



## Reasons for issuing a Waiver Notice

### Introduction

On 24 August 2015 Ofwat awarded a project licence to Bazalgette Tunnel Limited (now referred to as Tideway) to carry out all activities described in the [Project Specification Notice](#) apart from those activities that Thames Water is to carry out under the [Preparatory Work Notice](#) in respect of the Thames Tideway Tunnel Project (the Project).

At the same time, we issued a [notice](#) under regulation 6(8) of the Water Industry (Specified Infrastructure Projects) (English Undertakers) Regulations 2013 ([the SIP Regulations](#)) dis-applying to a limited extent Tideway's obligation to apply the procurement provisions set out in the SIP Regulations. When we refer to a Waiver Notice we are referring to this notice which dis-applies, in limited circumstances, the requirement on the infrastructure provider (IP) to conduct a regulated tender process. In accordance with section 195A of the Water Industry Act 1991 (as applied by the SIP Regulations), this notice sets out the reasons for our decision to issue a Waiver Notice.

### Relevant background

The SIP Regulations apply a procurement regime to the Project which the incumbent water or sewerage undertaker (in this case Thames Water) or the designated licensed IP (in this case Tideway) must follow in circumstances where the Utilities Contracts Regulations 2006 (the UCR) or the Public Contracts Regulations 2015 (the PCR) do not impose a requirement to conduct a competitive tender process. However, regulation 6(8) of the SIP Regulations permits Ofwat to issue a notice to dis-apply this regime (or aspects of the regime) in relation to the licensed IP.

After consultation, Ofwat exercised its discretion to issue a Waiver Notice in respect of:

- A. specified construction related contracts; the project management contract (PMC) and a Management Services Agreement (MSA);
- B. all contracts below a specified threshold value;
- C. all contracts that fall within some general exemptions that are available to utilities under the UCR.

The [consultation on the Waiver Notice](#) was part of a consultation on our intention to issue a project licence to Tideway. We received six responses to this consultation, only two of which referenced the Waiver Notice. Neither of these responses resulted in any material changes being made to the Waiver Notice. The first response was from Thames Water and it supported the issue of the Waiver Notice. The second was from an individual who did not support the issue of the Waiver Notice and who raised a number of general questions about whether Thames Water had complied with the relevant procurement requirements in its procurement of the IP.

## Waiver in respect of specified construction contracts

Schedule 1 to the Waiver Notice lists the following contracts in respect of which the waiver applies:

- the three main construction contracts and the System Integrator Contract;
- the contract for the services of an Independent Technical Assessor;
- two framework agreements – one dealing with occupational health and the other dealing with access control and security.

In relation to the above specified contracts, we were satisfied that customers would be protected because the specified contracts were all subject to a competitive process conducted by Thames Water under the UCR. Thames Water procured all these contracts on behalf of the IP. In some instances, these contracts were novated to the IP by Thames Water, once the IP had been appointed, and in other instances the IP entered into these contracts itself, following its appointment.

Thames Water consulted Ofwat and Government prior to adopting a procurement strategy that was designed to facilitate the procurement of the construction contracts and the procurement of the IP taking place in parallel. The alternative to this approach would have been for Thames Water to first procure an IP and for the IP to then procure the construction and other contracts. We agreed with the approach because:

- bidders for the IP were asked to bid a weighted average cost of capital (WACC) and without cost information gleaned from the procurement of the construction contracts this would have been difficult;
- had Thames Water first procured the IP on the basis that the IP would then procure the construction contracts it would not have been possible to award the construction contracts in 2015 to enable construction to begin in 2016. This would have prolonged the period of non-compliance with the Urban Waste Water Treatment Directive and exacerbated the consequences of such non-compliance.

## **Waiver in respect of the Project Management Contract (PMC) and Management Services Agreement (MSA)**

Schedule 2 to the Waiver Notice applies the waiver to the PMC and the MSA. The PMC has been entered into between Tideway and CH2MHill Inc. (CH2M) and the MSA has been entered into between Tideway and Thames Tideway Tunnel Limited, a subsidiary of Thames Water set up as a dedicated project team that would transfer to the IP following licence award.

