

Date: 24 June 2020

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Dear Sir/Madam

INNOVATION FUNDING AND COMPETITION: FURTHER CONSULTATION ON DESIGN AND IMPLEMENTATION

We welcome the opportunity to respond to this additional consultation on what is a vitally important topic for the sector.

Overall, we continue to be supportive of the approach, but we believe that the process for this fund should be as simple as possible, transparent and fair and that the framework in which it operates is cost effective and efficient. The greater the level of control and constraints the less likely the underlying reason why one innovates will be achieved in practice and hence whatever the final process, it should seek where possible to mimic a truly competitive market – including the funding of projects that may fail without penalty.

In our response to the September 2019 consultation “Ofwat’s Emerging Strategy: Driving Transformational Innovation in the Sector”, we highlighted areas that we believed needed further consideration to get the best benefit for customers. This consultation partly addresses some of those areas but there are still some points raised that haven’t been addressed, which we have summarised below alongside some additional areas for further consideration.

Customer Equity and Risk Sharing

Whilst we acknowledge the efforts undertaken to ensure that customer equity is addressed through the prioritisation of roll-out and enabling the uptake of outputs and results of the projects funded by the innovation competition, concerns remain that the practicalities of this are yet to be defined and we would welcome the opportunity, as expressed previously, to work together to develop the approach that adequately protects and is equitable to all customers.

With reference to our previous concerns regarding affordability, the introduction of “risk-sharing” to the innovation competition could be seen as a further contribution, above and beyond what customers will already be contributing to the pot to fund successful projects. Not only could this inhibit uptake of the fund from water companies who will have already contributed but this has other potentially unintended impacts (detailed in the Appendix, question 5) and further highlights

the need to consult more widely with customers, or customer representative bodies, in order to seek assurances that there is support for this position.

Importance of efficient project delivery

As we stated in our previous consultation response there are many commonalities between the proposals set out in the consultation with the Research England bid process and the work we have already undertaken with the University of Exeter in developing our Innovation and Resilience Centre (CREWW).

We were also pleased to be able to share the proposals in person with John Russell on 31 January and would be happy to continue the discussion regarding the positioning of CREWW in the development of the administration and governance of the fund and how we can support efficiencies in cost, process (assessment, monitoring and roll-out) and resource that will ultimately drive quality and impact for all customers.

Removing wider barriers to innovation

We would welcome further discussions and the opportunity to examine more closely the barriers to innovation in relation to the sector's regulatory framework and at what point these barriers occur in the regime. We feel there is room for this work to happen were it referenced more explicitly in the principles of the innovation competition and even presented as a theme, as part of the challenge-based approach of the competition, giving rise to projects that actively broach this subject and present co-designed and co-created solutions to any barriers – perceived or real – that inhibit innovation from a regulatory perspective.

We remain committed to supporting the competition, its ambition, principles, themes and the overarching sector innovation strategy but would welcome a more clearly articulated view as to how the competition will go above and beyond what companies would be able to achieve if cultural and regulatory barriers were addressed and freedom were granted to spend the contribution they will make to the competition in a more bottom up way, locally, with the input from customers and partners.

Open Data

As a progressive organisation we value the importance of developing a sector-wide approach to Open Data and will wholeheartedly contribute to and collaborate with others in this process. The benefits of opening data, as part of the innovation value chain, have been seen widely in other sectors and represent significant opportunities for the water sector in terms of how we maintain our assets now and in the future, how we interact with customers and how we forecast and analyse trends in external pressures on our system – societal, environmental etc.

The innovation competition will be an important step in testing and trialling solutions in this field and we urge Ofwat and others inside and outside of the sector to use this opportunity to find the balance between Open Data that enables innovation and respects the legal requirements and conventions that protect those who generate the data as well as its ethical processing, control and use.

