

Anglian Water

PR19 CMA Redetermination

Consultation response – The Elsham Scheme

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Elsham consultation response - Overview

1 Summary

- (1) Anglian has considered the consultation document (the “**Elsham consultation**”) setting out the CMA’s current thinking with respect to making amendments to Ofwat’s Final Determination regarding the scope of the Elsham candidate DPC scheme.
- (2) The Elsham Consultation seeks to set out the respective views expressed by Anglian and Ofwat during the redetermination. However, the document does not reference all of the materials Anglian has submitted on this matter, specifically Anglian’s annexes to its Provisional Findings response and more recently Anglian’s¹ 20 November 2020 letter and supporting information. This last submission corrected some important factual inaccuracies in Ofwat’s reply to main parties’ responses, upon which the CMA² has seemingly relied in reaching the views set out in its consultation document. Anglian therefore requests that the CMA addresses this apparent omission before reaching a conclusion on this matter.
- (3) Anglian would have preferred the Elsham DPC scope to be resolved bilaterally with Ofwat and has undertaken extensive engagement with Ofwat to achieve this. However, as stated in Anglian’s response to the Provisional Findings³, despite these extensive efforts, such agreement has not been possible.
- (4) The Elsham Consultation sets out the CMA’s view⁴ that the redetermination should not revise the scope of the Elsham DPC scheme. The primary reasons cited by the CMA in reaching this view are:
 - a. Ofwat’s emerging DPC IDoK process appears likely to address Anglian’s funding gap issue⁵ which the CMA suggests is Anglian’s particular concern raised in Anglian’s statement of case⁶;
 - b. The on-going DPC process will sufficiently review the case for descoping⁷;
 - c. There may be significant risks to customers associated with the CMA seeking to assess and conclude on a range of detailed issues Anglian’s proposal raises at this late stage of the redetermination process⁸; and
 - d. Agreement with Ofwat that the CMA forming a view on scope risks undermines the overall DPC process given the significant management control over timetables and the potential for perceived incentives to delay steps of the DPC process in order to increase the likelihood of delivery being brought in house⁹.
- (5) The CMA therefore concludes that the redetermination does need not to revise the scope of the Elsham DPC, and that no consequential adjustments to totex allowances, performance commitments or ODIs are required¹⁰.
- (6) Anglian assumes that by “risks”, the CMA refers to the implied *potential benefits* that *may materialise* through the DPC value for money assessment for the full Elsham scheme. The CMA does not appear

¹ Specifically PF010 and PF010a

² Letter to Douglas Cooper – 20 November 2020 sent on 23 November 2020 “Main parties replies to Provisional Findings responses”

³ Anglian Response to Provisional Findings – Chapter E, Section 3.5. Para 184

⁴ Specifically Elsham Consultation paragraphs 19-21

⁵ Para 18

⁶ Para 16

⁷ Para 20

⁸ Para 20

⁹ Para 21

¹⁰ Para 22

to have given weight to the very real risks of detriment to customers and the environment related to pursuing the wider scope for the Elsham DPC as proposed by Ofwat, in respect of the delay to timeframes. Anglian has been clear about these detriments throughout this process, both in discussions with CMA and with Ofwat, and Mike Woolgar's expert report¹¹ also highlights these same risks.¹²

- (7) The Elsham Consultation does not clearly set out what the CMA perceives the risks to be, nor how these have been balanced against the real risks to customers and the environment of the delay to timeframes that Anglian is legally required to meet.
- (8) **Anglian's view is that the risks of the CMA not changing the scope of Elsham DPC far outweigh the uncertain potential benefits of the full Elsham DPC scheme.**
- (9) Anglian does not consider that the evidence adequately supports the CMA's conclusion with regard to leaving the Elsham scope unadjusted, given the risks to customers, security of supply, resilience and the environment which this entails. It provides its reasons for this in this response.

2 Request to the CMA

- (10) The scope of and process for delivery of the Elsham scheme forms part of the Final Determination and is an aspect of Ofwat's Final Determination that Anglian disputes. While the nature of the dispute has evolved during the course of the CMA's Redetermination as parallel discussions with Ofwat have continued, it is nonetheless clear that the CMA forming a view on the scope of the Elsham scheme is within the remit of its Redetermination.
- (11) **Anglian requests that the CMA, by taking into consideration this response and the full suite of materials previously presented by Anglian, reflects in the final redetermination the necessary amendments to the scope of the Elsham DPC scheme so that only the Elsham treatment element (CLN13a) is taken through the DPC process.**
- (12) Anglian has previously provided the CMA with the relevant information required to make the necessary adjustments to totex allowances, performance commitments and ODIs¹³.
- (13) Such action would resolve matters swiftly to mitigate the risk of Anglian's environmental obligations not being met, mitigate the risks of security of water supply for customers not being met, and underpin resilience objectives. All of these are outcomes against which Anglian will be held accountable.
- (14) Ofwat's as yet untested DPC process creates significant potential for timetable delays which are highly likely to result in failure by Anglian to meet its time-bound environmental obligations and risk customers being without water as a result of unmitigated supply-demand balance pressures. As demonstrated previously to the CMA, this would create significant detriment to customers and the environment but is eminently resolvable through a decision by the CMA to reduce the scope of the DPC as part of the redetermination. A decision by Ofwat to reduce scope, at a later date, would have to go through a slower process which would not mitigate these risks.

¹¹ Sent to the CMA on 4 December 2020.

