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Trust in water

Summary of responses to the Infrastructure Provider Project Licence Award consultation (17 July to 14 August 2015)

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1. Purpose of this document

On 21 August 2015 Ofwat granted a project licence to Bazalgette Tunnel Limited enabling it to become the regulated infrastructure provider (IP) responsible for financing, building, maintaining and operating the Thames Tideway Tunnel project (the project). The project licence came into effect on 24 August 2015.

Now that it has been appointed as the regulated IP, Bazalgette Tunnel Limited will trade and be known to the public as 'Tideway'. Tideway is owned by a consortium of investors that includes Allianz, Amber Infrastructure, Dalmore Capital and DIF (Dutch Infrastructure Fund B.V). Further information on Tideway is available on its [website](#).

Prior to granting the project licence to Tideway on 21 August 2015, Ofwat consulted on its intention to:

- grant a project licence to the preferred bidder selected by Thames Water on 14 July 2015 in its procurement of an IP; and
- issue a waiver notice to the IP, once appointed, selectively dis-applying in specified circumstances the obligation on the IP to comply with the procurement regime set out in the Water Industry (Specified Infrastructure Projects) (English Undertakers) Regulations 2013 (the Regulations).

In this consultation, which ran from 17 July to 14 August 2015, we asked for views on:

- certain proposed changes made to the draft project licence following Ofwat's initial consultation on a draft project licence in October 2014 and input from bidders;
- the capacity of Tideway to be a licensed infrastructure provider;
- whether Allianz Infrastructure Luxembourg I S.a.r.l; Amber Infrastructure Group Holdings Limited; International Public Partnerships Limited (IPP); and Dalmore

Capital Limited, as owners of Tideway, were the appropriate entities to provide 'ultimate controller' undertakings¹; and

- Ofwat's intention to issue a waiver notice dis-applying the obligation on Tideway to comply with the procurement regime set out in the Regulations in respect of specified contracts and for specified circumstances.

This document summarises the responses we received to this consultation. All the responses were carefully considered before finalising and granting the project licence and issuing the waiver notice.

2. Background

On 7 October 2014 Ofwat published a [consultation on the regulatory framework](#) that was intended to regulate any IP appointed to deliver the project. The consultation invited comments on the following three documents: (i) a draft project licence intended to be issued to the IP; (ii) draft economic guidance to be issued by Ofwat setting out how Ofwat intended to regulate the IP; and (iii) a draft explanatory note to be issued jointly by Ofwat and the Environment Agency setting out how both authorities were likely to apply their existing enforcement policies in the context of the project.. This consultation ended on 17 November 2014 and we received four responses. We published a [responses document](#) that summarised the main issues raised as Appendix A to our July 2015 consultation on whether to grant a project licence to Tideway and issue a waiver notice.

As part of our July 2015 [consultation](#), we provided in Annex B a revised track change draft of the project licence highlighting all the changes made to the draft project licence since the consultation held in October 2014 and following input from bidders in the procurement process for the IP, as well as a table in Annex C summarising the main changes made.

¹ All water and sewerage companies are obliged to get undertakings from their owners. Such undertakings strengthen the ability of the licensed entity to comply with its licence obligations and to maintain independence from any associated companies to which it is related

3. Responses to the consultation

In response to our consultation on whether to grant a project licence to Tideway and issue a waiver notice, we received six responses:

- The Consumer Council for Water, which expressed its concern that the complexity of the project and the consultation document made it difficult for customers to respond and it asked about ongoing review of the costs of the project by Ofwat in order to ensure value for money for customers;
- Thames Water, which expressed its support for the issue of a project licence and a waiver notice; and
- Four individuals, all of whom expressed opposition to the project on the basis that they did not consider it to be the best solution and did not consider that it will provide value for money for customers.

None of these responses raised issues which resulted in any material changes being made to [the project licence or the waiver notice](#).

We also received a request for additional information from some of the respondents to the consultation and from Thames Blue Green Economy, which made its request under the Environmental Information Regulations 2004. In summary, the information requested related to the project's costs and technical specifications. In addition, copies of some of the commercial agreements were requested.

