledger.
- 6.5 **Where management has calculated a retrospective review of the previous year's accrual compared to the amounts actually billed, agree the amounts reported to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation. Where management are not able to complete a retrospective review of the previous year's accrual, ensure that NI Water has included an explanation of the reasons for this in their commentary.**
- 6.5.1 [Section 6.5.1 has been redacted].

7 Part E – Bad Debt (tables 6a and 21)

In line with the NIAUR guidance the following materiality levels have been used for part E:

- Bad debt charge – movements of +/- 10% of bad debt charge i.e +/- £17k
- Write offs – movement of +/- 0.1% of turnover i.e. +/- £327k
- Revenue outstanding – movement of +/- 1% of turnover i.e. +/- £3.27m
- We have assumed a materiality threshold of 0.1% of turnover for customer services operating expenditure i.e £327k

General Procedures

- 7.1 **Obtain NI Water's commentary on whether the data has been extracted directly from their billing systems or whether numbers have been manually calculated or adjusted in some way, for example to allocate data between households and non-households. Read NI Water's explanation and agree details of any assumptions or apportionment stated in the basis of preparation to the underlying accounting records or other supporting documentation. Describe the nature of the underlying accounting records or other supporting documentation.**
- 7.1.1 The data illustrated on lines 29 and 43 of Table 6a summarise revenue outstanding from non-households only. Household billing had not commenced in 08/09 therefore no such income has been recognised and as such there is no outstanding revenue at the year end.
- 7.1.2 [Section 7.1.2 has been redacted].
- 7.1.3 [Section 7.1.3 has been redacted].
- 7.1.4 The nominal ledger figure is £722k greater than the Rapid Xtra Debtors Ledger figure due to test meters which have been recognised in the Oracle nominal ledger but are not yet billed (£1,696k) on Rapid Xtra, offset by write-offs in relation to over billed income (£885k) and an adjustment in respect of potentially irrecoverable debt (£89k) currently in dispute. Approximately 75% (£1.2m) of the test meter debt still to be billed (£1,696k) has been provided for at 31 March 2009.
- 7.1.5 The information for revenue written off of £170k populated in lines 57a and 58a has been extracted directly from the nominal ledger.
- 7.1.6 The customer services operating expenditure of £16,873k in line 59 has been agreed as the total of line 13 in Table 21 and line 12 in Table 22. This total has been agreed to the Regulatory Accounts.
- 7.2 **Trace the data to NI Water's accounting records/billing systems. Describe the source of the underlying accounting records or billing systems that data has been agreed to.**
- 7.2.1 The total revenue outstanding detailed in lines 29 and 43 agree to the Oracle nominal ledger which agrees to the Regulatory Accounts. The reconciliation between the Oracle nominal ledger and the Rapid Xtra billing system has only operated for the

last three months of the year. We have reviewed this reconciliation which given its early stage requires further refinement and time to develop.

- 7.3 **Obtain NI Water's commentary on any changes in reporting methodologies (for example, apportionments used in calculating outstanding revenue collection operating expenditure) from year to year and the effect this will have on the data reported in the current, past and/or future years. Read NI Water's explanation and agree details set out in the commentary to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.**
- 7.3.1 Three new income streams have been created since the prior year. These new income streams relate to unmeasured non-domestic water income, measured non-domestic sewerage income and unmeasured non-domestic sewerage income. As a result 08/09 and 07/08 figures are not directly comparable. The income split by category has been agreed to the Oracle nominal ledger. Explanations for variances provided by management supports our understanding of the debtors/income process established during the statutory fieldwork.
- 7.4 **For any changes in methodology check that the previous years' data has been adjusted. If previous years' data has not been adjusted, discuss with management and state NI Water's reasons for this.**
- 7.4.1 There have been no changes in methodology that require an adjustment to prior year figures. However, a more detailed analysis of income is available for the year ended 31 March 2009 as outlined in 7.3.1 above. This information is not available in respect of the prior year ended 31 March 2008.

Specific procedures – revenue outstanding

- 7.5 **Describe the nature of the revenue outstanding reported in lines 1 to 56 (i.e. confirm that the definition of 'revenue outstanding' as set out in NI Water reporting requirements had been adhered to) of the Regulatory Table 6a and state where this information has been extracted from.**
- 7.5.1 Domestic billing has been postponed until 09/10; hence lines 1-28 remain blank. The revenue outstanding reported in line 29 is that of non-domestic measured water, measured sewerage and trade effluent billing. This is further broken down in lines 31 and 33. The revenue outstanding per line 43 is that of non-domestic unmeasured water and sewerage. This information has been extracted directly from the statutory accounts nominal ledger. Information is posted into the nominal ledger on a monthly basis from the information pack derived from the Rapid Xtra billing system.
- 7.6 **Check that the revenue outstanding shown in these lines has been aged into the relevant time bands correctly, through agreement to underlying accounting records. Specify the details of the underlying aged debt report or other accounting records that the revenue outstanding has been agreed to and details of sample tested.**
- 7.6.1 The ageing of outstanding debt has been agreed to underlying accounting records and agrees with work performed during the statutory fieldwork. The aged debt report provides totals for measured, unmeasured and trade effluent debtor categories aged from 0-30, 30-60 up to 365 days, after which it continues 1-2 years up to 4+ years.