¹² Anglian Statement of Case – WRMP Case Study 2 – Executive Summary – Page 25 and Chapter E3, page 188

¹³ Anglian Response to Provisional Findings – Chapter E, Section 3.5. Pages 33 – 37, paragraphs 184 - 209

Elsham scheme consultation – Main response

1 **Anglian accepts that the risk of *wholly* unfunded obligations is mitigated by the existence of Ofwat’s emerging DPC IDoK process but remains concerned about the risk of some partially funded obligations**

- (15) Anglian’s Statement of Case cited both the risk of unfunded obligations and timetable risks¹⁴ associated with the full scope of Elsham DPC. Anglian agrees that, at the time of writing this response relative to the Statement of Case, the unfunded risk associated with changes to DPC scope is mitigated by the development of the DPC IDoK process. Anglian has contributed to the development of these mechanisms, working with Ofwat, and welcomes the changes that Ofwat has now put forward.
- (16) However, retaining the full scope for Elsham DPC reintroduces the risk of unfunded obligations for Anglian unless there is assurance from Ofwat that it will apply Anglian’s proven efficient costs for delivery in the IDoK process (i.e. respecting the CMA’s conclusions in the Provisional Findings that Anglian has demonstrated the efficiency of its delivery costs). Otherwise the retention of the full scope for Elsham places Anglian and its customers in a “lose, lose” situation. It would mean either:
- a. waiting until the conclusion of the DPC tender and DPC IDoK process before being able to seek recovery of the appropriate efficient cost of the full DPC scheme, which significantly increases the risk that Anglian misses its environmental obligations; or
 - b. in order to meet environment obligations, Anglian having to invest now without knowing whether it will be able to recover its efficient costs from customers via a future DPC IDoK process. Whilst this risk persists should any candidate DPC scheme revert to delivery by Anglian, the magnitude of this risk is increased if the full Elsham DPC scope is retained.

2 **There is a clear detriment to customers and the environment by putting the full Elsham scope through the DPC process, whilst any potential benefits remain highly uncertain.**

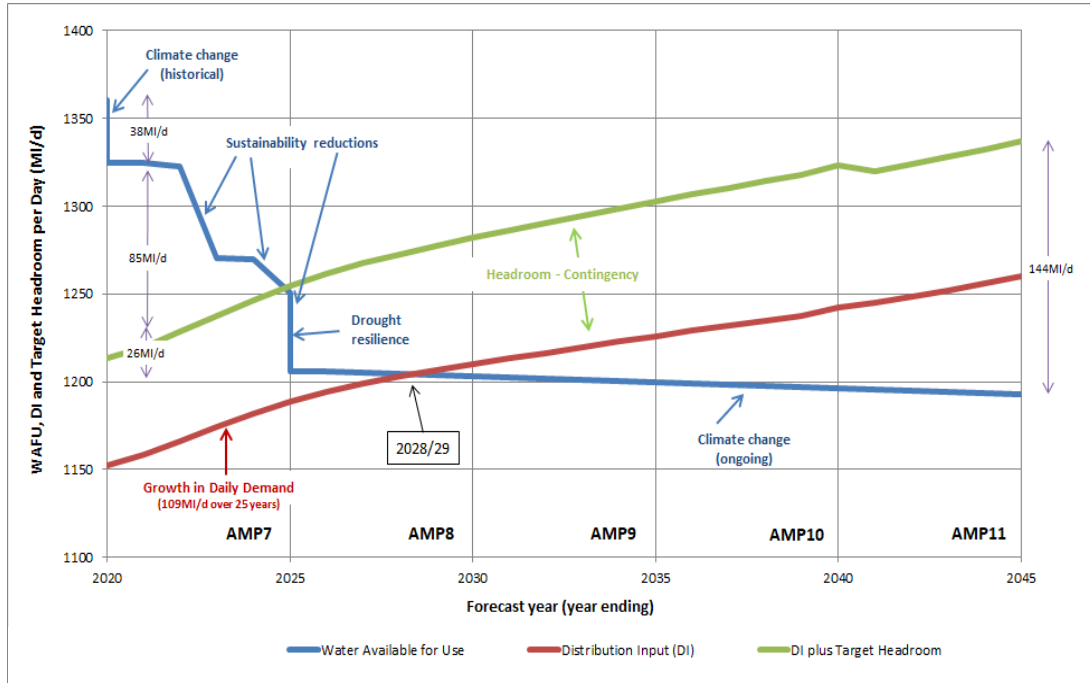
- (17) Taking the combined pressure on the region’s supply demand balance, it is clear that subjecting the full Elsham scheme to the DPC process introduces an unnecessary timing delay and delivery risk relative to the counterfactual of a revised descoped Elsham DPC scheme, with highly uncertain countervailing benefits to consumers.
- (18) **Any delay directly reduces the resilience of the region’s supply demand balance and Anglian’s ability to meet its legal obligations. Anglian asks that the CMA consider this risk of delay and how this is consistent with the execution of the Resilience Duty, or indeed its duties in the round, given the uncertainty of countervailing benefits.**
- (19) Anglian has presented to the CMA the importance of timely investment to ensure the supply demand balance of the region is maintained and the increased level of drought resilience, consistent with the WRMP19 guidance, can be achieved during AMP7. Peter Simpson highlighted these risks in his opening statement to the CMA at the most recent Hearing and has written to Kip Meek¹⁵ on the point, underlining just how critical these issues are.

¹⁴ Specifically – WRMP Case Study 2 – Anglian Statement of Case – Executive Summary – Page 25 and Chapter E3, page 188

¹⁵ Peter Simpson to Kip Meek – 17 December 2020 – Cover letter to Post-hearing follow-up

(20) In Anglian’s WRMP19¹⁶, Anglian’s Statement of Case¹⁷ and throughout the redetermination process Anglian has presented the impact of various factors on the supply-demand balance during the period to 2045:

Figure 1 Impact of various factors on Anglian’s supply-demand balance during the period to 2045 (Statement of Case - Figure 20)



(21) This demonstrates that Anglian will move from a regional surplus of 150MI/d to a deficit of 30MI/d over the next five years. Supply side risks are currently forecast to be minor post 2025; it is clearly the near-term issues which are the most critical in AMP7 and AMP8.

