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Industry and Regulators Committee

1st Report of Session 2022–23

The affluent and the effluent: cleaning up failures in water and sewage regulation

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Industry and Regulators Committee

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See Appendix 1.

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Evidence is published online at <https://committees.parliament.uk/work/6719/the-work-of-ofwat/publications/> and available for inspection at the Parliamentary Archives (020 7219 3074).

Q in footnotes refers to a question in oral evidence.

SUMMARY

Water is one of earth's most precious resources. It is essential for human life, agriculture, and industry. But water is not always treated with the care and importance it deserves, including in the UK.

The Environment Agency's annual water and sewerage company performance assessment for 2021, published in July 2022, found that the environmental performance of water companies was at its lowest ever level and most companies' performance was declining.¹ The Environment Agency told us that unless change is made, in 20 years the UK will not have enough water to match demand.²

Water companies, which supply our water and maintain associated infrastructure for water and sewage, must improve their practices dramatically to prevent further damage to the environment and secure future supply.

Since the privatisation of the water industry in England and Wales in 1989, there have been some improvements in the sector, such as the supply of good quality drinking water, investment in wastewater treatment, and protecting homes from sewer flooding. Nevertheless, pressures on the sewage network have increased substantially over time due to a combination of population growth, property development and climate change. Levels of investment have not risen to match these demands. The result is a network unable to cope, and which relies on releasing polluted water into the environment.

Nor has investment kept pace with the demands of future water supply needs, leaving us lacking appropriate plans and infrastructure to deal with future demand, and the loss of billions of litres of water to leakage every day.

Ofwat and the Environment Agency must go further to hold water companies to account for pollution.

It appears that it has often been individuals and organisations that have brought pollution issues and the abuse of storm overflow permits to public attention.

Ofwat and the Environment Agency only began penalising and prosecuting water companies for causing environmental damage in recent years, after monitoring of storm overflows and wastewater treatment sites was rolled out. The Environment Agency told us that it has not had the necessary funding or data access to take sufficient enforcement action against water companies. With widespread monitoring and data now in place, the Government must ensure that the Environment Agency has adequate funding to monitor and enforce environmental offences by water companies. Greater transparency is also needed and the regulators should explain how and when they will ensure open data on environmental performance is provided consistently by all water companies as a matter of priority.

1 Environment Agency, *Water and sewerage companies in England: environmental performance report 2021*, (22 July 2022): <https://www.gov.uk/government/publications/water-and-sewerage-companies-in-england-environmental-performance-report-2021/water-and-sewerage-companies-in-england-environmental-performance-report-2021> [accessed 22 December 2022]

2 Q 98 (Sir James Bevan)

Requiring water companies to disclose information to the same standard as publicly listed companies has the potential to improve their governance and increase scrutiny of their financial arrangements. Water company executives and board members should not receive large bonuses while their companies continue to fail the environment. Executives and board members should face greater individual accountability and sanctions for egregious environmental crimes, including being barred from working in the sector again.

Ofwat has failed to ensure companies invest sufficiently in water infrastructure, choosing to keep bills low at the expense of investment. Greater investment in the water industry is now urgently needed, accompanied by a single social tariff to protect vulnerable customers from bill increases.

Ofwat is responsible for setting the prices consumers pay for water and ensuring companies meet the conditions of their licenses and statutory obligations. This includes a requirement on water companies to provide and maintain sewers, to deal with the contents of those sewers, and to certify to Ofwat that they have the resources to do so.

The five-year Price Review process is appropriate for iterative improvements to underlying assets but long-term investment in environmental improvements and increasing water supply has remained low. Ofwat should find ways to increase investment outside the Price Review process and consider the important role that third-party competition could play in reducing costs, as it did with the Thames Tideway tunnel project.

We heard that the investment needed to update fully the water and sewerage systems could run into tens or hundreds of billions of pounds over multiple decades. The Secretary of State told the Committee that public money was not available for this. Therefore necessary upgrade investment will be financed by water companies, as they are primarily responsible for adequately maintaining their water and sewage networks, and/or specialist infrastructure investors.

Customer bills will likely increase, which by 2025 will have been flat or falling for 15 years in real terms. The Government should legislate to introduce a single social tariff in time for its inclusion in the next Price Review, in order to protect vulnerable customers from bill increases.

Cheaper, more innovative solutions to reduce water pollution should also be investigated, including the potential of nature-based solutions, such as the use of uncropped arable land for storing water. A move to outcomes-based regulation could support such innovation. The enactment of Schedule 3 of the Flood and Water Management Act 2010 and the subsequent requirement for new developments to have sustainable drainage systems could also provide a significantly lower cost way to reduce pressure on the sewage system.

The Government has historically failed to engage sufficiently with the sector and its regulators. The Government and regulators including Ofwat and the Environment Agency have not approached the key issues facing the sector in a joined-up way, including reducing water pollution and securing future supply. The Government's advice to Ofwat has not given clear guidance on how it should balance and prioritise its duties, even though it provides such guidance to other regulators. Putting right the problems in the infrastructure of the water and sewerage systems after decades of under-

investment is urgent but it must be understood that this is going to take a decade or more. It is also going to require more effective coordination and proactivity on the part of the Government, regulators and water companies.

Ofwat is required to balance statutory duties that can be contradictory—for example, protecting the short-term interests of consumers by keeping bills low while also ensuring enough strategic investment is made to secure future supply. Ofwat has tended to focus on keeping bills low. Further clarity is needed to empower Ofwat to take the strategic decisions necessary to address long-term issues and to ensure accountability to Parliament.

The Government must do more to support Ofwat and the Environment Agency in reaching their targets on pollution reduction and future supply. For example, the Government's Storm Overflows Discharge Reduction Plan lacks bite. Proper monitoring of the Plan's progress is required. As part of its Plan, the Government should consider banning the sale of wet wipes that are not rapidly biodegradable.

The draft National Policy Statement for Water Resources Infrastructure should be designated to facilitate the building of much-needed infrastructure such as reservoirs. The Government must also set out clear policies and expectations, allowing regulators and water companies to work together to support consumers to make water-friendly decisions. The Government has set an ambitious target to reduce water demand but little progress has been seen in this area. Tools such as mandatory water metering could aid this effort as only about half of households currently have one.

We therefore call on the Government to publish a National Water Strategy, which should address these issues in a holistic way and facilitate a joined-up approach. The Strategy should set clear expectations in relation to the quality of the water environment and the resilience of water supplies, giving regulators clear benchmarks to work towards.

The affluent and the effluent: cleaning up failures in water and sewage regulation

CHAPTER 1: INTRODUCTION

Background

1. In 1989, provision of water and wastewater services in England and Wales was transferred from the Government to private water-only or water and wastewater companies. Water-only companies supply water, while water and wastewater companies both supply water and treat wastewater.
2. Household customers in England and Wales have their water supplied by companies which operate as regional monopolies, while non-household customers have a choice of provider. There are 17 major companies that supply water and sewerage services to household customers in England and Wales. In some areas, water and wastewater services are provided by the same company, whereas in others, these services will be provided to the same areas by different companies.
3. The Water Services Regulation Authority (Ofwat) is the statutory economic regulator for water in England and Wales. Its duties are set out in the Water Industry Act 1991,³ and it is accountable to Parliament. Ofwat issues water supply and/or sewage licenses to water companies, and ensures licensees are meeting the conditions of their licenses. Ofwat is also responsible for setting the prices paid by consumers, which it does every five years through the Price Review (PR) process. The next Price Review is due to take place in 2024, which will set limits on prices for 2025 to 2030.
4. Ofwat has no direct role in regulating the environmental impact of water. In England, this area is covered by the Environment Agency, which is responsible for regulating water quality, monitoring pollution incidents caused by companies, and providing permits that allow the use of storm overflows. It has the power to prosecute companies that fail to meet environmental standards. Natural Resources Wales is responsible for regulatory oversight of the environmental performance of water companies in Wales.
5. The Drinking Water Inspectorate regulates drinking water standards in England and Wales.
6. The Environment Agency's annual water and sewerage company performance assessment for 2021, published in July 2022, found that the environmental performance of water companies was at its lowest ever level and most companies' performance was declining.⁴ 2022 saw a period of increased public and media scrutiny of water supply and management. Record temperatures and low rainfall in the summer months caused drought

3 [Water Industry Act 1991](#)

4 Environment Agency, *Water and sewerage companies in England: environmental performance report 2021*, (22 July 2022): <https://www.gov.uk/government/publications/water-and-sewerage-companies-in-england-environmental-performance-report-2021/water-and-sewerage-companies-in-england-environmental-performance-report-2021> [accessed 22 December 2022]

conditions and led to hosepipe bans in many parts of the country. Public concern about the use of storm overflows grew due to widely publicised incidents of bathing waters being contaminated by sewage.

Our inquiry

7. We launched our inquiry into Ofwat on 23 May 2022. We received 36 written submissions and held oral evidence sessions with 12 panels of witnesses from June 2022 to January 2023. We are grateful for all the evidence we received.
8. Our initial call for evidence focused largely on Ofwat and its interaction with the Government and other regulators. As we heard more evidence, it became clear that the inquiry should also consider the regulation of the water industry more broadly.
9. Given Ofwat is the economic regulator for water in England and Wales, we limited our inquiry to this geographical area.

Structure of this report

10. Chapter 2 provides an overview of the main regulators in the sector and reviews their co-operation. It also considers co-operation across sectors in addressing water issues.
11. Chapter 3 focuses on Ofwat's statutory objectives, including the need to balance competing objectives and direction from the Government in this area.
12. Chapter 4 examines the Price Review process, the role of competition in the sector, and the call from some witnesses for the introduction of a single social tariff. It also considers the Water Industry National Environment Programme's (WINEP) move to outcomes-based regulation.
13. Chapter 5 focuses on storm overflow overuse and poor management of wastewater treatment sites. It examines solutions including nature-based approaches, sustainable drainage systems, wet wipes, and capital investment. Additionally, the chapter covers monitoring and subsequent enforcement, as well as the Government's Storm Overflows Discharge Reduction Plan.
14. Chapter 6 examines fines, penalties, and enforcement, including a consideration of prosecution, prison sentences for chief executives and board members, and Ofwat's special administration powers.
15. Chapter 7 considers the role of debt and leverage in company financing, levels of executive pay and dividends, as well as models of ownership.
16. Chapter 8 looks at the issue of future water supply, and the threat that demand for water will outstrip supply in the UK in the next 20 years. It covers water transfers, changing consumer behaviour, water metering, and reducing leakage.
17. Appendix 1 provides a list of committee members who have worked on this inquiry. It also lists any interests they have declared in relation to this inquiry. Appendix 2 provides a list of witnesses and links to full transcripts of oral evidence, alongside a list of all written evidence. Appendix 3 details our public call for evidence which was issued in May 2022.
18. **We make this report to the House for debate.**

CHAPTER 2: WATER REGULATION AND POLICY

Oversight of the water industry

19. In 1989, the water industry was privatised, and provision of water and wastewater services was transferred to private companies operating as regional monopolies. Three regulators were established under the Water Industry Act 1991 to protect the interests of consumers and the environment by regulating these companies: the Drinking Water Inspectorate; the National Rivers Authority; and the Director General of Water Services supported by the Office of Water Services (Ofwat). In 1996, the functions of the National Rivers Authority were taken over by the Environment Agency, and in 2006, the Director General of Water Services and Office of Water Services were replaced by the Water Services Regulation Authority, which continued to be known as Ofwat.
20. Ofwat is the independent economic regulator of water companies in England and Wales, and is responsible for setting the price, investment and service package that customers receive. It grants licenses to water and wastewater companies to allow them to operate and can issue penalties (such as fines) to companies who do not meet the conditions of their licenses. Ofwat's duties are set out in the Water Industry Act 1991, and it is funded by the companies it regulates.
21. In England, the Environment Agency is responsible for regulating the environment, including in relation to water quality and resources, and overseeing the environmental performance of water companies. It monitors storm overflow use and tests water quality. It also advises the Government on the matters it oversees. Its duties are set out in the Environment Act 1995, and it is mostly funded by grants from the Government. Environmental regulation is conducted separately by each of the devolved nations, including Natural Resources Wales, who work with Ofwat in relation to water companies operating in Wales.
22. The Drinking Water Inspectorate (DWI) regulates the quality of drinking water in England and Wales. It checks that water companies in England and Wales supply water that is safe to drink and meets the standards set in the Water Supply (Water Quality) Regulations 2018.
23. The Department for Environment, Food, and Rural Affairs (DEFRA) sets the overall water and sewage policy framework in England, including standard setting and drafting legislation. The Welsh Government carries out this role in Wales. The Secretary of State for Environment, Food, and Rural Affairs is responsible for setting strategic objectives for Ofwat through a Strategic Policy Statement (SPS).

Co-operation between the regulators

24. In England, both Ofwat and the Environment Agency have a role in relation to water companies' environmental performance, in particular through the Water Industry National Environment Programme (WINEP), an investment programme through which the Environment Agency specifies works required by water companies to meet environmental goals. The WINEP forms part of Ofwat's Price Review process for water companies, which controls the levels

of prices, investment and spending allowed by water companies on regulated activities.⁵

25. In 2019, Ofwat, the Environment Agency and the DWI set up the Regulators' Alliance for Progressing Infrastructure Development (RAPID), a partnership that aims to facilitate the development and funding of new large-scale strategic water supply options by water companies by improving regulation and removing barriers.⁶
26. In November 2021, Ofwat and the Environment Agency launched a "major investigation" into sewage treatment works after water companies admitted that "they could be releasing unpermitted sewage discharges into rivers and watercourses". The investigation will cover all water and sewerage companies, involving more than 2,000 sewage treatment works.⁷ To date, Ofwat has opened enforcement cases into six water companies as a result of the investigation.⁸
27. Some evidence raised concerns that Ofwat and the Environment Agency do not work effectively together and should work more closely.⁹ Salmon and Trout Conservation stated that historically, "Ofwat has worked appallingly badly with the Environment Agency".¹⁰
28. Professor Catherine Waddams and Professor Michael Harker of the University of East Anglia suggested that the differing responsibilities of the two regulators "obscure accountability to the general public who often see them as a mechanism for 'buck-passing'". They also noted the possibility that their differing responsibilities:

"May result in environmental standards being set at a higher level than if the cost of implementing them was taken into account. This is likely to arise in practice because Ofwat is required to allow funding for environmental standards which have already been independently set."¹¹
29. Professor Ian Barker, Managing Director of Water Policy International Ltd, noted an example of this in 2014, where the Environment Agency indicated its approval for a proposed reservoir in Cheddar which Ofwat refused to provide the funding for, but which has subsequently been recognised as a potentially important strategic water resource.¹²
30. Christine McGourty, Chief Executive of Water UK, suggested that there have been positive steps forward in co-operation between Ofwat and the

5 Department for Environment, Food and Rural Affairs, Ofwat, Environment Agency and Natural England, *Water industry national environment programme (WINEP) methodology* (May 2022): <https://www.gov.uk/government/publications/developing-the-environmental-resilience-and-flood-risk-actions-for-the-price-review-2024/water-industry-national-environment-programme-winep-methodology#section-10-stage-5--price-review> [accessed 10 January 2023]

6 Ofwat, 'About RAPID': <https://www.ofwat.gov.uk/regulated-companies/rapid/about-rapid/> [accessed 12 December 2022]

7 Ofwat, Press Release: *Water companies could face legal action after investigation launched into sewage treatment works* (18 November 2021): <https://www.ofwat.gov.uk/joint-ofwat-environment-agency-and-defra-announcement-november-2021/> [accessed 27 January 2023]

8 Ofwat, 'Investigation into sewage treatment works': <https://www.ofwat.gov.uk/investigation-into-sewage-treatment-works/> [accessed 27 January 2023]

9 Written evidence from Professor Nigel Watson (TWW0005), Angling Trust (TWW0012), Water UK (TWW0021), Wildlife and Countryside Link (TWW0022) and Blueprint for Water (TWW0032)

10 Written evidence from Salmon and Trout Conservation (TWW0002)

11 Written evidence from Prof Michael Harker and Prof Catherine Waddams (TWW0007)

12 Q 9 (Prof Ian Barker)

Environment Agency. Yet there is “more to do” and the trade body would “love to see a tighter join-up between the economic and environmental regulators”. She raised the risk in the current system that the Environment Agency can specify outputs without Ofwat having said whether they are financeable, calling for the two regulators’ timelines to be joined up to provide a more efficient process.¹³

31. Ms McGourty argued the creation of RAPID “has brought big benefits” in terms of strategic water resources, but this co-operation is not seen in other areas, suggesting that a joint water quality programme between water regulators “could bring real benefits”.¹⁴ Stuart Colville, Director of Policy at Water UK, argued that the complexity of the system is very difficult to deal with on a day-to-day basis, calling for a better structured approach to water quality where all parties come together “with a single timeline and a clear sense of what we are all trying to achieve, to overcome those co-ordination issues”.¹⁵
32. On the other hand, Peter Perry, Chief Executive of Dŵr Cymru Welsh Water, said that he did not recognise a degree of conflict between the regulators, while Sarah Bentley, Chief Executive Officer of Thames Water, suggested that there is plenty of evidence of effective collaboration.¹⁶
33. Jonson Cox, former Chair of Ofwat, suggested that in recent years there has been a much greater degree of co-operation. For example, in the case of RAPID, he said: “I have never seen regulatory co-operation like that come together as it did in a year”. Yet he felt recent developments in relation to investigating wastewater plants have shown there needs to be closer working. This includes ensuring that the Environment Agency formally provides Ofwat with data about the performance of companies.¹⁷
34. Alan Lovell, Chair of the Environment Agency, argued that the Environment Agency works closely with Ofwat but it is inevitable and proper that there are some different priorities between the two, given their differing objectives. Sir James Bevan, Chief Executive of the Environment Agency, said his experience is that the relationship between the two regulators is good with both having clearly defined and complementary roles. He suggested that over the last seven years their overall strategic goals have been brought closer into line with each other, with Ofwat no longer focusing solely, “if they ever did”, on price and the customer, while the Environment Agency no longer focuses solely on the environment, although it is still its primary concern.¹⁸
35. Responding to criticisms that the regulators are not always aligned on investment needs, Sir James said that Ofwat and the Environment Agency work together to frame their asks and expectations of water companies in relation to environmental investment. He argued that the two regulators have constructive conversations, and while Ofwat makes the decisions on investment programmes, the Environment Agency plays a “leading role” in shaping what water companies need to do and “most decisions” embedded in the Price Review process “reflect the views of the Environment Agency”.¹⁹

13 [Q 54](#) (Christine McGourty)

14 *Ibid.*

15 [Q 54](#) (Stuart Colville)

16 [Q 117](#) (Peter Perry)

17 [Q 84](#) (Jonson Cox)

18 [Q 92](#) (Sir James Bevan)

19 [Q 99](#) (Sir James Bevan)

36. Sir James said that the Environment Agency shares data on spills with Ofwat and collaborates in tackling poor behaviour when they see it, pointing to the example of both regulators taking action against Southern Water in 2019, leading to separate fines and penalties.²⁰
37. David Black, Chief Executive of Ofwat, agreed that the regulators in the sector work in conjunction, while noting that there are “significant opportunities” to improve the planning process in future, particularly around environmental investment. Iain Coucher, the Chair of Ofwat, emphasised that environmental priorities are set by the Environment Agency and Ofwat’s role is to make sure that schemes “are delivered cost effectively and efficiently”, rather than challenging whether they are the right or wrong things to do.²¹
38. Mr Black also noted that RAPID makes sure that regulators are working together as effectively as they can in securing future water supplies, suggesting that there may be benefits to looking at that kind of approach in the wastewater space, while appreciating that there is a different set of issues and a role for local government in that area.²²
39. The Rt Hon Thérèse Coffey MP, Secretary of State for Environment, Food and Rural Affairs, acknowledged that the regulatory set up “is complicated potentially”, but stressed that she thought “it works pretty well”, with different regulators for different purposes. She pointed to the ongoing collaboration between Ofwat and the Environment Agency in their joint investigation into storm overflow discharges as an example of one of the “number of ways” that the two regulators work in partnership, stressing that “it is important to make sure that they work effectively together”.²³
40. **Ofwat and the Environment Agency may have differing remits, but they regulate the same industry. Therefore, effective collaboration is key to ensuring each regulator is able to achieve its individual aims and support the overall goals of the industry, such as reducing water pollution. We welcome recent progress on closer co-operation between the regulators, particularly through the Regulators’ Alliance for Progressing Infrastructure Development (RAPID) in relation to future water supplies. However, there is still a clear lack of effective co-ordination on issues such as Environment Agency outputs not aligning with what Ofwat deems financeable, and ineffective information-sharing.**
41. *Ofwat, the Environment Agency and the Drinking Water Inspectorate should set up RAPID-style structures, including joint working and close partnership with industry, in areas of high priority, including improving water quality, upgrading the wastewater network and reducing water demand.*
42. *It is crucial that Ofwat and the Environment Agency share relevant information effectively and efficiently on matters of joint interest. Ofwat and the Environment Agency should formalise and publish how they plan to share information on water company performance.*

20 [Q 92](#) (Sir James Bevan)

21 [Q 119](#) (Iain Coucher)

22 [Q 124](#) (David Black)

23 [Q 131](#) (Thérèse Coffey MP)

Co-operation across sectors and a National Water Strategy

43. A variety of sectors contribute to the state of the water environment. For example, water pollution is caused by sectors including water, agriculture, housing, and transport. These sectors are overseen by different Government departments or regulatory bodies.
44. Sir James told us that mechanisms to enable a joined-up approach to water pollution already exist, such as the National Framework for Water Resources that the Environment Agency issued in 2020, which set out the action needed across sectors to ensure resilience of supply and prevent environmental damage. However, he felt “that an overall strategic plan led by government with support from everybody else” would support a co-ordinated approach to water.²⁴ Mr Lovell agreed, arguing that “there needs to be a national water strategy” and the Environment Agency, Ofwat, and DEFRA are working together on the issue.²⁵
45. Mr Gosden said he “would always support anything which brings all the different organisations, thoughts and opinions around the water sector together to make sense of the entire picture and provide direction for the industry.” However, these strategies should be reflected in the level of investment permitted by the Price Review.²⁶ Ms Bentley pointed out that RAPID “has an aligned plan” for water, and therefore “is effectively a national water strategy”. She believes what is now needed is political will and for the National Policy Statement for Water Resources Infrastructure, which is drafted, to be finalised.²⁷
46. In January 2023, the Government published its Environmental Improvement Plan 2023, which aims to deliver on the Government’s environmental targets set as part of the 25 Year Environment Plan, including the goal to “achieve clean and plentiful water by improving at least 75% of our waters to be close to their natural state as soon as is practicable”.²⁸
47. The Environmental Improvement Plan sets out a number of existing policies and approaches aimed at meeting this target as well as providing new detail in some areas. The Plan acknowledged that “the current water policy and regulatory framework is complex, with over 15 national plans and strategic documents”, setting out a desire to ensure that the specific purposes for these plans are kept but that “they are brought together in a more coherent way”. The Environmental Improvement Plan said that the policies announced in it are “the first step in a broader water reform programme” and explained that the Government is “developing a suite of new policy interventions designed to transform how we manage the water system in a holistic way, as well as targeted action on each component of the water system.”²⁹

24 Q 99 (Sir James Bevan)

25 Q 99 (Alan Lovell)

26 Q 110 (Lawrence Gosden)

27 Q 110 (Sarah Bentley). The National Policy Statement for Water Resources Infrastructure sets out the need and government’s policies for the development of nationally significant infrastructure projects relevant to water resources in England. Nationally significant infrastructure projects can bypass normal planning processes.

