



Innovation consultation
Ofwat
21 Bloomsbury Street
London
WC1B 3HF

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**Anlian Water
Services Ltd**
Lancaster House
Lancaster Way
Ermine Business Park
Huntingdon
PE29 6XU

Tel 01480 323000
www.anlianwater.co.uk

Our ref

Your ref

Innovation funding and competition: Further consultation on design and implementation

Thank you for the opportunity to respond to this consultation. This letter and associated appendix constitutes our response.

Building on our existing engagement with Ofwat on this agenda, we very much welcome the ambition to support transformational innovation through activities in AMP7. As a sector, we believe we are more aligned than ever, strengthened by the work we have done together on the development of the sector strategy. We support the aim of trialling all three funding streams this financial year. These will allow us to build on our existing successful approaches to innovation, which include our Newmarket Innovation Shop Window, our Water Innovation Network and Innovate East. We have gained enormous insight through these ongoing innovation projects and partnerships and feel we can bring this learning to support the ambition to transform innovation in the sector, particularly through the proposed Centre of Excellence.

Overall Ofwat's proposals appear reasonable and pragmatic and helpful to enabling innovation. However, we would advise that all the funding sources leave open the possibility for alternative arrangements that deliver the same customer protections as Ofwat's proposals (or default arrangements) at the project assessment stage. This strongly aligns to a principles and outcomes based regulatory model. We would highlight this in three particular areas:

• Intellectual Property Rights and Royalties

We believe there is an opportunity to adopt more flexible arrangements than in the energy sector. We think this may facilitate greater engagement from third parties, SMEs and disruptors. The two principle outcomes that any arrangements should seek to deliver are that customers do not pay to access intellectual property that they have funded, and that customers receive a share of any royalties commensurate with their contribution.



Registered Office
Anlian Water Services Ltd
Lancaster House, Lancaster Way,
Ermine Business Park, Huntingdon,
Cambridgeshire. PE29 6XU
Registered in England
No. 2366656.

an AWG Company

· **Financial ring-fencing**

Some of the proposed requirements could cause issues in certain circumstances. For example, some securitised companies may have limits on the number of bank accounts they can operate under their financial covenants. If those companies are inadvertently excluded from accessing project funding, the potential for transformational innovation that benefits all customers could be constrained. The outcome we should be seeking to achieve is that all project related expenditure is transparently recorded and available for scrutiny. It is possible to achieve this outcome through budget reporting without using a separate bank account.

· **Interactions with the price control**

There may be interactions between existing regulatory instruments (e.g. the price control or instruments of appointment) that limit the scope for innovative projects. An example would be a conflict between Licence Condition E and the trialling of innovative tariffs. It would be premature to rule out any derogations from existing regulatory instruments at this stage, but instead allow for these to be considered on a case by case basis as part of the bid assessment.

In these areas and others, we believe Ofwat should leave open the possibility for alternative arrangements to be proposed and at this stage merely outline the outcomes that it seeks to achieve. As ever there is a balance to be struck between being totally flexible and creating significant burden in assessing proposals, with being rigid and stifling innovation. By outlining outcomes to be achieved upfront, Ofwat can place the responsibility for demonstrating that the alternative arrangements meet the desired outcomes on the project's proposer. The independent organisation and Ofwat can then consider the merits of these proposals, and we would urge that Ofwat ensure a rigorous and ongoing external audit process to ensure that the costs of administration of the system put in place are kept as low as possible.

We trust these comments will help inform Ofwat's work. Please do not hesitate to get in contact if you wish to explore anything further, either directly with me, or with my colleagues [REDACTED]

[REDACTED]

Yours faithfully

[REDACTED]

[REDACTED]

Appendix 1 - consultation questions and responses

Q1: Do you agree with our proposed default arrangements for managing IPR and royalties? Do you think these arrangements work for different types of projects and activities (e.g. new technology vs. process innovation, roll-out activities etc.)?

We believe there is an opportunity to adopt more flexibility in this area to attract greater engagement from third parties, SMEs and disruptors. It is important that, regardless of the arrangements adopted, differing arrangements that meet predefined principles and outcomes are considered on a case by case basis.

