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PRIME MINISTER

WATER PRIVATISATION - WHITE PAPER

Following consideration in E(A) on 19 November of the memorandum on Water Authority Privatisation submitted jointly by Nicholas Edwards, Michael Jopling and myself, we now submit a draft White Paper for colleagues' approval. This has been drafted to provide a clear statement of our policy and to meet the various points raised during the E(A) discussion.

In developing and clarifying our views on the form of regulation, John Patten and I have had the benefit of a report from Professor Littlechild which it is my intention should be published at about the same time as the White Paper. Section 4 of the draft White Paper follows his lead in proposing a system of regulating prices and service levels together; and the management would be motivated to make profits by achieving both as efficiently as possible. Our proposals also take full advantage of the potential for competition between the ten authorities in the stock market and in all other possible ways.

Flood prevention and land drainage cannot be dealt with in this White Paper though paragraph 3.10 states the new context in which the administration and financing of these functions must now be reviewed. On pensions we cannot go beyond the statement on para 7 of Section 1 until we have had discussions with the water authorities and the Treasury; the statutory water companies' employees are in the same pension arrangements as the authorities' and careful negotiation will be needed when the broad shape of our proposals has been disclosed. Tax issues too cannot be resolved unambiguously before water authority asset registers have been reviewed, but we shall not be under immediate pressure to show our hands on taxation. The proposals in Section 5 should allay the inevitable misgivings of the environmental interests, with careful presentation. The investors will have to accept them if water authorities are to be privatised at all.

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On water metering, the White Paper does I hope reflect your views as expressed in your Private Secretary's minute of 9 December. In particular it makes clear our support for the extension of metering, the advantages of economies of scale in installation and the need for large scale trials.

In conclusion I would just like to mention the statutory water companies. They are already in the private sector, so they are not the main focus of our policy. However, we do see advantage in their agreeing to convert themselves into PLCs and to come within the same regulatory framework as that to be established for the WSPLCs; our bill will provide for this voluntary transition. I am pleased to report that the initial response to this suggestion from the Water Companies Association has been quite encouraging.

As our policy paper E(A)(85)64 made clear, our aim is to legislate for water authority privatisation in the 1986/87 session, to incorporate all water authorities as WSPLCs as soon as possible after Royal Assent, and to be ready during 1987 to begin a sequenced flotation of all the authorities. This is a very tight timetable, and to hold to it is essential for the White Paper to be published very early in the New Year. I would therefore ask all colleagues to let me have any comments on the draft White Paper by Monday 13 January at the latest.

I am copying this minute to all Cabinet Colleagues and to John Wakeham, Bertie Denham, Sir Robert Armstrong and Brian Griffiths.

SWenderson

for

K B

*Approved by the Secretary of State and
signed in his absence*
23 December 1985

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10 DOWNING STREET

From the Private Secretary

13 January 1986

Dear Robin,

WATER PRIVATISATION - WHITE PAPER

The Prime Minister has seen the draft White Paper on Water Privatisation attached to your Secretary of State's minute to her of 22 December. She has no comments on it.

I am copying this letter to Private Secretaries to members of the Cabinet, to Lord Denham (Chief Whip, House of Lords), Murdo Maclean (Chief Whip's Office) and to Michael Stark (Sir Robert Armstrong's Office).

Yours ever
David.

(David Norgrove)

Robin Young, Esq.,
Department of the Environment

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DRAFT WHITE PAPER

PRIVATISATION OF THE WATER AUTHORITIES IN ENGLAND AND WALES

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1: INTRODUCTION

1. On 7th February 1985, the Minister for Housing and Construction announced in the House of Commons that the Government would examine the prospects for privatisation in the water industry. At the beginning of April, he sent a discussion paper to the chairmen of the water authorities and to others. After studying the responses and examining the issues, the Government has now decided to transfer the ten water authorities in England and Wales to private ownership.

2. This White Paper sets out the reasons for the decision and the basis for the proposals which the Government intends to put to Parliament in the form of legislation as soon as possible.

Why private ownership?

3. The Government's main reason for privatising the water authorities is the benefit their customers will ultimately gain in the following ways:

- * the industry will be able to take advantage of enterprise and innovation, and will become more efficient both by building on the gains of recent years and by more cost-saving investment;
- * there will be the opportunity for wide ownership of shares both among employees and among local customers;
- * employees will be more closely identified with their business, and motivated to ensure its profitability;
- * Managers will be able to manage free of Government intervention and they will be released from the constraints on financing which public ownership imposes;

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* there will be greater clarity in the requirements of public policy, particularly in environmental protection, the arrangement for which will be improved.

4. The Government has therefore decided to seek from Parliament the necessary powers to turn the water authorities in England and Wales into water service public limited companies (WSPLCs) and to transfer them to private ownership as rapidly as possible. Aerospace, motor manufacturing, oil, ports, road transport, shipping, telecommunications and other businesses have already been privatised; plans for airports, airways, buses and gas have been announced. Water will be a substantial addition to the privatisation programme, setting free 10 major businesses and adding a further 51,000 jobs to around 400,000 that have already been transferred to the private sector.

Who will benefit from private ownership?

5. The interests of customers, employees, the environment and the nation will not only be safeguarded by privatisation but will also benefit from it.

6. Customers will benefit from the prospect of higher standards, greater competition between regions to offer the best service, a more soundly-based charging system to pass on efficiency savings and keep bills down, and the opportunity to hold shares in the undertaking. There will be protection from monopoly power, and better consultation.

7. Employees will benefit from employee shareholdings, closer identification with their businesses, greater job satisfaction, better motivation, and the prospect of the rewards that enterprise has brought to those who work

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for other industries that have been privatised. Pension rights earned before privatisation will be safeguarded.

8. The environment will benefit from a new Government involvement in the setting of objectives for each river and estuary, defining the standards to which it is to be maintained or improved.

9. By setting explicit objectives for rivers, for drinking water quality and for other service standards before the authorities are sold into private ownership, the Government will give prospective shareholders the basis for a proper assessment of the nature and worth of the water authorities' business.

10. The nation as a whole will benefit from higher standards and greater efficiency in the provision of services which are of key importance to public health, from greater job opportunities arising from new enterprise, and higher earnings through successful endeavours overseas.

The new shape of the water industry

11. In considering the form in which to privatise the water industry, the Government has firmly concluded that the principle of integrated river-basin management - a single body controlling water and sewerage in each river-catchment - has worked well since it was introduced by the Water Act 1973, and should be retained. Hence the water authorities will be privatised on the basis of their existing boundaries and functions, with the single exception of the financing of land drainage and flood protection, which will remain in the public sector. The Government intends that the water authorities should continue to carry out their responsibilities for the management of rivers, control of

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pollution, fisheries, environmental conservation, recreation and navigation.

12. Water authorities regulate other users of their water including abstractors of water and dischargers of waste. At the same time the authorities are themselves major abstractors and dischargers. There will continue to be strong safeguards and a proper channel of appeal to ensure that the new water undertakings (WSPLCs) act evenhandedly.

13. To protect the interests of the customer, the Government will appoint a regulator to prevent the abuse of monopoly power, to see that standards are observed and to be responsible for consumer consultation. The charges of the water authorities will also be regulated.

14. The Government also intends to modernise existing water and sewerage law much of which has its origins in the 19th Century, and parts of which are unclear and outdated.

15. The proposals in this White Paper offer an opportunity to the water authorities. The Government is sure they will rise to it and put a major national industry onto a new and dynamic basis, while protecting the interests of all who use water, and safeguarding public health and the environment.

