

Environment, Food and Rural Affairs Committee

Oral evidence: Regulation of the water industry, HC 1041

Wednesday 11 July 2018

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[Watch the meeting](#)

Members present: Neil Parish (Chair); John Grogan; Dr Caroline Johnson; Sandy Martin; Mrs Sheryll Murray; Julian Sturdy.

Questions 182 - 288

Witnesses

I: Rachel Fletcher, Chief Executive Officer, Ofwat; Sir James Bevan, Chief Executive Officer, Environment Agency; and Tony Smith, Chief Executive Officer, Consumer Council for Water.

Written evidence from witnesses:

[Ofwat](#)

[Environment Agency](#)

[Consumer Council for Water](#)

Examination of Witnesses

Witnesses: Sir James Bevan, Rachel Fletcher and Tony Smith.

Q182 **Chair:** Good morning. Thank you very much for joining our inquiry this morning to present evidence to us. We are getting on with our water inquiry. It is good to have you here. Starting with Tony, could you introduce yourselves across the panel, please?

Tony Smith: I am Tony Smith, the chief executive of Consumer Council for Water, which is the water watchdog that looks after the customers of monopoly companies.

Rachel Fletcher: I am Rachel Fletcher, the chief executive of Ofwat, the economic regulator.

Sir James Bevan: I am James Bevan. I am the chief executive of the Environment Agency, which is the environmental regulator.

Q183 **Chair:** Thank you very much. When you speak, can you look forward towards the microphones, please, because it picks up better that way? Thank you.

I have a fairly straightforward question in the first instance: how do Ofwat, the Environment Agency and Consumer Council for Water work together to regulate the water industry?

Rachel Fletcher: The first thing to say is that it is really important that we do work together and that we have a coherent and holistic system that drives the best possible outcomes for customers and for the environment. There are a number of intersections and areas where we very consciously work together. There are also a number of, if you like, future-facing challenges that we have already agreed we want to work together on.

Q184 **Chair:** You would regulate the water companies themselves, would you not? The Environment Agency will talk later, but you would have the powers on pollution and that type of thing. As far as the pricing structure and everything is concerned, that is your job, is it?

Rachel Fletcher: It is, but we do work hand in hand with the Environment Agency to incentivise the companies to meet their statutory environmental standards and, very importantly, to engage with customers and find out what they might be doing above and beyond what the statutory requirements on them are with regard to the environment. Although we are the economic regulator, I believe that we have a very important role in protecting the environment. One of our duties is around resilience in water and wastewater, and I do not believe that we can possibly be effective in securing long-term resilience of water supplies without having deep regard to the sustainability of the ecosystem on which the water sector is built.

Q185 **Chair:** At the end of the day, the water companies will come to you and



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say, "We need to spend an awful lot on infrastructure and on cleaning up our water supply, our processing sewage plants and the like, so we need to put the bills up." The bill-payers do not want to pay any more, so how do you balance that?

Rachel Fletcher: This is exactly the kind of conversation that we have with the Environment Agency. The first thing is that improving the environment is not always about spending more money.

Q186 **Chair:** The question I really want to ask you is whether you have the ability and the staffing to drill down on the water companies as to whether they are telling you slightly inflated figures or not. They will always say they want more money—everybody wants more money—but the bill-payer does not necessarily want to pay for it.

Rachel Fletcher: Yes, we do challenge them. We have been looking very recently at their plans for meeting the new environmental standards and have been working jointly with the Environment Agency on that. We challenge them about whether they are taking the most cost-effective approach. We also challenge the companies to talk to their customers. Customers do care about the environment and do recognise that part of what they are paying for in their water bill is to meet improving environmental standards. It is important that the companies get a proper understanding from customers about what they are willing to pay for and that we work together to push companies to come up with the most efficient solutions.

Q187 **Chair:** We will leave it there, because Sheryll's questions are very much on the same lines. Sir James, how much attention can the Environment Agency devote to regulating the water companies, given its competing priorities and a reduced budget? Do you spend every working hour looking at the water companies?

Sir James Bevan: A lot, Chair. If I may answer your question about how we work together as regulators, we work well. There are three regulators. As well as the Environment Agency and—

Q188 **Chair:** You would say "well". I want you to prove to us why it is well.

Sir James Bevan: I would like to have that opportunity. It is important to understand that, in addition to the Environment Agency, which is the environmental regulator, and Ofwat, which is the economic regulator, we also have the Drinking Water Inspectorate, which is the health regulator. It is good to have three regulators because we can all focus on the thing that we are experts at, but, as Rachel said, it is essential that we work together, and we do. As an example, as you asked, the price review, which Ofwat are leading for the next five-year period, is a really integrated process. It is led by Ofwat, but the Environment Agency is a full player in inputting into that, in terms of what we want from the companies with regard to their environmental performance, what we want from them on drought, and all the other measures that we want to



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see are integrated into that process. That is a good example of where the three of us are effectively working to deliver a common output.

- Q189 **Chair:** You are naturally independent of the water companies, so you have a role very much to play in saying, to a degree, what the water companies are asking for in the means of extraction and doing more to their sewage works and the like. You would review all that, would you, and do you have the resource to do it?

Sir James Bevan: We are a classic regulator, so we set the standards that the water companies have to meet in environmental performance. We write those standards into the permits and licences that they need in order to operate, including what they discharge when they have gone through their systems. We monitor, we check, we inspect and we ensure that they adhere to those standards and, if they do not, we have measures of increasing severity to ensure that they do.

- Q190 **Chair:** Tony, as far as the consumer getting a good deal, are they getting a good deal or not?

Tony Smith: It is mixed. We are not a regulator, but we do represent customers in the regulatory process and with each of the regulators. We monitor the companies very closely, specifically from a customer perspective. We make sure, if there are any areas of detriment that Ofwat, the Environment Agency or Drinking Water Inspectorate can deal with, we propose solutions to that. When we were set up, customers hardly got a look in in the regulatory process. That has changed today. Customers are much more central. There is still a lot that can be done with the water companies and also with setting things like the environment programme; we would like to see much more customer involvement in that too, but it is a lot better than it was.

Are they getting a good deal? Clearly, the industry has improved things a lot in terms of the service standards, but it has come at a cost to customers; there have been quite spikey price increases over the last 20-odd years and there has been a degree of generosity, in the past, by the regulator, which we hope has put right now.

- Q191 **Chair:** You would like to see prices a little tighter, would you?

Tony Smith: Yes. The thing that really aggravates customers is when prices take a big hike. If you could have a smoother track—and, remember, inflation gets added to these prices too, and that can really aggravate customers. Particularly in the south-west we have seen that in the past, but it is true everywhere.

- Q192 **Mrs Murray:** Rachel, I wonder if I could ask you how Ofwat's approach to the price review evolved, and what the difference is between the price review 2019 and 2014.

Rachel Fletcher: At a high level, it is going to be a much tougher settlement for the water companies, and it is really helpful that Ofwat has



made that clear very far in advance. We have already signalled that there are going to be lower returns for investors than were seen at the current price settlement and has been seen across any other regulated settlement. We have already said that we are not going to allow customers to pay for inefficiency, so any companies that are not performing in the top quartile of efficiency will effectively not have their costs covered by customers.

We are continuing to push on in making real step changes in some of the performance commitments that we are expecting from the companies. On leakage, for example, we have put a challenge down to the companies that they need to be aiming for 15% reduction in leakage over that five-year period. I am pleased to say that some companies have already signalled that they will be aiming to reduce leakage by very much more than that. There are some really tough challenges on the companies.

Tony has already alluded to the involvement of customers in the process and that is another step change from the last price control process that Ofwat ran. We are requiring every company, in pulling together its business plans, to have really meaningful engagement with their customers, to understand what kind of performance levels they want, what they are willing to pay for and what is on customers' minds that the company needs to be addressing. We have put in place consumer challenge groups in each company, which are there effectively to make sure that companies do that customer engagement effectively and appropriately and then that they reflect what customers have said to them properly in their business plans. We will get an independent report from each of those challenge groups when the company's business plan comes in.

There are some real step changes and additional pressure on outcomes, especially on those that relate to the environment.

Q193 Mrs Murray: I am going to come on to the environment with Sir James. Sir James, how does Ofwat calculate and make allowance for environment in the outcomes of the PR19?

Sir James Bevan: One of the really big advances in PR19 is that it has much greater focus on incentivising the companies to invest in long-term resilience—greater resilience to drought and to flood. That is a good example, Chair, of Ofwat leading something that has had strong support from the Environment Agency. We feed into that in three main ways. First, we have set out and fed into the process and to the water companies our expectations of what we want to see from the companies in the PR19 process, which is basically three things: pollution down, enhancement of the environment up and greater investment in resilience.

Secondly, we have fed into and will look at their drought plans. Each company has to produce a drought plan—a fairly topical issue—and we are part of the process, with Ofwat, of agreeing those.



Thirdly, within the PR19 process there is a specific environment programme that each water company has to contribute to, and we help set, with the companies, what we want those companies to do in environmental enhancement over the five-year period of the PR process.

Q194 Mrs Murray: Mr Smith, we have heard that Ofwat is stepping back and, as Rachel has outlined, requiring water companies to talk directly to their customers about their customers' needs. Do you think this hands-off approach is working, or should Ofwat be more prescriptive?

Tony Smith: In principle, the idea of making the companies responsible for their customers has to be a good thing. In the past, companies have tended to hide behind Ofwat. When there is anything tough going on, they tend to blame the regulator rather than deal with it themselves. In principle, that has to be a good thing. It is still quite important, though, that Ofwat steps in and acts and punishes companies when they do not do the right thing.

We would also like to see a very strong incentive on the companies to focus on their customers all of the time, not just during a price review period. We have suggested a much stronger incentive on the companies to do just that. There is a mechanism there, called C-MeX, but the question is whether that is going to be tough enough and have a big enough financial impact on the companies to do that. In the big picture, though, the last three price reviews have been much more customer-focused than the previous ones, and that is a really good thing. This is really important, because if price reviews are not acceptable to customers, they will aggravate the legitimacy problem that exists in the water sector.

