

**Consultation on modifications to Thames  
Water's Instrument of Appointment  
required to give effect to the Thames  
Tideway Tunnel project**

## About this document

The purpose of this document is to seek comments on a proposal to modify Thames Water's Instrument of Appointment to enable Thames Water to implement the Thames Tideway Tunnel project. The proposed modifications are attached to this document as appendix 1. These modifications are being made with the consent of Thames Water under section 13 of the Water Industry Act 1991.

In this document, we set out:

- an overview of the regulatory framework for specified infrastructure projects;
- an overview of the proposed modifications to Thames Water's Instrument of Appointment; and
- a proposed timetable.

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Appendix 1: Proposed modifications to Thames Water's conditions of appointment necessary to give effect to the proposed appointment of an infrastructure provider to deliver the Thames Tideway Tunnel project – A consultation under section 13 of the Water Industry Act 1991

## Responding to this consultation

We welcome your responses to this consultation by close of business on 16 March 2015.

You can email your responses to [mala.shetty@ofwat.gsi.gov.uk](mailto:mala.shetty@ofwat.gsi.gov.uk) or post them to:

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If you wish to discuss any aspect of this consultation, please contact Mala Shetty on 0121 6447693 or by email at [mala.shetty@ofwat.gsi.gov.uk](mailto:mala.shetty@ofwat.gsi.gov.uk).

We will publish responses to this consultation on our website at [www.ofwat.gov.uk](http://www.ofwat.gov.uk), unless you indicate that you would like your response to remain unpublished. Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with access to information legislation – primarily the Freedom of information Act 2000 (FoIA), the Data Protection Act 1998 and the Environmental Information Regulations 2004.

If you would like the information that you provide to be treated as confidential, please be aware that, under the FoIA, there is a statutory 'Code of Practice' which deals, among other things, with obligations of confidence. In view of this, it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information, we will take full account of your explanation, but we cannot give an assurance that we can maintain confidentiality in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on Ofwat.

## 1. Introduction

The Thames Tideway Tunnel project (the Project) is of unprecedented scale, size and complexity in the water sector in England and Wales and will be the first project to be delivered under a new regulatory framework. That framework allows for certain large and complex infrastructure projects to be delivered by infrastructure providers that:

- are appointed by the incumbent undertaker following a competitive procurement; and
- are regulated by Ofwat under a project licence.

The Project is the first to be delivered under this new regulatory framework and an infrastructure provider is currently being procured by Thames Water to deliver the Project. The modifications to Thames Water's Instrument of Appointment, set out in annex A, are considered necessary to facilitate the delivery of the Project by an infrastructure provider.

The modifications in annex A have been agreed with Thames Water and this consultation is therefore taking place under section 13 of the Water Industry Act 1991 (the Act).

This consultation must also be seen in the context of other consultations on the Project. In October 2014 we consulted on the regulatory framework that will regulate an infrastructure provider (IP) appointed to deliver the Project. That consultation may be found on our [website](#). In response to the consultation on the regulatory framework we received four representations – from the Consumer Council for Water (CCWater), a London borough and two individuals.

In October 2014, we also consulted on a first set of modifications to Thames Water's licence necessary to give effect to the Project. Those modifications came into effect on 8 December 2014 and enabled Ofwat to determine a separate Thames Tideway Tunnel price control for those costs that will be incurred by Thames Water in connection with the Project over the next five year period. In response to the consultation on the first set of modifications to Thames Water's licence, we received three representations – from Thames Water, from CCWater and from an individual. The consultation, the representations received, our response to the representations received and the final modifications are also available on our [website](#).

On 26 January 2015 we started consulting on a proposal to amend guidance that we issued in July 2014 on the factors we will take into account in specifying a project as an infrastructure project. The consultation closes on 23 February 2015 and is also available on our [website](#).

## **2. Overview of the regulatory framework for specified infrastructure projects**

The Flood and Water Management Act 2010, among other things, amended the Act by inserting a new part 2A – Regulation of Provision of Infrastructure. Regulations made under Part 2A were made on 27 June 2013, coming into force on the 28 June 2013. These regulations are the Water Industry (Specified Infrastructure Projects) (English Undertakers) Regulations 2013 (the SIP Regulations).