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SECTION 2: THE WATER AUTHORITIES NOW

Integrated River-Basin Management

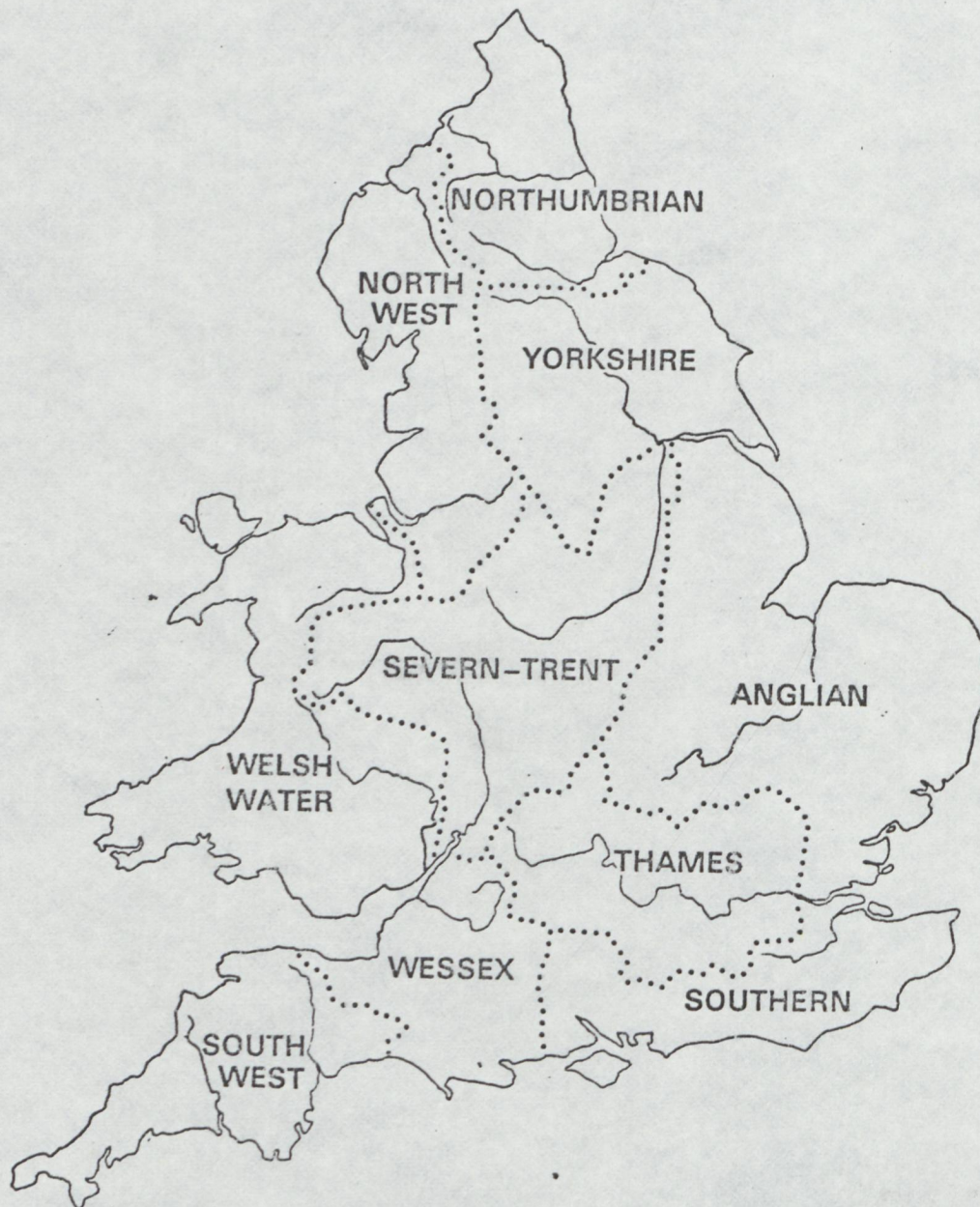
2.1 The nine English regional water authorities and the Welsh Water Authority were set up under the Water Act 1973 on the principle that a single body should plan and control all uses of water in each river catchment. Previously, nearly 1,600 local water undertakings had been responsible for water services. There were inevitable difficulties and conflicts of interest and the water authorities were created to provide a more workable mechanism, taking over the functions of water supply and sewerage and responsibilities for water-resource planning, pollution control, fisheries, flood protection, some navigations, water recreation and environmental conservation. The area of each authority comprises one or more river basins, and the boundaries of each, shown on the map opposite, were drawn to make water planning easier catchment by catchment, irrespective of boundaries drawn for other purposes.

2.2 The River Thames is a classic example of integrated river basin management. The catchment area supports 3,500 abstractions - 1,200 for agriculture, 500 for water supplies (by statutory water companies and the Thames Water Authority itself), and 1,800 for industrial and other uses. The river receives 6,550 discharges from industry and 450 discharges from the Authority's sewage treatment works. In addition, the river is used for fishing (193,000 rod licences are issued annually) and for boating (19,000 boats are registered and a million passages a year recorded through the river's 45 locks). The river and its tributaries are so regulated and managed that discharges do not pollute water supplies and abstractions do not so lower the level of the river as to compromise natural life or the enjoyment of those who get their recreation on the river.

2.3 Because the water authorities control and regulate all the uses to which their rivers are put, they have been able to satisfy all requirements even in conditions of extreme difficulty, and they have been able to plan for increasing demands at least cost and without detriment to existing users. Thus during the drought of 1984, when rainfall was 45% of the average

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WATER AUTHORITIES IN ENGLAND AND WALES



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in the months April to July, the South West Water Authority, with one of its three strategic reservoirs still under construction, went to exceptional lengths to tap new resources, to reduce river levels, and to pipe water from one river basin to another; the public exercised exceptional economy, and although certain inessential uses of water were prohibited the Authority were able to maintain supplies without resort to water rationing in any form, and without detriment to the rivers themselves and the natural life and uses they support. Water shortages of a different kind will be overcome by the Southern Water Authority by another application of the principle of integrated river basin management. Through its control of both abstractions and of pollution, the Authority will meet increasing demands for water in East Kent and East Sussex not only by taking more water from the North Downs aquifer, but also by improving the quality of the River Medway through more stringent consents for industrial discharges, allowing more water to be taken from it and transferred across country.

2.4 The catchment-based structure of the water industry has worked well in practice, and has been highly praised throughout the world as being a good and cost-effective model for other countries to follow. It is the main reason why the Government intends to transfer water authorities to private ownership much as they stand.

Constitution and Functions

2.5 The water authorities are large undertakings, employing some 51,000 people. Their capital investment for 1986/87 is expected to be in excess of £900 million. They have an annual turnover of about £2,600 million and assets including about 137,000 miles (220,000 kilometres) of water mains, 140,000^{miles} (225,000 kilometres) of sewers, 6,500 sewage works and 1,000 main water works.

2.6 Until 1983, the authorities were run by large boards with a majority of local authority representatives. The Water Act

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1983 set up the present boards, which are smaller and more businesslike. All members are appointed by Ministers.

2.7 As shown in Figures 1 and 2, the authorities' capital and operating expenditure is largely applied to their main functions of water supply, sewerage and sewage treatment.

2.8 More than 99% of the population in England and Wales is connected to a public water supply. The water authorities supply about 75% themselves, the remainder being supplied by the privately-owned statutory water companies, who act as agents for the authorities.

2.9 Before the 1973 Water Act, local authorities built and maintained the sewers, and in most areas district councils continue to do so as agents of the water authorities. It is the water authorities, however, who are ultimately responsible for sewers and for the safe disposal of sewage and other waste water; they own the sewers, and themselves deal with sewage treatment and disposal.

2.10 However, water authorities not only supply water and dispose of sewage; they also regulate other water users. They control abstraction, primarily through licences, and their consent is needed to the discharge of effluent into their waters. They grant licences and consents in the light of the standards of quality for each stretch of river and coast as part of the national water policy. The Secretary of State approves water authorities' own discharges and hears appeals against their decisions on abstractions and discharges by others in the few cases where these are made.

2.11 Water authorities also have responsibility for a number of other water-related activities ^{environmental} -/conservation, fisheries, navigation, flood defence and land drainage. These represent only 10% of the authorities' expenditure. They are, nevertheless, important areas of activity, and part of the integrated management of river catchment areas.

