Thames Tunnel

Second Phase of Consultation by Thames Water
Consumer Council for Water: Submission to the Thames Tunnel Consultation by Thames Water

Introduction

1. The Consumer Council for Water (CCWater) is the statutory consumer organisation representing water and sewerage consumers in England and Wales. We have four regional committees in England and a committee for Wales. This response has been prepared by members of the London and South East Committee who have been in regular dialogue with Thames Water, Defra and the Environment Agency (EA) over the development of proposals for the Thames Tideway since our establishment in 2005.

2. We have made representations at each stage of public consultation (links are given at Annex A). We draw particular attention to our response to the first phase of consultation Thames Water conducted on the Thames Tunnel proposal (Annex B). As many of the concerns we raised then remain, we have referenced our earlier submission rather than repeat our earlier arguments and explanations which are familiar to Thames Water.

3. We welcome the opportunity to respond to this latest phase of consultation on the Thames Tunnel proposal. Although this consultation is primarily aimed at those who are in close proximity to the proposed tunnel route, and therefore directly affected by construction and the operational sites, it also provides for comments on the wider issues associated with this scheme (Part 2) and the consultation process itself (Part 3). We address these issues in this submission.

Summary

Part 2: The Need, Solution and Tunnel Alignment

4. We recognise the need for increased investment in the capacity of London’s main drainage system and measures to manage surface and storm water in a more sustainable way. Between 2010 and 2015 more than £1.2billion will have been spent on Tideway water quality (which we supported) and is already being paid for by all Thames Water’s sewerage customers.

5. The proposed Thames Tunnel is an exceptional scheme; the largest sewerage scheme in terms of size and scope undertaken since privatisation. Yet the estimated costs have escalated since it was first proposed, and are now estimated to be at least £4.6billion by 2020 [not counting the Lee Tunnel], with a risk of further cost escalation. Even before this increase the projected impact on Thames Water’s sewerage bills significantly exceeded customers’ level of willingness to
pay. It is now set to add at least £70-£80 on average to Thames Water’s sewerage customers’ annual bills. We are concerned that this significant step change in bills may not be acceptable to customers; will exacerbate existing affordability issues; and may well create new problems as these large bill increases combine with the company’s intended roll out of compulsory metering.

6. The European Commission’s December 2011 Report on Implementation of the Urban Waste Water Treatment Directive (UWWTD), recognises that the UWWTD does not impose an absolute requirement, compromises are acceptable:

“Intelligent technical solutions are an appropriate treatment and an acceptable cost-efficiency should be maintained to solve the difficult situation between investment and environmental requirements”.

7. We would therefore question whether the Thames Tunnel proposal reflects this, and the ‘BTNEEC’ (best technical knowledge not entailing excessive cost) aspect of the UWWTD.

8. We also note that the Government has now introduced a Water Industry (Financial Assistance) Bill that, subject to affordability, provides for transparent forms of guarantee to support specific water and sewerage infrastructure projects where this provides best value for money for taxpayers and users, recognising that the private sector cannot always bear every risk. This commitment was in line with Government confirming, in a November 2011 statement to Parliament, that it was willing in principle to provide contingent financial support for exceptional risks in the construction of the Thames Tunnel. We welcome any intervention by Government that reduces the potential financial impact on Thames Water’s customers.

Part 3: Consultation Process

9. Thames Water has gone to considerable lengths to raise awareness to the Thames Tunnel scheme and consult with those who may face disruption or inconvenience, over several years, as the Tunnel is constructed. Loss of local amenity, like access to public parks and open space, increased traffic noise and disruption are amongst the concerns being raised by local people. While it is not within our remit to comment on the selection of sites, we feel that it is incumbent on the company to include in its overall scheme appraisal the wider social and environmental impacts at a local level and for London and does all that it reasonably can to mitigate the adverse impacts on local communities.

10. We also wish to see Thames Water communicating with its wider customer base to raise awareness of the need for the Tunnel; what it will deliver; and how it will impact on all sewerage customers’ bills.

