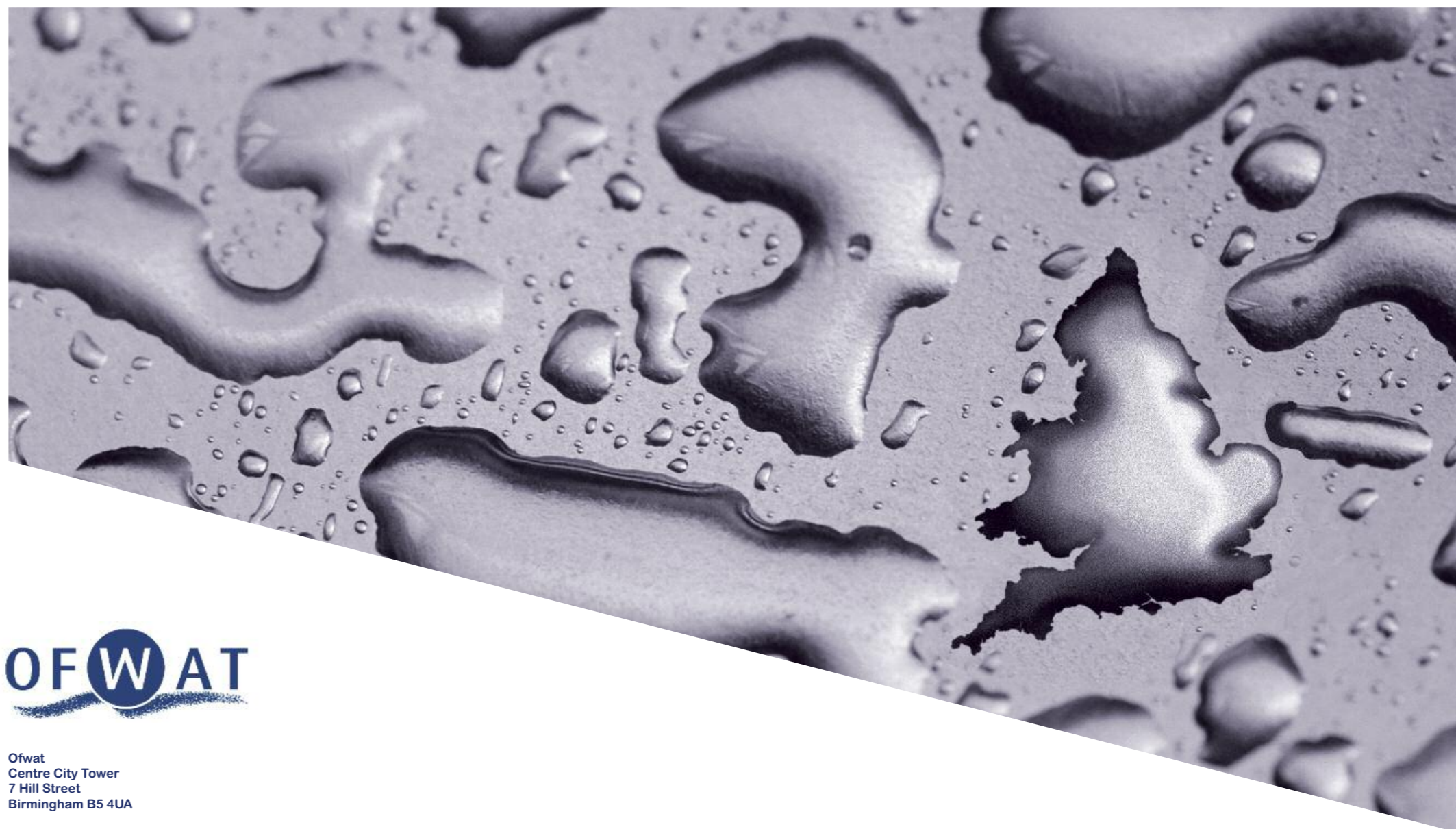


Ofwat (The Water Services Regulation Authority) is a non-ministerial government department. We are responsible for making sure that the water and sewerage sectors in England and Wales provide customers with a good quality and efficient service at a fair price.

Delivering sustainable water – Ofwat's strategy

Water today, water tomorrow



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About this document

This document sets out our long-term approach to regulating the water and sewerage sectors in England and Wales. It updates and replaces 'Ofwat's strategy – taking a forward look', which we published in April 2008.

The strategy informs our forward programme. This sets out the work we plan to deliver each year and the budget we require. We review how we have done in our annual report.

Our strategy reflects our legal duties. These are mainly set out in the Water Industry Act 1991 (as amended). We have also had regard to a wide range of other information, in particular the:

- UK Government's '[Future water](#)' strategy;
- Welsh Assembly Government's '[Strategic Policy Position Statement on Water](#)'; and
- Environment Agency's '[Water for people and the environment](#)'.

We continually review our strategy to ensure it is fit for purpose.

Where the document uses the term 'Government', this refers to both the UK and Welsh Assembly Governments as appropriate, unless otherwise indicated. Also, throughout the document, we have used 'we' to refer not only to Ofwat, but also to the wider water and sewerage sectors. We do this to highlight the part that everyone has to play in delivering sustainable water.





Contents

Foreword	4
Our strategy – a summary	5
1. Why sustainable water?	7
2. Delivering sustainable water: our vision and mission	15
3. Delivering sustainable water: our goals	23
Ensuring a fair deal for customers	24
Keeping companies accountable	26
Making monopolies improve	28
Harnessing market forces	30
Contributing to sustainable development	32
Delivering better regulation	34
4. Delivering sustainable water: our values	37
5. Using the best available information	38
6. Measuring progress	39
References	40

Foreword

The water and sewerage sectors have made significant progress since they were privatised two decades ago. Then, Government, regulators, companies and customers rose to the challenges they faced. And today, our reward is world-class drinking water and a cleaner environment. Services are also safer, better and more secure than ever before.

However, we now face a new set of challenges, including increased water scarcity and a growing population. These could threaten not only the progress we have made, but also our long-term water security. Our response will need to be different to that of the past 20 years. We need to find ways to make better, more informed decisions. And we must also renew, refresh and re-engage with the common purpose and shared sense of urgency that helped overcome the challenges we faced in 1989.

Our strategy, which updates and replaces the one we published in April 2008, builds on the work of many other organisations as well as our own. It also takes account of the many important events that have taken place in the past two years that could shape how the sectors develop over the long term. This includes:

- our 2009 price review;
- three key independent reviews on how the sectors operate;
- legislation and further projected legislation by the UK and Welsh Assembly Governments; and
- the global financial crisis.

All stakeholders need to respond to these events. But if we are to secure the services we have come to expect over the long term, we believe that what is needed is concerted and co-ordinated action at every stage of the water cycle – from abstraction to the point it is returned to the environment. We need the right

We face a new set of challenges, including increased water scarcity and a growing population

sustainable water and the part Ofwat will play in delivering it. Our ‘future regulation’ programme of work is designed to help us make our contribution. However, if we are to secure and improve for future generations the services that more than 50 million of us across England and Wales use and expect each day, we will need the help of everyone across these sectors. We are committed to working with stakeholders towards delivering sustainable water today, tomorrow and over the long term.

systems and information to help us make better decisions.

