

# Information notice

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## Update on Ofwat's process for Thames Water's application to increase bills

This information notice provides an update on our process for dealing with Thames Water's application to increase prices to customers. It includes timings of when we intend to consult and announce final decisions.

### The application

In 2009, we set limits on the prices that Thames Water could charge its customers for the period 2010-15. However, in August this year, [the company asked us](#) to increase the limits on its prices in the last 12 months of the current period, which run from April 2014. Thames Water said that it has experienced changes to certain specific costs of which Ofwat did not take account when price limits were set in 2009. It has indicated that this application would add around a further 8% – about £29 – to the average household bill. The current average Thames Water household bill is about £354. Some of the increase could affect the bills for customers of other companies who bill for wastewater services on behalf of Thames Water.

We are currently assessing Thames Water's application. Any increases to bills will only be allowed if they are fully justified.

Water and sewerage companies have until 15 September 2013 to apply for an additional increase in prices for 2014-15. Thames Water is the only company to have applied to increase its price limits since they were set in 2009.

### Further information required from companies

An important part of the work required to assess and make a determination on Thames Water's application is to look closely at the costs the company included in its application. We need to understand whether costs have increased compared with the costs allowed when we set price limits in 2009. Some of the costs we are assessing are specific to Thames Water – for example, the costs of land purchases for the Thames Tideway Tunnel project. But our assessment of some of the costs in the application needs to be in the context of the picture across

the whole of England and Wales. This is because other companies are also affected by some of the same factors that Thames Water cites as driving the increases in costs contained within its own application.

As a consequence, we are collecting information from other water and sewerage companies to help assess the application. This covers Thames Water's claims in relation to:

- the costs of dealing with bad debt;
- the impact of the transfer of private sewers after price limits were set; and
- sewer flooding performance.

Other companies have managed the impact of such costs without applying for an additional increase in the price limits they can charge their customers in 2014-15. Thames Water has told us that it has faced special, company-specific circumstances that have affected its own costs. The evidence we receive from other companies will help us assess

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.

whether the company's claims are valid, and whether the additional costs have been efficiently incurred and could not have been avoided or mitigated by prudent management action.

### Ofwat notices

There is an established process in Thames Water's licence which allows us to consider whether specific relevant changes in circumstances mean that the company is no longer delivering some of the outputs we assumed it would deliver when we set price limits. These outputs are being funded by customers in their current bills. The licence allows us to recover these amounts on behalf of customers.

We can consider these changes in circumstance at the same time as we assess the company's application.

In order to protect customers from unnecessary bill increases we have notified Thames Water of our intention to consider three additional relevant changes in circumstances ourselves. We consider that the effects of these three specific changes in circumstances are sufficiently large to be considered (they need to represent a value equal to at least 2% of relevant turnover). We now need to understand more of the details on the relevant circumstances before reaching a conclusion. The three items are as follows.

- The substantial savings that Thames Water has made by doing less to address sewer

flooding than was funded in the last price review. We have not been convinced of the change in circumstances that the company set out for these savings in its application, or of the extent of savings that should have been made, and have notified Thames Water of our intention to make our own determination of the appropriate level of these savings. We are requesting additional information from other companies to help us assess this.

- A major investment scheme, which we had assumed would be partly delivered in 2010-15 when we set existing price limits, is now unlikely to deliver benefits for customers until the end of the next price control period. We wish to recover the revenue allowed in the current period that has not been spent.
- Part of the company's sewerage network is not achieving the performance levels we assumed when we set price limits. We wish to recover on behalf of customers part of the revenue allowed to deliver this performance in the current period.

In light of Thames Water's application we are also examining other possible routes to ensure an appropriate balance of risk and reward between the company and customers. In this context, we are examining whether Thames Water has substantially benefited from wider economic circumstances which are beyond its control. We are considering this under the substantial effect mechanism set out in company licences.

This is an established process which companies have triggered before and which we can trigger on behalf of customers. As Thames Water is the only company to have applied for an additional increase in bills before the next price review, Ofwat will only examine whether there is a case for clawing back gains through this mechanism from the company.

Under the terms of its licence, we need to give a separate notice to Thames Water of our intention to make such an additional determination. We do not expect to set out any proposals on this issue until we have reached a final view on the company's application for an additional increase in price limits. This is because we need to consider the overall balance of risk and reward between Thames Water and its customers.

In December, companies are due to submit business plan proposals for price controls for the period 2015-20. We do not expect any determination for Thames Water to affect this process.

### Hearing your views and consultation period

Once we have gathered and assessed all relevant information, we plan to make a draft decision by mid-October on both the Thames application and our own notice of relevant changes in circumstances.

There will then be a consultation period of about one week. We will consider consultation responses carefully before announcing our

determination on both the application and the relevant changes of circumstances set out in our own notice.

Normally, we would like to have a longer period for consultation. Yet the short consultation period is necessary. It gives us sufficient time to:

- collect and examine carefully the relevant information which we have requested from all water companies;
- scrutinise Thames Water's proposals; and
- get the best possible overall deal for customers.

It also means we can adhere to the three-month period, set out in companies' licences, within which we are expected to deal with such applications.

We are highlighting the one-week formal consultation period at this point, so that relevant stakeholders can prepare to respond appropriately.

## More information

[What are interim determinations?](#) Ofwat webpage

['IB 16/13: Thames Water proposes significant increase in bills'](#), 9 August 2013

[Thames Tideway Tunnel](#), UK Government webpage

[Transfer of private sewers](#), Ofwat webpage

We also welcome earlier feedback now on Thames Water's application. You can submit your views on this to [mailbox@ofwat.gsi.gov.uk](mailto:mailbox@ofwat.gsi.gov.uk).

Please also note if it is established that there is a case for a substantial effect, we will then provide an update on that process.

### Our final decision

We are committed to providing certainty as soon as possible for Thames Water's customers about the expected size of any increases in their bill next year. We recognise

the importance of certainty for the sector, particularly as in December Thames Water and other companies are due to submit their business plans to us for the purposes of our setting price controls covering the 2015-20 period.

We will announce our final decision in early November. Thames Water may then choose to refer this decision to the Competition Commission.

### Key dates

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|--------------------|---|
| • Mid-October      | publish draft decision.   |
| • Mid-late October | one-week consultation period.   |
| • Early November   | publish final decision.   |
| • April 2014       | new bills for 2014-15 come into effect, taking account of our decision on Thames Water's application. |



**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.**



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