We feel it would be challenging to have a single arrangement regarding IPR which would be appropriate for the diversity of projects the Innovation Fund is intended to support. Where a project involves only water companies, the arrangements suggested could be appropriate as a default position, particularly for projects which aim to reduce the risk of rolling out new innovations that are currently on the market. In this case the IP created is most likely to be knowhow, and as such, would not incur the costs involved with IP protection and prosecution, or adversely affect the ability of the technology provider to exploit the product further.

However, where there are other organisations involved in the creation of new IP, such as the development or improvement of new technologies, we feel that the proposed arrangements may be a potential barrier to transformational innovation.

We understand the sentiment around foreground IPR being granted on a royalty free basis to the companies contributing to the fund. However, we do believe that this arrangement may pose some challenges, both in meeting the objectives of the fund to drive transformational innovation, and the subsequent practical arrangements in managing the IP once the project is complete.

Examples of some of the potential challenges with the proposed approach are outlined below:

- For technological innovation where the funded project seeks to improve an existing technology, access to foreground IPR without the same access to background IPR could result in the foreground IPR being unusable or worthless
- Technology based companies with potentially transformational products under development may be reluctant to participate in the competition if they are required to surrender the foreground IPR to organisations that are likely to be the main UK customers of the new technology
- If projects are collaborative, it may be difficult to differentiate which organisation has developed foreground IPR and consequently who owns it
- Consideration needs to be given to how IPR protection is funded, particularly for patents, which can take up to five years to be granted. These can incur ongoing costs of patent fees and filing in other territories in addition to the initial costs of patent drafting and prosecution, potentially for twenty years.

The relative importance of these factors will depend on the type of project being done and the technology readiness levels of the technologies being implemented. Different levels of investment made by the fund may also need to be taken into account when considering allocation of IP between the water companies supporting the fund and third parties, and any

level of royalty return.

We therefore believe that different arrangements are needed for different types of IP likely to be created by a project and that a small number of template agreements should be put in place. Academic institutions use [four model agreements](#) proposed by the Intellectual Property Office (known as Lambert Agreements), to provide the basis for collaborative projects and IP sharing. Whilst these agreements are not appropriate for this competition as they stand, some of the principles behind them could be useful in framing different projects and the considerations that could be made when deciding which type of IP management might be most appropriate for a particular project.

As ever there is a balance to be struck between being totally flexible and creating significant burden in assessing proposals, with being rigid and stifling innovation. By outlining outcomes to be achieved upfront, Ofwat can place the responsibility for demonstrating that the alternative arrangements meet the desired outcomes on the project's proposer. The independent organisation and Ofwat can then consider the merits of these proposals.

Q2: What alternative arrangements should we be considering for IPR/ royalties?

We feel the approach to royalties may need to differ depending on whether a project is being undertaken solely by the water companies or with a technology provider as well as the type of innovation being undertaken.

Projects which only involve water companies

For projects focused on large scale roll-out or testing of current technologies, where the main type of IP generated is likely to be knowhow, it is difficult to see how the knowledge gained could be marketised to generate new income streams or profit that would result in royalty payments. The primary way customers will benefit from this type of activity is through the efficiency gains made for those projects which realise their potential.

Where projects involving just water companies do generate IP resulting in a potential product or solution that can be marketised, royalty payments could be managed as companies have the knowledge of the sale and use of the IP generated. In exploiting these technologies, consideration will need to be made about the appropriate vehicle to use to optimise the return to customers. This includes the creation of spin-out companies to further develop technologies and attract investment from other sources for product development.

Royalty payments from projects with other organisations

As with IP management, projects carried out in collaboration with supply chain organisations will need more complex arrangements around royalty payments. Collaborating organisations will need to see a fair return to their own shareholders to enable them to continue to operate profitably. If the technologies developed are specific to the water sector, the UK market for these technologies is likely to be just those organisations who are also seeking a royalty return. This may result in a conflict of interest regarding pricing and have an impact on the market in terms of other technologies being developed to meet the same need.

We would advocate a revolving fund model that will enable the legacy of the fund to continue beyond the current proposed period to be adopted. This would also mitigate the risks around the potential conflict of interest concerning the primary customer of technology also receiving a direct return from the sale of that technology.

Q3: Do you agree with the principle that data generated through the innovation competition should be open by default?

We believe it is important to draw a distinction between treating data generated by the innovation funding as 'open data' and industry data more broadly.