This strategy sets out our vision for



Philip Fletcher
Chairman



Regina Finn
Chief Executive

Our strategy – a summary

<p>This is our long-term aspiration.</p>	<p>Vision</p> <p>A sustainable water cycle in which we are able to meet our needs for water and sewerage services while enabling future generations to meet their own needs (‘Sustainable water’).</p>
<p>Our mission and goals set out how we will contribute towards delivering our vision.</p>	<p>Our mission and goals</p> <p>To ensure customers continue to receive safe, reliable, efficient and affordable water and sewerage services that promote positive social, economic and environmental impacts today, tomorrow and over the long term (‘Water today, water tomorrow’).</p> <ul style="list-style-type: none"> • Ensuring a fair deal for customers • Keeping companies accountable • Making monopolies improve • Harnessing market forces • Contributing to sustainable development • Delivering better regulation
<p>Our values describe how our organisation, and individuals in it, will behave in delivering all aspects of our work.</p>	<p>Responsibility</p> <p>We have values that underpin our vision, mission and goals. We will operate to the highest standards of public office and conduct our business in a responsible and ethical way.</p> <ul style="list-style-type: none"> • Excellence • Leadership • Respect • Integrity
<p>Our vision, mission and goals provide the basis of our annual priorities, which we set out in our forward programme each year.</p> <p>These annual priorities form the basis of our senior management team’s objectives. These in turn cascade down the organisation to the objectives of all Ofwat staff.</p> <p>This ensures actions required to deliver our strategy are allocated and aligned with individual responsibilities.</p>	<p>Delivery</p>
<p>Our annual report and resource accounts show what we have delivered each year and report on progress in delivering our strategy.</p>	<p>Progress and accountability</p> <p>We review how well we have done in delivering our work programme and achieving our goals, mission and vision in our annual report each year. We also report on the efficiency and effectiveness of our organisation in our annual resource accounts. Both documents are laid before Parliament.</p>



1. Why sustainable water?

The last 20 years

The water and sewerage sectors in England and Wales have come a long way since privatisation in 1989. Then, a neglected infrastructure, along with polluted beaches and rivers, meant we were seen by many as the ‘dirty man of Europe’.

Today, our independent regulation combined with the hard work of everyone across the sectors has delivered considerable benefits for customers and the environment. For example:

- leakage levels are 35% lower than they were at their peak in the mid-1990s;
- there is higher environmental compliance, with 98.6% of bathing waters in England and Wales meeting the required EU standards; and
- consumers have access to excellent drinking water, with 99.96% compliance with tough EU standards.

At the same time, we have kept bills for customers more than £100 lower than they would otherwise have been.

Since privatisation, the regulatory framework has allowed the companies to invest about £85 billion in maintaining and improving assets

and services. That amounts to more than £3,500 for each household in England and Wales, delivering real improvements at no additional cost to the taxpayer.

A litre of tap water, supplied and taken away, costs less than half a penny

Against this background, we have continually

pushed the companies to become more efficient. This is how we have kept bills as low as possible. Customers pay an average of 94p a day for their water and sewerage services. And a litre of tap water, supplied and taken away, costs less than half a penny.

Using both incentives and tough targets, we have made sure that consumers’ interests have been protected. For example, our comparisons on services, have encouraged the companies to rise to the highest industry standards. If any have fallen short, we have held them publicly accountable and taken action. We have used our enforcement powers to impose penalties of almost £75 million on companies that failed their customers, as well as securing redress for those customers.

New challenges

Looking ahead, the sectors face a number of major new challenges that could have big effects on the services we all rely on every day.

Challenge	Cause	Effect
Adapting to climate change	Climate predictions for the UK indicate that our weather will be more volatile in the future. This could lead to increased water scarcity and devastating floods, such as those in 2007 and 2009.	This will affect the safety and reliability of services. Substantial investment and innovation is needed to manage supply and demand. We must also consider the impact this will have on other sectors. Water scarcity can reduce industrial output. It will have an impact on the amount of food we can grow. All sectors will need to find new ways of making the most of the resources we have.
Mitigating the effects of climate change	In 2008, the UK became the first country in the world to commit to legally binding carbon reduction targets. The sectors use a lot of energy and create greenhouse gas emissions. The companies have a role to play in reducing their impact on the global climate.	The sectors are energy intensive and have a large amount of carbon embedded in their production processes. Reducing carbon impact while also improving services and the local environment will be complex. The companies will need to invest and innovate in new technologies, processes and approaches that protect both the local and global environment.
Worldwide water scarcity	We currently export about two-thirds of our demand for water by importing water-intensive goods from elsewhere. This has a detrimental environmental impact in areas where water is scarce. By 2030, if no further action is taken, almost half of the world’s population will be living in areas where water scarcity is a serious issue.	As climate change increases and foreign environments become less productive, we may need to grow more of our own food. This will increase the amount of water we need in this country. However, water is already scarce in some regions and over-use is causing environmental damage. Growing worldwide water scarcity may increase these problems. This will require a variety of approaches to increase the use of scarce resources and assets, as well as more investment and innovation in delivering services.
A growing population	The UK currently has 0.9% of the world’s population but only 0.3% of its renewable fresh water. Our population is continuing to grow, particularly in the south-east where water resources are already stretched. By 2060, the UK is projected to have the largest population in the EU. There are also expected to be more single households, which use more water per person.	Population growth will increase the demand for services, particularly in areas where water is already scarce. Increased urbanisation will also intensify sewerage and drainage needs while reducing natural drainage on undeveloped land. This will require further investment and innovation to ensure services are effective and efficient.

Challenge	Cause	Effect
Complying with stringent environmental standards	The costs of implementing EU legislation are considerable. For example, the Water Framework Directive, could cost between £30 and £100 billion in England and Wales by 2027. Much of the cost of this investment is likely to fall on water customers.	Tough standards will require major investment to deliver. It also needs innovation if we are to avoid increasing carbon emissions. The impact on customers’ ability to pay for their water and sewerage services could be substantial.
Meeting rising consumer expectations	We live in a modern, globalised society. Introducing markets in other utility sectors has increased customers’ expectations about having choice over the prices they pay and the services they receive. Customers also want more tailored, environmentally-friendly and socially-conscious services.	All sectors need to respond to these changing needs. Meeting those expectations will require more investment and innovation in service delivery.
Affordability	Over the past 20 years, water and sewerage bills have increased on average by more than 40% in real terms. One aspect is that the cost of bad debt is rising and accounts for about £12 on each customer’s bill every year.	Affordability is already a problem for some customers. The large investment required to meet other challenges could make the problem worse, pushing those who need the most help deeper into debt. Higher bills would increase the incentive for customers who avoid paying their bills (but can afford them). This would increase bills for everyone else who does pay. We need better and smarter ways of getting these people to pay while protecting those who genuinely have difficulty with their bills.
Uncertain economic environment	Current economic pressures are placing greater emphasis on the need of UK businesses to maintain and improve their competitiveness. Households with limited budgets are looking for greater value from the services they receive. Those needs, even if economic conditions improve, will not decrease.	The difficult economic conditions have placed even greater focus on the affordability of bills and the competitiveness of businesses in England and Wales. The sizeable investment required to meet other challenges may mean that water and sewerage bills will need to increase in the future, placing more pressure on constrained household budgets and on the competitiveness of some businesses.



Dealing with uncertainty

Water is essential to life. Good quality water, sanitation and drainage services are fundamental to our society. But the challenges we face will make delivering safe, reliable, efficient and affordable services increasingly difficult.

Historically, providing water and sewerage services has been a fairly predictable business. The companies could use well-developed tools, approaches and past experience to make reasonably accurate forecasts of what, where and how much to invest.

Now we face a much wider range of uncertainty. For example, uncertainty about climatic conditions – temperature, wind, drought and excess rainfall. Also, uncertainty about the levels of demand, which could be altered by changing weather patterns, population growth, lifestyle, demographic shifts and geographic coverage.

Simply relying on the solutions of the past will not be enough to continue to deliver the services of the future. Nor do we know the

The solutions of the past will not be enough to continue to deliver the services of the future

nature and extent of the innovative solutions we need to develop. We need better information to

make choices about what we invest in, where we invest and how we can ensure we do it at a price we can afford.

Meeting these challenges will make an essential contribution to our way of life, the health of our environment and the competitiveness of our economy.

