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Ref: 2340-TDWAY-TTTUN-990-ZZ-CO-700081

DPC Licence changes consultation
Ofwat
Centre City Tower
7 Hill Street
Birmingham
B5 4UA.

21 April 2020

Dear Sir/Madam,

CONSULTATION ON PROPOSED AMENDMENTS TO LICENCE CONDITIONS FOR DIRECT PROCUREMENT FOR CUSTOMERS

We are pleased to submit this response to Ofwat's consultation on proposed licence amendments for direct procurement for customers (DPC). While Tideway's regulatory arrangements are different to those envisaged for DPC projects, we believe that there is sufficient similarity to provide some lessons for the development of DPC arrangements. Our comments below largely focus on observations from our experience of collection of Tideway's revenue by Thames Water, with some additional comments on the DPC procurement process from Tideway's perspective as an Infrastructure Provider. These comments are largely relevant to consultation questions 1 and 7.

In relation to the modifications to allow the appointee to recover the Competitively Appointed Provider (CAP) charges, we are keen to ensure that lessons from Tideway's arrangements are considered to ensure best value for customers. We support the proposal for the CAP charges to be paid in full rather than on a pay-when-paid basis. This will reduce administration costs for both the CAP and the appointee by avoiding the need to review and agree collected amounts. Although the appointee will need to track the collection of CAP charges for accounting purposes, this analysis will not need to be completed as frequently as it would under a "pay-when-paid" arrangement.

While we support the proposal for CAP charges to be paid in full, it will be important for Ofwat to provide the appointee with certainty as to the treatment of under/over collection of revenue through the DPC Allowed Revenue Direction. This will need to take into account the likely mismatch between the timing of payment and collection of the CAP charges, as well as the bad debt risk. Tideway's pay-when-paid arrangements deal with the risk of under-collection through an under/over recovered revenue building block. For a CAP with no control over revenue collection, it seems sensible for the appointee to take on the cashflow risk, and that, as proposed by Ofwat, this should be dealt with appropriately in the appointee's regulatory arrangements.

The timetable for the calculation of Tideway's Allowed Revenue ensures that Thames Water can be notified of the revenue requirement in advance of the charges-setting process. There may be timing challenges around incorporating the CAP charges into bills if these amounts can be varied,

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or timings are not written into the contract. To ensure customers pay the CAP charges in a timely way, while avoiding unduly increasing the risk to the appointee, it will be important for Ofwat to build an appropriate amount of flexibility into the DPC Allowed Revenue Direction.

While Tideway is less well-positioned to comment on the licence modifications related to the procurement process, there are a number of areas where we think it would be beneficial for Ofwat to provide greater clarity to the CAP and/or appointee in order to ensure best value for customers. For example, in the light of the current pandemic, it would be beneficial for Ofwat to provide explicit guidance on how such risks should be treated. It would also be helpful to provide further guidance on the role and reporting of the Independent Technical Adviser (ITA), as well as Ofwat's oversight, to ensure that the arrangements are clear ahead of a procurement process, and the level of assurance provided by the ITA is good value for customers.

We note that in part, the licence modifications address the lack of a direct relationship between Ofwat and the CAP given the proposed approach to DPC uses a contract rather than licence model. While it is important that Ofwat retains oversight of key aspects of the DPC to protect customers' interests, this needs to be balanced against the risk of introducing delay or uncertainty for the CAP that drives up costs due to the need to obtain regulatory approvals. For example, this could apply to provisions around Ofwat consent to changes in the CAP agreement and those related to the ultimate controller of the CAP. It will be important for Ofwat to be clear and committed on the timings that will apply to its decision-making processes.

To ensure best value for customers, it is crucially important that the appointee and the CAP work collaboratively to deliver schemes and outcomes. This has been an important consideration in the development of Tideway's arrangements and the management of the project, although we recognise there are differences between Tideway and DPC delivery models. Ofwat may wish to consider how this is best achieved, and how to provide assurances to CAP bidders and appointees during the procurement process.

Please do not hesitate to get in touch if you would like to discuss any aspects of this response further.

Yours faithfully

Matt Parr

Director of Strategy and Regulation