28 Department for Environment, Food and Rural Affairs, *Environmental Improvement Plan 2023*, (31 January 2023): <https://www.gov.uk/government/publications/environmental-improvement-plan> [accessed 31 January 2023]

29 *Ibid.*

48. The Secretary of State said it is worth considering a national water plan that brings together the various sources of funding and policy in the sector, and that “how we pull all that together is under very active consideration.”³⁰
49. **Effectively reducing water pollution and securing future supply will require the unified effort of a range of sectors, government departments, and regulators. Each of these areas has a range of funding sources, bodies and policies that affect the water environment, yet these must be co-ordinated to deliver overall success for the environment. Political will to deliver for the environment will also be necessary.**
50. *The Government should facilitate a co-ordinated approach to water pollution by publishing a National Water Strategy that approaches water policies in a holistic way. The Strategy should set clear expectations in relation to the quality of the water environment and the resilience of water supplies, giving regulators clear benchmarks to work towards. The Strategy should also set out clearly how the Government intends to oversee the regulators’ delivery of these expectations.*

CHAPTER 3: OFWAT

Ofwat's statutory duties

51. Ofwat was established under the Water Industry Act 1991, which stipulates its statutory duties.³¹ These are to:
- Further the consumer objective to protect the interests of consumers, wherever appropriate by promoting effective competition;
 - Secure that water companies properly carry out their statutory functions;
 - Secure that water companies can finance the proper carrying out of their statutory functions;
 - Secure that water supply licensees and sewage licensees properly carry out their licensed activities and statutory functions;
 - Further the resilience objective to secure the long-term resilience of water companies' water supply and wastewater systems; and
 - Secure that they take steps to enable water companies, in the long term, to meet the need for water supplies and wastewater services.³²

Balancing objectives and making trade-offs

52. Ofwat told us that in regulating the sector, it sought to “to achieve a balance between these duties, and avoid regulatory action which advances one duty at the expense of another.” The regulator did not “perceive a need to manage trade-offs in respect of [its] objectives.”³³
53. Witnesses such as Annabelle Ong, Director at Frontier Economics, did not agree. Ms Ong told us that Ofwat's objectives “are to be traded off by design ... there are multiple objectives that are at times difficult to balance.” She noted that sometimes there is a focus on storm overflows, but reducing leakage, reducing supply interruptions, reaching environmental targets, and meeting investment needs all matter. She said that “Going forward, it will be very difficult for Ofwat to balance its statutory objectives.”³⁴
54. IFM Investors felt that Ofwat has historically protected consumers by keeping bills low at the expense of investment in infrastructure, and Waterwise asserted that in recent Price Reviews, “too much weight has been put on short-term bills and not enough on meeting [Ofwat's] resilience duty.”³⁵ Christine McGourty, Chief Executive of Water UK, noted that “by 2025, bills will have been flat or falling for 15 years [in real terms]”, and “Ofwat's focus has been weighted somewhat too much to those short-term interests of current consumers.”³⁶
55. Afonydd Cymru, Angling Trust, the Salmon and Trout Conservation, Guy Linley-Adams, a Solicitor at Salmon and Trout Conservation, and Mark Lloyd, Chief Executive of The Rivers Trust, all held the view that Ofwat

31 [Water Industry Act 1991](#)

32 Ofwat, ‘ Our duties’: <https://www.ofwat.gov.uk/about-us/our-duties/> [accessed 9 January 2023]

33 Written evidence from Ofwat ([TWW0030](#))

34 [Q 9](#) (Annabelle Ong)

35 Written evidence from IFM Investors ([TWW0010](#)) and Waterwise ([TWW0027](#))

36 [Q 53](#) (Christine McGourty)

has prioritised keeping customer bills low at the expense of environmental protections and investment.³⁷ The Angling Trust said:

“Ofwat has duties to protect the interests of customers. Yet while it has often forced a reduction in investment plans put forward by water companies, under the guise of its potential impact on consumer bills, it has failed to fully protect consumers’ interests, by failing to recognise the value consumers place on a clean and healthy environment.”³⁸

56. The Water Act 2014 amended Ofwat’s statutory duties as set out in the Water Industry Act 1991 to include a duty to “further the resilience objective”. This is defined as an objective to:
- “Secure the long-term resilience of water undertakers’ supply systems and sewerage undertakers’ sewerage systems as regards environmental pressures, population growth and changes in consumer behaviour; and
 - Secure that undertakers take steps for the purpose of enabling them to meet, in the long term, the need for the supply of water and the provision of sewerage services to consumers”.³⁹
57. Mr Linley-Adams outlined that when the Water Act 2014 was being passed, many NGOs “fought very hard to have a strong duty towards the environment and towards sustainable development placed upon Ofwat, but what we got was a very unhappy muddle”.⁴⁰ The “muddle” is the resilience objective, which Mr Lloyd said “has been misinterpreted by many to mean financial resilience for companies rather than environmental resilience.”⁴¹
58. Professor Ian Barker, Managing Director of Water Policy International Ltd, said it “would be a brave company that proposed an investment programme that addressed ... long-term issues because of the potential impact on bills.” He believed that in such a scenario, Ofwat would want to “focus on the here and now”. He suggested “companies in some ways have managed [the] trade-offs more than Ofwat has by virtue of what goes into their business plans”.⁴²
59. Emma Clancy, Chief Executive of the Consumer Council for Water, acknowledged that Ofwat has a difficult task in balancing its objectives. She argued that this is not helped by the timeframes of the Price Review process, which requires that years in advance of any kind of execution, the regulator must try and predict the needs of customers and all other factors, including the environment and investment. She felt in the past “the pendulum had perhaps swung too far in favour of companies”, but applauded Ofwat for “swinging it back the other way for recent Price Reviews”.⁴³
60. Professor Catherine Waddams, a member of the Centre for Competition Policy at the University of East Anglia, argued that balancing trade-offs between objectives should sit with the Government or Parliament rather than the regulator. For example, she said water companies will argue for

37 Written evidence from Afonydd Cymru ([TWW0006](#)), the Angling Trust ([TWW0012](#)), Salmon and Trout Conservation ([TWW0002](#)), [Q 16](#) (Mark Lloyd) and [Q 17](#) (Guy Linley-Adams).

38 Written evidence from the Angling Trust ([TWW0012](#))

39 Water Act 2014, [section 22\(3\)](#)

40 [Q 17](#) (Guy Linley-Adams)

41 [Q 16](#) (Mark Lloyd)

42 [Q 9](#) (Prof Ian Barker)

43 [Q 34](#)

better financing, but this would raise bills and could threaten the consumer welfare: “That is a trade-off that I do not think is proper for Ofwat itself to make; that would be better coming from Parliament.”⁴⁴

61. Mr Cox told us he would “reject very strongly any suggestion that Ofwat, under my tenure, had an objective for bills that overrode other objectives. It categorically did not.” Similarly, David Black, Chief Executive of Ofwat, said he did “not think that it is right to characterise Ofwat’s focus as being on low bills”. He pointed to the 2019 Price Review where no schemes were rejected on the grounds of affordability. Mr Black acknowledged that bills have fallen in recent Price Reviews (PRs), but explained this has been due to a fall in allowed returns, and not at the expense of investment.⁴⁵ He said that going forward: “Substantial new investment is required, which may well impact on bills, depending on the other elements of the package.”⁴⁶ Iain Coucher, Chair of Ofwat, emphasised “it is not the case that [Ofwat] have held back investment”.⁴⁷
62. The Secretary of State said she felt Ofwat’s statutory objectives were clear and appropriate, and that the Government “had the opportunity in the Environment Act [2021]” to consider the issue. She argued that there had been changes to the original duties given to Ofwat in the Water Industry Act 1991, such as opening up competition for non-household suppliers. She outlined that using directive Government statements such as the Water Industry National Environment Programme and the Strategic Policy Statement, which sets the Government’s priorities for Ofwat, “is a reasonable way to keep going with [updating Ofwat’s objectives], as opposed to constantly having to wait to change primary legislation all the time”.⁴⁸
63. **It is the view of many in the water sector that Ofwat’s objectives require it to make trade-offs between prioritising consumer bills, investment, and the environment. It is the impression of some stakeholders that Ofwat has historically given more focus to a short-term desire to keep water bills low at the expense of long-term environmental and security of supply considerations.**
64. **Ofwat faces the challenge of balancing the financial needs of customers during a cost-of-living crisis with the urgent need for infrastructure and environmental investment. Given the distributional and intergenerational consequences of many of these decisions, it is crucial that Ofwat is given strong, clear guidance by the Government on how these trade-offs should be made.**

The Government’s Strategic Policy Statement

65. The Government has the opportunity to provide clear guidance on how Ofwat should prioritise its objectives. The Water Industry Act 1991 provides that “The Secretary of State may from time to time publish a statement setting out strategic priorities and objectives for [Ofwat]”, and Ofwat must

44 [Q 44](#)

45 [Q 120](#) (David Black). Mr Black explained that as part of recent Price Reviews, Ofwat limited the returns companies could make on capital investment, causing bills to fall.

46 [Q 120](#) (David Black)

47 [Q 120](#) (Iain Coucher)

48 [Q 134](#) (Thérèse Coffey MP)

carry out its functions in accordance with such a statement.⁴⁹ This is known as the Government’s Strategic Policy Statement (SPS).

66. In its January 2022 report on water quality in rivers, the House of Commons Environmental Audit Committee stated that witnesses had suggested to them that DEFRA’s 2017 SPS had “ducked the hard choices” by describing processes rather than specific outcomes. In its response to DEFRA’s then-draft updated SPS, the Environmental Audit Committee welcomed the protecting and enhancing the environment strategic objective, but expressed concern that the SPS was imprecise in its expectations, with no indication of the specific outcomes expected.⁵⁰
67. In February 2022, DEFRA published its latest SPS. It identified four priorities for the water sector:
- Protect and enhance the environment;
 - Deliver a resilient water sector;
 - Serve and protect customers;
 - Use markets to deliver for customers.
68. Mr Lloyd said that The Rivers Trust welcomed aspects of the 2022 SPS, but there was “a bit too much language about Ofwat enabling and encouraging things to happen rather than requiring them to happen, so it looked a bit gentle.” He said stronger language would be helpful to hold Ofwat to account, as it is far easier to assess if they have required companies to do something as opposed to merely encouraging them to.⁵¹
69. Mr Linley-Adams agreed that the language in the SPS is too weak:
- “We need the Secretary of State to make it absolutely clear to Ofwat that it is not just about encouraging or cajoling the water companies to do what they are required to do by law; it is about actually requiring them to do it—directing Ofwat to use its enforcement powers.”
70. He said that Salmon and Trout Conservation, together with the Angling Trust, had released a shadow SPS with stronger language.⁵² When asked if stronger language would compromise Ofwat’s independence, Mr Linley-Adams responded that outcomes—a better water environment—are what matters, and “If Ofwat needs to be told firmly what to do and that compromises its independence a little bit, then so be it.”⁵³ Mr Lloyd agreed.⁵⁴
71. Ms Bentley, Annabelle Ong, Director at Frontier Economics, Prof Barker, Water UK, Blueprint for Water, Waterwise, and Affinity Water, all told us that the SPS missed the opportunity for the Government to advise Ofwat as to which objectives it should prioritise.⁵⁵ For example, Affinity Water said:

49 Water Industry Act 1991, [section 2A \(1\)](#)

50 Environmental Audit Committee, [Water quality in rivers](#) (Fourth Report, Session 2021–22, HC 74)

51 [Q 22](#) (Mark Lloyd)

52 [Q 22](#) (Guy Linley-Adams)

53 [Q 23](#) (Guy Linley-Adams)

54 [Q 23](#) (Mark Lloyd)

55 [Q 105](#) (Sarah Bentley), [Q 11](#) (Annabelle Ong), [Q 11](#) (Prof Ian Barker), and written evidence from Water UK ([TWW0021](#)), Blueprint for Water ([TWW0032](#)), Waterwise ([TWW0027](#)), and Affinity Water ([TWW0013](#))

“The priorities as laid out [in the SPS] are not organised in any hierarchy and do not provide any indication or guidance in terms of relative importance. The implicit assumption is that all are equal, none are contradictory and all are achievable at the same time ... We consider that there is scope for more specific direction to be given on how Ofwat should prioritise these objectives and how the trade-offs should be considered ... Without clear direction on relative priority, there is a risk that the balance that is struck does not aligned with Government objectives.”⁵⁶

72. Ms Bentley and Blueprint for Water told us that a lack of clear priority-setting in the SPS differs to similar documents issued to other regulators.⁵⁷ Ms Bentley highlighted:

“Other regulators, such as Ofcom, [get] set very clear direction when it comes to the trade-offs and the balance of investment versus the bill profile ... Ofcom’s version of the SPS makes it very clear that the Government state that ‘promoting investment should be prioritised over interventions to further reduce retail prices in the near term’ ... That sets quite a clear steer in the Ofcom example, which I think Ofwat would benefit from.”⁵⁸

73. Ms Ong said an implication of a lack of prioritisation in the SPS is that it is difficult to measure if Ofwat is meeting the priorities set: “It will be very hard to say that [Ofwat] did not meet the SPS, given that the SPS does not prioritise.”⁵⁹
74. Several witnesses told us that there needed to be further scrutiny of Ofwat’s work to meet the objectives set in the SPS. Affinity Water noted “there is no mechanism to check or measure [Ofwat’s] delivery of [the SPS’] expectations.”⁶⁰ The Independent Water Networks Ltd. felt there was more scope “to regularly monitor the performance of the regulator in facilitating [the SPS’ objectives]”⁶¹. Lawrence Slade, Chief Executive of the Global Infrastructure Investor Association, commented that “there does not appear ... to be a really solid, formal way of understanding the regulator’s performance against [the SPS]”. He suggested such scrutiny could be conducted by a parliamentary committee⁶². This suggestion was also made by IFM investors and Water UK.⁶³ In its January 2022 report on *Water quality in rivers*, the House of Commons Environmental Audit Committee announced its intention to invite Ofwat to appear “routinely” to discuss its progress against the objectives of the new SPS.⁶⁴
75. Mr Cox said that Ofwat has the most directive government intervention of any of the economic regulators through the SPS, arguing that it provides very strong guidance. While the SPS does not explicitly state how to make trade-offs, it gives guidance. He felt it would “be wholly inappropriate to go any further” than the Government does in the SPS, due to the benefits of

56 Written evidence from Affinity Water ([TWW0013](#))

57 [Q 105](#) (Sarah Bentley) and written evidence from Blueprint for Water ([TWW0032](#))

58 [Q 105](#) (Sarah Bentley)

59 [Q 11](#) (Annabelle Ong)

60 Written evidence from Affinity Water ([TWW0013](#))

61 Written evidence from The Independent Water Networks Ltd. ([TWW0029](#))

62 [Q 67](#)

63 Written evidence from IFM Investors ([TWW0010](#)) and Water UK ([TWW0021](#))

64 Environmental Audit Committee, *Water quality in rivers* (Fourth Report, Session 2021–22, HC 74)

the independent regulation model, which attracts investors. Mr Cox believed it was the role of those heading the regulator to make decisions about trade-offs.⁶⁵ The Consumer Council for Water similarly argued “a more detailed SPS would run the risk of undermining regulatory independence.”⁶⁶

76. Mr Black said there is an argument about balance regarding the SPS. Ofwat is looking for the Government to set the outcomes it wants to see from the sector, which it is starting to do in the form of its 25 Year Environment Plan, which sets environmental goals, and Storm Overflows Discharge Reduction Plan, which sets targets on storm overflow use. The key is having clarity on the outcomes that are expected from companies and then having greater flexibility in the system to get the best value means of delivery. He felt that:

“The role of the Government in the process is more intrusive than it looks from the outside, if you look just at the SPS and Ofwat’s role. Every environmental investment scheme that was put forward at PR19 was designed and developed by companies and the Environment Agency ... The sign-off process is a matter for the Environment Agency, but there is the ability for the Government to sign that off, if they choose.”⁶⁷

77. Mr Coucher said that in the future, there will be significantly more investment in the environment, and “That may well cause the Government to get involved in decision-making or balancing between investment and bill payers.”⁶⁸

78. The Secretary of State said that the SPS allows the Government to show Ofwat “what we want to see”. She felt the 2022 SPS “is very good” and noted it had “a much stronger emphasis on the environment”.⁶⁹ On managing the trade-off between customer bills and investment, the Secretary of State said “Ofwat cannot stop the investment into things that the Government has directed. That is our influence in having involvement in the bill-setting process”.⁷⁰

79. **Ofwat needs clear guidance from the Government on how it should balance and prioritise its objectives. The Government should do this through its Strategic Policy Statement (SPS). However, the 2022 SPS failed to give a sense of prioritisation, particularly in relation to the balance between the affordability of bills and infrastructure and environmental investment. We recognise the concern that more directive Statements could impact Ofwat’s independence, but it is critical that elected politicians take controversial decisions which will have financial and environmental consequences for many generations, rather than passing that responsibility to regulators. The Government has not yet shown the necessary political will to make these decisions on the most important issues facing the sector.**

80. **Like the House of Commons Environmental Audit Committee, we welcome the greater emphasis the 2022 SPS placed on protecting and enhancing the environment. However, some of the outcomes are vague and the language tends to call for Ofwat to “enable” and**

65 [Q 77](#)

66 Written evidence from the Consumer Council for Water ([TWW0019](#))

67 [Q 119](#) (David Black)

68 [Q 119](#) (Iain Coucher)

69 [Q 131](#) (Thérèse Coffey MP)

70 [Q 135](#) (Thérèse Coffey MP)

“encourage” actions from water companies and the water industry rather than require these actions.

81. **Ofwat’s performance against meeting the objectives of the SPS should also be subject to greater Parliamentary scrutiny. We welcome the Environmental Audit Committee’s intention to carry out this scrutiny routinely.**
82. *The Government should update the SPS to strengthen the language contained within it to ensure that Ofwat requires companies to meet SPS priorities. It should also provide a clear steer to Ofwat on how to balance its priorities, particularly in relation to the need to ensure higher levels of infrastructure investment, and these lessons should be taken on board in future Statements.*

CHAPTER 4: PRICE REVIEW AND OUTCOMES-BASED REGULATION

Price Review

83. Ofwat notes that “most people receive their water services from a licensed monopoly company”. As competition is limited, there is a risk that water companies will not deliver the services their customers want or that they could charge higher prices to increase their profits.⁷¹
84. As the economic regulator, Ofwat is responsible for controlling the prices companies can charge their customers. Ofwat said it sets the price by balancing the duty to protect consumers’ interests with the need to ensure the sector is able to finance the delivery of water and sewerage services and meet its legal obligations, including its environmental and social duties.⁷²
85. Price limits are reviewed every five years in Price Reviews. Ofwat is currently working on the Price Review for 2024 (PR24). This will set wholesale price controls for water and sewerage companies for 2025–2030, which in turn will set the price paid by consumers. Ofwat published its draft methodology for PR24 in July 2022⁷³ and its final methodology in December 2022.⁷⁴ The regulator will set final price limits in December 2024.
86. During the Price Review process, companies put forward their business plans for the next period to Ofwat, which then makes determinations of the investments, targets and returns that the companies can make and challenges them on whether their plans can be delivered more effectively and at least cost. These determinations can be appealed by companies to the Competition and Markets Authority. In its methodology for PR24, Ofwat has announced that due to the long-term challenges facing the sector, it will ask companies to set their five-year business plans in the context of a long-term delivery strategy, which “will see the water sector take steps to embed an adaptive approach to planning for the future”.⁷⁵
87. At the 2019 Price Review (PR19), Ofwat set water companies performance targets for the period 2020–25. These performance targets cover a wide range of elements of water company performance, including pollution incidents, leakages, customer satisfaction, water consumption, unplanned outages and mains repairs, among others.⁷⁶
88. Most performance commitments have rewards and penalties associated with them. If a company performs better than the performance commitment level, it may get a financial reward, whereas if a company performs below the

71 Ofwat, ‘Price reviews’: <https://www.ofwat.gov.uk/regulated-companies/price-review/> [accessed 22 December 2022]

72 *Ibid.*

73 Ofwat, *Creating tomorrow, together: consulting on our methodology for PR24* (July 2022): <https://www.ofwat.gov.uk/consultation/creating-tomorrow-together-consulting-on-our-methodology-for-pr24/> [accessed 10 January 2023]

74 Ofwat, *Creating tomorrow together: our final methodology for PR24* (December 2022): <https://www.ofwat.gov.uk/publication/creating-tomorrow-together-our-final-methodology-for-pr24/> [accessed 10 January 2023]

75 Ofwat, ‘PR24 long-term delivery strategies’: <https://www.ofwat.gov.uk/regulated-companies/price-review/2024-price-review/pr24-long-term-delivery-strategies/> [accessed 23 January 2023]

76 Ofwat, *Water Company Performance Report 2021–22* (December 2022): <https://www.ofwat.gov.uk/publication/water-company-performance-report-2021-22/> [accessed 23 January 2023]

level it may pay a financial penalty.⁷⁷ For instance, Ofwat required Thames Water to return £51 million to its customers while Southern Water was ordered to return £28.3 million for missing targets on water treatment works compliance, pollution incidents and internal sewer flooding. Yet Severn Trent Water was allowed to make an extra £101.8 million from customers after exceeding its targets.⁷⁸

89. In its February 2022 Strategic Policy Statement for Ofwat, the Government outlined that it wants Ofwat to take a “long-term approach” to investment in water infrastructure. It added that a system that meets the “enduring interests of consumers” does not “simply mean lower prices in the short-term at the expense of future generations”, emphasising that Ofwat should promote efficient investment that delivers “value for money for customers, society and the environment over the long-term”.⁷⁹
90. Christine McGourty, Chief Executive of Water UK, said that the draft methodology for PR24 looks “tough” and “stretching” and welcomed the support for nature-based schemes and an overall focus on the long term. Stuart Colville, Director of Policy at Water UK, said that the final business plans depend on more than just the methodology, arguing that there is a need for decisions on long-term investment and outcomes to maintain sufficient momentum.⁸⁰ Lawrence Slade, Chief Executive Officer of the Global Infrastructure Investor Association, emphasised that while the draft methodology for PR24 is “a definite move in the right direction”, there is still a need to get “more of a long-term view”, allow more innovative spending and have “a more flexible approach”.⁸¹
91. Sarah Bentley, Chief Executive of Thames Water, said that the introduction of long term delivery strategies to the next Price Review is a “very welcome move” as Thames Water wants to look more at the long term, noting that Thames Tideway is an example of a longer-term investment but that this was undertaken outside the Price Review process.⁸² She suggested that longer-term programmes can help when investing in replacing water mains or large sewage treatment works, arguing that there is a need to turn the Price Review settlement into “some clear direction and certainty” for improvement initiatives that last beyond a five-year period.⁸³
92. Professor Catherine Waddams, a member of the Centre for Competition Policy at the University of East Anglia, said that water companies have been “gaming” the Price Review process by putting their argument across in a

77 Ofwat, ‘Price reviews’: <https://www.ofwat.gov.uk/regulated-companies/price-review/> [accessed 22 December 2022]

78 Ofwat, Press Release: *Thames Water and Southern Water to return almost £80m to customers for under performance*, (November 2022): <https://www.ofwat.gov.uk/in-period-2021-22-final-determinations-announced/> [accessed 22 December 2022]

79 Department for Environment Food and Rural Affairs, *February 2022: The government’s strategic priorities for Ofwat (March 2022)*: <https://www.gov.uk/government/publications/strategic-policy-statement-to-ofwat-incorporating-social-and-environmental-guidance/february-2022-the-governments-strategic-priorities-for-ofwat> [accessed 10 January 2023]

80 [Q 57](#) (Stuart Colville)

81 [Q 69](#) (Lawrence Slade)

82 Thames Tideway is an ongoing project to build a super sewer in London to prevent the spill of polluted water into the Thames. It was opened to external bidders outside the Price Review process, so that although it sits in Thames Water’s geographical remit, Thames Water is not involved in its construction and financing.

