

THE WATER REPORT

Please help us get fast feedback on key industry issues and policies by joining our The Water Report Expert Forum. The process is simple, easy and completely anonymous. You will be emailed a survey once every few months by our research partner Accent, to complete online. Accent send us aggregate, anonymised data which we report in the following issue.

We are actively seeking new members, so if you are working at a reasonably senior level in the sector, within a company or at another stakeholder organisation, please email karma@thewaterreport.co.uk to join. Thank you very much to our existing members.



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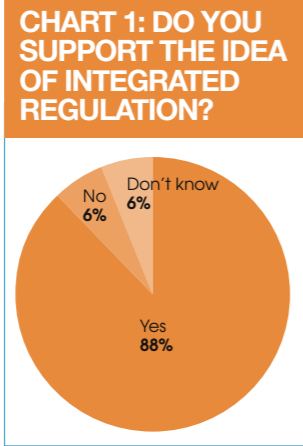
The sector strongly supports the prospect of one, joined-up water regulator – but views are mixed on how best to make it work.

Water sector opinion, as articulated by those on our Expert Forum, is enthusiastically behind the idea of setting up a single regulator in England and in Wales, wrapping in drinking water, environmental and economic functions. As chart 1 shows, 88% of respondents to our latest sentiment-seeking survey supported the idea of integrated regulation overall.

Opportunities
The opportunities are numerous, the Forum said. Factors listed included:

“Integrated regulation... reduces duplication, speeds approvals and focuses outcomes.”

- Ending the overlap / gaps between regulators, and instead enabling intelligence sharing and integrated solutions to address several challenges through one action or investment.
 - Providing better clarity for all, including on strategic direction, leading to less conflict.
 - Offering better value, including through ending duplication and better utilising resources.
 - Aligning priorities to overcome the current siloed approach and drive better outcomes. This includes enabling informed trade-offs to be made.
 - Agreeing a glide path between short and long term objectives.
 - Enabling a consistent strategic narrative.
 - Supporting regional (cross-sector) and catchment planning.
- Just a few of the many enthusiastic comments we received were:



“Integrated regulation... reduces duplication, speeds approvals and focuses outcomes. Companies gain certainty to invest, innovate and collaborate across catchments. Customers see better service, fairer bills and transparency. Environment benefits from holistic planning, data sharing, risk-based oversight and climate resilience.”

“There is an opportunity to streamline the duties of the regulator – making it clear what is essential, and what is merely nice to have.”

“I have long supported the integration of the EA and Ofwat (not so sure about DWI) as recent history has shown that political pressure to not increase bills has resulted in under-investment in the sector. By bringing them together, a national water policy that is cognisant of the environment as well as bill payers would be an improvement. We need to develop a medium-to-long term vision in a world of climate change – i.e. more floods and droughts – and invest in increasing the resilience of the asset base. A joined up regulator could look on the environment as a client.”

There was some wider reticence about the DWI being wrapped in. One member urged: “Do not include DWI in the new regulator – it is too important and doing a great job to be compromised by a large new regulator.”

But on the whole, the Forum was excited about the

forthcoming change, as this comment encapsulates: “This is a real opportunity to make a real step change that could have massive benefit for the whole country. I sincerely hope the opportunity is not wasted through political delays and uncertainty/watering down of the Independent Water Commission recommendations. The volatility, uncertainty and challenges we face are not going away and real change across the industry is essential if we are to meet these challenges and change the perception and performance of the industry.”

Mitigating risk
All that said, the Forum was cognisant of the many risks involved in bringing regulators together under one banner. A key concern was getting the right balance between the composite interests – environment, finance and customer. Comments included:

“Risk that the board discussions/decisions become too focussed on one or more of these agendas.”

“The risk is that economic regulation will consider itself to be the senior partner. The water companies’ main purpose is firstly to protect public health through the provision of clean drinking water and effective sanitation, and secondly to protect and improve the environment. Economics should support the behaviours and investment to deliver

these imperatives – rather than operate as a perverse influence. Government will need to be very clear about priorities and outcomes.”