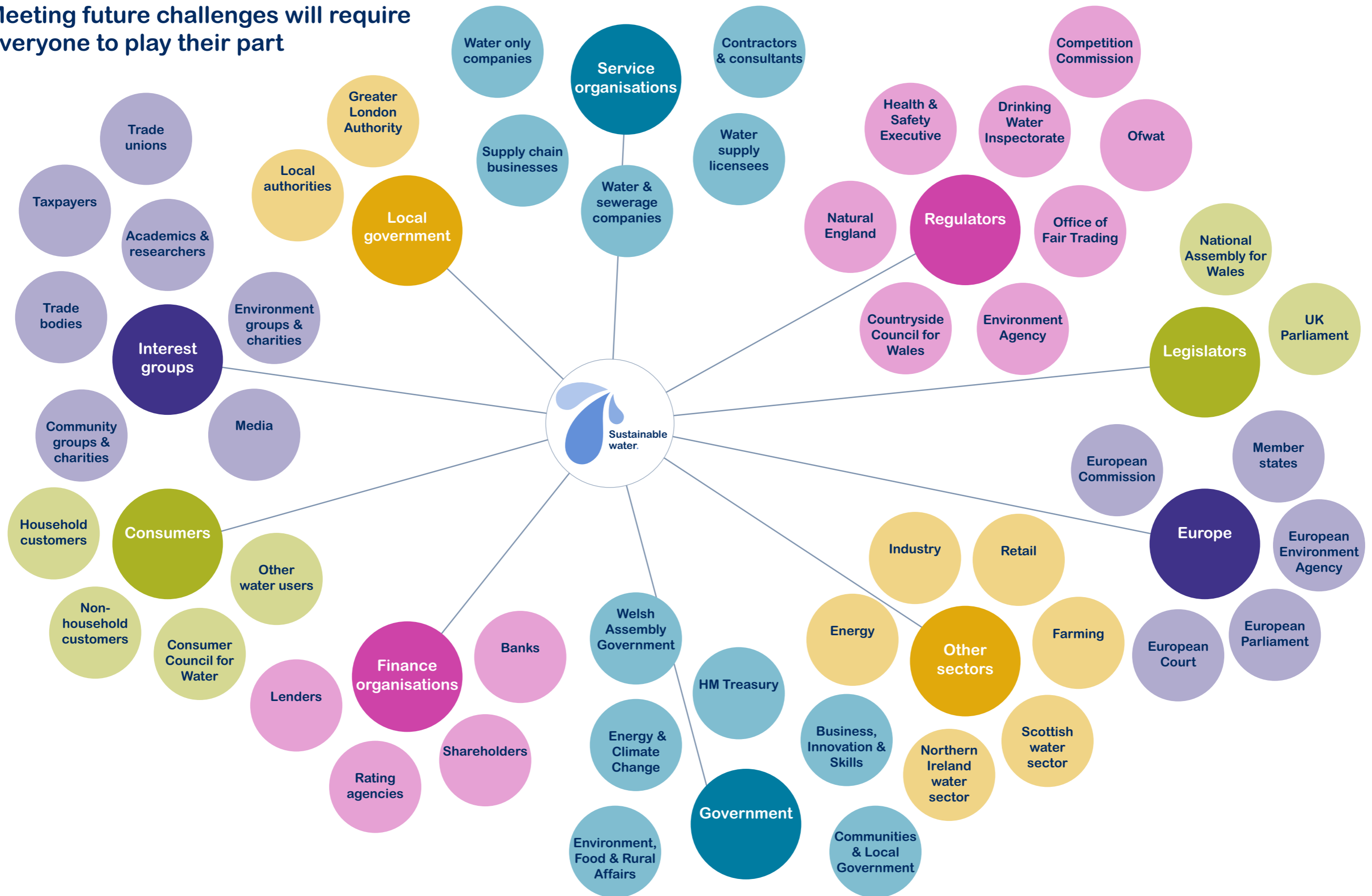
The need for change

To secure water services over the long term, there are a number of things we all must do.

- **We have to start looking for solutions now.** The challenges we face are so critical to services that we cannot wait 25 to 30 years into the future. It can take more than 20 years for a company to build a reservoir. If consumers are to continue to receive the services they need, then we all need action.
- **We need to find better ways of doing things.** We cannot rely on continuing to do things the same way as before. The way we all plan, manage and use water, sanitation and drainage services must be sustainable in the long term. We all must consider if other approaches could provide more effective use of scarce resources.
- **We all have to play our part.** Finding solutions to the challenges we face is not as simple as building more reservoirs or larger sewers. We all need to rethink every stage of how we plan and use water and sewerage services. The way we manage and value water more widely in our society has to change as well. For that to happen we need everyone, from Government to consumers, to work together.

If we do this, we can find new ways of ensuring the long-term future of the services we rely on. At Ofwat, we are committed to working with all of our stakeholders to help deliver sustainable water.

Meeting future challenges will require everyone to play their part





2. Delivering sustainable water: our vision and mission

Sustainability

Sustainable development (or ‘sustainability’) is a frequently misused and misunderstood term. The most widely accepted definition is:

“To meet the needs of the present without compromising the ability of future generations to meet their own needs.”

(Bruntland Commission, report to the United Nations, 1987)

It is not only about making sure we all have what we need to live (‘to develop’) today, but also to do with:

- understanding the long-term implications of our choices and decisions;
- preventing irreversible damage to society, the environment and the economy;
- leaving opportunities for future generations; and
- using scarce resources in the most efficient and effective way possible.

It is about making sure that we do not jeopardise the welfare of future generations.

Ofwat and sustainability

In ‘Water today, water tomorrow – Ofwat and sustainability’ (April 2009), we set out our overall approach to sustainability. We provided some examples of how we contribute to sustainable development. And we set out our sustainability principles, which are outlined below.

1. A safe and reliable water and sewerage service for consumers that minimises the impacts on the environment now and in the future.
2. Consumers continue to get a fair deal and receive a level of service that consistently meets their needs.
3. Financially robust sectors that are able to meet consumers’ needs at a fair cost, into the future.
4. Companies that remain accountable to their consumers.
5. Using the best available information to support decision making.

We use these principles to inform our decision making.

Sustainable water

Everyone, directly or indirectly, has an impact on the water, sanitation and drainage services we rely on every day.

From an industrial plant taking water out of a river as part of its production process, to the individual decisions customers make about what to buy from a supermarket. They all have a ‘water footprint’ in the same way that they all have a ‘carbon footprint’. So, it follows that everyone must treat water as a valuable resource if we are to ensure the security of those services over the long term.

As the economic regulator, the decisions we take and the framework we set will play a big part in how successfully the sectors respond to this challenge. But we are only part of the solution. We must each play our part to manage the water cycle (see page 18) in ways that allow us to meet our needs for water and sewerage services while enabling future generations to meet theirs.

Delivering sustainable water

Delivering sustainable water will be a continuous process rather than a target that can be achieved over time. This is because what we consider sustainable today may be considered less so in the future as a result of new information, ideas and experience. The important thing is to make progress – each drop of water should be more sustainable than the one before.

The key barrier that is preventing the sectors from making progress is the uncertainty caused by the challenges we now face and the lack of information to inform our choices. We cannot afford to wait for the future to be clearer before we act because it could be too late. Nor can we afford to act too rashly because the consequences could be equally as bad. What we need is to:

- reduce the necessity for us to act by using our existing scarce resources more efficiently;
- reduce our doubt about what action we should take by finding the information we need to make better choices; and
- reduce the consequences of getting our decisions wrong by making sure the action we take is flexible and leaves us options in the future to adapt them to deliver what we need.

At the heart of all of these things is making the right choices. This means having the right systems and information in place on which to base our decisions.

- The **right systems** encourage all of us to make better choices by:
 - making the most efficient use of resources;
 - finding new ways of doing things; and
 - ensuring what we do can be adapted in different ways in the future.

It is about making sure that we all contribute our fair share towards sustainable water.

