

September 2022

Business retail market: 2021-22 review of the Retail Exit Code – Consultation on proposals

Annex C – Proposed amendments to the Retail Exit Code

Annex C

Proposed amendments to the Retail Exit Code

This Annex sets out the amendments we would propose to make to the Retail Exit Code (REC) to give effect to our proposals to revise REC price caps.¹ Our proposed amendments concern price protections for customer Groups One and Two. Our intention would be for amendments to the REC to take effect from April 2023.

¹ Current version (v.6) of the REC available here: <https://www.ofwat.gov.uk/publication/retail-exit-code-v6-0-clean-version/>

1. Proposed amendments to the Retail Exit Code

Our main consultation document *Business retail market: 2021-22 review of the Retail Exit Code – Consultation on proposals* (chapters 3 to 7) explain that we propose to revise REC price caps in respect of Customer Groups One and Two. Our proposed revisions would take the form of amendments to Defined terms in §1.1, Annex A1 and Annex A2 of the Retail Exit Code. We set out here our current view of how our proposals for revisions to REC price caps for customer Groups One and Two would be expressed in revised Annexes to the REC (Annex A1 for Customer Group One, Annex A2 for Customer Group Two).

1.1 Defined terms

We would propose to introduce a new defined term "Unique service" in Section 1.1 Defined terms of the Retail Exit Code, as follows:

Term	"Unique service"
Definition	A service provided to a customer as follows: <ol style="list-style-type: none">1) a water service;2) a wastewater only service;3) a wastewater and trade-effluent service; or4) a trade effluent only service.

1.2 Proposed REC Annex A1

We would propose that the current Annex A1 of the REC is removed and replaced by the text given here below.

Note we have in our proposed amendments here expressed *acts* and *mc* components in terms of our best current estimate of the price basis for 2023-24. That is, we have applied CPIH inflation to July 2022 to the *acts* and *mc* allowances we set out in the main document, which are given there in 2021-22 prices. Hence *acts* is expressed here as $£37.81 = £34.07 \times \text{Jul 2022 CPIH} \div \text{Oct 2020 CPIH} = £34.07 \times 121.2 \div 109.2$, and similarly equivalently for *mc*. Our intention would be, for any amended REC to apply from April 2023, to update *acts* and *mc* in terms of CPIH applying in October 2022 rather than July 2022.

"A1 Allowed charges for Customer Group One

Maximum charge per unique service

For charging years 2023-24 and 2024-25

For the charging years 2023-24 and 2024-25 as relevant, in relation to Customer Group One, the Licensee's charges in respect of each unique service provided to each Customer in each Charging Year in respect of its Business Retail Activities shall not exceed C calculated in accordance with the following formula:

$$C = [(acts + mc + w) / (1 - nm - b)]$$

where:

acts = for the charging years 2023-24 and 2024-25 as relevant the allowed cost to serve component for a given customer type (in pounds) for the relevant charging year, as set out in Table 1.

mc = for the charging years 2023-24 and 2024-25 as relevant the allowed meter read cost (in pounds), as set out in Table 1;

w = the wholesale charges for a given Customer; and

nm = the allowed retail net margin for a given Customer type (expressed as a percentage) for the relevant charging year as set out in Table 1.

b = 2%, the allowed customer bad debt cost allowance (expressed as a percentage).

For charging years 2025-26 and subsequent charging years

For the charging year 2025-26 and subsequent charging years, in relation to Customer Group One where a customer takes a water service on a measured basis (ie. the service includes metered reads), the Licensee's charges in respect of each unique service provided to each Customer in each Charging Year in respect of its Business Retail Activities shall not exceed C calculated in accordance with the following formula:

$$C = [(acts + mc + w) / (1 - nm - b)]$$

where:

acts = £37.81

$$mc = \text{£}8.15$$

w = the wholesale charges for a given Customer; and

nm = 2%, the allowed net margin (expressed as a percentage).

b = 2%, the allowed customer bad debt cost allowance (expressed as a percentage).

For the charging year 2025-26 and subsequent charging years, in relation to Customer Group One where a customer takes a water and/or wastewater and/or trade effluent service on an unmeasured or an assessed basis, the Licensee's charges in respect of each unique service provided to each Customer in each Charging Year in respect of its Business Retail Activities shall not exceed C calculated in accordance with the following formula:

$$C = [(acts + w) / (1 - nm - b)]$$

where:

$$acts = \text{£}37.81$$

w = the wholesale charges for a given Customer; and

nm = 2%, the allowed net margin (expressed as a percentage).

b = 2%, the allowed customer bad debt for a given Customer type (expressed as a percentage).

