

## **1 What could the water sector look like in 2040, and how can Ofwat and water companies work towards that vision?**

Afonydd Cymru's (AC) vision for the future is that by 2040 water companies will be having a major and **positive** impact on the environment. The current status quo of water company operations and their negative impact on the riverine environment will be a thing of the past. This will require a significant step-change in how water companies operate, how water companies implement solutions and how Ofwat funds water companies to deliver these improvements.

Water companies have made significant strides since privatisation, mainly due to the introduction of stringent environmental legislation, to reduce their impact on the environment. The impact of cumulative investment programmes can be seen at River Basin Management level, where increasingly any negative impacts of water companies on achieving good ecological status has reduced. However, there is much still to be done. Water companies should as a bare minimum ensure that they are fully compliant with the Water Framework Directive by 2027.

Afonydd Cymru supports strong, effective regulation of the water industry, and all other sectors, to ensure adherence to environmental legislation. In the UK, environmental legislation is strong, and even stronger here in Wales. But these laws are only as good as the regulator which enforces them. Due to inadequate resources, Natural Resources Wales has failed to deliver this function as effectively as we would wish. Thus, we propose a fundamental change as to how regulation of the environment is delivered. Wales needs NRW to have regulation as its primary purpose and focus which requires a rethink as to how certain of its current services are delivered. To allow NRW to focus on regulation, we envisage a future model where some of NRW's current non-regulatory services could be better delivered by water companies and eNGO's. How these services are provided and funded are intrinsically linked and should be considered collectively.

Water companies have a pivotal role to play in delivering a green recovery and providing ecosystem services. To do this, water companies need to function and operate in a way that is aligned to these ecosystems which requires the removal of their current silos of water and wastewater operation. Ofwat should support water companies to innovate, to move away from traditional delivery mechanisms and to trial new solutions. This may entail higher risk in terms of compliance and effectiveness. We welcome new legislation in Wales under the Sustainable Management of Natural Resources which supports this type of approach. However, water companies are still constrained by an 'Asset' Management Plan (their focus being on the concrete, manmade asset) and by overcomplicated processes which burden their ability to change, to take risks and to work openly with other sectors. Afonydd Cymru welcomes Welsh Water's change in approach to delivery in AMP7 and our continued discussions regarding partnership delivery. We would strongly support further changes in economic regulation to allow the water sector to have cost-effective delivery, working with eNGO's across the sector.

Finally, we would ask Ofwat to consider further involvement of partnerships and eNGO's in the development of future price reviews. This process should be both inclusive and outcome based. Ofwat needs to support the industry to innovate, to involve partners in this process and to ensure that the water bill payer is fully aware and understands the drivers for change. eNGOs could be actively involved in this process. Few customers understand the full water cycle, the importance of the environment on their doorstep, or how some of their wider ecosystem services could and should be delivered.

## **2 How do we best regulate to help companies to achieve long term goals such as adapting to climate change, reducing leakage, improving water efficiency and delivery of net zero?**

We would urge Ofwat to reconsider its current economic regulation approaches to the water industry. For too long, the water industry has been driven and dominated by a single driver to keep water bills as low as possible. This has driven poor maintenance, cost cutting, short-term solutions and a lack of innovative thinking. Economic regulation of the water industry needs to recognise longer term aims both for the environment and society. It must support water companies to work across wider sectors and provide mechanisms to deliver enhanced operations in a different way. We should be considering the importance of water in terms of all the ecosystem services it provides. That means we can no longer just consider it in terms of a source and a disposal route. It must also be considered in terms of the role it has to play in flood management, supporting habitats and species, recreation, health and well-being to name but a few. Many of these services currently sit outside of a water company's responsibility but to protect and improve ecosystems all its roles need to be considered allowing it to work across sectors and to step out of its traditional services in order for society to effectively manage these issues.

## **3 How do we encourage companies to ensure services are affordable for all, both now and in the longer term ?**

The current mechanism of price reviews and capped water bills needs to be reconsidered. This does not necessarily mean a higher cost to society. Afonydd Cymru believes that there needs to be a fundamental shift change across society in how it views the value of services provided. This not only impacts the water industry and Ofwat but all sectors and industries. Currently, each sector is setting its own price limits (the water bill, the cost of food, energy production) and this drives negative and impacting behaviour in each sector. By 2040, we need to have removed barriers between sectors and we need to consider pricing mechanisms across them.

For example, here in Wales, we currently have huge issues with agricultural pollution. New agricultural legislation will apply more stringent requirements on farmers to farm sustainably by reducing their nutrient application and changing slurry management practices to hopefully help deliver an overall improvement to water quality in Wales' rivers. Afonydd Cymru wholly support this legislation but we also recognise it comes as a cost. The public and retailers also need to recognise this and be willing to pay more for their food. Can society afford this? Yes it can, because if by 2040 we have removed agricultural pollution, water companies will be operating in a significantly improved environment, its costs for operation and treatment would be dramatically reduced and thus a higher price for food would be offset by a lower water bill.

This panacea can only be achieved if current economic markets are re-set. We must recognise water in its natural cycle, we must be aware of its important role and we must invest on this basis. By 2024, payment for ecosystem services must be fully embedded across Wales with recognition of the true cost of water across all sectors. Afonydd Cymru believes water companies and Ofwat have a key role to play in achieving this.