KPMG tested a sample of invoices to ensure they had been aged correctly and reviewed movements with the prior year.

7.7 Check that NI Water has provided explanations for any material changes (+/- 20% between the report year and the previous year) in the "revenue outstanding" lines. Read NI Water's explanation and agree details set out in the commentary to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.

7.7.1 Revenue outstanding has increased by £1.43m (20%) on prior year due to the addition of three new income streams – measured sewerage, unmeasured water and unmeasured sewerage. This explanation is included in the commentary and is consistent with our understanding of debt collection and movements observed during statutory fieldwork. The opening and closing revenue outstanding balances for the year have been agreed to reports generated by the Rapid Xtra Billing system.

7.8 Check that the sum of the total revenue outstanding lines (lines 1, 13, 15, 27, 29, 41, 43 and 55) reconciles to the debt reported on NI Water's General Ledger. If numbers do not reconcile, test the reason for the difference in management's commentary can be agreed to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.

7.8.1 The total revenue outstanding per line 29 and line 43 was agreed to the Company's nominal ledger.

7.9 Check that the reasons for any adjustments made to revenue outstanding between data extracted from billing or accounting systems and that reported in the Regulatory Table can be supported by the underlying records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.

7.9.1 Total revenue outstanding for non households differs by £426k from the statutory financial statements due to (i) rechargeable debtors of £458k included in the statutory financial statements but not the Regulatory Table; offset by (ii) negative debtors of (£885k) included in the statutory financial statements but not the Regulatory Table (as they have been included within creditors). Rechargeable debtors relate to amounts due from third parties for unappointed activities. The negative debtors relate to those amounts identified in 7.1.4 in respect of over billed income.

7.10 Check that 'non-household revenue outstanding' has been correctly extracted from NI Water's underlying accounting records or other supporting documentation. Describe the nature of costs that have been reported.

7.10.1 Line 29 - the total of non-household revenue outstanding has been accurately extracted from the Company's nominal ledger.

Specific procedures – Customer Service Operating Expenditure

7.11 Obtain NI Water's commentary on the basis of allocating customer services operating expenditure (between lines 59 to 63). Check that this is consistent with the underlying accounting records and other supporting documentation.

7.11.1 Customer services operating expenditure has been allocated to line 59 only due to there being no household billing in 08/09 hence no associated costs. Similarly there

have been no donations to charitable trusts assisting customers in debt nor any operating expenditure incurred due to vulnerable household customers. The allocation of this customer services operating expenditure follows the same methodology as detailed in the commentary to Tables 21 and 22. Further work has been performed on the allocation methodology in section B – Activity Costing Analysis including walkthroughs of a sample of expense items to confirm that the allocation is being carried out as described in the methodology included in the commentary to Tables 21 and 22 – no issues were noted.

- 7.12 **Check that NI Water has provided an explanation for any material changes (+/- 30% between report year and previous year) in data reported in the 'customer service operating expenditure' lines. Read NI Water's explanation and agree details set out in the commentary to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.**
- 7.12.1 Customer services operating expenditure is consistent with prior year, hence no explanation for marginal variance required.
- 7.13 **Describe the basis of allocating outstanding revenue collection operating expenditure in line 60.**
- 7.13.1 As domestic billing has been postponed, there is no operating expenditure incurred in relation to households. No balance has been reported in this line.
- 7.14 **Check that reported numbers for household costs for outstanding revenue collection operating expenditure in line 60 can be agreed to the underlying accounting records or other supporting documentation. Obtain NI Water's commentary and check that NI Water has provided reasons for any material differences (+/-30% between the report year and the previous year) in each element. Read NI Water's explanation and agree details set out in the commentary to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.**
- 7.14.1 Not applicable as there was no domestic billing in 08/09 therefore no outstanding domestic revenue at the year end and no balance reported in line 60.
- 7.15 **Where a company has commented on a change to the methodology used to compile line 60 auditors should agree this to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.**
- 7.15.1 Not applicable as there was no domestic billing in 08/09 therefore no outstanding domestic revenue at the year end and no balance reported in line 60.
- 7.16 **Trace any amount reported in line 61 (Donations to charitable trusts assisting customers in debt) to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.**
- 7.16.1 The Company made no donations to charitable trusts assisting customers in debt as noted in the commentary to this table and no balance reported in line 61.