Roll-out

As identified in our consultation response in September, innovation in the water sector can take time and can span consecutive AMPs. With a clear focus on roll-out, technologies that are more mature in terms of readiness will likely be favoured and we feel there is still a lack of definition and clear thought as regards the ability of multiple Water Companies to adopt technologies/systems/processes unless there is greater standardisation and/or a convergence of strategic priorities among the sector to enable project outputs and outcomes to be rolled out.

As a cautionary note, it will be important to balance the prioritisation of more mature innovations with the need to incubate those that are less-developed and potentially more disruptive and/or beneficial in the longer-term. We therefore consider this should not be a deciding factor on project as it essentially could stifle innovation as only select deliverable projects.

Maximising impact and effective governance of the innovation competition

The overall governance and administration of the innovation competition and its enabling activities is essential, and we recommend a clear, open and transparent process in selecting the organisation(s) that will be appointed to this role. Key considerations that will build trust in this process are the suitability, credibility, track-record and independence of the organisation chosen and we urge that they are inclusive and representative of the wider sector, the customer voice and enfranchise the views of a wide range of stakeholders through the appointment of the independent expert panel that will assist them in the assessment of applications to the competition.

The cost of this organisation(s)'s role in the governance and administration process needs to be tightly controlled in order to maximise the impact of the fund, given that the current proposal is that it will be funded from the competition fund itself.

We feel the timeline for the selection of this body and indeed the overarching timeline for the roll-out of the innovation competition is ambitious, especially given the current climate and restrictions imposed by COVID-19. It is important to not rush the design of the competition and a focus on the enabling activities that will support the principles of the competition and collaboration that will lead to project applications in the first year seems like a sensible approach. We have provided more detail and insight to this in our response to question 15.

Looking forward

SWW welcomes the ambition of the sector, supported by the competition and Ofwat, to enable closer collaborative working between companies, academia, the supply chain and innovators. We also welcome the opportunities to share and capitalise on best practice that this fund enables, building on innovations that are in and outside of the sector, to reduce duplication of effort and resource and to provide best value for money to customers.

We have included answers to the specific questions raised in the consultation as an Appendix to this letter and welcome the opportunity to discuss with you as appropriate.

We hope that you find our comments helpful. Please contact us if you would like further detail.

Yours faithfully



Question 1: 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.)?

While we understand that it is helpful to have a set of default arrangements for managing IPR and royalties so that companies and third-party innovators understand the general expectations, in practice we believe that bespoke arrangements would be needed in most instances and that participants should be able to reach agreements on a competition-by-competition basis to allow for flexibility. These are some of the factors, not listed in the consultation, which could affect arrangements for IPR:

- whether companies own their background IPR or whether they are licensees and are therefore limited by those existing licensing arrangements;
- the kind of Foreground IPR that might be created, the legal rules around creation and ownership and the process and costs for protecting that IPR (for example comparing copyright with patents);
- the role of third-party innovators, such as universities and businesses, who will have their own strong views as to IPR and may be put off participating in competitions if the default arrangements are not aligned with their academic or commercial interests;
- the potential for Foreground IPR to be deployed in other sectors and for other uses outside the water and wastewater industries;
- practical arrangements and costs necessary for creating, maintaining and exploiting certain IPR (for example the need for a source code escrow account for software);
- whether it might make sense for Foreground IPR to vest in a special purpose vehicle created by the participants in order to best exploit that Foreground IPR.

If the intention is to produce a set of standard legal documents, then we would request the opportunity to comment in detail upon draft documents as they are developed.

Question 2: What alternative arrangements should we be considering for IPR/ royalties?

Our response to question 1 highlights some of the aspects of IPR arrangements that may not have been considered.

We would also propose that in some circumstances a proportion of royalties could be held by the Innovation Competition's administering body and used to fund both the body and future innovation projects to make the competitions self-sustaining.

Question 3: Do you agree with the principle that data generated through the innovation competition should be open by default?