- The **right information** allows us to decide what the best action is that we can take. It is about using the ‘true value of water’ in all that we do.

Finding solutions

We have identified the areas where we can play a part in finding these solutions. Our goals reflect this and are set out in chapter 3. We know that there are many issues that are critical to making progress towards sustainable water and go beyond our duties as the economic regulator. Some of these are illustrated on pages 20 and 21.

To make progress everyone needs to play their part. One example of where we are already working with others towards a common goal is illustrated below.

Delivering sustainable levels of abstraction

Water is currently taken out of the environment (‘abstracted’) by a variety of different industries, including farming, energy and water supply.

We already cause damage to the environment because we take out more water than is replaced naturally. One of the causes of this is that end users, including the companies and their customers, do not receive the right information about the water they use. At the moment, there is little relationship between water scarcity and the amount that is charged to abstract it. In fact, it can cost more to take water from areas where it is plentiful than where it is scarce. Therefore, the price that is paid for water does not reflect its ‘true value’.

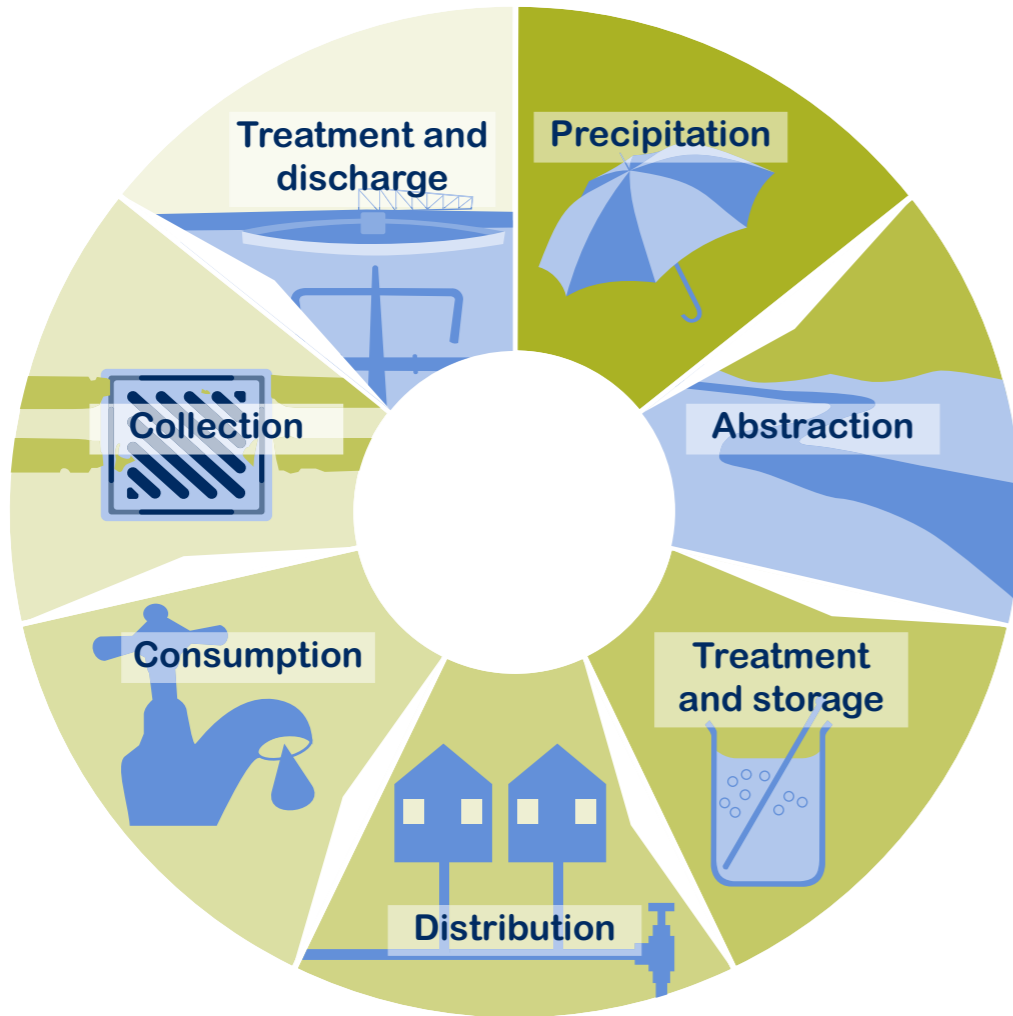
The result is that the companies that abstract water and the end users who consume it do not receive signals about how carefully to use water in their area. Without these signals, they will go on using the water in the same way, which could cause further damage to the environment. It could also mean that, when there are droughts, there may not be enough water to go around. It could mean restrictions on the amount of water that customers use. It decreases their water security.

This is why we have been working with the Environment Agency to remove barriers to trading of abstraction rights. We consider that a market would be the right system to reveal the relative social, economic and environmental value of water taken from different locations.

This would not only help achieve environmentally-friendly levels of abstraction. It would encourage all water users to be more efficient in how much they use. For the companies, it would mean they receive signals about where and how urgently innovation and investment is needed, for example in reducing water use or developing new resources elsewhere.

The challenge will be to ensure those same signals are passed along the water cycle, so that everyone – from Government to customers – can make the right decisions based on the true value of water. In this way, we can make progress towards delivering sustainable water.

To deliver sustainable water, we need action at every stage of the water cycle



1. Precipitation

Rainfall provides the fresh water we rely on. In England and Wales, much of our rain falls in the winter. Water soaks into the ground (groundwater) or flows into lakes and rivers. At the moment, our seasonal rainfall is fairly reliable, although it will be less predictable in the future as our climate changes. However, this does not make the task, on any given day, of predicting where (and how much) water will fall any easier – or building the systems to collect and store it.

2. Abstraction

We get most of our water from rivers, groundwater and reservoirs. It supplies our homes and businesses. Other sectors, such as agriculture and industry, also use it. Collectively, we take about 60 billion litres of water out of the environment every day. If we are not careful, there is a risk that, in future, we will not have enough to supply our homes and businesses, to grow our food, produce the goods we need or generate our power. Our environment will also be damaged.

3. Treatment and storage

Water is treated to a high standard before we use it in our homes and businesses. It all has to be safe to drink (even if we use it for other things like cleaning and flushing the toilet). Our water is also stored for when we need it. This is so that we get continuous supplies no matter what the time of year.

4. Distribution

Every day, almost 15 billion litres of clean drinking water is pumped through a complex system of pipes to get it to where we need it – and at a pressure we can use it. Transferring water long distances is expensive and uses a great deal of energy. This is one reason why there is no national grid for water like there is for electricity. In England and Wales, there are more than 338,000 kilometres of water pipes – enough to reach round the Earth eight times. Maintaining them is a huge task. It is also a difficult one, because many of the pipes run under buildings and roads. The companies have a difficult balancing act – finding and reducing leaks while making sure our roads and property are not constantly disrupted by repair work.

5. Consumption

On average, we each use about 150 litres of water a day in our homes for drinking, cooking, cleaning, flushing the toilet and gardening. We also use drinking water at work, and in our public spaces and places of leisure. It is always available. When things go wrong with our supplies we notice immediately – and it has a big impact on our lives. This is why safe, reliable supplies of water are so important.

6. Collection

When we use water at home or at work – the waste and water (or ‘wastewater’) flows into a vast network of sewers. It is then pumped away to be treated. This system needs maintaining to clear blockages and repair breaks, and also to stop wastewater flooding our homes or businesses. But it is not just wastewater that gets into the sewers. Water falling onto hard surfaces that do not drain (like our roofs or roads) also has to be taken away and treated. Not to mention the other things that get into sewers – from waste liquids to everyday objects. All of them need to be removed – or our properties could be flooded with sewage.