The documents requested were not considered to be relevant to this consultation as the consultation concerned Tideway's suitability and the suitability of its shareholders to assume their respective roles in the context of the regulatory framework in which they would operate. The nature of the regulated obligations that Tideway and its shareholders would be assuming was evident from regulatory documentation which either had been in the public domain for some time or which formed part of the consultation process.

Although Ofwat considered that the additional information requested was not relevant for responding to the consultation and for the most part was exempt from disclosure given that the procurement of the IP was still a live process at the time, we did make [some further information available](#) on costs and contract structure on 7 August 2015.

Other information requested during the consultation, which was considered to be commercially confidential at the time because of the live procurement process, has now been made available. On 7 September 2015 Government issued a [Written Ministerial Statement](#) to Parliament and made available redacted versions of the Liaison Agreement and the [various contracts that make up the Government Support Package](#).

Redacted versions of the other project documents requested [are currently available on the Tideway website](#), namely the Revenue Agreement; the Interface Agreement; and the Project Management Contract.

The table that follows summarises the main issues raised in the responses to the consultation on whether to grant a project licence to Tideway and issue a waiver notice and Ofwat's responses to those issues.

Table 1 Main issues raised in response to the consultation

Respondents	Issue raised	Ofwat response
Consumer Council for Water and an individual respondent	<p>Complexity</p> <p>The complexity of the consultation document made it difficult for Thames Water customers to respond</p>	<p>Ofwat acknowledges that the project is complex and that the regulatory framework which has been established for the infrastructure provider is new. However, Ofwat considers that sufficient clear information in relation to the project and the proposed regulatory framework was provided to enable interested parties to respond. The July 2015 consultation document provided a clear overview of the regulatory framework for specific infrastructure projects and the proposed infrastructure provider in Section 3 and the legal framework relating to the waiver notice in Section 4. Moreover, Ofwat considers that the July 2015 consultation formed the final part in a series of consultations by both the Department for Environment, Food & Rural Affairs (Defra) and Ofwat, including Ofwat's consultation of 7 October 2014 on the regulatory framework applicable to the IP that will deliver the project, all of which sought to set out the proposed project and/or regulatory framework in a transparent and clear way. Throughout the different consultation processes, Ofwat has been willing to discuss and explain the regulatory issues arising from specified infrastructure projects; for example at their request Ofwat discussed with the Consumer Council for Water the provisions of the proposed project licence intended to be issued to an infrastructure provider following its consultation of 7 October 2014. .</p>
Consumer Council for Water and two of the individual respondents	<p>Value for money for customers</p> <p>Whether there will be ongoing scrutiny of the IP's contractual arrangements to ensure customers receive value for money</p> <p>Questioning Ofwat's protection of customers and whether the project offers value for money for customers</p>	<p>We have scrutinised and challenged Thames Water's costs in respect of the project and established incentives to efficient delivery (as evidenced by the outcome of our price review last year).</p> <p>In respect of the IP's costs, we have ensured value for money by establishing incentives to efficient delivery and by exercising oversight over the:</p> <ul style="list-style-type: none"> • development of the project agreements (including the project management contract); • procurement of the IP by Thames Water to ensure that value for money is achieved in respect of financing and construction costs; and