In our view, the first guiding principle should be that the management of data generated through the innovation competition should comply with legal requirements. Such legal requirements would include: security requirements, GDPR requirements applicable to personal data and confidentiality obligations necessary to protect Background IPR and Foreground IPR. Making data generally open should be secondary to these legal requirements. We consider that this approach aligns with the existing obligations of companies under the Environmental Information Regulations 2004 and the exceptions regime that allows companies to withhold disclosure of information.

Putting legal compliance to one side, SWW absolutely recognises the benefits to Open Data and recognises our commitment to the responsible stewardship of data, its provenance and sovereignty in driving innovation that benefits not only our company, but ultimately our customers.

Before adopting a fully Open by Default position we would recommend a sector-wide agreement as to what datasets and data flows could be open, to support innovation among the ecosystem – academia, supply chain (inc. new and disruptive SME), NGOs – within and outside of the Water Sector in the UK. Once this is agreed and a baseline established, we, as a sector, could further build on this and increase the number, breadth and variety of open data sets dependent again on the impact and benefit realised to date and the expected benefit to the further opening of data.

Question 4: Do you agree with our proposed approach and that we should consider alternative arrangements beyond company contributions?

Yes, we consider that company contributions should be looked at broadly so that Background IPR or use of facilities, for example, can be considered as part of a contribution. The contractual arrangements (including in relation to IPR) and funding rules would need to cater for the particular contributions proposed.

We support the enabling of companies to leverage external funds to support the delivery and financing of projects. This would allow the competition to maximise its investment in projects seeing outcomes, results and impact in the widest possible context and range of settings – a multiplier effect. The use of external funds within the competition would naturally lower the contribution a company would have to make and would therefore be an incentive for participation.

We would welcome more clarity on how alternative arrangements can be agreed and at which point in the innovation competition process this will be done.

Question 5: Do you agree that a guideline minimum company contribution of 10% is appropriate in this context?

In part, but there are three issues:

1. This may be better considered on a project by project basis – it remains possible that selected projects could be regionally biased in terms of potential applicability/benefits. That is not to say such projects would not be worth pursuing where significant numbers of customers in some regions would benefit, but a 10% minimum contribution raises the possibility of regional cross subsidy.
2. The 10% contribution is also tied to our concerns, noted in the body of our response, regarding customer equity and affordability. An additional 10% contribution, on top of the initial company contribution to the competition fund could therefore be seen as a “double tax” on customers and would have limited or no support. We understand the need for companies to be 100% bought in to any project they are developing and providing an element of match-funding would further sharpen this focus but it is very unlikely that any applicant will not be supportive of projects coming forward to the competition and therefore the additional 10% contribution is unnecessary. Furthermore, SWW notes that this additional contribution will further increase totex and be borne by customers in future bills and could be argued to be another area of double counting of cost and therefore a double impact on affordability and cost to customers.

3. If the projects have been granted funding then it would seem appropriate that the correct governance has been put in place to ensure the project is appropriate for funding. As such why is additional input needed. A competitive process has been applied and therefore should be sufficient. In addition to the double counting, the inclusion of additional funding seems at odds with a competition?

Question 6: Do you agree with the overarching approach we set out here?

The emphasis of the fund is to promote innovation. To that end, there should be no limit on the type of project that should be considered. That itself stifles innovation. What should be done however, is transparency on the selection process for the projects and why those selected were chosen, and those that were not were rejected.,

As above, part of the central ethos on innovation is that some projects will succeed and others will fail. If one is seeking to mimic a competitive market then this should be allowed to endure here. As such we don't think roll-out itself (see question 8) should be a go/no-go on projects as it will self-select projects. One could take the example of the glue on Post-It notes which was a failed project to market that has since found a market route.

Question 7: 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?

There is an argument that this is not necessary, and projects are assessed on their merit/relevance/impact, regardless of size. Depending on the size of the company and/or organisations in the partnership "a small project" is not easy to define, due to the disparity of operating budgets and investment in innovation etc. across the different companies, as well as the wider supply chain and beyond. A small project also implies little impact and lesser value in monetary and non-monetary and this is not necessarily the case, as a process related innovation, or a project that is predominantly focused on intellectual capital could be relatively low in cost but significant in value.