83 [Q 105](#) (Sarah Bentley)

particular way in public to get the best possible revenue.⁸⁴ She argued in her written evidence with Professor Michael Harker that “companies may promote their own case for investment by depicting Ofwat as preventing them from being able to fulfil their roles, where the disagreement may rather be about the least cost way of doing so”.⁸⁵ Prof Waddams said that the regulator will always be as hard as it feels it can, but looking at the history of Price Reviews, “it turns out not to have been as hard as it thought”.⁸⁶

93. Jonson Cox, former Chair of Ofwat, said that he “cannot think of a single proposal” put forward at the last two Price Reviews where a “good, necessary investment scheme” was rejected by Ofwat, arguing that Ofwat often says that things could be done more efficiently, but that the only times where investment has been turned down are when the company has done “a sloppy and poor job of justifying it”.⁸⁷ He disagreed with the suggestion that the Price Review does not focus on the long term but suggested that one of the lessons of previous attempts at long-term planning was that companies cannot accurately assess needs over 25 years, which is why Ofwat wants companies to have an “adaptive plan” in their long term delivery strategy.⁸⁸
94. Alan Lovell, Chair of the Environment Agency, said that PR24 will be critical to enable investment by water companies to ensure future water supply. He argued that there is a “general recognition” that more investment is required and agreed with the suggestion that there has been too much of a focus on low prices that has restricted investment. He said that five-year periods are a challenge, as long-term projects would ideally have a longer timescale.⁸⁹
95. David Black, Chief Executive of Ofwat, emphasised that in recent Price Reviews, there has not been a need to constrain investment plans for affordability reasons, but it may be that looking ahead, significant increases in investment will be required, especially following the work of the Storm Overflows Taskforce.⁹⁰ In relation to long term delivery strategies, Mr Black explained that Ofwat wants to see companies setting out the plan for their area while avoiding “locking companies into a straitjacket about future decisions”, noting remarkable changes even within the current Price Review period.⁹¹
96. Iain Coucher, Chair of Ofwat, said that while Ofwat can monitor operating and maintenance performance very well over five-year periods, some large-scale investment schemes in new reservoirs, water management schemes and drainage plans will take more than five years and cover multiple Price Review periods. He said that the regulator needs to be able to fund long-term investments with certainty and stability in the long term, but this will need a change to how water companies and regulators operate.⁹²
97. Mr Black pointed out that at PR19, Ofwat “pushed companies sufficiently hard” that four of them appealed the determination, which had never

84 [Q 50](#) (Prof Catherine Waddams)

85 Written evidence from Professor Michael Harker and Professor Catherine Waddams, University of East Anglia ([TWW0007](#))

86 [Q 50](#) (Prof Catherine Waddams)

87 [Q 74](#)

88 [Q 75](#)

89 [QQ 98–99](#) (Alan Lovell)

90 [Q 120](#) (David Black)

91 [Q 121](#) (David Black)

92 [Q 121](#) (Iain Coucher)

happened before. He argued he has the ambition to push the sector further as he thinks it is capable of doing “much more”. However, he noted that one challenge Ofwat faces is getting companies to take action on the commitments they have already agreed, as in the most recent Price Review, some progress on infrastructure has been “slower than we would have liked”.⁹³

98. The Secretary of State set out that the Government expects “a significant amount of money to come through in the Price Review”, noting that the last Price Review led to “about £51 billion of capital investment”.⁹⁴
99. **We welcome Ofwat’s recognition of the need for a significant increase in investment at the next Price Review, given the challenges facing the sector. The Price Review process is appropriate for iterative improvements to underlying assets but investment in environmental improvements and increasing water supply has remained low, potentially due to the regulator’s focus on efficiency and the limited time horizon of the Price Review process. Given the likely shift in the sector towards large, long-term strategic infrastructure projects that are required to ensure future water supplies and resolve environmental issues, more of the sector’s investment will need to take place outside of the Price Review process in future.**

Competition

100. Traditionally, water and sewerage infrastructure has been built by the incumbent regional company. However, the Thames Tideway tunnel, a 25-kilometre sewer being built under the River Thames, has been financed and constructed by a third party company independent of Thames Water.
101. Mr Cox explained that Thames Water had the right to build waste infrastructure in the region but Ofwat was not satisfied with its provision, so it created a separate scheme to allow others to bid for the project separately. He acknowledged that there were “some very difficult battles” with Thames Water over it and although the project attracted fewer consortia than had been hoped for, the project’s cost of capital for construction was “half the then level for the water industry” and lower than anyone thought would be managed, reducing costs from around £80 per customer per year to around £20 per customer per year.⁹⁵
102. The project has taken a long time to be completed. The initial Thames Tideway Strategic Study Group was set up in 2000, but it took until 2013 for Thames Water to announce the shortlists of consortia bidding for the construction work. The third party infrastructure provider, Bazalgette Tunnel Limited, was given a regulatory licence in August 2015.⁹⁶ Tunnelling began for the project in 2018 and all works are set to be completed in 2025.⁹⁷
103. The Government introduced the Water Industry (Specified Infrastructure Projects) (English Undertakers) Regulations 2013 to enable the project to

93 [Q 121](#) (David Black)

94 [Q 131](#) (Thérèse Coffey MP)

95 [Q 83](#)

96 National Audit Office, *Review of the Thames Tideway Tunnel* (March 2017): <https://www.nao.org.uk/wp-content/uploads/2017/03/Review-of-the-Thames-Tideway-Tunnel.pdf> [accessed 7 February 2023]

97 Tideway, ‘Super Sewer Timeline’: <https://www.tideway.london/tideway-timeline> [accessed 7 February 2023]

be delivered in this way.⁹⁸ Ofwat set up a Specified Infrastructure Projects Regulations (SIPR) regime, putting the project out to competitive tender for a third party to design, build and finance, aiming to deliver “better value for customers and provide a wide range of benefits”.⁹⁹

104. Under this model, a special purpose vehicle (SPV) independent of the area’s water company is established to finance, build and operate the infrastructure project using project finance. The debt and equity used to finance the project is paid back from the cashflow generated by the project in the long term. Ownership of the SPV can be opened up to a range of different investors.¹⁰⁰
105. In January 2022, the then-Secretary of State for Business, Energy and Industrial Strategy, The Rt Hon Kwasi Kwarteng MP, asked Ofwat to conduct a high-level stocktake to identify opportunities and barriers to unlocking more competition in strategic investment in the water sector.¹⁰¹
106. Ofwat published its report in July 2022, finding benefits to competition including lower costs, increased speed and effectiveness, and wider benefits such as environmental improvements and innovation. However, Ofwat also outlined barriers to competition, including legislative restrictions to using its Specified Infrastructure Projects Regulations (SIPR) regime more widely and an inability for water companies to automatically apply for a development consent order under the Planning Act 2008.¹⁰²
107. The Water Industry (Specified Infrastructure Projects) (English Undertakers) Regulations 2013 provide that the SIPR regime can only be used where the project is “of a size or complexity that threatens the incumbent undertaker’s ability to provide services for its customers”.¹⁰³ Ofwat argued that this is a “high threshold to pass and prevents its use”, even where this would provide better value for money for customers, recommending that this test is removed from eligibility considerations.¹⁰⁴
108. Ofwat also raised concerns about the ability of large water infrastructure projects to gain planning permission. The Planning Act 2008 facilitates delivery by providing a streamlined planning process for projects that are deemed ‘nationally significant infrastructure projects’ (NSIPs). This allows project sponsors to apply directly to the Planning Inspectorate for planning permission and other statutory powers and consents through a Development

98 The Water Industry (Specified Infrastructure Projects) (English Undertakers) Regulations 2013 (SI 2013/1583)

99 Ofwat, *Competition in strategic investment: a high level stocktake* (July 2022) : <https://www.ofwat.gov.uk/publication/competition-in-strategic-investment-a-high-level-stocktake/> [accessed 22 December 2022]

100 Ofwat, *Pricing principles for strategic water resource solutions* (March 2022): https://www.ofwat.gov.uk/wp-content/uploads/2022/03/Pricing-principles-for-strategic-water-resource-solutions_Redacted.pdf [accessed 7 February 2023]

101 Department for Business, Energy & Industrial Strategy, ‘Strategic priorities and cross-sectoral opportunities for the utilities sectors: open letter to regulators’ (January 2022) : <https://www.gov.uk/government/speeches/strategic-priorities-and-cross-sectoral-opportunities-for-the-utilities-sectors-open-letter-to-regulators> [accessed 22 December 2022]

102 Ofwat, *Competition in strategic investment: a high level stocktake* (July 2022) : <https://www.ofwat.gov.uk/publication/competition-in-strategic-investment-a-high-level-stocktake/> [accessed 22 December 2022]

103 The Water Industry (Specified Infrastructure Projects) (English Undertakers) Regulations 2013 (SI 2013/1583), section 4

104 Ofwat, *Competition in strategic investment: a high level stocktake* (July 2022) : <https://www.ofwat.gov.uk/publication/competition-in-strategic-investment-a-high-level-stocktake/> [accessed 22 December 2022]

Consent Order (DCO) process. The Government publishes National Policy Statements (NPSs) to establish the need for NSIPs and the policies for their development, but currently there is no designated NPS for Water Resources Infrastructure, which “creates some uncertainty around the DCO process”.¹⁰⁵

109. The Government consulted on a draft NPS for Water Resources Infrastructure in 2018¹⁰⁶ but a finalised NPS is yet to be published. In its Environmental Improvement Plan, published in January 2023, the Government confirmed DEFRA will “Designate the National Policy Statement for Water Resources Infrastructure, to improve planning decisions and better enable new water supply infrastructure delivery.”¹⁰⁷
110. Ofwat recommended that designating the NPS should “be a priority for the Government” and called for the definition of NSIPs to be updated to cover some strategic water resource projects that would currently be excluded, including those delivered through special purpose vehicles or other competitively appointed providers.¹⁰⁸
111. Mr Slade said that there are almost certainly areas within the sector where greater competition can be brought in, with Thames Tideway often quoted as an innovative way of dealing with a significant piece of infrastructure that needed funding. He suggested that the issue is ensuring that the projects being put out to competitive tender are of sufficient scale to make it worth the time and money that goes into preparing and managing bids and bringing consortia together.¹⁰⁹
112. Mr Cox argued the project is a “fantastic success” and shows what can be done when the responsibility for completing significant infrastructure projects is taken away from water companies, allowing a separate focus on them. He explained that at the last Price Review, Ofwat asked companies to justify why any investments over a certain size should not be carried out externally. He suggested that the model lends itself to building a passive asset whose operation can be taken on by the incumbent company, as it needs to be integrated into their operations, and he is “confident” that there will be more opportunities for this.¹¹⁰
113. Ms Bentley agreed that Thames Tideway is a good example of delivering a large-scale infrastructure programme effectively, stressing that Thames Water is fully supportive of the increased use of competition. She argued that competition is attractive as it is done on a longer timeframe and spreads costs over the life of the asset rather than over a five-year cycle, suggesting that there is an opportunity for this approach to be the way forward for large infrastructure projects that improve water security. She suggested that

105 *Ibid.*

106 Department for Environment, Food and Rural Affairs, ‘Consultation on the draft National Policy Statement for Water Resources Infrastructure’ (29 November 2018): <https://consult.defra.gov.uk/water/draft-national-policy-statement/> [accessed 26 January 2023]

107 Department for Environment, Food and Rural Affairs, *Environmental Improvement Plan 2023* (31 January 2023): <https://www.gov.uk/government/publications/environmental-improvement-plan> [accessed 31 January 2023]

108 Ofwat, *Competition in strategic investment: a high level stocktake* (July 2022) : <https://www.ofwat.gov.uk/publication/competition-in-strategic-investment-a-high-level-stocktake/> [accessed 22 December 2022]

109 [Q 70](#)

110 [Q 83](#)

it makes sense to use competition for reservoirs and other large programmes that can be easily identified and separated from the rest of the network.¹¹¹

114. Ms Bentley said that other large, long-term investment programmes, such as replacing the Victorian clean water network, are a little harder to compete on as they are live systems and are integrated with the operating controls of the water company, making it harder for a third party to provide those assets. She argued that there are areas in more rural or semi-rural landscapes where this may be possible, but that the intense integration of London could make it difficult. She said that some areas of Thames Water’s plans could be provided in this way, particularly the provision of sustainable urban drainage systems which involve “spongifying” areas to help absorb surface water.¹¹²
115. Ms Bentley said that the regulations introduced to enable the Thames Tideway scheme were deliberately left flexible to allow other projects to use the same route. She supported Ofwat’s recommendation for changes that would allow “wider use” of the SIPR model and emphasised that putting in place a National Policy Statement would “help ensure projects are delivered”.¹¹³
116. Asked whether strategic infrastructure should run on a timeline outside the Price Review process, Mr Black said that this “may well be the approach”. He explained that at the last Price Review, Ofwat set a ten-year price control for the new Havant Thicket reservoir and put in place the Direct Procurement for Customers (DPC) process, which set a 25-year contract for the building of a new £1 billion aqueduct from the Lake District to Manchester. He emphasised that the future will see a significant step up into major infrastructure projects, requiring new skills and capacity to manage them within companies and the regulator.¹¹⁴
117. Mr Black said that Ofwat has options to bring about competition but explained that one of its requests to the Government is for it to “free up” the special purpose vehicle model used to take Thames Tideway forward under the Specified Infrastructure Project Regulations so that it can be used more widely. He explained that Ofwat thinks setting up special purpose vehicles is “the right way to go”, as this provides a licence that can be applied to the new investment, allowing Ofwat to intervene more effectively than in the DPC model.¹¹⁵
118. Mr Black stressed that if one looks at Thames Water and the challenges it is currently facing, it would be reasonable to suppose that if the Thames Tideway project had been taken forward by Thames Water, it would have been “less effective and successful”. However, he emphasised that as with Thames Tideway, there will still be interfaces with existing water companies and it is important that they work well. Mr Coucher said that Ofwat would like to see some bigger schemes taken out of the Price Control mechanism, such as the proposed Abingdon reservoir and similar projects, and delivered through different mechanisms, enabling water companies to focus on doing the basics well.¹¹⁶

111 [QQ 105, 111](#) (Sarah Bentley)

112 [Q 111](#) (Sarah Bentley)

113 [QQ 105, 110](#) (Sarah Bentley)

114 [Q 121](#) (David Black)

115 *Ibid.*

116 [Q 121](#) (David Black, Iain Coucher)

119. The Secretary of State pointed to the Direct Procurement for Customers (DPC) as an example of the ways in which Ofwat can “make sure that appropriate investment can go ahead but consumer bills are not overwhelmed”.¹¹⁷ She explained that the Government is “having discussions, recognising the scale of capital that needs to be invested in this industry more broadly to see the benefits of what happened with the [SIPR] model, which has significantly reduced the cost of financing”.¹¹⁸
120. The Secretary of State praised the Thames Tideway project for reducing costs and argued that it “shows that the competition works in that regard”. Davide Minotti, Deputy Director for Water Services at the Department for Environment, Food and Rural Affairs, said that the National Policy Statement “will specify” a number of strategically important water infrastructure projects, including through the Direct Procurement for Customers route. The Secretary of State said that she is “very open” to amending the designation process for projects to go through the SIPR regime.¹¹⁹
121. **Strategic, nationally significant infrastructure projects should be delivered outside of the Price Review process. The special purpose vehicle approach used for the Thames Tideway project provides a useful alternative model for funding such projects, reducing capital costs and spreading them over a longer timeframe than the five-year Price Review. Ofwat’s Direct Procurement for Customers model provides an opportunity for larger projects to be carried across multiple Price Review periods and is a useful outlet, but the expansion of the Thames Tideway model is more desirable as this allows Ofwat to intervene more effectively through the licence that can be applied to the new investment.**
122. *The Government should consider legislating to remove the scale and complexity test from the Water Industry Act 1991 and the Specified Infrastructure Project Regulations, ensuring that special purpose vehicles can be used much more frequently to build large water infrastructure projects.*
123. *The Government should designate the final National Policy Statement for Water Resources Infrastructure to ensure strategically significant water infrastructure projects are designated as nationally significant infrastructure projects and can progress through the planning process in a timely manner. The definition of nationally significant infrastructure projects should be amended to ensure strategic water resources schemes are not excluded, particularly those delivered through competitively appointed providers.*

Social tariffs

124. Ms Clancy explained that the water sector faces many serious and immediate challenges, such as climate change and changing expectations around the environment, all of which will cause upward pressure on bills. However, she noted that 1.5 million people are currently struggling to pay their water bill at today’s rate, which is why the Consumer Council for Water is campaigning

117 [Q 131](#) (Thérèse Coffey MP)

118 [Q 132](#) (Thérèse Coffey MP)

119 [Q 137](#) (Thérèse Coffey MP)

for the introduction of a water affordability scheme to protect those who need help at the same time as increasing investment.¹²⁰

125. Ms Clancy said that at the moment there is a “postcode lottery” of support with water bills. Two families in exactly the same situation “but on different sides of the same street” can receive different help depending on their water company, with some receiving a 90 per cent reduction on their bill while others get no help at all. She argued that this is why consistent support is important, suggesting that funding from a central pot for such a scheme would mean that the burden is spread evenly and does not fall disproportionately on areas with the highest levels of deprivation. She said that many customers are not even aware of what water company they belong to or are looked after, which layered with different support schemes on top poses a significant challenge for debt advice agencies to provide help.¹²¹
126. Ms Clancy emphasised that the introduction of a water affordability scheme or single social tariff would need legislative change, while noting that Ofwat does have a role in terms of affordability more generally. She said that the idea has received “really positive support” from the sector, the UK Government and the Welsh Government, with working groups looking at the viability and practicalities of the scheme. She urged Ofwat to signal the need for such a scheme in relation to the next Price Review, subject to the necessary legislation being in place.¹²²
127. Prof Barker explained that every company has a social tariff but it is called different things by different companies and is calculated differently, with 75 per cent of customers having no idea if water companies will offer support with bills. He said that proposals for a single social tariff could go “a long way” to addressing concerns about bill increases but emphasised that providing a national tariff could lead some customers in some areas to be worse off, calling for a no-detriment clause to be included in any such scheme.¹²³ Other witnesses argued in favour of retaining some of the benefits of local, company-led schemes, while agreeing on the need for a baseline level of support.¹²⁴
128. Ms Ong argued that there are good arguments in principle for a single social tariff, including removing the postcode lottery and increasing the support available. However, she emphasised that while it would address some issues, it would not be a panacea and would not resolve the conflict between customer bills and investment needs.¹²⁵
129. Mr Perry said that Dŵr Cymru Welsh Water already provides support for customers receiving means-tested benefits or with medical conditions, but that an emerging group needs help which can broadly be categorised as the working poor. He said that Welsh Water will be trialling the idea of supporting those people who have negative budgets and would turn up to a food bank by putting them onto a reduced tariff in January 2023.¹²⁶

120 [Q 32](#)

121 [Q 33](#)

122 *Ibid.*

123 [Q 13](#) (Prof Ian Barker)

124 [Q 51](#) (Prof Catherine Waddams) and [Q 58](#) (Christine McGourty)

125 [Q 13](#) (Annabelle Ong)

126 [Q 105](#) (Peter Perry)

130. Mr Gosden explained that Southern Water offers a social tariff which is standardised at about a 45 per cent reduction in bills but can range between 20 per cent and 90 per cent. He welcomed proposals for a single social tariff but emphasised the need to put in place the right entry mechanisms to ensure people are supported.
131. Ms Bentley said that Thames Water is very supportive of the single social tariff, arguing that it has a number of features that could really help to make a difference. She emphasised that it would require active sharing of data between water companies, HM Revenue and Customs and the Department for Work and Pensions to ensure support is going to those who need it most.¹²⁷
132. Mr Cox said that he can see why there is a desire for a more common system but expressed caution as to whether this would be a good thing, arguing that it could disrupt innovation by companies who are doing what is right for their region, which can sometimes provide a model for others to emulate but which might not happen with a standard, national scheme. He also argued that there may be a limit to which customers not covered by social tariffs are willing to subsidise other customers.¹²⁸
133. Mr Black said that Ofwat’s research suggests that customers are facing a very tough time, even prior to the impacts of the most recent cost of living increases, with around 50 per cent of customers struggling to pay their bills. He said that while all companies have social tariffs, Ofwat thinks more can be done in this space and he has written to companies asking them to think about how they can provide further assistance.¹²⁹
134. Mr Black welcomed that some companies had put shareholder funding into social tariffs but accepted that they are usually funded by cross-subsidy between customers, suggesting that the Government has a key role to play in setting guidance on the amount of cross-subsidy available for social tariffs. He argued that there would be “significant gains” from standardisation across companies, including in terms of greater awareness of the assistance. He explained his understanding that the Government intends to have a single social tariff from 2025, and that if this was the case, Ofwat will implement it as part of the next Price Review.¹³⁰
135. In January 2023, the Consumer Council for Water provided supplementary evidence that “a change of direction from the current Secretary of State has ended the prospect of a new scheme funded through a central pot, which could have lifted up to two million households out of poverty”. The Council said that the decision means “customers could face the double whammy of unaffordable bills and an environment starved of vital investment”, and stressed that helping people struggling to pay their water bill “should be a public policy matter and not be in the gift of private water companies”.¹³¹
136. The Secretary of State said that she is “more minded not to have one tariff for the entire country but to try to get consistency, water company by water company”. She expressed her view that due to different water stresses in different parts of the country, “a more localised approach will... almost

127 [Q 105](#) (Sarah Bentley)

128 [Q 91](#)

129 [Q 120](#) (David Black)

130 *Ibid.*

131 Supplementary written evidence from the Consumer Council for Water, ([TWW0036](#))

certainly have better outcomes”. She emphasised that she is “seeking a more consistent approach” across the country in relation to how support is provided, particularly in relation to eligibility.¹³²

137. **It is likely bills will have to increase to pay for some of the necessary investment in water infrastructure. It is therefore essential that appropriate support is given to those customers who need it. Current support schemes vary between water companies with no common baseline. This amounts to a postcode lottery for consumers in need.**
138. *The Government should legislate to introduce a single social tariff in time for its inclusion in the next Price Review. This should provide a baseline of support for customers regardless of who supplies their water. As this would require some customers to subsidise other customers, the Government should take decisions on the level of support having consulted with regulators, companies and consumer groups.*
139. *The single social tariff should include a no-detriment clause to ensure that no customer is worse off as a result of the introduction of the new arrangements. Water companies should continue to offer additional support where customers are struggling to pay their bills even with the single social tariff in place.*

Outcomes-based regulation

140. In July 2021, DEFRA, Ofwat and the Environment Agency published a review of the Water Industry National Environment Programme (WINEP), an investment programme through which the Environment Agency specifies works required by water companies to meet environmental goals. The review proposed reforms to move towards an outcomes-based approach.¹³³
141. An outcomes-based approach to regulation is one which stipulates a final outcome but does not prescribe how the outcome is reached. For example, if the outcome were to reduce storm overflow use 50 per cent by 2030, companies would have scope to reach this target in whatever way they see fit. This differs to output-based regulation, which prescribes the steps that must be taken to reach an outcome.
142. Annabelle Ong, Director at Frontier Economics, told us that outcomes-based environmental regulation was key to improving water sector regulation. She explained that as part of the current WINEP, a lot of water companies are given “hundreds of very specific output-based things they have to do, such as improve their discharge at a treatment works. It is more or less prescribed that there is a traditional solution available.” She argued that if the WINEP instead proposed outcomes and allowed companies to look at a wider range of solutions, this would allow more innovative solutions that could have “lower capital cost, less carbon cost and potentially more biodiversity”. This can involve, for example, nature- and catchment-based solutions, where

132 Q 136 (Thérèse Coffey MP)

133 Department for Environment, Food and Rural Affairs, Environment Agency, and Ofwat, *Water industry national environment programme (WINEP) roadmap* (May 2022): <https://www.gov.uk/government/publications/water-industry-national-environment-programme-winep-roadmap/water-industry-national-environment-programme-winep-roadmap> [accessed 10 January 2023]

natural solutions are designed to protect or enhance the environment while mitigating or preventing pollution¹³⁴

143. Mr Colville said that ideally, there would be top-level goals nationally that describe the level of ambition in the case of the environment, which are then translated to a catchment-by-catchment basis to reflect local pressures and opportunities and enable companies to deliver different solutions.¹³⁵
144. Lawrence Gosden, Chief Executive Officer of Southern Water, Mr Perry and Ms Bentley all emphasised the need for both outcomes and outputs as part of the regulatory system, suggesting that specific outputs are needed in maintaining the health of infrastructure assets, whereas outcomes are helpful when looking at long-term environmental goals. Ms Bentley accepted that it is a difficult situation for companies to play a bigger role in the WINEP given low levels of trust in the sector but argued that the next WINEP needs to be broken down into local, relevant plans that allow companies to work collaboratively with local authorities, environmental NGOs and agriculture owners, allowing companies to build trust on the ground.¹³⁶
145. Mr Cox said that Ofwat has used an outcomes-based approach in its last two Price Reviews and wants the Environment Agency to adopt a similar approach to encourage innovation in wastewater treatment. He suggested that in his conversations with them, the Environment Agency has some sympathy with the idea but has a distrust of water companies having greater leeway to determine outputs. He explained that there was agreement that only those companies at the top of the Environment Agency's performance rating could be given the opportunity of an outcomes-based regime.¹³⁷ Sir James confirmed that some companies are serious and others are not, with a great difference in performance and attitude between them. Nonetheless, the Environment Agency tried to be outcomes-focused and proportionate¹³⁸
146. Sir James argued that the then-Government's review of EU regulation on the statute book was an opportunity to deliver a more outcomes-based framework, with the Environment Agency having identified various EU legacy regulations that can be reformed or repealed. Mr Lovell said that he is highly motivated to take an outcomes-based approach and that there is some frustration at the amount of funding that is still restricted and used in a very closely prescribed way, arguing that the Environment Agency "shall certainly try and loosen those shackles".¹³⁹
147. Mr Black said that Ofwat has used an outcomes-based approach in its Price Review but not in the environmental area. He argued this was because the Environment Agency is held back by pre-existing EU legislation, but also called for a "very clear government steer" as to the outcomes it wants, allowing Ofwat and others to "unleash innovation, partnership working and getting the best solutions".¹⁴⁰
148. Asked whether companies are ready for an outcomes-based approach, Mr Black said that "some are and some are not", stressing that some companies

134 [Q 10](#) (Anabelle Ong)

135 [Q 55](#) (Stuart Colville)

136 [Q 118](#) (Lawrence Gosden)

137 [Q 90](#)

138 [Q 102](#) (Sir James Bevan)

139 *Ibid.*

140 [Q 125](#) (David Black)

are “well behind on their current delivery of outputs”, which “would raise concerns” while other companies are keen and ready.¹⁴¹

149. Mr Coucher agreed that there are roles for outputs, particularly in relation to issues such as mains renewals, and there are areas where Ofwat “might want an output measure as well as an outcome”. However, he stressed that outcomes are “absolutely the right way to go” and are “largely a better way of doing things”.¹⁴²
150. The Secretary of State said that it was “always better to have an outcomes-based approach” but that she was “conscious that sometimes not all the things that you are trying to do are in your control”. She explained that there will be many areas that are driven by outputs as outcomes-based regulation “is a novel approach”. She said that the Government, Ofwat and the Environment Agency were “working together” to include an outcomes-based approach in the next WINEP.¹⁴³
151. **The current Water Industry National Environment Programme (WINEP), an investment programme through which the Environment Agency specifies works required by water companies to meet environmental goals, is prescriptive about work water companies should undertake. Many stakeholders told us a move to outcomes-based regulation, where how an outcome is met is not prescribed, would give water companies greater opportunity to design innovative solutions to problems facing the sector. These solutions may be more cost-effective and environmentally friendly than traditional ones. We therefore welcome that the Government, Ofwat and the Environment Agency are planning to move towards outcomes-based regulation in the next iteration of the WINEP.**
152. *The Government, Ofwat and the Environment Agency should ensure that the next iteration of the Water Industry National Environment Programme has a greater focus on the outcomes to be achieved. This will give responsible companies more leeway to use nature-based and catchment-based solutions.*
153. *To the extent that prescriptive regulatory requirements are the result of retained EU law, the Government should examine whether the relevant provisions can be amended to enable an outcomes-based framework in time for the next Price Review.*

141 [Q 125](#) (David Black)

142 [Q 125](#) (Iain Coucher)

143 [Q 140](#) (Thérèse Coffey MP)

CHAPTER 5: STORM OVERFLOWS AND WATER POLLUTION

154. Storm overflows, agricultural runoff, and runoff from roads and transport all contribute to water pollution and ought to be tackled to safeguard the environment. Given that the focus of our inquiry is on the regulation of water companies, we have focused our attention on pollution that water companies bear responsibility for.