The SIP Regulations provide that:

- the Secretary of State or Ofwat may specify certain infrastructure projects which must be put out to competitive tender by the incumbent water or sewerage undertaker;
- the Secretary of State or Ofwat may specify an infrastructure project to be put out to tender only if the Secretary of State or Ofwat is of the opinion that:
  - the infrastructure project is of a size or complexity that threatens the incumbent undertaker's ability to provide services for its customers; and
  - specifying the infrastructure project is likely to result in better value for money than would otherwise be the case;
- where an infrastructure project has been specified, the incumbent water or sewerage undertaker will be prohibited from undertaking the project itself other than in relation to certain preparatory work; and
- the successful company that is awarded the tender may be designated by the Secretary of State or Ofwat as an 'infrastructure provider'(IP) for the purposes of the SIP Regulations and the Act, and may be directly regulated by Ofwat under the terms of a newly-established 'project licence'.

For the purpose of regulating specified infrastructure projects, the SIP Regulations introduce new provisions into the Act and also apply particular provisions of the Act with or without modification (the modified Act). So, for example:

- new provisions enable Ofwat to issue a project licence to a designated IP, subject to any conditions that Ofwat considers to be requisite or expedient (sections 17FA and 17HA of the modified Act);
- a licensed IP may charge either end user customers or an undertaker for its services (modified section 142 of the modified Act); and
- Ofwat may take enforcement action against an undertaker or a licensed IP if the undertaker or IP breaches its statutory or licence obligations or if it causes another undertaker or licenced IP to breach its statutory or licence obligations (modified section 18 of the modified Act).

On 4 June 2014, following a public consultation, the Secretary of State specified the Project under the SIP Regulations. The Project Specification Notice became effective on 5 June 2014. At the same time, the Secretary of State issued a Preparatory Work Notice in respect of the Project. The issue of these documents means that:

- the modified Act now applies to the Project;
- Thames Water (as the incumbent undertaker) was required to put the Project out to tender, which it did on 10 June 2014, placing a contract notice in the Official Journal of the European Union (OJEU); and
- the works set out in the Preparatory Work Notice are works in relation to the Project which Thames Water must (and in some cases may) carry out.

The Project Specification Notice sets out the scope of the Project, and at a high level, describes the Project as including:

- the design, construction, testing and commissioning of the Project and associated infrastructure; and
- once constructed and accepted by Thames Water, the operation and maintenance of certain IP-owned structures.

The Project Specification Notice and the Preparatory Work Notice are available on Defra's [website](#).

The intention is that once the successful bidder for the Project is selected by Thames Water, we will consider designating it as an IP under the SIP Regulations and issuing it with a project licence (the IP Project Licence). It is envisaged that this will be in summer 2015.

### **3. Overview of the proposed modifications to Thames Water's Instrument of Appointment**

The proposed modifications are considered necessary to give effect to the Project, in particular in that they will enable Thames Water to charge customers for the activities of the IP. The amount the IP can charge Thames Water will be regulated by the IP Project Licence and by an agreement that will be entered into between Thames Water and the IP (the Revenue Agreement). The Revenue Agreement may not be amended without our consent.

In addition, the proposed modifications introduce a new condition T (Thames Tideway Tunnel Project) to regulate various Project-specific issues, including: the collection of revenue for the IP where the award of the IP Project Licence is delayed (to effect bill smoothing); the treatment of Project land; the resolution of disputes relating to mandatory variations to the construction works; and the consequences of the Project being de-specified by the Secretary of State, of the IP Project Licence being revoked, or of the Revenue Agreement being terminated.

We set out below a summary of the proposed modifications.

#### **Condition A (interpretation)**

The definition of 'regulated activities' will be modified to exclude the activities which will be carried out by the IP. Various new definitions will be inserted.

#### **Condition B (charges)**

A new provision will permit Thames Water to charge customers for the allowed revenue of the IP. The amount the IP can charge Thames Water will be determined under the IP Project Licence.

A new provision will require Thames Water to pay to the IP the relevant proportion of monies that it has collected from wastewater customers (such payment to be determined in accordance with the Revenue Agreement).