There needs to be further clarity from Ofwat on the expectation in terms of the appetite to fund pilot/early stage research and innovation vs. the more fully fledged, further developed innovations as they are contradictory to one another and have very different outcomes attached to them.

If a small-scale project approach is adopted it could be for any projects seeking up to £100k funding.

Question 8: 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?

No. While we agree with the emphasis placed on roll-out on innovations, we do have some concerns in relation to incorporating a scalability requirement into the concept.

The scalable roll-out of an innovation is likely to depend upon a number of factors and potential barriers:

- Interoperability and standardisation of processes/systems/products/solutions developed
- Convergence of strategic priorities for companies
- Cost to implement across a breadth of different settings

- Value to customer of roll-out vs. drive to achieve ROI on fund's investment

Where a group of companies produce a joint entry then it can be assumed that all those companies believe they can roll-out the innovation at the end. However, it may be difficult for companies (or Ofwat) to accurately predict whether other companies could roll-out the same innovation with the same level of benefit and cost. In our view, the practical feasibility of roll-out at scale would need to be addressed at the application stage but may always be very speculative.

As stated above, the focus on roll-out essentially could self-select true innovation.

Waving or reimbursing the 10% contribution to project match-funding could be a practical incentive to rewarding innovation leaders in any project, but as above, this 10% contribution seems at odds with other principles. If taken forward, it would be useful to define what a leader looks like in this space, as impact of the innovations will not necessarily bear out until after the competition has ended, potentially being seen post 2025 in AMP 8. If this is more of a longitudinal process and participants were happy that they may not see a reward/return for their "leader status" until further down the line then a reimbursement or waving of match funding for future applications, based on their initial investment and eventual impact of any approved project could be a mechanism.

It is difficult to visualise how we might reward innovation followers but facilitating innovation followers is absolutely something the "enabling activities" of the innovation competition, especially the Centre of Excellence and Ofwat's One Stop Shop could play a central role in. By supporting uptake and roll out of innovative solutions (products, processes and services) across a wider group of stakeholders, promoting open source materials, methodologies and tools to implement them a far greater and more equitable impact could be realised by the fund and customers' money that ultimately will invest in any project. Making this scalability question a central point in the project assessment process would ensure more equitable and balanced success from the outcomes and results from a funded project.

Question 9: What practical arrangements should we introduce to ensure adequate ring-fencing of the innovation funding?

In order to ensure adequate ringfencing it may be appropriate to remove the innovation contributions from Botex modelling.

We do not believe that a separate bank account is required and would add undue administrative burden to companies. We would recommend companies maintain detailed project tracking of funding and expenditure and this is used to support and align to the PR19 reconciliation table for Innovation.

We would further recommend that tracking of the project detail to the PR19 table submission is included in procedures performed by companies' external assurance providers.

Question 10: 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 have provided comments in response to questions 1 and 3 in relation to ensuring that the innovation competitions, in general, allow and encourage participation from third party innovators.

Further, for the truly innovative projects, funding should be provided for early stage projects (including funding for proof of concept).

SWW agrees that a challenge-based approach can and will address the fundamental issues in the sector, if coordinated correctly, with proportionate and representative input from a range of stakeholders and voices from the top down and bottom up. We feel it is worthwhile noting that if the balance is tipped too far in favour of the bottom up there will be a lack of strategic sector-based challenges with an overriding operational view, an individual water company biased response and one that potentially could not deliver a transformative outcome and more of a BAU approach. This said, if the challenges are driven too much from the top down the strategic ambition needs to be practicable and (inter)operable meaning that if the challenges are too high level and not realisable by the applicant organisations then the £200M will not be spent and impact will not be achieved at the scale being sought. Applicants need to see themselves and their organisations in the challenges coming out and for this reason, extensive engagement needs to happen to determine:

