

WATER BILL SUMMARY IMPACT ASSESSMENT

Introduction

What is the problem?

1. In December 2011 the Government published its Water White Paper, *Water for Life*¹, and supporting documentation from the Environment Agency on the *Case for Change*². The Case for Change concluded that:
 - **Water resources are already under pressure.**
 - We can expect a **future with less water available for people, businesses and the environment.**
 - **Future pressures will not be limited to the south and east of England.**
 - Over the longer term **climate change could have a bigger impact on available water resources than population growth.**
 - **The water environment will change.** We will need to reconsider the requirements for future water ecosystems and the implications for the amount of water available for abstraction.
 - Demand management will have an important role to play, **but we may need significant new water resources to be developed.**
 - **Solutions will have to be found at both a local and strategic level** as even where a river basin may have enough water, local catchments within it might not.
2. The White Paper described a vision for future water management in which the water sector is more resilient; water companies are more efficient and customer focused; and water is valued as the precious resource it is. The Government set out in the White Paper the changes that are needed now to keep the country's water supplies reliable and affordable in a way that protects the environment while also stimulating the water sector to greater innovation and better customer service.
3. Building on the recommendations of Prof Martin Cave's *Independent Review of Competition and Innovation in Water Markets*³ and David Gray's *Review of Ofwat and Consumer Representation in the Water Sector*⁴, the White Paper set out plans to reform the current markets in water and sewerage and to amend Ofwat's powers to regulate the market; as well as some further proposals to reduce regulatory burdens in water resource management.
4. As delivery of these commitments requires primary legislation, the Government published a draft Water Bill⁵ in July 2012 for Pre-Legislative Scrutiny by the EFRA Select Committee.

¹ www.gov.uk/government/publications/water-for-life-market-reform-proposals

² www.environment-agency.gov.uk/research/planning/135501.aspx

³ www.gov.uk/government/publications/competition-and-innovation-in-the-water-markets-cave-review

⁴ www.gov.uk/government/publications/review-of-ofwat-and-consumer-representation-in-the-water-sector

⁵ www.official-documents.gov.uk/document/cm83/8375/8375.pdf

Territorial Extent

5. The Water Bill's measures mainly cover England and Wales. However, there are also two measures that refer to Scotland as well. The first builds a joint water and sewerage retail market (Scotland already has a functioning competitive retail market in place) and the second extends the Environmental Permitting Regulations to the Board River Esk with respect to fish passages.
6. The majority of the Bill's Impact Assessments apply to England and Wales, however two, *Introducing Retail Competition in the Water Sector (Defra 1346)* and *Upstream Competition (Defra 1347)*, apply only to England on a wholly and mainly basis⁶.

Updates since the draft Water Bill

7. Following the publication of the draft Bill there has been ongoing work to improve and strengthen the final Bill that is introduced into Parliament. This has included an internal review by the Defra Bill Team, consideration of recommendations from the EFRA Select Committee's Pre-Legislative Scrutiny Report⁷ and other concerns raised by stakeholders. Decisions around strengthening the Bill have taken account of new Impact Assessments as well as small revisions to existing ones.
8. The new Impact Assessments cover three new measures: Contestability of Water Connections, Drinking Water Inspectorate Charging Scheme (Defra 1382⁸) and Private Water Storage and Supply (Defra 1506). Alongside these there have also been changes to three existing Impact Assessments: Extending the Environmental Permitting framework to flood defence consents (Defra 1394), Extending the Environmental Permitting framework to water abstraction and impoundment licensing and fish pass approvals (Defra 1454) and Upstream Competition (Defra 1347).
9. The Bill also includes new measures to modify the way abstraction licence compensation is funded and also to specify a level of service that a water resources plan must address. The Impact Assessments to support these measures are currently being written and will be published during the passage of the Bill once they have been through the appropriate scrutiny. When these Impact Assessments are published a revised Summary Impact Assessment will also be published.

Policy Proposals

10. The Water Bill's policy proposals will deliver in four broad policy areas:

⁶ Following the Devolution Settlement and the Government of Wales Act UK Ministers generally have powers over water companies that are "wholly or mainly in England", which includes the mid-Wales part of Severn Trent Water.

⁷ www.publications.parliament.uk/pa/cm201213/cmselect/cmenvfru/674/674.pdf

⁸ Impact Assessments that require scrutiny by the Regulatory Policy Committee receive a four digit identifying number e.g. Defra 1234.

- Growth – a water sector that supports a growing economy, creates employment, drives innovation, and which continues to attract global investment
 - Resilience – as pressure on water supplies increases in the future, helping to ensure that water is available to supply households and businesses without damaging the environment
 - Choice – a water sector that offers choice and flexibility to customers and is open to new entrants with new ideas and approaches that will help keep bills affordable
 - Flood Insurance – the Bill will include any necessary legislation needed to help manage the financial risk of flooding.
11. Below is a broad outline of each policy, explaining the linkages between the measures in the Bill and their cumulative impact (if applicable). Each of the measures also has a supporting Impact Assessment which sets out the problem; rationale for action; options; and costs and benefits for each option. A summary of these Impact Assessments is also included below and Table Four summarises the benefits and costs of the preferred option and their assessment under One In One Out. The individual Impact Assessments can be studied in more detail if further information is required.
12. Following Royal Assent all Acts are subject to post legislative review (usually three to five years after Royal Assent) as well as any other existing review processes or scrutiny. This also includes a post-implementation review of the Act's Impact Assessments. This review will look at and consider whether or not the policy has achieved its objectives and if not how this can be remedied; the rationale for intervention and if it is still valid; and the extent to which the assumed costs and benefits have materialised and any unintended consequences.

Policies and Measures

Policy: Market Reform

13. In February 2008, the UK and Welsh Governments commissioned Professor Martin Cave to lead an *Independent review of Competition and Innovation in Water Markets*. The Review's principal purpose was to examine the case for introducing competition to increase efficiency of water use, drive innovation and deliver tangible benefits to both business and household customers.
14. The review acknowledged that in the 20 years since privatisation the Water Services Regulation Authority's (Ofwat's) framework for regulating regional monopolies had delivered a range of benefits, including service and quality improvements and reduced bills. However it concluded that alternative approaches and new ways of working, including a measured introduction of competition, were required to meet the future challenges facing the sector.
15. The Water White Paper considered the future of the water industry in the context of the challenges facing the sector including the need to address

climate change, demographic change, high customer expectations and the need for greater customer focus while keeping bills affordable.

