

Section N Tables - Transfer Pricing

General Comments

The N tables for the five months to 31 March 2007 have been prepared in accordance with Regulatory Accounting Rule 5 and related definitions.

Reconciliation to Statutory Accounts

The following table reconciles the information in the Statutory Accounts - Note 15 Related Party Transactions to the N Tables.

	£m
Amounts due to SW - transactions in year + outstanding amounts	131.7
Amounts due from SW - transactions in year + outstanding amounts	-67.9
Net amount due to/from SW - per Statutory Accounts Note 15	63.8
N tables to SW - wholesale charge	126.8
N tables to SW – interest	1.3
N tables to SW – SLA	1.6
N tables from SW	-0.5
Net amount due to/from SW - per N tables	129.3
Less loans from SW not included in the N tables (as not P&L)	64.5
Less other balances to SW not included in the N tables (as not P&L)	0.9
Net amount (adjustment for items not included in N tables)	63.9
Variance = rounding difference	-0.1

Table N1 - Transfer Pricing Summary (Capex)

A. Market Testing

Not applicable – no market tested contracts were in place during the period.

B. Cost Allocation: Recharges to Associate / Non-Core from Core

Not applicable.

C. Cost Allocation: Recharges to Core from Associate / Non-Core

Not applicable.

Table N2 - Transfer Pricing Summary (P&L)

A. Market Testing

Not applicable – no market tested contracts were in place during the period.

B. Cost Allocation. Recharges to Associate / Non Core from Core

Recharges from Core business to Scottish Water Business Stream

Wholesale Charges

The Wholesale Scheme of Charges 2006-2007 stated that all retail charges would be subject to a wholesale charge of 89.8%.

These costs totaled £126.8m in the five month period to 31 March 2007.

Interest Paid to Scottish Water on Loans

Scottish Water Business Stream (SWBS) borrowed £64.5m of loans from Scottish Water (SW) in the period; £35m of these were inherited as part of the transfer of assets on 1 November 2006.

The table below details each of the outstanding loans and the interest charged on each during the period.

Maturity Date	Amount £m	Interest £m	Rate %
Debt Transferred from SW			
24 April 2007	10.0	0.185	4.50%
26 June 2007	10.0	0.154	3.75%
15 September 2007	5.0	0.120	5.75%
15 March 2008	10.0	0.188	4.50%
New Debt Outstanding			
31 March 2008	25.0	0.483	4.70%
31 March 2008	4.5	0.020	5.50%
£10m short term loan repaid in period	<u>0.0</u>	<u>0.191</u>	5.16%
	<u>64.5</u>	<u>1.341</u>	

SLA Costs Overview

A number of services were procured by SWBS from SW during the period and vice versa. The terms and conditions, service standards and rates for each were set out in a Service Level Agreement, which was signed by both parties. Costs associated with each of these activities are reported in N2.

Metering SLA Costs

Metering SLA costs were recharged from SW at rates set out in the SLA.

Metering costs include the costs of the outsourced metering contracts, review and audit of the metering contract, field operations, office support and managerial support.

IT SLA Costs

IT SLA costs were recharged from SW at rates set out in the SLA.

IT costs include desktop support, applications support, infrastructure, maintenance and telephony. These costs have been recharged to SWBS as follows:

Desktop support and maintenance: unit cost per PC
Applications support/maintenance: actual costs/number of users

Telecoms: actual costs

Property SLA Costs

Property SLA costs were recharged from SW at rates set out in the SLA.

The property recharge was based on a standard unit charge per workstation.

Support Services SLA Costs

Support services SLA costs were recharged from SW at rates set out in the SLA.

Support services SLA costs includes recharges from SW for the provision of payroll, accounts payable, tax, internal audit, corporate affairs, HR, legal, procurement services and access to financial systems.

The recharge for tax, internal audit, HR, legal and procurement were based on hourly unit rates.

The recharge for accounts payable included a fixed cost for the maintenance of the SWBS business unit with Rebus and a unit rate for each invoice processed.

The recharge for payroll included a fixed cost for the maintenance of the SWBS pay group and a rate for maintenance of employee details, based on the number of SWBS employees.

The recharge for financial systems was based on the actual cost of business unit Maintenance and support and application development.

Customer Contact SLA Costs

The customer contact recharge was based on a standard unit rate per operational phone call handled by SW.

Miscellaneous Costs

Other costs include the recruitment of the SWBS Board of Directors, which was paid by SW initially and then recharged to SWBS.

Insurance SLA Costs

The insurance SLA costs includes costs for public and employer's liability, group life & directors and officers cover, based on the number of SWBS employees. Motor vehicle insurance cover was based on the number of SWBS vehicles.

Fleet Costs

The fleet recharge was based on a standard unit rate per vehicle.

C. Cost Allocation: Recharges to Core from Associate

Recharges from SWBS Stream to Core business

Sundry Billing SLA Costs

The costs recharged to SW relate to billing, cash collection, customer contact and credit management for sundry billing activities undertaken on behalf of SW. These costs were based on a standard unit rate per invoice raised.

Interest Received from SW on Wholesale Charge

The wholesale charge was paid in accordance with the Wholesale Service Agreement. Interest is paid to the Licensee on the advance paid element of the wholesale charge at the base rate minus 0.5%. The total amount of interest charged to SW for advance payment of the wholesale charge totaled £411k in the period.