Storm overflows

155. Sir James Bevan, Chief Executive of the Environment Agency, told us water companies are responsible for 36 per cent of water pollution.¹⁴⁴ Pollution from water companies can be caused by storm overflows and ineffective management of wastewater treatment works. Storm overflows are release valves used when sewage systems become at risk of being overwhelmed—for example, in periods of high rainfall. They release water and sewage into rivers and the sea to prevent damage to the sewage system that could cause flooding of properties and streets. Storm overflows can be found at wastewater treatment works and elsewhere on the sewer network, where they are known as combined sewer overflows (CSOs).

156. Wastewater treatment works take foul water from the sewage system, treat it, and release it back into the water cycle in a state that does not damage the environment. If pressure on sewage systems becomes too great, wastewater treatment sites are unable to treat and accommodate the volume of water they receive and thus release untreated water back into the environment.

157. In England, the Environment Agency is responsible for issuing permits to water companies to allow them to use storm overflows in exceptional situations. They also regulate wastewater treatment works by assessing the quality of wastewater they discharge against compliance limits. In Wales, Natural Resources Wales bear this responsibility.

158. Professor Ian Barker, Managing Director at Water Policy International Ltd, said that while the Environment Agency is responsible for setting and enforcing storm overflow permits, Ofwat may have a role if a company is breaking rules so often that it may not be delivering the statutory functions that Ofwat is responsible for enforcing.¹⁴⁵

159. Although storm overflows are intended to be used in exceptional circumstances, witnesses told us they are used routinely. In 2021, sewage was released from storm overflows 327,533 times for 2.6 million hours. In 2020, they spilled more than 400,000 times for over 3 million hours.¹⁴⁶ Jonson Cox, former Chair of Ofwat, urged that “we need to get down to a standard that is what the purpose of the storm overflow always was ... that it should operate at a time of extreme storm.”¹⁴⁷ His views were echoed by Ofwat, who said the “current overuse of storm overflows is unacceptable”,¹⁴⁸ and a range of environmental groups including Wildlife and Countryside Link, Salmon and Trout Conservation, Angling Trust, and Blueprint for Water.¹⁴⁹

144 [Q 96](#) (Sir James Bevan)

145 [Q 10](#) (Sir James Bevan)

146 Written evidence from Angling Trust ([TWW0012](#))

147 [Q 77](#)

148 Written evidence from Ofwat ([TWW0030](#))

149 Written evidence from Wildlife and Countryside Link ([TWW0022](#)), Salmon and Trout Conservation ([TWW0002](#)), Angling Trust ([TWW0012](#)), and Blueprint for Water ([TWW0032](#))

Causes of storm overflow overuse and solutions

160. Stuart Colville, Director of Policy at Water UK, told us that the issues with storm overflows stem from the 1850s to 1965, when they were “routinely inserted into the construction of sewers”. However, “the challenges of climate change, fat, oil and grease, and wet wipes ... were not necessarily being borne in mind when [storm overflows] were first designed”.¹⁵⁰ The Rt Hon Philip Dunne MP, Chair of the House of Commons Environmental Audit Committee, explained that population growth has put additional pressure on the sewer network. He also said more rainwater now needs to enter the system both because of greater rainfall caused by climate change and the building of properties, which has resulted in less porous ground to absorb rainwater.¹⁵¹ Alan Lovell, Chair of the Environment Agency, said that shortly after privatisation, water company investment was “directed primarily at the availability of more fresh water, more drinking water” rather than wastewater.¹⁵²
161. An independent evidence project commissioned by the Storm Overflows Taskforce, established by the Government in 2020, found that to reduce the volume and frequency of storm overflows, “Either more collected rainwater and wastewater must be retained in the system and provided with treatment at a wastewater treatment works. Or the quantity of rainwater entering sewers must be reduced, enabling a higher proportion of all flows to receive full treatment.” The Taskforce identified four approaches to reducing storm overflow overuse:
- Modify the current sewer system, which combines polluted water with unpolluted water, so that the two types of water are separate. When water needs to be released via storm overflows, unpolluted water can be released;
 - Add capacity to the sewer system to store and treat more water;
 - Manage storm runoff differently, so that it does not all enter the sewer system, using partly or wholly nature-based solutions such as sustainable drainage systems;
 - Treat discharges from storm overflows on site to a standard where environmental harm is avoided.
162. The Taskforce found that “there will be an optimum mix of approaches appropriate to specific locations”.¹⁵³

Combined sewage systems, the right to connect, and sustainable drainage systems

163. Currently, much of England is covered by combined sewage systems. Surface water¹⁵⁴ is combined with wastewater from toilets, bathrooms and kitchens when conveyed to sewage treatment works, polluting it. As a result, when

150 [Q 61](#) (Stuart Colville)

151 [Q 1](#)

152 [Q 95](#) (Alan Lovell)

153 Department for Environment, Food and Rural Affairs, *Storm Overflows Discharge Reduction Plan*: (August 2022): https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1101686/Storm_Overflows_Discharge_Reduction_Plan.pdf [accessed 4 January 2023]

154 Surface water is water present on the surface of earth. In this context, it refers largely to unpolluted water that enters the sewage system as runoff. This includes, for example, rainwater, or water runoff from cleaning a car.

storm overflows are used, polluted water is released. If foul and surface water were separated, clean surface water could be released in times of stress.

164. Mr Dunne reflected on an oral evidence session the Environmental Audit Committee held with then Secretary of State for Environment, Food, and Rural Affairs, The Rt Hon George Eustice MP, who said that separating foul and surface water within sewers was essential to reducing pressure on the system and preventing storm overflow overuse.¹⁵⁵ However, Mr Dunne highlighted that separating surface and foul water completely would be “a mammoth undertaking” as “there are in the order of 600,000 kilometres of underground drainage networks ... [and a] huge amount of infrastructure would be required to separate them.”¹⁵⁶
165. Mr Dunne suggested that a good place to begin is ceasing the right to connect.¹⁵⁷ Currently, in England, developers have the right to connect new developments to combined sewer systems, without separating foul and surface water, and without regard to the capacity of the sewer to take on a new connection. This differs to Wales, where the right to connect was removed in 2019. In Wales, all construction work with drainage implications, of at least two properties or 100m² or more, is required to have sustainable drainage systems that comply with national standards. County Councils have Sustainable Drainage Approval Bodies that developers must seek approval for their drainage systems from.¹⁵⁸
166. Schedule 3 to the Flood and Water Management Act 2010 was intended, by 2015–16, to make the right to connect conditional upon approval by a Sustainable Drainage Systems approving body at the county and unitary level.¹⁵⁹ Yet the Schedule was never enacted.
167. The Worshipful Company of Water Conservators called for Schedule 3 to be enacted, highlighting that “water companies and regulators have no powers to object to development but do have statutory obligations as a consequence of planning decisions”. They recommended water companies are made statutory consultees in the planning process. They also recognised that ceasing the right to connect could be “an impediment to development” that would “clash with the regular planning permission process”. Therefore, the National Planning Policy Framework would need to be updated accordingly.¹⁶⁰ David Black, Chief Executive of Ofwat, commented that the Government has “committed to reviewing” the enactment of Schedule 3, but Ofwat is looking for better solutions surrounding surface-water drainage.¹⁶¹ Guy Linley-Adams, a Solicitor at Salmon and Trout Conservation, argued that “it should not be possible to build new builds where there are surface water drains connected to sewers.”¹⁶²

155 [Q 1](#)

156 *Ibid.*

157 [Q 3](#)

158 Llywodraeth Cymru Welsh Government, *Statutory standards for sustainable drainage systems – designing, constructing, operating and maintaining surface water drainage systems* (2018): <https://www.gov.wales/sites/default/files/publications/2019-06/statutory-national-standards-for-sustainable-drainage-systems.pdf> [accessed 3 January 2023]

159 Flood and Water Management Act 2010, [Schedule 3](#)

160 Written evidence from Worshipful Company of Water Conservators ([TW0011](#))

161 [Q 124](#) (David Black)

162 [Q 25](#) (Guy Linley-Adams)

168. In January 2023, the Government published a review for implementation of Schedule 3. The review found that Schedule 3 should be implemented “subject to final decisions on scope, threshold and process once a full regulatory impact assessment has been consulted on.” In her foreword to the review, the Secretary of State said she intends to make “swift progress” with the implementation of Schedule 3. A public consultation will be launched in late 2023, with implementation expected during 2024.¹⁶³ She told us she did “not know what has happened” to cause the delay to the enactment of Schedule 3 but was glad the Government has “agreed to get on with it”.¹⁶⁴
169. **The prevalence of combined sewers in England, which combine surface water with foul water, results in polluted water being released to the environment via storm overflows. Although the Government will need to look at the possibility of separating sewers, significant progress could be made by reducing pressures on the existing network. We therefore welcome the Government’s intention to enact Schedule 3 of the Flood and Water Management Act 2010. This will ensure developers in England are not able to connect to existing sewer networks without designing appropriate sustainable drainage systems, and will place England in line with Wales, where most construction work is required to have sustainable drainage systems that comply with national standards.**

Wet wipes

170. In June 2022, Mr Cox, Professor Chris Whitty, Chief Medical Officer for England, and Emma Howard Boyle, then-Chair of the Environment Agency, wrote an opinion piece for The Telegraph where they set out that sewage in waterways is a serious public health risk. The piece states that “management of sewers is made more difficult by plastic wet wipes flushed down toilets which congeal together with fats poured down drains to form fatbergs that block sewers and cause avoidable use of the storm overflows.” They argued that ensuring only rapidly biodegradable wet wipes are available to purchase, or that wet wipes are only put in bins, would immediately assist the problem.¹⁶⁵
171. In a July 2022 report on customer research into river water quality, Ofwat found that only 64 per cent of surveyed customers understood that personal behaviour such as flushing wet wipes can directly impact sewerage systems.¹⁶⁶ Mr Lovell said it “is primarily the role of water companies to have dialogue with their customers” on issues such as wet wipes. Mr Cox told us that there needed to be a common campaign from the industry on wet wipes, as “it is no use each company having slightly different messages”.¹⁶⁷

163 Department for Environment, Food and Rural Affairs, *The review for implementation of Schedule 3 to The Flood and Water Management Act 2010* (January 2023): https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1128073/The_review_for_implementation_of_Schedule_3_to_The_Flood_and_Water_Management_Act_2010.pdf [accessed 24 January 2023]

164 [Q 133](#) (Thérèse Coffey MP)

165 Jonson Cox, Chris Witty, Emma Howard Boyle, ‘Sewage in waterways is a serious public health risk’, *The Telegraph* (25 June 2022): <https://www.telegraph.co.uk/news/2022/06/25/sewage-waterways-serious-public-health-risk/> [accessed 7 February 2023]

166 Ofwat, *River water quality: customer research* (July 2022): https://www.ofwat.gov.uk/wp-content/uploads/2022/07/River_Quality_Report_ENG.pdf [accessed 7 February 2023]

167 [Q 87](#)

172. Ms McGourty told us 90% of fatbergs are made up of wet wipes. She said Water UK would launch a national campaign around wet wipes in late 2022, but the issue required “help and support” from policy makers.¹⁶⁸
173. In December 2022, we wrote to the Secretary of State to ask why the Government has not banned non-biodegradable wet wipes. The Secretary of State did not answer this question in her response.¹⁶⁹
174. **Wet wipes pose a serious risk to the proper operation of the sewage system by contributing to “fatbergs”—build ups of fat that cause blockages and thus storm overflow use. Consumers must be properly educated about the problems of wet wipes by the water industry. We therefore welcome Water UK’s national campaign on the issue. However, policy intervention may also be needed.**
175. *We recommend the Government considers banning the sale of wet wipes that are not rapidly biodegradable.*

Nature-based solutions to water pollution

176. Nature-based solutions to water pollution are designed to protect or enhance the environment while mitigating or preventing pollution. For example, constructing a wetland adjacent to a wastewater treatment site can help to filter nutrient pollution, slow the flow of water and prevent flooding, and provide habitats for wildlife.¹⁷⁰ Uncropped arable land can be used to store water and limit pressure on the sewer system.
177. Witnesses from environmental groups highlighted the importance of nature-based solutions in the fight to tackle pollution. Mr Lloyd said he felt Ofwat had placed “too much emphasis on delivery of carbon-intensive and engineered solutions on water company assets, such as improving treatment works on small rural works” where you could spend less on a catchment solution which would greater benefit society.¹⁷¹ The Angling Trust told us that “Ofwat must do more to facilitate the use of both catchment and nature-based solutions by the water industry”, mainly through the upcoming Price Review, PR24.¹⁷² This sentiment was shared by Blueprint for Water¹⁷³ and Wildlife and Countryside Link, who said Ofwat should “incentivise the use of catchment and nature-based solutions (C&NBS) by the water industry ... through the PR24 methodology directly”.¹⁷⁴
178. Some witnesses emphasized that in order for nature-based or catchment-based solutions to be successful, a move towards outcomes-based regulation is necessary. This concept is explored in Chapter 3. Ms Ong said we need “a regulatory system that will incentivise companies to innovate, so that in five or 10 years we get the optimal mix between traditional, nature-based, partnership and other solutions.”¹⁷⁵

168 [Q 59](#) (Christine McGourty)

169 Letter from Lord Hollick, Chair of the Industry and Regulators Committee, to Therese Coffey MP, Secretary of State for Environment, Food, and Rural Affairs, 2 December 2022: <https://committees.parliament.uk/publications/31843/documents/179085/default/>

170 Environmental Audit Committee, *Water quality in rivers* (Fourth Report, Session 2021–22, HC 74)

171 [Q 16](#) (Mark Lloyd)

172 Written evidence from Angling Trust ([TWW0012](#))

173 Written evidence from Blueprint for Water ([TWW0032](#))

174 Written evidence from Wildlife and Countryside Link ([TWW0022](#))

175 [Q 12](#) (Annabelle Ong)

179. Professor Barker added that achieving such innovation will be difficult, as concrete and steel solutions have been popular in the past because companies know how to operate them. Transitioning to more innovative nature-based solutions “will take longer to establish and to deliver the environmental outcomes we seek. Until that is happening, regulators, Governments and water companies will need to hold their nerve and trust in the solutions”, sharing data with others in the process of discovering which solutions are most effective.¹⁷⁶ Stuart Colville, Director of Policy at Water UK, similarly remarked that “If you do not give yourself enough time to design a scheme, you will be driven down a concrete route because they are more familiar ... rather than a nature-based route”.¹⁷⁷
180. IFM Investors argued that nature-based solutions “require a more outcomes-based approach measured well beyond the current 5 year regulatory horizon.”¹⁷⁸ A similar view was expounded by Ms Bentley, who said a “move towards outcome measures is helpful when we look at some of these longer-term and perhaps nature-based solutions”.¹⁷⁹
181. Mr Linley-Adams expressed that it “is great” if “you can separate rainwater from sewage and put that into nature-based solutions rather than into the sewers”. However, he underlined that there will remain a need for foul water to be treated properly: “It is very difficult to see how you can apply a nature-based solution to that.”¹⁸⁰
182. **While regulators and companies in the sector may be more comfortable with traditional, infrastructure-heavy solutions to water pollution, and some will undoubtedly be needed, it is clear that there is also a place for innovative approaches, including nature-based solutions and catchment approaches. These can be a cost-effective, environmentally friendly way of reducing water pollution.**
183. *We recommend nature-based solutions and catchment approaches form a larger part of the next iteration of the Price Review and the Water Industry National Environment Programme (WINEP).*

Investment needed to address storm overflow overuse

184. David Black, Chief Executive of Ofwat, told us that the water sector has historically “been very slow to identify the early signs that more investment [to deal with storm overflows] needs to be made”. He outlined that in 2014, when monitoring of storm overflow use was rolled out, data became available which showed “there is a need for a major step-up in investments”, and that this “will now take place.”
185. The independent evidence project commissioned by the Storm Overflows Taskforce found that the elimination of discharges from storm overflows by separating rainwater drainage from wastewater in the sewer network would cost between £350 billion and £600 billion and would cause significant disruption. The Taskforce said that reducing discharges to zero in an average

176 [Q 12](#) (Prof Ian Barker)

177 [Q 54](#) (Stuart Colville)

178 Written evidence from IFM Investors ([TWW0010](#))

179 [Q 118](#) (Sarah Bentley)

180 [Q 19](#) (Guy Linley-Adams)

year through other options, such as building storage tanks to capture excess water during heavy rainfall, would cost between £240 billion to £260 billion.¹⁸¹

186. In its August 2022 Storm Overflows Discharge Reduction Plan, the Government set a target that by 2050, “no storm overflows will be permitted to operate outside of unusually heavy rainfall or to cause any adverse ecological harm”. Overall, the plan estimated there will need to be £56 billion of capital investment over the next 25 years to reach this target. The plan anticipated that there would be no consumer bill impacts of its plans to reduce storm overflow discharges by 2025, and that over the whole period to 2050, bills would eventually rise by £42 per annum. However, the Government emphasised that this is an average and that there is expected to be significant variations across years and water company regions, with impacts in some regions at three times the national average.¹⁸²
187. Mr Dunne said that the challenge of retrofitting and disconnecting systems is “enormous” but suggested that capital markets are “awash” with capital to invest in long-term, sustainable projects, arguing that the qualifier would be the capacity of the construction industry to deal with the volume of investment required. He said that there will be an argument about the pace and extent to which the use of storm overflows is reduced and how to find a balance between how this is paid for, over what period, and how to keep bill levels within reason. While this will come at some cost, he argued that this does not have to lead to an excessive increase in bills.¹⁸³
188. Professor Catherine Waddams, a member of the Centre for Competition Policy at the University of East Anglia, noted that there is an argument consumers should pay for investment “because they are the people who can benefit from it”. However, she felt that funding investment through bills was regressive, and suggested that there was a case for providing funding through general taxation as it is a public good.¹⁸⁴
189. Christine McGourty, Chief Executive of Water UK, suggested that storm overflows could take “tens of billions of pounds” to resolve but argued that the private sector had shown it could deliver high levels of investment after privatisation.¹⁸⁵ She argued that the cost can be minimised by the right public policy interventions, and with interaction with other areas of public spending, such as Environmental Land Management Schemes (ELMS).¹⁸⁶ She emphasised the need to act now and not “push the problem out to future generations”¹⁸⁷.
190. Lawrence Slade, Chief Executive of the Global Infrastructure Investor Association, emphasised the need for flexibility in funding settlements to enable water companies to respond to any imminent challenges, given

181 Department for Environment, Food and Rural Affairs, ‘Storm overflows evidence project’: <https://www.gov.uk/government/publications/storm-overflows-evidence-project> [accessed 4 January 2023]

182 Department for Environment, Food and Rural Affairs, *Storm Overflows Discharge Reduction Plan*: (August 2022), https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1101686/Storm_Overflows_Discharge_Reduction_Plan.pdf [accessed 4 January 2022]

183 [QQ 1, 4–5](#)

184 [Q 47](#)

185 [Q 56](#) (Christine McGourty)

186 Environmental Land Management schemes are environmental schemes where farmers and land managers are paid for taking actions which benefit the environment—for example, farming in a sustainable way.