Permitted Adjustments allowed for Customer Group One

In Charging Years 2024-25 and subsequent charging years, the licensee's charges in respect of each unique service provided to each Customer in Customer Group One are permitted to be adjusted. The adjustment is applicable from the start of each Charging Year and based on the CPI-H inflation rate as measured in October of the previous Charging Year. Specifically the adjustment is permitted to apply to the allowed cost to serve component acts, and the allowed meter read cost component mc, as defined by the formulae for the relevant charging years:

For charging year 2024-25:

$$acts = acts_{Table\ 1} \times inf_t$$

$$mc = mc_{Table\ 1} \times inf_t$$

where:

acts = the allowed cost to serve component for a given Customer type (in pounds) in charging year 2024-25, as adjusted.

acts_{Table 1} = the allowed cost to serve component for a given Customer type (in pounds) as set out in Table 1

mc = the allowed meter read cost component for a given Customer type (in pounds) in 2024-25, as adjusted

mc_{Table 1} = the allowed meter read cost component for a given Customer type (in pounds) as set out in Table 1

inf_t = CPIH (expressed as an index relative to the previous year) as reported by the Office for National Statistics for October of the previous year

This means for example that the acts to apply in the charging year 2024-25 will be the acts given for 2024-25 in Table 1 multiplied by the ratio of CPIH applying in October 2023 and October 2022.

For charging years 2025-26:

acts_{t+2} = acts_{t+1} x inf_{t+1}

mc_{t+2} = mc_{t+1} x inf_{t+1}

where:

acts_{t+2} = the allowed cost to serve component for a given Customer type (in pounds) in 2025-26, after adjustment for inflation

acts_{t+1} = acts_t x inf_t

acts_t = for the charging year 2025-26, £37.81 (expressed in 2023-24 prices).

mc_{t+2} = the allowed meter read cost component (in pounds) in 2025-26, after adjustment for inflation

mc_{t+1} = mc_t x inf_t

mc_t = for the charging year 2025-26, the allowed meter read cost component for a given Customer type (in pounds) as set out in Table 1 (expressed in 2023-24 prices).

inf_t = CPIH (expressed as an index relative to the previous year) as reported by the Office for National Statistics for October of the previous year

This means for example that the acts to apply in the charging year 2025-26 will be the acts given for 2025-26 (ie. £37.81) multiplied by the ratio of CPIH applying in October 2023 and October 2022 and by the ratio of CPIH applying in October 2024 and October 2023.

For charging years 2026-27 and subsequent:

$$\underline{acts}_{t+1} = acts_t \times inf_t$$

$acts_t$ = the level of acts applying for charging year 2025/26, as adjusted for inflation as above

$$\underline{mc}_{t+1} = mc_t \times inf_t$$

mc_t = the level of mc applying for charging year 2025/26, as adjusted for inflation as above

inf_t = CPIH (expressed as an index relative to the previous year) as reported by the Office for National Statistics for October of the previous year

This means for example that the acts to apply in the charging year 2026-27 will be the acts given for 2025-26 after inflation adjustment, then multiplied by the ratio of CPIH applying in October 2025 and October 2024.

Table 1 Customer Group One, allowed cost to serve components and allowed net margins in 2023-24 prices

Area	Customer type	Allowed cost to serve (acts)		Allowed retail net margin (nm)		Allowed meter read cost component (mc)
		2023-24	2024-25	2023-24	2024-25	
		£	£	%	%	
AFW	Water 0-0.5Ml measured or assessed; water unmeasured	£37.81	£37.81	2.70%	2.02%	£8.15
ANH	Water unmeasured	£20.17	£25.22	2.42%	2.00%	-
ANH	Water unmeasured (Hartlepool)	£19.53	£24.41	2.49%	2.00%	-
ANH	Water 0-0.5Ml measured or assessed	£37.81	£37.81	3.31%	2.48%	£8.15
ANH	Wastewater unmeasured	£20.91	£26.14	1.89%	2.00%	-
ANH	Wastewater 0-0.5Ml measured or assessed	£37.81	£37.81	2.94%	2.20%	-
ANH	Wastewater unmeasured (trade effluent)	£22.38	£27.98	1.95%	2.00%	-
ANH	Wastewater 0-0.5Ml measured or assessed (trade effluent)	£101.53	£76.15	3.15%	2.36%	-
BRL	Water 0-0.5Ml measured or assessed	£29.06	£36.33	3.24%	2.43%	£8.15
BRL	Water unmeasured	£11.64	£14.55	3.54%	2.66%	-
NES	Water unmeasured	£26.02	£32.52	5.50%	4.13%	-
NES	Water 0-0.5Ml measured or assessed	£34.65	£37.81	3.49%	2.62%	£8.15
NES	Wastewater unmeasured	£27.40	£34.26	3.76%	2.82%	-
NES	Wastewater 0-0.5Ml measured or assessed	£37.81	£37.81	2.49%	2.00%	-
PRT	Water unmeasured	£25.49	£31.86	2.49%	2.00%	-
PRT	Water 0-0.5Ml measured or assessed	£22.53	£28.16	2.49%	2.00%	£8.15

