



# Ofwat discussion paper on public value in the water sector

## Southern Water response

### Introduction

Southern Water provides water and wastewater services to 4.7 million people across an area stretching from Margate in Kent to Andover in Hampshire, taking in two national parks, four areas of outstanding natural beauty, 14 rivers (including world-renowned chalk streams) and 83 bathing waters.

Our vision is to deliver a resilient water future for the South East. Our plan for 2020-25 is built around the priorities of our customers and stakeholders and will deliver a huge range of benefits for customers, society and the environment.

We fully support efforts to explore how the sector can deliver even more public value. Southern Water has already taken significant action to create an enabling culture to support delivery of greater public value including:

- renewing our company purpose and values in 2018 (see annex A) - these inform decision making across the business
- Board and senior leadership commitment to company transformation and improved ways of working
- Development of tools to optimise the value we provide, e.g. risk and values process, 6 capitals approach (starting with Natural Capital)
- Tracking culture change through regular Gallup employee engagement surveys

This has helped us deliver significant public value outcomes across a range of activities including our Water for Life Hampshire programme, our Catchment First programme, our Bathing Water Enhancement programme, support for vulnerable customers, community engagement and our T100 water efficiency programme.

Having a clear understanding on Ofwat and wider government expectations on enhanced public value, developing measurable objectives and reflecting these in company ODIs (and simplifying ODIs) will help ensure the sector can deliver the required step-change. Consistent definitions, frameworks and reporting tools will ensure we can clearly communicate progress.

## Scope and ambition

- a) **What factors – outside regulation – impact on water companies’ ability to deliver ‘optimal’ public value outcomes when delivering their core services? What are the constraints to meeting ambitions in this area?**

We have focused on key ‘enablers’ to support the delivery of greater public value and help ensure we are taking a systems based approach to investment decisions. However, new approaches need time to be tested and become fully embedded before becoming business as usual. Resource is also needed to drive change internally and this may be challenging for some companies, particularly in the absence of clear policy/regulatory drivers.

We note Ofwat expects each company to develop their own ‘public value narrative’ and the term may mean different things to different people. **However, having a clear steer on direction of travel, government expectations and a working definition of ‘public value’ would facilitate a quicker cultural shift across the sector.** The sector (including companies, government and regulators) needs clear expectations about the role of water companies in delivering enhanced public value beyond the delivery of core business. This will drive the right decisions, help ensure consistent approaches, support partnership working and deliver outcomes which can be measured across the sector (where appropriate).

Beyond any obvious quick wins, optimising solutions for delivery of greater public value at no (or low) additional cost is likely to require more innovative, systems-based approaches with regulators, customers, and stakeholders. Effective co-creation and co-delivery requires time to build relationships and, while partnership projects can deliver greater overall benefits, they can be more complex and involve more risk than projects we can deliver alone. Organisations we might want to work with such as local environmental groups or community groups, may not have capacity to support the initial co-creation stage which is essential for successful co-delivery later down the line. **Greater tolerance of failure should be explored to encourage more innovative approaches.**

Investment planning cycles may also be out of synch. **Improved alignment of funding cycles should facilitate multi-sector, co-funded approaches.** For example, better coordination of funding within catchments could also provide efficiency gains of around 8%<sup>1</sup>. These efficiency gains could help water companies and public bodies deliver more effectively and efficiently.

- b) **What are the risks in the pursuit of greater public value; and what could companies, and/or Ofwat, do to mitigate these risks?**

We believe there are a number of risks, particularly if ‘public value’ remains ill-defined and expectations unclear:

- Losing customer trust and support if companies are seen to be pursuing public value goals which are outside their core services, without support from customers

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<sup>1</sup> Catchment's if you can – making the most of England's annual catchment spending, Indepen report for Southern Water, South West Water and Wessex Water

- Attempting to deliver a large range of public value goals could weaken overall impact
- Delivering best value rather than lowest cost could increase customer bills. If best value is supported by customers, it's not clear whether this would be supported through the price review process.

These could be mitigated by clear government expectations for the sector (reflected in regulation), alongside continued engagement with customers on expectations/priorities.

- c) In pursuit of better public outcomes, to what extent should companies focus on an enabling culture that drives public value holistically; versus a more discrete, targeted approach?

An integrated approach, embedded in company decision making and processes, should enable companies to identify what's important to customers and stakeholders, and design approaches centred on those priorities. Certain public value objectives may be delivered more effectively at scale via company/industry wide action (e.g. water sector Public Interest Commitments), whereas others may require a locally targeted approach.

Public value outcomes need to be measurable and reportable in order to be able to demonstrate progress. This is particularly true where delivering public value involves investment over and above the lowest cost solution.

## Incentives and barriers

- d) How does the regulatory framework contribute to, or limit, companies' ability to deliver better public value outcomes?


Companies can already deliver solutions which optimise public value outcomes if no discretionary investment is required. However, while public value can be delivered without additional cost in some instances, it is undoubtedly the case that additional discretionary investment – beyond the least cost solution to delivering core services - is necessary in many cases.