Anglian Water is supportive of the principles of open data in association with the innovation funding, but must emphasise that the term 'open data' can be overly simplistic and potentially misleading. We believe the levels of openness of data exists on a spectrum, similar to how the Open Data Institute describes. The industry would need to reach an agreed definition of open data before making a commitment to take an open by default stance as there are many downstream effects that would create impact.

We have been developing a central open data strategy within our business over the past 12 months, and feel we have gained significant valuable insight to share with the industry. Underpinning our open data strategy has been data classification and ownership and is complex, but essential for success. This approach to data classification is now being established at a national level and we would urge Ofwat to consider this in the development of its position.

We think a whole spectrum approach should be taken towards data, and focus given to moving data from the closed towards the open end, and examining how it could benefit the industry. Our business recognises four high level categories of data as detailed below, which we would be happy to explore in more detail at a later stage.

1. **Closed (need to know):** Data sets shared within Anglian Water only as a result of our obligation to protect it.
2. **Shared (external to specific stakeholders, b2b):** Data sets shared with specific partners of Anglian Water (e.g. contractors and suppliers) to analyse and drive action against outcomes. For example, sharing pressure data with noise logger suppliers to drive intelligent analytics.
3. **Shared (external with customer consent):** Data sets which Anglian Water holds and can release for the benefit of the customer, but only with their permission or instruction to do so. As an example, when you cycle and use the Strava app, you can view that data on a Garmin device. The data is collected on the customer's behalf by Strava but shared with Garmin for the customer to then understand, resulting in a more customisable experience. However, this is only possible with the customer's consent to do so.
4. **Shared (Public):** Data sets shared openly for anyone to access and use in any way. For example, annual reports or regulatory water quality data.

We believe all data should be able to fit within a matrix for openness, spanning from closed to shared and there should be a method developed for positioning data within it. Developing this for the industry could indeed be a powerful driver for innovation. However, alongside this should be an appropriate method to share data, offering the necessary level of understanding to manage risks introduced by this movement in position.

We would recommend considering the risks associated with sharing data through an ‘open by default’ stance or indeed moving along the spectrum. For each data set held by water companies, the risks increase for each step taken towards open. For example, consider the issues which could arise through sharing data with organisations who come under different regulation. If, in pursuit of driving innovation, a water company shares its strategic water main location data with a local authority, this sharing of data could spark a whole range of opportunities to better serve its local communities. However, local authorities are subject to freedom of information acts and therefore could be made to release that data if a request was made. Without restrictions in place, that data could find its way into the public domain and put the public water supply at risk.

We therefore recommend that a serious consideration is given to how we define open data, how we classify data and how we share it throughout the competition, regardless of whether that data is generated through the competition or not.

Q4: Do you agree with our proposed approach and that we should consider alternative arrangements beyond company contributions?

We are supportive of the approach outlined in the consultation and believe a very broad definition of contribution should be considered. An example could be companies using existing contacts and agreements to leverage additional funding for innovative projects.

Anglian Water is the only UK water company who has a membership with WaterStart and can secure funding contributions towards projects. As well as access to a global innovators and innovation, WaterStart can contribute up to 20% of project costs. We would be willing to leverage this partnership to support projects from the innovation fund.

We are keen to be able to demonstrate that our organisation and shareholders support this approach and that we are sharing the risk of innovation appropriately and fairly with customers. We would be open to discussing this with Ofwat. Some areas would consider representing a contribution beyond simply project funding including offering discounted staff time, a signed letter of commitment from our board and some potential gifting of IP as a starting point.

We would be grateful for more clarity regarding the funding of bid preparation costs. Using Ofgem’s Network Innovation Competition¹ as an example indicates approximately 5% or £175K maximum per annum could be an appropriate level of funding for bid preparation costs. All eligible costs need to be considered and we need to ensure parity across proposals. Providing funding for bid costs would ensure a wide range of transformational projects are brought forward, not ‘safe bets’.

Q5: Do you agree that a guideline minimum company contribution of 10% is appropriate in this context?

¹ See paragraph 4.10 of Ofgem’s Network Innovation Competition governance document <https://www.ofgem.gov.uk/ofgem-publications/119230>

We are wholly supportive of a guideline company contribution to projects resulting from the competition. The form of this contribution should be flexible and assessed on a case-by-case basis. We believe a flexible contribution to project costs would, for example, constitute the provision of staff resources. This contribution could take many forms.

