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**A1.1 Public value in the water sector:
a supporting set of principles.
Detailed summary of responses**

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This is a summary of what companies told us from the questions in our December 2020 discussion paper. The central overarching themes are addressed in the main document.

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?

- A1.2 A number of companies noted that a trusted, two-way customer/stakeholder relationship was key in the delivery of optimal public value outcomes as part of their core services. Two companies set out that they have created a 'Social Contract' by engaging with customers, as they believe success relies on a customer/citizen mandate. There was widespread recognition of the value of partnerships with a wider range of stakeholders, to develop and deliver regional priorities.
- A1.3 A number of responses also raised the need for sector-wide collaboration. Governments, NGOs, companies and communities all have essential roles to play but can sometimes work at cross-purposes rather than in alignment. One company noted that partnerships across sectors are necessary to drive change at pace and scale, recommending that the alignment of priorities of these cross-sector partnerships is crucial for the efficient delivery of public value. Building strong partnerships with environmental groups in the delivery of the WINEP was cited as an example.
- A1.4 Another company flagged the risk that the increased complexity of delivering some public value outcomes in partnership created additional delivery risks compared to projects delivered alone. For example, local environmental or community groups may not have the capacity to support the initial co-creation stage essential for delivery in the long-term.
- A1.5 Some companies raised the need to consider how actions taken by the company are perceived by its stakeholders, alongside other trade-offs and considerations (including environmental, social and economic factors) which all can influence how public value is generated.
- A1.6 The timeframe of company goals has a bearing on public value focus. The Consumer Council for Water (CCW) recognises that the timescales of the return on investments may work against the long-term focus required for public value issues. This sentiment is echoed by several companies, with one proposing a valuation framework to

maximise the benefit for communities and reduce cost in the long-term. As noted in our themes for PR24, assets in the water sector have very long lives, decisions made now will impact the services and bills customers experience in the future. By planning their investments in a long-term context, companies can identify and sequence what actions they need to take and when.

A1.7 One company suggested Ofwat provide a clear steer on the direction of travel, with a statement of government expectations and a working definition of public value to facilitate a quicker cultural shift in the sector. CCW consider that public value may need representation at board level to maintain a culture. Another company noted that that the political climate can sometimes lean towards solving short-term issues, rather than developing solutions for more complex, systemic problems.

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

A1.8 Two companies noted that a public value focus can distract from the optimum delivery of core services. A possible issue cited was the potential for loss of customer trust for completing public value outcomes without an agreed consensus between stakeholders on what those outcomes should be. CCW state companies may be complacent, regarding their current activities as achieving public value rather than challenging themselves. Companies agree that public value should be rooted in the core service, and some companies suggested that the pursuit of wider public value should not have adverse consequences or require a cautious approach for that core delivery.

A1.9 Some companies wanted Ofwat to clarify what public value is, and our expectations, stating Ofwat needs to be clear about its role, and whether it is interested in national or local view (or both).

A1.10 Conversely a number of companies expressed the view that Ofwat should not over-regulate public value to prevent public value becoming a tick-box exercise. One company addressed the risk of public value forming a boilerplate disclosure demonstrating compliance that does little in practice, whilst drawing cynicism of 'greenwash' commitments. Another set out that 'any incentives set for companies should reward the delivery of outcomes and value, not process and plans'.

A1.11 CCW suggested a periodic assessment of companies' board governance and long-term strategic plans to highlight and share good practice. In order to mitigate the risks in the pursuit of public value outcomes one company advocated that Ofwat can monitor what companies do with clear signposting of how priorities have been set, specific action plans and regular, transparent reporting on progress. Others suggested that Ofwat should avoid standardised reporting, comparability and benchmarking for public value at this stage, noting that a number of public value models are currently

being tested in the sector, with this being a regionally differentiated concept which is more about meeting bespoke customer preferences beyond core service and price offerings. One company echoed this in recommending that Ofwat should move to a principles-based approach over rules-based tools.

A1.12 In terms of considering customers and wider stakeholders, three companies addressed the risk of additional cost to customers. One considered the risk that customer bills would be used as a vehicle to collect revenue for investment in creating public value, where it should be delivered through general taxation and wider government actions.