16. Taken together, these challenges will place a requirement on the industry to find new and more efficient ways of allocating, treating and using water. This is important not only to ensure that supply and demand are balanced, but also to protect the environment by first using less inputs (for example energy, chemicals) and also by reducing the need for new infrastructure (for example new supply investments) by considering other cheaper and environmentally friendly options (for example sharing through inter-connections, catchment management to improve water quality etc.). This will ultimately protect consumers by minimising the cost to them of meeting the challenges.
17. Under the current arrangements efficiency in the industry is almost totally driven by Ofwat's economic regulation. Although this approach has delivered savings, the challenge today is that the rewards for outperformance are relatively modest and the risks from failure are high. Accordingly the Water White Paper recommended reforms to both the regulatory and legislative frameworks of the water sector to encourage the industry to become more innovative so that it is better able to anticipate manage and respond to the challenges.
18. The measures in the market reform package for the Water Bill are designed to: introduce greater clarity within the Special Merger Regime; amend the legislation covering the Water Supply Licensing regime in order to remove barriers to effective competition; reform the handling of new appointees and of existing appointees involved in the inset process to make the market more attractive to new entrants; improve the regulator's existing enforcement tools; reduce the bureaucracy around water companies' charges scheme to promote greater innovation; and provide new charging frameworks for setting charges for water and sewerage services.

Measure: Reform of the Water Special Merger Regime

19. The current water special merger regime creates uncertainty and unnecessary costs for water companies considering a merger. This is due to lack of knowledge of the methodology that would be adopted by Ofwat in assessing the implications for comparative regulation of the loss of a comparator and the fact that the Office of Fair Trading (OFT) is unable to accept undertakings from the merging parties to remedy or mitigate any prejudicial effects of a merger and is obliged to refer all qualifying mergers to the Competition Commission (CC). Government intervention is required to remove these barriers and burdens and make it easier for water companies to evaluate the costs of a potential merger.
20. The policy objective is to provide greater clarity to water companies that wish to merge, bring the regime into closer alignment with the general merger regime whilst ensuring that the implications for comparative competition continue to play an important role in merger decisions.

Policy options considered

Option 0 – do nothing (baseline case)

Option 1 – require Ofwat to publish guidance on how it would assess the loss of a comparator;

Option 2 – require Ofwat to publish guidance on how it would assess the loss of a comparator; and the introduction of a first stage merger test by the OFT⁹ (informed by the Ofwat guidance) and the introduction of powers whereby OFT can accept undertakings from water companies in lieu of a reference to the CC. This is the preferred option.

Measure: Retail Competition in the Water Sector

21. The water and sewerage industry in England consists of vertically integrated regional monopolies. Although the current form of price cap (RPI – X) regulation has been successful, the sector is facing new challenges which demand reform. To meet these challenges the Water White Paper, building on the *Independent Review of Competition and Innovation in Water Markets* led by Martin Cave, recommended a series of reforms to facilitate effective retail competition for non-households. Intervention is necessary as there are a number of barriers to competition in legislation.
22. The policy objective is to put a framework in place which enables all business customers in England to choose their water and sewerage retailer. The intended effect is that all non household customers will have the opportunity to switch suppliers, and that actual or the threat of competition will incentivise companies to provide improved and more innovative services, improve efficiency and reduce costs to customers. Businesses operating on multiple sites could receive a single bill instead of dealing with a range of individual water companies. This is in contrast to the current arrangements where non household customers are largely tied to the regional monopoly supplier, and efficiency and customer service levels are driven by targets set by Ofwat with very limited scope for business customers to demand their own bespoke arrangements.

Policy options considered

Option 1 – do nothing (baseline case)

Option 2 – WSL & legal separation: Reforming the Water Supply Licensing (WSL) regime and mandating the legal separation of companies' retail and wholesale functions for all those companies serving more than 50,000 customers.

Option 3 – WSL & functional separation: Reforming the WSL regime and mandating the functional separation of companies' retail and wholesale functions for all those companies serving more than 50,000 customers.

⁹ The functions of the OFT and the CC will be transferred to the Competition and Markets Authority in April 2015.

Option 4 – WSL & optional separation: Reforming the WSL regime and giving companies the option of separating their retail and wholesale functions to enter the competitive market.

Option 5 – WSL only: Introducing a package of reforms to the WSL regime without any separation of the companies' retail and wholesale functions. This is the preferred option.

Measure: Upstream Competition

23. Since its inception in 2005, the number of WSL licences (Water Supply Licensing regime) granted has grown and there are currently seven licensees, two of which are new entrants and five of which are subsidiaries of the existing incumbent water companies. However, activity in the regime has been limited, only three customers have switched supplier in eight years and there are no upstream combined supply arrangements currently operating.
24. The policy objective is therefore to promote upstream competition in relation to water and sewerage. The intended effects are to reform the existing competition regimes which have proven to be ineffective at facilitating competition. The reforms are expected to encourage market entry and deliver more effective competition by:
 - Removing barriers to entry;
 - Improving the transparency of the market opportunity for potential entrants;
 - Addressing issues of information asymmetry; and
 - Increasing the size of the market opportunity for potential entrants.
25. Effective upstream competition is expected to promote more efficient allocation of water and achieve better outcomes for consumers and the environment.

Policy options considered

Option 1 – do nothing (baseline case): The existing arrangements persist but Ofwat may implement some adjustments using its existing powers to regulate water companies without legislative change.

Option 2 – upstream water and sewerage licences: This includes a package of reforms to the existing WSL regime to encourage effective competition in the provision of new water and sewerage treatment capacity and water resources. Benefits are delivered in the form of lower prices to consumers and environmental improvements, major areas of risk/cost are around the potential impacts on the future cost of borrowing. This is to be the option pursued in the Water Bill.

Option 3 – upstream water and sewerage licences and network licences: This includes all of the changes in Option Two as well as a new network licence that would replace the existing New Appointments and Variations (NAV) regime and deliver additional benefits by reducing the regulatory costs faced by entrants in that

regime as a result of site-by-site application. Although this option follows the recommendations of the Cave Review, new network licences are not being considered in the Water Bill.