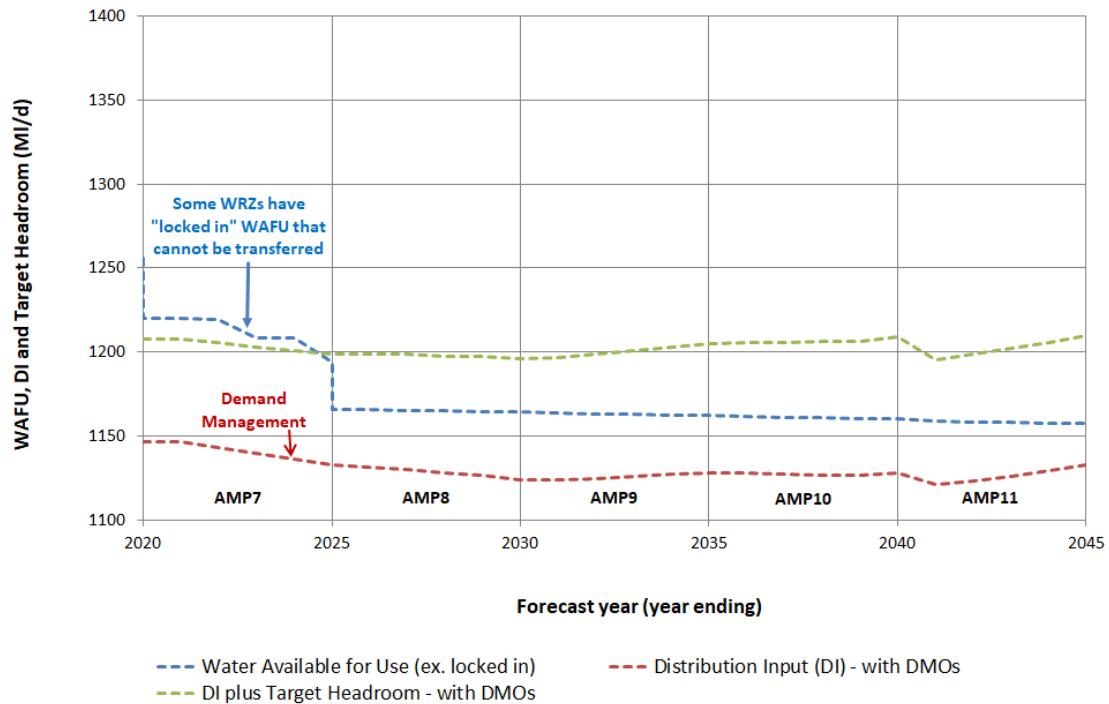
(22) As set out in Anglian’s Strategic Outline Case to Ofwat¹⁸ this supply demand balance becomes even tighter during AMP7 when regionally “locked in” Water Available For Use (WAFU) is excluded (because there is no means by which to transfer surpluses from one area in surplus to other areas in deficit), However, successful implementation of demand management options (including Anglian’s proposed further leakage reduction) offsets growth impacts providing just enough benefit, with an acceptable level of risk for customers, to the supply-demand balance in AMP7:

¹⁶Anglian Water Water Resource Management Plan 2019 (SOC279) (available [here](#))

¹⁷ Specifically Figure 20 Statement of Case page 80

¹⁸ December 2020 – Strategic Outline Case – Elsham treatment and transfer scheme

Figure 2 Impacts of demand management options on growth impacts



- (23) This highlights the urgent need for delivery of the overall strategic interconnectors schemes, of which the Elsham investment is a significant element. It is critical to enable Anglian to redistribute WAFU from 2025, ensuring supply demand balance across Anglian’s supply area during AMP8 and AMP9.
- (24) The urgency of the situation may be further reinforced by the emerging new needs from Cambridge Water linked to the pressure to reduce abstraction from the River Cam, and with the EA indicating that it may need to go beyond Anglian’s current 85MI/d reduction in abstraction to ensure no deterioration to watercourses in AMP7. All of this means that the region’s water supply challenges are acute and urgent and securing an early resolution of a reduced scope of DPC is one essential means to address them.
- (25) Following Anglian’s December hearing, Anglian has also provided recent correspondence between Anglian and the Environment Agency¹⁹ with respect to further abstraction caps.

2.1 Anglian’s legal environmental obligations

- (26) Anglian has legal obligations to meet new environmental limits by the end of AMP7²⁰. The Elsham scheme, including the treatment works and transfer pipeline, will provide 40MI/d during AMP8 towards meeting the legal environmental obligations; 26MI/d is allocated to supporting drought resilience and 14MI/d is allocated for restoring supply capacity in the face of reductions to current abstractions. Of the 14MI/d to mitigate sustainability reductions 1MI/d is required by December 2024 and 13MI/d by March 2025.