“Loss of genuine world-class expertise (especially important with DWI) in favour of more generalist approach – this has happened in the EA with the reduction in the scientific programme leading to loss of experts.”

“Risk that drinking water quality issues are lost in the new regulator.”

“Must retain investor confidence for the privatised model to work - a regulator not focused on the City-view could lead to a flight of capital.”

Many were concerned that change could prove superficial if behaviours don’t also shift:

“The main risk is that current mindset / practices continue, if the new regulator doesn’t have the right forward-looking culture and becomes an extension of the current system.”

“Creating the best of all regulators rather than a mediocre mishmash from what went before. Avoiding this will require a clear focus, senior sponsorship and engagement with all stakeholders.”

“This is the opportunity of a generation. We can’t let that slip through our grasp by just having the same old regulation with a pretty new ribbon around it.”

Other risks identified included:

- Size and complexity slowing decision-making.
 - Less transparency and blurred accountability.
 - More centralisation – “One size does not fit all – regulator must take a regional approach to water management plans rather than force everything into a national model”; “A less specialised body will be less able to deal with the nuances of the industry”; “Danger everything gets dumbed down.”
 - Increased regulatory burden, micromanagement, intrusive regulation
 - New silos – “By integrating in one way, silos are created elsewhere. For example a water only regulator may not take account of emissions to air or land... [and] how will water be allocated if an integrated regulator is just for the water industry? Agriculture, industry and the environment are also users of water.”
 - Speed of transition – “Too fast and there is a danger that things are missed; too slow and the sector will lose momentum.”
- However, on the whole the Forum indicated risks could be managed, if implementation is effective, long term strategic objectives clear, and simplicity championed.
- So what might that look like?

Equal partners?
First, we asked: should the regulatory functions (economic, environmental and drinking

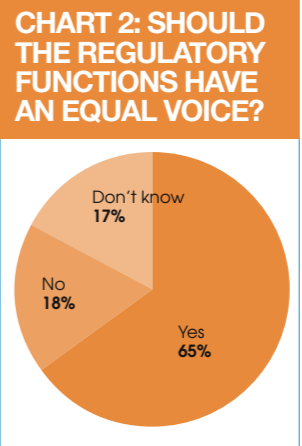
water quality) have an equal voice in strategic decision-making within an integrated regulator? As chart 2 shows, two-thirds said yes, with the remainder split between disagreeing and being unsure. One respondent called this “the million dollar question”.

Most thought equal balance was key, as this comment epitomises: “It will be key to have parity between regulators – to create a functioning, and healthy, tension.” Another said: “Equal weighting will be needed to fully understand the challenges and balance the best outcome.”

As indicated in some of the earlier comments, some believed economic functions would try to dominate and would need to be reined in. One said: “Without this [equality], funding and direction goes / is directed by whoever is loudest. Historically this has been the economic regulator, which has almost entirely led to the dire situation the industry is in now.” Another argued: “The raison d’être for existence of water companies is to provide a service: drinking water for public health and environmental protection. Money/finances/economic regulation are only a facilitator for these primary purposes.”

Notable though is that not all agreed with that outlook. One said: “While it would be equitable if all were equal, the practicalities are economic regulation should take priority, public health next and then environmental regulation.”

More widely, some respondents put forward the view that customer preferences should guide the balance of power between regulatory



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WHAT SHOULD THE INTEGRATED REGULATOR'S CORE OBJECTIVES AND DUTIES BE?

“Restore trust and confidence in the sector through being open about how and why decisions are made.”

“The existing ones can still apply: promoting the interests of customers and protecting the environment.”

Primary: 1. Protect interests of customers including for public health/drinking water quality. 2. Ensure the financeability of efficient companies. Secondary: 3. Protect and enhance the environment.”

“Protection and enhancement of the environment. Efficient and effective regulation of sectors including compliance, performance reporting and enforcement. Allocation of water.”