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OPERATING EXPENDITURE: WATER AUTHORITIES

ENGLAND & WALES INC LAND DRAINAGE 1984/5

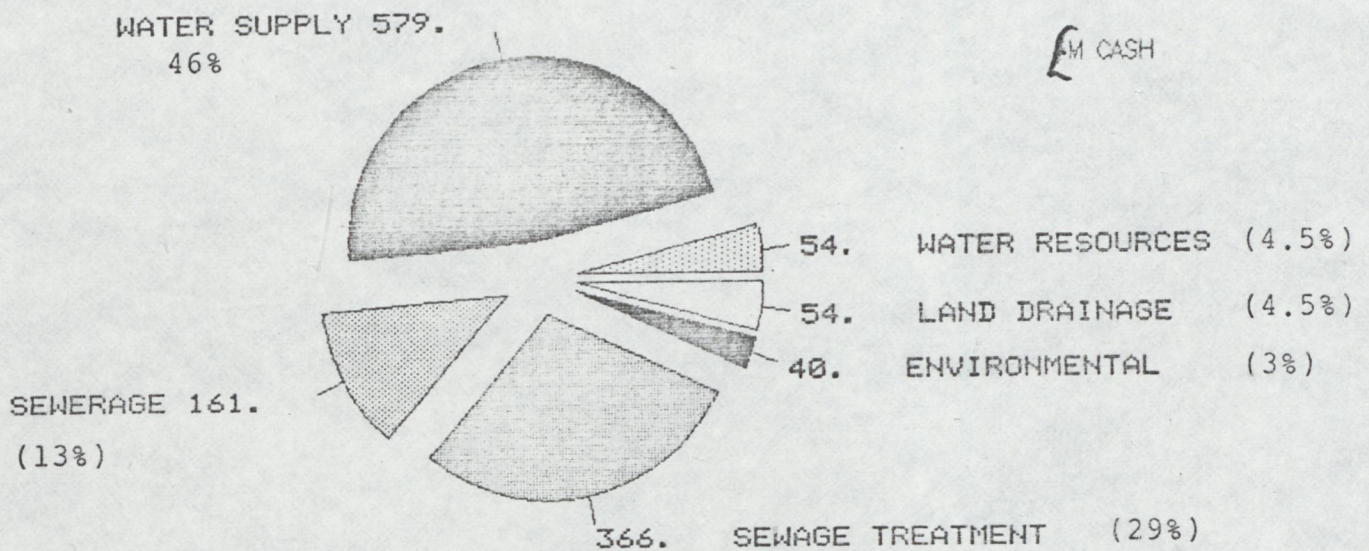


Figure 1

CAPITAL EXPENDITURE: WATER AUTHORITIES

ENGLAND & WALES INC LAND DRAINAGE 1984/5

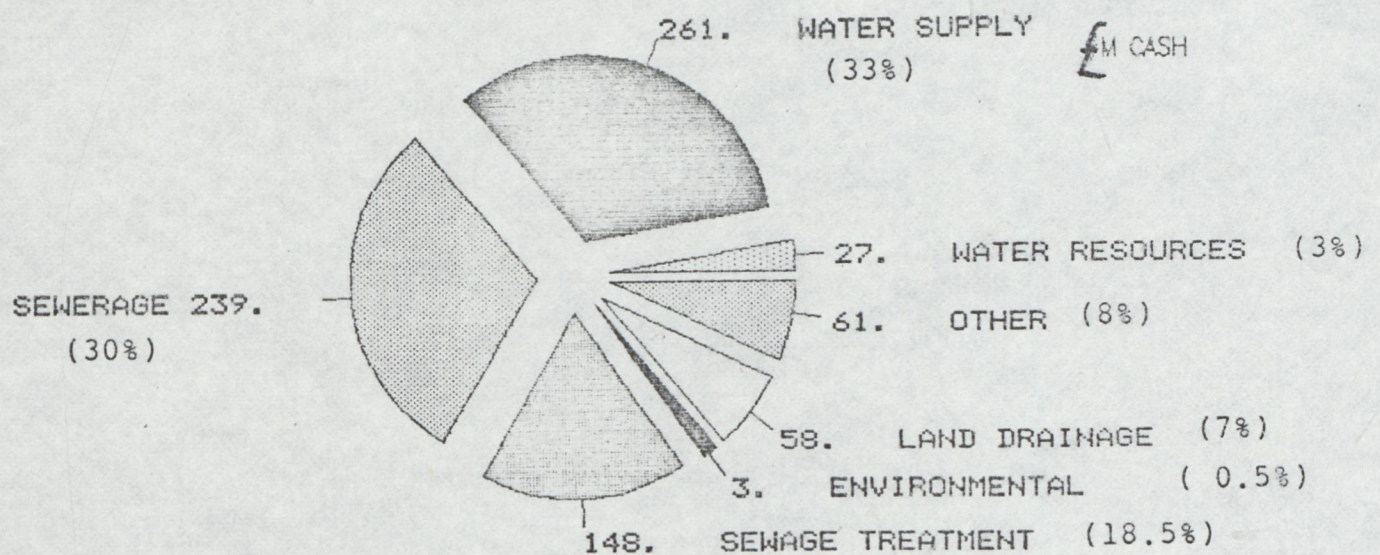


Figure 2

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Achievements since 1974

2.12 The water authorities' ability to operate on the basis of integrated river-basin management and to plan and develop water resources regionally has enabled them to improve their services and to keep pace with rising demand.

- Water Supply

2.13 Between 1961 and 1971, domestic water supply rose from 2,361 million gallons (10,733 million litres) a day to 3,114 million gallons (14,157 million litres) a day. By 1984, it had increased to 3,615 million gallons (16,434 million litres) a day. In addition, about 6,600 million gallons (30,000 million litres) a day were abstracted in 1984 for non-domestic purposes, about a third of this being used by the Central Electricity Generating Board, mainly for cooling.

2.14 The authorities' improved ability to cope with demand for water was demonstrated by their performance in the droughts of 1976 and 1984. In 1976, Anglian Water were able in a period of weeks to lay a main from Rutland Water to the River Witham, establish a new treatment works at Etton, and reverse the flow of the Ouse to increase supplies from Grafham. The drought also taught the industry some useful lessons, so that by the time of the 1984 drought many schemes for safeguarding water supplies had been completed and more are in hand. The Yorkshire Water Authority, for instance, had developed a regional water grid which allowed them to transfer supplies to areas of acute shortage. All the authorities mobilised resources of finance, management and engineering to tackle shortages at a speed which would have been impossible before the 1973 Water Act.

- Water Quality

2.15 The quality of water supplied has also been improved. In the Summer of 1985, in accordance with the Drinking Water Directive of the European Community, the Government completed

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a review of the quality of all drinking water supplies and an assessment of the shortcomings. 90% of supplies meet all the requirements of the Directive. The water authorities are putting right all defects arising from lead or microbiological pollution.

The Government has granted derogations within the terms of the Directive for concentrations of nitrates, manganese, iron and others, where it is satisfied that there is no risk to health.

- Sewerage

2.16 Much has been said about the need for heavy investment in the renovation of Britain's sewers. Properly laid, however, sewers can last for a very long time, and about half the 140,000 miles (225,000 kilometres) of sewers in England and Wales have been built since the Second World War. Only .. per cent predate 1914. Sewers currently fail at a rate of 26 per 1,000 miles (16 per 1,000 kilometres) per year. Three-quarters of all failures affect sewers less than 9 inches (230 mm) in diameter, and most are due to blockages rather than collapse. In the last decade the industry has developed sophisticated techniques of sewer survey and renewal by remote control. It has become orthodox practice to identify critical sewers and to locate those where preventative maintenance is cost-effective. The Water Research Centre's Sewer Rehabilitation Manual has codified the best available techniques for dealing with sewer dilapidations and the problem now appears to have been reduced to manageable proportions.

- Pollution Control

2.17 River quality lies at the heart of the water authorities' performance of their functions. The authorities have tackled pollution partly by controlling their own discharges and partly by controlling the discharges of others. The discharge of raw sewage into rivers such as the Tyne and Mersey has been a major cause of pollution. In other areas, the sewage works inherited by water authorities were often small, outdated and inefficient. Where possible, authorities have updated or replaced them in projects such as Severn-Trent Water Authority's Black Country

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strategic sewage treatment scheme, which will further improve the quality of the River Tame. The North West Water Authority is in process of cleaning up the Mersey by means of a 25-year, £2.5 billion scheme, combining higher investment in sewage works, increased sewerage capacity and a progressive tightening of consents for industrial discharges. A similar programme of works has already improved the quality of the Tyne estuary.

2.18 The last national survey of river quality showed that grossly polluted rivers had been reduced in length from 792 miles (1,274 kilometres) in 1975 to 506 miles (814 kilometres) in 1980, while lengths of "grossly polluted" and "poor" tidal rivers were reduced by 21% and 47% respectively in the same period. A new survey, to be held in 1986, has just been announced.

2.19 Many authorities are taking action to prevent the pollution of bathing waters by sewage, on which standards are laid down by the EC Directive on the Quality of Bathing Water (76/160/EEC). For instance, Wessex Water has built a £33 million sea outfall to free the beaches around Weymouth and Portland from pollution and to prevent flooding. The cost of the scheme had been beyond the means of the predecessors of Wessex Water. Welsh Water has recently completed a long sea outfall at Tenby, costing £2.2 million, and plans to spend a further £75 million on similar schemes by the turn of the century in order to reduce the pollution of coastal waters and improve popular beaches.