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Respondents	Issue raised	Ofwat response
		<ul style="list-style-type: none"> • appointment of an Independent Technical Assessor (ITA), who will owe a duty of care to Ofwat (as well as to other stakeholders) and who will review the progress of the project (including costs) and report regularly to the key stakeholders including Ofwat, Government, Thames Water and the IP. <p>Following a competitive procurement process run by Thames Water, Tideway was chosen to be the preferred IP bidder, and the cost of capital for the project (2.497%), has resulted in a significant reduction in the cost to customers than had previously been forecast.</p> <p>Previous downside forecasts had predicted the impact of the project on average bills would be £70 to £80. In fact the impact is now expected to be much lower than this: around £20 to £25 per year by the mid-2020s. £7 of this is, on average, already included in current bills.</p> <p>Thames Water also conducted a competitive procurement to choose the preferred main works contractors:</p> <p>BMB JV (Joint Venture of BAM Nuttall Ltd, Morgan Sindall Plc and Balfour Beatty Group Limited) for the West contract, FLO JV (Joint Venture of Ferrovia Agroman UK Ltd and Laing O'Rourke Construction) for the Central contract and CVB JV (Joint Venture of Costain, Vinci Construction Grands Projets and Bachy Soletanche) for the East contract.</p>
Consumer Council for Water and an individual respondent	<p>Equity Commitment and financing structure</p> <p>Concern that the commitments of investors fall short of the equity required to complete the project</p> <p>Considers that the funding structure is deeply flawed and only 'part-committed'</p> <p>Considers that the IP funding structure is not straightforward;</p>	<p>A regulated water company's management and investors are responsible for determining the company's capital and financing structure, and they, not customers, bear the risk associated with it. This principal equally applies to Tideway.</p> <p>The weighted average cost of capital (WACC) for the project of 2.497% was bid by Tideway rather than being determined by Ofwat. This figure along with details of Tideway financing was considered until licence award to be commercially confidential by both Thames Water as procuring authority and Tideway's investors.</p> <p>In bidding a fixed WACC Tideway will have made assumptions as to return on equity, cost of debt and other factors. The risk and reward associated</p>

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	<p>suggests a mutual as an alternative structure</p> <p>Disappointed that further details re: allowed return on equity and borrowing were not provided as part of the consultation</p>	<p>with the underlying assumptions and the WACC rests principally with Tideway.</p> <p>Similar to other utilities Tideway will finance construction of the project through shareholder investments, debt raised and monies received from customers. Not all of the funding required to complete the project was required to be in place at licence award. Making this an obligation would have significantly increased the cost to customers.</p> <p>A significant level of financial commitment was however required to be demonstrated at licence award, particularly from equity providers. These commitments alongside Tideway's financing plan resulted in investment grade credit ratings being assigned to Tideway.</p> <p>Equity providers were required to provide a minimum of £400 million upfront in either cash or letters of credit. Tideway's investors went beyond this requirement, in providing fully supported upfront equity commitments alongside a committed bank credit facility of circa £1 billion. Ofwat considered that an appropriate level of finance commitment was in place at licence award – a level that provided confidence in the financing of the project while not imposing unnecessary costs on customers.</p> <p>Tideway proposes to finance the project with a mix of shareholder provided funds (equity and loans) and third party debt (listed bonds, European Investment Bank loans and bank facilities). In respect of the shareholder provided funds Tideway proposes to inject funds in the form of 40% equity and 60% subordinated loans.</p> <p>Before granting the licence, Ofwat was satisfied that Tideway was able to finance the project up to the threshold outturn. The threshold outturn is defined in the project licence as £4,087,726,822 (being about 30% more than the original base case forecast).</p> <p>Although there was nothing in the project licence to prevent a mutual-type structure, it was considered that the scale, complexity and risk profile of the project is more appropriately financed using equity risk capital.</p>
Individual respondent	Board Governance	As set out in our consultation , in order to ensure that Tideway is a competent body to hold a project licence, we reviewed the financial,