“Regulate monopoly water companies ensuring they comply with their licence conditions and deliver a sustainable service for all today and in the future. There is a need to rebuild trust.”

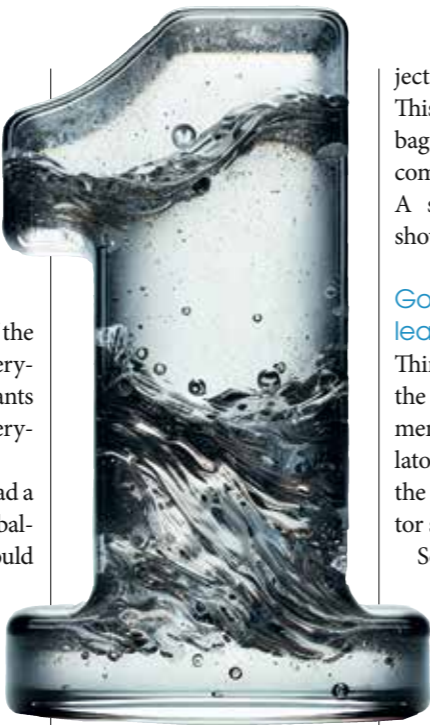
“We need to develop a long term vision of water resource management for the country and then devolve that into regional water management plans (WRMP & WWRMP). The new regulators core objectives and duties should fall from that: 1. Ensure it is financeable (if it is to remain privatised). 2. Progressive in its quality indicators (DWI etc). 3. Led by science not by politics. 4. Police the environment. Everything else must be tactical to achieve that strategy. Five year economic plans driving 100 year investment programmes does not work.”

“To protect public and environmental health. But the regulator needs to also be more than just cognisant that solutions are not just held and owned by those they regulate. There needs to be a wider remit to ensure where solutions are best delivered at customer level, that happens. There needs to be a greater focus on societal responsibilities.”

“To arrive at the correct prioritisation of improvement / investment to meet the key prevailing issues. To ensure the failures of the current system are properly addressed, eg base maintenance. To be cognisant of the impact of bill increase on customers and vulnerable customers.”

“Assuring that water companies meet their obligations affordably and that they are appropriately incentivised to continually improve. The regulator should also be an integrator, promoting collaboration within and outside the water industry to deliver its objectives.”

“Long term, sustainable development of a resilient and integrated water industry balancing the needs of the customers and environment in a transparent way. Making clear what can and cannot be achieved for the funds available.”



jectives and duties should be. This attracted quite a mixed bag of answers, hinting at the complexity of the task in hand. A selection of responses is shown in the box.

Governance and leadership

Third, we asked for views on the best governance arrangements for an integrated regulator, and/or on what qualities the leadership the new regulator should have or avoid.

Some had clear views on a desirable structure. One offered: “An integrated regulator should have a unitary board with a majority of independent non-executive directors, a single accountable CEO, and statutory committees for economic, environmental and drinking water quality functions. Include an independent consumer panel, robust audit/risk, published minutes, and clear conflict-of-interest rules, with regional advisory forums.

Leadership should demonstrate integrity, independence, technical breadth, systems thinking, stakeholder empathy, and decisive, evidence-based judgement. Prioritise transparency and

Objectives and duties

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public health. Avoid politicisation, regulatory capture, defensiveness, groupthink, short-termism, and opaque decision-making.”

Another shared: “There will need to be an accountable chair, but the structure of the regulator board should contain more expertise (the accountable ‘chiefs’ for the regulatory functions. The role of non-execs can change to customer, engineering, technical advisors using constrained discretion, rather than through board decision making.”

Another offered: “Governance: move to a lean supervisory model. Leadership: move to a grown up partnership like Scotland away from the current adversarial approach.”