To be truly transformative, we will need to be flexible on the contributions made by water companies and partners involved in the project. It's possible that a contribution larger than 10% from a water company would suggest that the projects could be considered business as usual activity.

We feel more clarity is needed on how fair contribution costs are reached when multiple water companies and or supply chain are working together.

Our preference would be to provide commitment to projects in the form of resource allocation, to ensure individuals from the company are deeply embedded in the project and integral to its direction and success.

We believe that Ofwat could consider adopting the successful model used by Ofgem to incentivise participation and focused project management, at least in the early years of the competition.² This could be used where a company receives its contribution back on successful delivery of a project against pre-agreed criteria. This would further align incentives so that companies go above and beyond to ensure projects are successfully delivered.

Q6: Do you agree with the overarching approach we set out here?

For a project to be transformative it needs to involve components we don't currently understand or use at scale. Typically where there is still a requirement for external funding for delivery of a solution, the project is either not financially sustainable or there are outstanding risks. A way of capturing roll-out potential could be to include it in project periodic or final reporting requirements, where the lead company undertakes an assessment of the feasibility of roll-out towards the end of the project.

For projects focused on roll out and implementation, perhaps sacrificing an element of transformation in place of better understood offerings with a more predictable impact on customers is worth considering. The need to understand a solution and its market offering is still valid, and often it is finding this mature understanding which limits innovation in the industry.

In both examples, the use of Commercial Readiness Level (CRL) indicators should be employed. We believe this understanding can accelerate our industry's pace of innovation forward. Anglian Water has benefitted from growing this understanding through its Shop Window initiative, a real geography in the town of Newmarket which aims to facilitate the development of innovation through technology, process and people.

² See section three of Ofgem's Low Carbon Networks Fund governance document:

[https://www.ofgem.gov.uk/sites/default/files/docs/2015/04/lcnf_gov_doc_v7 - final_clean_0.pdf](https://www.ofgem.gov.uk/sites/default/files/docs/2015/04/lcnf_gov_doc_v7_-_final_clean_0.pdf)

Innovation Shop Window case study

The Shop Window has been operating since 2015 and its success is largely down to its ability to bring together solutions providers, academia and industry professionals within a real-world environment. One example of this is our work with Syrinix, a company transforming water utilities' ability to manage water, time and resource scarcity through its cutting-edge technology, data collection and insight tools.

Syrinix entered the market before the Shop Window launched. Anglian Water was one of the project research partners late in AMP4 which led to the spinning out of the company from the University of East Anglia. Its pressure monitors held a high TRL but identifying its place in the market was difficult and its USP was unclear.

Syrinix had access to an entire water distribution system and was able to openly outline its development roadmap, and Anglian Water was able to clearly articulate its challenges and provide immediate feedback to the team. Over two years, Syrinix was able to develop its technology alongside the service it enabled. It developed its ability to deploy its technology by answering the questions which really mattered to the industry.

Syrinix was able to move its CRL from likely a 2 (when its TRL was an 8/9) through to 6, 7 and even touching into 8. It could repeat the methodology for proving its offering developed in the Shop Window and implement it with most UK water companies in 2018 and has repeated this in the USA and Australian markets.

In reference to Ofwat's point on developing solutions together, pooling facilities and testing solutions, we would openly offer our Shop Window platform to the industry. Using this way of working through the Shop Window and fund could unlock huge opportunity for the industry. Through the sharing of staff and bringing people into the area to work on projects, we could truly build the water company of the future together. Through staff exchanges learning can be deeply embedded and then more easily implemented in respective businesses. This includes involvement of staff from the relevant regulators, Ofwat, the Environment Agency and the Drinking Water Inspectorate.

There are many potential opportunities we could unlock for customers with the direct engagement of Ofwat staff in the development of the Shop Window. This could form part of the proposed 'one stop shop'. Not only could we develop the water company of the future, but the industry and the future generation of leaders who will guide it.

We agree that we should maintain flexibility throughout rather than risking stifling innovation by over-defining the criteria. This presents the risk of companies struggling to efficiently and responsibly resource activities around the innovation competition if that activity is continually changing throughout the AMP. To avoid this, we suggest that consideration towards covering the costs of activities associated primarily with the implementation of the innovation funding and competition is given.