A 'Best Value' approach is promoted by the Environment Agency in the National Framework for Water Resources and its (draft) Water Resources Planning Guideline. WRSE is currently consulting on its approach for developing a 'Best Value' plan<sup>2</sup>. We are following Defra/EA guidance for Drainage and Wastewater Management Plans (DWMPs) to co-create plans with partner organisations, ensure they consider the potential for collaboration and how collaboration could achieve best value for the economy, society and the environment over the long-term.

However, Ofwat has not historically taken wider public value into account as part of its periodic review process. This discourages the inclusion of schemes which deliver enhanced public value but are not least cost solutions in company business plans.

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<sup>2</sup> <https://www.wrse.org.uk/news/news-posts/2021-1/february/help-us-create-a-best-value-regional-plan>



***Where there is customer support for delivery of benefits that accrue to society as a whole, rather than just bill payers, Ofwat should take a flexible approach to setting cost allowances. Where additional funding is provided, the benefits need to be measurable and reportable.***

Ofwat's price review regime supports the delivery of mandatory investment, such as the WINEP programme, which already delivers a range of public value outcomes. Our ability to deliver WINEP funded improvements using a catchment based approach which would deliver enhanced public value has been restricted by the Environment Agency due to our Environmental Performance Assessment rating. However, there is disconnect between the metrics that make up the EPA (for example - pollution and wastewater compliance) and catchment based schemes. ***Where environmental performance needs to improve this should be addressed through underperformance penalties applied by Ofwat, rather than limiting our ability to deliver more nature based solutions.***

Ofwat's Outcome Delivery Incentive (ODI) regime, alongside Environment Agency regulation for innovation and compliance, can influence decision-making towards less innovative solutions which have greater certainty of outcomes and/or shorter timescales for outcome delivery – but less public value outcomes. ***Ofwat should explore greater tolerance of failure where companies are putting in place innovative solutions to meet their targets.***

Ofwat set a large number of performance targets as part of the recent price review – 47 separate metrics for Southern Water. ***Simplifying reporting arrangements by developing fewer, higher level targets should allow greater scope and flexibility in delivering solutions which can optimise public value outcomes.***

- e) What role, if any, should the price review play in encouraging or incentivising companies' delivery of public value?


The price review should help companies deliver what customers, consumers and stakeholders want and expect - both now and in the future. The price review should set clear expectations on the delivery of public value where this is over and above core service delivery. These expectations should reflect government policy and customer views.

The PR24 methodology should set out the approach Ofwat will take to considering solutions which maximise public value where these are not the least cost options. Where there is clear customer support for delivering wider public value, this should be reflected in the outcomes we deliver and, if appropriate, in customer bills. CCGs could also have a role to play in ensuring companies listen to, and act on, customer views on public value.

## **Understanding impact**

- f) What are the markers of progress on public value, both in the context of enabling culture and outcomes?

The sector will need to be able to demonstrate what it is doing differently, and the measurable outcomes as a result of this. A clear set of objectives and measures to demonstrate progress will be essential. Companies are well placed to identify which enablers are needed at company level in order to achieve the desired objectives. However, consistent frameworks and reporting tools will be needed across the sector.



As mentioned earlier, we are exploring a 6 capitals approach, starting with Natural Capital. Incorporating natural and social considerations into our decision-making, monitoring and integrated reporting will help ensure we capture, review and track progress on a wide range of public value outcomes. The 6 capitals approach will also help to align our plans, where appropriate, with the UN Sustainable Development Goals.

We are also working with Water Resources South East to develop criteria and metrics to assess the additional value delivered by different water resources programmes (or set of options) as part of the development of a 'Best Value' regional plan.

**The sector (companies, government and regulators) should work together on a framework for assessing and measuring public value.**

- g) What role, if any, should Ofwat have in monitoring progress? How else can we, customers and other stakeholders be assured that genuine and meaningful progress continues to be made?

Given Ofwat's statutory duties focus on the delivery of core services and protection of consumers, we will be interested to see how the promotion of public value is reflected in the government's Strategic Policy Statement. It will be essential to have a clear steer on government expectations and for the sector to work together to develop an agreed approach and set of metrics that can demonstrate progress to customers and stakeholders. These can then be reflected in ODIs to better align private financial incentives with the delivery of public goods, be reported in company reports and potentially on the Discover Water website.

## Other

- h) Is there anything else Ofwat should be considering in order to meet our objectives on public value?

Public value needs to move from broad concept to a clear description of the value which companies contribute to society that can be measured, and clearly articulated to customers and stakeholders.

## Annex A: Southern Water purpose and values

### OUR VISION

### OUR AMBITION

To create a resilient water future for customers in the South East

### OUR VALUES

### HOW WE DO THINGS FOR OUR CUSTOMERS

**Succeeding together** **Doing the right thing** **Always improving**

### OUR PURPOSE

### WHO WE ARE

To provide water for life to **enhance** health and wellbeing, **protect** and **improve** the environment and **sustain** the economy

**WATER  
for LIFE**

**Southern Water**

Ensuring water for life