A further modification will be made for the purposes of the Thames Tideway Tunnel price control to clarify that any interim determinations are made in respect of the period of that price control, that is for the period from (and including) 1 April 2015 until 31 March 2020.

## **Condition D (charges schemes)**

Thames Water's charges scheme must make reference to the money it will collect to pay the IP.

## **Condition L (underground asset management plans)**

The definition of 'network assets' is modified to exclude IP assets.

## **Condition T (Thames Tideway Tunnel Project)**

- New provisions which will facilitate bill smoothing in the event that there is a delay in the award of the IP Project Licence (we deal with this under paragraph 4 below).
- New provisions require Thames Water to refer certain disputes to Ofwat for determination – for example, a dispute over a change to the works that is required by law.
- New provisions deal with the sale of Project land to ensure that any disposal (such as a sale) of Project land is on a 'no pain/no gain' basis – that is any gain from a disposal will go back to customers and any loss from a disposal will be borne by customers.
- New provisions deal with the consequences of revocation of the Project Specification Notice or of the IP Project Licence or of termination of the Revenue Agreement. In particular those provisions: 1) provide that if the IP Project Licence or the Project Specification Notice is revoked or the Revenue Agreement is terminated, Ofwat may direct Thames Water as to the treatment of revenue it has already collected from customers in relation to the project; and 2) provide that within a period of 6 months of the Project Specification Notice being revoked Thames Water must present a proposal to the Secretary of State and to Ofwat which addresses the issue of sewage discharges into the river Thames with a view to securing compliance with the Urban Waste Water Treatment Regulations 1994, together with an estimate of the costs of delivering such proposal.

## **4. Bill smoothing**

The proposal on bill smoothing is to introduce a licence mechanism that will allow Thames Water to collect revenue on behalf of the IP in circumstances where there has been a delay to the appointment of the IP beyond October 2015.

The proposal was put forward by Thames Water in its representations to us on our draft price determination. It made the proposal as it aligned with its research that customers prefer a smooth bill profile. We flagged the issue in our October 2014 consultation on the first set of licence modifications for Thames Water but as this modification was not required for the price review, we considered that it should form part of the second set of modifications.

The new provisions will enable Thames Water to request that Ofwat provide an estimate of the likely IP charge for the period from award of the IP Project Licence to (and including) 31 March 2017. This is to deal with the possibility that the grant of the IP Project Licence will be made too late for inclusion of the IP charge in Thames Water's charges scheme for the year 2015/16. Ofwat's estimate will be based on evidence produced for it by Thames Water. If this provision is utilised and money is collected from customers prior to the award of the IP Project Licence, money collected must be adequately ring-fenced as amounts payable to the IP, in order to protect customers. As part of its evidence base presented to Ofwat, Thames Water must propose an adequate ring-fencing mechanism. A consequential amendment will be made to the draft IP Project Licence to introduce a reconciliation procedure and thus to avoid double counting.

While Thames Water requested the licence modification to allow it to collect revenue from customers from April 2015, the impact on customer bills in the year commencing 1 April 2015 was not considered by us to be material. The more material scenario relates to a significant delay to the appointment of the IP, such that it is unable to raise revenue from customers in both 2015-16 and 2016-17 which would lead to a subsequent, larger step increase in bills in 2017-18.

CCWater and Thames Water's Customer Challenge Group have indicated support for Thames Water's proposition, with particular reference to scenarios where there is more significant delay to the appointment of the IP.

## 5. Indicative timetable

It is proposed that most of these modifications to Thames Water's licence that we are now consulting on, will come into effect on 1 April 2015 with the remainder of the modifications coming into effect on the date that the IP Project Licence is granted, ie the summer of 2015. Shortly after granting the IP Project Licence and modifying Thames Water's licence, we will issue a responses document, summarising the responses received to the consultation on the regulatory framework (which closed in November 2014) and to this consultation and setting out how comments received were taken into account in finalising both instruments.

Ofwat (The Water Services Regulation Authority) is a non-ministerial government department. We regulate the water sector in England and Wales. Our vision is to be a leading economic regulator, trusted and respected, challenging ourselves and others to build trust and confidence in water.



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