



Water 2020
Ofwat
21 Bloomsbury Street
London
WC1B 3HF

10 February 2016

Dear Sir/Madam,

Water 2020: Regulatory framework for wholesale markets and the 2019 price review

We are pleased to respond to Ofwat's consultation on the regulatory framework for wholesale markets and the 2019 price review. Although as an Infrastructure Provider Tideway's regulatory arrangements differ somewhat from those of undertakers, certain elements of the consultation are directly or indirectly relevant to Tideway. The attached consultation response focuses on the issues of most relevance for Tideway.

The proposed shift from RPI to CPI indexation would be a significant change to well-established regulatory arrangements, under which the industry has successfully financed £120 billion of investment since privatisation. It is important that the sector addresses its future challenges and maintains its legitimacy with all stakeholders. This has implications for several aspects of the potential shift from RPI to CPI, which should be considered further as Ofwat develops its detailed proposals. For example the need for legitimacy implies that any switch to CPI should move in parallel with the development of a market for CPI-linked gilts and corporate debt.

Ofwat has proposed a specific approach for the transition to CPI. It may be beneficial to explore the option of protecting the proportion of RCV funded by RPI-linked debt for each company. This would provide a flexible mechanism that could reflect the development of the market for CPI-linked debt and allow companies to continue to make efficient financing decisions. Rather than introducing a short term transitional mechanism there may be benefits for all stakeholders from an enduring approach supported by a licence modification in order to ensure NPV neutrality and maintain confidence.

Irrespective of the mechanism, regulatory certainty is central to minimising the cost of change for customers and companies. Tideway's regulatory arrangements are fixed to 2030, with RPI applying to RCV and revenues. For Tideway, the certainty provided by our licence and Ofwat's guidance on the economic regulation of the infrastructure provider for the Thames Tideway Tunnel underpinned a successful procurement process that has provided value for money for customers. We would welcome confirmation from Ofwat that it is not intending to modify Tideway's licence for the pre-2030 period with respect to indexation, and that the approach post-2030 will be carefully considered in the light of Tideway's circumstances and the basis of the procurement process. We are happy to engage further with Ofwat as it develops its proposals.

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Other industry reforms will have indirect impacts on Tideway, for example the separation of wholesale wastewater price controls may affect the mechanics of the collection of Tideway's revenue. It will be important for Tideway's arrangements to be considered during implementation so that commercial arrangements around revenue, agreed during the procurement process, are maintained.

We support Ofwat's emphasis on stakeholder engagement. Stakeholders are important to Tideway and engagement is a high priority in delivering the project successfully. Best practice in stakeholder engagement is likely to look different for Tideway than for undertakers as Tideway is a wholesale company delivering a specific project. We are happy to engage with Ofwat to discuss our approach to stakeholder engagement.

As Ofwat has identified, the experience of the Tideway procurement could provide useful lessons for the further development and use of direct procurement in the sector. Drawing on this experience, it will be important to develop a model that is proportionate to the size of the scheme. We are happy to work with Ofwat to consider the benefits of the Tideway procurement and how these might be replicated.

We look forward to engaging with Ofwat and the rest of the sector as Water 2020 proposals are developed further.

Yours sincerely

A handwritten signature in black ink that reads "Matt Parr". The signature is written in a cursive, slightly slanted style.

Matt Parr

Head of Regulation and Business Planning