## **4 How can we encourage companies to innovate and to take advantage of technological change to increase productivity, reduce costs and improve resilience, service and the environment?**

By first recognising that current issues may not be solved by a technological change! Since privatisation, this is the traditional water industry approach to fixing problems in the system, requiring carbon intensive, high cost solutions across the industry. It is time for a change. Whilst there will always be a place for a technological improvements, we recommend that Ofwat gives

greater consideration to improving the environment through the delivery of upstream catchment, nature based solutions and by supporting water companies to deliver this way rather than through more traditional delivery mechanisms. Done effectively, this could result in lower costs, improvements in service, resilience and an improved environment.

#### **5 How do we encourage companies to improve service to customers and operational resilience?**

Water companies must continue to be benchmarked against each other to continually drive best practice. Water companies should continue to engage their customers through different media, recognising that not all customers are social media savvy. They should work in partnership with other organisations to deliver messages, identifying stakeholders that can support communications with specific sectors. The best solution to operational resilience is diversification, to ensure that there is not reliance on a single system. The Sustainable Management of Natural Resources provides natural diversification rather than relying on technical and engineering solutions. It is apparent from our work on the ground that the public do not recognise the wider delivery of Dwr Cymru investment to environmental and green benefits, only their role in water and wastewater services. This emphasises the need for good communication, increased education and continuing to raise the profile of the organisation.

#### **6 How can we encourage companies to best take account of customer needs and priorities, while ensuring services are comparable across companies?**

Afonydd Cymru would question why Ofwat is aiming for comparable services across companies? How does this incentivise companies to change behaviours and operate in a different way? Afonydd Cymru would encourage Ofwat to incentivise water companies to achieve more than their counterparts and to recognise that water companies should be rewarded for achieving more. This could underpin innovation and greater performance in the sector.

#### **7 What, if any, could the role of the price review be in encouraging or incentivising companies to better deliver public value?**

See response to Q1 and 3. A more comprehensive evaluation of ecosystem services and their societal value will naturally identify the incentives required.

The current price mechanism does not encourage water companies to innovate or take risks. Penalty systems are applied when water companies take risks and they fail, this does not incentivise the industry to work outside of their traditional comfort zone and with new sectors. Equally, when a water company applies a new approach and is successful, their reward is only recognised for that AMP period. Linked to Q11, if you want water companies to deliver using new approaches, such as nature-based solutions, these may be long-term approaches and water companies should be incentivised over multiple price reviews to deliver these.

#### **8 How do we better use markets to deliver better value to customers and the environment?**

Environmental protection needs to be at the core of the price review. Afonydd Cymru would encourage Ofwat to support water companies and the environmental sector to consider the development of payment for ecosystem services and necessary trading markets to deliver far greater environmental benefit at a lower cost. Currently, we feel much of that work is being done behind closed doors and eNGOs are not being involved in its development and application.

**9 How can we best account for specific issues, circumstances and Government policies/priorities in England and Wales?**

Afonydd Cymru very much welcomes the introduction of an Ofwat office in Wales. The differences and specific circumstances in Wales have long been ignored through price reviews and we hope that this will now receive greater understanding and attention for PR24.

**10 How can we best align the interests of investors with delivering for customers, the environment and society?**

Afonydd Cymru's interest is focussed solely in Wales and on our cross border rivers. In Wales, there is currently a unique operating model in Dŵr Cymru Welsh Water which does not require consideration of the interests of investors. We strongly support this model and would wish to ensure that it continues to deliver the best service for customers in Wales and that Dŵr Cymru Welsh Water is not penalised for operating under such a model.

**11 How do we encourage companies to collaborate and work in partnership with others, such as on nature-based solutions, to better achieve outcomes for customers and the environment?**

Ofwat needs to support water companies to work openly and honestly with new sectors. We need an economic platform that does not drive just traditional engineering solutions and delivery. Water companies should be able to work in partnership with eNGOs to deliver nature-based solutions. To do this, it must be recognised that eNGOs need financial support. It is a huge step change for what is a historically grant funded sector, so even though they might have the knowledge and the expertise, they do not have a core funding structure which would enable them to develop at the speed and to the timescales the water industry needs. Traditional procurement and financial mechanisms are alien to these sectors and Ofwat could play an important role in enabling environmental partnerships to meet a common position for delivery.

Nature-based solutions may not deliver the immediate, time-lined obligation that the current price review mechanism dictates. This will require Ofwat to reconsider the constraints of a 5-year planning cycle.

Afonydd Cymru welcomes the introduction of the Ofwat innovation fund to develop thinking in this area. However, as an eNGO, we consider that the current approach is not conducive to involvement by many of those in the environmental sector who could provide huge insight and delivery in this area. Much greater support is needed to bring eNGOs into this process. Currently, water companies are still waiting for the sector to bring applications and thinking to them to consider rather than trying to develop these ideas in partnership.

**12 How can we simplify the price review while increasing value to customers, the environment and wider society?**

We hope that Afonydd Cymru has provided ideas for this throughout this response. Whilst our strength is not in understanding the economics of the price review, that is exactly the reason we would encourage its simplification. If Ofwat encourages water companies to look outside of their traditional funding and thinking of end of pipe solutions, we strongly believe that value, an improved environment and beneficial societal change could all be achieved.