Measure: Updating Ofwat's Enforcement Powers

26. The policy objective is to strengthen the ability of Ofwat to regulate the industry in the interests of consumers by improving their enforcement tools. When water companies breach their conditions of appointment, licence or statutory provisions, it can have a detrimental impact on customers through reduced customer service and potential increases to bills. When imposing a financial penalty on a water company for such a breach, Ofwat are not always able to calculate the appropriate penalty to recompense for the impact of the breach as the investigation period is restricted to 12 months from a breach or failure occurring.
27. An extension to five years will give Ofwat a greater ability to fully consider the nature and implications of breaches therefore enabling a more accurate assessment of penalties. It will also enable Ofwat to investigate and impose penalties (if necessary) on breaches that have not come to light until the 12 month period has elapsed. This will provide a strong deterrent to future non compliance and could reduce the number of breaches as companies will be aware that penalties will reflect the full nature and impact of the breach. This protects customers and also ensures that companies do not profit from a breach.

Policy options considered

Option 0 – do nothing (baseline case)

Option 1 – a change to primary legislation to address a specific deficiency in the existing enforcement regime (the time limit for pursuing contraventions). Two sub options considered extending to two years or five years. This is the preferred option, with an extension to five years the preference as it enables a more comprehensive and accurate assessment of protracted cases and is consistent with the Price Review timeframe.

Measure: Changes to the approval process for water company charges schemes

28. Legislation requires that all water companies have their charges scheme approved by Ofwat each year (this is in addition to the quinquennial Price Review which caps charges). Water companies see this as a barrier to tariff innovation, while Ofwat regards it as a barrier to light-touch regulation, placing unnecessary burdens on compliant companies and encouraging behaviours driven by the regulator rather than the customer. The Ofwat Review recommended that Ofwat reduce the regulatory burden it places on the water industry and incentivise more innovative, customer-focused behaviours. The Water White Paper responded with commitments to support Ofwat in this.

29. In line with this Ofwat will move to a risk-based approach to regulate charges, allowing them to deploy their resources in an efficient, proportionate manner.

Policy options considered

Option 1 – do nothing (baseline case)

Option 2 – revise the guidance from the Secretary of State on the approval of charges and introduce a licence modification to allow Ofwat to set rules for charging, which would allow a limited move to ex-post checks.

Option 3 – remove Ofwat’s function of approving charges schemes contained in section 143(6)-(9) of the Water Industry Act 1991 (WIA91). Give Ofwat a general power to set rules for charging under WIA91, consistent with the transparent access pricing rules intended to replace the cost principle with a risk-based approach to ensuring compliance with guidance and price limits. This is the preferred option.

Measure: Charging for water and sewerage infrastructure within new developments

30. Recent reviews and feedback from stakeholders have identified difficulties in the way water and sewerage companies recover the cost of the additional water and sewerage infrastructure needed to support new developments. Developers and water and sewerage companies find the current charging framework complex, unclear and a barrier to greater competition. Therefore, existing arrangements have led to a large volume of disputes on charges with many cases being referred to Ofwat for determination.
31. The policy objective is to provide a new charging framework that will facilitate improved cost reflectivity, the efficient use of resources and fair competition; by simplifying processes for developers it will help stimulate growth. The new charging framework should improve clarity and coherence with other related charging schemes. This should enable a reduction in the overall administrative burden of charging for new development. The new charging framework needs to be readily adaptable to future market changes. The regime should be designed to incentivise development to be located in areas where there is capacity in existing infrastructure, or where the cost of providing additional infrastructure is lower than at alternative sites.

Policy options considered

Option 0 – do nothing (baseline case)

Option 1 – attempts to resolve problems by the regulator (Ofwat) issuing further guidance, this approach has been attempted but problems remain. Many of the problems relate to detailed provisions which are set in primary legislation where there are very limited opportunities for change. It is considered that a more fundamental change is now required.

Option 2 – replaces the current primary legislation with a power to make regulations which would set out a detailed charging framework.

Option 3 – puts a duty on Ofwat (through primary legislation) to introduce rules on a charging framework. This is the preferred option.

Measure: Drinking Water Inspectorate Charging Scheme for England

32. Defra currently funds the Drinking Water Inspectorate (DWI) for both its regulatory and policy functions; it now proposes to enable DWI to recover the costs of its existing regulatory functions from the water industry. This proposal brings the funding arrangements for the DWI in line with general government policy on charging, which states that businesses which benefit from regulation should bear the cost of regulation, not the taxpayer. Also, the Hampton Review 2005¹⁰ included a specific recommendation that regulators should be more accountable to those who benefit from their delivery functions
33. The proposal will:
- make DWI more accountable to those who benefit from its regulatory functions;
 - make DWI's funding more transparent; and
 - contribute around £2m per annum saving in the current spending review and reduce future pressures.
34. The proposal will also bring DWI in line with the cost recovery mechanisms for the other regulators.

Policy options considered

Option 0 – do nothing (baseline case)

Option 1 – enable cost recovery for existing services using basic methodology. This is the preferred option. This will enable DWI to recover the cost of its existing regulatory functions from water companies. It is also consistent with the views of water companies that the scheme should be as simple as possible. Although the option involves a modest net cost of around £1m, this is judged to be more than outweighed by the non-monetised benefits of aligning the charging of DWI services to those who benefit.

Option 2 – provide the regulatory service through the private sector.

35. This was originally conferred by Section Four of the Public Bodies Act 2011¹¹ and was accompanied by an Impact Assessment¹². However, there was a slight inaccuracy in the original Order which the Water Bill addresses.