187 [Q 63](#) (Christine McGourty)

the unpredictability of climate change and its impact on water capacity. He argued that if long-term planning is done right, with companies and investors having confidence in the direction of travel and the regulatory approach, then the impact on bills should be minimal, although engagement with consumers will be needed as there will definitely be costs.¹⁸⁸

191. Lawrence Gosden, Chief Executive of Southern Water, said that early estimates of the cost of an 80 per cent reduction in storm overflow discharges in Southern Water's area would be in the order of £2 billion. He explained that this would be a doubling of Southern's capital programme for the five-year Price Review period.¹⁸⁹ Mr Perry said that the large number of river catchments and Wales' sparse population mean that Dŵr Cymru Welsh Water's bill to reduce storm overflows would be £9 billion, as it has more lengths of sewer.¹⁹⁰ Sarah Bentley, Chief Executive of Thames Water, said that the current estimate for Thames Water to make the necessary reductions in discharges by 2030 is £2 billion, as the company is advantaged by the Thames Tideway project resolving a large part of London's infrastructure.¹⁹¹
192. The Water Industry Act 1991 provides a duty on sewerage providers to "provide, improve and extend" a system of public sewers, to "cleanse and maintain those sewers", and "to make provision for the emptying of those sewers", including by "effectually dealing... with the contents of those sewers".¹⁹² Mr Cox told us:
- "Nearly a third of breaches of storm overflows resulted from inadequate maintenance of sewers. Operating performance is for companies to manage. They certify to Ofwat every year that they have the resources to operate and maintain their services to meet their legal obligations, and failure to do that should be at their cost."
193. He said that the model of private investment in the water system is "hugely attractive" and continues to be so to private capital markets. He argued that it is a "fantastic model" for pension funds looking to make long-term investments and that there is no shortage of private capital funds to invest, as shown by the fact that new investors were found for Southern Water when it was virtually put into special administration and its previous investors lost money.¹⁹³ Iain Coucher, Chair of Ofwat, said that Ofwat is very aware that some of the environmental improvements that it wants would have an upward impact on bills. He stressed the need for early conversations as to the scale of ambition on the environment and what this will do to consumer bills. He explained that Ofwat has the ability to "sculpt" where costs will fall and can push back impacts on bills towards the end of the next Price Review to ease the impacts in earlier years, but noted that this is still a real issue for the sector.¹⁹⁴
194. Mr Black said that Ofwat cannot yet say what the scale of future investment will be, noting that the Government's Storm Overflows Discharge Reduction Plan talks about £56 billion over 25 years. He outlined that this would be a doubling of current environmental spend but that this was "certainly

188 [QQ 68–69](#)

189 [Q 106](#) (Lawrence Gosden)

190 [Q 106](#) (Peter Perry)

191 [Q 106](#) (Sarah Bentley)

192 Water Industry Act 1991, [Section 94](#)

193 [Q 79](#) (Jonson Cox)

194 [Q 120](#) (Iain Coucher)

not the limit” as storm overflows are only one aspect of the environmental issues facing the sector. He argued that Ofwat will not know the full scale of expenditure until companies have submitted their business plans and stressed that it is ultimately the responsibility of companies to put investment needs to Ofwat.¹⁹⁵

195. Mr Coucher said that Ofwat has some very good ideas about what investment plans will be going forward and can quantify what it believes the investment cost will be for environmental schemes under discussion but noted that those are Ofwat’s estimates and the regulator wants companies to propose what the costs will be, as it is conscious that some of the increased expenditure will affect some water companies much more significantly than others.¹⁹⁶
196. The Secretary of State said that the Storm Overflows Taskforce estimated the cost of eliminating storm overflows at “about £600 billion, which would be an average of about £850 extra on people’s water bills”. She said that the Government was “not prepared to go to that level [on bills]”, because it did not think that “getting bills to that level was the right thing to do.”¹⁹⁷
197. The Secretary of State explained that the Government’s plan will require “about £56 billion of investment” to tackle the storm overflows issue between 2025 and 2050. She stressed that the Government “will continue with the existing model” to fund this investment and that she is “pretty clear that there will not be any money coming from the Treasury”.¹⁹⁸
198. **A huge level of investment—that the Government has estimated will cost £56 billion over 25 years—is required so that storm overflows are only used in times of exceptional weather. Given that water companies are responsible for maintaining their own sewage networks, they must bear a significant degree of responsibility for the necessary investment costs. However, we recognise that the scale of investment needed is vast, and for the private sector to meet this challenge there will need to be stable, long-term funding arrangements that provide certainty for investors.**
199. *The Government should set out how it envisages the investment needed to prevent pollution will be funded through a National Water Strategy. Water companies should take the lead in meeting the majority of costs.*

Prioritising investment in storm overflows

200. Given the cost of reducing or eliminating storm overflow use could run to billions of pounds, the question arises of whether prioritising storm overflows provides value for money—especially considering there are a number of other sources of water pollution.¹⁹⁹ Mr Perry said that in Wales, “nutrient pollution is the key issue ... If our focus is on [combined sewer overflows], it will be absolutely marginal and we will not make the same level of progress.”²⁰⁰

195 [Q 120](#) (David Black)

196 [Q 120](#) (Iain Coucher)

197 [QQ 131–132, 135](#) (Thérèse Coffey MP)

198 *Ibid.*

199 [Q 94](#) (Sir James Bevan)

200 [Q 106](#) (Peter Perry)

201. Pennon Group emphasized that in the case of water quality:

“cross-sectoral action is needed to deliver least cost solutions. For example, we could undertake expensive sewer maintenance programmes, or Government policy could set the way for behavioural change on wet wipes, making unflushable products unacceptable.”²⁰¹

202. The Secretary of State pointed out that while the Treasury would not provide funding for water infrastructure, “we are already spending money in different ways, through things such as flood defences, in our area.”²⁰²

203. **Pollution caused by the routine use of storm overflows is environmentally damaging and the public is right to demand better. However, we recognise that there are other causes of water pollution which must also be tackled.**

204. *A National Water Strategy should include consideration of how funding should be balanced across causes of water pollution, to maximise environmental protection and minimise costs.*

Monitoring

Development of monitoring

205. Storm overflows can be monitored to ascertain how frequently they are used. Mr Dunne told us that in 2010, the Environment Agency moved to a system where water companies self-monitored discharge incidents, “partly because it had fewer personnel engaged”. He said a result of this move to self-monitoring seemed to be that the Environment Agency were unaware of the extent of pollution incidents. Sir James said that the Environment Agency “identified that there was a problem at [storm overflows]”, so the fitting of monitors was rolled out across the sector from 2014. This rollout will be completed by the end of 2023, at which point all 15,000 storm overflows will have monitors fitted.²⁰³ The Secretary of State said it was The Rt Hon Richard Benyon MP, then Minister for Natural Environment and Fisheries, who took steps to require water companies to introduce monitoring.²⁰⁴

206. Sir James outlined that as monitors began to be rolled out to oversee storm overflows, it became clear from the data that “overflows were spilling far more frequently and for longer than anyone, including the Environment Agency, had been aware of.”²⁰⁵ At that point, the Environment Agency “started to investigate actively”²⁰⁶ and began to work with the Government to ensure changes were made.

207. Mr Cox outlined a similar story with Ofwat and the monitoring of wastewater treatment works. He told us that in 2015, there started to be concern about the operation of wastewater treatment works, and as a result “Ofwat funded the rollout of monitors in every company and every works over a certain size”.²⁰⁷ Yet it was only in October 2021 that data became available to show

201 Written evidence from Pennon Group ([TW0023](#))

202 [Q 132](#) (Thérèse Coffey MP)

203 [Q 94](#) (Sir James Bevan)

204 [Q 131](#) (Thérèse Coffey MP)

205 [Q 94](#) (Sir James Bevan)

206 [Q 96](#) (Sir James Bevan)

207 [Q 73](#)

significant failings across wastewater treatment works and enforcement action could begin.

208. Sir James said he did “not think anybody, not even the water companies, was aware of the scale of what was going on, because until a few years ago people had not really thought that it was an issue of particular importance.”²⁰⁸ On the issue of wastewater treatments, he added that the Environment Agency “did not have the resources to put a lot of our people on to sewage treatment plants and sewage outfalls to check what was actually going on”, which contributed to the Environment Agency only recognising there was a problem recently.²⁰⁹ Mr Black similarly said: “The issue of storm overflows was known about, but the extent of the issue was not known” prior to 2014.²¹⁰
209. Lawrence Gosden, Chief Executive of Southern Water, told us he could not see how “before [monitoring began] we could have understood exactly what was occurring in some of those places out in the network.”²¹¹ Sarah Bentley, Chief Executive of Thames Water, argued that in the case of wastewater plants, “It seems to have been the case that the measuring that was done [initially] was on some of the quality parameters ... regarding levels of ammonia and phosphorus, not levels of flow”, in line with the EU Water Framework Directive.²¹² She also posited that “A number of the treatment works and storm discharge points are not manned, so there is no one there looking at these things.”²¹³
210. Mr Coucher did not believe that water companies knew the extent of pollution being caused by storm overflows prior to the introduction of monitoring. However, he said that this raises a concern about how much water companies know about their assets, so Ofwat “absolutely have to get on top of that” so that companies can “respond when things are not going right.”²¹⁴
211. Mr Cox was more sceptical. He noted that data was only presented by water companies “as it became very clear that the rollout of these monitors was going to show very significant non-compliances with the regulations and permits relating to wastewater treatment works.”²¹⁵ Sir James set out that:
- “It was not until the Environment Agency insisted a few years ago that the water companies put monitors both on their combined sewage overflows and, critically, on what was happening at their sewage treatment plants ... that some of the water companies came to us and said, “We think that when you see the data we will find that at least some of our sewage treatment works are not compliant”.
212. He went on to say it was conceivable that “at least some of the leaderships of those companies were not aware” of the amount of non-compliance happening on the network, but that it is “quite hard to believe that some of the people working on the ground at some of the sewage treatment plants did not know that those plants were failing to meet the terms of their permits”.

208 [Q 94](#) (Sir James Bevan)

209 [Q 96](#) (Sir James Bevan)

210 [Q 120](#) (David Black)

211 [Q 116](#) (Lawrence Gosden)

212 [Q 116](#) (Sarah Bentley)

213 *Ibid.*

214 [Q 124](#) (Iain Coucher)

215 [Q 73](#)

He emphasized, however, that this is something that would need to be established by an ongoing investigation.²¹⁶

Effectiveness of monitoring and enforcement

213. Mr Cox said that when Ofwat and the Environment Agency became aware of data that indicated significant failings at wastewater treatment works, they acted quickly, opening investigations against five and then six companies within a month in November 2021.²¹⁷ Then, in March 2022, Ofwat announced that it was opening enforcement cases into five water and wastewater companies (Anglian Water, Northumbrian Water, Thames Water, Wessex Water and Yorkshire Water) as part of this investigation. The companies have been served formal notices to gather further information for enforcement purposes.²¹⁸ In June 2022, a further enforcement case was opened into South West Water, which was also served with a formal notice to gather information.²¹⁹
214. In 2019 Ofwat fined Southern Water £126 million after concluding that it had underinvested in a number of its works, leading to equipment failures and sewage spills. The company had also “manipulated its wastewater sampling process” to avoid revealing the sites’ performance and so avoid penalties under Ofwat’s incentive scheme.²²⁰
215. Separately, in 2021 the Environment Agency prosecuted Southern Water for breaches of the conditions of its permits which had resulted in the dumping of billions of litres of raw sewage into the sea over several years. The company admitted 6,971 unpermitted spills from 17 sites in Hampshire, Kent and West Sussex between 2010 and 2015. The £90 million fine for the spills was the highest ever awarded by a court for a sewage discharge permit breach.²²¹
216. Professor Ian Barker, Managing Director at Water Policy International Ltd, said that the Environment Agency had made it very clear to the House of Commons Environmental Audit Committee that it “does not have adequate resources to monitor and enforce.” This is because “there has progressively been a reduction in the grant in aid given to the Environment Agency”, which it uses to fund monitoring—though it is unclear exactly how much the fund had reduced.²²²
217. On 29 November 2022, The Times published an article claiming the Environment Agency had told officials that if, following reports of an incident, a water company was able to demonstrate no impact, the Environment

216 [Q 95](#) (Sir James Bevan)

217 [Q 73](#)

218 Ofwat, ‘PN 10/22: Five water companies targeted in next phase of Ofwat wastewater treatment work investigation’, (9 March 2022) : <https://www.ofwat.gov.uk/pn-10-22-sewage-treatment-works-investigation-march-2022-update/> [accessed 4 January 2023]

219 Ofwat, ‘PN 24/22 South West Water latest company targeted in Ofwat investigation due to poor environmental performance’, (28 June 2022): <https://www.ofwat.gov.uk/pn24-22-south-west-water-latest-company-targeted-in-ofwat-investigation-due-to-environmental-performance/> [accessed 4 January 2023]

220 Ofwat, ‘PN 21/19: Ofwat confirms Southern Water will pay £126m following investigation’, (10 October 2019): <https://www.ofwat.gov.uk/pn-21-19-ofwat-confirms-southern-water-will-pay-126m-following-investigation/> [accessed 4 January 2023]

221 Environment Agency, ‘Record £90m fine for Southern Water following EA prosecution’, (9 July 2021): <https://www.gov.uk/government/news/record-90m-fine-for-southern-water-following-ea-prosecution> [accessed 4 January 2023]

222 [Q 10](#) (Prof Ian Barker)

Agency should accept this without further investigation.²²³ We wrote to Sir James asking for further information. Sir James responded that the Environment Agency is not funded to respond to all incident reports, so made the decision to only focus on the most serious incidences. Earlier this year, the Environment Agency issued guidance to staff that they should “reduce response levels” to minor and no impact pollution incidents. However, they must still consider attending such incidents “in certain circumstances and at sensitive locations. For example, at bathing waters where we can expect people to be in the water.”²²⁴

218. When we asked Sir James if the Environment Agency was underfunded, he acknowledged that “All public sector organisations are under resource pressure”. Yet he explained the Environment Agency had faced particular issues with funding enforcement:

“For various reasons that the Treasury has imposed, we are not allowed to use the £200 million, on average, that we get every year from the water companies to fund the cost of regulating them, to prosecute them. That means that the only money we have to enforce and prosecute has to come in the form of grant. Over the last 10 years, the overall grant that the Environment Agency has had from successive Governments for our environment work has diminished.”

219. However, he said the Environment Agency has seen a “welcome reversal of that decline in the budget” this year.²²⁵
220. The Secretary of State said that “every organisation funded by taxpayers often wants a lot more money than they have”. She said this is often a result of the Government having to make choices like prioritising putting money into the NHS.²²⁶ Nonetheless, she noted that “the [Environment Agency’s] budget has “certainly increased” for the purposes of enforcement, highlighting that Anglian Water has recently been prosecuted and fined in court.²²⁷
221. **The levels of storm overflow overuse by some companies are unacceptable. We welcome that monitors will be present on all storm overflows by the end of 2023 and that the Government has increased the Environment Agency’s funding for monitoring. However, it appears that the Agency’s monitoring and enforcement has in the past been seriously compromised by cuts to its grant, leading to an over-reliance on self-monitoring by water companies. It is crucial that the Environment Agency is provided with adequate funding to carry out inspections. Failure to do this would risk returning the regulator to a position where it must rely on water companies to police their own behaviour.**

223 Adam Vaughan, ‘Beach sewage inspections to be scaled back’, *The Times* (25 November 2022): <https://www.thetimes.co.uk/article/environment-agency-scales-back-beach-sewage-pollution-inspections-66ld0nvg8> [accessed 4 January 2023]

224 Letter from Sir James Bevan, Chief Executive of the Environment Agency, to Lord Hollick, Chair of the Industry and Regulators Committee, 7 December 2022: <https://committees.parliament.uk/publications/33338/documents/180401/default/>

225 [Q 97](#) (Sir James Bevan)

226 [Q 137](#) (Thérèse Coffey MP)

227 [Q 138](#) (Thérèse Coffey MP)

222. *We recommend the Government ensures adequate funding is available to the Environment Agency to inspect and enforce environmental offences by water companies.*

Open data

223. The Environment Agency hold data on pollution incidents, but do not make this data public. Sir James told us that “When we know about spills and we have data that is relevant to that, we share it with Ofwat.”²²⁸ Mr Black was positive about Ofwat’s information sharing relationship with the Environment Agency, saying “we work very well [together]”.²²⁹
224. Mr Cox also praised the working relationship he had with the Environment Agency while Chair of Ofwat, but said he “cannot deny that this summer ... [has] shown that there needs to be a better-defined system about environmental regulation, pollution control and holding to account.” Mr Cox said that Ofwat has called on companies for several years to endorse the principles of open data, but feels “the barrier is the companies accepting that open data is a good thing”. We asked him if he believes Ofwat has the power to compel companies to make their data open, to which he said the Environment Agency “probably have the powers to do it more than Ofwat”.²³⁰ He recommended that “Regulators should require all companies to commit to open data, in a useable form, so that customers can see in real, or near real, time the environmental performance of their sewerage network and sewage works.”²³¹
225. Mr Black expressed that he was “really disappointed” that some companies were not sharing their data openly, and flagged that there is a live review of the issue at the moment in the sector.²³² He highlighted that more open data is “part of the Government’s plan” and that Ofwat had recently held a roundtable with senior company executives on open data.²³³ Mr Coucher said Ofwat “want to find ways in which we can get that information and make it publicly available, with an obligation on water companies to do that.” However, he expressed uncertainty that Ofwat has powers to compel water companies to make data public.²³⁴
226. The water companies we heard oral evidence from all expressed support for open data. Lawrence Gosden, Chief Executive of Southern Water, said information about storm overflow use was “fully publicly available through a really easy to use portal on our website. We also have that portal directly electronically connected to the Surfers Against Sewage app.”²³⁵ Sarah Bentley, Chief Executive of Thames Water, said “We are working through a live monitoring pilot which will be completed by the end of this year. We are on track for that and have committed to providing live discharge notifications.”²³⁶ Peter Perry, CEO of Dŵr Cymru Welsh Water, said his organisation shares open data on environmental performance.²³⁷

228 [Q 92](#) (Sir James Bevan)

229 [Q 124](#) (David Black)

230 [Q 78](#)

231 Supplementary written evidence from Jonson Cox ([TW0034](#))

232 [Q 124](#) (David Black)

233 [Q 122](#) (David Black)

234 [Q 124](#) (Iain Coucher)

235 [Q 115](#) (Lawrence Gosden)

236 [Q 115](#) (Sarah Bentley)

237 [Q 118](#) (Peter Perry)

227. The Environment Act 2021 amended the Water Industry Act 1991 to require water companies to publish the following information in a readily accessible form the public can understand in near real time:
- That there has been a discharge from a storm overflow;
 - The location of the storm overflow;
 - When the discharge began;
 - When the discharge ended.²³⁸
228. The Government’s Storm Overflows Discharge Reduction Plan, which sets environmental targets, states water companies must make this reporting available no later than 2025.²³⁹ The Secretary of State highlighted that Thames Water “has decided to proactively make [its] data” on storm overflow monitoring available.²⁴⁰ She said the information from monitoring outlets “has to be made public by the end of 2024 or 2025”.²⁴¹
229. **Water companies should commit to providing public, open data in a useable form on the environmental performance of their sewerage network and sewage works. Customers should be able to see how water companies are affecting their areas in real or near-real time, and regulators should have access to this information in order to ensure that water companies are fulfilling their duties. It is welcome the Environment Act 2021 amended the Water Industry Act 1991 to require companies to provide open data, but no detail about how such plans will be implemented have yet been outlined.**
230. *The Government, Ofwat, and the Environment Agency should publicly outline their plans to ensure open data on environmental performance is provided by companies as a matter of priority.*

Government policy and strategy

Storm Overflows Discharge Reduction Plan

231. In August 2022 the Government published its Storm Overflows Discharge Reduction Plan.²⁴² The plan requires water companies to achieve several targets, including that by 2035, water companies will have to improve all storm overflows discharging into or near designated bathing water, and improve 75 per cent of overflows discharging to high priority nature sites. By 2050, this will apply to all remaining storm overflows covered by the targets, regardless of location. The Plan will be reviewed in 2027 to consider where the Government can go further, taking account of innovation and efficiencies.
232. The Plan also states that water companies will be required to publish discharge information in near real time as well as committing to tackling the root causes of the issue by taking steps to improve surface water drainage.

238 Environment Act 2021 [section 81](#)

239 Department for Environment, Food and Rural Affairs, ‘Storm overflows evidence project’: <https://www.gov.uk/government/publications/storm-overflows-evidence-project> [accessed 4 January 2023]

240 [Q 144](#) (Thérèse Coffey MP)

241 [Q 131](#) (Thérèse Coffey MP)

242 Department for Environment, Food and Rural Affairs, *Storm Overflows Discharge Reduction Plan* (August 2022): https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1101686/Storm_Overflows_Discharge_Reduction_Plan.pdf [accessed 4 January 2022]

It outlines the expectation that water companies ensure their infrastructure keeps pace with increasing external pressures, such as urban growth and climate change, without these pressures leading to greater numbers of discharges.

233. The Plan sets out the Government’s expectation that Ofwat will challenge, support and enable water companies to meet the targets set out, and enable investment to follow investigations as quickly as possible without waiting for the next Price Review period. It called for Ofwat to incentivise companies to meet the targets as soon as possible and go beyond them if this is supported by customers, to challenge companies to meet their public commitments, and to actively support companies in the use of green infrastructure where it is the most appropriate and best value approach.
234. Mr Gosden viewed the Plan as setting out a “minimum” and said Southern Water will seek to accelerate meeting its targets.²⁴³ Mr Lloyd similarly argued that the Plan is “too little too late” and noted that some water companies have already committed to meeting its targets earlier than the prescribed dates.²⁴⁴ Mr Linley-Adams added that the Plan seems to “allow water companies decades more to deal with [the] problem”.²⁴⁵
235. Ms Ong criticised the Plan for not setting “environmental targets and ambitions at that outcome level”, instead listing specific outputs such as not allowing storm overflows to discharge above an average of 10 rainfall events per year by 2050. She said an outcomes-based approach “would allow companies to be more innovative”.²⁴⁶
236. Ms Bentley raised concern that the Plan exhibited a disconnect between DEFRA and regulators. She highlighted that “DEFRA targets are about the number of sites that are improved, while Ofwat has a proposal out at the moment for the number of events per storm overflow.”²⁴⁷
237. Other witnesses argued the Plan needs to be part of a more joined-up approach across Government more generally. Mr Barker said “putting all the onus on the water companies, on the discharge end of it, ... does not face up to the reality” of the causes of storm overflow overuse. He posited that surface run-off from areas that combined sewers serve, such as roads and industrial estates, are significant contributors to storm overflow use: “It would make a lot more sense, in order to manage storm overflows, if [the Plan] were part of a more coherent and integrated effort to manage surface water better in the urban environment.” This effort would cut across DEFRA, the Department for Levelling-Up, Housing and Communities, and the Department for Transport.²⁴⁸ Mr Lloyd similarly said the Plan “is very focused on just the water industry and fails to grasp the holistic approach ... It needs to set a statutory objective to bind in all other sectors—local authorities, housing developers, highways agencies.”²⁴⁹

243 [Q 106](#) (Lawrence Gosden)

244 [Q 20](#) (Mark Lloyd)

245 [Q 20](#) (Guy Linley-Adams)

246 [Q 11](#) (Annabelle Ong)

247 [Q 106](#) (Sarah Bentley)

248 [Q 11](#) (Prof Ian Barker)

249 [Q 20](#) (Mark Lloyd)

238. Both Mr Dunne and Mr Black welcomed the Plan.²⁵⁰ Mr Black said companies will reflect the Plan in their business plans which they submit to Ofwat. However, he noted that of plans Ofwat had already received, “Many companies still have not adequately reflected the Government’s overflows plan in their planning process.”²⁵¹
239. Davide Minotti, Deputy Director of Water Services at DEFRA, said that the Government are “certainly not going to wait until 2050” to make the £56 billion investment the Storm Overflows Discharge Reduction Plan predicts will be needed to reduce storm overflow overuse. The Secretary of State emphasized that the Plan will be reviewed in 2027. She set out that if the Government “could [take steps to reduce storm overflow overuse] a lot more quickly, without it being massive on bills, of course I would want it done more quickly.” The Secretary of State said innovation could help in reducing storm overflow overuse more quickly, and that while water companies should invest in this innovation, she is considering if some of DEFRA’s research budget could be used.²⁵²
240. **We welcome the Government’s Storm Overflows Discharge Reduction Plan and its expectation that water companies reduce their use of storm overflows to their original intended use—during exceptional periods of rainfall. However, we recognise that there are concerns over whether the targets in the Plan are sufficiently ambitious, especially in terms of its 2050 goal for reducing storm overflow use. We also recognise that tackling storm overflow overuse will require a joined-up approach across government and regulators, which the plan currently lacks.**
241. *We recommend that the Government’s commitment to a mandatory review of the Storm Overflows Discharge Reduction Plan in 2027 is used as an opportunity to set stretching targets to reduce storm overflow overuse. We would welcome Defra’s research budget being used to examine how these more stretching targets could be met. In the meantime, Ofwat must ensure that significant incentives are in place to encourage companies to meet the targets in the Plan ahead of prescribed dates. We also recommend that a National Water Strategy should include a co-ordinated approach to reducing and preventing water pollution.*

250 [Q 5](#) (Philip Dunne MP) and [Q 122](#) (David Black)

251 [Q 122](#) (David Black)

252 [Q 135](#) (Thérèse Coffey MP)

