

Initiating and delivering major projects in regulated industries

Highlights

Highlights from the Major
Projects Association event
held on 7th November 2023



**MAJOR PROJECTS
ASSOCIATION**

'I can't think of a single entity that doesn't have to step up and think differently. We can't just look back at what we've done, because what we've done is never going to get us where we want to get to.'

Andy Mitchell CBE, Chief Executive Officer, Tideway

This seminar explored the challenges facing project professionals operating in regulated industries, with a focus on the water sector. The water sector is gearing up to deliver a capital investment programme of size, scale and complexity not seen in the post-privatisation era.

Business as usual will not be sufficient. Regulators, investors and industry need to work collaboratively to use the flexibility available to the sector to establish robust delivery models that deliver best value for customers. All players, including the regulators, face a huge task to upskill and develop the capability and capacity to deliver a programme of this scale and complexity. Coordination and prioritisation within the sector and with other parts of the UK infrastructure investment programme is likely to be needed.

Demand is high across the regulated sectors

Andy Mitchell, CEO of Tideway, opened proceedings by observing that the seminar was timely, because historic underinvestment, population growth, net zero and other challenges are also generating the need for very large investment across the UK's regulated energy, transport and communications sectors. This is placing huge demands on the capacity and capability of clients, regulators, investors, advisers and the construction supply chain.

Andy observed that **Tideway** is essentially a delivery and finance mechanism. Tideway and its partners had to commit time and resources over a period of years to ensure they all understood how the model worked, and its implications. In particular, the key concern was the impact on Thames Water bill payers, so it had to be clear how risk would be apportioned and managed in a way that protected their interests. As a result, while there has been some slippage in programme and an escalation in budget, the final cost to bill payers is likely to be around £25pa, which in inflation-adjusted terms is significantly below the £20–25 estimate made in 2014.

The role of the regulator

Colin Green, Director of **RAPID** (Regulators' Alliance for Progressing Infrastructure Development) explained that a range of factors has created a projected shortfall of circa 25% in the water sector's ability to meet customer needs. Demand reduction will help, but new supply infrastructure will be needed.

Against this backdrop, in 2018 **Ofwat**, the **Environment Agency** and the **Drinking Water Inspectorate** wrote to water companies stressing the need for collaboration to secure best-value outcomes for all stakeholders.

Ofwat also recognised its role in de-risking the early development phase of potential solutions, and made £469m available to water companies to kickstart development work on 17 potential schemes. RAPID was formed to provide coordinated regulatory oversight of this process and work through any blockers in existing arrangements.

A key challenge is that the UK's post-privatisation legal framework is built around individual water companies, but to meet the scale of demand a regulatory and commercial framework will be needed that supports multi-party, multi-beneficiary projects.

RAPID is currently overseeing a programme of 18 projects worth circa £15bn. It operates a gated process, taking proposals from early-stage concept design to the submission of a planning application, at which point it hands over to Ofwat which then supports projects through the delivery phase.

Picking up this baton, Kate Kendall, Ofwat's Interim Senior Director, Major Projects, described how Ofwat was in the process of reviewing its role in overall management of the investment programme and the support it provided to individual major projects. Kate added that Ofwat recognises it is likely to need to take a lead in managing the pipeline, including the phasing of projects.

Drawing on the positive experience of Tideway, Ofwat is committed to competitive delivery of any project over £200m, and currently has two broad delivery models in its toolkit: Direct Procurement for Customers (DPC) and Specified Infrastructure Project Regulations (SIPR).

Direct Procurement for Customers (DPC)	Specified Infrastructure Project Regulations (SIPR)
Used for HARP (Haweswater Aqueduct Resilience Programme)	Used for Tideway
Competitive tender issued by water company to find a Competitively Appointed Provider (CAP) to design, build, finance, operate and/or maintain the infrastructure on a 25-year concession basis	A new third party company licensed and regulated by Ofwat is created to deliver the infrastructure. Receives payments on a regulated price control basis
Ofwat default model for any project over £200m	Legislation permits this model to be used if: • The project is of a size or complexity that threatens a water company's ability to provide services for its customer • Delivering the project via this route is likely to result in better value for money

Ofwat also believes it has a role in market engagement and market shaping. This demands an investable pipeline, and the regulator's role includes identifying opportunities at the programme level for standardisation and sharing data and knowledge.

