

February 2021

Direct procurement for customers: Ofwat's reasons for modifying the conditions of appointment of five water and sewerage companies

1. About this document

This is a notice under section 195A of the Water Industry Act 1991 (the Act), setting out our reasons for our decision to modify the licences of the following five companies to give effect to our direct procurement for customers initiative:

Water and sewerage undertakers:	Water only undertaker:
<ul style="list-style-type: none">• Anglian Water Services Limited• United Utilities Water Limited• Southern Water Services Limited• Dŵr Cymru Cyfyngedig (Welsh Water)	<ul style="list-style-type: none">• Affinity Water Limited

The modifications to Welsh Water’s licence conditions were made on 11 February, coming into effect on 12 February 2021. The modifications of the other four companies were made on 26 January 2021, coming into effect on 1 February 2021.

The [notices](#) modifying each of the five companies’ licence conditions are on our website.

2. Overview of licence changes

Direct procurement for customers (DPC) involves a water or wastewater company (referred to in this paper collectively as a ‘water company’) competitively tendering for services in relation to the delivery of certain large infrastructure projects, resulting in the selection of a third-party competitively appointed provider (CAP). DPC will result in water companies competitively procuring more aspects of an infrastructure project, including financing for the project. We believe that by outsourcing the delivery of infrastructure projects using DPC, water companies can achieve significant benefits for customers. This includes both through innovation and lower whole life costs of the project.

The licence modifications were made to give effect to DPC. A summary of the licence conditions is set out below.

Licence Change 1 – new Condition U

The first proposed licence change is a new condition which will establish the framework for the regulation of DPC projects. Amongst other things, the new condition will specify the process which companies must follow in carrying out a DPC procurement.

Licence Change 2 – Amendments to Condition B for recovery of CAP Charge

The second proposed licence change will allow a water company to recover from its customers, outside of price controls, the designated charges that the water company must pay to the CAP for services.

Licence Change 3 – Amendment to Condition B for DPC Interim Determination

The third licence change will be an amendment to the interim determination provisions in Condition B of companies’ licences. This will facilitate, in specified circumstances, the return of the project to delivery by the company rather than by the CAP.

3. Background

We set out in our [2019 price review \(PR19\) methodology](#) that we expected water company business plans to consider DPC where this was likely to deliver the greatest value for customers. DPC promotes innovation and resilience by allowing new participants to bring fresh ideas and approaches to the delivery of key projects. In chapter 7 and Appendix 9 of the PR19 final methodology we set out our approach and expectations for DPC in relation to company business plans.

In February 2020 we published a non-statutory consultation – [Consultation on proposed amendments to licence conditions for Direct Procurement for Customers](#). In that consultation we proposed a new condition to enable us to regulate DPC projects, and we invited stakeholders to provide comments on the proposals made.

We published a further non-statutory consultation in July 2020 – [Consultation on the proposed amendments to licence conditions for DPC including an uncertainty mechanism](#). This provided updated proposals on the provisions we had previously consulted on, and it proposed introducing a bespoke DPC interim determination. It also sought to provide clearer guidance on how we expect Allowed Revenue Directions to work. An Allowed Revenue Direction is a direction issued by Ofwat allowing companies to collect from customers the charges payable to the CAP.

In November 2020 we published a statutory consultation under section 13 of the Act – [Direct procurement for customers: statutory consultation on proposed changes to the](#)

[conditions of appointment of five water and sewerage companies](#). Our November statutory consultation closed on 4th January 2021. The four companies whose licence conditions have been amended, all gave consent to the modifications. We also received consent from Welsh Water. As indicated above, we anticipate making the modifications to Welsh Water's licence later this month.

We summarise the responses to the statutory consultation below.

4. Responses to the statutory consultation

We received eight responses to the statutory consultation. Five of these provided consent from the companies whose licences have or will be amended. We also received responses from South West Water, Wessex Water and Yorkshire Water. All responses have been published alongside this decision document.

All the responses were supportive of the licence changes. Respondents also commented on the need to keep the process under review and to learn from the experiences gained from early DPC projects.

5. Reason for the modifications

In our [November statutory consultation](#) we provided our reasons for our proposal to modify the licence conditions of the affected companies. In particular, Part B of that document set out the modifications proposed, their effect, and our reasons for proposing those modifications. Given the supportive responses we received, we did not make any substantive changes to the drafting and our reasons therefore remain the same. In summary our reasons for making the changes are:

- to protect customers, the new Condition U puts appropriate controls in place, giving Ofwat oversight over the delivery of a DPC project;
- Ofwat consent is required at various points in a DPC project, to check that best value for customers is being achieved;
- the licence changes are necessary as they provide the mechanism for companies to charge customers for the charges of the appointed CAP;
- the licence amendments introduce a new interim determination which will provide companies with certainty that they will be funded if a DPC project is brought back in-house in full or part.

**Ofwat (The Water Services Regulation Authority)
is a non-ministerial government department.
We regulate the water sector in England and Wales.**

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