7. Treatment and discharge

Wastewater needs treating before it is returned to the environment. This can be a complex and energy-intensive process that emits a lot of greenhouse gases. Some of the waste that is removed (known as sludge) can be used to generate energy. Once it has been made safe, the sludge is ultimately disposed of, usually by spreading it on land as fertiliser, or by being burned. Eventually, the water remaining after treatment is safe to put back into the environment – where it evaporates to form rain clouds – and the cycle starts again.

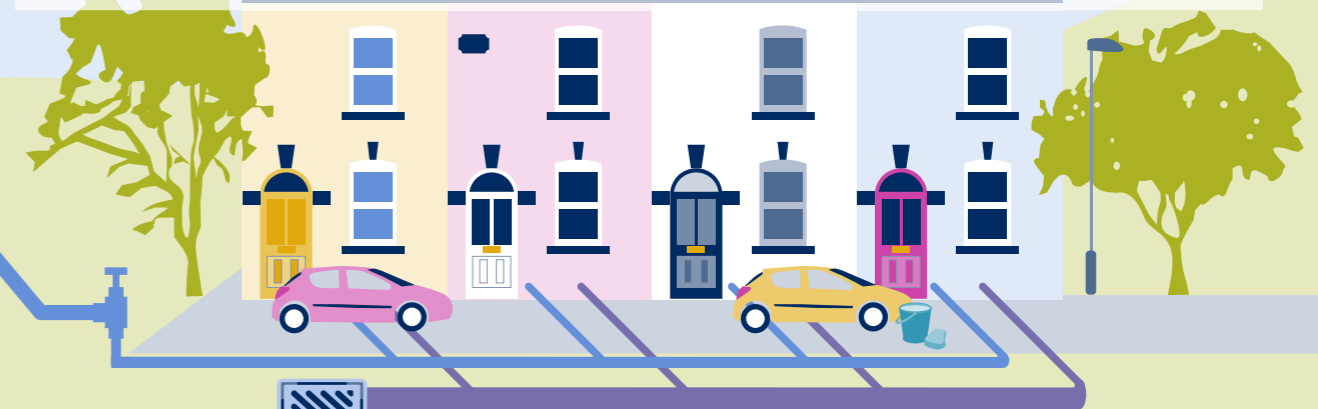
Promoting a fairer, greener society

Rainfall often washes pollution into water sources. This may come from urban sources, such as garage forecourts and industrial premises, or run-off resulting from poor agricultural practices. Treating poor-quality water to remove chemicals, fertilisers and pesticides increases the costs to the companies and their customers. So, they end up paying to clean up pollution from other sectors so that the UK complies with environmental laws. We need to find better ways of making sure that all polluters pay their fair share of preventing or cleaning up such pollution.



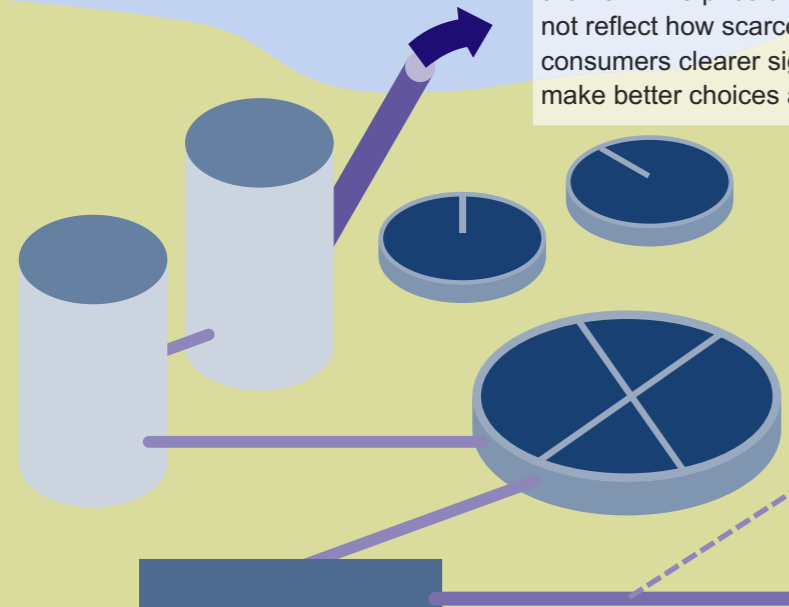
Delivering a better environment

We all want clean local rivers. We also want to reduce the effects of global climate change. That is why tougher environmental standards are being set. But this means using more energy – and generating more greenhouse gases. We need to ensure that environmental standards are sensitive to the needs of both the local and global environment. But we also need to find better ways of delivering this.



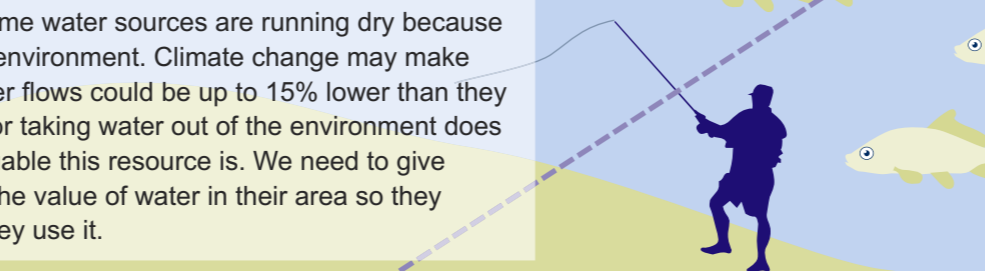
Revealing the true value of water

In parts of England and Wales, some water sources are running dry because too much is being taken from the environment. Climate change may make things worse. By 2050, annual river flows could be up to 15% lower than they are now. The price all users pay for taking water out of the environment does not reflect how scarce or how valuable this resource is. We need to give consumers clearer signals about the value of water in their area so they make better choices about how they use it.



Adapting to a changing climate

Climate change may affect the seasonal reliability of our weather, leading to more droughts and floods. Predicting these changes will be difficult. We need to find ways to ensure the right infrastructure is in place, at the right time and for the right price to cope with this variable weather. Sometimes the solutions will involve ‘green’ infrastructure (for example, increased water storage and sustainable urban drainage). We also need to make sure that water services are resilient to severe weather events.



Ensuring resilient infrastructure and sustainable drainage

In England, about one in six households and businesses are at risk of flooding. We need to find better ways to plan for such events, as well as maintaining and improving the infrastructure we rely on to drain our homes and surroundings. But we cannot always have bigger sewers. We also need to encourage sustainable approaches to reduce the amount of surface water we produce. For example, replacing tarmac or concrete driveways with materials that allow water to soak naturally into the ground.



Encouraging sustainable consumption

In the future, climate change may mean we have less water available when we need it – and more when we do not. We need to find better ways of encouraging all users to make more sustainable choices about the water they use and the wastewater they produce. This includes using more water-efficient products or harvesting rainwater to use around the home. We also need to find new ways of protecting the most vulnerable customers to ensure they receive the services they need.





3. Delivering sustainable water: our goals

Our goals in helping to deliver sustainable water and achieve our mission are:

- ensuring a fair deal for customers;
- keeping companies accountable;
- making monopolies improve;
- harnessing market forces;
- contributing to sustainable development; and
- delivering better regulation.

They are founded on our principles of sustainable development (see page 15), and are also complementary. No single goal can be delivered in isolation or to the detriment of any of the others. For example, we cannot ensure a fair deal for customers without making sure the sectors contribute to sustainable development.

Under each goal, we state:

- what it means;
- our long-term view of what we are trying to achieve;
- an example of how we propose to turn our strategy into action; and
- key elements of our legal duties and powers that are most relevant (although in practice we will consider all elements of our legal duties and powers that are relevant).



Ensuring a fair deal for customers

What it means

- Making sure that all customers receive the services they expect at a price that treats them and others fairly, is transparent and gives them choice and some control over the charges they pay.
- In the absence of customer choice, challenging monopolies to improve on all aspects of service and price they offer. And where there is choice, making sure that markets deliver benefits to customers and the environment.
- Making sure that customers now and in the future contribute their fair share – and no more – towards sustainable water.
- Making sure that our work takes account of customers’ priorities, including those who need additional help and those on low incomes.