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	<p>Queries what assurances Ofwat received from Tideway, in relation to its adherence to the board leadership, transparency and governance principles published by Ofwat</p>	<p>management and investment structure proposed by it for the project. The proposed composition of the Tideway board is in accordance with Ofwat's published board leadership, transparency and governance principles and Tideway has committed to comply with these principles in the future.</p> <p>We will review how Tideway is meeting our principles as part of our annual monitoring of companies' performance in this area. As this year, this review will focus on relevant information in companies' annual reporting.</p> <p>As set out in our consultation, we have also obtained undertakings from each of the ultimate controllers and UK holding companies of Tideway, as we do for all companies that we regulate.</p>
<p>Consumer Council for Water</p>	<p>Ultimate controllers Queried tax status of Bazalgette Ventures Limited; also queried why DIF and Swiss Life were not being asked to provide ultimate controller undertaking</p>	<p>Ahead of licence award it was agreed that DIF would provide both an ultimate controller undertaking and a separate undertaking from its UK holding company (as DIF is a non-UK resident entity). While Swiss Life has a significant shareholding, voting control over the Swiss Life shares in Tideway lies with Amber Infrastructure (under a separate management agreement between Swiss Life and Amber Infrastructure). For this reason we required Amber to provide an undertaking in respect of the Swiss Life shareholding. Should the agreement between Amber and Swiss Life come to an end we have already advised Swiss Life that we would require them to provide equivalent undertakings.</p>
<p>Consumer Council for Water and an individual respondent</p>	<p>Risk allocation CCWater queried risk allocation if costs go above the original base case forecast and asked how those risks have been mitigated Individual respondent thought Thames Water customers and tax payers were bearing 'high and unacceptable' risk</p>	<p>The risk allocation between different parties involved in the project was designed based on a number of interrelated principles including allocating risks to the party best able to manage the risk and achieving value for money for customers.</p> <p>Specifically, the risk on cost overruns during construction is shared between the main works contractors, Tideway, Thames Water's customers and Government.</p> <p>Cost overruns up to the threshold outturn are shared between the main works contractors, Thames Water, Tideway investors and customers.</p>

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		<p>If the project is delivered for less than the original base case then customers, main works contractors, Thames Water and investors will share the benefits, with customers receiving 70% of the net benefits. This type of risk sharing arrangement is in line with the rest of the industry, and aims to provide a suitable incentive to manage costs efficiently, while also ensuring the risk exposure is at a level where finance was obtainable on competitive terms.</p> <p>In order to attract finance and achieve value for customers, the Government is providing contingent support for high impact, low probability events. However, Tideway remains responsible for financing the project up to the threshold outturn. Only if it is likely that the threshold outturn will be exceeded can Tideway request that the Government provide equity finance to cover costs above the threshold outturn.</p> <p>Details of the contingent Government Support Package for this project were announced in a Written Ministerial Statement on 5 June 2014 and further details were issued on 7 September 2015.</p>
Individual respondent	<p>Incentives</p> <p>Considers that the incentives related to the project are largely about 'beating indices' and essentially adopt a "cost plus approach"</p>	<p>We do not consider that the licence provides "an essentially cost plus approach." To incentivise Tideway to deliver the project on time and on budget the project licence includes developments of existing regulatory mechanisms. These mechanisms are applied on an ex post basis, following construction, by way of the revenue and/or RCV adjustment and thus they may impact the revenues of Tideway throughout the operational life of the project. Additionally the incentives are asymmetrical in that the pain suffered by Tideway for underperformance is greater than the gain it may achieve through outperformance.</p>
Individual respondent	<p>Ofwat's legal powers</p> <p>Queried the legal powers under which Ofwat awarded a licence to the IP and asked how Ofwat has balanced its duties to customers. This respondent also asked whether</p>	<p>Under the Regulations, either Ofwat or the Secretary of State may by notice designate as an infrastructure provider a company which appears to Ofwat or the Secretary of State to be wholly or partly responsible for the specified infrastructure project that was put out to tender in accordance with the Regulations. A designation notice may be subject to such conditions as Ofwat or the Secretary of State considers appropriate, including the</p>