CHAPTER 6: FINES, PENALTIES, AND ENFORCEMENT

Fines and penalties

242. The Environment Agency’s annual water and sewerage company performance assessment for 2021, published in July 2022, found that the performance of water companies was at its lowest ever level and most companies’ performance was declining. The Environment Agency argued that despite continuing enforcement action against those breaching environmental laws, water companies remain undeterred by the penalties currently being issued by the courts, calling for courts to impose much higher fines for serious and deliberate pollution incidents.²⁵³
243. The Agency’s then-Chair, Emma Howard Boyd, said that the Environment Agency “would like to see prison sentences for Chief Executives and Board members whose companies are responsible for the most serious incidents”, and for company directors to be “struck off so they cannot simply delete environmental damage from their CV and move on to their next role”.²⁵⁴
244. On 3 October 2022, then-Secretary of State for Environment, Food and Rural Affairs, the Rt Hon Ranil Jayawardena MP, announced that he would bring forward proposals to raise the limit on civil penalties that the Environment Agency can directly impose on water companies from £250,000 to up to £250 million. The Variable Monetary Penalties (VMPs), which offer a quicker method of enforcement than lengthy and costly criminal prosecutions, can be issued for more serious offences, including where there is evidence of negligence or mismanagement or when there is a serious environmental impact.²⁵⁵
245. Prof Barker said that the Environment Agency has moved towards having fewer prosecutions and more civil sanctions, noting that civil sanctions provide a direct benefit in that sums are paid to benefit the environment, but that they do not have the same level of publicity or reputational damage as prosecutions.²⁵⁶ Guy Linley-Adams, of Salmon and Trout Conservation, suggested that civil penalties should not be used in cases of water pollution, arguing that they are “extremely attractive” to companies because they avoid the “useful stigma” that is attached to prosecution.²⁵⁷
246. Professor Catherine Waddams, a member of the Centre for Competition Policy at the University of East Anglia, said that fines “may not be” at the right level and there is some evidence that it is “worth risking the fine” by not meeting standards. She said that she is “personally in favour of much stronger sanctions for individuals”, arguing that it might concentrate minds if there was a risk that those responsible could be unable to participate in boards as a result of their actions.²⁵⁸ She noted an occasion during her time

253 Environment Agency, *Water and sewage companies in England: environmental performance report 2021*, (22 July 2022): <https://www.gov.uk/government/publications/water-and-sewerage-companies-in-england-environmental-performance-report-2021/water-and-sewerage-companies-in-england-environmental-performance-report-2021> [accessed 22 December 2022]

254 *Ibid.*

255 Ofwat, ‘Water companies face new penalties up to £250million’, (3 October 2022): <https://www.gov.uk/government/news/water-companies-face-new-penalties-up-to-250million> (October 2022) [accessed 22 December 2022]

256 Q 14 (Annabelle Ong)

257 Q 28 (Guy Linley- Adams)

258 QQ 48–49

on the board of Ofwat where she was involved in fining a water company that had deliberately lied to the regulator. In this particular case, she explained that the entire management and board of the company had been replaced by the time the fine was levied.²⁵⁹

247. Alan Lovell, Chair of the Environment Agency, said that the Agency has the opportunity to take matters through the courts but this takes time and has to be proved to a criminal standard, noting that the current investigation into combined sewer overflows will be “a very long process”.²⁶⁰ He said that he was “quite delighted” with the Government’s proposal to increase the amount that the Agency can levy in Variable Monetary Penalties, arguing that this will give the regulator “a much bigger stick with which to go after bad behaviour among water companies”. He said that this still requires a criminal standard of evidence and is not a simple process, but that it will “tip the balance” in terms of discussions with water companies and should make a significant difference. He said that he hoped the Government “will rapidly be able to deliver on that commitment”²⁶¹.
248. Sir James Bevan, Chief Executive of the Environment Agency, said that the Agency normally always prosecutes when there is evidence of serious wrongdoing. However, he said that the Environment Agency has increasingly been using enforcement of undertakings as an option. He emphasised that prosecution is a “key weapon” for the Agency but explained that while they are doing less of it, this is partly down to resource constraints, as well as because it is “broadening the palette of options” available to it.²⁶²
249. David Black, Chief Executive of Ofwat, said that the regulator’s power to fine companies 10 per cent of their turnover is “quite substantial” but there “may be further scope for change” given that water companies are asset-intensive businesses. However, he argued that the current penalties imposed by Ofwat and the Environment Agency provide “very serious challenge to companies and their investors”, stressing that it is “now getting very painful for shareholders and regulators are seeing changes”²⁶³. Mr Coucher said that Ofwat would like to see greater powers to debar directors from companies that are “egregiously and continually poorly performing”, meaning that they cannot take up new, senior positions within the regulated sector.²⁶⁴
250. The Secretary of State felt that regulatory fines and penalties are adequate, stressing that the Government had “listened to Ofwat” and provided it with powers to modify licences. She explained that while Ofwat does not have the power to debar companies or executives, “the Environment Agency does, where appropriate”.
251. The Secretary of State said that she was “very keen” for the Environment Agency to use the powers that it has. She noted that for criminal prosecutions by the Environment Agency, “unlimited fines are possible, but the judge decides what the fines will be. To date, the largest fine a judge has given has been about £5 million”. She outlined that the Government is intending to

259 [QQ 48, 51](#)

260 [Q 97](#) (Alan Lovell)

261 *Ibid.*

262 [QQ 97, 103](#) (Sir James Bevan)

263 [Q 119](#) (David Black)

264 [Q 123](#) (Iain Coucher)

consult on its proposals in relation to Variable Monetary Penalties in “this quarter, or perhaps stretching into just the other side of Easter [2023]”.²⁶⁵

252. **It appears that for some time, regulatory deterrents such as penalties and fines have been insufficient to ensure an acceptable level of performance by water companies, particularly in relation to the environment, where performance is at its lowest ever levels. We welcome that some recent fines and penalties have been at a more appropriate level but remain concerned that they may not be a sufficient deterrent. The length of enforcement processes can result in those in penalties being applied long after those responsible have left the company.**
253. **Recent Government proposals to increase substantially the limit on the Variable Monetary Penalties that can be directly imposed by the Environment Agency on companies could help to provide strong enforcement in a more reasonable timeframe. However, it is concerning that the Environment Agency has not used these powers often in the past, a situation possibly brought about by the Agency’s shortage of resources for enforcement.**
254. **While civil penalties can help to bring about enforcement more quickly, it is important that regulators prosecute criminal behaviour. It is alarming that the Environment Agency is prosecuting less due to resource constraints.**
255. *The Government should deliver on its proposals to increase the limit on Variable Monetary Penalties for serious offences committed by water companies. The Government should ensure the Environment Agency has adequate funding to use its new powers effectively and prosecute criminal behaviour in the sector.*
256. *There is a need for greater individual accountability for executives and directors of companies that are responsible for serious and deliberate pollution incidents, including criminal prosecution where appropriate. The Government should give Ofwat powers to prevent directors of companies that are responsible for serious pollution incidents from continuing to work in the sector.*

Special administration and changes of ownership

257. Under the Water Industry Act 1991, Ofwat is responsible for granting water supply licences.²⁶⁶ Licences continue in force, unless revoked or suspended in accordance with their conditions, for the period specified in or determined by the licence.²⁶⁷ However, the Water Industry Act 1991 gives Ofwat the power to transfer businesses to new owners through a special administration process under certain conditions, including where a company fails to meet its legal obligations or where it is unable to finance its functions.²⁶⁸
258. Jonson Cox, a former Chair of Ofwat, outlined that in 2021 Ofwat brought about what was called a “virtual special administration” of Southern Water, as the company was “failing on many fronts, and we had given investors

265 [Q 138](#) (Thérèse Coffey MP)

266 Water Industry Act 1991, [section 17A](#)

267 Water Industry Act 1991, [section 17F](#)

268 Water Industry Act 1991, [sections 23, 24 and 25](#)

notice to put more money in or we would take control of the situation”. He said that Ofwat, with the assistance of the owners, ran a “competitive auction” to bring new capital into the company.²⁶⁹ In August 2021, Macquarie Asset Management announced that it had reached an agreement to acquire a majority stake in the company and would invest “over £1 billion in new equity to recapitalise the business”.²⁷⁰

259. Mr Cox explained that the company’s previous owners lost a “very large share of their investment” and stressed that it was an important message that if assets are not run well, investors will lose a “big part” of their investment.²⁷¹ He argued that it would be good to have a more competitive process for licences and that licence powers “were underused by regulators”, given their ability to “control behaviour”. However, he was not sure that the current problems in the sector are best answered by looking at duties and licences, as there is a “simpler way forward”.²⁷²
260. Prof Waddams said that she does not think that Ofwat has a fundamental reluctance to take away a licence for serious infringements, and while it would lead to costs that would need to be carefully considered, Ofwat felt that it could find someone to take the licence on if necessary.²⁷³
261. Of licence removal, Sir James said that “the more stick and carrot there is, the better. That is an obvious stick”. He explained that the Environment Agency has had “those conversations” with Ofwat about particular companies and while the question is about how to sustain public water supply after a licence is stripped, “there are ways round that”. He noted that at a lower level, the Environment Agency does suspend licences and permits when water companies do not perform at the necessary level.²⁷⁴
262. Mr Black said that the special administration powers to take away water company licences are “part of the toolkit” for Ofwat but they have a high bar to be applied, requiring a high burden of proof and approval from the Secretary of State and the courts, so “they will not be used lightly”. He argued that Ofwat had used the threat of these powers to achieve changes at companies and has “come close to looking at the need” to use them.²⁷⁵
263. Mr Black said that introducing competition for water company licences is “certainly an idea worth considering” but emphasised that there are upsides and downsides. He argued that if licences were expiring ahead of a bidding process, it “might be difficult” to get companies to focus on and make provisions for the long term. He instead argued in favour of introducing more powerful incentives on companies in the existing model, with companies held to account.²⁷⁶
264. The Secretary of State said that there have been examples of water companies being taken over, as “sometimes investors have come in and not realised

269 [Q 83](#)

270 Macquarie Asset Management, Press Release: ‘Macquarie Asset Management agrees to acquire majority stake in Southern Water’ (August 2021): <https://www.macquarie.com/au/en/about/news/2021/macquarie-asset-management-agrees-to-acquire-majority-stake-in-southern-water.html> [accessed 1 February 2023]

271 [QQ 79, 83](#)

272 [Q 86](#)

273 [Q 49](#)

274 [Q 103](#) (Sir James Bevan)

275 [QQ 119, 123](#) (David Black)

276 [Q 123](#) (David Black)

quite the demands that may be made on them”. However, she expressed her view that “it is for Ofwat to decide how best to use its powers”.²⁷⁷

265. In relation to introducing greater competition for licences, the Secretary of State said that she is “not sure” that opening up the non-household water market “has had quite the impact that may have been hoped for”, and also pointed to the impacts of the introduction of competition to the retail energy market.²⁷⁸
266. **Ofwat’s special administration powers allow it to change the ownership of water companies that are falling short in meeting their responsibilities. This a powerful tool that has the potential to be used more widely where companies have been found not to have been meeting their obligations.**
267. *Ofwat should consider whether to be more proactive in using these powers to change the management of continued poor performers in the sector.*

277 [Q 143](#) (Thérèse Coffey MP)

278 [Q 145](#) (Thérèse Coffey MP)

CHAPTER 7: DEBT, DIVIDENDS, AND FINANCIAL RESILIENCE

Debt and dividends

268. Under its statutory duties, Ofwat must “secure that water companies can (in particular through securing reasonable returns on their capital) finance the proper carrying out of their statutory functions”.²⁷⁹
269. Professor David Hall of the University of Greenwich published a paper in January 2022 highlighting that between 2010 and 2021, English water and sewerage companies paid shareholders a total of £18.9 billion in dividends, an annual average of £1.6 billion. He suggested that the dividend payments have “significantly” reduced the money available for investment by companies and increased the cost of water and sewerage to consumers “by an average of £69 per household per year over the last 12 years”.²⁸⁰ Dr Kate Bayliss of SOAS University of London argued that water companies have used “financial engineering to create returns for shareholders”, including by restructuring company finances to accrue high debts while paying dividends to shareholders”.²⁸¹
270. In July 2022, Ofwat published a consultation on proposals to improve financial resilience in the sector, which would give the regulator extra powers to stop water companies making dividend payments if their financial resilience is at risk. The proposals would also enable Ofwat to take enforcement action against companies that do not link dividend payments to performance, or those failing to be transparent about their dividend pay-outs.²⁸²
271. Ofwat Chief Executive David Black explained that the proposals would give Ofwat the power to “lock money into the company” if its credit rating fell to a level “deemed insufficient for a water company”. He said that the change “has been fiercely resisted by companies”, who may choose to refer the licence conditions to the Competition and Markets Authority (CMA).²⁸³
272. Jonson Cox, former Chair of Ofwat, said that a “very long-standing mantra” at Ofwat before his tenure was that capital structure was “for the companies to determine”. He argued that it was “unfortunate” that regulators had allowed companies to take ownership of capital structures, emphasising that if a public utility is owned privately then it should be “held to a higher standard than other businesses”. He explained that in the 2000s, investment banks began to realise their ability to acquire water companies and “put significantly more” debt onto their capital structures. He suggested that most water companies with highly leveraged structures had “run into real difficulties”, requiring action to “bring about significant reinvestment”²⁸⁴.
273. Emma Clancy, Chief Executive of the Consumer Council for Water, argued that the money put towards shareholder rewards and profits “could

279 Ofwat, ‘Our duties’: <https://www.ofwat.gov.uk/about-us/our-duties/> [accessed 22 December 2022]

280 David Hall, *Water and sewage company finances 2021: dividends and investment - and company attempts to hide dividends*, (January 2022): https://gala.gre.ac.uk/id/eprint/34274/14/34274%20HALL.Water_and_Sewerage_Company_Finances_%28Rev.2%29_2021.pdf [accessed 11 January 2023]

281 Written evidence from Kate Bayliss (TW0024)

282 Ofwat, ‘PN 27/22 Ofwat raises bar on financial resilience’, (28 July 2022): <https://www.ofwat.gov.uk/ofwat-raises-bar-on-financial-resilience/> [accessed 22 December 2022]

283 Q 130 (David Black)

284 QQ 79, 84

very much help” with the problems in the sector, but suggested that what customers “really want” is a level of transparency about what companies are being rewarded for.²⁸⁵

274. Peter Perry, Chief Executive of Dŵr Cymru Welsh Water, suggested that Dŵr Cymru Welsh Water, which operates on a non-profit basis, has “not had a problem raising finance” without paying dividends and is funded by debt on the bond market. He said that the company has “one of the best credit ratings in the utilities sector” and that it has been “oversubscribed” every time it has gone to the market. He argued that the retention of profits means Welsh Water has “very solid liquidity” which can be drawn on during shocks, which “works very well”²⁸⁶. However, other witnesses suggested that Welsh Water’s performance is not “significantly better” than its counterparts²⁸⁷ and that the non-profit model “is not a silver bullet”²⁸⁸.
275. On the other hand, Christine McGourty, Chief Executive of Water UK, argued that the model of companies raising a mix of debt and equity finance had delivered benefits, suggesting that “it is the dividends that enable the equity that funds the investment”. She also said that in the last year, three companies paid no dividends.²⁸⁹ Stuart Colville, Director of Policy at Water UK, said that the financial performance of companies over the last couple of years “does not quite match some of the stereotyping”, with a total return on regulated equity of 2.3 per cent in the 2020/21 financial year. He stressed that Ofwat has been “pushing down the cost of capital and effectively the assumed return for companies” during recent Price Reviews.²⁹⁰
276. Lawrence Slade, Chief Executive of the Global Infrastructure Investor Association, acknowledged that there have been disagreements between investors and the regulator over financial models, suggesting that investors have “the sense that the regulator has become too involved and too engaged” in regulating the funding models used by the sector. He argued that this element “should be one for company boards and not necessarily for the regulator”²⁹¹, a point also raised by other investors²⁹².
277. Lawrence Gosden, Chief Executive of Southern Water, and Sarah Bentley, Chief Executive of Thames Water, both emphasised that their companies had not paid dividends in recent years and that they were taking action to reduce debt levels. Mr Gosden suggested that in the long term it is “not sustainable” to have zero dividends.²⁹³
278. David Black, Chief Executive of Ofwat, said the regulator is “concerned” about debt and the financial resilience of water companies. He suggested that debt levels have “stabilised” rather than increased in recent years but that three companies in particular raise concerns: Thames Water, Southern Water and Yorkshire Water. He suggested that there has been progress with those companies but that Ofwat remains concerned that the licence is “still

285 [Q 40](#) (Emma Clancy)

286 [Q 113](#) (Peter Perry)

287 [Q 17](#) (Mark Lloyd)

288 [Q 40](#) (Emma Clancy)

289 [QQ 60, 64](#) (Christine McGourty)

290 [Q 64](#) (Stuart Colville)

291 [Q 71](#) (Lawrence Slade)

292 Written evidence from IFM Investors UK ([TWW0010](#))

293 [Q 106](#) (Lawrence Gosden) and [Q 113](#) (Sarah Bentley)

too permissive” and “does not set stringent enough standards of financial resilience”.²⁹⁴

279. Iain Coucher, Chair of Ofwat, said that the sector’s finances are currently “about 70 per cent” debt, explaining that Ofwat “would like to see it come down” to “about 60 per cent”, with Mr Black clarifying that Ofwat would like to see this reduction occur during the current Price Review period. Mr Black also pointed out that it is “important not just to look at the headline debt numbers”, as “other factors in the financial structure can add to the stresses”, including the use of derivatives.²⁹⁵
280. The Secretary of State said that Ofwat “thought there was an issue” in relation to dividends, “which is why, in the Environment Act [2021], powers were given on dividends” and related issues. She argued that “it is that unlocking of the private capital... that has led to investments” but recognised “some of the issues and dividends seeming to have been prioritised”. She stressed that the Government has responded to Ofwat’s concerns “and it is now over to Ofwat to deliver any changes that it thinks are necessary”.²⁹⁶
281. **It is clear that in the past, a number of water companies have been overly focused on maximising financial returns, including by increasing debt levels, at the expense of operational performance and protecting the environment. We welcome that some companies have exercised more restraint in recent years, in part due to tougher regulatory settlements as well as wider economic conditions.**
282. **While financial structures are usually a matter for company boards, water companies’ monopoly role in providing an essential service means that a higher standard should be demanded, especially in a sector of such importance to households and the environment. We support Ofwat’s increased interest in the financial structures of water companies and wholly support its proposals to amend licenses to ensure that dividends are linked to performance and companies are financially resilient.**

Executive pay

283. In February 2022, Ofwat Chief Executive David Black wrote to the chairs of water companies’ remuneration committees about performance-related executive pay. In the letter, Black explained that companies’ performance in some areas, and particularly the environment, “risks eroding trust and confidence in the sector”. He wrote that it is “essential that companies provide robust and clear explanations of performance related executive pay” and how this links to performance for customers, urging committees to give “particular consideration to the clarity of reasoning” for any awards made in relation to environmental performance, given the current concern in this area and ongoing investigations into compliance.²⁹⁷ In December 2022, Mr Black wrote a follow-up letter stressing that Ofwat’s board is “deeply concerned that, generally, companies have not taken sufficient action” to respond to the regulator’s measures. He wrote that Ofwat wants to be clear

294 Q 130 (David Black)

295 Q 130 (Iain Coucher)

296 Q 143 (Thérèse Coffey MP)

297 Ofwat, ‘Letter from David Black to Chairs of Remuneration Committees - Performance related executive pay for 2021–22’, (February 2022): <https://www.ofwat.gov.uk/publication/letter-david-black-remcos-performance-related-executive-pay-21-22/> [accessed 24 January 2023]

that it expects companies to “much better account for overall performance in making decisions on performance-related elements of executive pay.”²⁹⁸

284. The Rt Hon Philip Dunne MP, Chair of the House of Commons Environmental Audit Committee, said that there is a need to question whether some of the “very high” bonuses paid to executives of water companies that are in breach of their permits and licences “are appropriate for a public utility”.²⁹⁹ Wildlife and Countryside Link called on Ofwat to use powers under the Water Industry Act 1991 to limit payment of bonuses to water company executives who “consistently” breach their permits, arguing that this would disincentivise pollution.³⁰⁰
285. Mr Cox said that Ofwat has “intervened” with remuneration committees where it was not satisfied with their approach and would call in their Chairs to explain what is expected. He suggested that if he were still at Ofwat, he “would encourage it to think about going further on that”.³⁰¹
286. Ms Bentley said that part of Thames Water’s turnaround plan is being “responsible” on executive pay, with a “substantial proportion” of the management team’s bonus relating to environmental and customer measures. Mr Gosden said that three-quarters of executive pay at Southern Water is linked to performance, including environmental and customer service performance.³⁰²
287. Mr Black said that it is “really concerning” given the current environment and criticism of water companies that they “have not yet been more responsible in linking executive pay to performance”. He stressed that Ofwat is “currently looking” at payments and engaging with companies.³⁰³ He said that Ofwat needs to act in this space and is looking at how it can “bolster arrangements”, noting that companies made a commitment at PR19 to align executive pay to performance.³⁰⁴ However, Mr Black argued that it is not the regulator’s role to “micromanage executive pay”, suggesting that company boards and remuneration committees “need to take responsibility for making those decisions”.³⁰⁵
288. **Water company executives should not be able to receive substantial bonuses while their companies have missed performance targets and polluted the water environment, potentially in breach of their permits.**
289. ***We support Ofwat’s increased interest in executive pay, including its expectation that companies set out their proposed policies for performance-related executive pay during the next Price Review period. These proposals should ensure performance-related pay is***

298 Ofwat, ‘Letter to Chairs of Remuneration Committees regarding performance related executive pay’, (December 2022): <https://www.ofwat.gov.uk/publication/ofwat-letter-to-chairs-of-remuneration-committees-regarding-performance-related-executive-pay/> [accessed 24 January 2023]

299 [Q 2](#)

300 Written evidence from Wildlife and Countryside Link ([TWW0022](#))

301 [Q 86](#)

302 [Q 113](#) (Lawrence Gosden)

303 Ofwat, ‘Letter from the Chief Executive of Ofwat to Chairs of Remuneration Committees for all regulated water and wastewater and water-only companies, Performance related executive pay for 2021–22’, (18 February 2022): <https://www.ofwat.gov.uk/wp-content/uploads/2022/02/Letter-from-David-Black-to-RemCo-chairs-18-February-2022.pdf> [accessed 22 December 2022]

304 [Q 130](#) (David Black)

305 *Ibid.*

much more closely linked to performance, particularly in relation to the environment. Ofwat should set out further provisions to ban bonuses at companies who have been found to have caused serious pollution incidents as part of the conditions of water company licences.