Q195 Chair: Rachel, some would suggest that Ofwat has allowed the water companies a licence to print money, basically. The City has had a very good return and it needs a good return, but it has probably had almost too good a return. Have you allowed them to get away with murder, or are you really changing now? While I accept they have done a good job in many respects, in others they do need to give less money to shareholders and more to infrastructure. Are you confident that you have the teeth to deliver that?

Rachel Fletcher: We are pushing on a number of fronts to make sure that the profits and returns to investors are properly balanced against and in return for delivering great things for customers. In the price review that we are about to set, as I said earlier, we have already set a very low level of return.

Q196 Chair: I cannot remember how long you have been in the job; it is not that long, I think. The politics and the mood music has changed out there and Ofwat seems to have changed with it. Do you not think Ofwat should have been more ahead of the game than what you were?

Rachel Fletcher: For about five years now, Ofwat has really been pushing on the agenda to make sure that companies are acting as you



would expect from a monopoly provider of an essential service. We have put in, as I said, a very low rate of return in the current price review. We have been pushing as well to improve the governance of the companies. What we are doing right now is another wave in that direction—another wave of regulatory initiatives; that is not just low returns and returns that we think are commensurate with the level of risk that the companies are taking on, but only last week we announced that companies must share any benefits that they get from having high levels of debt in their structure. We are pushing the companies to have much more financially resilient structures and to make sure that they share any benefits from financial engineering.

Q197 **Chair:** Sorry to interrupt you. On the governance side of the companies, do you have the powers to intervene and say, “The governance of your company is wrong”?

Rachel Fletcher: Only today we have gone out with a consultation suggesting that we put a requirement in the licence on companies to comply with standards of governance and governance principles that we set. At the moment, our principles are voluntary, but I must say that even with a voluntary set of principles in place we have seen improvements in corporate governance. We think it is time now that those companies should be bound to those principles through the licence.

Q198 **Chair:** Do you need more powers, or what?

Rachel Fletcher: One of the things we have flagged is that our powers to impose new licence conditions on water companies are constrained. If a water company does not agree with our proposals, our only recourse is to refer the matter to the Competition and Markets Authority. We feel that that slows things down, it hampers our ability to drive through important changes and, ultimately, were there to be a legislative opportunity, that is the kind of new power that we would really welcome.

Chair: We will probably talk more about it, but it will be interesting to be able to put in our report the fact that you feel clearly that you need more powers on governance, because there has been a problem with a number of companies—Thames Water and others—in the past, which they are trying to put right now. We want to perhaps try to act a bit more quickly than we have in the past.

Q199 **John Grogan:** Could I turn to the retail market, where there has been a big change in the last few years, particularly on the business side? Ofwat has just done an analysis, so I would be interested in your initial conclusions. We have had some criticism from organisations like the Wildlife and Countryside Link, which has said that it was concerned that “Government and Ofwat are creating an increasingly fragmented and disjointed sector. This brings risks to the environment which relies on an integrated and joined up approach”. Waterwise said something similar: “In driving for competition we must be careful not to fragment the industry”. Could you give some comments on that?



Rachel Fletcher: It is a year since the business retail market has been opened and, yesterday, we published our first annual report of the market. Our overall assessment is that the first year has shown some promising signs, but there is a huge amount more work to be done for that market to really reach its full potential in terms of the benefits it can bring. I would have to say that when we talk about benefits, yes, of course, we are talking about savings to businesses, but we are also talking about the potential that the market brings for water efficiency products to come forward. So far, we have seen up to 500 million litres of water saved as a result of competition, but we think that is just scratching the surface of what we would expect to see as new retailers come into the market with new product offerings to attract customers.

You raise a very legitimate concern about the risk of fragmenting the market, and that is something that we will be keeping a very close eye on. But we do believe that there is a role for competition—new players coming in with products, frankly, that the water companies are quite often slow to offer to their customers. We have already opened up the market for businesses to connect new housing developments, for example, and it is through those new entrants that we are seeing the cutting edge of innovation on introducing dual water systems, grey water systems and quite interesting water efficiency systems. Unless we really allow room for new players to come in, we are constantly going to be looking to the water companies, which have lots of other things on their mind, to bring forward some of the water efficiency that we are hoping to see in the future.

Q200 **John Grogan:** I will ask Tony for a comment on that in a second. You regulate both England and Wales, do you not, and this retail competition is just in England at the moment?

Rachel Fletcher: That is right, yes.

Q201 **John Grogan:** It is also in Scotland, which you do not regulate, and it has been there for slightly longer. In Scotland, it operates in a model where the ownership structure is publicly owned, so, in theory, there is nothing to stop retail competition with a publicly owned water industry, is there?

Rachel Fletcher: As you say, Scotland has demonstrated it is possible to do that, yes.

Q202 **John Grogan:** Tony, do you have any comments from a consumer point of view? Also, in the next 20 years, do you see the water industry having possible competition for individual consumers as well as business?

Tony Smith: First, on the business market, we are talking to business customers all the time and we are doing customer research of those customers. As Rachel said, customers are engaged in the market, particularly bigger customers, and some of them are switching and some of them are renegotiating, so that is good.



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The issue at the moment is amongst the smaller business customers. Probably around 50% of them do not even know they have a choice and those that do need to see real benefits of the sort that Rachel has described. It is early days. It is working. We do need to make sure the wholesalers and the retailers work well together, because that is definitely an issue when there is a problem for customers.

Your question about domestic customers is an interesting one. For us, the real test is how it works for small business customers, as that will give us a strong indication of how it would work for domestic customers. A couple of years ago, Ofwat did an analysis of the opportunity for domestic retail competition, which showed that although many domestic customers wanted a choice, they were disappointed with the potential savings on offer. Somewhere between £10 and £40 is really the maximum amount of money you are going to get out of the retail market. As we have seen in the energy sector, where customers are not switching for £200, that small saving was likely to create a bit of disinterest in the market. What we need to do is look to see if the business market works for smaller customers and then take a view from there as to whether there is an opportunity.

Q203 Chair: On competition, there is no real competition, is there? Basically, even if you are in the business sector, you only really save a bit on billing. All the charges for each company are then recognised in that bill. Competition only works if companies can bid lower for business and it just does not seem to work in the water sector. It is a monopoly, Rachel, as you said. They are monopolies in their own areas. Do we not need competition? In my constituency, you have Wessex Water on one side and South West Water on the other. Why should they not have a bit of a competition with each other, because we might get prices down and we might get things running a bit better? At the moment, they largely do as they like. Is Ofwat keen on that or not? Where are you on that one, or do you not want to venture into the competition market?

Rachel Fletcher: As Tony said, we are at the very early stages of seeing how the business market works, and there is a huge amount of potential to be—

Q204 Chair: There is very little saving there, is there? It is not going to work, really. If you are Tesco, one company can do retail for you and save money on getting all the bills together. That is virtually the only saving there is out there. There is no saving on the cost of the water, since that is still a monopoly in every different area because of the company. That is the problem. I do not quite see the way out of it; I accept that. Most private business works because of competition and, in a way, the water companies are private monopolies.

Rachel Fletcher: There is also saving of the business's time. As you said, a lot of the feedback we have had from businesses is that the convenience of having a single bill aggregated across all of your multiple



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sites is huge. We could not achieve that without opening up the retail market.

Also, the potential for innovation and technological innovation, particularly around data, is massive. We all see that in other aspects of our daily lives. One of the things that we are pushing on, as a regulator, is an improvement in the quality of data within the water sector.

Q205 **Chair:** That would be water usage. We will talk about metering in a moment, but all those types of things is what you are talking about, is it?

Rachel Fletcher: Absolutely. What new services and convenience can you provide to businesses once somebody comes in with a different view?

Q206 **Chair:** Does it create any real competition between the companies? I am not convinced it does, really.

Rachel Fletcher: It is certainly creating competition between those at the retail end.

Q207 **Chair:** Yes, that is right, but while there is only a small amount of saving to be made at the retail end, I am particularly interested in the fact that there could be savings and also some pressure to be put on companies if they had competition.

Rachel Fletcher: One of the things we want to explore—in fact, there is enabling legislation already in place that could be switched on—is allowing much more water resource trading and competition. We know that there are a number of organisations out there that are sitting on water resources.

Chair: We will probably talk about extraction in a minute.

Rachel Fletcher: That is an area. As you say, getting into other aspects of the value chain and creating markets and competition there is something that we are very interested in, not only because of the potential cost savings that that could bring, but of course that could also help us manage some of the environmental impact of the sector more effectively as well, and build resilience, particularly in situations of extended hot weather. There are other parts of the value chain.

The other area we are introducing is competition in and a market for the use of the bioresources that the water companies produce out of their waste treatment. Effectively, there is now a very vibrant market for those resources and they have been used to produce renewable energy. Increasingly, there is a question about whether that really needs to be part of the regulated value chain when, in fact, it is part of a wider and very competitive market.

Tony Smith: You are right that the retail market is very limited in terms of its scope, but good retailers can help their customers reduce their bills a lot. If you are a heavy water user and you save even 1% of your water, that is worth a lot of money. Similarly, on the wastewater side, trade



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effluent charges are huge for some customers, so again, if retailers can help, it reduces their bills, adds a lot of value to customers and does not affect the margins of the retailer. There are opportunities, despite the fact that it is only the billing and the—

Q208 Chair: If you save the amount of water you use, you are also going to save your costs on then disposing of the wastewater, are you not?

Tony Smith: Exactly, so there are opportunities, and we hope to see those things for those customers.

On the monopoly side of the business at the moment, that is why we are arguing that you want this focus on the customer. What you are trying to do is mimic what a competitive market would do, which is about what your customers think of you. That is why we are arguing with Ofwat that you should have a heavy, quite impactful financial incentive on the companies to focus on their customers.

On the issue of upstream competition, as it is called, there are definite benefits there to reduce the average cost to customers of the water. That is undoubtedly the case. We just have to be careful that we do not start unravelling cross-subsidies, which, in the geographic side of the business, on the wholesale side, can be very large and could have a very big impact on some customers.