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	Ofwat was acting on the open, or covert, instruction of ministers	<p>condition that the designated infrastructure provider is granted a project licence for the project by Ofwat under section 17FA of the Water Industry Act 1991 (as applied by the Regulations) (the modified Act).</p> <p>Section 17FA of the modified Act empowers Ofwat to grant a project licence to a designated infrastructure provider and such a project licence may be made subject to conditions under section 17HA of the modified Act. Section 17FA (2) of the modified Act requires Ofwat to consult before issuing such a project licence. The project licence awarded to Tideway was issued under these provisions of the modified Act.</p> <p>In awarding a project licence, under section 2 of the modified Act Ofwat is required to exercise and perform our relevant powers and duties in a manner which we consider is best calculated to , for example, secure that efficient undertakers and infrastructure providers can finance their functions and, separately, protect the interests of consumers, wherever appropriate by promoting effective competition.</p> <p>In applying our general duties, following extensive discussions with Government, Thames Water and relevant professional advisers, we concluded that customers would be better protected if the infrastructure provider for the Thames Tideway Tunnel project was a regulated entity with a project licence. We believe that our view has been proved correct by the very low WACCs received from both short listed bidders. The indication we received from relevant financial advisers was that without the certainty that comes from being a regulated entity, investors would not have had the same confidence in the procurement.</p> <p>Ofwat wants to stress that it did not, and does not, act on any open, or covert, instructions of ministers. As an independent statutory body we are required to act consistently with the statutory framework provided by Parliament.</p>

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Individual respondents	<p>The need for the project</p> <p>Challenged the need for the project and suggested alternative solutions</p> <p>Considers that the need for the project is based on 'false or redundant technical information (amounting to 'fiscal fraud'); and refers to past, current and future legal proceedings</p>	<p>The decision that the project is necessary to comply with the requirements of the Urban Waste Water Treatment Directive² was made by Thames Water, and confirmed by Government, in 2007 following a number of in-depth studies. The project was considered to be the optimum solution, alongside the Lee Tunnel and five London sewage treatment works upgrades (together the Thames Tideway Improvement Scheme).</p> <p>Since then, a number of expert opinions and studies have concluded that the alternative approaches proposed are not viable for meeting the environmental objectives set by Government including the need to address the judgment of the European Court of Justice³ that the UK is in breach of the Urban Waste Water Treatment Directive.</p> <p>For example, the alternative of sewer separation across London would be significantly more expensive than the project and would result in massive social and economic disruption during construction.</p> <p>The use of dispersed detention tanks was also considered. However, this would require large land areas and would be expensive if designed to provide the same storage capacity as the project which is effectively a very large pipe and storage tank. Another alternative were floating booms as these can be effective in certain situations. However, they are impractical to install in a fast flowing river and would impinge upon navigation. They would also have a high capital cost and would require expensive operational activities to remove sewer litter. Additionally, floating booms would not be possible to install in some locations such as where CSOs discharge under bridges.</p>

² Directive 91/271/EEC.

³ Case C-301/10, judgment of 18 October 2012.

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		<p>Sustainable Urban Drainage Systems (SUDS) present a good solution in new builds and where soil conditions are suitable. However, in order to have the same benefits as the project, the scale of SUDS required as a retrofit across London today would be costly, disruptive and take decades to construct. It is relevant to note that several SUDS applications have been planned and installed across the UK including in Thames Water's sewerage services area and Ofwat supports their adoption where practical.</p> <p>We have no knowledge of any current legal proceedings challenging any decision that has been taken in respect of the project.</p>
Individual respondent	Review of report by Professor Binnie Queries why recent evidence from Professor Chris Binnie (that the project is not needed) has not been considered	<p>We have considered Professor Binnie's December 2014 report and are of the view that his analysis is deficient in a number of respects. His report uses statistical manipulation of dissolved oxygen (DO) data to argue that the tidal River Thames is already meeting water quality standards. We are of the view that the method used by Professor Binnie misinterprets how breaches of the four DO standards are counted and how data across a tidal cycle is used. We consider that this report erroneously averages data across the ebb and flow of a tidal cycle resulting in a higher value of DO and therefore does not truly reflect the low values recorded during the tidal cycle. In our view the argument that the DO standards are met because of this higher, average value is incorrect.</p>
Individual respondents	Licence issues 1) Queries why there is no third party mechanism in the licence for dispute resolution	<p>Similarly to the regulatory regime for water and sewerage undertakers, certain questions under or in connection with the project licence may be referred by Ofwat to the Competition and Markets Authority for determination. Others may be subject to a judicial review by the courts.</p>
	2) Considers the concept of an 'Appropriate Discount Rate' to be nonsensical	<p>The definition of Appropriate Discount Rate is: "such rate of return as...investors and creditors would reasonably expect of a properly managed company holding this project licence whose sole business consists of performing the project." This is a term that is used in all undertakers' licences. When judging the Appropriate Discount Rate it is likely that precedents from other projects/ businesses that share characteristics with Tideway will be considered. While there are no exact precedents in relation to the IP, this does not mean that there are no other</p>