- What the questions are (content/themes)
- When they will be posed (timelines across the AMP)
- Why these challenges are being posed (issues addressed/outcomes)
- How they will be delivered (principles of the fund and wider sector innovation strategy)

It is clear that the sector needs to work more closely with the supply chain and encouraging this cooperation and partnership through a more “mandated approach” will achieve this, to some extent. With this in mind though, the enabling activities will need to facilitate the emergence of new partnerships and alliance, enabling routes into the sector and the companies. The Centre of Excellence/Water Innovation Centre would be a logical place to start given that it will have the ability to signpost newcomers to needs/gaps/operational challenges and opportunities that face the water sector as well as practical steps to contact key personnel and leads to progress partnership conversations and project ideas.

As a final point in relation to third party innovators, we would be grateful for clarification from Ofwat on its views as to whether any projects involving third party innovators might engage the Utilities Contracts Regulations or the Public Procurement Regulations and, if so, how compliance would be managed.

Question 11: 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 support the return of unused or inappropriately used funds to customers although as a company SWW will endeavour to utilise all funds where possible as ultimately the outcomes from innovation is in the best interests of the industry and customers for the long term.

Question 12: Do you agree with our proposed approach for managing interactions with the price review?

The interaction with ODIs is probably small (as noted by Ofwat), but this depends on the scale of trials and sensitivity of the ODI. Rather than dismissing the potential impact, we would suggest leaving some flexibility by allowing companies to justify (on a case by case basis and with evidence) if a trial has materially impacted an ODI outturn position. This could be done through normal audit processes.

Question 13: 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?

In part.

The position on risk sharing is a valid one, in order to drive up standards in terms of application quality and support for ideas coming from applicants owing to their match funding commitment. It is worth noting that this approach could be seen as a disincentive to some, given that the money for the programme will be invested each year by companies and this could be viewed as our match-funding contribution, without further contribution to each project being necessary.

We feel, very much in line with our previous comments, that more needs to be made of a Customer Equity and Affordability principle, instead of a wider “public value” statement that seeks a return for a wider grouping of citizens and social capital. There needs to be more of a customer voice throughout this process, in order to align and ensure maximum positive impact for those that are seeding the investment in projects funded by the innovation competition.

We do not think that roll-out per se should be a deciding factor. As mentioned above by definition one may find that projects fail – that is its nature of innovation. The projects should instead be judged on their ability to achieve a beneficial outcome.

A further principle could be considered relating to a regulatory framework that acts as an enabler to innovation and the competition will uphold this principle in all stages of its architecture, design and operation.

Question 14: Do you agree with our proposed focus, major strategic themes and overall approach for the competition?

The focus and the themes of the competition are absolutely relevant to a water sector that is fit-for-purpose and drives value, improvement and benefits to society, the economy and the environment, as a Triple Bottom Line. These themes also align closely with the innovation strategy for the UK water sector, which will be driving much of the innovation activity for water companies across the UK.

The Open Data theme will be a challenge to the sector and will need careful consideration as to the sovereignty/provenance/source of the data and therefore how it is used and how it can leverage new insights and discussions with customers, increasing the maturity of the public discourse around water, its usage, scarcity and how we protect this vital resource, as well as how we develop new solutions to improve our services to customers in both the treatment and disposal of water.

We feel there is room for regulation and policy as a specific theme. As described above, this is the main driver of cost to customers, so it seems important to consider ‘what’ we have to do as well as ‘how’ we do it; or the innovations become only about efficiency rather than addressing more fundamental opportunities for upstream change. We note that Ofwat propose to continue looking at the regulatory regime outside of the innovation competition, but quality regulators should also be part of this opportunity.

Question 15: What is the appropriate split of available funding between the Innovation in Water Challenge, the main competition and enabling activities?

It feels proportionate to give the biggest allocation to the Main Competition, given its scope, remit and the support it will provide to enable WOC's and WASC's to realise the transformational innovation being sought, with investment to go above and beyond BAU.

