

By Email Only to: [DPC@ofwat.gov.uk](mailto:DPC@ofwat.gov.uk)

21<sup>st</sup> April 2020

To whom it may concern

**Consultation on proposed amendments to licence conditions for Direct Procurement for Customers**

Transmission Investment manages one of the largest offshore electricity transmission portfolios in terms of the capacity of offshore wind connected. By the end of 2020, our offshore wind transmission portfolio will comprise circa £2.5bn of assets under management. We are also a leading developer of utility network assets, in particular developing, in partnership with the French national grid company, a circa £1bn electricity interconnector between France and Britain.

Transmission Investment has for many years been a strong advocate of introducing competition into the delivery of utility network assets and we continue to support the development of the required arrangements for these competitive processes inter alia through industry groups, responding to consultations such as these and, when called upon, providing evidence to parliament.

As such we are very supportive of the work that Ofwat has done to date, and continues to push forward, in implementing Direct Procurement for Customers and we provide our comments to the consultation below.

**General Oversight**

1. We support the continued involvement of Ofwat throughout the DPC procurement process as we think it will provide comfort to prospective CAPs (as well as customers) that the process will be run fairly and will not be unnecessarily terminated part way through.

**Oversight of process**

2. We support Ofwat approval of the planned DPC procurement process prior to it being undertaken. However, to ensure such approval effectively achieves best value for money and best protects customers, we consider that the initial approval to start the DPC process should come ahead of the DPC PQ stage (as opposed to the ITT stage) as the PQ stage is a significant part of the procurement process itself and may require significant work from prospective CAPs (in terms of consortia formation etc.).

**Oversight of Form of CAP Agreement and changes to it**

3. We recognise the need for flexibility of each DPC process, given the specifics of each designated project and the potential need for bespoke terms and requirements. However, we would welcome “a standardised and repeatable model across different companies” (including form of CAP Agreement) as Ofwat noted KPMG had recommended in its consultation on the PR19 methodology<sup>1</sup>. We would prefer that Ofwat approve the form of CAP

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<sup>1</sup> Delivering Water 2020: consultation on pR19 methodology, Appendix 10: Direct procurement for

Agreement ahead of the ITT stage, and then only need to approve changes to it.

4. In addition to the form of contract, Ofwat could usefully provide an indicative set of criteria or contractual principles to provide guidance on whether such approval of any requested changes would be forthcoming. This would increase the transparency, efficiency and robustness of the process as such criteria or principles would help all parties ensure the contract remained acceptable.
5. We understand that Ofwat will only want to consent to major changes to the CAP agreement and that the use of a materiality threshold to consent to those changes may provide some guidance. We note how the concept of materiality may prove difficult to define, whilst still preserving simplicity and clarity of concept. We are not sure that it is necessary to define a materiality threshold and instead a mark-up could be presented to Ofwat for approval as a whole.

#### ***Constraints on Ultimate Controller***

6. We have some concerns over the approval of change in Ultimate Controller – we understand and support the need to ensure that the restriction vis-à-vis Associated Companies is not breached but investors will generally want few constraints on the ability to sell investments. It would therefore be beneficial if Ofwat could provide some limitations to this approval requirement or at least guidance as to the circumstances under when they may not grant approval for a change in Ultimate Controller.

#### ***Associated Companies***

7. It would be helpful if the licensee was obliged to inform all prospective bidders at the commencement of the DPC process of its Associated Companies. This would negate the need for every bidder to research this and would mitigate the risk of a CAP being disqualified at a later stage.

#### ***Performance incentives on the CAP and the licensee***

8. In setting the balance of risk and reward in the form of CAP Agreement, Ofwat may want to consider how to drive innovation in the long-term operation and maintenance of the asset. A mechanism that rewards performance higher than the required minimum level would incentivise the CAP to outperform on an on-going basis and proportionally reward best performing CAPs<sup>2</sup>.
9. Aligning the licensee's incentives with those of the CAP, such that the licensee also benefits from outperformance of the DPC asset, may result in the best outcome for the customer. In the absence of such incentives on the licensee, the licensee may only be focussed on to what extent the CAP's performance is putting its licence at risk, which is clearly a fairly extreme scenario and not one that should be relied upon to incentivise good performance on a daily basis.

#### ***DPC Exit***

10. We appreciate that a DPC Exit is distinct from a CAP Agreement termination and the need to prudently define circumstances where the DPC is proved not to provide the best value for money for customers. We note that to foster competition and minimise costs to bidders, confidence is crucial. To support such confidence, considering the costs of some earlier stages of the procurement we agree with Ofwat on the decreasing appropriateness of a DPC Exit as the procurement progresses. We welcome more detail on the principles and scrutiny Ofwat will apply to consent a DPC exit especially when this occurs during at the end of the procurement process (referred as "Stage 5" in the DPC Briefing Note).

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customers, Section 4 Draft principles for the DPC contract, 11 July 2017

<sup>2</sup> This has successfully been used in the offshore electricity transmission space where the availability mechanism incentivizes performance well above the 98% nominal target.

We would be happy to answer any questions that you may have on the above points.

Yours sincerely



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