- 7.17 **Trace line 63 to the sum of table 21 line 13 and table 22 line 12. If they are not in accordance, check that reasons for any difference can be agreed to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.**
- 7.17.1 The total figure in line 63 has been agreed to the total of line 13 in table 21 plus the total of line 12 in table 22.
- 7.18 **Where NI Water has included an explanation of any significant exceptional capital costs associated directly with outstanding revenue collection or provision for vulnerable customers, agree these to the underlying accounting records or other supporting documentation. Where applicable, describe the nature of the underlying accounting records or other supporting documentation.**
- 7.18.1 No significant exceptional capital costs have been described in the Company's commentary.

Specific procedures – interaction between charge, provision and outstanding revenue

- 7.19 **Obtain a commentary from management on the bad debt provisioning policy, particularly where this has changed from the prior year. Where a change has been reported to have taken place, check that this is consistent with the Regulatory Accounts and the underlying accounting records.**
- 7.19.1 The bad debt provisioning policy has been included in the commentary to Table 6a. This was refined at the end of 07/08 and remained the same in 08/09 with the exception of increasing the provision against debts greater than one year from 90% to 100%. This was to allow the company extra coverage against old debt originating before 1 April 2007. The bad debt policy included is consistent with the policy that has been applied in deriving the bad debt provision in the statutory accounts and regulatory accounts.
- 7.20 **Provide in a table the level of consistency over time between the bad debt charge (from Tables 21 and 22), and revenue outstanding (Lines, 1, 13, 15, 27, 29, 41, 43 and 55 of table 6a). Through discussions with management, explain any large movements.**
- 7.20.1 The level of revenue outstanding has increased in the year due to the influences outlined in 7.7.1 above.

Table	Line	AIR 2008 £m	AIR 2009 £m	Variance £m
21	18	(0.544)	3.225	3.769
22	17	-	-	-
6a	1	-	-	-
6a	13	-	-	-
6a	15	-	-	-
6a	27	-	-	-
6a	29	7.029	7.875	0.846
6a	41	-	-	-
6a	43	-	0.584	0.584
6a	55	-	-	-

The prior year bad debt charge (£0.544m credit) consisted of £834k bad debts written off, offset by a £1,378k release of provision. The current year bad debt charge (£3.225m) is the result of £278k bad debts written off and a £2,947k increase in bad debt provision. No bad debt charge is allocated to table 22 (Sewerage).

Line 29 of table 6a representing measured non household debt has increased by £0.846m from the prior year due to three new income streams (see 7.7.1) and increased tariffs.

Line 43 of table 6a representing unmeasured non household debt less than 48 months old has increased by £0.584m from the prior year as this is a new income stream in the current year.

Lines 1, 13, 15 and 27 above relate to domestic debt and as such are not applicable for the company.

Lines 41 and 55 above relate to non-domestic debt greater than 48 months old. These debts are fully provided for and as such are included at nil value.

7.21 For the effect of changes in the provisioning policy (set out in management's commentary), obtain an assessment of the impact of the change and agree to supporting documentation. Describe the nature of the supporting documentation.

7.21.1 The Company's provisioning policy has not changed significantly from prior year with the exception of the provision made against debts greater than one year old which are fully provided for in the current year (90% in the prior year). Had the current year provisioning policy been in place in the prior year a further £150k would have been provided for.



As a result, a comparison of provisioning levels between 07/08 and 08/09 has not been included in the commentary. The commentary appears consistent with our understanding of trade debtors and the bad debt provision established for the statutory accounts.



8 **Part F – Taxation (Tables 18a and 18b)**

[Part F – Taxation (Tables 18a and 18b) has been redacted]

9 Part G – Accounting Charges (Table 33 & 34)

Current Cost Depreciation (CCD) - Table 34

- 9.1 **Check that any amounts reported by NI Water for assets fully depreciated still in use and assets written off or replaced in the year which were not fully depreciated can be agreed to the underlying accounting records.**
- 9.1.1 The current cost net value of assets fully depreciated but still in use, has been agreed to the fixed asset register. At 31 March 2009, there is a total of £2,967k (2008: £650k) of fixed assets with a Net Current Replacement Cost ('NCRC') of zero still in use. These have been agreed to the fixed asset register at the year end. A significant number of assets were decommissioned in April 2008 following an extensive management review. These assets written off in the year but not fully depreciated with a Gross Current Replacement Cost ('GCRC') of £12,815k and accumulated depreciation of £576k have been agreed to the current cost fixed asset register and regulatory accounts.
- 9.2 **NB. Include any specific procedures required by the Reporter in addition to 1 above.**
- 9.2.1 No specific procedures were requested by the reporter to be completed by KPMG.