'This is the first time since privatisation, that we've seen a significant increase in the number of large-scale projects. We recognise that this increase in project pipeline requires Ofwat to consider how we can best fulfil our role in facilitating these projects.'

Kate Kendall, Interim Senior Director, Major Projects, Ofwat

Investor and supply chain challenges

Amar Qureshi, Joint Managing Director of Agilia, stressed that the UK water sector is attractive to investors. Political stability is high, neither main party is interested in unpicking privatisation, and there is consensus that major investment in infrastructure is needed. Our regulatory regime is genuinely world leading, providing both stability of revenues and flexibility within a set of clear principles.

Illustrating this point, he contrasted his experience with PFI, where a single model was applied by HM Treasury across multiple sectors, to his work with Tideway, where the project had the freedom to make fundamental choices, for example to run separate procurements for investors and the construction supply chain.

All of this contributes to the positive view of the sector amongst ratings agencies, which is vital to keeping the cost of capital low and minimising cost to bill payers.

Anthony Faughan, Partner at Arcadis, broadened the conversation to the challenges and opportunities in the wider business environment. Across the regulated industries the rail, energy, water and telecoms sectors are all looking to accelerate multi-billion-pound programmes. He pointed to a contradiction between this huge demand for supply chain capability and the redundancy programmes many corporates are undertaking in response to balance sheet fragility and rising costs.

This supply chain fragility is mirrored by the financial pressures currently being experienced by governments and individuals. In the face of these pressures business as usual is not an option. The efficiency and effectiveness of the whole infrastructure eco-system needs to improve to make these programmes affordable.

That demands a system-wide approach, orientated around key priorities such as decarbonisation.

Long-term investment needs to be combined with better collaboration at national, regional and local levels. There are opportunities to enhance effectiveness through areas such as data, modern methods of construction, supply chain development and contingency planning.

Setting up for success

Drawing on The Nichols Group's wide experience across multiple sectors, Oliver Bayne highlighted five areas where the water sector will need to focus to deliver a best-value programme:

- Leadership and culture
- Outcomes and requirements
- Clear roles and aligned governance
- Management of stakeholders
- Data and reporting

Mark Malcolm, Anglian Water's Programme Director, Major Infrastructure, explained that the business was currently pursuing the SIPR model (see table above) for two major schemes in development. This generates very different challenges to promoting a more traditional scheme.

The business has to put itself in the mind of investors, and work to create a fully functioning corporate entity that is an attractive acquisition. This demands a high level of front-end activity to ensure the technical solution is robust and buildable. Anglian are also working through the challenges of establishing multi-party, multi-beneficiary schemes.

The seminar concluded with a panel discussion on critical success factors for the programme. Kate Kendall and Amar Qureshi were joined by Rachael Saville of Arcadis and Kirsty Invanoski-Nichol of The Nichols Group.

Recurring themes identified by the panellists included a definitive shift away from 'Punch and Judy' transactional relationships towards models that do not push any player to the brink; promoting the attractiveness of the water sector to investors, supply chain and individual professionals; and identifying ways to bring greater to all aspects of the programme.

'We have all talked about collaboration but what we need is purposeful collaboration, recognising that people will play different roles at different parts of the programme – and that at different stages of the programme we need different types of collaboration. It's not just having everyone in the room for every decision that is made.'

Kirsty Invanoski-Nichol, Director of Transformation and Change, The Nichols Group

Points for further discussion

- How can water sector stakeholders collaborate to improve the phasing of major projects? Could this be extended to a cross-sector coordination mechanism?
- What are the best mechanisms for sharing lessons from water companies' efforts to develop projects under the DPC and SIPR models?

Chair

Andy Mitchell CBE, Chief Executive Officer, Tideway

Contributors

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Alliance Manchester Business School
Anglian Water
Arcadis (UK) Limited
AWE
CJ Associates
Costain Ltd
EY
Grant Thornton UK LLP
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