¹⁹ Specifically HII001 and HII002

²⁰ Specifically – PF010a DPC discussion with Ofwat – 28 Sept 2020

3 Neither Ofwat's responses, nor the CMA consultation, adequately takes account of the detriment

- (27) Ofwat's response to the Provisional Findings and subsequent documents continue to make no reference to the potential harm to customers and the environment if the environmental obligations to which Anglian is subject cannot be met.
- (28) Either customers face risks of insufficient supply which would be a direct breach of Anglian's licence obligations, or the environment faces risks of over-abstraction. Any consideration of potential financial benefits for customers under DPC should be set against these risks. Anglian's view is that the CMA has not sufficiently taken these concerns into account when informing its view not to amend the scope of Elsham as part of the redetermination.
- (29) Disappointingly, the Elsham Consultation does not give weight to the benefit to customers and the environment of timely investment to deliver against Anglian's legal obligations²¹. It instead only refers to the financial mitigations related to the development of Ofwat's DPC IDoK process and the importance of the nascent broader DPC process.
- (30) The CMA also suggests that there may be significant risks to customers associated with the CMA seeking now to assess and conclude on the range of issues that Anglian's proposal raises, giving the example of increasing costs that customers may bear for delivery of the scheme²². Anglian assumes this refers to the implied *potential benefits* that *may materialise* through the current DPC value for money assessment for the full Elsham scheme. The Elsham Consultation does not clearly set out what these risks are perceived to be, nor weigh them against the very real risks to customers and the environment of the delay to timeframes that Anglian has to meet.
- (31) Ofwat also continues to misrepresent the role of the WRMP in determining need, and its interaction with the Business Planning process. Ofwat²³ notes the significant detail and strategy development in WRMP19 relating to the year 2045, but contends that "the evidence and argument supporting the 2025 needs case is not adequately detailed and as such it is not possible with the current draft of the Strategic Outline Case to fully understand and approve the 2025 needs and outcomes case". This fails to understand the WRMP, which sets out 25-year forecasts and strategy based on annual steps: although summary graphs were provided for 2045, the WRMP contains just as much information for 2025 as 2045 and given the short duration of the 2025 forecast is very much more accurate than the 2045 numbers would reasonably be expected to be. It is generally acknowledged that the conditions pertaining in 2045 are likely to differ somewhat from the assumed situation which is why the WRMP process itself renews every 5 years to refine the short term investment needs based on best current information as well as reflecting updated guidance from Defra, for example the move to 1-in-200 year drought resilience in WRMP19 and the proposed future move to 1-in-500 currently under consultation in the draft WRMP24 guidance²⁴.
- (32) As expected given the different time horizons, Anglian has much *greater* confidence in the forecast 2025 supply-demand position compared to 2045. For this reason Ofwat is generally only prepared to accept an investment case for shorter term forecasts. Ofwat provides a specific example around growth but appears to mis-interpret the difference between a baseline forecast (which shows forecast growth but no demand management) and a final forecast (which takes into account the reduced demand due to demand management).

²¹ See PF010 and PF010a specifically.

²² Elsham consultation – Para 20.

²³ Reference of the PR19 final determinations: Costs and outcomes – Ofwat December response (December 2020) – Para 8.10 page 22

²⁴ July 2020 - Water Resource Planning Guidance – Draft for consultation (available [here](#))

- (33) Ofwat also makes a similar point regarding options and appears to fail to understand that the WRMP investment modelling considers all years for which a deficit is forecast in search of the best value investment plan across the planning horizon, not just at 2045. Anglian has stated repeatedly that in the shorter term there are very limited options available before the late 2020s. These options as previously expressed to the CMA at both Anglian’s main party hearings are either demand management or to redistribute where possible the existing available resources. The latter point is the very premise of the interconnectors; namely to distribute and use the only water resources available in the short term. Clearly the role of demand management, specifically the role of managing per capita consumption (PCC) is severely challenged by the persistence of Covid-19 and its consequences, most recently triggering the third national lockdown which is likely to maintain a higher PCC as a result²⁵.
- (34) Ofwat’s suggestion that Anglian should consider options that are “not critical to the 2045 strategy or are necessarily operational and short term in nature” undermines the WRMP process. The determination is entirely for the short term; for solutions to problems now, which take account of the uncertain future in 2045, not the other way around.

4 Anglian has presented clear evidence that the full Elsham scheme, relative to the descope scheme, has significant operational, commercial and contractual complexity