A long-term view

All customers deserve a fair deal on their water and sewerage services. We want them to receive a level of service that meets their needs at a price they are willing to pay.

So, subject to Government decisions, we will be implementing a number of the agreed recommendations from the independent review of household charging and metering (the ‘Walker review’). This includes:

- managing the transition to universal metering; and
- reviewing charges to check that all customers are treated fairly.

We will also work with Government to provide a clear framework to support customers who are unable to pay their bills.

To ensure a fair deal for customers over the long term, we consider that we need to make greater use of market forces. Markets reveal information about services in a way that regulation alone cannot. This will be important in delivering long-term water security. Market forces also give customers choice – not just over their service provider, but over the package of services they receive.

The most visible aspect of this work will mean increasing the number of customers able to choose their water and sewerage service supplier. However, we will also look to introduce markets in other areas where this will benefit the services customers receive.

Markets may take a long time to develop. They may not be possible at all in some areas. In these cases, we will continue to challenge the monopoly companies on all aspects of the service and price they offer to customers. We want them to have the same pressure to improve that they would have in a competitive market.



We also want to make sure that all companies deliver their wider social, economic and environmental obligations. This includes:

- reducing the environmental impact of their services;
- encouraging sustainable behaviour by their customers; and
- providing effective management, support and encouragement to customers in debt or with affordability concerns.

So, we will be seeking changes to the way that companies deliver services and the way that customers use them. We will also be changing the way that we regulate to make sure the right incentives are in place, and we will be seeking to influence others to take account of customers’ priorities and their interests.

For example, we think it is fair that the person, organisation or sector responsible for producing pollution should also be responsible for fixing it – or, better yet, preventing it. This is the ‘polluter pays’ principle as promoted in EU legislation such as the Water Framework Directive. However, at the moment water customers can end up paying far more than their fair share towards investment in the environment. We think this needs to change.

Turning strategy into action: charging and metering

Over the next two to five years, we are planning a fundamental review of our policy framework for charging for water and sewerage services.

The project will address challenges from:

- the Walker review on household charging and metering;
- affordability and debt;
- the transition to universal metering;
- potential links to the roll-out of smart metering in the energy sector;
- climate change; and
- market reform.

We want the companies to develop charging systems that are fair to all customers and encourage sustainable behaviour. We also want charges that:

- do not require customers to meet the costs of treating pollution caused by others; and
- reflect the value of the resources used to deliver water and sewerage services.

Relevant key duties and powers

- We exercise our powers in the manner best calculated to further the consumer objective (by promoting competition and by having regard to the interests of vulnerable customers and customers of licensees).
- We ensure that there is no undue preference or undue discrimination in the charges customers pay.
- We ensure that customers receive proper benefit from the disposal of protected land.

Keeping companies accountable

What it means

- Making sure the companies deliver the services they promise at the price they agreed and meet their legal obligations.
- Making sure that monopoly suppliers listen to their customers, deliver their priorities and are honest about their performance. And, where there are open markets, ensuring that the companies operating in them do not break the market rules.
- Making sure that the companies meet their wider social, economic and environmental obligations.
- Where companies fail, taking fair and appropriate action against them to protect customers, put things right and deter them from further failures.

A long-term view

We aim to create an environment where the companies are accountable to their customers rather than to us.

We want a level of accountability similar to more competitive sectors. There, companies are under constant pressure to focus on their customers’ needs. If customers are unhappy with the service they are receiving, or they consider that their needs are not being met, they will take action by taking their business to another supplier.

We will focus on ensuring that all the companies listen to their customers and deliver their priorities. We will also place the emphasis on them to be honest with their customers and take responsibility for their performance.

In all that we do, we will make sure we continually encourage the right behaviour from the companies. We will also continue to meet our obligations to take action against companies found to be failing. And to ensure this happens, we will continually review the approaches we use. For example, we will:

- make sure that incentives are in place to enable the companies to behave in an accountable way towards their customers;
- set out clearly what enforcement action we could take if a company fails to deliver and give reasons why we take any action;
- publish clear guidance on what the companies need to do to secure compliance;
- make sure that, in monitoring whether companies comply with our requirements, the information we collect is relevant and keeps the regulatory burden to a minimum;
- make sure that, as the sectors develop, the licences and conditions companies operate within remain fit for purpose; and
- carry out proactive investigations into company performance that are targeted on high-risk areas.

Ensuring that the companies are accountable over the long term will be difficult. This is because they will need to deliver investment today that may only begin to have benefits for future generations. However, we will make sure that all companies are incentivised to make balanced decisions that take account of the needs of customers today, tomorrow and over the long term.



Turning strategy into action: regulatory compliance

Over the next few years, we will review how we monitor compliance and enforce that the companies deliver appropriate service standards and their other regulatory and legal obligations.

This work aims to create a risk-based framework that protects consumers’ interests by:

- developing incentives to encourage the companies to take full responsibility for complying with their obligations to customers and the environment;
- looking to reduce the regulatory burden;
- strengthening the reliability of company reporting;
- targeting examination of contractual, compliance or performance concerns about companies; and
- establishing the principles we use to carry out investigations into company compliance.

We want the companies to be fully accountable to customers for their performance and compliance with other standards. We also want customers to be able to get redress when the companies fall short.

Relevant key duties and powers

- We exercise our powers in the manner best calculated to secure that the functions and duties of companies and licensees are properly carried out.
- We ensure that customers are protected with respect to companies’ unregulated activities and that trade with associates is at arm’s length.
- We shall investigate anti-competitive behaviour, where appropriate.

Making monopolies improve

What it means

- Challenging the monopoly companies to improve in all aspects of their performance, delivering their customers’ priorities as well as their other legal obligations.
- Making sure that the way that monopolies operate does not interfere with efficient and effective markets – and that they are encouraged to learn, adapt and behave in ways that mimic competitive markets wherever possible.
- Making sure that monopoly companies help ensure water security and meet their wider social, economic and environmental obligations effectively and efficiently.
- Making sure that our system of regulation provides the right incentives to ensure that monopolies innovate to improve all aspects of their services.

A long-term view

Most customers in England and Wales receive their water, sewerage or water and sewerage services from 21 monopoly suppliers. These companies are responsible for providing a range of services, from managing the collection, storage, treatment and distribution of water and sewage to dealing with customer enquiries.

While the current framework has achieved much since privatisation, it has its drawbacks. And this tried and tested regulatory approach may not be the best way to help them find the solutions that are necessary to ensure water security for their customers over the long term.

This is why we will continue to explore the likely benefits of accounting separation (and potential legal separation) of the different activities that the companies currently carry out. This involves significant change. But it can reveal more information about the provision of water and sewerage services. This, in turn, will highlight where we need better information and systems to make more sustainable choices.

This may involve introducing regulated markets. Equally, it could also mean developing better tools for regulating monopolies. However, we will ensure that the companies, in whatever form, continue to fulfil and finance their functions and deliver long-term water security.

Where there are monopolies we want them to strive constantly to improve the services they offer – on price, quality and choice. We also want them to encourage their customers to think more carefully about the water and sewerage services that they use. We want to nurture a spirit of innovation that means companies go beyond the minimum required by their regulator.

Making monopolies improve in new ways will require us to find new ways to encourage them. So, we will explore using new tools and systems to encourage the companies to consider more sustainable approaches to service delivery.



Turning strategy into action: future price setting

Monopoly regulation in the past 20 years has achieved much for consumers and the environment. However, future challenges will require the companies to deliver more in terms of investment, innovation, efficiency and effective services.

