

# Information notice

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## Simplifying the revenue correction mechanism

We set limits on the prices ('price limits') that monopoly water and sewerage companies in England and Wales can charge their customers. We last set price limits in November 2009 for the period 2010 to 2015.

When we set price limits, we assume that each company will be able to recover a certain amount of revenue. In practice, the amount of revenue a company can recover will be different from the assumption we made. In ['Future water and sewerage charges 2010-15: final determinations'](#), we included a new way of sharing the benefits and risks of this between the companies and their customers. We called it the revenue correction mechanism (RCM). The RCM also provides a financial incentive for the companies to encourage consumers to use water wisely.

We will use the RCM by adjusting the revenue that each company can collect from its customers when we next set price controls in 2014. This will reflect any over or under recovery of [tariff basket](#) revenue that each company has

made from its customers during 2010-15. We will spread the effect of these adjustments across the next price review period.

Since the RCM was introduced, several companies have raised concerns about the complexity and the incentive properties of the billing incentive that forms part of the RCM.

We held a workshop with the companies on 22 November 2010 to discuss areas where the RCM could be simplified. This notice summarises our decision to simplify two areas of the RCM.

Further information on these changes are available in the [supporting information](#) to this notice.

### Billing incentive

We have simplified the calculation of the billing incentive. We introduced this as part of the RCM to provide the companies with a financial incentive to bill all eligible properties. This change will reduce the information the companies need to send to us in June 2011 as part of their main

annual regulatory submission (the 'June return').

### Back billing

We have simplified the back-billing incentive. This was included in the RCM to give the companies an incentive to identify properties that have been charged less than they should have been ('under-billed properties') – and to recover the amount owed ('back billing').

Companies wishing to claim the incentive will no longer have to provide us with detailed information on each individual under-billed property. Instead they will simply need to provide us with the total amount of under-billed revenue that it wishes to claim for.

### Social tariffs

We have not changed our charging policy on social tariffs, or how these are reflected in the RCM.

Section 44 of the Flood and Water Management Act 2010 allows the companies to charge other customers more so that they can offer social tariffs to groups of

This is a formal document that alerts our stakeholders to a change in the way that we regulate the water and sewerage sectors in England and Wales.

customers who would have difficulty paying their water bills in full. But this is dependent on the UK and Welsh Assembly Government issuing guidance on how these tariffs should operate. Until this guidance is issued, our existing charging policy on social tariffs applies. This includes how we reflect these tariffs in the RCM.

We restate our current policy on social tariffs and how we reflect them in the RCM in the [supporting information](#) to this notice.

### RCM spreadsheet model

In April 2010, we published an illustrative spreadsheet model to help our stakeholders understand how the RCM works. We have updated the model to take into account changes we have described in this notice and to improve the model's structure. The [updated example](#) is available on our website.

### Enquiries

If you have any questions about this information notice or want to know more about the RCM, please contact Jenny Ngai at [jenny.ngai@ofwat.gsi.gov.uk](mailto:jenny.ngai@ofwat.gsi.gov.uk).



**Ofwat (The Water Services Regulation Authority) is a non-ministerial government department. We are responsible for making sure that the water and sewerage sectors in England and Wales provide consumers with a good quality and efficient service at a fair price.**

## More information

[‘Simplifying the revenue correction mechanism: supporting information’](#)

Updated [spreadsheet model](#)\* of how the RCM works

[Explanation of the tariff basket](#)

A [letter](#) we sent to each of the companies to respond to questions we received from them about the RCM (April 2010)

[‘Future water and sewerage charges 2010-15: final determinations’](#) (November 2009)

[‘PR09/31 Revenue correction mechanism – technical details’](#) (July 2009)

[‘PR09/10 Revenue Correction mechanism– worked example’](#) (April 2008)

[‘Setting price limits for 2010-15: Framework and approach’](#) (March 2008)

[‘RD 14/07 Review of form of price control mechanism’](#) (July 2007)

\*Updated since first published



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