Operating Efficiency and Financial Performance since 1979

2.20 Although the reorganisation of the industry following the 1973 Act enabled water authorities to make significant improvements in the service provided, it is only in the years since the present Government took office that they have made comparable improvements in their operating efficiency and financial performance.

2.21 Consultants who reviewed the water authorities' budgets for 1981/2 and 1982/3 found much scope for reducing costs without damaging standards of service. In addition, the Monopolies

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and Mergers Commission reported on the Severn-Trent Water Authority in 1981 and has published three further reports on aspects of the water industry, which contained valuable suggestions for improvement. The water authorities have responded positively and the Government has agreed performance aims which have reversed the rising trend in operating costs. Targets for further cost reductions by 1986/7 have been agreed. As the more obvious opportunities for cost-savings are used up, further cost reduction is coming increasingly to depend on effective exploitation of new technology. Nearly every authority has streamlined its headquarters and many have cut the number of operating divisions, sometimes to half the previous number. Table 1 shows the number of staff employed by the authorities over the period from March 1976 to September 1985. Between 1976 and 1979, numbers employed in the ten authorities rose from 60,649 to 63,204. By September 1985, the figure was down to a little over 51,000 - a saving of nearly one-fifth since 1979. As indicated earlier, and as levels of service indicators (paragraph 2.25) show, this has been achieved while at the same time maintaining or improving standards of service.

2.22 The improvements that the Government has encouraged the authorities to make in their financial performance are indicated by the degree to which they have become self-financing. Previously, internal finance contributed little to capital expenditure, which had been sharply reduced in the late 1970s (Table 2). The separation of water charges from general rates had focussed public attention on them, and had called in question the efficiency of the authorities. Since 1979, the Government has stimulated them to more effective financial management by requiring the authorities to accept the discipline of making adequate depreciation provision, and of achieving real profits.

2.23 In 1980/81, the authorities' capital expenditure was £694 million, of which 41% was financed from borrowing. For 1986/87, their planned capital expenditure will have risen to £942 million, of which only 10% is to be financed from borrowing. The authorities are moving towards a position where they are substantially self-financing, and capable of standing independently as commercially viable entities.

WATER AUTHORITY - MANPOWER (at 31 March each year)

	<u>1976</u>	<u>1979</u>	<u>1982</u>	<u>1985</u>	30 September <u>1985</u>
North West	9005	9379	8782	8166	8096
Northumbrian	2279	2453	2151	1759	1707
Severn-Trent	10464	11240	10502	9269	9080
Yorkshire	6340	6338	6506	5835	5680
Anglian	6726	6978	6700	5549	5388
Thames	11810	12061	11753	9089	8981
Southern	4120	4207	3948	3336	3281
Wessex	2260	2425	2291	2050	2029
South West	2315	2534	2276	2023	1989
Welsh	5330	5589	5677	4709	4799
<hr/>					
Total	60649	63204	60586	51785	51030
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Note Figures prior to 1979 were calculated on a slightly different basis to later figures.

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WATER AUTHORITY CAPITAL EXPENDITURE

TABLE 2: £ million cash

Service	1975/6	1978/9	1981/2	1984/5	1985/6* (est)
Water resources	35.7	56.3	41.3	27.6	33.0
Water supply	128.8	148.8	193.9	261.4	277.0
Sewerage	} 308.8	161.0	191.5	238.8	267.0
Sewerage treatment and disposal		111.4	148.5	147.5	167.0
Environmental	1.6	3.5	5.0	3.3	6.0
Other water services	9.4	17.2	31.8	61.1	68.0
Land drainage and flood protection	27.0	52.5	84.4	58.0	48.0
TOTAL	511.3	550.7	696.4	797.7	866.0

* Note: 1985/6 total based on water authorities' latest estimates. Distribution by service is based on 1985 plans and given only as a guide.

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Investment Needs and Plans

2.24 As Figure 3 shows, the principal investment carried out by the authorities is that needed to sustain their business and replace assets as they wear out or become obsolete. The water industry has net assets of about £500,000 per employee at replacement cost, so capital investment in renewing and upgrading the assets is important.

2.25 In order to identify deficiencies in the level of service provided, authorities measure their performance against 25 indicators agreed with Government. Likely overall investment needs are:

a. Water resources: Water resources in most regions will meet demand (expected to grow by about 1% pa overall) until the year 2000 and beyond. But more water is needed in the South West (Roadford scheme in Devon), East Midlands (Carsington scheme in Derbyshire), in the Thames area and in Kent (as described in paragraph 2.3). Water resource schemes account for less than 5% of the annual investment of water authorities.

b. Water supply: Water mains can deteriorate and overloading demands investment in some areas. The authorities will be spending about £345 million pa on water supply investment in 1986/87, and the Government is satisfied that progress is being made in dealing with the problems that have been identified.

c. Sewerage: Investment has increased from about £200 million in 1980/81 to about £325 million in 1986/87 and the Government anticipates expenditure at the present level or above continuing for the foreseeable future, although investment in treatment and disposal will be affected by future quality objectives for rivers and coastal waters.

d. Flood protection and land drainage: In the next four years, capital expenditure of £200-250 million will be

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CAPITAL EXPENDITURE BY PURPOSE

PERCENTAGES

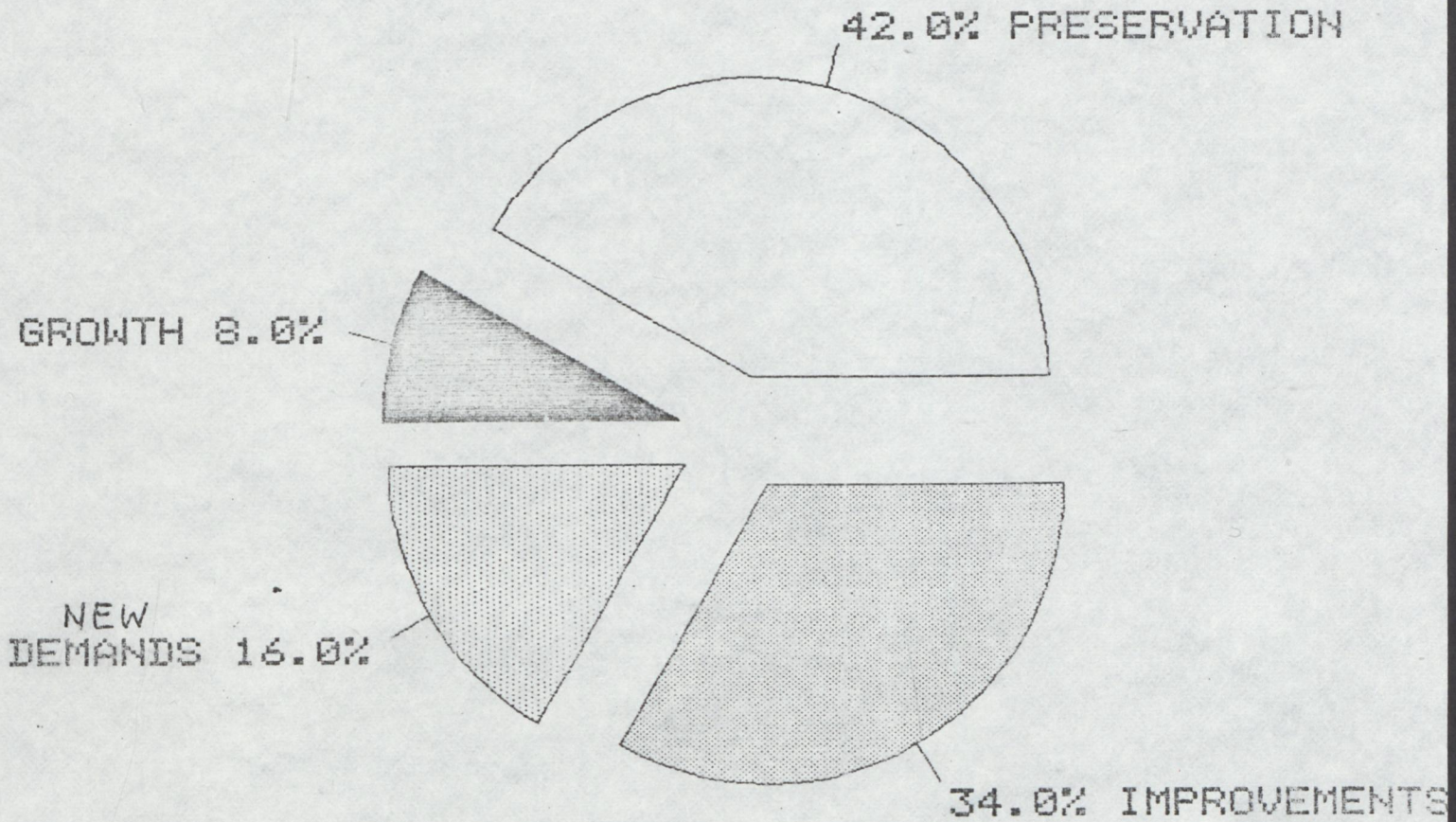


FIGURE 3

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made to prevent flooding. This level of spending should continue into the 1990s as many sea-walls need rebuilding. The financing of flood protection will, however, remain in the public sector.

e. Fisheries, conservation, recreation, etc:

Investment at the 1986/87 level of about £5 million pa should continue.