The most commonly cited issue in terms of governance concerned the regulator's relationship with government. Some briefed that independence was key: “Independence from political gaming; strength of character to withstand political criticism and authority to regulate for the long term – outwith the five year political cycles;” and “The new regulator should be arms length from government. Political interference in regulatory decision making is a significant risk.” An adjacent comment was: “The system planner and the regulator must be kept separate.”

In stark contrast, others argued regulator and government should be closer. “The new regulator should have the ethos of a government department. Ofwat have in the past had too much focus on academic economic theory rather than delivery of government objectives;” and “I would convert it from a non-ministerial government department to a ministerial government department.”

Another main thread was on the credentials of those

in leadership roles, and from where they should and shouldn't be sourced. Comments included:

“It should be led by and guided by pragmatists rather than idealists. Water regulation is messy and searching for perfect solutions and decisions is a fool's errand.”

“They need to be able to think and act holistically and at a societal level...not just towards those they regulate.”

Leadership qualities: visionary, collaboration, listening, purpose driven, strive for continuous improvement.”

Chair: consumer background/focus. CEO: eco reg background. Execs: environment, drinking water quality, enforcement, price reviews/regulation, supervisory. INEDs: majority of independents (??) covering relevant backgrounds. INEDs should be full time or near full time, not one day a month.”

“It cannot be dominated by ex-water industry executives. It needs expertise across industry sectors, environment, customer, regulation, data and digital management.”

The transition

Finally we asked for recommendations on the practical aspects of the transition/merger. There was tension between a desire for clarity quickly, and taking time to get things right. Comments included:

“New regulator should be set up now in shadow. Ofwat could allocate budget and floor space to allow new regulator to be put in place. Defra could appoint chair and CEO now. Ofwat and EA/DWI could TUPE staff across to new entity to work on changes to regulatory regime in line with IWC.”

“Take the time to do it right. Pace could be the enemy of a well-designed organisation. Put effort into creating a

WHAT ABOUT WALES?

“It is not clear how Welsh Water will manage with two systems – they provide water and sewerage services in Herefordshire which will be under a different regulatory system from the rest of their area. Should they follow Severn Trent's lead with Hafren?”

“Make sure the Defra White Paper prioritises enabling legislation and the Wales Act.”

“There has always been a lot of confusion over the English/Welsh border with respect to water. It would be nice to have a clearer demarcation.”

“I would, obviously, look on Wales as a unique habitat and consider regional sensitivities but no more than anywhere else.”

“Rivers are no respecters of national boundaries and so cross-border accountabilities need to be established early, and transparently, so that both sides of the border are clear who does what, where. The Danube catchment involves 19 separate nations, so we should be able to manage the complexities of two!”

shared culture. Pay enough to attract and retain talent.”

There was also tension between getting new blood in and retaining expertise. Comments included:

“It will be important to retain the majority of Ofwat staff, to ensure continuity. The emphasis needs to be on changes in strategic structure and guidance – evolutionary rather than revolutionary.”

“Keep the good people.”

“Existing regulators (especially Ofwat) should NOT be allowed to develop the changes/reforms to the regulatory framework envisaged. IWC report is quite clear that they are not up to it and the cultural problems/concerns people have with them will mean that whatever they come up with will not be accepted by companies and stakeholders.”

There was more agreement that engagement in and out of the sector should be thorough, continual and transparent; that good project management principles should be deployed; that communications should be effective throughout to help rebuild trust; and that approaches should be tested through regulatory sandboxes and a shadow organisation.

Some respondents had practical considerations front of mind, including that AMP8 has to be delivered in parallel

to any transition, and regarding forward business planning. One said: “Avoid having two business planning processes simultaneously (i.e. not PR29 plus a new process).” Another advised: “Scrap the current strategic frameworks, implement a bridging AMP instead of a full PR29, and focus our efforts on developing the new system planning framework first, with integration in 2033.”

Some comments specific to the situation in Wales are shown in the box.

In the round, while the idea of a single regulator unites the sector, establishing one that is effective and meets everyone's idea of what good looks like will be quite the task. As one participant commented: “Good luck to all involved!”

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