Sir James Bevan: Just because they are monopoly suppliers does not mean that there are not some powerful incentives for them to improve and disincentives to doing the wrong thing. On reputational incentives, we have published today our annual league table of the performance of the big nine in terms of how they are doing on pollution and other major indicators. They hate being at the bottom and they want to be at the top and that helps to drive behaviour.

In terms of operational incentives, we will be less in the face of water companies that are doing the right thing, according to our regulatory framework, than those that are doing the wrong thing; there is an incentive to behave well.

Financially, in addition to all the financial incentives that are built into the Ofwat model, we will go after a water company that does not perform properly, up to and including very substantial fines. There are some incentives and disincentives built into the system, even though it is a monopoly.

Chair: I understand and I accept that. It is just that if you are a customer and you are not happy with your retailer or whatever, you just go to another retailer. If you have one water company right next to another, it is always very tempting, I would have thought, if you do not like the environmental management and the structure of one company, to buy your water from another. You cannot do that in water. At the moment, much as you are doing a good job as regulators, it still does not



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put enough pressure on these companies, I do not think. That is probably a debate for another day.

Q209 **Julian Sturdy:** Can I come back on something you said, Rachel? You talked about biowaste and the trade in biowaste. Could you touch on that in a little bit more detail?

Rachel Fletcher: Currently, this is part of the regulated value chain. What we are trying to do now is have a separate control for that part of a company's business, so that we can think, ultimately, whether this is something we can allow to be opened to competition, and where, effectively, the constraints on charges and so on, and revenue that is earned from that, comes through participating in the wider competitive market. What we really want to see is companies maximising the value from what is a really valuable resource and one that is an input into renewable energy production.

Q210 **Chair:** I take it that is sludge, is it, in biodigester plants?

Rachel Fletcher: Yes, either directly into the grid as biogas or being used to power combined heat and power plants. We are seeing pretty much all the companies with waste treatment plants now producing renewable energy from their sludge. It is a great example of the circular economy, and we want to regulate in a way that maximises the extent to which they do that, because the environmental benefits are huge.

Q211 **Julian Sturdy:** We are still classifying it as waste, are we?

Rachel Fletcher: We are calling it "bioresources", because we see it as not a waste product that you have a problem to dispose of; it is a valuable resource, which can be an input.

Q212 **Julian Sturdy:** There have been problems with the Environment Agency in what is classified as waste and non-waste, and the waste panel has closed and now been reopened, so is that becoming an issue?

Sir James Bevan: No. One definition of waste is that it is a resource that is in the wrong place. As Rachel says, there is lots of good stuff that you can do with biowaste provided it goes into the right places, whether it is fertiliser or feeding energy.

Q213 **Chair:** The Environment Agency has no problem with what you still class as a waste.

Sir James Bevan: We welcome and are working with Ofwat and the industry to ensure that waste is used as a resource rather than becoming a problem. The formula for success is having the right commercial drivers, but also the right regulatory framework to ensure that the right waste goes to the right place rather than ending up in the wrong place.

Q214 **Julian Sturdy:** Okay, but we are still classifying it as waste, though. If it is classified as waste, it is dealt with in a different way, is it not?



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Sir James Bevan: It will still be classified as waste and it will be regulated according to that classification.

Q215 **Chair:** This sludge goes into the biodigester; it then creates a digestate that goes onto the land. Are you confident that it does not have heavy metals and all those things in it? When you start to play around with all these things, it is all very good until such time as you spread something on the land that you should not be spreading. Has that been looked at?

Sir James Bevan: We have a regulatory role at every stage of the process—regulating what comes out of sewage plants, what goes on to land, and what ends up in the water environment, which is where it usually ends up. We monitor very carefully the waste at each stage of the process. At the moment, we are satisfied that, if it is properly regulated and provided that the operators follow the right guidelines, this can be managed in a way that is safe.

Q216 **Chair:** You and I have had conversations on biodigesters. I do not think you have enough powers on what comes out of them and what is spread on the land. Are you now telling me you are confident?

Sir James Bevan: I am always cautious about adding more “red tape”, because my and everyone else’s job on this panel is to help ensure that we have sustainable growth in the country as well as ensuring that we protect the environment and regulate well. I am always reluctant to reach for another regulatory tool if we do not need to. At the moment, I think that we have the tools we need to address this particular issue. If we conclude that we do not—and I have not yet seen the evidence that we do not—then obviously we ought to have another conversation.

Q217 **Chair:** Are you monitoring them properly across the country, because they are growing all the time? You will have more sewage going in them and it will be more digestate being spread on the land.

Sir James Bevan: We operate a risk-based, proportionate approach to monitoring, so we will always have proper monitoring where we think there are significant environmental risks.

Chair: Carry on, Julian. There is a little local difficulty I have, so I am using the opportunity to have a go.

Q218 **Julian Sturdy:** I was not aware of it, Chair, so I did not raise it for that reason. The point to make clear, though, is that if it is not going to be used, reused or recycled as waste, it ultimately ends up going to landfill, so there are other issues within that.

Can I move on to customer protection and complaints? Is the current consumer protection framework sufficient to protect the domestic consumer?

Rachel Fletcher: It is. There are a number of strands to it. There is obviously the work that we do, as the economic regulator: driving standards and having automatic penalties in place. There is the ability



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within the companies themselves to handle complaints, and there are clear requirements on them to have an accessible and efficient complaints-handling process. Obviously, we have the role of CCWater in handling any complaints that are not satisfactorily dealt with by the company and an ultimate recourse to alternative dispute resolution.

One of the questions we have put in our submission is whether that represents a really easy journey for the customers. There are a number of hand-off points in it and we see large dropout rates at each of those hand-off points. One of the conversations Tony and I have had since I joined in January is about what we can do to make that process more streamlined, and that is something that is worth considering.

Q219 Julian Sturdy: That is a really good point, is it not? Tony, how many people are aware of what the Consumer Council for Water does, would you say?

Tony Smith: Anybody who has a complaint is, because companies are required to tell customers, if customers have a complaint, that we would be the next stage of the process. Companies are required to do that, so we are on the back of every water customer's bill; we are in the *Yellow Pages*; and our website works so that customers can find us. The main thing is, when a customer has a problem, they know that we are there to pick up the next stage.

The complaints system works a lot better than it used to. When we were first set up, complaints were rising rapidly—20% per annum. They have fallen by 65% over the last few years, and that is because we have put pressure on the bad-performing companies. We got Ofwat to change the regulatory system around complaints. There are still issues, though. There are over 2 million complaints and unwanted contacts to the industry a year. About 10,000 of those come to us. Obviously, we get the more difficult cases, but there are issues still there. In particular, if you like, the growth area is billing problems. Over 50% of the cases to the industry and to us are around billing issues, particularly unexpectedly high bills and things like that. I agree with Rachel: we want to try to improve the process for customers so that they get what they need at the first point, ideally. That is what we are trying to do: to get the companies to resolve the cases.

Q220 Julian Sturdy: You say you are now getting about 10,000 complaints a year, and you say that has come down. Do you have any idea as to what level the water companies are getting complaints at? Obviously, you are the second point of call, so if it is resolved or people give up at the first stage, you do not hear about it, do you?

Tony Smith: As I say, there are over 2 million complaints and unwanted contacts a year to the water industry. That is down from well over 3 million a few years ago. The issue is that some of the companies take several stages to resolve a problem, so the customer is losing the heart to go through this process already, even by the time they have got to the



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end of the company's process. They might have three stages themselves before it comes to us, so that is one of the things we need to rationalise so it is much slicker. Also, you can often identify which cases are going to need more firm action more quickly, and they can get lost in a company's engine room for too long.

There is an issue around the number of complaints and then there is an issue around the timeliness of those complaints, and it is the timeliness bit that really needs to be addressed. What we want to see is an end-to-end look at this, to say, "How can we improve the whole process for customers?"

Q221 **Julian Sturdy:** If my maths is correct, and it might not be, what you are saying is you are getting less than 1% of those complaints coming through.

Tony Smith: Yes, which is not untypical for bodies of our sort; that is what you tend to see. Also in our research, we try to find out if there are customer complaints that are unresolved but we do not know about them. We are not seeing any evidence of that. We do explore this. We do a lot of customer research every year and customer tracking, to try to find out if there are hidden complaints as far as we are concerned. We are not seeing much evidence of that, so that is reassuring, to some extent.

Q222 **Chair:** I have one or two constituents who have complained to me that when they have got through to you, as the Consumer Council, not much has happened with their complaint. Do you think you need to get to grips with the complaints a bit more? I will throw you a relatively gentle ball at this stage.

Tony Smith: It depends what they are. We do not have any powers, which is an interesting point. We have no powers, so all we can do is argue with the company about, if you like, best practice across the sector. We are pretty successful at doing that most of the time, but there are some quite intractable cases where, often, the files are this thick. Some of these, and particularly the more complex issues, are quite difficult to do. Again, we are up against monopoly companies.

Q223 **Chair:** You say you have no powers, so I suppose if the company, at the end of the day, wants to ignore you, it can.

Tony Smith: That is what the ADR scheme—the ombudsman scheme—is there to do. Although it is a voluntary scheme, they cannot ignore it. If the ADR scheme finds that the company needs to do something, it has to do it; it has no choice in the matter. Also, there are other complaints that are Ofwat-related complaints, so these are in the more technical area.

Q224 **Chair:** The complaint very much is the bureaucracy of it all and, in a way, you have just highlighted that. I am not putting the blame at your door; it is just that by the time consumers have been to you, to the ombudsman, and here and there, they have almost lost the will to live. Of



course, quite a lot of them will give up through the process. What can you do, or what do you need, to sharpen up the response that you can give to consumers?

Tony Smith: There are two points. One is that we need to sharpen up what the companies do already. Some of them use three stages to go through the process, so the customers are already worn down by the time they have dealt with the company, and so we need to be able to put more pressure on them. The other thing is having a more seamless system between us and the final ADR adjudication. Those are the things we are keen to do, and that is what we have been talking about.