¹⁰ www.bis.gov.uk/files/file22988.pdf

¹¹ www.legislation.gov.uk/ukpga/2011/24/contents/enacted

¹² www.legislation.gov.uk/ukia/2012/29/pdfs/ukia_20120029.pdf

Table One: Market Reform Costs and Benefits¹³

Measures	Costs	Benefits	Net Benefit
<p><i>Reform of the Water Special Merger Regime</i></p> <p><i>(Require Ofwat to publish guidance on how it would assess the loss of a comparator, the introduction of a first-stage merger test by the OFT, and introduction of powers whereby OFT can accept undertakings from water companies in lieu of a reference to the CC).</i></p>	<p>The costs to Ofwat of publishing guidance are expected to be small.</p> <p>Under the proposed reforms, the first stage test becomes potentially more substantive thereby increasing the cost to companies. For smaller water only companies the range of costs for a first stage test could be between £50k to £250k but we cannot at this stage be sure. However, this cost needs to be viewed alongside that associated with a full Competition Commission (CC) referral, which now might not be necessary, and could range from £50k up to £1m. However, we cannot accurately state what these costs might be as we cannot know which water companies (or how large they are) might be considering a merger.</p> <p>There is a possibility that the proposals could increase the time and, perhaps to a lesser extent, costs of a merger in a situation where the Office of Fair Trading (OFT) still decide (after the first stage test) to refer a case to the CC. However, water companies would be better informed of the chances of success at earlier stages and would have the choice as to whether to pursue the merger reference and any additional costs would be avoided if they chose not to. Furthermore, we would not expect analysis at the OFT “first stage test” to</p>	<p>The reform will introduce greater transparency and give water companies greater certainty over the way in which future mergers will be considered. In addition, a first stage test with a power to accept undertakings to mitigate against the loss of a comparator could potentially reduce costs, particularly for smaller water only companies in looking to merge.</p> <p>Removal of this uncertainty might lead to increased merger activity, though the threshold for referral of mergers to OFT will remain the same so the general level of scrutiny will be streamlined rather than loosened.</p>	<p>Costs and benefits have not been estimated in money terms for introduction of a first stage test because we cannot know which companies might be considering a merger. However, the benefits of transparency and the potential efficiency of the first stage test are judged very likely to more than outweigh the small costs of introducing the proposal.</p>

¹³ General note to Table One: Where monetary values are quoted with the suffix “PV” these are Present Value (discounted) totals over a 30-year period. Please see the Impact Assessments for individual measures for more detail.

Measures	Costs	Benefits	Net Benefit
	<p>be nugatory; it would in practice be expected to inform any subsequent CC assessment, yielding some saving in both time and costs at that stage.</p>		
<p>Retail Competition in the Water Sector</p> <p><i>(Introducing a package of reforms to the WSL regime without any separation of the companies' retail and wholesale functions)</i></p>	<p>The primary costs under this measure relate to those incurred by the regulator to set up the necessary market arrangements. This includes setting up and operating the market settlement and switching infrastructure (estimated at £79m as a Present Value (PV) over 30 years); and designing and administering the new arrangements (£75m PV).</p> <p>Additionally incumbent companies will incur some ongoing costs under the new arrangements (£34m PV) and would also be expected to incur costs in order to retain and attract customers (£52m PV).</p>	<p>The primary benefit is that incumbents are incentivised to seek out productive and dynamic efficiency savings in relation to the provision of non-household retail services (£64m PV). This would also be expected to generate efficiency savings in relation to the provision of non-household retail services (£230m PV). In addition greater upstream pressure from retailers would generate wholesale efficiencies (£100m PV) and some water efficiencies would also be realised (£31m PV).</p>	<p>Best estimate: £190m</p> <p><i>Present Value over 30 years</i></p>
<p>Upstream Competition</p> <p><i>(Upstream water and sewerage licences including a package of reforms to the existing WSL regime)</i></p>	<p>Ongoing costs to the government and regulators will be minimal but additional work will be required by Ofwat and the quality regulators (EA and DWI) to ensure applicants are fit to hold new upstream water and sewerage licences and in administering the regime but these will be incremental to the costs incurred in relation to the regime that already exists (c. £2.7m per annum). Companies will incur minor ongoing compliance costs (c. £1m per annum). There may be an increase in the ongoing cost of borrowing in the sector as a result of these reforms which represents the most significant area of cost (c. £414m-£689m PV over 30 years).</p>	<p>The key monetised benefits arise from the one-off productive (£1,790m NPV) and ongoing dynamic (£581m NPV) efficiencies against the likely future investments in upstream water and sewerage services. These savings accrue to incumbent water companies in the first instance who avoid incurring full economic costs in the building of new upstream capital assets and these savings are then passed on to end customers in the form of lower bills as a result of lower unit costs.</p>	<p>Low: £426m</p> <p>High: £3,072m</p> <p>Best estimate: £1,750m</p> <p><i>Present Value over 30 years</i></p>

Measures	Costs	Benefits	Net Benefit
<p>Updating Ofwat's Enforcement Powers</p> <p><i>(A change to primary legislation to change the time limit for pursuing contraventions).</i></p>	<p>There are no monetary costs associated with this option. Water Companies are under a statutory duty to supply Ofwat with financial information and evidence relating to compliance with licence conditions. Therefore there are no additional burdens or costs on companies. The extension to five years merely enables Ofwat to act appropriately in cases where evidence of a breach is identified more than 12 months after it occurred; and in cases where there have been repeated or prolonged instances of the same breach.</p> <p>Ofwat does not believe that the change to the time limit will materially impact the level and depth of analysis required in individual cases, or result in a change in the number of contraventions which Ofwat investigates.</p> <p>There is therefore no anticipated additional staff cost to Ofwat. The change will not introduce new obligations on companies, so Ofwat does not consider that it will materially impact on the administrative burden placed on water companies in the day-to-day running of their business. The only financial impact will be on companies responsible for infringements (who could – rightly face larger penalties).</p>	<p>Due to a high degree of variability in the type and scale of cases and no adequate means of calculating the likelihood or frequency of contraventions by companies it hasn't been possible to assign specific monetary values.</p> <p>Neither has it been possible to estimate the increased value of historic penalties had the 12 month investigation restriction not applied. This is due to the amount and scope of information collected in each case did not take into account contraventions and impact over a longer timescale.</p> <p>Ofwat have imposed eight financial penalties totalling £74.3m since gaining powers in 2005. In all cases the penalty did not take into account the full extent of the contravention due to the time limit imposed. In addition in two further cases a financial penalty could not be applied due to the 12 month restriction. By making changes it would enable Ofwat to impose a more accurate penalty that reflected the nature, scale and impact of a breach, ensure more compliance with better regulation principles and natural justice, provide a greater deterrent to companies and remove the incentive to delay notification of a breach. Customers would benefit as companies will be more accountable when they contravene licence conditions, to the extent that companies face larger penalties and consumers receive greater compensation.</p>	<p>Costs and benefits have not been estimated in money terms for this proposal because it is not possible to predict infringements. However, the benefits of broadening opportunities for redress of infringements are judged very likely to more than outweigh the negligible costs of introducing the proposal.</p>