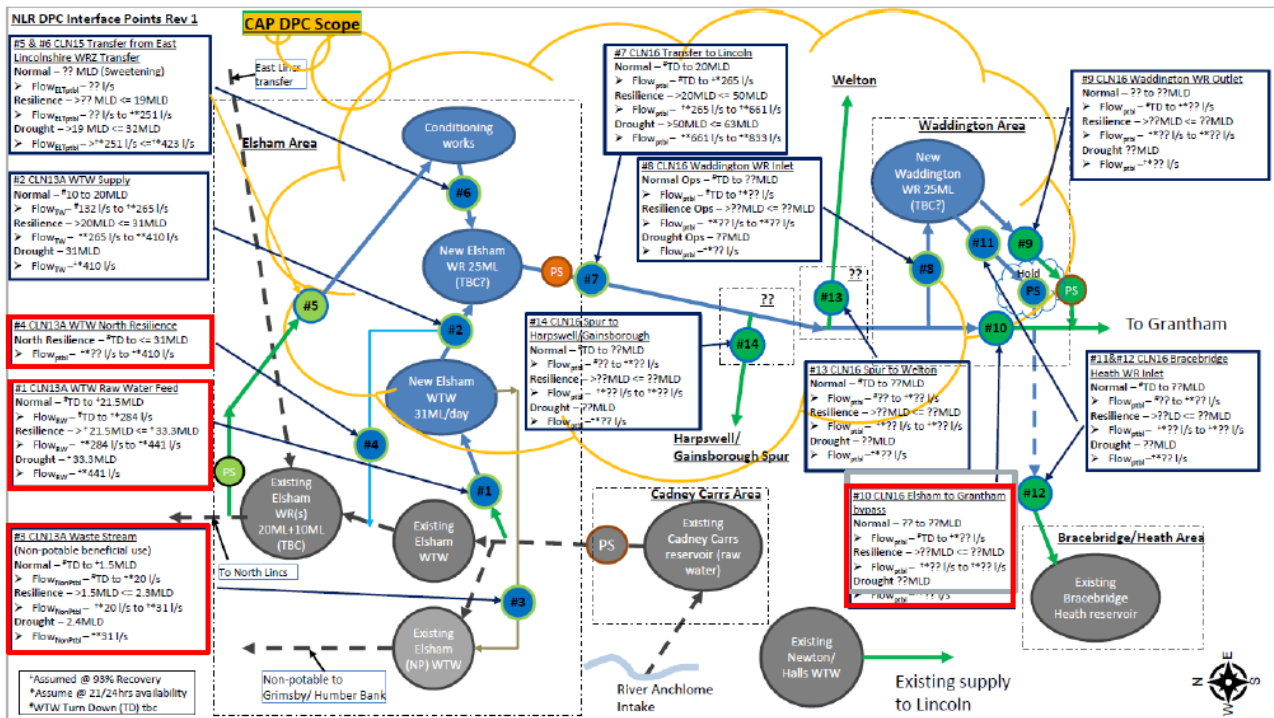
- (35) Ofwat claims that there is no evidence that the pipeline element (of Elsham) is more complex than the treatment works. It also states that there is no evidence that a commercial construct, whereby Anglian retains operational control of the pipeline, is not a possibility²⁶.
- (36) Anglian has consistently shown to Ofwat and the CMA, that whilst technically and from a construction perspective the pipeline is not more complex to build, there is a clear increase in operational complexity associated with the full DPC scheme compared to the descope DPC covering treatment works only²⁷. Such a difference is intuitive given the hugely increased number of operational interfaces between a range of infrastructure and non-infrastructure assets.
- (37) Ofwat’s view strongly contrasts with that of Anglian’s independent review (“**the review**”) of the Elsham DPC scheme conducted by Mike Woolgar, who has 40 years of international experience, including latterly supporting Ofwat in the development of their DPC approach for other potential DPC projects.
- (38) Figure 3 below sets out an indication, based on the full Elsham scope which the CMA proposes to retain, of the suite of rules which will need to be defined and incorporated into any contract form for the full scope. This would likely make this wider scope less attractive to the market, would inevitably add costs, and would certainly add further time given the complexities inherent within any contractualisation process:

²⁵ Anglian submission following November and December Main Party hearings - Annex 2 - Chapter B – Covid -19

²⁶ Reference of the PR19 final determinations: Costs and outcomes – Ofwat December response (December 2020) – Para 8.8 page 22

²⁷ For example as part of the discreteness test undertaken to inform Anglian’s September 2018 Business Plan which determined the full Elsham scheme was less suitable for DPC

Figure 3 Suite of interactions which will need to be incorporated into any contract form for the full scope



(39) Each box indicates a set of operational options which need to be defined separately, and in appropriately chosen combinations, to allow sufficient operating control and for managing the contracted cost for the Commercially Appointed Provider (“CAP”) to adopt these options under Anglian’s advice/direction. The red outlined boxes are not nominally within the CAP scope but need to be taken into consideration as their operating modes can affect the decisions on operating modes within the scope line. In addition, there would be similar interfaces for water quality considerations and for control and instrumentation which could also interact with the control options shown.

(40) This independent review concluded that:

“the full scope Elsham will take markedly more time to adequately describe to the market, tender, negotiate and reach financial close than a BAU approach, given the immaturity of the DPC approach and the complexity of the scheme interfaces”.

5 The Elsham Consultation gives no weight to the financial benefits of descoping the DPC project so that timely investment can be made to ensure Anglian’s legal obligations are met and the region’s supply demand balance is maintained

(41) The Elsham Consultation gives no recognition to the financial benefits of descoping the DPC project, specifically:

- a. the reduced costs of running the remaining DPC process (£4.4m);
- b. the increased incentive to deliver the overall interconnectors by way of making the ODI a higher-powered incentive by increasing penalty rates; and
- c. the reduced cost of the incentive for running the DPC programme.

(42) Furthermore, the Elsham Consultation fails to recognise that any *potential* financial/customer benefit of full scope DPC is far from certain when offset against the risks.

6 Ofwat's current application of the DPC process for assessing the Strategic Outline Case for DPC undermines the need for investment underpinned by the WRMP and PR19 processes which raises further concerns as to the CMA's proposed approach

- (43) Ofwat's previous DPC guidance stated that consideration and establishment of the needs case for a project to be procured within the 2020-2025 period would have been expected to have already been undertaken by Appointees as part of the formation and submission of Business Plans²⁸. Anglian, supports this view, however Ofwat's latest submission to the CMA and reflected in the Elsham Consultation directly contradicts this:

"Ofwat said that its ongoing review of Anglian's submissions as part of this process includes detailed consideration of a range of matters, including evidence on the extent and implications of the timing pressures Anglian faces (and, in particular, its assessment of its 2025 supply-demand need case, its response options, and its preferred commercial delivery approach)"²⁹.

- (44) By actively seeking to challenge the needs case for investment in the 2020-25, Ofwat is undermining both the WRMP and Business Planning development and assurance processes. Specifically, for the WRMP this includes formal approval by the Secretary of State.
- (45) Such subsequent challenge by Ofwat clearly undermines the confidence that can be taken from letting the new DPC process run its course and reaffirms the CMA's proposed approach for Elsham is an inadequate remedy to Anglian's request for the CMA to redetermine on this issue.