Q225 **Chair:** If we can make the process a bit more streamlined, people will feel as though they are getting somewhere and feel happier. At the moment, they feel as though they are pushing into a sponge and are not sure whether they are getting through.

Rachel Fletcher: In other sectors, once a customer's complaint has not been resolved for a particular period of time with the company, the company then effectively ends up paying automatically for that complaint to go to the ombudsman for review. That does tend to focus minds somewhat.

Q226 **Chair:** That is not the case with the water companies at the moment.

Rachel Fletcher: No, it is not, so these are the kinds of things that we need to look at.

Q227 **Chair:** Perhaps we could do the same with the Rural Payments Agency as well, while we are at it; that would be quite good. That is an aside.

This is something interesting that we might look into in our report, then; okay. This is what power companies are saying, is it—that they have to pay for the ombudsman complaint?

Rachel Fletcher: Absolutely. For an unresolved complaint, the customer takes it to the ombudsman and the company pays. It does focus them on resolving those issues that are within their gift to resolve. As Tony says, there are always going to be complicated cases.

Chair: Yes, I accept that. That is an interesting point.

Q228 **John Grogan:** Looking at consumer trust in the industry, Rachel, you referred to the financial engineering and so on. Looking at the financial structures, I think I am right in saying that you said that it is obviously always balancing the consumers and the shareholders, but the consumers should enjoy more the benefits of the debt structures that the water companies have and the financial engineering. Is there not an argument that consumers would benefit if the debt was a lot less? Greenwich University say it is £42 billion. Should you not be encouraging the water industry to reduce their debt, never mind consumers benefiting from it?

Rachel Fletcher: The package that we announced last week will give companies a very strong incentive to look at their gearing levels, because



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the financial benefits to them from being highly geared will reduce. We are also really pushing companies to make sure they have resilient financial structures in place.

Q229 John Grogan: Yes, and you have more powers now, following the 2014 Act, have you not?

Rachel Fletcher: Yes, and we have for some time now been asking companies to provide us with long-term financial resilience statements, so that we understand what their financial position is and how they can deal with the challenges emerging for them, as a company. As we go into the price review, we are asking each company, alongside their business plans, to show us that they are financially resilient over the next five to 10 years. That will form a really important part of our price review process, making sure that each of these companies does have the balance sheet in place that will allow it to withstand shocks and the money it will need to continue to provide customers with the services that they require.

Q230 John Grogan: You refer to the price review, which will be for the period 2020 to 2025, will it not?

Rachel Fletcher: That is right.

Q231 John Grogan: As I understand it, for years Ofwat has given what is called a “notionally efficient” level of gearing. That was as low as 50% in 1990, then it rose to 57.5% in the period to 2015 and to 62.5% in the current period. Are you saying that now you are going to reverse that? Prices are based on those levels. You have really adapted to the private equity model of financing water companies; you have not challenged it. Are you saying now that the water companies can look forward to that 62.5% coming down quite a bit in 2025?

Rachel Fletcher: The notional gearing that we have set—the allowed cost of capital, the allowed returns—for the 2025 period will be 60%.

John Grogan: I see. It is coming down.

Rachel Fletcher: We think that companies have strong businesses that they can raise debt on. The financing arrangements and exactly what balance of debt and equity they want to have is a decision individual companies should be making.

Q232 John Grogan: Should they bring it down or not? I am not clear. Are the current levels of debt a bad thing or a good thing, or are you indifferent?

Rachel Fletcher: We are saying that where high levels of debt are bringing benefits to companies, they should be sharing those benefits with customers. That feels only fair. We are also saying that companies that have high levels of debt need to convince us that that is not jeopardising the financial resilience of the company.

Q233 John Grogan: Financing costs, as I understand it, in the last period were



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27%, which is very high. Would consumers not benefit from it being 10%? Are you not being a bit soft on them?

Rachel Fletcher: We are not being soft. It is important that the industry can attract capital for the investment that is needed. We want to make sure that we get the balance right so that we can keep these companies afloat, but making sure that excess returns are not earned from companies focusing on financial engineering when they should be focusing on delivering better services and resilience for customers.

Q234 **John Grogan:** They can finance this through profits, though, can they not? A very senior politician—it was not my good colleague, John McDonnell; it was the Secretary of State—told the Water UK conference that, in cash terms, over £18.1 billion was paid out to shareholders of the nine largest English regional water and sewerage companies over the decade between 2007 and 2016; 95% of the profits went in dividends to shareholders. That seemed to be a clear lead that he was saying that more should be financed out of profits and less out of debt. Do you agree with that?

Rachel Fletcher: We have been really clear that we want to see companies submit transparent dividend policies where there is a very clear link between the dividends paid to shareholders and good performance for customers, and we want to see that they are making sure that, before they pay out dividends, they are meeting their obligations to customers and to other stakeholders.

Q235 **John Grogan:** I will ask Tony what he thinks in a minute, but should more profits go into investment? Some 95% of the profit went to shareholders. Should it be a bit less—80%, 50% or something like that?

Rachel Fletcher: I am not going to set a figure here. We have an incentive-based regime, so a well-performing company that is exceeding its performance standards—

Q236 **Chair:** Sorry to interrupt, Rachel, but I asked you a question about governance just now. If you are interested in governance and you think you should be interested in governance, you should have an opinion on whether 95%, 25% or 10% should be going to shareholders, or whether 90% should be reducing debt or being invested. That is what most private businesses do. They do not pay it all out to themselves; they put it into building up their businesses and reducing debt. I do not think you can wriggle too much. Either you are interested in governance or you are not. If you are interested in governance, which you have previously said you are, then you need to have an opinion. On the 95% to shareholders, the Secretary of State has a fair point, has he not?

Rachel Fletcher: We are interested in governance, but we do not run companies. That is a really important distinction.

Q237 **Chair:** Unless you lay down some guidelines to these companies, they are not necessarily going to change their attitude and they could carry on



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paying out 95% to shareholders. Either it is right or it is wrong. You have to have some opinion, because you are the regulator.

Rachel Fletcher: We are the regulator, but it is not appropriate for us to set a number. It is appropriate for us to set a set of principles by which companies should be being—

Q238 **Chair:** Is the principle of 95% too high?

Rachel Fletcher: With respect, that is a number. The principle here is that companies look, first and foremost, to serve their customers and that dividends are paid when statutory obligations are met and after making sure that the dividends and returns to shareholders match.

Q239 **Chair:** You also talked about high levels of debt. Do not forget that many of us have run businesses. You cannot keep paying out lots of money to your shareholders and keeping high levels of debt. Let us rephrase the question: if companies have high levels of debt, should they be concentrating on lowering that debt before they give 95% to their shareholders? Surely that is something you could look at.

Rachel Fletcher: Yes. We have been very clear with companies that if the high level of debt is impacting on the financial resilience of the company, they should be bringing down their gearing. We made that very clear to companies last year. I am pleased to say that a number of companies are listening to our message and we have commitments, at least in writing, from a number of the more highly geared companies that they will, in fact, be doing that.

I do want to stress that the details here, rightly, sit with the boards of these companies. We should be putting pressure on them, and we do, to take their responsibilities seriously.

Q240 **Chair:** If you, as Ofwat, announce that company X has huge levels of borrowing and is paying its shareholders 95% of its profits—it is not really profit, in some ways—are you going to state that publicly? That would put a huge amount of pressure on that company to do more about it.

Rachel Fletcher: This information is all publicly available and we do make sure that it is transparent and available.

Q241 **Chair:** But you do not name and shame these people. You are not prepared to do that. We have to dig through lots and lots of detailed work that you are doing to see if we might find it in a subparagraph somewhere. How open and transparent is all this? If we are going to do anything about this and change the attitude of these companies, it needs to be more public than it is at the moment.

Rachel Fletcher: In fact, we have been quite public in our criticism of particular companies and, as I said, I am pleased to see that those companies are taking some of the challenges that we have given to heart. As a result of public statements we have made, we have seen a



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complete change in the board structure at Thames Water, a change in the chief executive and chairman, and a substantial change in the ownership composition of that company. That is one of the companies that has made a commitment to reduce its gearing. We need to be careful how often we use that tool, but we are very prepared to name and shame and use reputational incentives; they are powerful.

We are stepping in and making it clear that we expect every company to have a transparent dividend policy that satisfies us that they are meeting the requirements of customers and other stakeholders—including, by the way, their pension funds—before they attend to their dividends.

Q242 **John Grogan:** I will ask Tony to comment on what he has heard, but you mentioned that companies are reducing their gearing ratios and some have been better than others. Welsh Water has been particularly good at reducing the level of debt. It is a mutually owned company.

Rachel Fletcher: Yes. One of the really interesting things about this sector is the variety of ownership models that we have. We have publicly listed, privately owned and, as you mentioned, the Welsh Water arrangement. That certainly helps us, as a regulator, and it is something I would like to protect.

Q243 **John Grogan:** Finally, would you have a view on pay levels of chief executives in terms of public trust? It is a monopoly business. It is easier than some businesses to run, you might argue. Is 20 times the pay of an MP sufficient, do you think, for anybody taking such a role?

Rachel Fletcher: We have been asking the companies to take the level of trust that customers have in them very seriously. As you say, they are monopoly providers of an essential service. It is right that customers expect different types of behaviours, different standards and higher standards in these companies than you might see in other sectors of the economy. Again, with respect to the Chair, it is not our role to set pay levels. What we have done is, again, to make it very clear that we would like executive incentives to be linked much more closely to how the company performs for customers and to stretching performance for customers; and that we would like incentives related to the financial performance of the company to be much less. That will drive executives to focus on the right things, and that is another of the new requirements that we put out last week.

Tony Smith: This is a big area where customers get very aggravated on the question of legitimacy, with some justification. If you look over the years since privatisation, the water industry has outperformed the market—FTSE—almost every year in terms of the returns for a lower regulatory risk than the FTSE companies. They have outperformed what you would expect, by a long way, almost consistently. In addition, some companies have geared up, as you were saying. In doing that, they have given special dividends back to their shareholders and, in effect, have



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increased the risk to customers, so there is a big issue here and it is not before time that Ofwat has stepped in to do this.