Part 2: The Need and Tunnel Solution
The Need

11. In our submission to the first phase of public consultation we made clear that we accepted the need to invest in improving London’s sewerage system, and in reducing the volume and frequency of discharges into the river Thames in order to comply with the UWWTD and thereby avoid EU infraction fines. That said, we believe that the UWWTD does allow the issue of excessive cost to influence the preferred solution. Moreover, the Water Framework Directive (WFD) allows the adoption of less stringent environmental objectives where achievement of the standards would be technically infeasible or disproportionately expensive, subject to conditions. One of the conditions is that there should be no further deterioration in status.

The Solution

12. Given that the projected cost of the Thames Tunnel has more than doubled, there are continuing questions over the current preferred solution (as demonstrated at the Selbourne Inquiry), and questions about the adequacy of the willingness to pay and benefits assessments undertaken to date still to be addressed, there is more work to be done to convince us that the Tunnel is the right solution.

13. We continue to believe that the scheme costs will place a disproportionate and unacceptable financial burden on Thames Water’s customers for the level of benefit they will see delivered. This is particularly so in the current economic climate.

14. Much is being made of the employment and wider economic benefits that are associated with major infrastructure projects. We would question whether these opportunities are likely to benefit the significant proportion of the company’s customer base currently living in some of the most deprived boroughs in the UK who may find themselves paying double the amount for their water and sewerage services in future years as a result of increasing prices and a move to metered charging.

The Costs

15. The estimated cost of the project has escalated, from £1.7billion in 2004 (including Lee Tunnel and sewage treatment works costs) to the current figure of £4.6billion for the main tunnel, on the assumption that it will be funded on a pay-as-you-go basis. There is no guarantee that the current estimate will not be subject to further cost escalation. These costs will potentially be borne by all Thames Water’s sewerage customers, in and outside of London. If a different funding process were to be selected, very significant financing costs would have to be added to the estimate for engineering costs.
16. It is imperative that customers are provided with an accurate picture of bill increases that are likely to be derived from the costs of this project, other likely pressures on bills, how such bill increases will accumulate over time, and how long they will last. Thames Water does have comparatively low sewerage charges at present, but there will be a number of investment drivers forcing bills up in the future, some of which might have greater priority amongst customers; many customers may simply wish to keep their bills as low as possible.

17. The contribution that customers will potentially make to the cost of the project will be determined by the final cost of constructing, operating and maintaining the Tunnel, the way the construction is to be funded and the way that customers are billed for their sewerage service. Ofwat has a duty to guard against cost overruns and ensure value for money. However, the bill impacts on individual households will reflect the basis on which their bill is calculated (metered or unmetered) and the size of the variable element of their bill. Unless alternative cost recovery mechanisms are put in place or protection is extended to those on low incomes the Tunnel costs combined with the move to metered charging will place the biggest financial pressures on those who can least afford it.

18. Thames Water is looking to introduce a social tariff, in line with Government and Ofwat guidance. The scope for a company based social tariff to tackle the existing let alone future affordability problems is limited by the amount that other customers are prepared to support such cross subsidies. Currently the Government has suggested a capped percentage increase on average bills that would equate to a contribution of around £5 per customer in the case of Thames Water. With twenty per cent of the customer base currently on means tested benefits the targeting of the financial assistance available is only likely to help those in the most extreme hardship, possibly the worst off five per cent, while loading another £5 on to the bills of those who just miss qualifying for help.

19. The Government introduced a Water Industry (Financial Assistance) Bill on 2 February 2012 that would enable contingent funding for the enormous risk attached to major infrastructure schemes like the Thames Tunnel through Government guarantee. This will help secure finance for the scheme which might otherwise have difficulty in raising capital or make the cost of capital very expensive. The Bill also provides for financial assistance to be given to water and sewerage undertakers to secure a reduction in water and sewerage bills where Government considers it desirable to do so. We welcome any intervention that will help to minimise the risk and financial burden carried by Thames Water’s customers.

20. We would wish to see the costs attributed to this and other major infrastructure schemes shown separately on water and sewerage bills to allow customers to see how these investments are impacting on what
they pay, and so that assurances about bill impacts are seen to be delivered.