7 Anglian has consistently welcomed the longer-term benefits of testing the DPC process

- (46) Ofwat incorrectly suggests³⁰ that Anglian is both actively seeking to circumnavigate the DPC process and has only recently raised descopeing and timetable issues with Ofwat associated with the DPC process. Neither of these statements are true.
- (47) For the avoidance of doubt, Anglian's Statement of Case³¹ flagged potential concerns with the additional risk associated with the Elsham scheme. These concerns have been consistently referenced during the CMA process, from the initial Statement of case submission and during both Anglian main party hearings.
- (48) Ofwat's suggestion that Anglian is seeking to circumnavigate the DPC process is incorrect and not supported by the facts. As set out in correspondence with Ofwat from May 2019 (SOC209) and more recently (PF010); Anglian has demonstrated commitment to using the DPC processes both pre- and post-FD and fully recognises the potential benefits to customers in future beyond the assessment of the single Elsham scheme.
- (49) As cited in Anglian's correspondence with Ofwat³², Anglian is committed to the development of markets and market mechanisms where these are in the interests of customers. Anglian view DPC as a critical means of exploring the benefits that new markets can bring both now and in the long term for suitable discrete infrastructure projects. **Both Anglian and Ofwat share a mutual dependency to ensure the DPC process works well, recognising how important it is for Anglian, new market participants, and Ofwat to learn the lessons from this.** This learning will enable larger projects, such as a potential

²⁸ Specifically – July 2020 - Appendix 5: Direct Procurement for Customers – Briefing Note on the Procurement Process for 2020-25 – Stage 1 – Feasibility of project

²⁹ Elsham consultation – para 20

³⁰ Ofwat reply to responses to PFs – costs & outcomes, paragraph A1.7.

³¹ Specifically – Anglian Statement of Case – WRMP Case Study 2 – Executive Summary – Page 25

³² For example – PF010 DPC letter and note AW to Ofwat October 2020

new reservoir in AMP8, to be taken forward with that experience which may generate even greater benefits for customers in the future.

8 Anglian strongly refutes Ofwat's suggestion that Anglian's timetable concerns are new. Neither is there any basis for Ofwat's assertion that Anglian has contributed to a 16-month delay to the DPC process

8.1 Anglian has consistently flagged the risks associated with the full Elsham DPC scope

- (50) Anglian has consistently raised concerns with the full scope for Elsham being subject to Ofwat's developing DPC process. For example, Anglian's analysis which informed its Business Plan showed that the full Elsham scope was less suitable for DPC. This informed Anglian's May 2019 proposal to take only Elsham treatment through the DPC process.
- (51) Anglian has continued to express these concerns in its Statement of Case, highlighting Ofwat's full Elsham scope created a situation where the entire overall strategic interconnectors programme would be dependent on the successful delivery of the Elsham DPC process. Such a dependency is clear counter-evidence to Ofwat's assertion that Anglian has an incentive to delay the successful operation of the DPC process.

8.2 The Elsham Consultation does not reflect the full information presented by Anglian, including the correction to factual errors recently presented by Ofwat relating specifically to timetable concerns

- (52) The Elsham Consultation makes no reference to Anglian's letter dated 20 November 2020 which specifically responded to some factual errors in statements made by Ofwat in relation to DPC. Some of Ofwat's statements therefore remain uncorrected, and yet the CMA has seemingly relied on them in reaching its provisional view on the matters in the consultation.
- (53) Specifically regarding the timetable, Ofwat incorrectly asserts that Anglian's delivery timetable and de-scoping concerns have recently arisen³³ suggesting commencement in earnest in September 2020. As set out previously, Anglian's concerns can clearly be evidenced from before the Final Determination.
- (54) Anglian recognises that the timing pressures have become more acute during the redetermination process. They are however not new, have not arisen as a result of the redetermination nor as a result of Anglian's inaction activities as Ofwat suggest.
- (55) As stated in Anglian's 20 November letter³⁴, Anglian has had detailed discussions throughout the Summer, including regular discussion between CEOs and senior people in both organisations as well as regular calls and letters between regulation, procurement and water resources specialists in Anglian and Ofwat's DPC team.
- (56) Anglian's submission expressed surprise that Ofwat's reply to responses to Provisional Findings³⁵ failed to mention on any occasion Anglian's concerns over failure to deliver against legal obligations, not being able to maintain the supply demand balance, nor deliver the improved level of drought resilience, none of which is in customers' interests.

³³ Ofwat response to provisional findings responses: Costs and Outcomes para A1.10

³⁴ Specifically pages 7-8

³⁵ Specifically Annex A1 – Anglian Water – Elsham direct procurement for customers scheme – A1.1 – A1.14 pages 37 - 41

8.3 There is clear evidence of Anglian’s contribution to the development of the DPC process and of Anglian’s active efforts to resolve issues

- (57) Anglian has fully committed to the DPC process and established a dedicated team since before the start of this AMP. The 10 members of the cross-functional team with further experts from the wider business have successfully delivered a number of key activities as well as establishing processes and governance. This has been completed in advance of elements of the DPC framework and licences changes being finalised.
- (58) For example, Anglian has procured, appointed and mobilised:
- The enabling partners;
 - Legal advisors; and
 - Financial advisors.
- (59) In addition, Anglian has:
- developed and tested a detailed project plan for the delivery;
 - drafted an outline commercial model and tested the principles with SME’s;
 - drafted the enabling scope and started to develop the tender design documentation; and
 - developed and submitted the Strategic Options Case (SOC).
- (60) To support the pace required and development of the DPC process, since March 2020 members of Anglian’s and Ofwat’s DPC teams have met weekly to share progress and explore emerging issues. For example, through this forum Anglian has discussed with Ofwat the development of the proposed licence conditions required to enable DPC to be reflected in companies’ licences. This collaboration includes “soft-testing” Ofwat’s draft licence condition consultations ahead of formal publication.
- (61) Anglian has continued with market engagement which was started in 2019. An event inviting feedback has been held as well as one-to-one engagements.