The companies must take responsibility for this. They cannot keep outperforming, otherwise that regulatory risk and political risk will increase dramatically, because it is right at the heart of customers' aggravation. I mentioned earlier that when prices go up it aggravates customers. When prices go up and customers see that the companies are making excessive returns, that they are gearing and that they have high salaries, they are giving a really bad impression to their customers, and we have to fix that.

Just going back to what we have done, in the past, we have been quite successful at getting companies to share some of their outperformance with their customers, to the tune of several hundred million pounds. We work with people like Welsh Water as to where they put their money back in, in terms of investment, but it is only scratching the surface. This is the one big area where there is a legitimacy problem and the companies need to deal with it quickly, backed by a tougher regulatory system.

Q244 Chair: It is interesting with this executive pay, because if you have a chief executive who makes sure that the shareholders get nice big dividends, the shareholders are not going to put much pressure on that chief executive's level of salary. The whole thing is self-fulfilling if you are not careful. Therefore, I think there is a problem here, because it is the shareholders who should deal with executive pay, but they are not going to if they are being dished out lots of money. The consumer, on the other hand, who consumes water from the company, has no say whatsoever in the executive pay of that company. That is where both the Consumer Council and Ofwat need to be tougher on these companies.

Rachel Fletcher: One of the governance reforms we want to make is a requirement that independent directors are the single largest group on the boards of water companies. That is a good way around the very problem you have just talked about.

Chair: That is a very interesting point.

Q245 Sandy Martin: Sorry to butt in on this, Chair. Please forgive me if I have missed a crucial point. You were talking about debt, and it occurs to me that there are, of course, different sorts of debt incurred in different sorts of ways. How much, if any, of the debt that you are talking about is actually incurred as part of a company purchase of another company? Clearly, the water industry has re-aligned the ownership several times since privatisation. How much of that is corporate debt incurred during that process, and how much of it is debt as a result of investment in the water industry?

Rachel Fletcher: I do not have an exact answer to that question. The point is that that debt sits on the balance sheet of the regulated company, and the important thing is that that debt is not undermining



the company's ability to perform its essential duties for customers, regardless of what the origin of that debt is.

Q246 **Chair:** Would you have these figures available?

Rachel Fletcher: I am not sure that we do. I am not sure we can unravel a composite debt figure in the way that you suggest but I will certainly take that away and look at it.

Q247 **Sandy Martin:** I hear what you are saying about the effect of the debt but, actually, the public perception of the need to pay that debt off and the public perception of what that debt represents is very important. If we operate on a model whereby we consider it to be a good thing to pay off debt, we are encouraging people to think that it is also a good thing to artificially generate debt.

As an analogy, I will give you the care sector. Major hedge funds have bought up sections of the care sector by borrowing money, loading that debt on to the very companies that they have bought and then using public money, through the care system, to pay off the debt that they have leveraged in order to buy the sector in the first place. That is the sort of international capitalism that nobody in this country—with the exception of the people who benefit from it—actually think is a sensible model. If that is present in the water industry, I would want to know, and I think you ought to know, too.

Rachel Fletcher: I agree that the impression and the sentiment of investors coming in and seeing these businesses as vehicles on which you can raise debt—hence my reference earlier to financial engineering—is exactly the opposite of what we are looking for. Frankly, that is one of the reasons we have pushed so hard on the new requirement on companies to share the benefits of financial engineering.

We want investors coming into the sector who are in it for the long term and who realise that they are going to make their returns by delivering great things for customers, being more efficient and providing the environmental and service benefits we have been talking about today. We are seeing more of that kind of investor coming into the sector. There is a big market and a big pool of investors with that kind of motivation out there. It is really important and we are passionate about driving a regulatory system that naturally attracts those kinds of investors and not those who see water companies as vehicles for raising finance.

Chair: Thank you for that. If you do have any of those figures, it would be useful. You make an interesting point on investment because people are looking for ethical investments as well. If the water company can generally prove that they are improving their environment and improving the quality of water, there could be an issue there where people would invest because of that and may not necessarily expect quite such big a return either.



Sir James Bevan: Can I add to this debate? The sense that you and others around the table have, that companies should not be making huge profits if they are doing bad things including to the environment, is absolutely right. There is a fundamental principle, which is that the polluter pays. A company making vast profits whilst doing huge damage to the environment is not a place that any of us want to be. We need to look at how we can tackle that further.

One way in which we are doing so is by significantly increasing the fines for companies when they really behave badly. The Thames Water fine last year was £20 million. That was a record fine. The case was pursued by the Environment Agency. It was the right number because they committed very serious damage: 1.4 billion litres of raw sewage went into the Thames. It is good that the sentencing guidelines have been increased, so the principle now is that the fine should be proportionate to the turnover of the company. Even so, in Thames' case, £20 million is 1% of their turnover, so there is still room for even more pain, because when a company really does something bad to the environment, it needs to hurt even more.

Q248 **Chair:** That is a fair point you make, because it also encourages them to get on with the Thames Tunnel as well, because, if you are getting more and more raw sewage into the Thames, that is naturally what the tunnel is there to do. There is a bit more digging to do yet but they are getting on with it.

Let us move to metering and smart metering. Should smart water metering be increased? Should there be more conditions where it can be made compulsory? A little bit like the energy industry, do we have to be absolutely certain that the smart meters that are put in are not so much company-specific? Again, there is only one company who you can usually have the water from, but it is something we need to be careful of if we ever did bring competition in.

The thing with smart metering, which I am not sure the public altogether gets, is that they think the smart meter itself saves you water. Of course, it only gives you an idea of how you use water and how perhaps you can use it more efficiently. I am a great believer in meters generally, because I think people should pay for the water they have and, environmentally, they might not use as much water. Where is Ofwat, in particular, on metering generally? I do not just mean smart metering.

Rachel Fletcher: The matter of compulsory metering is a matter for Government and it is governed by primary legislation. Where metering has been put in, we have seen reductions in water consumption. That is partly to do with awareness of the customer about how much they are using but it is also to do with some of the other water-saving devices that have been installed at the same time. Regardless of the legislative framework, water companies need to keep questioning themselves about the case for metering. Metering, as well as bringing forward the benefits in water efficiency, can also improve the water company's understanding



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of what is going on on their network, give them a better understanding of where leaks and bursts might be happening, and can also help with some of the data issues that we have in the sector as well—the mismatch between bills and customers' addresses.

Q249 Chair: There is a real mismatch across the country; some companies, especially in the south and the west, have a lot of metering, while companies in the north have not as much. There are social problems as well that have to be met with social tariffs but to what extent does Ofwat say to those companies that have a very low number of meters, "You should be doing better"?

Rachel Fletcher: We have a number of incentives on the companies that might drive them to look again at the case for metering. In the next price review period, we will ask every company to make a performance commitment around reducing per capita consumption. Metering might be part of the solution to meeting that outcome.

As I said, we are also driving them to be better at operating their networks. Again, that might drive them to think about whether an increase in meters is something that they should be pushing for. We are leaving the specifics of the input to the company but there are a number of outcomes that we are incentivising where metering might be part of the solution.

We are also expecting companies to be talking to their customers about metering. It can be quite controversial but I believe that water companies have a role to play in explaining and helping customers understand the benefits that can come from water meters, and that is something, particularly as companies take the per capita consumption challenge seriously, that is exactly the kind of conversation they need to be having with their customers.

Q250 Chair: From an environmental point of view, you can have a water company extracting more and more water—sometimes putting pressure on rivers and others—and yet they do not have enough metering and they may not be fixing their leaks like they should. We have had the water companies in here and, without the meters, they are not terribly sure exactly where the wastage is either. There are two issues really: one about what the consumer may or may not use but also how the water companies can monitor how much water is being wasted as well. Does the Environment Agency have a view on metering and reducing water and reducing the amount taken?

Sir James Bevan: Yes, we do. We are strongly in favour of metering for the reasons you have identified. It will encourage people to drive down their own water use and allow the companies, as Rachel has said, to know what is happening in their system. It is part of a much bigger solution to the mega problem we all face, which is that we will run out of water in a few decades. The solution to that includes measures to drive down demand, of which metering can be one, as well as repairing leaks



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and dealing with reducing abstraction, of which our business is also a part. You have to drive down demand but you also have to enhance supply, and there we get back into the collaboration between the regulators to ensure that we have a system that incentivises the companies to invest in the infrastructure and all the other measures that you need to enhance long-term supply.

Q251 Chair: Here we are in what is getting very close to a drought situation and water supply will get tight. Until you actually bring in a hosepipe ban, people without meters can turn their hoses on, water their garden as much as they like, wash their car as much as they like and leave the hosepipe running, because the meter is not running. That surely is not right.

Sir James Bevan: I certainly agree that changing personal behaviour is a key part of fixing this problem, and I think you can. You do not necessarily need to have laws. We do not have any plastic bottles here, I am pleased to say.

Chair: We actually have glasses. I also have my Water UK bottle this morning.

Q252 Sandy Martin: The analogy of the plastic supermarket bag is a very good one. Before they were charged for, people had been exhorting people to stop using plastic bags for years and years with virtually no effect. The moment you introduced a charge—even a very small charge—usage reduced by 90%.

Sir James Bevan: You can push behaviour with charging and with tax, and all the things we know about. You can also make it culturally unacceptable to have plastic and, over time, we will have to make it culturally unacceptable to waste water.

Chair: The beauty of metering water is that if people were more careful with the water, they probably would not pay such high bills. While I agree with your analogy, Sandy, on the water metering, it is almost the reverse: people could actually save money if they changed their behaviour. We could also help the environment and the amount of water we use. It may not get to a situation where we need a hosepipe ban. It might start raining next weekend and not stop for six months. You know what our weather is like. On the other hand, if this weather does continue, parts of the country will be under severe water pressure.