Our view is that the fund must be focused on specific, identified opportunities for accelerating, stimulating and improving efficiency of innovation activities. Further consideration must be made on the niche it will exploit in the existing funding and supporting environment and how

it interacts with these activities. There is a risk that it is too thinly spread and competes with existing solutions instead of aligning and complimenting.

Q7: What are your views on introducing separate, proportionate, arrangements for small-scale projects? How might we define small-scale projects for the purposes of the innovation competition?

We are fully supportive of proportionate arrangements for small-scale projects, as the effort and investment required to access the funding must still be attractive relative to the size of the funding required. Existing arrangements such as Ofgem's Network Innovation Allowance could be considered as a starting point for proportionate arrangements, e.g. self-certification that projects meet funding criteria. This would facilitate quick starting of some projects within this financial year.

Defining small-scale projects creates the potential for conflict. We must be careful not to replace existing funds through the targeted funding of small-scale projects, but it is difficult to see the definition going anywhere else than to focus on the development of technology. In order to address this potential conflict, we would suggest that small-scale funding is aimed towards the application of technology and understanding best fit for the industry. In order to do this, we must consider the innovation in the round - people, process, information and technology, all coming together to drive change. To succeed in this differentiation, we consider the USP of the Ofwat competition and fund to be the close link to water companies. We have seen, through Anglian Water's Water Innovation Network and Shop Window, that when suppliers are able to get focused time from the right water company staff, developments can be accelerated exponentially.

Providing routes into the fund through initiatives like the Water Innovation Network sign posting opportunities and then the Shop Window and its real work location testing and developing offerings, could radically enhance the competition. Opening the Shop Window to the other water companies as part of the competition and developing solutions for application across the industry could be incredibly powerful and efficient. The Shop Window may form part of the centre of excellence and project learning could be shared virtually but as projects would be run in partnership, we would already have representation from water companies across the country through the development and delivery of the work, meaning almost no delays through handover and dissemination of learning. For sharing knowledge further, we could use a similar approach to the collaboration portal in the energy sector.

Q8: Do you agree with our proposal for ensuring roll-out is at the heart of the innovation competition? How might we reward both leaders and fast followers in this space?

For projects where we are considering something truly transformative, we do not believe that it is necessarily feasible to put a plan in place to roll out a solution before fully understanding the solution and its place within the market. However, we recognise that the roll-out of proven innovations is what will unlock consumer benefits.

We agree that for the funding to deliver maximum benefits to customers, some of the proven solutions must be implemented. However, we believe that for true transformational

innovation, it is impossible to have a detailed roll out plan in place before the solution is fully developed and understood. Once delivered and understood, if a further financial incentive is required at that stage to move to roll out and the demand for the solution is not there, the solution may not be viable for application in the water industry in its current form. Therefore, we do not believe the funding should be used to incentivise rollouts. Funding projects to the extent where rollouts can be achieved within the funding of the competition however, may be advisable. Given that the results of these projects will be delivered during the AMP, there may not be scope within the water companies' determinations to then be able to invest in this roll out, unless already in its business plan which would preclude the project being accepted within the fund.

To illustrate this with an example, take benefits mapping with lead and lag measures. Here the goal is to maximise rollouts of successful innovations, resulting in maximum impact for the customer. For the competition, the roll-out of an innovation is a lag measure, once you can measure it you can do little to impact the end goal because the project needs to run its course, then go through a dissemination phase and implementation in other companies.

A lead measure for this example could be the number of projects funded which fall into the 'transformational' category versus the 'incremental'. Based on probability more incremental projects would reach roll-out, which can be measured early in the competition and can be adjusted frequently, hence it is a lead measure.

Another lead measure could be the number of representatives involved in the delivery of projects or the certainty in the plans for knowledge transfer outlined in the project proposals. These are both easily measurable early in the competition and directly correlate to the likelihood of a project being picked up by other companies if successful, once delivered.

Therefore whilst we agree that roll-outs of innovation through the competition should be central to whether it is deemed a success or not, we believe its incentivisation could be considered further at a later stage with the priority of setting up and trialling the funding streams in the short term.