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		<p>projects/ businesses that can be used for comparability or benchmarking purposes. The evidence from this will likely be combined with other considerations (particularly those that are unique to Tideway) to arrive at an overall Appropriate Discount Rate.</p>
	<p>3) Alleges that the IP will receive unfair tax protection under the project licence and that the IP's financing structure is a UK tax evasion mechanism</p>	<p>While some of the ultimate investors are domiciled outside of the UK, Tideway and its holding companies are registered in the UK and domiciled in the UK for tax purposes.</p> <p>During the construction period we understand that Tideway will not, under existing tax legislation, be considered to be "trading" and as such will not be liable to pay corporation tax during the construction period. We understand that this is not a bespoke arrangement established for Tideway but is a consequence of existing tax legislation and interpretation of that legislation. However, there is a possibility that tax legislation or interpretation of the legislation may change during the construction period.</p> <p>Generally water companies are funded within a price control period for corporation tax that they are expected to actually pay during the control period. Assumptions relating to the funding of corporation tax are reset at each 5-year price review to reflect each company's business plans, and legislation and tax rates applicable to it.</p> <p>Unlike other water companies Tideway will not have price limits determined by Ofwat during construction and so this reset mechanism is not available to it. Neither are the normal interim determination mechanisms which provide other companies with a degree of protection against major changes in tax legislation affecting water and sewerage companies during a price control period available to Tideway. This risk is essentially outside the control of Tideway, and requiring Tideway to bear and price this risk was not considered to provide good value.</p> <p>Thames Water has purchased or leased the necessary land for the project, the cost of which has been financed by Thames Water and is funded by its customers within Thames Water's existing price control. On completion of construction, Tideway will enter into a lease in respect of land that it will require to operate and maintain the project. This could give rise to a taxable</p>

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		<p>capital gain but at this time there is significant uncertainty about the potential scale of this tax liability. This uncertainty will only be resolved when the construction is complete, and the risk is essentially outside Tideway's control. Exposing Tideway to this risk would have resulted in bidders taking a conservative view, through the bid WACC, on the potential value of this tax payment, therefore increasing customer costs during construction in a way that was not considered good value.</p>
<p>Individual respondents</p>	<p>Procurement of the IP by Thames Water Alleges non-compliance with procurement regulations by Thames Water and the IP Considers that the IP tender process was 'highly irregular' in particular because there were only two final bids Considers that use of bid WACC to evaluate bids is a 'flawed measure' to assess the financial capacity of a bidder to finance, build and operate the project</p>	<p>Thames Water is subject to the Utilities Contracts Regulations 2006 (UCR) and accordingly procured the IP under the UCR. The evaluation of bids as part of the procurement was largely based on the WACC submitted by tenderers (the bid WACC). Regulation 65(4) of the Public Contracts Regulations 2015 requires that no less than three organisations are invited to negotiate (or if less than three, sufficient numbers to ensure "genuine competition"). By contrast, the UCR does not stipulate a minimum number of economic operators that must be invited to negotiate but instead has a requirement that the utility must take into account the need to ensure "adequate competition" in determining the number of economic operators selected to negotiate the contract. Ofwat exercised an oversight role in respect of the procurement of the IP and we are satisfied that the requirements of the UCR were met. We are also satisfied that there was adequate competition, as evidenced by the low bid WACC that was accepted. This bid WACC is fixed up until 2030. By focussing the financial evaluation on the bid WACC, the process focussed on the tender that had the lowest cost to customers, which was considered an appropriate basis by Ofwat. Thames Water in their evaluation also considered a number of criteria in addition to the bid WACC including deliverability of financing.</p>
<p>Individual respondent</p>	<p>Outcome of procurement of IP</p>	<p>Thames Water's press release sets out that the strong competition for both construction and financing has driven down costs for its 5 million+ bill payers. All of Thames Water's sewerage customers will fund the project. On average annual household bills from April 2015 already include £7 for the</p>