Investment at current levels should, therefore, be broadly sufficient for the preservation, restoration and improvement of existing assets, which is the main element of water authorities' expenditure, as well as to accommodate foreseen growth and new demands. WSPLCs will, however, be free of public expenditure constraints, and therefore able to plan investment at a higher rate, if they wish, for instance in improving levels of service more rapidly than would otherwise have been possible.

2.26 As this Section shows, the water industry in England and Wales has been transformed from a hotch-potch of undertakings, whose organisation owed more to history than logic, into ten modern businesses. The finance of the industry have strengthened beyond recognition, worthwhile investment has increased, efficiency and performance have substantially improved. This raises the question, why does the Government think that the time has now come to privatise the water industry? The answer is that there is a limit on the extent to which further improvements can be achieved in the public sector. State ownership is not conducive to enterprise or customer service, and privatisation is necessary if customers are to get full benefit from the changes pursued since 1973.

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SECTION 3: STRUCTURE OF THE PRIVATISED WATER INDUSTRY

3.1 Once privatised, water undertakings will be able to organise their affairs without reference to central Government and, in particular, will be free to focus on their primary responsibility - providing a service to their customers whilst safeguarding the environment. Privatisation should lead to improved standards, greater efficiency, and a better allocation of resources within the water industry. Provided the interests of customers are fully protected, and Section 4 of this White Paper sets out how the Government intends to do this, the water industry, their customers, and the nation as a whole should all benefit.

3.2 In developing its plans for privatisation, the Government has thought it right to take as its starting point the present organisation of the water industry and not to lose the benefits of the 1973 and 1983 Water Acts, described in Section 2. Subject to the necessary legislation, it has decided, therefore, to convert existing water authorities into 10 new water services public limited companies (WSPLCs) and to transfer them to the private sector with their present functions largely intact. This Section describes the reasons for the organisational and company structure chosen together with those changes to the industry that are proposed, and why the Government has rejected the alternative of franchising.

Scale of Operation

3.3 The Government has considered whether the benefits of unified river basin management could be retained if water authorities were to be sold in operational units smaller than the present authorities - say, based on their present divisional structure. It is not convinced that there would be any advantage in this approach. On the contrary, the size of the authorities as presently constituted allows both the planning and development of water resources on a regional basis and the fullest use to be made of scarce professional skills. Some of the benefits have been illustrated in Section 2 by projects such as the Lancashire conjunctive use scheme, the Yorkshire grid, and the South West trunk main.

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Statutory Companies or PLCs

3.4 At present there are 28 statutory water companies supplying water to about a quarter of the population of England and Wales. They provide a precedent for private-sector operations in this industry. The Government has considered whether it would be appropriate for the water authorities to be privatised as statutory companies rather than as public limited companies. It has concluded that this would not be the better course. To establish statutory companies is an out-dated method of forming a business. Powers necessary to protect investors are already provided by general company legislation. Writing a privatised water authority's constitution into an Act would be unnecessarily restrictive, whereas PLC status under the Companies Act 1985 would provide a framework within which enterprise can flourish while affording all the normal protection of company law, and automatically subject to any changes that may be made in company law. If necessary, additional safeguards can be made, as in previous privatisations, by the Government's holding a "special share" for purposes defined in the articles of association.

Statutory Water Companies

3.5 Under the Water Act 1973 the statutory water companies supply water in their areas not in their own right but as agents of the water authorities. Financial controls are written into their statutes, limiting the maximum rate of dividend, the size of reserves, and the amount of balances carried forward from one year to another. The Government sees advantage in ending the agency link between the water companies and the authorities once they become WSPLCs, and in bringing the companies under the same form of financial regulation as is proposed in Section 4 for the WSPLCs. At the same time, the companies would be able to convert to PLC status, and take advantage of the greater scope for enterprise this would offer them. The Government will be discussing these proposals further with the water companies.

Sewerage

3.6 The local authorities have proposed a return to the pre-1973 situation, when they were responsible in their own right for sewerage. The Government does not believe that this would be in the best

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interests of efficiency nor would it be consistent with the integrated management principle. It would blur the link between investment in sewers, the efficient development of sewage treatment and disposal and wider environmental considerations.

3.7 It would be inconsistent with the aims of privatisation for the district councils to continue to have the presumptive right to act as sewerage agents, which they enjoy under S15 of Water Act 1973. The choice of agents, or whether to carry out the work in-house should rest with the privatised authorities themselves.

Land Drainage and Flood Protection

3.8 Land drainage and flood protection, in which the emphasis nowadays is mainly on defences against river and coastal flooding, involve capital and maintenance expenditure of around £100 million pa. Their non-commercial nature would make it difficult to vest them in private sector bodies having no commercial incentive to carry out works desirable in the public interest. On the other hand these activities are an integral part of the unified system of river basin management and it would be counter-productive to divorce them from other WSPLC activities.

3.9 The Government proposes to reconcile these opposing ideals by funding and coordinating flood defence activities through special public bodies which will make the fullest possible use of WSPLC expertise, perhaps by employing them as managing agents under contractual arrangements based on levels of service data. Maximum use of competitive tendering for works is envisaged to protect the public purse.

3.10 The detailed arrangements

will be considered as part of the review of flood protection and land drainage being undertaken in the light of responses to the Green Paper (Cmd 9449) issued in March 1985.

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Alternative Ways of Privatising

3.11 In responding to the discussion paper issued by the Government in April 1985, some organisations advocated privatisation only of the main functional activities (water supply, and sewerage, sewage treatment and disposal), perhaps with the retention of regulatory and non profit making functions in the public sector. Their objection to the privatisation of water authorities as a whole is based on three main considerations:

- they are natural monopolies, offering no scope for direct competition except at the margins;
- they have important regulatory functions, concerning the abstraction of water from and discharge of effluents to rivers and aquifers;
- activities such as recreation, environmental conservation, navigation and fisheries are loss-makers.

The Government, however, believes that any advantages in partial privatisation are more than outweighed by the damage it would do to integrated river basin management, and that the problems identified can be better dealt with in other ways. The issues are discussed more fully below.

Franchising and Competition

3.12 One aim of the alternative model put forward is to introduce competition by requiring the water authorities to franchise out the whole of their main operational functions, for which potential franchisees would bid - a system which is widely practised in France. It is difficult, however, to see any real competition arising from this in any effective form. Where the arrangements involve the ownership of the assets by the franchisee, the long life of the water authority assets would mean that the contract would have to run for as long a period, say 25 years, as that it is envisaged the WSPLCs would be licensed for (paragraph 4.8). Operating franchises, where the franchisee leases the assets from the public authorities could be renewed more frequently - at up to 10 year

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intervals - but neither the owner nor the operators is well placed to maintain, renew, or replace the capital assets in an economical way.

3.13 The Government does not rule out franchising or contracting out by the WSPLCs themselves but it does not propose to put them under any duty to do so. The regulatory system described in Section 4 provides incentives for the industry's managers to find the most efficient ways to achieve standards and make profits. The motivation is not dissimilar to that engendered by direct competition, and they can be expected to franchise operations which are more effectively carried out under franchise.

Regulatory Responsibilities

3.14 In safeguarding water resources, the authorities impose costs and constraints on other parties, while at the same time being actual or potential dischargers and abstractors themselves. For these reasons, it has been argued that these functions should be retained in the public sector. To do so would, however, undermine the concept of integrated river-basin management and prevent the sort of schemes described in paragraph 2.3. The existing rights of appeal to the Secretary of State on individual cases will be reinforced by a new statutory basis of regulatory control described in Section 5. This will ensure that WSPLCs deal with abstractions and discharges even-handedly and in the public interest.