Ownership models

290. Mr Dunne said that the nature of water companies' capital structure is so variable that it is difficult to get a "clear picture" of each company's activities, as while public companies have to make disclosures through annual reports, water companies that are owned by private equity companies are less transparent. He suggested that some water companies, particularly those owned by private equity, are more heavily indebted than others.³⁰⁶
291. Mr Cox said that in the 2000s, a "raft" of public listed water companies went private, leading to a "predisposition" for companies to look at water companies "as financial assets" rather than public service businesses.³⁰⁷ Water companies in England now consist of a mix of public listed and privately owned companies.
292. Asked whether water companies should be required to be publicly listed companies, Mr Gosden said that the water company licence already requires companies to act as if they are listed from a transparency point of view through an annual reporting process.³⁰⁸ Ms Bentley said that one can debate the pros and cons of different ownership models but argued that what is important is having "patient, long-term investors".³⁰⁹
293. Mr Black argued that requiring water companies to trade at least some of their shares publicly would "have some benefits", including minimum requirements for board governance and "the additional scrutiny that analysts bring when a company is listed". He noted the regulator's concerns around the highly indebted structures used by Thames Water, Southern Water and Yorkshire Water.³¹⁰
294. Mr Black acknowledged that Ofwat has replicated "to a large extent" the governance benefits of public listing by introducing licence requirements for governance standards, and stressed that Ofwat has real concerns about the performance of some listed companies, including South West Water. He said that it would be "wrong to pretend that listed companies are the answer to the problem", as being listed "does not guarantee good performance".³¹¹
295. The Secretary of State said that she does not think that the Government "should force companies to be publicly traded". She argued that private equity can work "in a variety of ways" and comprise of "different kinds of investors", including pension funds. She emphasised that there are examples of private equity owned water companies that are performing well and public listed companies that are performing less impressively, suggesting that "there is a role for both approaches".³¹²

306 [Q 2](#) (Philip Dunne MP)

307 [Q 79](#)

308 [Q 113](#) (Lawrence Gosden)

309 [Q 113](#) (Sarah Bentley)

310 [Q 130](#) (David Black)

311 *Ibid.*

312 [Q 143](#) (Thérèse Coffey MP)

296. **Some witnesses told us the introduction of private equity ownership to the water sector has been a driver in some companies focusing on financial performance rather than service delivery and securing resilience. This has led some privately owned companies to take on debt and introduce complex financial structures in order to pay out large returns, even where performance has been unacceptable. Requiring water companies to disclose information to the same standard as publicly listed companies has the potential to improve their governance and increase scrutiny of their financial arrangements.**
297. *Ofwat should ensure that water companies are subject to the same level of transparency as publicly listed companies, in order to improve transparency through the regular reporting cycle.*

CHAPTER 8: FUTURE WATER SUPPLY

298. Sir James Bevan, Chair of the Environment Agency, told us that every water company's business plan contains a graph with two lines. One tracks the rise in demand for water over the next 30 years, and the other the fall in the amount of water available. He said that in 20 years, the lines cross, a "point at which, unless we intervene, we do not have enough water for the country." It is critical that those lines do not cross.³¹³

Water transfers

299. Water infrastructure and storage capacity varies across different parts of England and Wales, as does levels of rainfall. Water transfers use new or existing infrastructure, such as dams, pipes, reservoirs, and canals, to transfer water from areas of surplus to areas of need.
300. Jonson Cox, former Chair of Ofwat, told us that water transfer schemes have existed since the Victorian era. Municipalities "jointly invested in schemes that transferred water from one region to another". Yet this only accounted for four per cent of water supply, a proportion which did not increase for "at least" a generation, if not considerably longer. Therefore, Ofwat recognised the need to build more water transfers.³¹⁴ Mr Cox said shortly after he joined Ofwat in 2012, the regulator "started on collaborative work with companies about how to transfer water across the country". He outlined that initially, some companies were less enthusiastic than others about transfer schemes because it would require them to "give up some headroom in its water resources for the benefit of another company." But the establishment of the Regulators' Alliance for Progressing Infrastructure Development (RAPID) in 2019, which brought regulators and companies together to work collaboratively on ensuring future water supply, put water transfers "on a different footing". Within a year of the establishment of RAPID, 18 strategic resource schemes had been established.³¹⁵
301. Sarah Bentley, Chief Executive of Thames Water, felt that "the strategic solutions we need" to ensure future water supply "are well set out". She pointed to the success of RAPID, and discussed how in the South East, "The six regional companies have joined together to form [a] group ... called Water Resource South East." The group are overseeing the development of six water transfer schemes which will be finished between 2030 and 2050. Ms Bentley felt that the challenge these schemes faced was being "deemed nationally significant infrastructure projects so that they can go through the appropriate planning and accelerate through", as this will require political will.³¹⁶
302. Mr Perry acknowledged Wales is "one of the wetter parts of the UK", and with the approval of the Welsh Government, Dŵr Cymru Welsh Water would support water transfers. However, he highlighted that water transfers are a politically and culturally sensitive issue in Wales following the Tryweryn flooding in 1965, where a rural community was flooded to create a reservoir to supply water to Liverpool and Wirral. Mr Perry said in order for Dŵr Cymru Welsh Water to support water transfers, criteria would need

313 [Q 98](#) (Sir James Bevan)

314 [Q 76](#)

315 [Q 81](#)

316 [Q 107](#) (Sarah Bentley)

to be in place. This would include “no detriment to our customers or our environment” and certainty “that the commercial rate for that transfer was appropriate.”³¹⁷

303. David Black, Chief Executive of Ofwat, told us that at the last Price Review (PR19), there was insufficient co-ordination across companies, and there was frustration within Ofwat at companies failing to discuss water transfers. Yet he was happy to report that he thinks “there has been substantial change” because of the establishment of RAPID. He also noted that the Environment Agency’s regional water resource management planning process and the National Framework for Water Resources foster “much better co-ordination at the regional level”—even if there are disparities between regions.³¹⁸
304. Alan Lovell, Chair of the Environment Agency, said that “there are some decent examples around” of water companies working together on water transfers. This includes “water transfer arrangements in place from north Wales into the Midlands that Severn Trent Water is looking after” and a reservoir in Portsmouth Water’s district which will primarily be used by people in Southern Water’s remit.³¹⁹
305. Mr Black said that costs are decided by both companies using a “bulk supply framework”. Ofwat has been working with the water sector “to make sure that the framework is fit for purpose.” There are challenging issues, for example, about sharing water resources in a drought. But Mr Black felt this “can be resolved and we are working through that with the companies.” He also said that there are environmental challenges to water transfers, such as the potential transfer of invasive species, which must be worked through.³²⁰
306. **The Regulators’ Alliance for Progressing Infrastructure Development’s plans to increase the levels of water transfer between regions are set to be very important in using existing water resources more effectively. The regulators should continue to ensure that companies work co-operatively in this area.**

Reservoirs

307. Reservoirs store vast quantities of water that can be used in times of need, such as during drought conditions. Ms Bentley told us that London and the South East particularly lack enough reservoirs—London has roughly a month’s worth of raw water in storage. She said that if London had more reservoirs, the drought restrictions put in place in summer 2022 would not have been needed.³²¹
308. Yet despite the need for reservoirs, we heard that under current plans, not a single major one will have been built in the UK between 1991 and 2029.³²² In 2018, the National Infrastructure Commission published a report on preparing for a drier future, which found that in order to avoid the risk of a severe drought, more than £20bn of investment in new infrastructure

317 [Q 107](#) (Peter Perry)

318 [Q 126](#) (David Black)

319 [Q 98](#) (Alan Lovell)

320 [Q 126](#) (David Black)

321 [Q 107](#) (Sarah Bentley)

322 [Q 98](#) (Alan Lovell)

such as reservoirs is needed over the next 30 years, alongside a reduction in leakages.³²³

309. Mr Lovell said that not building a major reservoir for 30 years was leaving the country “exposed”, but PR24 would “be critical to enable some investment by the water companies” and take a step in the right direction.³²⁴

310. Prof Barker highlighted the case of Cheddar Reservoir:

“In 2014, the Environment Agency confirmed to Bristol Water that it was happy for a proposed Cheddar reservoir to go ahead, but Ofwat then refused to fund it on the basis that the case had not been made. Subsequently, it has been recognised that Cheddar is potentially an important strategic water resource for water security in the south-west of England.”³²⁵

311. Mr Black told us that planning controls have also impeded the creation of reservoirs in the past: “the last time a major reservoir—the Abingdon reservoir—went to planning process, in 2011, it failed. It did not get planning consent on the grounds that it was not immediately needed.” He said the planning process will need to align with the needs of water resource management.³²⁶

312. The Secretary of State told us:

“I see the challenges that local farmers have, never mind water companies, for getting planning permission for reservoirs. I am hoping that you will see stuff coming in the new [National Policy Statement for Water Resources Infrastructure] that will help with clarity for the planning process.”³²⁷

313. Davide Minotti, Deputy Director for Water Services at Defra, said that 20 new large infrastructure projects are currently being considered, five of which are reservoirs.³²⁸

314. **Under present plans, the UK will not have built a single new major reservoir between 1991 and 2029. The Government, regulators, and companies must work together to deliver more reservoirs to meet the UK’s future water needs. Failure to do so will result in a less resilient, secure water supply that risks leaving households without water during extreme weather conditions that are becoming more frequent due to climate change. We welcome the Government’s intention to address the planning issues impeding reservoir development in the National Policy Statement for Water Resources Infrastructure.**

315. *The Government should set out plans to accelerate the planning process for reservoirs, including by designating, and if necessary amending, its National Policy Statement for Water Resources Infrastructure as a matter of priority.*

323 National Infrastructure Commission, *Preparing for a drier future: England’s water infrastructure needs* (April 2018): <https://nic.org.uk/app/uploads/NIC-Preparing-for-a-Drier-Future-26-April-2018.pdf> [accessed 22 December 2022]

324 [Q 98](#) (Alan Lovell)

325 [Q 9](#) (Prof Ian Barker)

326 [Q 126](#) (David Black)

327 [Q 141](#) (Thérèse Coffey MP)

328 [Q 141](#) (Davide Minotti)

Changing consumer behaviour

316. Sir James stated: “Changing behaviour and ensuring that we all cherish water and treat and use it wisely will be one of the most powerful interventions we can make” in ensuring future water supply.³²⁹ The National Framework for Water Resources, established by the Environment Agency in 2020 to explore long-term water needs, outlined a potential shortage of 3,435 million litres of water per day in England by 2050 if no action is taken.³³⁰ The Consumer Council for Water said roughly “one third of this gap needs to be plugged by customer behaviour change, yet this is where the least progress is being made.”³³¹
317. Sir James told us that each person in England uses an average of 140 to 145 litres of water a day. This compares to 80 litres a day in Denmark.³³² Alan Lovell, Chair of the Environment Agency, said that it is essential to reduce consumer demand to a maximum of 110 litres a day to ensure future supply.³³³
318. We heard a variety of ideas about how consumer demand might be reduced. Effective consumer messaging campaigns³³⁴ and water metering³³⁵ could encourage consumers to consciously reduce the amount of water they use—for example, by taking shorter showers. Devices such as water-efficient shower heads and toilet parts can be provided by companies to reduce demand.³³⁶
319. Water efficiency labelling may encourage consumers to make informed choices to reduce water use,³³⁷ which the Secretary of State said was one approach the Government was taking.³³⁸ The Government’s Environmental Improvement Plan sets out that over the next decade, the Government will deliver mandatory water efficiency labelling.³³⁹
320. At PR19, Ofwat set each company a target of reducing per capita consumption of water. However, no company is on target,³⁴⁰ and Ofwat will waive penalties until at least 2025 because of a rise in working from home, which has increased demand for water.³⁴¹
321. The Secretary of State highlighted that in January 2023, Parliament approved The Environmental Targets (Water) (England) Regulations 2023.³⁴² These regulations, which were required by the Environment Act 2021, set a target

329 [Q 98](#) (Sir James Bevan)

330 Environment Agency, *Meeting our future water needs: a national framework for water resources – accessible summary* (March 2020): <https://www.gov.uk/government/publications/meeting-our-future-water-needs-a-national-framework-for-water-resources-accessible-summary> [accessed 20 January 2023]

331 Written evidence from Consumer Council for Water ([TWW0019](#))

332 [Q 100](#) (Sir James Bevan)

333 [Q 98](#) (Alan Lovell)

334 [Q 59](#) (Christine McGourty) and [Q 100](#) (Sir James Bevan)

335 [Q 98](#) (Alan Lovell)

336 [Q 100](#) (Sir James Bevan)

337 [Q 100](#) (Sir James Bevan) and [Q 35](#) (Emma Clancy)

338 [Q 142](#) (Thérèse Coffey MP)

339 Department for Environment, Food and Rural Affairs, *Environmental Improvement Plan 2023* (31 January 2023): https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1133967/environmental-improvement-plan-2023.pdf [accessed 31 January 2023]

340 [Q 127](#) (David Black)

341 Matt Oliver, ‘Water companies to dodge fines for missing targets because of rise in home working’, *The Telegraph* (14 August 2022): <https://www.telegraph.co.uk/business/2022/08/14/water-companies-dodge-fines-missing-targets-rise-home-working/> [accessed 4 January 2023]

342 [Q 142](#) (Thérèse Coffey MP)

of a 20% reduction in the amount of water supplied per day per head of population in England by March 2038.³⁴³

Responsibility for changing consumer behaviour

322. Mr Lovell said that “it is primarily the role of the water companies to have dialogue with their customers” on reducing water usage.³⁴⁴ Mr Cox held the same view, saying water companies are best placed to persuade customers about the importance of water conservation and water efficiency—mainly because water companies can be held to their license obligations to work with customers.³⁴⁵
323. Ms Bentley told us that Ofwat provides companies with a “fixed revenue settlement over the five-year period irrespective of consumption for customers who are metered”, meaning that companies are “absolutely incentivised to roll out metering and reduce demand” through targets set by the regulator. She said Thames Water are working “with the Consumer Council for Water and other bodies to encourage better water consumption”.³⁴⁶ Lawrence Gosden, Chief Executive of Southern Water, said his company wants to support customers in reducing usage, pointing to its “You Save, We’ll Pay Scheme”. Under the scheme, small businesses that “could find ways to be water efficient” would not only “save by not paying for that water on their water meter but [Southern Water] would double the return, so we paid them the same money again.”³⁴⁷
324. Mr Perry said that “producing less water actually benefits [Welsh Water] in cost efficiency” which is a huge incentive for reducing demand.³⁴⁸ While he recognised that Dŵr Cymru Welsh Water “[has] to engage with customers to encourage them to use less,”³⁴⁹ he also noted the Consumer Council for Water, Ofwat, the Environment Agency, and Natural Resources Wales had begun messaging on water reduction. He suggested the Government should also be involved, as “it is about joined-up messaging from the Government to the companies through our regulators.”³⁵⁰ Christine McGourty, Chief Executive of Water UK, said companies are doing “a huge amount” on messaging, but “companies need help and support from policymakers.” For example, through introducing water efficiency labelling of white goods.³⁵¹
325. Emma Clancy, Chief Executive of the Consumer Council for Water, told us that the Council “would definitely like to see Ofwat place far greater emphasis on reducing consumption and encouraging behavioural change as part of the price review.” She suggested “a body such as RAPID or a similar group could address [the demand reduction] side of things to help people make good decisions and begin to value water.”³⁵²
326. The Government’s Environmental Improvement Plan stated that DEFRA is “working to develop additional policy options” on the issue of demand

343 The Environmental Targets (Water) (England) Regulations 2023 ([SI 2023/93](#))

344 [Q 100](#) (Alan Lovell)

345 [Q 87](#)

346 [Q 108](#) (Sarah Bentley)

347 [Q 108](#) (Lawrence Gosden)

348 [Q 108](#) (Peter Perry)

349 [Q 107](#) (Peter Perry)

350 [Q 108](#) (Peter Perry)

351 [Q 59](#) (Christine McGourty)

352 [Q 35](#)

management, including “supporting communications campaigns on the value of water and how we can use it more efficiently”.³⁵³

327. **Reducing water demand is crucial to ensuring sufficient water supplies. The UK has one of the highest water usage figures per capita in Europe and while the Government has set an ambitious target to reduce consumption, clearer detail is needed on how it, regulators and companies plan to address this issue. The Regulator’s Alliance for Progressing Infrastructure Development (RAPID) has proved to be a successful model for co-operation, and given the need for co-operation to reduce consumption, a similar alliance could be used to focus on this area.**
328. *The Government should set out in a National Water Strategy how it envisions meeting its targets for reducing water demand. This should involve setting out new policies and setting clear expectations for regulators and companies.*
329. *Ofwat, the Environment Agency and water companies should work closely together, as they do with RAPID, in order to set out schemes and proposals to reduce water demand.*

Water metering

330. Water meters are devices that can be fitted in people’s homes to track how much water they are using and subsequently the household’s water bill. Ms Clancy told us that around 60 per cent of people currently have water meters installed.³⁵⁴
331. In 2019, the University of Southampton published research which found water metering can reduce overall water consumption by 22 per cent by the time the customer receives their fourth metered bill, around two years after meter installation.³⁵⁵ Mr Gosden reflected that water metering had contributed to Southern Water supplying 200 million litres of water a day less than it did 30 years ago, despite population growth in this time.³⁵⁶ Arqiva, a smart water meter provider, estimated that “if just one million smart water meters were to be fitted in the UK each year for the next 15 years, then by the mid-2030s, savings of at least one billion litres of water a day (1,000 Mld) could be made”.³⁵⁷
332. Water metering is not currently mandatory. Meters are installed by companies, either at the request of the consumer or, in water-stressed parts of the country, as a matter of course. Mr Black said that some companies were doing interesting work on smart metering, but that more leadership and co-operation across the sector was needed.³⁵⁸ Iain Coucher, Chair of Ofwat, told us that companies “are really promoting the installation of water meters”—for example, by speaking to customers who ring up their call centres about

353 Department for Environment, Food and Rural Affairs, *Environmental Improvement Plan 2023* (31 January 2023): <https://www.gov.uk/government/publications/environmental-improvement-plan> [accessed 31 January 2023]

354 [Q 35](#)

355 Carmine Ornaghi, Micro Totin, ‘The effects of the universal metering programme on water consumption, welfare and equity’, *Oxford Economic Papers*, vol. 73, issue 1 (2021), pp 399–422: <https://doi.org/10.1093/oeq/gpz068> [accessed 5 January 2023]

356 [Q 107](#) (Lawrence Gosden)

357 Written evidence from Arqiva ([TWW0017](#))

358 [Q 127](#) (David Black)

them. He thought that companies “should be out there installing meters ahead of customers signing up for them.”³⁵⁹

333. Mr Cox said: “It seems blindingly obvious that we should have all households metered.” He argued that proper meters and in-home displays can help consumers monitor their consumption and can show when there are invisible leaks. He noted one barrier to uptake may be consumer concern at companies holding their data, but this is “a perception issue utility providers have to deal with”.³⁶⁰ The Consumer Council for Water said combining compulsory metering “with customer engagement and the provision of information could provide additional encouragement for people to act on the information the meter provides.”³⁶¹
334. Mr Lovell said he was in favour of compulsory metering where possible. However, he outlined that compulsory metering “is not quite as simple as it sounds because in some apartment blocks it is difficult to do.”³⁶² This point was reiterated by Ms Bentley, who said Thames Water face this challenge as there are “a disproportionately higher number of [flats] in the Thames region”. However, she told us that she has “set a clear mission for [her] team to eradicate” issues with properties that cannot currently be metered.³⁶³
335. Currently, Dŵr Cymru Welsh Water install meters in all new properties, and from 2025 will use a change of occupancy as a mechanism to promote meter uptake. Mr Perry said that in making such a change, it is important to make sure “that the people who make those changes are protected from an affordability perspective”, while emphasising that metering “plays a part” in dealing with the challenges of climate change.³⁶⁴
336. Mr Lovell told us he believed the Environment Agency and water companies had the power to make water metering compulsory. However, Sir James differed, saying “Ultimately, I think there would need to be legislation if they were to be made compulsory.”³⁶⁵
337. The Secretary of State said she personally benefits from a meter, but did not believe “the Government are at a stage yet to mandate [metering] for every household across the country.” She said that without a meter, there is an element of certainty as to what water bills will be, and “people may feel that they will use a lot more water or that they will not be able to use as much water as they do now” if they were metered. She underlined that meters are automatically fitted into new developments.³⁶⁶
338. **Metering helps to inform consumers about their water usage by providing greater visibility of the amount of water used and the costs this is placing on the consumer. Metering has also been shown to reduce water consumption and could make a valuable contribution to managing future water supplies.**

359 [Q 127](#) (Iain Coucher)

360 [Q 88](#)

361 Supplementary Written evidence from the Consumer Council for Water ([TWW0035](#))

362 [Q 100](#) (Alan Lovell)

363 [Q 109](#) (Sarah Bentley)

364 [Q 109](#) (Peter Perry)

365 [Q 100](#) (Alan Lovell)

366 [Q 142](#) (Thérèse Coffey)

339. *The Government should make water metering compulsory for all households and businesses where it is possible to do so. In introducing compulsory metering, the sector should clearly communicate the benefits of metering to customers. Given the low levels of trust in water companies, the Government should proactively set out its view that the public should reduce its water consumption, both in the national interest and in order to reduce consumer bills.*

Leakage

340. In March 2020, the Environment Agency launched the National Framework for Water Resources, exploring England’s long-term water needs. The Framework aims to ensure that by 2050, leakage will have been reduced by 50 per cent.³⁶⁷ Leaks, which are often caused by faulty pipes or faulty water storage, cause clean water to be wasted. Given the predicted scarcity of future water supply, it is essential that water loss to leakage is minimised.
341. The majority of leaks occur on pipes owned by water companies. In Ofwat’s Annual Report and Accounts 2021–2022, the regulator noted that: “After a sustained period of poor performance, the sector is making encouraging progress reducing leakage.” 13 companies (75 per cent) had achieved their 2020–21 targets.³⁶⁸ However, Ofwat explained that in 2020–21 in England and Wales, leakages amounted to “51 litres of water per person per day”.³⁶⁹ As Mr Cox summarised, “Clearly, there is further to go on leakage”.³⁷⁰
342. Ms Clancy highlighted that “we know that high levels of leakage, when witnessed, have a significant detrimental impact on people’s willingness to [reduce their own water consumption]. They will not have a three-minute shower if they can see evidence of water companies having big leaks.”³⁷¹ Ms Bentley also recognised water companies “are not going to encourage anyone to reduce their consumption if we do not stop wasting [water].”³⁷²
343. Mr Lovell identified that leakage must be reduced, but “we are suffering from Victorian pipes”, making fixing leakage an expensive operation.³⁷³ This was echoed by the water companies. Mr Gosden said: “Soon we will get to the position where we need to need to start ramping up the replacement of [Victorian] cast-iron mains with new plastic ones that are fit for the future.” However, while “mains replacement is a really important investment need”, this need must be balanced alongside prices.³⁷⁴ Ms Bentley explained that London pipes are 84 years old on average, but the average life expectancy of a pipe is 80 years. Therefore, “a sustained uptick in investment” was needed, but “this can be bundled together ... over a multi-regulatory-cycle period, 15 or 20 years, so that we can spread the cost.”³⁷⁵

367 Environment Agency, *Meeting our future water needs: a national framework for water resources* (March 2020): https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/872759/National_Framework_for_water_resources_main_report.pdf [accessed 5 January 2023]

368 Ofwat, *Annual report and accounts 2021–22*, HC 196, July 2022: <https://www.ofwat.gov.uk/wp-content/uploads/2022/07/ARA-final.pdf> [accessed 5 January 2023]

369 Ofwat, ‘Leakage in the water industry’ (21 November 2022): <https://www.ofwat.gov.uk/leakage-in-the-water-industry/> [accessed 20 January 2023]

370 Q 81

371 Q 39

372 Q 112 (Sarah Bentley)

373 Q 98 (Alan Lovell)

374 Q 112 (Lawrence Gosden)

375 Q 112 (Sarah Bentley)

344. The Secretary of State highlighted that “targets have been set for reducing leakage, some near term and some long term”, and stressed she is very keen for water companies to address their leaks.³⁷⁶
345. **Water companies must play their part in reducing future water demand by minimising the amount of clean water wasted through leakages. Companies will find it far easier to make the case that their customers should reduce their water consumption if they can show that they have already taken similar action.**
346. *Ofwat must continue to set stretching targets on reducing leakage and incentivise companies to exceed these targets. Ofwat should ensure the necessary investment to reduce leakage is provided for through the Price Review process.*

376 [Q 142](#) (Thérèse Coffey MP)

SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS

Water regulation and policy

1. Ofwat and the Environment Agency may have differing remits, but they regulate the same industry. Therefore, effective collaboration is key to ensuring each regulator is able to achieve its individual aims and support the overall goals of the industry, such as reducing water pollution. We welcome recent progress on closer co-operation between the regulators, particularly through the Regulators' Alliance for Progressing Infrastructure Development (RAPID) in relation to future water supplies. However, there is still a clear lack of effective co-ordination on issues such as Environment Agency outputs not aligning with what Ofwat deems financeable, and ineffective information-sharing. (Paragraph 40)
2. *Ofwat, the Environment Agency and the Drinking Water Inspectorate should set up RAPID-style structures, including joint working and close partnership with industry, in areas of high priority, including improving water quality, upgrading the wastewater network and reducing water demand.* (Paragraph 41)
3. *It is crucial that Ofwat and the Environment Agency share relevant information effectively and efficiently on matters of joint interest. Ofwat and the Environment Agency should formalise and publish how they plan to share information on water company performance.* (Paragraph 42)
4. Effectively reducing water pollution and securing future supply will require the unified effort of a range of sectors, government departments, and regulators. Each of these areas has a range of funding sources, bodies and policies that affect the water environment, yet these must be co-ordinated to deliver overall success for the environment. Political will to deliver for the environment will also be necessary. (Paragraph 49)
5. *The Government should facilitate a co-ordinated approach to water pollution by publishing a National Water Strategy that approaches water policies in a holistic way. The Strategy should set clear expectations in relation to the quality of the water environment and the resilience of water supplies, giving regulators clear benchmarks to work towards. The Strategy should also set out clearly how the Government intends to oversee the regulators' delivery of these expectations.* (Paragraph 50)

Ofwat

6. It is the view of many in the water sector that Ofwat's objectives require it to make trade-offs between prioritising consumer bills, investment, and the environment. It is the impression of some stakeholders that Ofwat has historically given more focus to a short-term desire to keep water bills low at the expense of long-term environmental and security of supply considerations. (Paragraph 63)
7. Ofwat faces the challenge of balancing the financial needs of customers during a cost-of-living crisis with the urgent need for infrastructure and environmental investment. Given the distributional and intergenerational consequences of many of these decisions, it is crucial that Ofwat is given strong, clear guidance by the Government on how these trade-offs should be made. (Paragraph 64)
8. Ofwat needs clear guidance from the Government on how it should balance and prioritise its objectives. The Government should do this through its