Sandy Martin: I may well be wrong here, but is it not the case that in the south—in particular in London, and in the Thames and the Anglia region—the shortage of water has led companies to really go hell for leather to try to get metering across as wide an area as possible and as many people as possible, simply because it is actually cost-effective for them to do so? In the north, however, where there is more water available and less people who need it, the level of demand has not made it as cost-effective for them to promote metering. So it would actually be more helpful to leverage any legal requirement on to the water



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companies rather than on to the individual consumer. Incentivising people is clearly not working in those areas where most people do not have water meters. Making it a requirement for water companies to install water meters wherever they are asked for would be a helpful step in the right direction, would it not?

Rachel Fletcher: In the south-east it can be compulsory to have a meter. That means that the company does not need to work to get customer acceptance; they have the right to install it and charge the customer for that meter.

I agree very strongly with Sir James's view that metering is only part of a wider set of solutions that need to be looked at. After all, a typical water and wastewater bill is £400, which, for a lot of people, is not anywhere close to the biggest bill that they face. We are seeing that there is new technology, particularly for new-build properties, which can radically reduce the need for treated water—the use of grey water and dual water systems, and the installation by default of automatic water-saving devices. Just relying on customer behaviour—relying on customers responding to a water bill that will, for some of them, be a small proportion of their monthly outgoings—is probably not enough to meet the challenges we know we face with population growth.

Q253 **Chair:** In some places you have high-priced water, like in the south-west, because South West Water have the cost of the beach cleaning and water cleaning, to stop it going out to sea. You have had a lot more metering there by choice, because of that. While we do not want particularly high charges, sometimes the result of higher charges is that people are more careful with what they use. We cannot wish for lower prices as well as that, but with the metering we could have both.

Tony Smith: We agree with all the points that have been made about the need for a twin-track approach. Metering plays a big part, and it is actually the fairest way to pay over time. The issue is around how you implement it. You mentioned South West Water and Anglian Water, both of which did not compulsorily meter; they have done it by choice. The issue with compulsory metering is that a sizeable percentage of the customers—about 25% of customers—are strongly opposed to not having a choice and to having a compulsory meter.

We have been working very closely with the companies that have put in compulsory metering, in the south-east in particular, to make sure that they understand what their customers think and take those customers along with them. This is not just about social tariffs. Social tariffs play a part, but one of the big issues with putting meters in is that if you think about a large household in a low rateable value property, they might have a price impact overnight of more than £200. They may be able to afford that, but it will aggravate them. There is a danger of a backlash. The companies have done pretty well in the south-east, in terms of implementing it slowly.



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The idea of metering over time makes sense. You have to be very careful in the way you implement it. The danger is that if you start imposing targets on companies everywhere, they might start becoming very draconian about it, and you will get a big customer backlash. Remember that you have a much more compelling case, if you are in an area of water stress, to say, "We have to do metering because of water stress". It is rather less compelling where you do not have a water-stress problem and you have lots of water.

Q254 **Chair:** The only trouble is, Tony, you are still processing that water, from an environmental point of view. We need social tariffs to help those who really cannot pay their bill, but there is no fairness in water not being metered. Why should one set of bill-payers pay on the amount of water that they take, while another set of bill-payers can take whatever water they like and not pay anything extra for it? It is just not logical.

Tony Smith: That is why it makes sense to have metering over time. Presumably, we all want the water industry to do this in a way that customers accept and that does not generate an even bigger legitimacy problem. If you think about it from the customer's perspective, they have not had a meter, nobody has asked them to have a meter yet and now all of a sudden they have a meter. You need to take that customer along with you. It is particularly important in areas of non-water stress. The other issue is about leakage.

Q255 **Chair:** You talk about the customer who has not had a meter, but what about all the customers that do have a meter? They are being short-changed at the moment.

Tony Smith: That is why you need to do it over time. I am agreeing with you, but the issue is that if you do it overnight, you will get a backlash. You will get a particular backlash if at the same time as you are giving a customer a compulsory meter, the company is leaking a lot of water.

If you think about it from the customer's perspective, you have to take them along. Otherwise, you will get a backlash. This is why some of the companies have done it without compulsory metering, because they realised that.

Q256 **Chair:** I also accept that if you are going to change to metering, you need to have some good social tariffs in place so that you can help those families and big households where there are genuinely a lot of people using water on low income. I accept all that, but the only issue I might have with you is over the timescale; you may want to go a little slower than I would like.

Tony Smith: Southern Water did it in five years.

Q257 **Chair:** Do you think that that is acceptable?

Tony Smith: They did it pretty successfully in five years, so it is possible to do. Just do it carefully.



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Q258 Dr Johnson: Do all water companies replace the meters when households change house? When I got my new house, I was a bit disappointed to find that it had a meter, because I appreciated that my bills with a big family might be more expensive, but I accepted it because that is just what it was. Do you think that people would be open to the idea that, if they move into a new property, they know they will have a meter because when a house changes hands they have to?

Tony Smith: I mentioned that some companies have not done it compulsorily. That is the way many of them have done it: they have put a meter in when the house has changed hands.

Q259 Dr Johnson: Do you think it should be compulsory when it changes hands?

Tony Smith: It is a way of increasing metering and it is reasonably successful. Clearly, some customers react to that because they say, "I am a large household so this is going to disadvantage me", so we are back into that debate. Again, it needs to be very customer-specific. The companies that have promoted metering successfully are the ones that deal with their customers almost at an individual level to address their concerns. Then it works. If they do it in a very offhand and very rapid way, they will get a big reaction.

Chair: Even the north-west at the moment is getting relatively short of water. I thought it rained every day in Manchester, but it obviously does not any more. Even in the north, there are some quite tight situations over water, so there is perhaps an argument for the metering.

Q260 Sandy Martin: This is a question about the draft water resource management plans. Ofwat has expressed disappointment at the lack of ambition. Rachel, what more do you think water companies should be doing to increase resilience, especially in the context of the response to the beast from the east and people being left without water for long periods of time, and also in respect of the way that the bulk water supply negotiations work or do not work?

Rachel Fletcher: There is quite a lot in there. The water resource management plan is a great example, again, of Ofwat and the Environment Agency working together to give some strong and consistent messages to the sector about how they can step up and improve their long-term resource planning. Some of the areas that we felt were really lacking in ambition were, on the demand side, quite low ambitions around reducing per capita consumption, even over a large number of years. We think that there are really huge opportunities for the companies to do more. There are very low levels of water resource transfers between water companies. We actually have water-rich and water-scarce companies side by side. It begs the question of why transfers are not happening to improve resilience.

We were even disappointed with some of the supply-side solutions that companies were coming up with, not bringing them forward enough in



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the planning horizon. There are quite a number of things, if you like, on the long-term planning where we felt, frankly, that there was not enough evidence that companies were taking the real challenge around a growing population seriously enough.

You asked about the beast from the east, which of course is related. There, actually, the resilience challenge was more around the companies' pipes and the extent to which they were resilient to a very sharp reduction and then increase in temperature. The lessons from our review of how the sector performed showed that some companies were well prepared, some companies were able to act quickly to stem the bursts on their system and some companies were really good at keeping their customers informed and making sure that those customers, and particularly vulnerable customers, had good access to alternative water supplies. Unfortunately, around four of the companies in the country really showed that they were way behind the pace and that they just had not taken planning for unexpected or extreme weather events seriously enough. They had not learned the lessons from previous weather events.

One of the lessons for companies, particularly given the current weather that we are facing, is the need for them just to be better prepared for weather patterns that we have not typically seen in the past. Overall, there is a need for the sector to take the lessons from the cold snap and build them into their overall resilience and planning for extreme weather events. I am gaining some confidence that the report we put out a few weeks ago on the cold weather is having an impact on the companies' preparedness for what is happening right now.

Q261 Sandy Martin: You must forgive me for not having read that report. I am sorry; I am sure everybody else in the room has.

There are two levels of resilience, are there not? First of all, there is obviously looking at what may occur and planning for your systems to be able to resist that and, secondly, there is having a level of emergency planning that enables you to cope with the consequences when it does not. Any water company would need to do both. Did you find, as a result of the beast from the east situation, that there were certain types of installation that clearly were no longer fit for purpose? There has been a series of massive infrastructure investments in water over the past 50 years such as replacing lead pipes with steel pipes or plastic pipes, and various other things. Is there a particular type of installation that has been particularly vulnerable or shown to be particularly vulnerable?

Rachel Fletcher: We did not receive the information to allow us to make that assessment, if I am honest, but underlying that statement is a deeper concern. A number of the companies do not have a sufficient understanding of the condition of their assets, how their assets will perform and how they are performing in any particular circumstance to enable them to respond quickly and get to the heart of where problems are occurring on their network. That challenge for the companies to



better understand their assets is a challenge that Ofwat is giving the sector as a whole.

Q262 **Chair:** If the drought does continue and we need to transfer water from company to company, how does it work? Companies will want to hang on to their water, so how does it work in terms of how this water is traded? How do you deal between companies with prices? There must be a temptation for a water company that has quite a lot of water to say, when it is dry, "My water is worth more." There are ways that you get around it. Is there arbitration? There needs to be co-operation, because it must be quite tempting to hang on to your water. How do you deal, first, with the fact that some companies may want to hang on to more water than perhaps they should; and, secondly, the pricing when you sell it wholesale between companies?

Rachel Fletcher: There is very little water trading; around 4% of water is traded between companies and that level has stayed pretty static.

Q263 **Chair:** When it gets very dry, that situation will change quite rapidly, will it not?

Rachel Fletcher: Where there are trades between companies, there are commercial arrangements in place that govern the terms of those trades, both in terms of the volume and the price, including what happens when there is water-resource pressure. What is really important, though—I think you alluded to it, Chair—is that when you have an emergency situation, companies are actually not thinking about this as a commercial transaction but are co-operating and collaborating so that customers get the best possible service. That, again, is a lesson that came out of our review of what happened during the cold weather spell, which is that we are not seeing quite enough of that collaboration and joint assistance.

Q264 **Chair:** You are looking at that, are you?