Environmental Services

3.15 The third argument put forward for retaining parts of the water authorities in the public sector is that their responsibilities for fisheries, pollution control and monitoring, navigation, recreation and amenity services are generally not commercial. All these services receive some support from the Environmental Service Charge. The Government considers that these activities should be continued, but that as the scale of expenditure upon them amounts to no more than 2.5% of any authority's income, and some authorities collect less than 1% of their income through it, their continuation is no barrier

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to the transfer of the authorities to the private sector. It would be appropriate for them to be financed from the charges which WSPLCs make for their main services, and paragraph 4.23 below describes how the amount of that contribution could be regulated.

3.16 The Government proposes to make only those changes to the structure of the industry which are consistent with the private sector status of the WSPLCs, or which are necessary to place that part of the industry that is already in the private sector - the statutory water companies - on an equivalent footing. The safeguards described in Sections 4 and 5 avoid the need for a fundamental restructuring of the industry, and enable the existing advantages of integrated, regional management to be retained.

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SECTION 4 : REGULATION AND CUSTOMER PROTECTION

The Need for Regulation

4.1 The water authorities are for the most part natural monopolies, the large investment required in creating their infrastructure making it more efficient for the services to be provided by one company than by several. The services they provide are also essential to public health, as well as to the protection of the environment. Safeguards are obviously therefore, necessary to prevent the WSPLCs from overcharging or providing a low standard of service, while **not** inhibiting their enterprise.

4.2 The water industry differs both from telecommunications, where there is more scope for competition which the Government is encouraging, and from gas, which has to compete with alternative sources of fuel. New technology is unlikely to increase the scope for competition in water, as it has done for telecommunications, and regulation of prices will remain a permanent feature of the industry.

4.3 The water industry does not, however, consist of a single authority, but ten. Although each is solely responsible for the provision of main services within its area, there is considerable scope for competition in services such as consultancy. The Government would expect WSPLCs to expand such entrepreneurial activities considerably. In addition, it hopes to devise a system of regulating main service activities which will encourage competition between authorities for funds on the capital market.

4.4 As with telecommunications and gas, the Government intends that the main water services should be regulated by a Director General of Water Services, through licences granted to the WSPLCs. The terms of these licences would limit what consumers could be charged and set requirements as to the standards of service to be provided. The Director General's main duty will be to balance the interests of the customers

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and shareholders. He will also be responsible for setting up and maintaining the consumer consultative arrangements described in paragraph 4.24. In considering the elements of the regulatory system the Government has been assisted by a report, "Economic Regulation of Privatised Water Authorities", commissioned from Professor Littlechild of Birmingham University, which is being published at the same time as this White Paper.

Operating Licence

4.5 The licence would formally designate the WSPLCs as bodies licensed to conserve rivers and other water resources, and to make them available for the whole range of uses to which fresh waters are ordinarily put, to do so for profit, but with attendant obligations within the limits of the regulatory system. The licence will not replace existing statutory duties, but it will amplify those duties where necessary.

4.6 The purpose of the licensing system is that once the charging limit and the performance standards have been set in the licence, the principal incentive for the owners and the managers should be the opportunity to make profits. By making a profit, the management of the company will satisfy its shareholders, and by meeting the prescribed standards of performance it will satisfy its customers. Managers will then be driven by the normal commercial motivation of the private sector. And apart from the disciplinary measures provided for in the licence, and applied by the Director General, they will be subject to the disciplines of the capital market, including the possibility of management change.

4.7 WSPLCs, like other private technology-based organisations, will require a sound research and development capability. The licence would require WSPLCs to make an adequate contribution to research and development, including that directed at environmental and long-term issues.

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4.8 Given the long life of assets created by WSPLCs, the licence itself would need to run for a considerable period of time (the licence for British Telecom and that proposed for British Gas are both for 25 years), although the price formula would be subject to periodic review within that period (5 years in the case of British Telecom and British Gas). Target standards of service would need to be agreed over a rather longer period than prices, but interim stages could be set to coincide with price reviews. There would be provision for interim changes to be agreed between the Director General and the licensee under special circumstances. In the absence of agreement, changes could be referred to the Monopolies and Mergers Commission.

4.9 The terms of the licence would be enforceable in the Courts. In extreme circumstances the licence could be revoked, and the company taken over/by ^{- for example} another WSPLC. The Government will also need to retain powers to secure adequate contingency schemes for responding to emergencies and to require civil defence provision.

4.10 The relationship between the Director General and the Monopolies and Mergers Commission and the Director General of Fair Trading will need to be clearly defined, and the existing powers under the competition legislation in relation to water authorities reviewed.

Limiting of Charges to Customers

4.11 There are various ways in which charges to customers can be limited. The method with which the water industry is most familiar is that applied to the statutory water companies. The principal control upon them is a limit to the rate of dividend paid to their ordinary shareholders. Profit controls of this kind provide no incentive to efficiency, however, since increases in expenditure are allowed to feed through directly into prices.

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4.12 Price controls such as the RPI-X formula applied to British Telecom are more attractive in that, once set they do provide an incentive to efficiency. Price control will need to cover the main services of WSPLCs, water supply and sewerage, in which they have a monopoly. It is for consideration whether a single RPI-X formula should be applied to both main services, or whether separate formulae should be applied to each, or even to different tariffs. The more the application of the price control formula is differentiated, the more protection is provided to individual groups of customers. On the other hand, a single formula has the advantage of simplicity, and if it were set to reflect changes in the average performance of the industry, it would provide an additional incentive by passing on to the customer the benefit of the average cost reduction, while allowing authorities of above average efficiency to retain the additional profits earned by their performance.

4.13 The controls will not need to be applied to services where direct competition is possible. The Government would like to see WSPLCs expand their entrepreneurial activities, such as the provision of consultancy services, particularly overseas. Authorities are already beginning to enter the market for customer services, such as meter installation and pipe repairs. It is possible that WSPLCs could compete to provide other WSPLCs with services such as laboratory analysis or sewage treatment if these were franchised out. It is even possible that WSPLCs could compete directly for customers situated on the borders of their areas.

4.14 However, it would not be right to allow competitive kinds of business to be sustained by hidden support from the customer of the main services. So it will be necessary to ensure that commercial business is run at arm's length from the main services. If the main services are carried out by a subsidiary company separate from those carrying out the unregulated, non-monopoly business, the Director General, the competitors and the public will be able to satisfy themselves that there is no unfair subsidisation.

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Service Standards

4.15 The second area for regulation is service standards. Water authorities already have a number of duties imposed on them by law but these are of a general character. It is intended that statutory standards, relating to public health and environmental protection should continue to be set by the Government. For drinking water, standards are laid down in the European Community Directive on the Quality of Water intended for Human Consumption (80/778/EEC). Implementation of its standards has rested on administrative interpretation of the water authorities' duty to supply "a wholesome water" (as set out in DOE circular 25/84). The legal basis of these standards will be clarified as part of the privatisation legislation; but that will not alter the standards themselves or the departures from them which the Government has already approved; in future, as now, departures from them would only be possible in exceptional circumstances with Government authorisation.

4.16 The standards of discharge of effluent from sewage treatment works are already matters for Government decision in the light of water quality objectives, which the authorities agree with Government. Section 5 sets out the Government's proposals for putting the water quality objectives on a statutory basis; again this change is a change of legal form, to clarify the framework within which standards of performance will be set.

4.17 In addition to their statutory duties, the water authorities already publish details of their performance against a set of ^{twenty-five} "levels-of-service indicators" covering such matters as response time for new connections, reliability of water supplies and the incidence of sewer failures. Some of these are not consistently evaluated between authorities, and not all are of equal importance, but they nevertheless provide a basis for setting targets for key aspects of service quality, and for monitoring progress, which as stated in Section 2 has been positive against almost every indicator in each area. It could be a

requirement of their licence that WSPLCs should continue to publish their performance against such indicators. For some indicators, specific targets could be set by the Director General. These together with the statutory standards set by Government, would become a basis for the improvement of standards over a period of, say, 15 years with interim levels of attainment set for stages in between. Only certain indicators are suitable as the basis of common verifiable targets, but setting too many targets would lessen the weight that could be attached to any one of them.

4.18 The remaining levels of service indicators could be subject to targets set and monitored by the WSPLCs themselves, in consultation with their Consumer Consultative Committees (see paragraph 4.24).

