

Water UK response to the abstraction licence reform consultation

Introduction

1. Water UK is the policy development organisation for water companies in the United Kingdom. We are pleased to respond to this consultation.
2. We are grateful to Ministers and officials at Defra for their openness and collaborative approach at all stages of this process. We worked, with Ofwat and the Environment Agency, on several areas of principle within the water resources policy area before the White Paper was published. We have been involved on the Abstraction Reform Advisory Group and at the workshops Defra facilitated in the run up to the publication of this consultation.
3. Generally, the current abstraction regime has worked well for public water supply (PWS), and at the same time, Ofwat's price regulatory regime has ensured an affordable and reliable water supply. In particular, the following features of the current abstraction regime have worked well for PWS:
 - Through the water resources management planning process water companies are planning for the potential impacts of climate change and increasing demand for water resources. In addition, water companies have recognised the need for regional strategic multi-sector planning, and companies are working to address this need, through groups such as Water Resources East Anglia and Water Resources in the South East.
 - There are strong incentives within the current system for water companies to reduce levels of leakage, reduce demand for treatment water resources, and increase resilience to extreme weather.
 - The current system gives certainty over the amount of water available from a source and therefore the confidence to invest in catchment management, water treatment and distribution from this source of water.
 - Numerous water company abstraction licences are already conditional in nature, with mechanisms built in to protect the environment and other abstractors.
 - Through the Environment Agency's Restoring Sustainable Abstraction programme, water companies are investigating and addressing unsustainable abstractions and licences, and will ensure compliance with the Water Framework Directive and the Habitats Directive in the 2020s. In addition, some water companies are reducing licence headroom as a direct result of the Water Framework Directive's 'no deterioration' clause.
 - Severe and long-term droughts are effectively managed through robust drought management procedures, which link well with the current nature of abstraction licences.
4. However, while we believe that the current system has generally worked well for PWS, we understand that water companies are not the only abstractors of water resources, and that there are opportunities to improve the current system.
5. We are aware that Defra is undertaking a great deal of work to understand how the reform options may affect abstractors. It is unfortunate that the detail behind the impact assessment has not been made visible, as this would have helped to generate more confidence in the process. We understand that the work is on-going, and we would welcome the opportunity to better understand and contribute towards the modelling of policy options. In particular, we would like to work with Defra to understand the impact of the different reform proposals on water companies' deployable outputs.

6. We welcome the proposals to better link abstraction to water availability, provided that any flow conditions used are well founded. In particular, we think that the proposals to move away from seasonally related conditions, and the ability to abstract water under high or very high flow conditions (without that abstraction counting towards the authorised annual licence), will be beneficial to many abstractors. In addition, we think that the introduction of electronic licences is a sensible proposal that will help to reduce the costs of administering the system. However could not these changes be introduced under the existing system?
7. We are concerned about the impact of some of the reform proposals on PWS. We would welcome the opportunity to work more closely with Defra to understand how the reform proposals will impact PWS, and to ensure that unintended consequences are avoided. Specific areas of concern are detailed below.

Process

8. The consultation highlights a number of times that the current process of applying for, or varying a licence, is slow and complicated. Whilst it is always right that the application process should be as quick, simple and as low cost as possible, it is only appropriate that any change to an abstraction licence is well evidenced. The majority of our members believe that abstraction licences should only be increased if detailed environmental studies have shown that this is acceptable, and abstraction licences should only be decreased if detailed environmental studies have shown that this is required. By contrast the process of renewing time limited licences should be streamlined. However, some of our new members strongly disagree. They feel the reform agenda rightly considers how new entrants, the environment and economic growth could benefit from adequate access to a sustainable water resource, that a 'water reserve' system might facilitate this objective, and that there are compelling market, environmental and economic reasons why existing surplus licensed abstraction should be clawed back. They believe that it is possible to meet the needs of the PWS (including forward looking resource issues) and new entrants whilst also maintaining sufficient flows for the aquatic environment.
9. It should be recognised that an abstraction is only part of a water use process. In the case of public water supply the water needs to be treated, stored and piped to customers – all of which involve significant operating, and in particular, capital costs. The infrastructure that sits downstream of an abstraction licence is relatively inflexible, and therefore changes to licences should only be made if we are very confident that they are required (if the licence is being decreased) or acceptable (if the licence is being increased).
10. Overall the proposed options appear to be more complex than the current system, and we would be concerned that the increased administrative costs would be reflected in higher abstraction licence charges.

Water resources management planning

11. As a consequence of the proposal to reduce licensed volumes as part of the transition to the new system and the reform options themselves (both current system plus and water shares), the deployable output of sources would be affected. However we note that there is no assessment of how the proposed changes would impact deployable output (the amount of water companies would have available to meet demand in a dry year) and the consequent impact on their supply demand balance, Water Resources Management Plans, Drought Management Plans and investment programmes. Potentially these plans could change radically as a result of abstraction reform, and this would need to form a central consideration in the current round of WRMP19 planning. We think that this effect may be particularly pronounced under the Water Shares option.
12. We are working to understand these impacts; however, the consultation document does not provide sufficient information for companies to make a proper assessment of the risks. We would welcome

the opportunity to work with Defra to develop a shared understanding of how the reform proposals may affect water company deployable outputs and consequently investment plans.