9 Ofwat’s suggestion that in-house and DPC processes can fully progress in parallel is incorrect

9.1 Differences between in-house and DPC processes

- (62) Anglian considers that developing and running both in-house and DPC processes fully in parallel is not practical. Anglian’s view is that to do so would have a significant detrimental impact on the effectiveness and efficiency of both scheme delivery and the DPC process itself. For example:
- Anglian would be required to develop two agreements and commercial models for the delivery of the works covered by the DPC scope – i.e. an agreement with the potential CAP and one with the in-house delivery route. Clearly the DPC agreement remains uncertain until the scope of the works is agreed;
 - Specific aspects which would be delivered in-house would be unable to progress in earnest as the activities may pass back to the CAP;
 - Network Rail’s Basic Asset Protection Agreement (BAPA) process requires the contactor undertaking the works to be named in order to progress. Anglian could not progress this element until the scope is known; and
 - The impact of having to focus on the parallel process on an already constrained timetable will impact the DPC process as it diverts the core teams time away from DPC.

- (63) Anglian also considers that the focus and priorities for outline design are different for in-house delivery compared to delivery via DPC, specifically:
- The focus of DPC outline design is to provide a level of reference design to specify inputs/outputs in terms of water quality & performance, a conservative footprint to allow for Environmental Impact Assessments (EIA) and planning progression and detailed specification around the interface point control and operation to allow for a robust contract to be developed;
 - Whilst the focus of in-house outline design would also cover additional EIA and planning, there would be more specific design on the critical Mechanical and Electrical components for the process. This would allow for earlier procurement of these items soon after Outline Business Case development (this would align with Anglian's in-house DM2 stage);
 - Under in-house delivery, aspects such as interface control and operation would be of a lower earlier priority given that all assets would remain in Anglian ownership. This contrasts with the requirements under DPC, where a significant level of detail would be required in the outline design needed for the CAP contract.
 - Anglian does not intend to provide the CAP with specific equipment requirements for the WTW process in order to prevent either restricting their options to deploy new innovative processes and in recognition of existing relationships the potential CAP may have with existing equipment manufacturers. This will introduce longer time periods into the process relative to using Anglian's existing supply chain arrangements with approved suppliers.
- (64) Anglian believes these differences do not support running these both in-house and DPC processes in parallel.

9.2 External comparison

- (65) A study undertaken by the National Audit Office³⁶ (NAO) of PFI deals in the UK between 2004 and 2006 stated:

"We have found examples of well managed and properly resourced projects that have taken 18 months to tender, including preferred bidder negotiations lasting less than six months. This suggests that a target of between 18 to 24 months would not be unreasonable for many projects, although it may be unrealistic for particularly complex, one-off PFI deals."

- (66) Anglian considers that the first DPC scheme is comparable to a one-off PFI deal as it has never been done before in the water industry and is highly complex.

9.3 Impact on the potential DPC parties

- (67) Undertaking both processes in parallel would create a level of uncertainty during the market engagement phase of the DPC process. It would undermine the credibility of Anglian and the DPC project if it is known by the market that Anglian is developing a fallback option. This is critical to ensuring the investor market is interested and starts to establish partnerships or supply chains ready to respond to a call for competition. If the investor market understands there may be an alternative route to delivery this could lead them to not investing early in the process until certainty is established.
- (68) In discussing which activities can be progressed in parallel, Ofwat fails to recognise the impact that the scale and depth of in-house preparation would have on the potential CAPs, specifically their incentive to fully engage and sink time and resources into the DPC process. Put simply, if the potential CAP

³⁶ NAO (March 2007) - Improving the PFI tendering process; available at <https://www.nao.org.uk/wp-content/uploads/2007/03/0607149.pdf>

providers expect that reversion to in-house delivery is highly likely, this is will have a detriment to the level of expected market engagement, which makes in-house reversion even more likely.

10 Ofwat and the CMA are overstating the risk to the overall DPC process

- (69) In reaching its conclusion the CMA gives weight³⁷ to Ofwat's argument³⁸ that, should the CMA redetermine the Elsham scope, this would undermine the DPC framework.
- (70) Anglian disagrees with this conclusion as this fails to recognise a range of specific factors that apply solely to Elsham. Specifically, the combination of:
- a. The legal obligations Anglian are required to deliver by the end of AMP7;
 - b. The technical complexities of the Elsham and Lincolnshire system;
 - c. The fact the DPC process has been in development during the last 18 months and will be fully in place for future schemes; and
 - d. The "first of a kind" engagement with potential CAPs that will not be repeated for future schemes.

10.1 "Size test" risk

- (71) Ofwat is concerned that in progressing only the treatment works element of Elsham the scheme fails to meet its "size test" and hence may not be in customers' best interests³⁹.
- (72) As Ofwat notes, the size test threshold (£100m totex) is based on the theoretical assumption that the potential benefits to customers of larger schemes would outweigh the marginal increase in procurement costs. Anglian recognise the merit of this argument as far as it goes and does not dispute the overall principle.
- (73) However, Ofwat seems to fail to recognise that it is not only totex that will impact on the potential value for money for customers, but also operational and commercial complexity. Essentially the discreteness test for the full Elsham DPC captured this by concluding that the full scheme was less suitable for DPC. It follows that this operational and commercial complexity will be "priced in" to bids from potential CAPs.
- (74) Ofwat does not recognise the evidence provided by Anglian of positive value for money for the treatment only scheme⁴⁰ nor the views of Mike Woolgar's independent review which concluded that Anglian's proposal to offer the Elsham treatment works seems reasonable for the following reasons:
- a. the market is comfortable with single facility opportunities;
 - b. the ability to describe scope and operations will be simpler; and
 - c. work can proceed in parallel on procuring other critical path items which are necessary for the effective commissioning of the scheme and it should be of sufficient scale to interest the market.

