



Audit of the Utility Regulator's PC15 Financial Model

FTI Consulting LLP

Confidential

11 October 2014

Copyright 2014 FTI Consulting LLP. All rights reserved.

FTI Consulting LLP. Registered in England and Wales at
200 Aldersgate, Aldersgate Street, London EC1A 4HD.

Registered number OC372614, VAT number GB 815 0575 42.

A full list of Members is available for inspection at the registered address.



F T I
CONSULTING™

CRITICAL THINKING
AT THE CRITICAL TIME™

11 October 2014

Alan Craig
Regulatory Finance Manager
Utility Regulator
Queens House
14 Queen Street
Belfast, BT1 6ED

Dear Sirs

Review of the PC15 Financial Model for the Utility Regulator

In this letter, we set out details of the review work, which FTI has undertaken for you in connection with the Financial Model ("the Model") used for the PC15 Price Review.

Background

The Model has been developed by for the Utility Regulator to calculate the allowed revenue for Northern Ireland Water (NIW) over the six year period from 1 April 2015 to 31 March 2021.

Scope

We have been engaged by the Utility Regulator to provide an independent review and opinion on certain aspects of the Model. The "Certain Aspects" of the Model we were asked to review and provide an opinion on were those changes to the Model that had been made since the PC10 Price Review, when the Model was last audited for the Utility Regulator. These Certain Aspects were highlighted in red throughout the Model and related to worksheets A3, A5, A7, B5, P1, P6, P7, P9, P11, O1, T7, T17, T21 and T26.

FTI has been asked to perform a review of these Certain Aspects of the Model and report our findings and opinion against the Utility Regulator's objectives ("the Objectives"):

- that the Model is arithmetically accurate; and
- that the Model functions and calculates allowed revenue consistently with the Utility Regulator's financial, regulatory, economic and tax assumptions.

FTI's scope of work excluded consideration of the appropriateness or validity of the Utility Regulator's assumptions.

FTI expresses no opinion on the Model other than in relation to the Certain Aspects.

Our review has been undertaken using the following information provided to FTI by the Utility Regulator:

- the Model

Filename: "2014-08-29 PC15 Financial Model_DD 4th Model Run revised unmeas tariffs1check.xlsm"

Last Modified: 29 August 2014

Size: 889 KB

- Draft report from the Utility Regulator's tax consultants, dated 2 July 2014
- Various correspondence between the Utility Regulator and NIW on tax issues
- Correspondence between HMRC and NIW in relation to adoptions and PFI issues

Basis of review and opinion

Our review is based upon the following procedures, agreed upon with the Utility Regulator:

- a review of the Model for arithmetical errors, the correct application of Microsoft Excel functions and the functionality of links between sheets; and
- a review of the logic, derivation and internal consistency of key calculations within the Model (e.g. revenues, costs, financing, tax etc) and their consistency with the Utility Regulator's financial, regulatory, economic and tax assumptions.

In performing our review, we have relied exclusively on the information and explanations provided to us by the Utility Regulator, and have not undertaken any form of investigation, verification, validation, audit or other work in relation to such information and explanations.

Subject to the scope agreed, we have planned and performed our review of the Model to provide reasonable assurance to the Utility Regulator that they materially meet the Utility Regulator's Objectives. It should be noted however that it is not practicable to test spreadsheet models to the extent whereby it can be certain that all errors have been detected and accordingly no such guarantee can be given in respect of the Model.

It should also be noted that our review of the tax issues in the model has been based on our understanding of information provided by the Utility Regulator up to 16 September 2014. This information has indicated that there are some aspects of the modelling of tax issues which require further dialogue between HMRC and NIW before the modelling can be finalised. The Utility Regulator has confirmed that the main outstanding point that will impact the mechanics of the model is the treatment of cash customer contributions for tax purposes, which could impact the current tax calculations in respect of the tax treatment of both the contributions received and the corresponding capital expenditure. In the absence of an agreed tax treatment of the relevant contributions with HMRC, we cannot conclude on whether the relevant model calculations reflect the agreed tax treatment or not at this stage.

Results and opinion

Based on the agreed upon review procedures outlined above, and the representations made to us by the Utility Regulator, in our opinion the Objectives have been materially met.

We express no opinion as to how closely the actual results and financial positions of NIW will compare with projections generated by the Model.

Distribution

This letter is intended solely for the information and use of the Utility Regulator. However, its content may be disclosed publicly by the Utility Regulator in connection with the PC15 Price Review.

FTI does not accept any responsibility and disclaims all liability whatsoever (including in respect of any negligence, fault, breach of contract or breach of duty or otherwise) to any person (other than the Utility Regulator) who acts or refrains from acting as a result of the contents of this letter. Any person (other than the Utility Regulator) who chooses to rely on this report does so entirely at their own risk.

Yours faithfully



Greg Harman
Senior Managing Director
FTI Consulting LLP



Anthony Legg
Director
FTI Consulting LLP