

10 December 2012



Tim Brooks
Water Regulation and Consumer Protection Team
Area 2C, Ergon House
Horseferry Road
London SW1P 2AL

1 Queen Anne's Gate
London SW1H 9BT
Telephone 020 7344 1844
Fax 020 7344 1866
e-mail contact@water.org.uk website
www.water.org.uk

Pamela Taylor
Chief Executive

Dear Tim

Defra consultation on Strategic Policy Statement

1. Water UK represents all major UK water and wastewater service suppliers at national and European level. We provide a positive framework for the water industry to engage with government, regulators, stakeholder organisations and the public, and are pleased to respond to this consultation.
2. We support the new framework set out by Defra in the Strategic Policy Statement, and the aim of providing clear and unambiguous direction to Ofwat, so that Ofwat can carry out its role of independent economic regulator with confidence that it is acting within a clear policy framework set by Government.
3. We note that the Strategic Policy Statements to economic regulators are being implemented across government in different ways, with for example the Energy Bill providing an explicit statutory framework for the Strategy and Policy Statement to Ofgem.
4. This explicit statutory framework provides greater clarity on the status of the Strategic Policy Statement, and we suggest that Defra considers the merits of this approach for the water sector.
5. There is much that the industry supports in the directions to Ofwat and we comment on a number of the directions below.
6. We note however that there are inherent tensions between the directions, for example between avoiding regulatory uncertainty and taking account of investor views, and promoting competition.

Continued...

7. It would provide greater clarity on the Government's policy position for the directions to make clear which objectives should be given greater priority when tensions such as this arise.
8. We note that one area of the statement where there is not an explicit direction is effective engagement.
9. We agree that effective engagement and collaborative approaches will be key to finding solutions to many of the challenges facing the sector, such as managing catchments more effectively and making the best use of our nation's water resources.
10. The industry will continue to play its full role in engaging effectively and constructively with the full range of stakeholders in the water sector, including all our regulators.
11. We also note the intention in the *Principles of Economic Regulation* that strategic policy statements should provide long-term stability to both the regulator and the regulated, and so should not be revised more frequently than once a Parliament.
12. However, it will be important to keep the statement and its directions under review in light of any changes that arise during this period, most notably in relation to the Draft Water Bill and the changes to the regulatory framework for the next price review.

Direction I

13. We welcome the direction that Ofwat should avoid regulatory uncertainty wherever possible, and take appropriate account of investor views. In a sector as capital intensive as water, maintaining the confidence of investors is fundamental to being able to fund the investment essential to maintain services at a rate that keeps bills affordable.
14. The regulatory system for the England and Wales water industry is seen as a global gold standard by investors, and has attracted over £100 billion of private investment over the last 20 years at efficient rates.
15. We welcome the statement that the government will not take risks with this successful regulatory model. Investor confidence is hard won, and given that over the next 20 years a similar amount of

investment will be needed to the last 20 years, maintaining investor confidence will be an ongoing and continual requirement.

16. We also welcome the direction that Ofwat needs to provide thorough impact assessments of significant proposed changes. We note this has not always been the case in the past.
17. Any proposed changes should be evolutionary, to safeguard the benefits to customers of the current model, and should be supported by robust evidence on the benefits, and costs, of the specific changes being considered so that evidence-based decisions can be made.

Direction V

18. The direction is right to focus on ensuring that the sector, through the regulatory framework set by Ofwat, is focussed on meeting long term challenges such as climate change.
19. Price reviews must be stepping stones towards longer term goals, rather than ends in themselves, and we agree that the 25 year water resource management plan time horizon should be seen as a minimum, not a maximum.
20. In taking a long term view, it will also be important to recognise that it may be necessary to invest now to avoid compromising future service delivery, despite the inevitable uncertainty caused by climate change and the imperfect scientific understanding of its impacts.

Direction VI

21. We welcome the Government's direction to Ofwat to keep under review the impact of its regulatory approach on innovative schemes such as catchment management.
22. The industry has been at the forefront of developing private sector ecosystems services payments, as acknowledged in the Natural Environment White Paper.
23. Companies are always mindful that catchment management schemes should deliver demonstrable customer benefits; however, operational and financial partnerships could be developed in future with conservation, farming and community groups where the benefit to customers and the environment could be greater than it would be if smaller projects were developed separately.

Continued...

Direction VII

24. We welcome the Government's direction that Ofwat should have regard to the impact of their regulatory approach on water companies' sustainable management of water resources.
25. The recent drought has concentrated thinking within the industry and amongst other abstractors about what level of resilience would be acceptable to customers, and whether, for example, standpipes, part of many drought management plans, would be acceptable should there be another drought.
26. We are keen to establish with our regulators, other abstractors and government what level of resilience we should be planning for as a country, and what level of investment would be appropriate to that end.

Direction VIII

27. While for most customers, water bills are affordable, we acknowledge that some customers find their water bills, along with other household expenses, difficult to pay. Companies are keen to help those who have difficulty in paying, and to have better tools to be able to take effective action against those who could pay.
28. This area of social policy is one where it is rightly for government to provide direction, so we support the direction for Ofwat to keep this area under review. In doing so, it will be important to recognise that affordability is a complex problem, and different solutions may be appropriate in different parts of the country.

Direction IX

29. It is a fundamental principle of independent economic regulation that regulators act within the boundaries set by Parliament. The direction that Ofwat should not anticipate or pre-empt decisions regarding future reform of the sector, which are for the Government and Parliament to make, is therefore a welcome confirmation of the established constitutional arrangements.
30. The requirement on Ofwat to report annually on how its approach to competition aligns with wider Government policy will provide helpful transparency. As well as covering the retail market reforms for

business customers, explicitly referred to in this section of the document, it would be helpful for Defra to confirm that this report, and the direction itself, would cover any activities where Ofwat proposed to promote competition, including upstream activities.

Direction X

31. This direction is right to focus on the 2014 price review and its impact on customers and other key stakeholders.
32. However, in addition to Ofwat reporting on the impact of the review after the event, so that lessons could be learnt for future reviews, it would be helpful for Ofwat to report on progress towards the 2014 Price Review, bearing in mind the significant changes to the regulatory framework that Ofwat has proposed and the need to ensure that any changes are implemented effectively.
33. If there are any points that you would find it helpful to explore further, I would be happy to do so.

Yours sincerely



Rob Wesley

Head of Policy

Tel 020 7344 1819

Fax 020 7344 1853

E-mail rwesley@water.org.uk

www.water.org.uk