Key to making monopolies improve are the limits we set every five years on the charges these companies can pass on to their customers. However, so that the companies continue to improve, we need to look again at our approach to setting price limits. Just as our accounting separation project will improve the information we use in setting prices, so our future price setting project will make sure our overall approach will, among other things:

- make the best use of water resources;
- encourage investment in the right place, at the right time and for the right price;
- support the use of markets to deliver social, economic and environmental goals;
- reveal information and ensure prices at every stage of service supply reflect costs; and
- provide incentives to encourage creativity and innovation.

A key part of the project will be to work with our stakeholders, to understand their views and use their expertise to build a future approach to price setting that helps deliver sustainable water.

Relevant key duties and powers

- We exercise our powers in the manner best calculated to secure that companies can finance the proper carrying out of their functions.
- We promote economy and efficiency in the carrying out of the functions of a company.

Harnessing market forces

What it means

- Using regulated markets to reveal new information or new approaches to help deliver long-term water security.
- Introducing regulated markets where there are clear long-term benefits to customers and the environment.
- Monitoring markets to make sure they operate effectively and efficiently – and taking action where they do not.
- Designing markets, and the regulatory tools to harness them, in ways that promote positive social, economic and environmental benefits.

A long-term view

We want to build on what regulated monopolies have achieved in the past 20 years. We consider that markets can play an increased role in these sectors because they:

- give a wide range of people the incentive to think in new ways;
- provide the incentive to deliver investment and operations efficiently;
- reveal information about where and when innovation is needed; and
- adapt quickly to change.

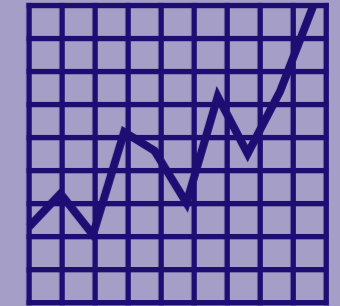
All of these things will be vital in addressing the challenges the sectors face in a more uncertain world. Markets can help deliver the new, innovative and more flexible solutions we need, such as:

- a sharper customer and business focus from the companies;
- more efficient financial structures;
- new services and management processes;
- reallocating water between areas;
- ensuring new water demand is located efficiently; and
- technological innovation in response to climate change.

We think there are benefits from introducing retail markets to give customers a choice of supplier. We will work with Government and other stakeholders to achieve this.

However, it is in the upstream processes of water and sewerage service delivery that markets can play the biggest role. These account for 90% of investment and almost all of the environmental impact. And it is the process of allowing rival companies to compete for customers that we wish to harness in these areas.

Evidence suggests that opening the markets in other utilities, such as telecommunications, electricity and gas, has led to improved productivity within those sectors. This is why we will work with Government and other stakeholders to introduce upstream markets.



But, experience in other sectors has also shown that they can have unforeseen side-effects. This means that we will need to be more flexible and adapt the way we regulate. We want to maximise the benefits markets can deliver. We may even look to withdraw regulation altogether. However, we will only withdraw where markets offer the same level of protection to consumers that we can offer. Even then, we will continue to monitor market performance closely. We will make sure we retain the tools – and knowledge of how to use them – should it become necessary to intervene to deliver long-term water security.

Turning strategy into action: market reform

We need the companies to innovate and find solutions to meet the challenges facing them. Regulated markets can help deliver sustainable solutions by revealing information and allocating scarce resources efficiently. They can also adapt more quickly to changing circumstances.

Our market reform projects are looking at every stage of the water cycle to see where and how markets could play a part in helping to deliver long-term water security. For example:

- enabling trading of water abstraction licences could result in water users (including the companies) making better use of resources where they are scarce – and so reduce damage to the environment from over-abstraction;
- allowing more customers to choose their water and sewerage suppliers could deliver keener prices and more choice over services; and
- opening up wholesale markets for water and sewerage services, or certain parts of supply and treatment, could result in increased efficiency, innovation and environmentally-sound approaches.

This work will be used to inform Government and Parliament on where and how markets can deliver benefits, as well as what changes to legislation are necessary to implement and develop them.

Relevant key duties and powers

- We exercise our powers in the manner best calculated to further the consumer objective (by promoting competition and with regard to the interest of vulnerable customers and customers of licensees).
- We exercise our powers in the manner best calculated to secure that companies can finance the proper carrying out of their functions.
- We promote economy and efficiency in the carrying out of the functions of a company.

Contributing to sustainable development

What it means

- Making sure that customers continue to receive safe, reliable, efficient and affordable water and sewerage services that promote positive social and environmental impacts now and over the long term.
- Making sure that the companies meet their customers’ needs and deliver long-term water security effectively and efficiently.
- Making sure the companies contribute towards wider social, economic and environmental objectives.
- Making sure that we make sustainable choices and our approach to regulation encourages others to do the same.

A long-term view

We need to find fresh approaches that will enable the sectors to meet the challenges facing them efficiently, affordably and in a way that is environmentally and socially responsible.

This will require a joined-up approach from customers, the companies, other regulators and Government at every stage of the water cycle. It also needs widespread and co-ordinated change. To help make this happen, we will work with our stakeholders to help find the solutions we need. In this way, we can all start making progress towards delivering sustainable water.

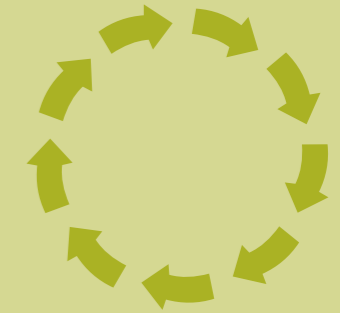
In terms of the direct role we can play, we will make sure that the companies are able to carry out their functions efficiently and effectively so that they:

- meet their customers’ needs; and
- plan and deliver long-term water security.

We will also work with Government and our other stakeholders to understand how the companies can contribute to achieving wider social, economic and environmental objectives, such as:

- helping meet the UK’s carbon targets;
- delivering local environmental improvements;
- meeting social policy obligations; and
- playing their part in increasing the competitiveness of the UK economy.

We want the companies to contribute their fair share to sustainable water – and the larger aspiration of sustainable development.



We want the companies to challenge themselves to improve and respond proactively to the challenges ahead. We also want them to view being sustainable as a key part of their success. To achieve this, we will make sure our overall approach to regulation promotes socially responsible, economically efficient and environmentally-friendly choices by companies and customers alike.

Turning strategy into action: sustainable drainage

In the future, particularly as climate change increases the intensity of rainstorms, the capacity of current drainage systems will be insufficient to meet our needs. Predicting where, when and how big to build sewers, for example, is unsustainable in the long term. Managing demand by using more natural drainage processes offers an alternative, but still has its risks.

Our sustainable drainage project will review and potentially reform our approaches to governance, stewardship and regulation of drainage infrastructure. As part of the project, we will:

- develop new evidence-based approaches to valuing and managing flooding risks and urban drainage;
- improve available evidence on the costs and benefits of different solutions for managing surface water flooding;
- promote new methods for incentivising, regulating, engineering and charging for drainage and surface water flooding risk management;
- identify and help remove barriers to the adoption of sustainable drainage systems or demand management approaches; and
- develop a new, clearer framework for the roles and responsibilities of individuals and organisations involved in urban drainage.

We aim to encourage more sustainable approaches throughout the drainage cycle – from better urban planning, to a clearer framework for demand management.

Relevant key duties and powers

- We contribute to sustainable development.
- We protect and preserve areas of natural or historic interest and allow freedom of access.

Delivering better regulation

What it means

- Effective regulation, delivered efficiently at a minimum cost to customers and a minimum burden to the companies.
- A system of regulation that encourages the companies to meet the needs of customers and the environment – and takes action against those that do not.
- Continually reviewing the tools, approaches and information we use to ensure that monopolies improve the services they offer and the markets deliver benefit to customers and the environment.
- Regulation that promotes positive social, economic and environmental impacts.