The innovation in water challenge will be the flagship initiative for water companies, engaging with Supply Chain, Academia, NGOs and other stakeholders and whilst it may focus on potentially smaller projects the size of its allocation needs to still be significant if we are to be able to achieve the step change in collaboration and partnership working being sought.

The enabling activities are more difficult to define as there is still little detail in terms of the scope and specification of the work relating to Open Data. This could take many shapes and forms and will need significantly more input from a wide range of stakeholders to design the types of interventions that are relevant and of benefit to the sector and its customers. There is more detail on the scope and ambitions of a Centre of Excellence (water innovation sector) in the sector innovation strategy but costs and mechanisms for implementation and delivery are not understood currently and therefore it is difficult to preempt how much of the fund would need to be allocated to this programme. Based on the above we suggest a split on the following basis:

- main challenge 50-60%
- innovation in water 30-40%
- enabling activities 10-15%.

Given the experimental nature of the fund and a lack of precedent it would be prudent to build in as much flexibility to these nominal splits and enable virements between the different strands of the competition, reacting to demand and benefits, as they emerge.

Question 16: 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?

Running all three will be a challenge, especially given that there are a number of fundamental initial activities and actions to complete before applications can even be invited:

- assimilation and agreement on consultation responses
- design and scoping of Innovation Fund – mechanisms for stakeholder engagement, funding, delivery, assessment, monitoring, evaluation etc
- tendering for and selection of the fund's administering body
- selection of expert panel and assessment criteria for applicants
- define priorities and themes for projects to address in each of the calls
- selection of Centre of Excellence and Water Innovation Centre administering body
- definition of Open Data framework.

The above list is not exhaustive and will all need to be completed in two months' time, during the CV-19 pandemic with most organisations not operating at full capacity.

It feels more sensible to focus on the enabling activities, defining and agreeing their scope and approving a roadmap for implementation of this strand. Alongside this, launching the innovation in water challenge to test, trial and refine a smaller, more insulated version of the bigger competition which would allow for a smoother roll-out of the main competition either later in this financial year, or early into the next. WACS's and WOC's would have more time to develop applications of the size and scale expected for this main element of the competition.

The risk with not running a call of the main competition in this year is that it will be harder to spend the allocation to this element of the fund, having effectively lost one fifth of the time initially foreseen to spend and deliver against this.

Question 17: Do you agree with our proposed approach to key implementation considerations outlined here?

On the basis of the information provided at this stage, we broadly agree with the proposals but would make the following points:

Recovering the costs of administering the innovation funding and competition:

To this point, it could be argued that the biggest impact of the fund could be realised if the costs to manage/administer/govern the fund were not born out of the central innovation fund allocation, providing the maximum amount of money to support projects that will enable positive change through transformational innovation. As architects of the fund, it feels appropriate that Ofwat should bear the majority, if not all of these costs, in the spirit of sharing risk.

Assessment process and decision-making

This approach seems logical, rational and in-line with the approach to the fund. The expert panel will need to be diverse, representative of the sector (and wider relevant sectors) and its customers, knowledgeable across a wide spectrum of innovation and disruptive processes/products/technologies as well as being skilled in assessing impact and value from applications to drive the quality standards and change being sought from the fund. A range of strategic, technical and operational experts would need to be consulted if there are questions/uncertainties the expert panel couldn't address between them and having this mechanism in place would build confidence in the process and the fund more broadly, which is an important factor to its success. If there isn't faith and confidence in this then engagement and trust will erode, limiting uptake and undermining the overall process.

Monitoring

This seems ultimately sensible and proportionate. Not placing an overbearing amount of monitoring workload on companies and other organisations will allow them to focus on delivery and impact of projects, which in turn will drive value for money and benefit for customers. The process could benefit from a system support (portal) which can automatically track and facilitate the process and any interactions of the participants, with steps and processes embedded. This would ultimately and inevitably need to be considered and designed by the body that will administer the fund.