Form of Regulation

4.19 There is a considerable degree of scope in how the price controls and target standards could be applied to the WSPLCs. The choice is between:

- i. tailoring standards and price controls individually to each authority, taking account of its geography and investment needs; and
- ii. setting uniform standards and price controls throughout the industry, variations in their situation being reflected in their capital structures and flotation prices.

The first allows for greater flexibility, but would involve the Director General in complex and probably continuing negotiation with each WSPLC, making it difficult to judge the success or failure of an individual company, and leading to the risk that the Director-General would usurp some of the management's functions. It would also be difficult to

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demonstrate even-handedness between the regulated companies. The second method has the advantage of simplicity once it is in operation. By encouraging direct comparisons between authorities by investors, it would also promote efficiency by means of competition. The threat of takeover would become as much a spur to poor performers

as any sanctions threatened by the Director⁴General himself. However, to be effective the standards and price controls would have to last for 5 to 10 years and considerable care would be needed in setting them at the right level. Factors affecting likely performance against targets will, of course, be made plain in any prospectus at the time a WSPLC is offered for sale.

Charges

4.20 While the rate of increase in the average level of water charges will be governed by the formula described in paragraph 4.12 and controlled by the Director General, the general principle now expressed in Section 30 of the Water Act 1973 that charges for the Water Services should be cost-related and non-discriminatory between classes of customers will still be applicable. Details of charging practice will need to be settled.

4.21 The option of being charged by meter is already open to all customers of water authorities and water companies. Although all industrial and many commercial customers are metered, few domestic customers have seen sufficient advantage in this method of charging to be prepared to incur the cost of having a meter installed. A programme of compulsory meter installation would, however, lead to significant economies of scale. The recently published report of the Watts Group on domestic metering suggests

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that there are circumstances in which compulsory domestic metering could reduce water consumption sufficiently to justify the additional costs of charging in this way, and recommends that the Government legislate so as to make more extensive trials of metering possible. The Government will include the necessary provisions in its privatisation Bill. In the meantime, water undertakers will continue to be able to use rateable value, moderated by standing charges, as a proxy for consumption where meters are not installed; and those domestic consumers who consider that their charges are unfairly onerous will continue to have the option of getting a meter installed and paying on that basis.

4.22 Another aspect of water charging policy over which the Government considers it will be important to retain some general powers is the supply of water in bulk between undertakings. The right of appeal will remain when undertakers are unable to agree terms for such transfers, but this will be to the Director General, rather than the Secretary of State. In determining appeals, he will apply the same general principles - that charges should be cost-related and should not discriminate - as apply to other aspects of charging policy.

4.23 As described in paragraph 3.15, WSPLCs will be able to meet the net cost of services currently funded by the Environmental Service Charge from the charges for their main services. The Government will expect efforts to be made for the maximum possible cost recovery for those services which receive a contribution in this way. Some new areas of enterprise could well be done on a profit-making basis. However, it is accepted that some desirable activities may have to continue to be run at a loss. As part of the continuing regulatory arrangements, each WSPLC will propose the amounts of the contribution (at present no higher than 2.5% in any part of the country) which the Director General may accept or amend,

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bearing in mind the cost to customers, and the views of the regional recreation and conservation committees, or their equivalent in Wales. There is no question of repealing obligations, whether general or specific, currently placed upon water authorities in this area of activity, and the statutory duties and obligations of the WSPLCs, or specific requirements laid upon them by Ministerial policy, must be taken into account by the Director General in assessing the reasonableness of the subsidy proposed.

Customers

4.24 Arrangements will also be made for more direct account to be taken of customers' interests. The Water Act 1983 provided for the creation, for the first time in the industry, of formal arrangements to represent customers' interests. Each regional authority's divisional consumer consultative and regional recreation and conservation committees provide a forum in which customers' representatives discuss with the appropriate authority its policies and actions and their effect on customers. The Government considers that these arrangements (and their Welsh equivalents) have worked well and it intends to retain their essential features.

4.25 It believes, however, they should be strengthened in various ways so that consumer bodies can assume an additional responsibility after privatisation. It therefore proposes that consultative committees should be established at authority level (in parallel with the English recreation and conservation committees which will be retained), and that these will replace the existing divisional committees*. The regional committees will be independent of the water authority they monitor and will report to the Director General, who will be responsible for appointing their members. They will be financed from the licence fee charged to WSPLCs, and will employ their own secretariat. In addition to their existing duties, the Government wants them to investigate specific complaints, including complaints of maladministration, on behalf of consumers, in cases where they have not received a

*The arrangements for Wales have yet to be finalised

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satisfactory response from the WSPLC themselves. They will have an ultimate right of complaint to the Director General. Accordingly the Government intends to remove water authorities from the jurisdiction of the local Ombudsman.

4.26 Privatisation itself will encourage the WSPLCs to compete effectively in those areas where they can. Where this is not practical, the Government's aim is to introduce a system of regulation which will stimulate a competitive approach. Profit is a more effective incentive than Government controls. It is right, therefore, that successful WSPLCs should be able to retain the rewards of their effort. Success must, however, be achieved by genuine gains in efficiency, and not by cutting services. By setting targets in terms of standards of service, the Government will be able to ensure that services are not only maintained, but actually improved, and that customers will benefit. And customers will also benefit from the price-control, containing price increases within limits which are pre-determined in relation to the trend of retail prices. These are the cornerstones on which the Government will establish the regulatory system proposed in the foregoing section.

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SECTION 5: SAFEGUARDING THE ENVIRONMENT

5.1 The improvement of water supply and sewerage services and the enhancement of the water environment have been closely linked since the early public health legislation of the 1840s. In recent years, in particular with the implementation of Part II of the Control of Pollution Act, the Government has placed increasing emphasis on the improvement of the water environment, conservation of its wildlife, and promotion of the recreational opportunities it provides. This section describes how the Government will ensure these policies can continue after privatisation and the part which WSPLCs can play in them.

5.2 The environment is everyone's concern. Public and private bodies have always had a part to play. Legislation has, for instance, preserved the critical role of riparian owners in the enforcement of pollution controls, and the Mersey Initiative, described in paragraph 2.17, involves the collaboration of private industry and statutory undertakers in a long-term programme for environmental improvement. The Government now intends that privatisation should promote a more effective alliance for the improvement of the environment between central Government, providing clearer strategic policy direction, the water authorities, with more scope in their new form for innovation and cost-effectiveness, and a critical and informed public.

Environmental Water Quality

5.3 Rivers provide both the material for water supply and the means of disposing of sewage and other liquid wastes. So the conservation of rivers lies at the heart of the water authorities' activities. Accordingly, and as more fully explained in Section 3, the Government has decided that when they are transferred to private ownership, the water authorities should retain executive responsibility for the protection of rivers and other natural waters from pollution.

5.4 Important though the responsibilities for water pollution control and monitoring are, they do not consume enormous resources.

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For instance, the Thames Water Authority, which has been notably successful in cleaning up the Thames, and in its daily operations is an outstanding example of the integrated management of a river basin for every kind of water use, directly employs about 75 people on pollution control and monitoring (out of a total staff of 9,000), and spends about £3.3 million (including full corporate overheads) on these purposes each year, as compared with a total turnover of £468 million.

5.5 The steady improvement in water quality in recent decades, described in Section 2, was achieved largely through the introduction of a series of enactments designed to improve pollution controls. Their central feature is the licensing, by water authorities, of all discharges of trade effluent and sewage effluent. In carrying out these responsibilities, water authorities have developed, in consultation with local interests, a system of river quality objectives to define the quality of water necessary for the uses to which the river is to be put, and what discharges can be safely permitted. The authorities' inspectors also monitor both individual discharges and the waters that receive them, and play a critical role in enforcing the prohibition of polluting matter.

5.6 These regulatory functions are to be retained by the WSPLCs. The recent implementation of Part II of the Control of Pollution Act 1974 has put the regulatory system on a firmer footing - including powers of appeal, call-in and public inquiry - able to accommodate a role for private bodies in the granting of discharge consents. The WSPLCs will inherit their predecessors' expertise and tradition of public service, and their role in abstraction for supply will provide a continuing incentive to maintain quality.

5.7 Certain changes will however be necessary to underpin the exercise of these functions by private bodies, in particular a clearer strategic framework of national policy (paragraphs 5.8-5.10), sound public involvement (paragraphs 5.17-5.19) and a satisfactory system of finance and management (paragraphs 5.20-5.22). These changes will provide the WSPLCs with a clear

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and stable remit on which to plan their operations. They are in line with the Government's increasing emphasis on pollution policies, and will help maintain their effectiveness in the light of the changing pressures on the water environment.