A long-term view

Delivering better regulation is about improving the way we do our job. This is to ensure that the companies innovate, plan and deliver the services we need for the long term efficiently and effectively.

It means that our approach to regulation must be flexible enough to help them achieve this goal. We will continually review and challenge the way we regulate so that it is:

- targeted only at the areas where it is necessary;
- proportionate to the issue we are seeking to tackle;
- accountable to ourselves and our stakeholders;
- consistent, so that we treat everyone fairly and equitably; and
- transparent and delivered in the clearest and most open way possible.

In this way, we can deliver more effective regulation.

However, delivering better regulation also means doing so more sustainably.

So, we will also continually review our expenditure and the regulatory burden we impose to keep them to a minimum.

In carrying out our work, we also want to promote positive social, economic and environmental impacts. We will do this by making sure that we make sustainable choices in all that we do – whether this is buying our own goods and services or designing the frameworks for encouraging sustainable procurement practices by the companies.



Turning strategy into action: future regulation

As the economic regulator of the water and sewerage sectors, we need to ask ourselves some tough questions if we are to help the companies meet the challenges of the future. We need to make sure that the way we regulate achieves our mission and helps to deliver sustainable water.

That is why we are planning to carry out a number of key projects as part of a ‘future regulation’ programme (including all of the projects set out in this document). The aim of the programme is to review fundamentally what we do, why we do it and provide recommendations on what our future approach should be.

To inform and advise on our future regulation programme, we have formed an expert advisory panel. It comprises respected professionals from a number of key fields of study. The group will help us generate ideas, learn from their experience, harness their expertise and provide challenge to our work.

As well as reviewing our regulatory approach, we have and will continue to review the skills our organisation needs to both deliver the future regulation programme and our continuing regulatory duties. These internal changes in structure and work practices will mean we are more focused and better equipped to work with our stakeholders to deliver sustainable water.

Relevant key duties and powers

- We employ the principles of best regulatory practice (transparency, accountability, proportionality, consistency and targeting action).

Summary of our goals

Ensuring a fair deal for customers

- Making sure that all customers receive the services they expect at a price that treats them and others fairly, is transparent and gives them choice and some control over the charges they pay.
- In the absence of customer choice, challenging monopolies to improve on all aspects of service and price they offer. And where there is choice, making sure that markets deliver benefits to customers and the environment.
- Making sure that customers now and in the future contribute their fair share – and no more – towards sustainable water.
- Making sure that our work takes account of customers’ priorities, including those who need additional help and those on low incomes.

Keeping companies accountable

- Making sure the companies deliver the services they promise at the price they agreed and meet their legal obligations.
- Making sure that monopoly suppliers listen to their customers, deliver their priorities and are honest about their performance. And, where there are open markets, ensuring that the companies operating in them do not break the market rules.
- Making sure that the companies meet their wider social, economic and environmental obligations.
- Where companies fail, taking fair and appropriate action against them to put things right to protect consumers, and deter them from further failures.

Making monopolies improve

- Challenging the monopoly companies to improve in all aspects of their performance, delivering their customers’ priorities as well as their other legal obligations.
- Making sure that the way that monopolies operate does not interfere with efficient and effective markets – and that they are encouraged to learn, adapt and behave in ways that mimic competitive markets wherever possible.
- Making sure that monopoly companies help ensure water security and meet their wider social, economic and environmental obligations effectively and efficiently.
- Making sure that our system of regulation provides the right incentives to ensure that monopolies innovate to improve all aspects of their services.

Harnessing market forces

- Using regulated markets to reveal new information or new approaches to help deliver long-term water security.
- Introducing regulated markets where there are clear long-term benefits to customers and the environment.
- Monitoring markets to make sure they operate effectively and efficiently – and taking action where they do not.
- Designing markets, and the regulatory tools to harness them, in ways that promote positive social, economic and environmental benefits.

Contributing to sustainable development

- Making sure that customers continue to receive safe, reliable, efficient and affordable water and sewerage services that promote positive social and environmental impacts now and over the long term.
- Making sure that the companies meet their customers’ needs and deliver long-term water security effectively and efficiently.
- Making sure the companies contribute towards wider social, economic and environmental objectives.
- Making sure that we make sustainable choices and our approach to regulation encourages others to do the same.

Delivering better regulation

- Effective regulation, delivered efficiently at a minimum cost to customers and a minimum burden to the companies.
- A system of regulation that encourages the companies to meet the needs of customers and the environment – and takes action against those that do not.
- Continually reviewing the tools, approaches and information we use to ensure that monopolies improve the services they offer and that markets deliver benefit to customers and the environment.
- Regulation that promotes positive social, economic and environmental impacts.

4. Delivering sustainable water: our values

Our staff are crucial to the successful delivery of our strategy. That is why our organisation, and every individual at Ofwat, will act in accordance with our values of:

- excellence;
- leadership;
- respect; and
- integrity.

They describe how we will behave in delivering our strategy and our approach to regulation. They also help us ensure that we are consistent and fair in all that we do.

Excellence	
Focus on being the best	
Be clear about what we want to achieve	
Take consistent, proportionate and targeted action	
Leadership	
Take difficult decisions based on the best available evidence and measured risks	
Challenge where appropriate and be prepared to be challenged	
Initiate and embrace change	
Respect	
Be professional and treat others as we would like to be treated	
Learn from others	
Create and encourage open, honest and transparent communication and relationships	
Integrity	
Doing what we say we will do	
Maintain an independent, balanced and fair approach	
Be accountable and take responsibility for our decisions	

5. Using the best available information

In aiming to regulate in a way that allows the sectors to deliver sustainable water, we must be sure that our strategy is clear. It also needs to be flexible enough to allow us to deal with the uncertainty of the challenges we face in the future. And, most of all, it must be based on the best available information to support decision making.

As part of our commitment to delivering better regulation, we will continually review our strategy to make sure what we do is appropriate in helping to deliver long-term water security.

To this end, we will carry out a project to outline a number of different future scenarios. We aim to ensure what we do is based on the best available information. The project will draw together available evidence on a range of key factors affecting the sectors over the long term. This includes:

- climate change and the environment;
- population, health and social economics;
- political climate;
- UK and global economic environment;
- public interest and consumer expectations for water and sewerage;
- developments in competitive markets;
- technical innovation; and
- legislative change.

The outcome of the project will be a small set of plausible scenarios of the future to help us in our decision making. They will also provide our stakeholders with context to our work, as well as provide reassurance and transparency that our actions and decisions are based on the best information available. We will publish this work during 2010-11 and continue to update it as necessary.

6. Measuring progress

We view the delivery of sustainable water as a continuous journey, not a final destination. Things may change because of new approaches or innovations. This is why it is important to measure progress. We want to show how far we have come, but also how far there is still to go.

Each year, we will set out what we will do in our forward programme to deliver our aim and our goals. We will also review progress in our annual report. This includes reporting on our long-term progress towards delivering sustainable water.

We plan to develop a set of sustainability targets and indicators during 2010-11 and 2011-12, covering both our performance and that of the companies. We need meaningful targets against which to measure our progress and the future regulation projects will provide the basis for this work.

At times, it will be harder to demonstrate that our policies deliver sustainable water. Conflicts may arise with some requirements (such as new laws on local environmental quality) that we have to accommodate.

In such cases, we will make sure that our overall vision of sustainable water remains core to our decision making. We will promote evidence-based policy making, and voice our

concerns if new policies or commitments threaten the delivery of sustainable water.

The delivery of sustainable water is a continuous journey, not a final destination

We will also evaluate our approach continually and make improvements

so that we deliver effective and consistent outcomes to consumers, the companies and the environment. This includes reviewing our strategy regularly so that we can be sure it has the right elements to deliver our mission and contribute to our vision.

Finally, we recognise that we are just one organisation acting in an area with responsibilities for – and impacts upon – the water cycle. We will work with other stakeholders to ensure that all aspects of the water cycle are sustainable.



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