Measures	Costs	Benefits	Net Benefit
<p>Changes to the approval process for water company charges schemes</p> <p><i>(Remove Ofwat's function of approving charges schemes contained in section 143(6)-(9) of the Water Industry Act 1991 (WIA91). Give Ofwat a general power to set rules for charging under WIA91)</i></p>	<p>Overall, the cost of going from the current scheme to the preferred is assessed to be neutral. For the majority of water companies and Ofwat, the administrative cost of complying with a new risk based approach under the preferred option is assumed to be broadly equivalent to the cost of complying with and monitoring the annual approval process under the current scheme. Also, the administrative resource commitment is assumed to remain constant but be better targeted.</p> <p>There is potential that non-compliant water companies may face greater scrutiny from Ofwat under a risk-based approach. As a consequence, they may incur marginally higher but more proportionate costs.</p> <p>However, it is has not been possible to assign monetary costs due to the significant variation in administrative processes adopted by companies and complexity in predicting future levels of non-compliance.</p>	<p>It has not been possible to assign monetary benefits for the preferred option due to the high degree or variability and complexity of the approval process depending on the nature of charges schemes.</p> <p>Compliant companies are likely to achieve a small administrative saving though this is negligible and difficult to quantify given the range of charges schemes and variability in processes.</p> <p>Supports a more efficient and proportionate allocation of Ofwat/water company resources. The Ofwat allocation of £320k will be targeted at more risky schemes enabling them to highlight and implement corrective measures to ensure customers are not over-charged. If all companies complied with charging rules this could result in an illustrative industry wide annual administrative saving of between £1,900 and £11,250.</p> <p>Enhances flexibility to address compliance issues outside the annual approval window. Ofwat will be able to immediately rectify non-compliance, including compensating customers for over-charging and thereby boosting incentives for water companies to comply.</p> <p>Removes a significant barrier to development of innovative tariffs. 55% of water companies claim the annual approvals process is a barrier to tariff innovation. In conjunction with other measures, the removal of this barrier could realise potential benefits of £25.6 million to customers in the development of social tariffs. Ofwat estimate that innovative tariffs could reduce water demand by up to 10% resulting in costs savings of up to £40</p>	<p>This Impact Assessment does not include monetary estimates of costs or benefits for these options. This is driven by the high level of uncertainty in predicting or projecting future costs that companies may face in complying with a risk based compliance approach. However, the efficiency, flexibility and innovation benefits are judged very likely to more than outweigh the negligible costs of the proposal.</p>

Measures	Costs	Benefits	Net Benefit
		<p>per annum in reduced bills.</p> <p>Significantly improves consistency with recommendations of Ofwat Review, BIS principles of economic regulation and Water White Paper. Enables Ofwat to adopt a light-touch, risk-based regulatory approach consistent with the Principles of Economic Regulation, Ofwat Review and White Paper.</p>	
<p>Charging for water and sewerage infrastructure within new developments</p> <p><i>(A duty on Ofwat to introduce rules on a charging framework)</i></p>	<p>There will be some further one-off administrative costs associated with developing the legislation, but overall the proposal will lead to cost savings for Ofwat, water and sewerage companies and developers.</p> <p>At this stage costs have not been given a monetary value. The eventual charging rules will have a more detailed Impact Assessment, and will be subject to separate consultation.</p>	<p>The current charging provisions are cumbersome, lack transparency and are open to interpretation which has led to excess costs for all involved in new developments. By modifying primary legislation to reflect key charging principles only, and delegating detailed arrangements to charging rules, new charging arrangements will be established which will save administrative costs and secure other benefits.</p> <p>At this stage benefits have not been estimated in monetary terms. The eventual charging rules will have a more detailed Impact Assessment, and will be subject to separate consultation.</p>	<p>This Impact Assessment supports the case for change. At this stage it does not attempt to calculate costs and benefits, as the proposed option will make no change to the existing charging framework until a new framework is developed and introduced.</p>
<p>Drinking Water Inspectorate Charging Scheme for England</p> <p><i>(Enable cost recovery for existing services using basic methodology)</i></p>	<p>Average annual costs are £1.7m. This is made up of additional administrative costs of £200k in the first two years, then £100k thereafter, as well as £2m in charges raised from the water industry (from year three onwards). Over 10 years, the total cost has a net present value of £13.9m. The majority of this is the cost of the charges raised on industry (a cost to business with a net present value of £12.8m or £1.5m as an annualised cost (£1.4m as an EANCB at 2009 prices).</p>	<p>Benefits are the reduced cost to the government arising from transferring the annual funding of DWI operations to the industry. This exactly offsets the increased cost to the industry (£12.8m in total PV terms, or £1.5m as an annualised cost).</p> <p>DWI will be able to inform the public on how well water companies have progressed with their drinking water safety management. Improved independence of DWI in relation to its regulatory budget & improved accountability of DWI in</p>	<p>Best estimate: £-2.26m (£-1.021m)</p> <p><i>Present Value over 30 years with 10 year figures in brackets</i></p>

Measures	Costs	Benefits	Net Benefit
	<p>The cost to water companies and licensed water suppliers of reviewing and processing a bi-annual invoice from DWI are negligible and not monetised. No additional data/administrative costs are incurred.</p>	<p>relation to the water industry and consumers – through approval mechanism on proposed charges. The proposed system will encourage water companies to help deliver lighter touch regulation as charges will reflect their respective regulatory burden.</p>	

Policy: Water Resources

36. Water Resources covers a whole plethora of topics and policies from abstraction licensing (the taking of water supplies from watercourses) through to drought. In the Water White Paper the Government committed to reform of the abstraction licensing system. This will require further primary legislation in due course, but is not being pursued through this Bill. The measures included in this Bill are designed to repeal redundant legislation that requires the Environment Agency to maintain certain records of maps and reduce burdens on water undertakers by aligning drought planning with the water resource management planning cycle.

Measure: Private Water Storage and Supply

37. Owners of private water storage, like on-farm storage and large land owners, cannot currently sell water to water companies. While private transactions are technically possible, there are regulatory barriers that hinder them. Making this transaction easier may encourage the development of water storage capacity by providing a market mechanism for the sale of said water. This, supported by enabling activities such as access to funding, could help increase the number and capacity of water storage facilities, which can increase the resilience of farmers and landowners to extremes of weather. Therefore, Government intervention is necessary to create an enabling framework as the market is subject to an economic regulation regime which currently effectively excludes supply from private water storage.
38. The overall objective is that more private water storage facilities are built where this makes economic sense, increasing resilience of both storage owners and the public water supply to drought and reducing pressure on other sources. This measure is designed to open up a market which is currently inaccessible, in practice, to private water storage owners. This may then play a part in increasing the total volume of private water storage facilities, by providing a market mechanism which could make the storage and sale of water more viable.