Strategic planning

13. Although the consultation document appears to be predicated on additional storage, there is little consideration of the need for greater strategic planning in the provision of that storage or its costs. While water can be stored to address deficits at times of low flows, the amount that can be carried over between seasons is limited by the available storage capacity. Significant investment and planning would be required to address this.
14. Water companies have recognised the need for greater strategic planning, and are working to address this gap through groups such as Water Resources East Anglia and Water Resources in the South East. We believe that co-operation with the agricultural sector and environmental NGOs could create, in appropriate locations, multi-sector reservoirs, that not only could provide useful additional winter storage for agriculture, but which could also enhance the environment, fulfilling Birds and Habitats Directive obligations.
15. In addition, there is little consideration of the role for Government in the development of large-scale interconnection and storage assets. In theory, market forces could play a substantial role in the development of this strategic infrastructure; however, there is a question as to whether the market alone will be enough to facilitate such investment. Such strategic assets can raise many complex social, environmental, political and economic issues, which create heightened uncertainty around whether any investment will be recoverable. This is because they typically involve the use of, and interaction with, natural water resources that are managed by government agencies.
16. The relationship between water companies and their customers is central. Companies are charged by our customers and our economic regulator to keep costs down. There is concern from many in the industry that the reforms in this consultation could potentially end up driving unforeseen additional costs and the impact on customers' bills of the different options is an important omission from the work presented in the consultation document and the cost benefit analysis in particular. They feel that clarification of the relationship between this consultation and future water industry business planning processes would be helpful, as would be a recognition that these reforms are not intended to lead to higher customer bills. However, some of Water UK's new members feel that this view is heavily partisan, and that it is as likely that the reforms will drive down costs or produce unforeseen additional savings.

Drought and resilience

17. A critical issue for all sectors is the lack of resilience offered during long-term dry events. The question of drought and resilience is closely connected to the need for strategic planning, because in order to buffer the impact of long-term dry events it will be necessary to develop storage at farm, catchment and regional levels.
18. We believe that more work is required to understand how the reform options would perform when the system is stressed, i.e. during a drought, and how the reform proposals will interact with drought management arrangements. We believe that the new system should be designed to function effectively during times of drought as well as "normal" conditions. Administrative allocation rules which override market outcomes when the system is under most stress are likely to dampen the impact of market-based reform – particularly on investment in peak capacity.
19. We understand that Defra is working to address this issue, and is looking to model the performance of the two systems under drought conditions. We hope that Defra will make the results of this work available, and we would welcome the opportunity to contribute to this work.

Transition and environmental protection

20. We agree that the over-licensing of catchments is an issue that needs to be addressed ahead of the reform. We would also agree with the principle set out within the 2011 Water White Paper that the process of abstraction licence reform should not be used to resolve any unsustainable abstractions – which we would take to include licences which authorise abstraction which may be unsustainable.
21. To this end we think that there should be a further review of whether existing powers within the current system should deliver the objectives being sought through the proposed transition process – including
 - Seeking voluntary changes
 - Application of the 4 year rule
 - Reverse auctions
 - Use of the serious environmental damage powers
 - Provision of mitigation rather than changing licences – adaptive management, stream support, AIM or habitat improvement for example
 - Ensuring that the RSA process considers licensed quantities as well as actual abstraction rates
22. Many companies are concerned about the proposal to reduce licensed volumes as part of the transition to the new system. They feel that the “transition” processes outlined in the document take no account of why, for different abstractors, there is a difference between their licensed volumes and their actual abstractions. They believe that there could be many legitimate reasons for this difference, including business planning considerations, fluctuations in demand due to climatic variation, water quality concerns, drought contingency, pump storage and artificial recharge requirements, resilience and operating efficiency.
23. They feel that in any transition process abstractors should be given the opportunity to re-justify their need for their current licensed volume – and only be subject to a proportionate reduction if this justification is poor or not forthcoming. Whilst this would be an extensive exercise, they do not think that it would be disproportionate given the potentially significant changes to existing rights. It may also put abstractors at ease about the legal justification for the impact on their property rights.
24. However, some of our new members believe that it is for the water company to present an adequate justification to maintain licensed volume substantially above actual abstraction. They feel that presumption in favour of reducing licensed volumes (after allowing for reasonable justification for headroom) and transferring a percentage of this into the ‘water reserve’ would greatly assist in achieving the aims of abstraction reform.
25. It is not clear how current processes to address unsustainable abstraction will interact with the proposal to reduce licences to reflect recent use. The consultation document states that: “If licences were changed to protect the environment before the new system is implemented, the revised licence would be converted to the new system.”¹ We are concerned that a licence may be reduced once as part of the RSA programme, and then again as part of the transition to the new system.
26. Water companies have been working with the Environment Agency for more than 20 years to establish whether catchments are over-licensed and to make changes where this has been shown to be the case. This work has been undertaken via various processes including CAMS, the Restoring Sustainable Abstraction (RSA) programme, Habitats Directive Review of Consents, local studies as well as the more recent Water Framework Directive programme. The studies have involved detailed flow impact and environmental assessments. Where these assessments have shown that full utilisation of current licences would cause a serious environmental impact then the licences should be, and in the vast majority of cases, have been, changed.