Rachel Fletcher: Yes, we have put a challenge to Water UK to bring the water companies together and to refresh how they co-operate and collaborate when there are these kinds of emergencies.

Q265 **Chair:** I do not know whether you are able to give us, in writing, just a little more detail about what you might be asking for, because that could be an interesting part of our report.

Rachel Fletcher: Yes, I am happy to do so.

Q266 **Chair:** Sir James, did you want to comment?

Sir James Bevan: As Mr Martin said, there are certainly two levels of resilience, one being the resilience for the day-to-day and the other being resilience to an event, such as the beast from the east. There is, however, also a third, which is resilience to climate change—long-term resilience—which is what we are all really focused on. That is the big existential challenge, including to the business of the companies, because if you do not have any water, you do not have any business. You are



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right, Mr Martin, to underline the importance of the water resource management plans. Those are the key ways, in working with Ofwat, as Rachel says, we can encourage the companies to devise strategies that will start to put us in a place where we can manage the long-term water resilience of the country.

How we feel about the plans we have seen so far is, to coin a phrase, "glass half-full, glass half-empty." There is some good news in those plans from the companies, such as the commitment from most of them to hit the Ofwat 15% leakage reduction target. There are some water transfer schemes in there, although, as Rachel says, not very many. There is more commitment to manage for an extreme drought than there has been in the past. All of that is good.

What is the bad news? We would like to see even stronger leakage targets. The National Infrastructure Commission has just come out saying 50% would be a good leakage reduction target. As Rachel says, the approach to water transfers is minimal and not very joined up. At the moment, in individual plans, when you compare one water company's commitment to transfer with another water company, they do not actually mesh together.

Q267 **Chair:** Can the Environment Agency directly get that to the water companies? How do you do it?

Sir James Bevan: It is part of the PR19 process where we are commenting on and helping shape the water resource management plans of all the major companies with Ofwat. That is one way in which we do it. We also have direct bilateral conversations with each of the water companies about what we think they need to do to put themselves in the place where, in the long term, they can ensure a sustainable water supply.

Q268 **Dr Johnson:** As usual, I refer Members to the fact that my husband is a farmer and he does have a contract with a water company, though it is not for abstraction. I want to ask about abstraction. We have heard a lot about the usage of consumers and the usage of agriculture, but we have a lovely chart demonstrating the water usage in total, and it is not possible to even appreciate the amount that is used by agriculture because the line is so tiny it does not even appear in the print. Actually, the water used for drinking or for consumers in the home is only just over a quarter of the total. What proportion of abstraction that is unsustainable is from those sources, what is from other sources and what is being done about that?

Sir James Bevan: First, you are right that farming takes a very small proportion of water that is consumed. It is less than 1%, which is why you cannot see it on the bar chart.

Q269 **Dr Johnson:** We hear a lot about farmers and we hear a lot about consumers, but we are not hearing about the major water uses.



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Sir James Bevan: The biggest users of all, if you draw a pie chart, will be the energy-generating sector, including hydropower, which is about 49%. The second biggest will be the water companies, at about 34% that they take out. There will then be a smaller set of others, with farmers just under 1%. Obviously, the hydropower in particular is going back into the system, so that is sustainable by definition. When we talk about unsustainable abstraction, we are talking about water that is coming out of sources that are not likely to be replenished or will not be replenished quickly enough to sustain the amount of abstraction that is coming out of them. For example, many of the chalk aquifers, which feed a lot of the water supply, particularly in the south-east, are unsustainable at the rates at which they are being abstracted. The people who are abstracting from those are primarily water companies, although there will also be some farmers that are abstracting from sources that we do not think are long-term sustainable.

Q270 **Dr Johnson:** Presumably, they abstract it to pour it on the fields where it soaks through again.

Sir James Bevan: Anyone who wants to take more than 20 cubic metres out of the ground or out of a river in a day needs an abstraction licence from the Environment Agency. The problem with the abstraction licensing system is that it is very old and it was designed for a period where there was no water stress and no climate change and far fewer people. Many of the abstraction licences have no limits on the amount of water that you can take out of the ground, and many of those abstraction licences are very long-term, so there is a problem built into the old abstraction licensing system.

What we are doing is starting to have conversations with the people who do abstract, which is primarily the water companies but will include farmers and others, about ways in which, preferably in a voluntary agreement, we can come to them and reach agreement on new abstraction licences that will give them the water that they need but ensure that the abstraction happens in a sustainable way. That process is already ongoing. We have reformed or adjusted over 270 big abstraction licences where we do think the sources are unsustainable, and that has saved something like 30 billion litres of water, which would supply Liverpool for a year. We are making progress but we would much rather do it by agreement with the customers, including farmers, than by coercion.

Q271 **Dr Johnson:** As well as applying pressure and trying to get voluntary agreements with farmers, who, as you say, are less than 1% of the total, what are you doing to encourage water companies?

Sir James Bevan: Most of the conversations about most of the water will be with the individual water companies. Obviously, there are far fewer water companies than there are farmers. We have a lot of individual conversations with farmers but we have direct conversations with all of the major water companies.



Q272 **Dr Johnson:** What have they said?

Sir James Bevan: They have been receptive. Affinity Water, for example, who do the north-west area around London, depend greatly on groundwater for their supplies. Quite a lot of that groundwater has come out in the past from chalk aquifers and other sources that we do not think are sustainable. We have had very fruitful conversations with them about either adapting the amount of water that they will take out of particular aquifers so that we think it is sustainable, or finding alternative sources of supply. We are conversing with the water companies, and I think they get it and they are trying to be helpful in managing down unsustainable abstraction levels.

Q273 **Dr Johnson:** You have had fruitful conversations and they seem receptive, but have you had action?

Sir James Bevan: Yes. There are some sources where we have agreed with the water companies that there will be no further abstraction of water, full stop. There have been other sources where we have agreed with the water companies that they will limit or reduce the amount of abstraction that they will take, or there have been examples of sources where they have agreed with us that they will not take water at a certain time, for example during the summer, when that particular source is stressed. We have had agreements that are starting to bear down on unsustainable abstraction. It is an ongoing process and we are not there yet but, as I say, I would rather try to reach voluntary agreements than wield a big stick.

Q274 **Dr Johnson:** That brings me to my next issue. This is a voluntary approach but does the Environment Agency have sufficient powers to alter these licences if people are unwilling?

Sir James Bevan: What strikes me is that when you talk to farmers—and we do spend a lot of our time talking to farmers in particular, because I am conscious of how sensitive the amount of water they get is to their businesses—I feel that there is a strong sense of collective responsibility.

Q275 **Dr Johnson:** What about the water companies? We are hearing about the farmers, but they are a tiny issue. If they stopped using water altogether, it would make almost no difference to your water usage. What about the big users of water? Do you have enough powers to make the water companies do what you need them to do?

Sir James Bevan: At the moment, we are finding that the water companies understand the importance of reducing unsustainable abstraction and we are concluding agreements with them that are getting us down to the level that we want to reach to ensure that we are at sustainable abstraction levels. Those levels will have to come down further in future, so this will have to be a continuing conversation. At the moment, I think we have the powers that we need to get to where we want to get to.



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Q276 Dr Johnson: I was going to ask Mr Smith about the tariffs and the concept of social tariffs. Do you know if social tariffs apply to any other forms of utility, such as electricity or gas? Do you know, from the surveys of your consumers, how the moderately low-paid, who might not fall into a social category, feel about people being charged differently for the same usage?

Tony Smith: It is a good question. The answer to the question about other utilities is, yes, there are social tariffs, for example in the energy sector.

With regards to customers' receptiveness to cross-subsiding others, all the companies, when they are developing social tariffs, have to go and talk to their customers about the level of acceptance. That limits the amount of money that they can put into their social tariff pots. Typically, it may be £2 per customer in cross-subsidy that customers are prepared to pay, but obviously that varies according to the customer. Some are very receptive to paying more money.

The point you make is the right one, which is that those customers who probably will not be able to use the social tariff but who are on the edge of it are the ones who are least likely to. That is the same discussion about meters and everything else. It is the customers that are just outside the social tariff arrangements who are the most sensitive to paying more. Some of these customers are still living on a cash basis; they are having to make difficult choices between paying their water bill and buying children's shoes, or whatever it might be.

That is one of the problems with the social tariffs being funded by water customers. We have found from our research that customers are much more receptive to paying a bigger contribution, on average, if they see the water company also contributing and potentially if they saw Government contributing as well, for example in the south-west where there is the £50 discount. Those are things that we have encouraged the companies to contribute, so that the pot is bigger, so they can help more customers and so it has less effect on the customers who are outside it.

Dr Johnson: If Government contribute, it is still the customer's money.

Tony Smith: Yes, but at least it is progressive. It should be based on the benefit system. It is quite difficult for some of the companies to target their social tariffs, so a number of them use the benefit system. If you are on a particular benefit, you can have the social tariff. Others do it on an individual basis, so they talk to the customers and they use third parties like Citizens Advice to help identify which customers should get help. Others have a low income trigger point—perhaps £16,000 for the household—which is the point at which they will help those customers.

Chair: The issue on South West Water is that we have 3% of the population and 30% of the beaches, and the argument was that the support there of the £50 on the bill was to help the general taxpayer pay; why should 3% of the population pay for 30% of the beaches? This



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argument went on for a very long time but that is where that one came from.

Sandy Martin: This is an issue that we have not actually touched on but you did mention, Sir James, earlier on about the need to be resilient in the face of climate change. I am quite surprised, actually, at the very small proportion of water that is used in agriculture in this country, but I think we can be fairly confident it is going to grow. If I were a sheep farmer in the hills of Cumbria, I probably will not need artificial irrigation at any time in the next 50 years. However, if I was an asparagus grower on the sandy soil of Suffolk, I would be desperately keen to see where I could source additional water in order to be able to continue with my business. Do we have any plans in this country for a national agricultural water scheme? Countries that are successfully growing in dry conditions—Israel is a very good example—have national schemes for transporting agricultural water from the places where there is more of it than they need to places where there is less of it than they need.