Policy options considered

Option 0 – do nothing (baseline case). There would be no mechanism for supporting market development. At present, if a private water storage owner wished to sell their water, they could:

- a. Privately negotiate and contract with a water company; or
- b. Become licensees under the reformed Water Supply and Sewerage Licensing (WSSL) regime, which involves a significant administrative burden

Option 1 – this option would introduce an enabling power into the Water Bill to allow us to introduce secondary regulations to extend the definition of “supplier” in the bulk supply regime, to include private water storage owners and people with water storage capacity. A supplier under the bulk supply would have a 'right to negotiate'

with water companies, and access to market codes and recourse in case of disputes. This is the preferred option.

Non-regulatory alternatives: There are ways to incentivise the development of storage via access to funding and planning reform, however these do not provide a market mechanism or the protection of a regulated market.

Measure: Maps of Agency waterworks – repeal section 195 of the Water Resources Act 1991

39. The Environment Agency is required to keep and maintain records in the form of maps showing resource mains, discharge pipes and waterworks vested in the Agency and to make these maps available for public inspection. As this is an unused record of maps, and there are other overriding legal obligations on the Environment Agency to disclose information, the aim is to remove this particular, redundant legal obligation as part of a programme to reduce bureaucracy and red tape. The effect will deliver a small efficiency and cost saving to the Environment Agency.

Policy options considered

Option 0 – do nothing (baseline case): would leave the provision and obligation in place even though the records are unused and potentially duplicated by other general estate records. This would also prevent a modest efficiency and cost saving from being realised.

Option 1 – repeal this provision through legislation. This is the preferred option.

Measure: Statutory drought and water resources planning by water undertakers: frequency of the planning cycle

40. Water undertakers have a statutory duty to provide adequate supplies of water for domestic purposes. An independent review of the water resources planning process¹⁴ recommended that the Government should seek better alignment of the plans. Therefore, we propose to achieve this by extending the planning cycle of drought plans to five years.
41. The ongoing policy objective is to ensure that water undertakers are able to meet their supply duties, including during a drought. By changing the frequency of drought plans water companies will be able to use the information from up to date water resources plans to feed through into their drought plans, ensuring consistent data and better alignment. In addition, we will avoid circumstances in which both plans become due at the same time, creating a significant peak in regulatory burden for companies. By taking a power to make future changes through secondary legislation we will be able to ensure these plans remain aligned with other statutory plans such as the periodic review by Ofwat, into which the WRMP feeds.

¹⁴ www.gov.uk/government/publications/review-of-water-resources-management-plan-process

Policy options considered

Option 0 – do nothing (baseline case): If we do nothing, companies will still prepare effective plans but the planning cycles will remain out of alignment and will, at some point in future, fall due for completion at the same time, creating a significant burden. To avoid the plans coinciding the Secretary of State could use powers to Direct earlier completion of plans but this would mean bringing forward a burden when the planning requirement itself does not need it.

Option 1 – change the frequency of drought plans to five yearly and so achieve better information alignment and reduce the risk that plans will fall due at the same time. A power to make further changes by secondary legislation will enable us to continue to keep the plans aligned with other statutory processes such as Ofwat's price review and ensure the optimal flow of information and minimise duplication of effort by the companies. Water companies welcome this move. This is the preferred option.

Table Two: Water Resources Costs and Benefits¹⁵

Measures	Costs	Benefits	Net Benefit
<p>Private Water Storage and Supply</p> <p><i>(Extend the definition of “supplier” in the bulk supply regime, to include private water storage owners. Suppliers would have a 'right to negotiate' with water companies, and access to market codes and recourse in case of disputes)</i></p>	<p>Water Companies: Administrative costs of negotiation, estimated at between £0.15m and £0.72m per year. This includes staff costs for negotiating with 5 to 10% of private storage owners in a year, and a range of staff cost estimates.</p> <p>Suppliers: Costs are voluntary (not direct) and would only be incurred where suppliers judge that a net beneficial opportunity exists.</p> <p>There will also be minor administrative costs to Defra, EA and Ofwat, including policy development and development of market codes; and minor running costs to EA and Ofwat as part of normal operations.</p>	<p>This is a competition measure designed to open market access. To give a sense of the scale of potential benefit, if the amount of extra water available in a shortage year was 10% of non-water company storage (i.e. between 720m and 825m m3, the combined sums of reservoirs at low and high estimates), for “1 in 10 year” drought events, benefit would be around £7.5m per year.</p> <p>Other key non-monetised benefits include access to a variety of new sources of water for Water Companies, and access to a market for the sale of water; a 'right to negotiate' with water companies and use of market codes for suppliers.</p>	<p>Best estimate: £-6.8m (£-7.9m)</p> <p><i>Present Value over 30 years with 40 year figures in brackets</i></p> <p>NB: given the uncertain nature of benefits, this figure only relates to the costs of the measure.</p>
<p>Maps of Agency waterworks – repeal section 195 of the Water Resources Act 1991</p>	<p>The Environment Agency would be the only directly affected body and does not expect any costs to arise from the repeal provision.</p> <p>The general public will not be affected as no use has been made of these records and other routes to access and disclose the prescribed information are available. No new or additional costs will therefore fall on them as they are not affected by this proposal.</p>	<p>The Environment Agency should realise a small cost and efficiency saving (estimated to be £0.01m) each year as unnecessary duplication is removed.</p>	<p>Best estimate: £0.20m (£0.09m)</p> <p><i>Present Value over 30 years with 10 year figures in brackets</i></p>

¹⁵ General note to Table Two: Where monetary values are quoted with the suffix “PV” these are Present Value (discounted) totals over a 30-year period. Please see the Impact Assessments for individual measures for more detail.