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	<p>Considers that the IP procurement has not resulted in a reduction of projected costs</p>	<p>project and this is estimated to eventually rise to a total of £20 to £25, before inflation. As a result of the costs of finance being lower than anticipated and efficiencies identified through the procurement, this is significantly lower than previous estimates of £70 to £80.</p>
<p>Individual respondent</p>	<p>How the bid WACC compares to the WACC set by Ofwat at PR14 Queries how the WACC was arrived at, and whether Ofwat has changed its position on WACC since PR14</p>	<p>In respect of the WACC and the projected impacts on customers' bills, the WACC applicable during construction is being set by way of a competition. This is a different approach from the methodology applied for PR14 and prior price controls.</p> <p>It is important to note that the WACC was bid by Tideway, not determined by Ofwat, and that the project bid WACC reflects:</p> <ul style="list-style-type: none"> • an atypical risk profile compared to water and wastewater companies and regular wastewater related infrastructure projects; • the highly competitive nature of the IP procurement process; • a bespoke regulatory regime which has been developed specifically for the construction phase of the project; and • a contingent support package from Government which seeks to address investor risks in respect of low probability but high impact unforeseen circumstances. <p>These factors have contributed to a bid WACC (that is lower than the WACC published in our Final Determination for PR14 in December 2014 for the water and wastewater companies) that is designed to support the IP in financing the construction of the project at an efficient cost to customers, whilst maintaining appropriate incentives.</p> <p>In addition, Tideway as a newly created special purpose company has no pre-existing debt, unlike water and wastewater companies which have over the last 25-years accumulated debts which bear historic higher interest rates.</p> <p>For PR14 we assessed that the average real cost of such embedded debt was 2.65% which related, on average, to 75% of a company's total debt during 2015-2020, while our assessed cost of new debt during the control period, representing 25% of the total, was 2.0%. The absence of pre-</p>

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		<p>existing debt removes the impact through the WACC of historic embedded interest rates and the availability of an interest rate incentive mechanism moderates market risk (but not project risk) during the construction period, with the impact shared between investors and customers. Both in part are considered to account for the lower WACC.</p> <p>The bespoke regulatory regime supports the construction of the project and the IP delivery mechanism. We have reflected in the project licence conditions that support and incentivise Tideway during the construction phase, while ensuring that customer's interests are protected and cost impacts controlled.</p>
Individual respondents	<p>Cost-benefit analysis and bill impacts</p> <p>Concerned about bill impacts and affordability; requests review of cost-benefit analysis</p> <p>Asks when Defra's updated cost-benefit analysis might be available</p>	<p>Defra has recently updated its 2011 cost-benefit analysis for the project. Copies of the revised strategic and economic case for the Thames Tideway Tunnel and cost-benefit analysis are available on Defra's website.</p> <p>In relation to affordability, along with other key stakeholders, we have played an active role over the last few years in reviewing and challenging the costs of the project in order to control the impact on bills. As the risks of the project are different from those more usually faced by water and sewerage companies, Thames Water has been required to market test the two main drivers of bills — the cost of construction and the cost of finance. This is a different approach from a formal price cap but it has resulted in value for money for customers.</p> <p>As noted above, previous downside forecasts had predicted the impact of the project on average Thames Water sewerage bills would be £70 to £80 per annum. In fact, as a result of the competitive procurement and wider economic conditions, the impact is now expected to be significantly lower than this: around £20 to £25 per year by the mid-2020s. £7 of this is on average already included in current Thames Water sewerage bills.</p>
Individual respondent	Waiver Notice	