Q277 **Chair:** Can I add to your question? In our water-stressed areas, which are sometimes where we need to grow crops, we have more recycled water but we do not actually recycle much water in this country. If we are going to get dryer and dryer in parts of the country, and if we cannot move the water around terribly successfully, should we be recycling more and could that be used for agriculture? The point that Sandy makes about whether we need a policy on this is a good one.

Sir James Bevan: The short answer is “yes”. We certainly need a national approach to ensure that we are water-resilient for the long-term, and that needs to ensure that all the users of water, including, critically, farmers, get the water that they need—if they will not get all the water that they want—and we have talked already about some of the measures to manage down demand and enhance supply that need to be part of that strategy. There is broad agreement between the regulators, the industry and the Government that the twin-track approach is the right one. We just need to get on and deliver it.

I also think, Mr Chairman, that you are right that we also need to look at innovative approaches, for example using treated water or wastewater for purposes that we currently are not using it for, including possibly in some agricultural areas. All I would say is that water and the environment are indivisible. You cannot just have a policy for agriculture because obviously that will affect the rest of the environment. What you need is a policy that will work for agriculture and will work for all the other parts of the economy.

Q278 **Chair:** Recycling water in some ways is a cost but, if we do not have enough water, we will need to face that, will we not? Where do you stand on that one?

Rachel Fletcher: We completely recognise the longer-term challenges around climate change and population growth. We are crucially aware that some of the plans for improving and increasing housing stock,



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notably in the Oxford-Cambridge corridor, are in very water-stressed areas where it will be difficult to get the levels of abstraction required in an environmentally sensitive manner. As a sector, we need to think about the bigger picture in terms of transferring water from one region to another. We have to shift the frontier in the technology that we are using in delivering water supplies. The idea of using treated drinking quality water to water our gardens and wash our cars in the 21st century just does not seem appropriate. There are some really big things for us to grapple with as a sector.

Certainly, as a regulator, it is something that we will push the companies to innovate. I have already talked about opening up so that new players can come in and push that innovation. We will work collaboratively with other regulators and with Government to do everything we can to make sure that we have a secure, affordable and environmentally friendly approach to delivering future water supplies.

Chair: That is a good point you make on the watering of gardens.

Q279 **John Grogan:** I was going to come back finally, Sir James, to the issue of river pollution, which is very important. We have had some representations from both anglers and canoeists, and they do not often agree, but they do agree on the importance of water quality. You have just published a report listing the water companies. Could you perhaps refer to that and also say whether you have enough inspectors? Are you too reliant on the water companies putting their hands up? Do you have a lot less than you used to have? Is it making a difference?

Sir James Bevan: The big fact is that water quality in rivers is better than it has ever been since the start of the industrial revolution. There are many reasons for that, including the fact that it has been well regulated, and that is fantastic. I remember, as a child, standing on a bridge in Wakefield looking at the river and I could not see the river because it was covered with foam and, when the foam blew away, all I could see was black, biologically dead water. Now you never see that in any of our cities, and that is a remarkable fact that we should just clock. That is partly down to regulation, which has delivered it.

That does not mean that we are anywhere near where we would like to be. The fact that the water companies have played a major role in getting us to better water quality in the rivers does not mean that they are yet delivering all the performance that we want. The big picture from the report that we issued this morning, which is an annual report that ranks the nine major water companies in terms of their environmental performance, is that, over time and overall, water companies are getting better, polluting less, enhancing the environment more and respecting more closely the terms and conditions that we apply to them. That is all good. There is bad news too, and there are a couple of companies that are down in the relegation zone that are nowhere near where they need to be, and we will have very direct conversations with those companies.



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We did see a slight increase in the total number of serious pollution incidents that happened in the course of last year.

However, the big picture is that the water environment is getting better and the water companies are performing better. That is because we are regulating them better. Do we have the tools we need? I think we do. Again, I am always reluctant to ask for more powers. We have strong powers that we exert effectively.

Q280 John Grogan: Do you have enough inspectors?

Sir James Bevan: We have about 1,800 people in the Environment Agency who, in one way or another, are involved in ensuring that the water companies are doing the right thing. They are very committed. We also raised the costs of our regulation through the charges that we impose on the water companies and others we regulate, so we are not in that case dependent on government grant; we are raising the money we need from the people we are delivering the regulation on to fund what we are doing. I think we have the right resources.

Q281 John Grogan: One of the points the anglers make is that there is an argument that water quality should be measured more at night or in particularly wet weather and so on. Are you doing some strategic monitoring review?

Sir James Bevan: We do a lot of very specific, detailed and technical monitoring that tells us a great deal about the nature and the quality of the water at any given moment. We are conducting a review to see how we can do it better and more effectively. That is what the review is about. It is not about stopping doing monitoring; it is about doing it better so that we know what is in those rivers. That is the technical side.

On the visible evidential side, there are otters in every county in this country now. The anglers will tell you that the Environment Agency put the otters in the water, and that is one of the issues that I get letters about. We did not put the otters in the water; the otters came back into all of those counties because the water quality had become so much better.

Q282 John Grogan: One thing you also say in the document you have just produced is that expectations of citizens and of stakeholders have increased dramatically from when you stood on the bridge at Wakefield. People expect a lot better now. Have the water companies caught up with that in terms of sewage? For example, in the beautiful Yorkshire town of Ilkley, which I represent, there is a continuing controversy whereby anglers and others are reporting every week that there is sewage going into the river and Yorkshire Water is saying it is not. If I wrote to you, could you look particularly at that case?

Sir James Bevan: Of course.

Q283 John Grogan: Is there not a problem here if it is just the water



companies that you are primarily relying upon?

Sir James Bevan: Yes, I am very happy to respond to any letter, Mr Grogan. We respond to every single report that we have on environmental pollution and we send people out to about 7,000 incidents a year, so we do take it seriously. Anglers are an important part of our intelligence networks, so we encourage anglers and others who use the rivers to report. There is a report line that they can ring in so we welcome that and we will make sure that we treat all those reports seriously.

Q284 **John Grogan:** Finally, as I say, the actual expectations have risen. Without going into all the technical details, do you have the powers to make the actual levels you set more stringent in line with that increase in expectation, or do you need legislative change?

Sir James Bevan: Yes, we do. We already set very tough standards for what water companies need to do, including in terms of their sewage treatment works. In the league table that we published today, when we launched this in 2011, we had tough standards against which we measured the companies. In 2015, we jacked up those standards. Again, it is a good example of collaboration with Ofwat because the period for which the new standards are measured are between 2015 and 2020, which is the current Ofwat price review period. We have set higher expectations until 2020 and, again, as we are going through the PR19, for beyond 2020 we will both be setting even tougher expectations on water companies.

Q285 **Chair:** To use a football analogy, because we have a strong match coming up tonight, you issued a red card to a number of water companies, including one in my own area, South West Water. Further to John's question, how much time do you give these companies to put it right? Time ticks on and we know it costs a lot of money to put the infrastructure right, especially with sewage treatment plants and the like. You have to be flexible and you have to give them some time, but surely, once you start issuing red cards, you cannot just keep issuing red cards; there has to come a time where you bite a bit harder.

Sir James Bevan: Absolutely. It is right to say that all companies, including South West Water, have improved their environmental performance over time. We welcome that. That is partly because of the engagement that we have had with them on a daily basis.

Q286 **Chair:** They have done a lot with the beaches. I give credit to South West Water but they still have more to do. How do you put that added pressure on them, other than, "We have issued you a red card and we might issue you with another red card next year and the year after"?

Sir James Bevan: The red card in the report today, Chairman, is just one of the levers that we have, and it is probably one of the less important ones. Companies care about it because the chief executives ring me up as soon as they find out where they are. That is a good thing,



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because I want them to care and I want the public to know where their own water company stands. There is definitely pressure, because of this transparency, on the water company chief executives to get themselves out of the relegation zone, and I expect that South West Water will feel that pressure themselves this morning. However, there are many other tools that we use. We have daily conversations with the water companies, including with South West Water.

Chair: I suppose, ultimately, fines like with Thames Water.

Sir James Bevan: We have soft measures like advice and guidance about what we want them to do. We have increasingly tough measures like giving them written warnings or requiring them to accept measures that we dictate in order for them to retain their permits to operate. The ultimate sanction we have is to take them to court and seek very severe penalties. We have, and will continue to use, all of that suite of measures, not just with South West Water but with every one of the water companies.

Q287 **Chair:** Do you think you are being tough enough?

Sir James Bevan: The water companies would probably tell you that we were being—

Chair: They are always going to think you are tough. They would say that anyway, would they not?

Sir James Bevan: The evidence is ultimately the effect on the environment. We can all agree that, over time, the environment is getting better. That tells me that something right is happening in the regulatory sphere. However, we would like—and we have said this before—even tougher penalties against the water companies that commit the most egregious pollution.

Q288 **Chair:** Let us face it; that is very much your role, is it not? It is the Environment Agency's role to check what these water companies are doing and to improve the environment. It is fundamental. You have said you think you have an adequate number of inspectors. Would you like a change in the law or do you think the law is sufficient and it is just a case of making sure that they are adhered to?

Sir James Bevan: I am conscious that you have a Minister before you this afternoon.

Chair: Yes, we have some questions for her this afternoon.

Sir James Bevan: In terms of current regulation, the Environment Agency has the powers and the resources that it needs. There are adjustments to the legal framework within which we all operate that could be made. It may be that there are others besides the Environment Agency that should have greater powers. For example, courts might profit from having greater powers to take action against the most egregious offenders. The Government or local authorities might benefit from greater



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powers to make quicker decisions about investment in terms of the infrastructure that will deliver the long-term water resilience of the country. I am comfortable that, at the moment, the Environment Agency has the right powers and that we are exercising those in the right way.

Chair: Thank you very much. That was a very good evidence session with good stuff for our report. We have Thérèse Coffey, the Minister, coming this afternoon, so we might well put to her many of the points you have raised with us this afternoon. It has been a very good evidence session. Thank you very much.