CH2M was initially appointed by Thames Water in 2008 following a competitive procurement process, to provide project management services to Thames Water in respect of the Thames Tideway Tunnel. To provide continuity and a transfer of necessary skills, Thames Water negotiated a new contract with CH2M and the IP was required, as part of the procurement process, to enter into this new contract with CH2M.

We considered that the continued involvement of CH2M in the management of the project was efficient and likely to result in value for money for customers. We therefore agreed that the IP should not be required to tender for a PMC provided that the terms of the contract that the IP was required to enter into with CH2M had been subject to an independent bench marking exercise and only core skills and experience were transferred to the IP under that contract. This was done and we were consequently satisfied that customers would be protected and the arrangement represented value for money in that:

- the IP was able to start delivering on its obligations immediately after appointment;
- if the IP had been obliged to procure its own PMC, the competition for an IP may have been distorted if CH2M Inc., as the incumbent service provider, had joined the consortium of one particular bidder, whereas the proposed arrangement meant CH2M was made available to all bidders on an equal footing.

The MSA is a contract between Tideway and the Thames Tideway Tunnel Limited, which was acquired by Tideway as part of the procurement for an IP. We agreed to extend the waiver to include the MSA as this is proposed to be a temporary agreement pending Tideway making alternative arrangements and any services under the MSA will be at cost.

## **Value threshold for application of waiver**

The UCR do not apply to the award of low-value contracts which are estimated to fall below certain prescribed value thresholds. There is no equivalent provision in the SIP Regulations which means that, without the Waiver Notice, the IP would have had

to conduct a regulated tender process for all contracts, irrespective of the value of the contract.

In awarding low-value contracts, we consider that the IP should be treated in the same way as water and sewerage undertakers and we are therefore applying a generic exemption that dis-applies the Regulations for all contracts below the value thresholds in the UCR (see schedule 3 of the Waiver Notice). We are adopting a minimum value threshold for the following reasons:

- the IP can be compared to a medium sized water and sewerage company and we therefore consider that there are good grounds for treating it in a similar manner to such comparator companies in some circumstances;
- it is considered disproportionate to require that the IP follow an OJEU process for all contracts irrespective of the estimated value of those contracts; and
- the IP is incentivised to bring the project in or under budget so we are satisfied that it will carry out appropriate procurement processes to ensure value for money.

## Other exemptions under the UCR

In line with the principle outlined above, we consider that the IP, in carrying out its procurement activity, can be treated in a similar manner to a medium sized water and sewerage company in some circumstances. Accordingly, the Waiver Notice extends to the IP a number of the general exemptions that are available to water and sewerage companies under the UCR but that are not available to the IP under the procurement regime set out in the SIP Regulations. The Waiver Notice does this by including, in paragraph 5(c), cross references to general exemptions in the UCR that exempt utilities from seeking offers in respect of:

- services which are to be provided by a contracting authority where that contracting authority has an exclusive right (under law) to provide those services or which is necessary for the provision of the services;
- the acquisition of land or of any interest in land;
- arbitration or conciliation services;
- financial services in connection with the issue, purchase, sale or transfer of securities or other financial instruments, in particular transactions by the relevant entity to raise money or capital; and
- works or services concession contracts<sup>1</sup>.

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<sup>1</sup> See Regulation 6; sub-paragraphs (i) – (m) and (o) of the UCR for equivalent provisions applicable to utilities.

## Conclusion

If the Waiver Notice had not been issued, the IP would have been obliged to conduct a fresh tender process in respect of the construction contracts and would have had to procure a PMC. We do not consider that this would have provided value for money for customers and consider that issuing the Waiver Notice in respect of the contracts listed in schedules 1 and 2 to the notice will ensure that the project benefits from continuity, technical expertise, bidder certainty and improved commercial terms, resulting in enhanced customer value for money.

We consider that as the IP is equivalent to a medium sized water and sewerage company, it is proportionate that it should be required to follow a procurement regime that is broadly similar to the regime that applies to water and sewerage companies. For this reason, we considered that it was appropriate to extend some of the general exemptions that are available to utilities under the UCR to the IP.