We propose that the Shop Window could play a considerable role within this idea if there is sector appetite and if it can be supported to evolve in the competition and fund. Actively engaging staff from other water companies, academia and regulation in the delivery of projects and the development of what a water company of the future could look like has the potential to be truly transformational. Through this embedded working we can create opportunities to progress the industry, not only through the subject matter of the projects developed, but the development of the people who make up the industry and the systems which govern its existence.

This removes a leader versus fast follower issue as the area becomes one for everyone. Even if only to create a space for smaller companies who do not have the ability to have their own areas to extensively test, this idea could be exceptionally powerful. With full commitment from the industry behind this, we could truly transform the role of water companies within society.

A good example of this is the pioneering work we have developed using virtual reality in our employee learning modules. We R makes use of 360° images, videos, CGI features and

multiple-choice questions to deliver targeted training across various subjects, enhancing engagement and more importantly, increasing retention rates on critical subjects like health and safety. The use of VR training on these topics is now business-as-usual for us. The long-term goal is to be able to collaborate with other utilities, retail and construction companies. This has been demonstrated in the way the software and modules have been designed to use across all industries, however we currently lack a central mechanism to do so.

Q9: What practical arrangements should we introduce to ensure adequate ring-fencing of the innovation funding?

We largely agree with the three-step process for ring-fencing funding detailed within the consultation. It would ensure the reallocation of money is streamlined and give full assurance to utilities that the same financial regulation is being exercised across the board. It could also ensure that key stage gates, such as knowledge transfer, are formally adhered to prior to the release of final funding.

We note that some securitised companies may have limits on the number of bank accounts they can operate under their financial covenants. If those companies are inadvertently excluded from accessing project funding, the potential for transformational innovation that benefits all customers could be constrained. From a practical standpoint, akin to grant applications administered by the EU, we would not see the need nor requirement for the funding to be held in a separate bank account as accountability for the funds can be demonstrated in other ways. For example, where funds are required to be separately identified, they can be held separately in balance sheet control accounts and managed within an enterprise management system.

Below are two examples where we hold separate balance sheet accounts to hold advance payments.

- Developer Services contribution - these are contributions from a developer in advance of AWS completing a scheme (usually growth). We hold this contribution and then release it against the scheme as it is completed.
- Customer in advance payments. We hold a separate balance sheet account to show payments in advance our customers have made towards their future water bill. We hold this amount and release it as appropriate once the customer is invoiced for their water.

The outcome we should be seeking to achieve is that all project related expenditure is transparently recorded and available for scrutiny. It is possible to achieve this outcome through budget reporting without using a separate bank account. We believe Ofwat and the funding organisation should consider alternate arrangements that deliver the same customer outcome, transparency of project expenditure, should be considered on a case by case basis.

We have some reservations about the payment schedule. The allowable revenue increase is scheduled to be collected from customers as part of regular payments, and this is likely to be across the full year. If the transfer of the increase is paid during the year to the fund, then there is a negative working capital impact to consider. We propose two payment tranches (end of Q2 and close of Q4) would partially alleviate this in the first year. We believe this is

reasonable as the full funding may not be allocated in this trial year and funded projects will take some time to mobilise.

The consultation touches on bad debt of customers regarding payment schedules but does not propose provisions for this implication. Since it has been suggested that a recession is looming, we believe this should be further considered by Ofwat.

Q10: Do you think the proposed innovation challenge approach will help better enable partnerships and collaboration between companies and third-parties, in particular smaller innovators? Are there alternative approaches we should be considering? How can we make sure this approach works in practice?

We agree that the Innovation in Water Challenge does have the potential to attract new market players and disruptors who do not usually operate in the sector. It could also provide SMEs with better access to water companies, resulting in increased awareness of new technology development.

To enable this to work there will need to be investment in the marketing of the challenge to organisations not currently looking to sell to the water industry and enabling them to gain an understanding of the needs of the sector. For example, Innovate East, a collaborative innovation event run by Anglian Water and Northumbrian Water Group in 2019, was able to attract a number of stakeholders from outside the sector and expose them to challenges and systems within the water industry.

Partnering with organisations such as InnovateUK, or regional business development agencies who work with a wide range of organisations, would support this as many businesses are already engaged with the right groups, and therefore do not need to look for a new communication channel.

IP needs to be particularly carefully considered, especially for SMEs where IP is vital to their commercial success. Thought needs to be given to which organisation is best suited to exploiting IP in the wider sector in the UK and overseas.

