Tuesday 20 July 2021
1:00 pm to 3:00 pm

Summary of Outcomes Working Group discussion – Environmental incentives

Evolving incentives for natural capital need to be consistent with the views of customers. The discussion noted that some changes in society, such as reducing the carbon in energy production, will occur anyway and we need to ensure that additional financial incentives are targeted where it will deliver added value for customers beyond this. Notwithstanding, members of the group suggested there is evidence that customers support water companies going further and faster on some areas such as reducing GHG emissions.

General support was expressed that reducing operational carbon could have financial incentives as well as biodiversity. But there were varying views on what other financial incentives are required. The difficulty of measuring some benefits consistently is a factor, including how we could measure embodied carbon. Sustainable abstraction was also suggested as a key outcome. While some considered the benefits covered by United Utilities natural capital PC appeared a good starting place, this view was not shared by all.

Further suggestions were

- Water quality with a focus on avoiding ecological impacts and ensuring drought resilience
- CSO improvements linked to water quality as well as addressing visual impacts of overflows (links made to amenity value)
- Flood risk reduction
- In relation to biodiversity addressing the spread of invasive species was also mentioned, rather than just preserving or increasing species
- Heating of rivers
- Odour
- Climate adaptation and other aspects related to climate change (e.g., capital emissions)

There are greater opportunities for wastewater companies to deliver nature based solutions and so deliver wider benefits. While there is some overlap with catchment management approaches there are varying levels of opportunities across water companies. We need to consider the flexibility of any common approach so that they remain fit for the circumstances of all companies. A more sophisticated approach could deliver more benefits for wastewater customers but the regulatory burden for water companies will need to be carefully considered.

Valuations are key and are unlikely to be constant across companies and between locations. Trees in urban locations could have higher benefits than in rural and the amenity value of different rivers are not the same. The potential for joint work between companies was raised to move forwards. The findings from UKWIRs future assets work should also be considered as well as new tools beyond B£ST.

Different companies have advantages in terms of which capitals they can target for improvement, and their baselines, so competitive incentives are less likely to work. Some companies noted the need for metrics that are within their control, but it was also noted that incentives need to encourage work with third parties. The need for further clarity on long term thinking on ambitions for the environment and that water companies should be aligned to the expectations in the Environment Bill when it is enacted, were also discussed.

In terms of how we might incentivise wider benefits, there were a range of views spanning from selecting only a handful of outcome focused metrics; to others that considered wider metrics should be used. Some considered a need for a mix of output and outcome approaches using both absolute and incremental measurements. Some companies considered that adding a further metric focused on value could improve incentives. Considering how natural capital is embodied within all PCs was a further possibility.

In terms of the structure of incentives, we may get different results from a mix of sticks and carrots based on an ex-ante expectation, compared to a carrot only basis of delivering stretching improvements, especially where there were not clear statutory expectations. A more positive approach to regulation might lead to greater change, on the proviso that statutory expectations were met. It was also suggested that metrics that allowed trade-offs could lead to better outcomes, rather than attempting to deliver stretching performance in all areas simultaneously.

A further aspect raised was that the outcome framework should clearly fit with wider ESG reporting, which is increasingly important in attracting investment to the water sector.