Strategic Policy Statement (SPS). However, the 2022 SPS failed to give a sense of prioritisation, particularly in relation to the balance between the affordability of bills and infrastructure and environmental investment. We recognise the concern that more directive Statements could impact Ofwat's independence, but it is critical that elected politicians take controversial decisions which will have financial and environmental consequences for many generations, rather than passing that responsibility to regulators. The Government has not yet shown the necessary political will to make these decisions on the most important issues facing the sector. (Paragraph 79)

9. Like the House of Commons Environmental Audit Committee, we welcome the greater emphasis the 2022 SPS placed on protecting and enhancing the environment. However, some of the outcomes are vague and the language tends to call for Ofwat to “enable” and “encourage” actions from water companies and the water industry rather than require these actions. (Paragraph 80)
10. Ofwat's performance against meeting the objectives of the SPS should also be subject to greater Parliamentary scrutiny. We welcome the Environmental Audit Committee's intention to carry out this scrutiny routinely. (Paragraph 81)
11. *The Government should update the SPS to strengthen the language contained within it to ensure that Ofwat requires companies to meet SPS priorities. It should also provide a clear steer to Ofwat on how to balance its priorities, particularly in relation to the need to ensure higher levels of infrastructure investment, and these lessons should be taken on board in future Statements.* (Paragraph 82)

Price Review and outcomes-based regulation

12. We welcome Ofwat's recognition of the need for a significant increase in investment at the next Price Review, given the challenges facing the sector. The Price Review process is appropriate for iterative improvements to underlying assets but investment in environmental improvements and increasing water supply has remained low, potentially due to the regulator's focus on efficiency and the limited time horizon of the Price Review process. Given the likely shift in the sector towards large, long-term strategic infrastructure projects that are required to ensure future water supplies and resolve environmental issues, more of the sector's investment will need to take place outside of the Price Review process in future. (Paragraph 99)
13. Strategic, nationally significant infrastructure projects should be delivered outside of the Price Review process. The special purpose vehicle approach used for the Thames Tideway project provides a useful alternative model for funding such projects, reducing capital costs and spreading them over a longer timeframe than the five-year Price Review. Ofwat's Direct Procurement for Customers model provides an opportunity for larger projects to be carried across multiple Price Review periods and is a useful outlet, but the expansion of the Thames Tideway model is more desirable as this allows Ofwat to intervene more effectively through the licence that can be applied to the new investment. (Paragraph 121)
14. *The Government should consider legislating to remove the scale and complexity test from the Water Industry Act 1991 and the Specified Infrastructure Project Regulations, ensuring that special purpose vehicles can be used much more frequently to build large water infrastructure projects.* (Paragraph 122)

15. *The Government should designate the final National Policy Statement for Water Resources Infrastructure to ensure strategically significant water infrastructure projects are designated as nationally significant infrastructure projects and can progress through the planning process in a timely manner. The definition of nationally significant infrastructure projects should be amended to ensure strategic water resources schemes are not excluded, particularly those delivered through competitively appointed providers. (Paragraph 123)*
16. It is likely bills will have to increase to pay for some of the necessary investment in water infrastructure. It is therefore essential that appropriate support is given to those customers who need it. Current support schemes vary between water companies with no common baseline. This amounts to a postcode lottery for consumers in need. (Paragraph 137)
17. *The Government should legislate to introduce a single social tariff in time for its inclusion in the next Price Review. This should provide a baseline of support for customers regardless of who supplies their water. As this would require some customers to subsidise other customers, the Government should take decisions on the level of support having consulted with regulators, companies and consumer groups. (Paragraph 138)*
18. *The single social tariff should include a no-detriment clause to ensure that no customer is worse off as a result of the introduction of the new arrangements. Water companies should continue to offer additional support where customers are struggling to pay their bills even with the single social tariff in place. (Paragraph 139)*
19. The current Water Industry National Environment Programme (WINEP), an investment programme through which the Environment Agency specifies works required by water companies to meet environmental goals, is prescriptive about work water companies should undertake. Many stakeholders told us a move to outcomes-based regulation, where how an outcome is met is not prescribed, would give water companies greater opportunity to design innovative solutions to problems facing the sector. These solutions may be more cost-effective and environmentally friendly than traditional ones. We therefore welcome that the Government, Ofwat and the Environment Agency are planning to move towards outcomes-based regulation in the next iteration of the WINEP. (Paragraph 151)
20. *The Government, Ofwat and the Environment Agency should ensure that the next iteration of the Water Industry National Environment Programme has a greater focus on the outcomes to be achieved. This will give responsible companies more leeway to use nature-based and catchment-based solutions. (Paragraph 152)*
21. *To the extent that prescriptive regulatory requirements are the result of retained EU law, the Government should examine whether the relevant provisions can be amended to enable an outcomes-based framework in time for the next Price Review. (Paragraph 153)*

Storm overflows and water pollution

22. The prevalence of combined sewers in England, which combine surface water with foul water, results in polluted water being released to the environment via storm overflows. Although the Government will need to look at the possibility of separating sewers, significant progress could be made by reducing pressures on the existing network. We therefore welcome the Government's intention to enact Schedule 3 of the Flood and Water

Management Act 2010. This will ensure developers in England are not able to connect to existing sewer networks without designing appropriate sustainable drainage systems, and will place England in line with Wales, where most construction work is required to have sustainable drainage systems that comply with national standards. (Paragraph 169)

23. Wet wipes pose a serious risk to the proper operation of the sewage system by contributing to “fatbergs”—build ups of fat that cause blockages and thus storm overflow use. Consumers must be properly educated about the problems of wet wipes by the water industry. We therefore welcome Water UK’s national campaign on the issue. However, policy intervention may also be needed. (Paragraph 174)
24. *We recommend the Government considers banning the sale of wet wipes that are not rapidly biodegradable.* (Paragraph 175)
25. While regulators and companies in the sector may be more comfortable with traditional, infrastructure-heavy solutions to water pollution, and some will undoubtedly be needed, it is clear that there is also a place for innovative approaches, including nature-based solutions and catchment approaches. These can be a cost-effective, environmentally friendly way of reducing water pollution. (Paragraph 182)
26. *We recommend nature-based solutions and catchment approaches form a larger part of the next iteration of the Price Review and the Water Industry National Environment Programme (WINEP).* (Paragraph 183)
27. A huge level of investment—that the Government has estimated will cost £56 billion over 25 years—is required so that storm overflows are only used in times of exceptional weather. Given that water companies are responsible for maintaining their own sewage networks, they must bear a significant degree of responsibility for the necessary investment costs. However, we recognise that the scale of investment needed is vast, and for the private sector to meet this challenge there will need to be stable, long-term funding arrangements that provide certainty for investors. (Paragraph 198)
28. *The Government should set out how it envisages the investment needed to prevent pollution will be funded through a National Water Strategy. Water companies should take the lead in meeting the majority of costs.* (Paragraph 199)
29. Pollution caused by the routine use of storm overflows is environmentally damaging and the public is right to demand better. However, we recognise that there are other causes of water pollution which must also be tackled. (Paragraph 203)
30. *A National Water Strategy should include consideration of how funding should be balanced across causes of water pollution, to maximise environmental protection and minimise costs.* (Paragraph 204)
31. The levels of storm overflow overuse by some companies are unacceptable. We welcome that monitors will be present on all storm overflows by the end of 2023 and that the Government has increased the Environment Agency’s funding for monitoring. However, it appears that the Agency’s monitoring and enforcement has in the past been seriously compromised by cuts to its grant, leading to an over-reliance on self-monitoring by water companies. It is crucial that the Environment Agency is provided with adequate funding to carry out inspections. Failure to do this would risk returning the regulator

to a position where it must rely on water companies to police their own behaviour. (Paragraph 221)

32. *We recommend the Government ensures adequate funding is available to the Environment Agency to inspect and enforce environmental offences by water companies.* (Paragraph 222)
33. Water companies should commit to providing public, open data in a useable form on the environmental performance of their sewerage network and sewage works. Customers should be able to see how water companies are affecting their areas in real or near-real time, and regulators should have access to this information in order to ensure that water companies are fulfilling their duties. It is welcome the Environment Act 2021 amended the Water Industry Act 1991 to require companies to provide open data, but no detail about how such plans will be implemented have yet been outlined. (Paragraph 229)
34. *The Government, Ofwat, and the Environment Agency should publicly outline their plans to ensure open data on environmental performance is provided by companies as a matter of priority.* (Paragraph 230)
35. We welcome the Government's Storm Overflows Discharge Reduction Plan and its expectation that water companies reduce their use of storm overflows to their original intended use—during exceptional periods of rainfall. However, we recognise that there are concerns over whether the targets in the Plan are sufficiently ambitious, especially in terms of its 2050 goal for reducing storm overflow use. We also recognise that tackling storm overflow overuse will require a joined-up approach across government and regulators, which the plan currently lacks. (Paragraph 240)
36. *We recommend that the Government's commitment to a mandatory review of the Storm Overflows Discharge Reduction Plan in 2027 is used as an opportunity to set stretching targets to reduce storm overflow overuse. We would welcome Defra's research budget being used to examine how these more stretching targets could be met. In the meantime, Ofwat must ensure that significant incentives are in place to encourage companies to meet the targets in the Plan ahead of prescribed dates. We also recommend that a National Water Strategy should include a co-ordinated approach to reducing and preventing water pollution.* (Paragraph 241)

Fines, penalties, and enforcement

37. It appears that for some time, regulatory deterrents such as penalties and fines have been insufficient to ensure an acceptable level of performance by water companies, particularly in relation to the environment, where performance is at its lowest ever levels. We welcome that some recent fines and penalties have been at a more appropriate level but remain concerned that they may not be a sufficient deterrent. The length of enforcement processes can result in those in penalties being applied long after those responsible have left the company. (Paragraph 252)
38. Recent Government proposals to increase substantially the limit on the Variable Monetary Penalties that can be directly imposed by the Environment Agency on companies could help to provide strong enforcement in a more reasonable timeframe. However, it is concerning that the Environment Agency has not used these powers often in the past, a situation possibly

brought about by the Agency's shortage of resources for enforcement. (Paragraph 253)

39. While civil penalties can help to bring about enforcement more quickly, it is important that regulators prosecute criminal behaviour. It is alarming that the Environment Agency is prosecuting less due to resource constraints. (Paragraph 254)
40. *The Government should deliver on its proposals to increase the limit on Variable Monetary Penalties for serious offences committed by water companies. The Government should ensure the Environment Agency has adequate funding to use its new powers effectively and prosecute criminal behaviour in the sector.* (Paragraph 255)
41. *There is a need for greater individual accountability for executives and directors of companies that are responsible for serious and deliberate pollution incidents, including criminal prosecution where appropriate. The Government should give Ofwat powers to prevent directors of companies that are responsible for serious pollution incidents from continuing to work in the sector.* (Paragraph 256)
42. Ofwat's special administration powers allow it to change the ownership of water companies that are falling short in meeting their responsibilities. This a powerful tool that has the potential to be used more widely where companies have been found not to have been meeting their obligations. (Paragraph 266)
43. *Ofwat should consider whether to be more proactive in using these powers to change the management of continued poor performers in the sector.* (Paragraph 267)

Debt, dividends, and financial resilience

44. It is clear that in the past, a number of water companies have been overly focused on maximising financial returns, including by increasing debt levels, at the expense of operational performance and protecting the environment. We welcome that some companies have exercised more restraint in recent years, in part due to tougher regulatory settlements as well as wider economic conditions. (Paragraph 281)
45. While financial structures are usually a matter for company boards, water companies' monopoly role in providing an essential service means that a higher standard should be demanded, especially in a sector of such importance to households and the environment. We support Ofwat's increased interest in the financial structures of water companies and wholly support its proposals to amend licenses to ensure that dividends are linked to performance and companies are financially resilient. (Paragraph 282)
46. Water company executives should not be able to receive substantial bonuses while their companies have missed performance targets and polluted the water environment, potentially in breach of their permits. (Paragraph 288)
47. *We support Ofwat's increased interest in executive pay, including its expectation that companies set out their proposed policies for performance-related executive pay during the next Price Review period. These proposals should ensure performance-related pay is much more closely linked to performance, particularly in relation to the environment. Ofwat should set out further provisions to ban bonuses at companies who have been found to have caused serious pollution incidents as part of the conditions of water company licences.* (Paragraph 289)

48. Some witnesses told us the introduction of private equity ownership to the water sector has been a driver in some companies focusing on financial performance rather than service delivery and securing resilience. This has led some privately owned companies to take on debt and introduce complex financial structures in order to pay out large returns, even where performance has been unacceptable. Requiring water companies to disclose information to the same standard as publicly listed companies has the potential to improve their governance and increase scrutiny of their financial arrangements. (Paragraph 296)
49. *Ofwat should ensure that water companies are subject to the same level of transparency as publicly listed companies, in order to improve transparency through the regular reporting cycle.* (Paragraph 297)

Future water supply

50. The Regulators' Alliance for Progressing Infrastructure Development's plans to increase the levels of water transfer between regions are set to be very important in using existing water resources more effectively. The regulators should continue to ensure that companies work co-operatively in this area. (Paragraph 306)
51. Under present plans, the UK will not have built a single new major reservoir between 1991 and 2029. The Government, regulators, and companies must work together to deliver more reservoirs to meet the UK's future water needs. Failure to do so will result in a less resilient, secure water supply that risks leaving households without water during extreme weather conditions that are becoming more frequent due to climate change. We welcome the Government's intention to address the planning issues impeding reservoir development in the National Policy Statement for Water Resources Infrastructure. (Paragraph 314)
52. *The Government should set out plans to accelerate the planning process for reservoirs, including by designating, and if necessary amending, its National Policy Statement for Water Resources Infrastructure as a matter of priority.* (Paragraph 315)
53. Reducing water demand is crucial to ensuring sufficient water supplies. The UK has one of the highest water usage figures per capita in Europe and while the Government has set an ambitious target to reduce consumption, clearer detail is needed on how it, regulators and companies plan to address this issue. The Regulator's Alliance for Progressing Infrastructure Development (RAPID) has proved to be a successful model for co-operation, and given the need for co-operation to reduce consumption, a similar alliance could be used to focus on this area. (Paragraph 327)
54. *The Government should set out in a National Water Strategy how it envisions meeting its targets for reducing water demand. This should involve setting out new policies and setting clear expectations for regulators and companies.* (Paragraph 328)
55. *Ofwat, the Environment Agency and water companies should work closely together, as they do with RAPID, in order to set out schemes and proposals to reduce water demand.* (Paragraph 329)
56. Metering helps to inform consumers about their water usage by providing greater visibility of the amount of water used and the costs this is placing on the consumer. Metering has also been shown to reduce water consumption

and could make a valuable contribution to managing future water supplies. (Paragraph 338)

57. *The Government should make water metering compulsory for all households and businesses where it is possible to do so. In introducing compulsory metering, the sector should clearly communicate the benefits of metering to customers. Given the low levels of trust in water companies, the Government should proactively set out its view that the public should reduce its water consumption, both in the national interest and in order to reduce consumer bills.* (Paragraph 339)
58. Water companies must play their part in reducing future water demand by minimising the amount of clean water wasted through leakages. Companies will find it far easier to make the case that their customers should reduce their water consumption if they can show that they have already taken similar action. (Paragraph 345)
59. *Ofwat must continue to set stretching targets on reducing leakage and incentivise companies to exceed these targets. Ofwat should ensure the necessary investment to reduce leakage is provided for through the Price Review process.* (Paragraph 346)

APPENDIX 1: LIST OF MEMBERS AND DECLARATIONS OF INTEREST

Members

Lord Agnew of Oulton
 Lord Blackwell (until 31 January 2023)
 Baroness Bowles of Berkhamsted
 Lord Burns
 Viscount Chandos (from 1 February 2023)
 Lord Clement-Jones (from 1 February 2023)
 Lord Cromwell
 Baroness Donaghy (until 31 January 2023)
 Lord Eatwell (until 31 January 2023)
 Lord Gilbert of Panteg (from 1 February 2023)
 Lord Hollick
 Lord Leong (from 1 February 2023)
 Baroness McGregor-Smith (from 22 June 2022)
 Lord Reay
 Lord Sharkey (until 31 January 2023)
 Baroness Taylor of Bolton (from 22 June 2022)

Declaration of Interests

Lord Agnew of Oulton
Ongoing application to the Environment Agency for a water resources abstraction license to build a farm reservoir

Lord Blackwell
No relevant interests declared

Baroness Bowles of Berkhamsted
No relevant interests declared

Lord Burns
Former Chairman of Welsh Water (2001–2010)

Viscount Chandos
Trustee of the Esmee Fairbairn Foundation, which funds charities working to protect and restore freshwater habitats in the UK from threats such as pollution. The foundation's endowment is an investor in the RobecoSAM Sustainable Water Equities Fund.

Lord Clement-Jones
Chair of the board of Trust Alliance Group (formerly Ombudsman Services Limited)

Lord Cromwell
No relevant interests declared

Baroness Donaghy
No relevant interests declared

Lord Eatwell
No relevant interests declared

Lord Gilbert of Panteg
No relevant interests declared

Lord Hollick
No relevant interests declared

Lord Leong
No relevant interests declared

Baroness McGregor-Smith

Board member of Thames Tideway Tunnel

Board member of SNC-Lavalin Group Inc, whose subsidiary (Atkins Global) is a supplier of Ofwat

Lord Reay

No relevant interests declared

Lord Sharkey

No relevant interests declared

Baroness Taylor of Bolton

No relevant interests declared

A full list of Members' interests can be found in the Register of Lords Interests:
<https://members.parliament.uk/members/lords/interests/register-of-lordsinterests>

APPENDIX 2: LIST OF WITNESSES

Evidence is published online at <https://committees.parliament.uk/work/6719/the-work-of-ofwat/publications/> and available for inspection at the Parliamentary Archives (020 7219 3074).

Evidence received by the Committee is listed below in chronological order of oral evidence session and in alphabetical order. Those witnesses marked with ** gave both oral and written evidence. Those marked with * gave oral evidence and did not submit any written evidence. All other witnesses submitted written evidence only.

Oral evidence in chronological order

*	The Rt Hon Philip Dunne MP, Chair of the House of Commons Environmental Audit Committee	QQ 1–8
*	Professor Ian Barker, Managing Director, Water Policy International Ltd	QQ 9–15
*	Annabelle Ong, Director, Frontier Economics	QQ 9–15
*	Mark Lloyd, Chief Executive Officer, The Rivers Trust	QQ 16–31
**	Guy Linley-Adams, Solicitor, Salmon & Trout Conservation	QQ 16–31
**	Emma Clancy, Chief Executive, Consumer Council for Water	QQ 32–43
**	Professor Catherine Waddams, Centre for Competition Policy, University of East Anglia	QQ 44–52
**	Christine McGourty, Chief Executive, Water UK	QQ 53–64
**	Stuart Colville, Director of Policy, Water UK	QQ 53–64
*	Lawrence Slade, CEO, Global Infrastructure Investor Association	QQ 65–71
**	Jonson Cox, former Chair of Ofwat	QQ 72–91
*	Sir James Bevan, CEO, Environment Agency	QQ 92–103
*	Alan Lovell, Chair, Environment Agency	QQ 92–103
*	Sarah Bentley, CEO, Thames Water	QQ 104–118
*	Peter Perry, CEO, Dŵr Cymru Welsh Water	QQ 104–118
*	Lawrence Gosden, CEO, Southern Water	QQ 104–118
**	David Black, Chief Executive, Ofwat	(QQ 119–130)
**	Iain Coucher, Chair, Ofwat	QQ 119–130
*	The Rt Hon Thérèse Coffey MP, Secretary of State for Department for Environment, Food, and Rural Affairs	QQ 131–145
*	Davide Minotti, Deputy Director for Water Services, Department for Environment, Food, and Rural Affairs	QQ 131–145

Alphabetical list of all witnesses

**	Guy Linley-Adams, Solicitor, Salmon & Trout Conservation (QQ 16–31)	TWW0002
	Affinity Water Limited	TWW0013
	Afonydd Cymru	TWW0006
	Angling Trust	TWW0012
	Arqiva	TWW0017
*	Professor Ian Barker, Managing Director, Water Policy International Ltd (QQ 9–15)	
	John Bates, Barrister, Old Square Chambers	TWW0001
	Dr Kate Bayliss, SOAS University of London	TWW0024
*	Sarah Bentley, CEO, Thames Water (QQ 104–118)	
*	Sir James Bevan, CEO, Environment Agency (QQ 92–103)	
**	David Black, Chief Executive, Ofwat (QQ 119–130)	TWW0030
	Blueprint for Water	TWW0032
**	Emma Clancy, Chief Executive, Consumer Council for Water (QQ 32–43)	TWW0019 TWW0035 TWW0036
*	The Rt Hon Thérèse Coffey MP, Secretary of State for Environment, Food, and Rural Affairs (QQ 131–145)	
**	Stuart Colville, Director of Policy, Water UK (QQ 53–64)	TWW0021
	Simon Cooper, Founder and Managing Director at Fishing Breaks	TWW0004
**	Iain Coucher, Chair, Ofwat (QQ 119–130)	TWW0030
**	Jonson Cox, former Chair of Ofwat (QQ 72–91)	TWW0034
*	The Rt Hon Philip Dunne MP, Chair of the House of Commons Environmental Audit Committee (QQ 1–8)	
	Everflow Limited	TWW0009
	Future Water Association	TWW0025
*	Lawrence Gosden, CEO, Southern Water (QQ 104–118)	
	Professor Peter Hammond	TWW0003
	Professor Michael Harker, Professor of Law, University of East Anglia	TWW0007
	IFM Investors (UK)	TWW0010
*	Mark Lloyd, Chief Executive Officer, The Rivers Trust (QQ 16–31)	

- * Alan Lovell, Chair, Environment Agency (QQ 92–103)
- ** Christine McGourty, Chief Executive, Water UK [TWW0021](#)
([QQ 53–64](#))
- * Davide Minotti, Deputy Director for Water Services,
Department for Environment, Food, and Rural Affairs
([QQ 131–145](#))
- MOSL - the water retail market operator [TWW0008](#)
- * Annabelle Ong, Director, Frontier Economics
([QQ 9–15](#))
- Pennon Group [TWW0023](#)
- * Peter Perry, CEO, Dŵr Cymru Welsh Water ([QQ 104–118](#))
- * Lawrence Slade, CEO, Global Infrastructure Investor
Association ([QQ 65–71](#))
- The Independent Networks Association [TWW0028](#)
- The Independent Water Networks Limited [TWW0029](#)
- William Thomas [TWW0031](#)
- UK Water Retailer Council (UKWRC) [TWW0020](#)
- ** Professor Catherine Waddams, Centre for Competition
Policy, University of East Anglia ([QQ 44–52](#)) [TWW0007](#)
- Waterwise [TWW0027](#)
- Professor Nigel Watson, Professor of Geography and
Environmental Management, Lancaster University [TWW0005](#)
- Wave [TWW0016](#)
- Wessex Water [TWW0015](#)
- Wild Justice [TWW0018](#)
- Wildlife and Countryside Link [TWW0022](#)
- Windrush Against Sewage Pollution [TWW0014](#)
- Worshipful Company of Water Conservators [TWW0011](#)

APPENDIX 3: CALL FOR EVIDENCE

The House of Lords Industry and Regulators Committee launches an inquiry investigating the role of Ofwat, the Water Services Regulation Authority. The Committee will consider Ofwat's performance against its statutory objectives and whether it has the powers and resources needed to meet those objectives. The Committee is seeking answers to the following questions from interested individuals and organisations.

1. Is Ofwat meeting its statutory objectives?
2. Are Ofwat's statutory objectives clear and consistent? How can performance against these be measured? How well does Ofwat manage any trade-offs between its objectives?
3. Does Ofwat have the necessary powers to meet its objectives? Does it need greater powers to ensure that water companies reduce sewage overflows?
4. Does Ofwat have the necessary resources to meet its objectives?
5. What are the main challenges facing Ofwat and how well is it meeting them?
6. Does Ofwat have strategic guidance from the Government on how to balance its objectives?
7. How well does Ofwat work with other regulators and authorities to meet joint challenges and overlapping responsibilities?
8. How satisfactorily does Ofwat take the consumer interest into account?
9. How effective is Ofwat's Price Review process?
10. In its engagement with the water industry, does Ofwat strike the right balance between being open to industry whilst also providing robust regulatory oversight?
11. Does Ofwat sufficiently consider the long term in its regulation? Does Ofwat strike a balance between more visible, short-term issues and long-term considerations?