The administrative burden on applicants to the fund needs to be proportionate to the funding that is available as this may become a significant barrier to entry for small organisations. Speed of decision making is also important to small businesses and should be taken into account.

We also believe further consideration should be given to the allocation of risk for these projects. If the water companies are held fully liable for successful delivery by the third party, they will likely seek to share these risks with the third party contractually. This could stifle innovation. Ofwat may need to accept more risk from these types of projects, in the expectation of more diverse innovation, than it would from the competition.

An alternative approach could require water companies to regularly seek proposals from third parties that are then considered through the competition. This could remove significant additional admin burden of distinct funding streams. A similar model is used in the electricity Network Innovation Competition with annual calls for ideas.

There is a risk that rather than a collaboration or partnership, this could effectively turn into a procurement exercise, with a more diverse set of suppliers. This could be helped by WaSCs working with new organisations to adapt their product and service to the water sector as exemplified by the Water Innovation Network.

Lastly, we feel we must not lose sight of the diversity of organisations we need to engage to make the innovation competition be as successful as possible. While we appreciate the majority bidding into the Innovation in Water Challenge will be suppliers, we must ensure organisations such as the Rivers Trust, Water Resources East and the Anglian Centre for Water Studies will be actively involved in helping to transform our sector through transformational innovation, not just product focused solutions.

Q11: Do you agree with our proposed approach to returning funds to customers? Are there any other circumstances, not considered here, under which we might consider returning funding to customers?

We believe the decision to adjust funding where it has been misspent and or projects have not complied with conditions, is a reasonable one. Any funds to be returned to customers should be made available, in full, to the water companies by the administering body.

Q12: Do you agree with our proposed approach for managing interactions with the price review?

We believe there is huge potential to be unlocked through exploring transformational change by providing the opportunity to change services offered in a controlled manner and understanding their impact. An example of this could be the implementation of innovative tariffs. Whilst we understand the proposal that specifics can be discussed at the one stop shop, we believe it premature to rule out any derogations from performance commitments and licence requirements (e.g. Condition E for tariff trials) at this stage. As such we propose that this not be ruled out at the outset, but that individual requests for derogations are considered on a project by project basis.

Q13: Do you agree with our proposed amendments to the principles? Are any further amendments to the principles required to reflect our approach to outstanding policy issues outlined in this document?

We are largely supportive of the amendments to the principles outlined, but we have some suggested amendments and points we feel could do with further clarification.

Principle 1

We believe this could evolve to recognise that innovations can be opportunity led at times, and not everything can be categorised as a challenge. We are always exploring to make improvements, but we don't know what we don't know and so there will be times when we need to classify innovations as opportunities rather than planned challenges.

Principle 2

We would appreciate more clarification of what is meant when we refer to the 'innovation competition'. Is this all funding or just the main competition?

Principle 3

The roll out of successful innovations across the sector will be a strategic decision taken by the water company operating in a specific area. Local factors and previous investment decisions will influence the starting point of each company and will mean the opportunity represented by an innovation may not be uniform across the sector.

We believe that effective resourcing and industry commitment to the enabling activities (principally the proposed centre of excellence), will ensure we maximise knowledge transfer. This will enable opportunities for roll out for all projects delivered using the proposed innovation funding, while providing a mechanism to share learning from previous innovation activities and focus future investment.

Principle 5

A definition of 'combined company contribution' is necessary here. Assuming it refers to all contributions to the project outside of the allocation from the fund, 10% appears appropriate but must be flexible and the makeup of total project funding needs to be clarified.

Principle 7

Again, we believe that the proposed Centre of Excellence is a key enabler to providing transparency and a common approach across all projects. We believe that having Ofwat and the appointed fund administrator as key stakeholders of the Centre of Excellence will help to ensure that it is resourced and deployed with greatest impact.

Q14: Do you agree with our proposed focus, major strategic themes and overall approach for the competition?

The consultation suggests some promising aspects and we largely agree with the overall approach. However, rather than run the competition in fixed-period calls relating to specific themes, we would like to see an 'always open' approach applied. Being definitive on themes now could risk 'picking winners' prematurely. We feel this will further separate the competition from existing planned innovation activities and will enable the industry to be more open to emerging opportunities. Ofwat could reserve the right to be more specific about themes in the future if it believes important opportunities are being missed.