A1.13 Two companies explored how the interests of different stakeholders should be balanced. Both referred to a dialogue with customers and stakeholders to inform decision-making through a well thought out engagement plan. One went further, suggesting that where decisions that generate returns for investors are capable of benefitting a wider range of stakeholders, the 'additional return' should be made available for reinvestment in the business.

A1.14 CCW noted the risk that shareholders' priorities may eclipse public/consumer priorities, so the ring-fence of the regulated businesses from the wider ownership structure is important. They support Ofwat's recent licence changes to reinforce this and would welcome a periodic assessment of how well these protections are helping to keep companies focussed on public value. They also recognised that some companies have or are considering incorporating public value in their articles of association, and suggested that Ofwat should look at how water company licence conditions could be improved to strengthen companies' focus on public value.

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

A1.15 The responses largely supported a space for both an enabling culture and a targeted approach in the pursuit of public value outcomes. However there is recognition that company culture should support and deliver a public value ethos that permeates throughout the business. CCW, and others noted that businesses with long-term public value ambitions should integrate such thinking into their business strategy and decision making process. Examples used included evolving the company purpose, the use of 'capitals frameworks' and social contracts.

A1.16 Two companies observed that a targeted approach cannot be achieved without an enabling culture. They were of the view that such a culture will inform the decision-making process to enable companies to identify what's important to customers and stakeholders to design approaches centred on these priorities. A targeted approach is

easier to engage with stakeholders on, driving accountability through measurable outputs. This reflects commitment, transparency and accountability.

- A1.17 A targeted approach was valued by one company in the context of an enabling culture “It is important that we focus efforts on the most material issues and those that have the greatest relevance for our stakeholders; a more bespoke targeted approach can make the broad notion of public value much more real and grounded to the Company and its stakeholders, particularly if underpinned by authentic engagement”.
- A1.18 Some companies noted that collaboration can lead to more opportunities in the way the sector provides services and can be part of the central strategy. Whilst some illustrated that certain public value objectives can be delivered more effectively at scale with industry wide action (e.g. [Water UK's Public Interest Commitments](#)), others may require a targeted approach.

Incentives and barriers

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

- A1.19 The overarching theme addressed by respondents was how the framework will balance the trade-offs for short-term solutions which are generally incentivised against long-term solutions which may not have the same certainty of outcome but have the potential to deliver greater public value benefits.
- A1.20 Nature-based solutions were the predominant example used. Under the price review totex allowance and ODIs, companies could pursue conventional capital programmes for environmental schemes in order to achieve the outcomes in a timely manner with high certainty, whereas a nature-based solution may be much cheaper and generate additional benefit for the environment and society (e.g. increasing wetlands for phosphorus removal) but could take much longer and carry less certainty of success.
- A1.21 One respondent advocated that if the regulatory framework has the flexibility to encourage companies to trial nature-based solutions, allow these trials to succeed or fail over a period, and promote sharing all lessons learnt. This will incentivise the development of optimal environmental solutions with the best economic value and public value.
- A1.22 Some respondents suggested that the current regulatory framework could limit public value considerations in investment. The current measurement of efficiency of networks does not capture the types of trade-offs captured above. To address this, Ofwat could work with water companies to adapt the regulatory framework to allow the full value of a particular solution to customers to be assessed, particularly for those solutions that would otherwise look inefficient when considered in isolation.