³⁷ Elsham Consultation – Para 21

³⁸ Ofwat reply to responses to PFs – costs & outcomes, paragraph A1.7.

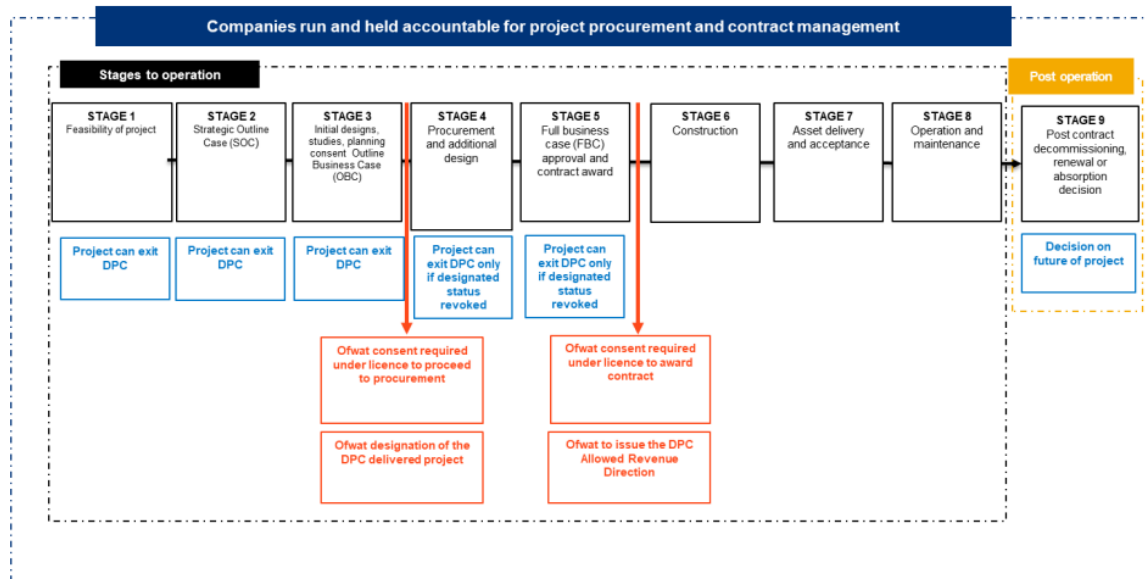
³⁹ Reference of the PR19 final determinations: Costs and outcomes – Ofwat December response (December 2020) – Paras 8.11 – 8.12

⁴⁰ The three scenarios which assessed value for money on the revised scope (focussing solely on treatment (CLN13a)) produced a positive potential outcome for DPC ranging from £0.42 to £2.61 million.

10.2 Process risk

- (75) The CMA's view is that the redetermination should not revise the scope of the Elsham DPC⁴¹. In support of this view, the CMA states that if it were to revise the scope it would risk undermining the DPC process⁴². Anglian disagrees with this conclusion.
- (76) Consistent with Ofwat's own view of the DPC process, there is an expectation that for potential schemes occurring during the 2020-25 period, the feasibility of DPC projects will be undertaken and form part of the PR19 Final Determination. The full process⁴³ Ofwat envisage is set out below:

Figure 4 The detailed 9 stages of a DPC delivered project



- (77) This clearly demonstrates that it is Ofwat's own expectation that projects can exit or be amended at the first three stages of the overarching DPC process. Given that Anglian has asked the CMA to redetermine its PR19 Final Redetermination, it is a legitimate expectation that CMA now undertakes this first stage of the overall process rather than relying on subsequent stages. This is particularly relevant for the Elsham scheme given the timing pressures.

10.3 Wider Ofwat DPC incentives

- (78) It should also be noted that Ofwat has a clear incentive to use the early DPC schemes as a mechanism to demonstrate to the sector that there is an effective DPC IDoK route should potential schemes revert to in-house delivery. Anglian believes Ofwat is placing greater weight on demonstrating this than it is to securing the necessary drought resilience and supply demand benefits to Anglian's customers. The CMA's conclusion therefore risks doing the same.
- (79) Ofwat has a further incentive to use the DPC IDoK process to create a further opportunity to challenge the efficiency of a companies' proposed expenditure. In the case of Elsham this is the case despite the CMA in its provisional findings supporting the benchmarking evidence Anglian provided.

⁴¹ Elsham consultation – para 22

⁴² Para 21

⁴³ July 2020 - Appendix 5: Direct Procurement for Customers – Briefing Note on the Procurement Process for 2020-25 – Page 12

11 Conclusion

- (80) **Anglian requests that the CMA, by taking into consideration this response and the full suite of materials previously presented to it by Anglian, reflects in its final redetermination the necessary amendments to the scope of the Elsham DPC scheme. Specifically, Anglian requests that, in the interests of customers and the environment, only the Elsham treatment element (CLN13a) is taken through the DPC process.**
- (81) This is the only course of action that would resolve matters swiftly and enable Anglian to meet its environmental obligations within the timeframes set out and mitigate the risk of insufficient water supply.
- (82) The alternative, using Ofwat's untested and developing DPC process for the full scope of Elsham, would create the almost certain outcome that Anglian could not meet its environmental obligations within the timeframes required.
- (83) This would leave customers and the environment exposed to risks of shortage of supply or overabstraction, which would be of significant detriment, and would be inconsistent with a proper discharge of the CMA's duties, including the Consumer Duty and the Resilience Duty.
- (84) Anglian has previously provided the CMA with the relevant information required to make the necessary adjustments to totex allowances, performance commitments and ODIs⁴⁴.

⁴⁴ Anglian Response to Provisional Findings – Chapter E, Section 3.5. Pages 33 – 37, paragraphs 184 - 209