Cost/Benefit Assessment

21. In our submission to the first phase of consultation we called for the updating of the 2007 Regulatory Impact Assessment (RIA) so that the most recent information on costs and benefits, as well as improvements delivered through the 2010-2015 investment programme, could be taken into account. Defra has since published “Thames Tunnel, Strategic and Economic Case”, and “Thames Tunnel, Costs and Benefits”\(^1\) which summarise the strategic and economic case for the Tunnel.

22. In the Strategic Overview, Defra states that the European Commission’s position is that the “magnitude” of the discharges now occurring in London does not constitute an adequate collection system. In relation to benefit values and value for money there are many caveats attached to the various assumptions/factors applied by Defra in the cost/benefits analysis. It states that “The analysis of costs and benefits should be viewed as high level, with particular uncertainty attaching to benefits estimates” as, too, the issues surrounding “baseline environmental conditions”.

23. Defra’s quoted range of benefits is now put at “between £2,969billion and £5,058billion” - a very wide range, but without making a strong statement about the most likely point within it. Defra then assumes benefits will be in the upper band and concludes: “The broad conclusion that the Tunnel is a net beneficial investment for “UK Plc” would appear reasonable.”

24. With such caveats, uncertainties and reservations surrounding the cost/benefit analysis, we question whether the Tunnel can properly be described as value for money for customers. Even taking the highest figure in the range of benefits (£5.1billion), against the potential cost of the Thames Tunnel and £1.2billion for the Lee Tunnel and associated works, the case is less than compelling.

25. Defra increase the £2.969billion basic benefit estimate to £3.948billion based on presumed real income growth over the life of the Tunnel “assuming only modest growth over the next few years, in line with the current economic situation” using ONS GDP estimates to 2010 and Treasury estimates of mid-term growth to 2014, followed by an assumed return to long-term real growth rate of 2%. But the growth estimates used were taken from HMT Forecasts published in August 2010, which exceed the equivalent HMT Forecasts published in November 2011, the same month in which Defra published its analysis. A comparison with the

latest forecasts shows the Defra assumptions as to growth are overstated and the benefit value likewise.

26. Defra is still relying on the willingness to pay survey conducted in 2006. The doubts attaching to this survey, expressed in the original 2007 RIA, and which we have raised on several subsequent occasions, remain significant. Defra say the 2006 survey “suggested that people would value these benefits [reducing fish deaths, adverse health impacts and sewage litter and odour] within a range of around £4.4bn in aggregate (up-dated to 2011 prices)”. Defra acknowledge “the uncertainty surrounding benefit estimates of this type (namely derived from a survey of willingness to pay for essentially un-marketed goods and services)”. Yet no further survey has been undertaken or evidence produced to deal with such doubts, nor to support Defra’s conclusion that “On balance….we would argue that the benefit is more likely to be in the upper half of the range”.

Conclusions

27. While the need for investment is accepted, and the case for a Tunnel has been strongly made by Thames Water and is clearly supported by Defra, many of the concerns we have previously stated relating to cost, benefit, customer acceptability and affordability remain. These would be increased if some PFI type of funding model were to be adopted.

28. We accept also that Thames Water is in a difficult position in that, as a statutory water and sewerage provider, it has a duty to help deliver Government objectives and commitments that may not be popular with its customers or indeed shareholders. We therefore believe:

- It is for Defra, Ofwat and EA to ensure that this scheme represents value for money;
- that the Government must provide a meaningful contribution to the financing of such an exceptional scheme;
- the benefit of any Government contributions/funding must accrue to Thames Water customers, and not to the benefit of Thames Water or its shareholders: Defra, HMT and Ofwat need to impose funding structures and regulatory controls that deliver this;
- in the interests of Thames Water customers, and UK taxpayers under a Government guarantee, there must be an incentive on Thames Water to guard against further escalation of anticipated project costs and against cost overruns once the project commences;
- suitable protections should be in place to ensure that any efficiency savings and underspends are given back to customers;
• customer acceptability and affordability should be key considerations in the timing and mechanisms for cost recovery; if customers do not support the degree of social tariff cross-subsidy that would be required to meet affordability issues attributed to this step change in bills, Government must consider its responsibilities to help ease the impact on households, as it has for customers of South West Water; and,

• that, in the interests of transparency and accountability, Thames Water bills should show the amount attributable to the cost of the Tideway improvements.

**Enquiries**

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