- A1.23 Similarly some respondents regarded the framework as 'too focussed on comparators and incentives' without considering public value contribution. A broader approach by Ofwat is recommended, with light centralised targets to allow companies to hold themselves accountable to new targets and ambitions.
- A1.24 In terms of barriers to public value, the regulatory treatment of the interactions and boundaries between 'regulated' and 'non-regulated' and 'appointed' and 'non-appointed' businesses, including transfer pricing arrangements, were understood to create a constraint for new activities. An example cited related to non-regulated activities such as developing solar arrays on third party land which cannot contribute to a company's price review performance commitments.
- e) What role, if any, should the price review play in encouraging or incentivising companies' delivery of public value?
- A1.25 A number of water companies valued the opportunities presented in the price review as having the potential to encourage positive action on public value. Progress of public value performance could be assessed through various means. One might be to adapt conventional schemes for public benefit (e.g. sustainable drainage systems (SuDS)), with additional costs considered in the price determination process. Secondly Ofwat could ask companies to demonstrate how they will deliver public value over the current AMP. Ofwat could use this to reward and incentivise (e.g. fast track status) companies that demonstrate a track record in achieving benefits for society.
- A1.26 Others noted that there is no reward for companies going beyond their core service to achieve public value outcomes. Beyond the extent to which companies' existing ODIs overlap with the broader delivery of public value, Ofwat's framework neither rewards companies that go out of their way to deliver public value, nor penalises companies that neglect public value concerns. This is worth consideration if there is apathy to 'conducting their core services differently' with no incentives.
- A1.27 Some recommended a framework for outcomes and incentives to provide room for trusted companies to innovate and act with discretion to maximise the opportunity to deliver public value in addition to their core service offering.
- A1.28 Others suggested that the price review should focus on the delivery of outcomes related to the existing regulated parts of public value water companies provide, although they were concerned that an incentives framework would likely discourage innovative approaches. They suggested the price review should keep pace with envisaged future changes to what will be considered core outcomes such as meeting the sector-wide ambition of net zero carbon.
- A1.29 One company made the case that an explicit consideration of public value initiatives, and funding for these through the price control framework, would more strongly

encourage all companies to consider and implement these schemes. Providing greater regulatory certainty would also encourage companies to work together and share learning. As more schemes are delivered, and greater value is captured, then the regulatory framework could become more effective in assessing both the schemes proposed and the benefits that they deliver.

A1.30 Some also discussed the value from performance improvements beyond what customer's value, for example the wider value to society of reducing water supply interruptions. Some are looking to investigate how this value can be considered.

Understanding impact

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

A1.31 The most indicative measure of progress on public value discussed in the responses was the degree of customer, stakeholder and local community satisfaction. CCW's 'Water Matters' tracking research acts as a long-term measure of how well companies are serving their customers, and can track public value over time. The level of customer satisfaction regarding value for money and fairness is lower than what CCW would want it to be. CCW acknowledged that many issues can drive customers' perceptions of these factors, but also recognised the link to public value.

A1.32 Some companies agreed with the view that the degree of trust shown by the public and other stakeholders towards water companies is highly indicative of progress or success. Indicative markers referenced include the presence of projects and programmes that involve multi-agency partnerships; recruitment and retention; diversity in staffing; and sentiment shown through social and conventional media.

A1.33 Others discussed how companies could demonstrate their public value in a way which resonates with all stakeholder priorities, for example, articulating this through existing integrated business reporting such as Severn Trent's Sustainability Report. This was set out by reference to three pillars: taking care of the environment, helping people to thrive and being a company you can trust.

A1.34 Another method used to measure progress in public value related to customer satisfaction is transparency. It was suggested that companies disclose what they do, and why, and explain what value this is generating in a manner that is relevant to the stakeholder group at which it is targeted. Furthermore there was general consensus that companies should disclose information on subjects relevant to as many sector audiences as possible, not what the sector cares most about. A transparent, third-party review of progress towards environmental and social benefit is worth considering to give a targeted focus.

- A1.35 Some companies also stated progress should be publicly reported where appropriate for stakeholders through annual reports, press releases or bespoke reports. They suggest the 'anchor measurement framework' which sets out markers of progress for an organisation to measure its progress against any public value ambitions, whilst comparing its progress to other public service organisations. This would mean visibility of company effectiveness is provided for stakeholders, with an opportunity to influence those objectives through a collaborative approach.
- A1.36 Various companies advocated that tangible outcomes are the true markers of the progress of public value service delivery. Several companies suggested we consider drawing on the UN Sustainable Development Goals (UNSDGs) as these are already used by regulated companies. It is recommended Ofwat builds on the substantial expertise behind this and bases any new policies on measurement and reporting around this framework. Some currently use the framework in their plans, and the framework supports the adoption of innovation. With ODIs such as the biodiversity index in tandem they can help to shape future environmental programmes and WINEP, by understanding the best solution locally to shape national delivery. Others agree with the use of the UNSDGs, but believe the metrics within indices are becoming increasingly prescriptive and there is a risk of emphasis on boilerplate disclosures to demonstrate compliance, rather than disclosures providing meaningful insight for all stakeholders. A number of other respondents also consider public value is not suited to prescriptive performance indicators.

