

11th May 2023

FAO: RAPID

Thames to Southern Transfer (T2ST) Strategic Resource Option (SRO) – response to Gate 2 Draft Decision

This letter forms Southern Water and Thames Water's joint response to RAPID's Gate 2 draft decision published on 30 March 2023 for the Thames to Southern Transfer (T2ST) Strategic Resource Option (SRO).

We are pleased the draft decision proposes that the T2ST SRO should progress to Gate 3. We also note that the Gate 3 Checkpoint 1 funding request of £1.90m has been allowed; that all Gate 2 expenditure has been deemed efficient and allowed; and that the T2ST submission is recognised as having the top rating of 'Good'.

We are grateful for the opportunity to provide representations ahead of the final Gate 2 decision, with a number of areas where we have feedback as set out below.

Proposed changes to partner arrangements

The Gate 2 submission proposed that funding for the SRO from Thames Water would cease at the end of AMP7 with Southern Water paying for 100% of the continued investigation and development of the scheme from the start of AMP8. Southern Water would become fully accountable for progress of the scheme post-Gate 2. This proposal was based on Southern Water's customers being the primary beneficiaries of this SRO. We note that RAPID's draft decision proposes Thames Water's continued involvement beyond AMP7 but with a minority interest, funding 10% of the scheme, with the majority stake at 90%, funded by Southern Water.

By holding a minority interest, Thames Water would need to participate in project governance, and incur the management overhead associated with oversight and reporting, which both companies consider would not be efficient use of funding. Both, Thames Water and Southern Water believe a more efficient funding approach is for Southern Water to provide a single point of delivery accountability given it is Southern Water's customers who benefit from, and ultimately fund, the investment. This remains our preferred arrangement for Gate 3.

Irrespective of the financial split between Southern Water and Thames Water, given the interdependency between the South-East Strategic Reservoir Option (SESRO) and T2ST and operational asset connectivity, together with the pending bulk supply agreement that makes T2ST commercially viable for Thames Water, there is a strong incentive for both Thames Water and Southern Water to collaborate and hold each other to account.

As such, should RAPID wish Thames Water to remain involved in T2ST to support scheme development a 50:50 funding split has been discussed with both companies and is an alternative approach providing equal influence over decisions and management of risk.

We note RAPID's draft decision statement that partner arrangements cannot change at AMP cycles. We note this, however cost forecasts have already been agreed for the current AMP

(post-Gate 2 and inclusive of part of Gate 3) and are due to be finalised for AMP8 in the PR24 submissions in the near future. Both companies welcome any opportunity to discuss this point with RAPID, prior to the Gate 2 final decision, allowing us to develop and confirm ways of working as soon as possible.

Solution funding to standard gate three

We note RAPID's decision that the T2ST SRO can take the underspend of £0.87m from Gate 1 and 2 into Gate 3, increasing the Gate 3 allowance to £6.20m. We also note that the draft decision welcomes '*a detailed revised forecast to be submitted during the representation period*'.

Within Appendix A accompanying this letter (where all costs are in 17/18 prices), we have provided a cost breakdown of both the Gate 3 Checkpoint 1 at £1.90m (provided as part of our Gate 2 submission) and a new breakdown to the Gate 3 submission (forecasted as November 2027) of £17.85m. We accept that this is significantly above the Gate 3 allowance totalling £6.20m (inclusive of underspend from previous gates) and we seek an increase to the Gate 3 allowance in the final decision.

The original Ofwat PR19 determination RAPID development allowance was based on a capex estimate of approx. £250m. The current capex estimate, provided at Gate 2, is £850m, therefore we have calculated an indicative estimate for Gate 3, using the RAPID's calculation approach, to be £17.85m. This is broken down in Appendix A (attached).

It should also be noted that in Section 7.4 of our Gate 2 submission, we flagged a number of dependencies and complex interactions linked to the progression of this SRO through to Gate 3 which will impact this estimated value, hence the request for a Checkpoint 1 to confirm the more accurate Gate 3 forecast.

This estimate of £17.85m will be matured and updated at RAPID Checkpoint 1, where a schedule-based estimate will be presented to RAPID for further discussion. Should the estimate increase, we will be seeking a revision to the Gate 3 allowance provided in the Gate 2 final decision at the Checkpoint 1.

At this point, assuming that the Water Resource Management Plans 2024 (WRMP24) are published as currently forecast, we expect to be able to provide a schedule based more detailed estimate through to Gate 3 which would replace the current indicative forecast of £17.85m. Through the Gate 3 Checkpoint 1 amount of £1.90m we have sufficient funding to complete planned activity for Gate 3 activities in AMP7, using the already agreed PR19 funding.

We would be grateful if you could confirm in the final decision that funding for AMP8 will be separately determined through the PR24 process and that it will reflect any changes to project schedules arising from the WRMP process.

Gate three timing

We note that RAPID's agreement on the proposed dates for Gate 3 and Gate 4. In relation to the proposal for a mid-gate checkpoint, we agree that we will discuss this with RAPID at regular checkpoint meetings and formalise any requests in writing. The key programme milestones and associated proposed dates are set out below.



Key programme milestones	Planned delivery*
Gate 3 Checkpoint 1	Mar-24
Gate 3 Checkpoint 2	Sep-25
Gate 3	Nov-27
Gate 4	Jan-29
DCO submission	Jan-29
DCO Award	Oct-30
CAP Award	Nov-31
Construction start	Jan-34
Construction completion	Dec-39
Operation starts	Jan-40

**As noted in Section 7.4 of our Gate 2 report, Gate 3 Checkpoint 1, which would be after the final WRMPs are published and a period of targeted design development and targeted de-risking. The purpose of this checkpoint is to re-evaluate the timing and need for the scheme based on the WRMPs and to agree a way forward with RAPID that allows for continued interaction with other projects while ensuring efficiency of spend. All other dates are indicative to be agreed at Checkpoint 1.*

Actions & Recommendations

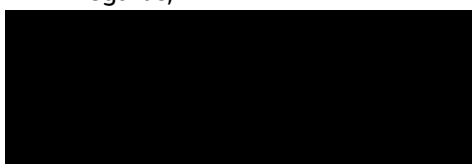
We are pleased to note that RAPID have not identified any priority actions for the T2ST SRO.

There are no concerns with the actions and recommendations in the draft decision and we will work to resolve each item for Gate 3. We have prepared an action plan to address them and we will continue to provide regular updates on these and on our other Gate 3 technical workstreams through the next gated process and interim checkpoints, so that RAPID can have confidence that we are on track to a resolution.

Summary

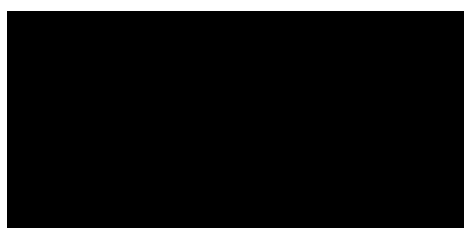
We would like to take this opportunity to thank RAPID, EA, Ofwat and DWI for their engagement and collaborative working throughout Gate 2, and for their positive draft response to our Gate 2 submission.

Regards,



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