Infrastructure Renewals Charge (IRC) - Table 33

- 9.3 **Check that the Infrastructure Renewals Charge is based on an operational assessment of activity needed to maintain the serviceability of the underground infrastructure over a reasonably long period using the definitions within RAG 1.04.**
- 9.3.1 The calculation of the infrastructure renewals charge has been reviewed. It is based on a limited operational assessment of activity needed to maintain the serviceability of the underground infrastructure using the definitions within RAG 1.04. This operational assessment is based on an average of the previous five years Infrastructure Renewals Expenditure ('IRE') and the projected five year IRE for 08/09 to 12/13. The previous five years IRE has been calculated with reference to actual costs incurred in 01/02 as reported in a proforma 'June Return' and the actual costs incurred in 06/07. The company has made an assumption for the intervening period (i.e. 02/03 to 05/06 inclusive) that expenditure has been made at a constant annual rate. The projected five year expenditure for 08/09 to 12/13 is based on the SBP prepared in 2007 which was based on the Northern Ireland Interim Asset Management Plan dated June 2002. The Company have noted in the commentary to tables 21 and 22 that their method of calculating IRC is a practical solution to limited data and as a result reduces the confidence level ascribed to the current IRC. This is also disclosed in the notes to the Regulatory Accounts.

The limited historical IRE information (dating back to a 'June Return' completed in 2001/2 by NI Water Service for the Department for Regional Development ('DRD')),

which was subjected to audit but not a full review by an External Water Reporter), gives rise to uncertainties in determining the actual levels of IRE in the period since 2001/2. Management updated their estimates of actual IRE when preparing their Strategic Business Plan ('SBP') for submission and agreement with DRD prior to the set up of NIWL in 2006/7 – however as these were again based on limited historical information, and estimates of actual funding requirements for future periods to 2012/13, significant estimates and assumptions have been made by management in arriving at the Infrastructure Renewals Charge ('IRC') which is derived from the IRE information. NIWL have now put systems in place to enable detailed information on IRE to be captured and reported, which will facilitate historical trend data to be developed through time, and enable management to make increasingly sophisticated estimates of future IRC (and consequently more accurate estimates of IRC, which will be based on management's assessment of expenditure required to maintain the serviceability of the underground infrastructure).

An adjustment of £3.79m was made in the year to reduce IRC based on management's review of the forecasted IRE required to maintain the operating capability of the infrastructure asset. This was fully discussed between NIW, NIAUR and DRD. This assessment is supported by a review of the forecasted IRE by the Water Reporter.

Management have acknowledged the key components of their estimates of IRE and IRC in their commentary to table 21. We note that management estimates of IRE and IRC should become more robust in future years as more detailed historical trend analysis becomes available and the Company develops more sophisticated operational performance measurement systems.

9.4 **Check that NI Water's explanation for the difference between the IRC reported in the Regulatory Accounts and the Statutory Accounts can be agreed to underlying accounting records.**

9.4.1 There is no difference between the IRC in the regulatory and statutory accounts.



10 **Part H – Land Sales**

[Part H – Land Sales has been redacted].

11 Part I Analysis of borrowing (Table 19a)

- 11.1 **Confirm that the total carrying value of all instruments reconciles back to the appropriate line in table 19 as required by the reporting requirements of table 19a.**
- 11.1.1 The carrying value of £457,560k (per Part D Totals) has been agreed to table 19 line 20.
- 11.2 **Confirm that each instrument has been included within the correct category (A,B,C) in accordance with the definitions of FRS 26.**
- 11.2.1 Each instrument has been included in the correct category (A-C) in accordance with the definitions of FRS 26.
- The capital loan notes have been classified as a fixed rate instrument under other borrowings (C).
- 11.3 **Agree the interest rates recorded in table 19a back to loan documents and other supporting documentation.**
- 11.3.1 The interest rate of 5.25% recorded for the capital loan notes has been agreed to the Fixed Coupon Unsecured Loan note 2027 agreement dated 1 April 2007.
- We have noted that the interest rate of 5.25% relates to loan notes issued before 31 March 2010. Any loan notes issued after this date are subject to interest rates based on a margin of 0.85% above the reference gilt rate published by UK HM Government Debt Management Office. This amendment to interest rates has also been agreed to the loan note agreement and has been noted in the Company's commentary to Table 19a.
- 11.4 **Agree the hedging strategy to supporting documentation. Describe the nature of the supporting documentation.**
- 11.4.1 As per the statutory accounts, the Company does not adopt a hedging strategy.
- 11.5 **Review NI Water's commentary on any significant borrowings that mature in less than one year and agree the details back to supporting documentation.**
- 11.5.1 The Company does not have any significant borrowings which mature in less than one year.