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?

- A1.37 Most companies agreed that Ofwat should not use standardised monitoring or reporting measures regarding public value. The general theme is that instead of Ofwat defining a rigid set of public value outcomes, a more flexible approach is preferred. Companies could demonstrate what they have delivered in terms of public value in a framework under which companies self-report to Ofwat. This approach would be flexible enough for innovation, whilst setting parameters for companies to adhere to in order to deliver public value. Conversely a universal set of markers were believed to stifle innovation. On the grounds that regional differences can impact on companies' approach to investment and innovation to deliver public value. If markers exist for one and not the other, companies will have little incentive to pursue public value. Additionally, the framework should be adaptable compared to rigid targets that would frequently be under review as public value understanding matures over time. One company suggested such a framework should not be prescriptive, but set out 'buckets' for companies to report against to show their public value delivery.
- A1.38 Some put forward the notion that public value can be subjective and difficult to measure in cases. An example from one company's public value framework is the

commitment to reach every school child with their education programme, measured by the number of school children they reach. They consider this as the delivery of significant public value, however this is difficult to account for with figures and metrics. They advocate that public value benefit should be described in the narrative and be accepted as evidence of regulatory submissions and part of the performance assessment. Another also discuss Ofwat developing high level principles around public value that could be incorporated as part of the Board leadership and reporting requirements.

- A1.39 CCW advocated that Ofwat needs to hold companies to account if they are not delivering, and that a monitoring framework should be established. They advised a possible additional feature in the Annual Performance Reports where companies provide evidence of what they have done, similar to Ofwat's work in measuring the extent to which companies adhere to Ofwat's Board Leadership principles. If this feature was in conjunction with CCW's 'Water Mark' measures, Ofwat could track progress against the delivery of company commitments. This could also act as a barometer of progress in delivering aspects of public value if there is confidence that the outcomes and Performance Commitments being measured reflect evidence of what consumers expect and value.
- A1.40 Others recommended that Ofwat develops a regulatory framework to match ambitious public policy goals and resilience investment. The delivery of these elements could be monitored similar to other business plan objectives. An example put forward was Dŵr Cymru's 'Resilience Community' projects that broadened focus of zonal studies to undertake largescale mains replacement. Others discussed that regulation may need to evolve to more directly incentivise companies to deliver what customers want, but they also stated that the current framework already aligns customer preferences with shareholder returns through cost, outcome and other incentive regimes. The current model is clear and empirically observable in terms of benefits compared to alternative experiments of public value, so some discouraged that the focus should be on deeper customer engagement and noted that the shift to outcomes-based regulation has meant companies are able to reflect customer preferences in the round.

Other

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

- A1.41 The need for collaboration across companies, government, regulators and the full range of stakeholders was prominent throughout the responses we received. It was recommended that the sector should collaboratively work together to develop a set of principles to guide the water industry to implement public value. These principles would be needed to find an affordable, effective and a sustainable approach to public value. These principles would provide flexibility for water companies to tailor their

own bespoke approach to public value, to reflect the material priorities to the communities they serve.

- A1.42 One company noted that Ofwat is right to be considering public value and that the sector needs to collaborate to work through any issues. However, the company also noted that any framework or definition of public value should only be considered once an understanding of customer wants and expectations has been undertaken.
- A1.43 It was suggested that Ofwat may need to provide greater clarity in terms of defining the reach of those stakeholders we expect company public value ambitions to target. Some respondents stated their principal relationship is with customers and bill payers not citizens and tax payers. The extent to which customers want the company to focus on environmental and social issues will determine their public value initiative. Any deviation without customers' consent is considered a risk to the legitimacy of the company and the wider sector. CCW discusses how companies need to look beyond today's bill payers to consider public expectations and look to the wider beneficiaries in terms of what the sector delivers. This includes meeting the needs of future customers in company's plans and strategies.

List of respondents

	Name of responders
1	Affinity Water
2	Anglian Water
3	Bristol Water
4	Consumer Council for Water (CCW)
5	Dŵr Cymru
6	Northumbrian Water
7	SES Water
8	Severn Trent
9	South West
10	Southern Water
11	Thames Water
12	Tideway
13	United Utilities
14	Wessex Water
15	Yorkshire Water
16	South East Water

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