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Respondents	Issue raised	Ofwat response
	<p>Considers that it is unacceptable for Ofwat to issue a waiver notice dis-applying, in specified circumstances and for specified contracts, the procurement requirements set out in the Regulations.</p>	<p>The Regulations sought to ensure that a procurement regime would apply to the incumbent undertaker and the IP in relation to large-scale projects such as the project where the general/utility UK procurement rules are not applicable, an exemption in the UK procurement rules is relied upon or where those rules allow the undertaker or IP to negotiate with one party only. Therefore, the Regulations create a requirement for more, not less, competition in relation to the project and go beyond what is required under UK procurement law. However, regulation 6(8) of the Regulations allows for a waiver notice to be issued in order to dis-apply those additional requirements in limited circumstances. A waiver may be beneficial, for example, in circumstances where the cost of running a tender procedure is likely to outweigh the benefits which would be generated by additional competition. In circumstances such as those, a waiver notice is clearly appropriate and in the best interests of consumers.</p> <p>The reasons for our decision to issue the waiver notice in relation to the project may be found here. In respect of specified construction related contracts, we are satisfied that customers are protected in that the specified contracts have all been subject to a robust competitive process conducted by Thames Water. With regard to the project management contract, we are satisfied that the original appointment of the project manager (CH2MHill Inc.) by Thames Water in 2008 was subject to a competitive process and that its continued involvement in the management of the project is efficient and likely to result in value for money for customers</p>
Individual respondent	<p>NAO report Queries whether Ofwat has met National Audit Office (NAO) expectations in particular by carrying out gateway reviews of the project at important points</p>	<p>A report from the NAO makes a number of recommendations, most of which are project wide and not directed specifically at Ofwat. Ofwat has had regard to these and taken appropriate steps to meet them. For example, we have drafted a project licence that includes appropriate mechanisms for protecting customers and we exercised oversight over the development of the project contracts (including the project management contract).</p> <p>Gateway reviews are carried out by the Cabinet Office. The NAO report said that appraisal of different strategies and options should be revisited from time to time. In response to this, five Project Assessment Reviews were conducted by the Cabinet Office Major Projects Authority over the last three</p>

Summary of responses to the Infrastructure Provider Project Licence Award consultation
(17 July to 14 August 2015)

Respondents	Issue raised	Ofwat response
		and a half years, with the last being in March 2015. Ofwat has participated in these reviews. In addition, Thames Water has carried out separate independent progress reviews during the development of the project.
Individual respondent	Requests dates of all meetings when the Ofwat Board has considered the project and also requests relevant minutes	<p>The development of the regulatory framework for the IP has been regularly considered by the Ofwat Board. It is a standing item in the Chief Executive's report to the Board and has been a separate agenda item at Board meetings since October 2005. The Board has considered in particular:</p> <ul style="list-style-type: none"> • the main provisions of the draft project licence for the IP; • the rationale for pursuing an IP model consistent with a regulated utility; and • Ofwat's role in the IP procurement process and the parallel licensing process. <p>In addition, in early 2015, a Board Committee was established to exercise oversight in respect of Ofwat's continuing role in the project and to take certain specified decisions in respect of the project. The Board Committee, which comprises predominantly non-executive members of the Ofwat Board, is chaired by the Ofwat Chairman Jonson Cox, and has met 6 times so far this year. The responses to this consultation were considered by members of the Board Committee and the decisions to grant the project licence and issue the waiver notice were taken by the Board Committee.</p>
Thames Water	Considers that Tideway is a fit and proper entity to be licensed as IP	We have noted and agree with Thames Water's view that in addition to our fit and proper assessment of Tideway, there was also a robust assessment process of all bidders in the IP procurement which included assessment of the financial ownership structure of bidders.
	Supports our proposals to issue a Waiver Notice in relation to specified contracts	We have noted Thames Water's support in respect of these proposals.