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SVE	Water 0-0.5Ml measured or assessed; water unmeasured	£37.81	£37.81	3.29%	2.47%	£8.15
SVE	Wastewater 0-0.5Ml measured or assessed; wastewater unmeasured	£41.52	£37.81	2.63%	2.00%	-
SEW	Water unmeasured	£37.81	£37.81	1.92%	2.00%	-
SEW	Water 0-0.5Ml measured or assessed	£37.81	£37.81	2.54%	2.00%	£8.15
SRN	Water unmeasured	£18.93	£23.66	2.49%	2.00%	-
SRN	Water 0-0.5Ml measured or assessed	£27.72	£34.65	5.23%	3.92%	£8.15
SRN	Wastewater unmeasured	£23.32	£29.15	2.49%	2.00%	-
SRN	Wastewater 0-0.5Ml measured or assessed	£37.81	£37.81	3.21%	2.40%	-
SSC	Water 0-0.5Ml measured or assessed; water unmeasured	£37.81	£37.81	2.71%	2.03%	£8.15
SWB	Water unmeasured (South West)	£20.21	£25.27	2.49%	2.00%	-
SWB	Wastewater unmeasured	£22.62	£28.28	2.49%	2.00%	-
SWB	Water 0-0.5Ml measured or assessed (South West)	£15.79	£19.74	2.84%	2.13%	£8.15
SWB	Wastewater 0-0.5Ml measured or assessed	£23.19	£28.99	2.55%	2.00%	-
SWB	Water unmeasured (Bournemouth)	£22.58	£28.22	2.49%	2.00%	-
SWB	Water 0-0.5Ml measured or assessed (Bournemouth)	£24.66	£30.82	2.75%	2.06%	£8.15
SES	Water unmeasured	£29.26	£36.58	2.49%	2.00%	-
SES	Water 0-0.5Ml measured or assessed	£37.23	£37.81	2.49%	2.00%	£8.15
TMS	Water 0-0.5Ml measured or assessed	£27.15	£33.93	2.65%	2.00%	£8.15
TMS	Wastewater 0-0.5Ml measured or assessed	£37.81	£37.81	2.85%	2.14%	-

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TMS	Wastewater 0-0.5Ml measured or assessed (trade effluent)	£37.81	£37.81	3.03%	2.27%	-
TMS	Water unmeasured	£34.57	£37.81	2.49%	2.00%	-
TMS	Wastewater unmeasured	£37.81	£37.81	2.49%	2.00%	-
UUW	Water 0-0.5Ml measured or assessed; water unmeasured	£37.81	£37.81	2.62%	2.00%	£8.15
UUW	Wastewater 0-0.5Ml measured or assessed; water unmeasured	£48.09	£37.81	2.62%	2.00%	-
WSX	Water unmeasured	£29.15	£36.44	2.30%	2.00%	-
WSX	Wastewater unmeasured	£23.36	£29.20	2.45%	2.00%	-
WSX	Water 0-0.5Ml measured or assessed	£26.53	£33.16	2.97%	2.22%	£8.15
WSX	Wastewater 0-0.5Ml measured or assessed	£25.92	£32.40	3.05%	2.29%	-
WSX	Wastewater 0-0.5Ml measured or assessed (trade effluent)	£34.65	£37.81	2.97%	2.23%	-
YKY	Water unmeasured	£26.44	£33.05	9.27%	6.95%	-
YKY	Wastewater unmeasured	£26.63	£33.29	5.76%	4.32%	-
YKY	Water 0-0.5Ml measured or assessed	£32.07	£37.81	3.15%	2.36%	£8.15
YKY	Wastewater 0-0.5Ml measured or assessed	£37.81	£37.81	2.69%	2.02%	-
YKY	Wastewater 0-0.5Ml measured or assessed (trade effluent)	£34.68	£37.81	2.49%	2.00%	-

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1.3 Proposed REC Annex A2

We would propose that the current Annex A2 of the REC is removed and replaced by the following:

"A2 Allowed charges for Customer Group Two

Maximum charge per customer

In relation to Customer Group Two, the Licensee's charges to each Customer in each Charging Year in respect of its Business Retail Activities shall not exceed C calculated in accordance with the following formula:

$$C = (1 + gm) \times w$$

where:

gm = the allowed gross margin for a given Customer type (expressed as a percentage) and is the gm for the relevant charging year as set out in Table 2.

w = the wholesale charges for a given Customer type.

Table 2 Customer Group Two and allowed gross margins

Customer group	gm%	
	2023-24	2024-25 and subsequent charging years
Water supplies 0.5 Ml to 50 Ml	8.49%	8.0%
Wastewater services 0.5 Ml to 50 Ml	10.49%	10.0%

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