In addition to the restriction due to timing, we believe that restricting projects to specific themes could potentially, but significantly, limit the potential for transformation. We want to foster and support opportunities that transform our industry wherever they occur rather than prescribe the areas of innovation that the sector should be open to. In prescribing themes, we also run the risk of missing multi benefit projects as there might not be an obvious 'best fit'. We recognise the need to highlight areas we believe offer the biggest opportunities for innovation and we think that the sector wide innovation strategy will provide more specific guidance on the outcomes and themes that the sector it is committed to. Some areas such as

people, behaviour change and water poverty are clearly outlined in the sector wide innovation strategy but are not referenced in the consultation.

A potential issue for securitised companies is establishing joint ventures and limits on collaborative expenditure. This is another area where flexibility may be required to ensure the broadest participation in the innovation funds. An example solution would be establishing a subsidiary company to run the project on behalf of the securitised water company. This type of arrangement should not be prohibited if the outcomes of protecting customer interests can be demonstrated. This may be an area that merits further detailed discussions.

We would like to see open access to all projects to all interested companies rather than projects being run and excluding some companies (and therefore the customers of that company). We believe that establishing a mechanism for this as an enabling activity should be a key piece of work in the pilot year.

Q15: What is the appropriate split of available funding between the Innovation in Water Challenge, the main competition and enabling activities?

Answered below in question 16.

Q16: What are your views on the feasibility of running all three types of activities in the pilot year, and on the proposed timings in Annex 3?

We agree that the pilot year focus should be weighted towards the 'enabling activities' and the 'Innovation in Water Challenge', while utilities consider what proposals would be truly transformational. Our longer-term view is that, once established, the Innovation in Water Challenge and the enabling activity should require minimal funding, or be self-sustaining, otherwise they will serve no benefit post AMP7, unlike projects that would have been funded through the main competition. We further suggest that the overheads of administering the Innovation in Water Challenge, the main competition and the enabling activities should be at most 5% of the total fund based on our experience of running the WIN and Ofgem's costs for running its innovation funds. Later in the AMP when the set up phase is complete, we would expect this to be much lower.

We believe that the most funding should be allocated to the biggest opportunity area with the least amount of alternative support. The areas of biggest opportunity and highest potential benefit for customers may only become visible once proposals are put forward and we must remain flexible in funding from each channel to ensure there is a balanced portfolio of projects established within the pilot year.

We feel the timeframe is ambitious and that it is important not to underestimate the time needed to effectively canvas ideas and develop compliant bids. Resourcing needs to be considered and informed to allow companies and suppliers to actively participate. There are some areas of work, such as behaviour change, which we feel are extremely important and should be considered a key part of the programme of work. Due to the significant amount of work the sector has already completed around this subject, we would suggest this could be an early focus of our collective efforts.

If some types of activity are run later (and particularly the main competition) there may not be time to realise the benefits this AMP (although that is going to be a challenge for all projects), but this needs to be balanced by the need for time to get processes sorted and promote the opportunities more widely. This is particularly important for the innovation in water challenge if organisations from other sectors are going to engage with the fund.

Lastly, is it important to consider communicating calls for bids at the same time of year to allow for planning, or that the fund is always available to be bid into (i.e. not set call deadlines). This might be more appropriate for the innovation in water challenge.

Q17: Do you agree with our proposed approach to key implementation considerations outlined here?

From identification of a project to full delivery, we believe there are a few extra considerations to be included in the principles and final guidelines. We outline these below. We need to be clear whether the fund is going to support the cost of the administration of the competition. We believe there may be an advisory role for industry in the tendering process for the organisation who will administer the finding.

To enable rapid development of projects we need to have clear decision-making and awarding guidelines to ensure the process is transparent and fair for submissions. This includes having a diverse panel of experts involved in the process - experience drawn from being part of a research council suggests that funding panels aren't easy to run.

We believe that the arrangements should have the ability for the same project to be progressed through different themes e.g. Innovation in Water challenge funds small but relatively high-risk projects. If these prove successful, they can bid into the main competition.

Finally, and fundamentally, we need to be able to fail, we need to be able to learn and this should be applied to all future activity in this area. A collective definition of failure also needs to be agreed to ensure that a project isn't considered a defeat just because it hasn't delivered the projected outcomes.