<p>Statutory drought and water resources planning by water undertakers: frequency of the planning cycle</p> <p><i>(Change the frequency of drought plans to five-yearly, with a power to make further changes by secondary legislation to keep plans aligned with other statutory processes such as Ofwat's price review)</i></p>	<p>No new or additional costs will affect the water undertakers, inset appointees or regulators. The only other non-monetary cost will be that, on average, plans will be slightly older.</p>	<p>The key monetary benefits are the savings (administrative and associated costs) that will arise by water undertakers having to prepare plans less frequently. Estimated savings are based on the 24 water undertakers and are based on average cost per company per plan. If the costs are spread over a 5 yearly cycle rather than 3.5 yearly cycle estimated savings over a 10 year period are £2.20m undiscounted total saving.</p> <p>Also by aligning the plans to a five yearly cycle it will avoid water resource and drought planning requirements coinciding and creating a peak administrative burden.</p>	<p>Best estimate: £4.05m (£1.830m)</p> <p><i>Present Value over 30 years with 10 year figures in brackets</i></p>
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Policy: Environmental Permitting Regulations

42. The Environmental Permitting Regulations (EPRs) are a common framework for environmental consents, with the aim of minimising administrative burdens without affecting environmental protection standards or policies. The EPRs came into effect in April 2008 when part of the Environmental Protection Act 1990, the Waste Management Licensing Regulations 1994 and the system of permitting in the Pollution Prevention and Control (England and Wales) Regulations 2000 were replaced with a new system of environmental permitting in England and Wales. Since then it has been expanded to encompass a wide range of related, but previously separate, Environment Agency and local authority consenting regimes, to deliver a flexible, risk-based single regime for businesses and others.
43. The recent Penfold Review of non-planning consents¹⁶ recommended expanding the environmental permitting regime to cover other non-planning consents. In general this will not change the substantive requirements of permits, but is expected to reduce the administration necessary to deliver those requirements. The benefits are, therefore, generally expressed in terms of savings in administrative costs.

Measure: Extending the Environmental Permitting framework to incorporate water abstraction and impoundment licensing and fish pass approvals

44. Existing environmental permitting regimes have previously been developed largely in isolation and have, often for good reasons at the time, adopted a variety of approaches to controlling different types of activity even where they are undertaken on the same site. This has led to a system of regulatory control with elements of duplication, which is complex for industry, regulators and others and may act as a barrier to entry for new businesses. Government intervention is necessary to add water abstraction and impoundment licensing and fish pass approvals into the Environmental Permitting framework to reduce the administrative costs of environmental regulation while continuing to achieve the intended outcomes.
45. Adding Water Abstraction and Impoundment and Fish Pass Approvals will reduce the current administrative costs to businesses and facilitate more cost-effective implementation of new directives.

Policy options considered

Option 0 – do nothing (baseline case): This models the status quo, where the Water Abstraction and Impoundment and Fish Pass Approvals regimes remain outside the Environmental Permitting framework.

Option 1 – is for the regimes to be incorporated within the Environmental Permitting framework. This is expected to cut unnecessary red tape, to continue to protect the environment and human health, and to increase clarity and certainty for all

¹⁶ www.gov.uk/government/publications/penfold-review-of-non-planning-consents

stakeholders on how the system protects the environment. This is the preferred option.

Option 2 – is for non-legislative changes to be made to the regimes. This option aims to replicate some of the benefits associated with environmental permitting by providing clearer guidance to applicants, but without any associated legislative change.

Measure: Extending the Environmental Permitting framework to Flood Defence Consents

46. Current legislation requires consent by the Environment Agency in England or the Natural Resources Body for Wales for certain works on or near watercourses which may affect flood risk. These consenting requirements can add to the administrative burdens of public, business and developers' projects. There is also some duplication with other planning and non-planning permit regimes. The numbers and extent of these regimes can be complex for both industry and regulators, and may act as a barrier to new business developments and start-ups.
47. Government intervention is necessary to reduce the administrative burdens while continuing to ensure flood risk management. Therefore, the policy objective is to make applications for flood defence consents easier. This would be done by removing duplication with other Environment Agency or Natural Resources Body for Wales consenting schemes and removing complexity from the application process. This will remove barriers and associated costs whilst ensuring that flood risk management is not affected.

Policy options considered

Option 0 – do nothing (baseline case)

Option 1 – Invest to streamline flood defence consenting regime as far as existing legislation will permit.

Option 2 – Integrate the flood defence consenting regime into the Environmental permit. This provides the greatest scope for reduction in administrative burdens, especially to applicants. This is the preferred option.

Option 3 – Align the flood defence consenting regime with environmental permitting schemes of other arms length bodies.

Table Three: Environmental Permitting Regulation Costs and Benefits¹⁷

Measures	Costs	Benefits	Net Benefit
<i>Extending the Environmental Permitting framework to water abstraction and impoundment licensing and fish pass approvals</i>	There will be some implementation costs to the Environment Agency and the Natural Resources Body for Wales through process change, developing standard rules permits, amalgamating public registers, writing guidance and a temporary reduction in process efficiency; and to business, for example investing time to read guidance. A small ongoing cost is forecast for Standard Rules permits being transferred at the point of variation or apportionment for the Water Abstraction and Impoundment regime.	Mostly through reduced administrative costs for the industry (including households) and the Environment Agency and the Natural Resources Body for Wales. There are also benefits (not given a monetary value) through increased clarity and certainty and also a simplified system for transposing environmental directives.	Best estimate: £9.3m (£4.2m) <i>Present Value over 30 years with 10 year figure in brackets</i>
<i>Extending the Environmental Permitting framework to flood defence consents</i>	There will be some transitional costs to: <ul style="list-style-type: none"> Environment Agency / Natural Resources Body for Wales: through staff training (£17k), development of new permits and guidance (£44k), upgrading IT (£150k) Applicants: through time spent understanding the new system and guidance (£608-808k of which 50% to business). <p>There will also be ongoing costs to the Environment Agency of running a new system (£398-591k Present Value total over 10 years).</p>	There will be savings in administrative costs to the regulators ((£3.3-3.5m PV, 34%) and applicants (£6.4-6.6m PV, 66%), of which half to business), in particular from integration of permitting regimes (in 30% of cases where flood defence consents are required, other environmental permits are required) and the facilitation of simpler “standardised rules” permits for low risk situations. There are also non-monetary benefits for applicants through reduced resources and time needed for flood defences consents, clearer criteria ahead of application, a single regulator, applications and permit; and for the regulator through focusing resources on high risk activities without compromising flood risk.	Low: £5.1m High: £7.5m Best estimate: £6.24m (£2.8m) <i>Present Value over 30 years with 10 year figure in brackets</i>

¹⁷ General note to Table Three: Where monetary values are quoted with the suffix “PV” these are Present Value (discounted) totals over a 30-year period. Please see the Impact Assessments for individual measures for more detail.