¹ Defra 2013, Making the most of every drop, page 46

27. Where the EA has concerns at other locations about deterioration many companies consider that it is important they initiate appropriate detailed environmental studies at both a site and catchment level. These could be done either before or after transition to a new licensing system. However, some of our new members point out that avoiding serious environmental impact is not the sole aim of abstraction reform, and that new entrants can drive both efficiency and environmental improvement.
28. Before we can meaningfully change the system to ensure a fair allocation and management of water in the future, more clarity should be brought to who is actually using water under the current system. There are some significant users that currently do not have licenses – for example, the MOD, trickle irrigators and the canal network – which means it is not clear where the resource stresses in come catchments lie. We suggest that before the abstraction licence system changes, all catchment users are brought into the existing system. This will allow the Environment Agency to gather sufficient and robust data over a period of time.
29. Once these processes are concluded, with all abstractors licensed and abstraction licences set at a sustainable level, it would allow a far clearer understanding of available catchment resources and the need for, and benefits arising from, reform of the underlying licensing system. It would also clarify whether it would be possible to use the current system, or a variant of it, to achieve the Government's aims for abstraction over a shorter timescale.
30. Both reform options envisage the use of Environmental Flow Indicators (EFIs) as the means by which the environmental flow needs of a river are protected. However EFIs are risk assessment measures and for any individual catchment or water body they are not the best way to define water availability or ensure environmental protection as they do not usually reflect local hydrological and ecological conditions. This has been demonstrated by water companies in work done in association with the Environment Agency for National Environment Programme (NEP) studies over the last 20 years. In particular EFI based flow targets do not take into account other anthropogenic impacts e.g. channel modifications and diffuse pollution which can have a much more significant effect on waterbody status under the Water Framework Directive than abstraction impacts.
31. A flow based approach would only work with detailed study of all reaches, providing a robust, scientific evidence base. Whilst the EFI approach would reduce the cost to the Environment Agency in calculating flow targets and bands, we consider it is a poor substitute for detailed investigations, similar to those that have been undertaken in many catchments over the last 20 years. Potentially the use of EFIs could result in insufficient protection for the environment in some circumstances and significant economic inefficiency in others if abstraction licences were unnecessarily restricted as a result.
32. A number of impacts of licence changes do not appear to have been considered. For instance many abstraction licences are linked to Acts of Parliament and commercial contracts. It would be helpful to understand how these would be affected under the proposed regimes.

Water company discharges

33. The consultation raises the question of how water company discharges should be treated in the new system. We think that the new system should recognise the benefits of water company discharges, which are often important for supporting river flows and downstream abstractors. However, we are nervous about the potential impacts of requiring water companies to discharge specified volumes from defined locations. The consultation acknowledges that this requirement could lock companies into inefficient solutions and reduce their scope for innovation. In addition, it is not clear how this sort of requirement would interact with water efficiency initiatives (which in turn reduce volumes of wastewater) and schemes to separate surface water and foul drainage.

34. We would welcome the opportunity to work with Defra to better understand these issues and in the development of the new system. We would also like to understand better how “net abstraction” would be calculated and operated within the two reform options.

Next steps

35. We will continue to work with Defra and the Environment Agency to understand the impacts of the proposed reforms on PWS, and we would welcome opportunities for more collaboration. We would expect and anticipate further public consultation. We understand that Defra is undertaking a significant amount of work to develop the reform options and to understand their potential impacts, and we hope that the detail behind this work can be made visible to water companies. We are particularly interested in understand and contributing towards the following areas:
 - the potential impacts of the proposed reforms on water company deployable outputs;
 - the treatment of water company discharges;
 - the performance of reform options during a drought, and interface between the new system and drought management arrangements;
 - how water company abstraction licences should be transitioned into the new system; and,
 - the development of trading rules and markets.
36. Various projects are being undertaken to fully understand the impact of the proposed reform options on deployable outputs and upstream resource security, including a project being undertaken on behalf of the water industry by UKWIR (Evaluating abstraction reform proposals). These key projects are unlikely to be delivering outputs until close to or after the date for responses to the consultation; we look forward to sharing the results with Defra once they have been completed.