Other Specific Impact Tests

48. An Impact Assessment also involves the consideration of certain other specific impacts. These include: Net Costs to Business, Equality & Human Rights, Justice Systems, Rural Proofing and Sustainable Development. While some of these impacts were considered not to be material at individual measure level (and so are not reported in all individual Impact Assessments), this summary presents the overall picture for the Water Bill.

Net costs to business (One In One Out and One In Two Out methodologies)

49. As part of the process the Impact Assessments have applied the One In One Out or One In Two Out methodologies¹⁸ to identify any new net costs to business from the Water Bill's policies and measures. With the exception of three all are within the scope of these methodologies and their assessments show that they are either considered as an "Out" or as a "Zero Net Cost" to business. This is due in part to the majority of the measures being deregulatory in nature as they aim to introduce market reform into the water industry.
50. For the whole Water Bill, where monetary benefits and costs have been provided, the totals estimated for all measures are:

Total Net Present Value:	£1,951m (over 30 years)
Business Net Present Value:	£1,937m (over 30 years)
Net cost to business:	£-101.7m (per year)

(Where Net Present Value = Total Present Value Benefit – Total Present Value Cost)

51. A breakdown of these summary figures by measure is provided in Table Four below; the vast majority of net benefit is derived from the market reform measures. Please note that some measures were assessed over a 10-year period in their individual Impact Assessments; these figures have been rebased to allow consistent aggregation with the market reform estimates (see Table Four for both the original and rebased figures). Furthermore, one Impact Assessment (Private Water Storage and Supply (Defra 1506)) was assessed over a 40-year period because of the nature of the assets involved; this has also been rebased to 30 years for aggregation purposes.
52. It should also be noted that the aggregate net present value of the Water Bill measures as a whole may be underestimated to the extent that certain other benefits have not been able to be expressed in money terms (see Tables One-Three above). Nevertheless, despite this, the summary aggregate figures do indicate a sound economic case for the Water Bill, at least over the longer term.

Equality and Human Rights Impact

53. The impacts of all the policies and their measures in the Water Bill are not expected to have any impact on any of the responsibilities under the Equality Act

¹⁸ The majority of the Water Bill's Impact Assessments were prepared for the Water White Paper (Water for Life) and the draft Bill and were assessed against the old One In One Out methodology; whereas the newest measures were assessed against the newer One In Two Out methodology.

2010 (age, disability, gender reassignment, marriage and civil partnership, pregnancy and maternity, race, religion or belief, sex, sexual orientation). There is also not expected to be any impact on rights under the Human Rights Act 1998 (European Convention on Human Rights). However, the impact on human rights has been considered under the Retail and Upstream Competition Impact Assessments with regards to property. We do not consider that there is an adverse impact.

Justice System Impact

54. There are two measures within the Water Bill that have a potential impact on the Justice System. Under WSL Reform two new offences have been created of illegal access to sewer systems which will protect the integrity of the licensing regime and prevent unlicensed and unregulated activity. The impact on the courts system is expected to be negligible. No prosecutions have been made in England or Wales for the equivalent offence for water supply and there have been no prosecutions in Scotland for either water supply or sewerage.
55. Under the provisions to extend the Environmental Permitting Regulations existing offences will be repealed and re-enacted – though we do not expect the extent of these offences to change.

Rural Proofing Impact

56. The measures in the Water Bill are not expected to have a disproportionate impact on rural areas. Nonetheless, effects may vary across individual rural areas.

Sustainable Development Impact

57. The measures in the Water Bill are expected to lead to more efficient use of water resources, innovative methods of sewerage treatment, reduced costs to business and benefits to the economy, and better customer service in the water and sewerage industry. We expect the Bill therefore to have a positive impact on sustainable development.

Table Four: Summary table of benefits and costs (Present Value and Costs) and One In One Out (OIOO)

		Total Net Present Value* (£m)	Business Net Present Value* (£m)	Net cost to business per year (£m)	Within scope of OIOO	In / Out / Zero net cost
Market Reform	Reform of the Water Special Merger Regime (Defra 1435)	N/A	N/A	N/A	No	N/A
	Introducing Retail Competition in the Water Sector (Defra 1346)	190^	161^	-8^	Yes	Zero
	Upstream Competition (Defra 1347)	1,750^	1,801^	-95^	Yes	Zero
	Updating Ofwat's Enforcement Powers (Defra 1417)	N/A	N/A	N/A	Yes	Zero
	Changes to approval process for water company charges schemes (Defra 1455)	N/A	N/A	N/A	Yes	Out
	Charging for water and sewerage infrastructure within new developments (Defra 1383)	N/A	N/A	N/A	Yes	Zero
	Drinking Water Inspectorate Charging Scheme (Defra 1382)	-2.3 (-1.0*)	-28 (-13*)	1.4	No	N/A
Water Resources	Maps of agency waterworks – repeal section 195 of the water Resources Act 1991	0.2 (0.1*)	N/A	N/A	No	N/A
	Private Water Storage and Supply (Defra 1506)	-6.8 (-7.9**)	-6.8 (-7.9**)	0.3^	Yes	Zero
	Statutory drought and water resource planning by water undertakers: frequency of the planning cycle (Defra 1432)	4.1 (1.8*)	4.1 (1.8*)	-0.2	Yes	Out
Environmental Permitting	Extending the Environmental Permitting framework to water abstraction and impoundment licensing and fish pass approvals (Defra 1454)	9.3 (4.2*)	3.5 (1.6*)	-0.2	Yes	Out
	Extending the Environmental Permitting framework to flood defence consents (Defra 1394)	6.2 (2.8*)	2.2 (1.0*)	-0.1	Yes	Out
TOTALS:		1,951	1,937	-102		

Net Present Value: The term is used to describe the difference between the Present Value of a stream of costs and a stream of benefits.

Present Value: The total value of a policy, over the appraisal period, expressed in present terms by means of discounting.

* / **: Note that Present Value estimates are all 30-year "best estimate" figures except where indicated with * (10 year figures) or ** (40 year figures), as presented in the individual Impact Assessments for these measures. Please see the individual Impact Assessments for more information.

^: These values are for England only (on a wholly and mainly basis).