5.8 The following measures will be introduced to provide a clearer strategic framework for the protection of the water environment:

i. the quality objectives developed in recent years for rivers and estuaries will become part of a formal statutory system and will require approval by the Secretary of State. They will reflect national policies for the water environment and, through the licence, provide targets and performance measures against which WSPLCs can prepare environmental programmes. Insofar as it is possible for the Secretary of State's approval to have been given to these long term river quality objectives before prospectuses are issued for the flotation of the WSPLCs, investors will have a better assurance about the cost implications, and those who use or enjoy the resources of our rivers will be able to foresee with confidence the standards to which they are to be maintained or improved;

ii. recently implemented provisions of the Control of Pollution Act allow water authorities both to require others to take precautions and to regulate others' activities for the avoidance of water pollution. These powers will be used to provide a protective regime for the resources on which water authorities depend and for those areas of the water environment of particular importance to conservation. These provisions will substantially supersede authorities' present byelaw making powers and provide a more effective means of tackling sources of pollution not susceptible of regulation through discharge consents.

5.9 At present the Secretary of State has the duty under the Water Act 1973 of giving effect to national policy for the

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restoration and maintenance of the wholesomeness of rivers and for related environmental purposes. To that end the Act gives the Secretary of State the power to give water authorities general directions. In practice, it has never been necessary for the Secretary of State to give such a direction, because water authorities have readily responded to instructions and guidance given less formally, for instance in circulars on public statements of policy.

5.10 These public sector conventions will need some revision when the water authorities are transferred to private ownership. Ministers will remain responsible for environmental policy, but a private company will expect any policy instructions or guidelines from the Government to be conveyed explicitly and openly. A wide power of general direction is clearly inappropriate, but it will still be necessary for the Secretary of State to have a power to direct WSPLCs only in their capacity as pollution control authorities, in order that international commitments can be met, and environmental policies can be given effect. The legislation will be drafted accordingly, and will include the provisions described in paragraphs 5.21 and 5.22 to enable WSPLCs to recover the costs arising from their environmental functions and responsibilities. No general power of direction is proposed.

Environmental Services

5.11 These policies will enable the Government's long-standing commitment to maintain and improve water quality to be effectively carried forward after privatisation. They will also ensure a sound basis for meeting objectives for the environmental services - conservation, fisheries, recreation and navigation - which are dependent upon it. In formulating objectives and policies in this area water authorities have had the benefit of advice from their Regional Recreation and Conservation Committees on matters such as standards of service, complaints and the balance to be sought among the competing uses of the water environment.

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- Wildlife and Conservation

5.12 Since 1973, the Water Act, the Control of Pollution Act and the Wildlife and Countryside Act have required water authorities to have regard for the conservation of the natural environment and exercise their other functions so as to further it. Authorities have promoted more effective consultation on conservation issues and developed greater sensitivity in the design and execution of capital projects. A number have produced their own conservation guidelines, published specific objectives and standards of service, or carried out detailed surveys of wildlife in specific areas.

5.13 The Government intends that the various activities undertaken by water authorities to fulfil their present statutory duties to further nature conservation and protect amenity should be continued. The privatisation of the water industry will provide an opportunity to consolidate these achievements and carry them forward within a new statutory and administrative framework. In particular, environmental programmes undertaken by WSPLCs to meet the terms of their licences will allow conservation needs to be periodically reviewed and the measures described in paragraph 5.8(ii) will provide a basis, when necessary, for special protective regimes for environmentally sensitive areas.

- Fisheries

5.14 Water authorities have a statutory duty to maintain, develop and regulate fisheries for salmon, trout, eels and freshwater fish. They are also required to consult affected interests through statutory fisheries advisory committees. These duties are fundamental to the continuation of the fisheries which are important to large numbers of anglers, to riparian owners and, in coastal areas, to commercial netsmen. They also have a bearing on river water quality, for which the health of the fish stocks provides a sensitive indicator. It is the Government's intention that the WSPLCs should retain their full range of fisheries responsibilities. The Minister of Agriculture, Fisheries and Food and the Secretary of State for Wales would continue to

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exercise the general responsibilities placed on them under the Water Act, 1973 and their specific responsibilities for making and approving regulatory measures under the Salmon and Freshwater Fisheries Act 1975.

- Navigation

5.15 In common with certain other private and public bodies, three water authorities at present exercise extensive navigation responsibilities set out in local acts but in relation to a public right of navigation. The Government has concluded that these responsibilities can pass to their successor bodies by statute amendment or agency arrangements. The terms of their operating licences will leave them free to develop facilities and levy charges in accordance with the principles of the navigation statutes.

- Recreation

5.16 Water authorities already provide wide opportunities for enjoyment of the water environment. Their statutory duty to make the waters they control, and any associated land, available for recreation, as far as reasonably practicable, has also contributed to the dramatic increase in recent years in opportunities for active water-based recreation. These opportunities must be preserved. Conditions within the operating licence will therefore provide for the maintenance, in general, of the existing range and level of facilities, including those for private clubs. There remain, however, many opportunities to expand and develop the recreational potential of the water environment. The Government believes that private bodies will be best placed to undertake this in a vigorous and innovative manner and with sensitivity to customer preference. The arrangements for privatisation will ensure they are free to do this.

Public Information and Consultation

5.17 The Government recently implemented the public register provisions of the Control of Pollution Act which ensure public

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access to information on discharge consents and samples of discharges. These provisions are a model for public information on environmental matters and enjoy wide support among environmental and industrial interests. There is no reason to depart from the principles and practices already established, although in the light of the arrangements proposed for privatisation the Government considers there may be merit in adapting the provisions to allow inclusion of information on the receiving waters, their quality objectives and incidents affecting them and such other data as may assist public understanding of the purposes and operation of pollution controls.

5.18 The Government proposes at the same time to consolidate and streamline existing requirements for the submission of information for national and European Community purposes, so far as possible on an annual basis. In conjunction with the River Quality Survey, undertaken about every five years, they will provide a full analysis of changes in environmental water quality and a basis for review of, and consultation on, the relevance and effectiveness of environmental protection measures.

5.19 The Government proposes to preserve the arrangements for consultation on environmental matters, including the Recreation and Conservation Committee in each region. Like other representatives of consumer interests, they will be appointed by the Director General*, who will therefore be concerned that a reasonable balance be struck between the provision of facilities and the costs to shareholders and customers.

Management and Finance

5.20 Government approval of local water quality objectives (paragraph 5.8(i)), provisions for the protection of water resources (paragraph 5.8(ii)), and the specific Ministerial power of direction (paragraph 5.10) will ensure a consistent framework of environmental policy. The development of public information (paragraphs 5.17-5.19) will provide a stimulus to action; but

*The arrangements for Wales have yet to be finalised

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it is the water authorities themselves and their predecessors who have done most to bring about the development of effective systems of environmental management. After privatisation they will have every reason to go on advancing their expertise - including the freedom, as private companies, to operate and sell their skills overseas.

5.21 Investors in the new companies will be concerned about the financial implications of their environmental duties. These expenses are not large but the Government considers that, consistently with the polluter pays principle, WSPLCs should be able to recover the necessary costs of carrying out their responsibilities for environmental control and monitoring. Industrial dischargers and individuals enjoying the water environment should also have a direct incentive to help maintain and improve water quality. The Government will therefore work out in consultation with the WSPLCs and other interests how the costs of pollution and pollution control and monitoring can be assigned to those responsible for causing it, and the costs of averting pollution to those whose actions make that necessary.

5.22 At the same time there must be a sound general basis for financing environmental improvement programmes required to meet quality objectives and for financing those amenity and recreational services which are socially important but for which the full costs cannot be directly recovered. To the extent necessary, the terms of their licences will permit WSPLCs to reflect such costs in their general charges.

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6.1 The Government intends to introduce legislation at the earliest opportunity to

- restructure the ten water authorities in England and Wales as Water Service Public Limited Companies;
- establish a system of regulating them;
- modernise water and sewerage law;
- permit domestic water metering trials on a compulsory basis;
- improve the legislative framework for the control of drinking water and river water quality.

6.2 As soon as the necessary legislation is in place, the Government will ^{formally} appoint a Director General of Water Services and convert all the authorities into WSPLCs. Initially, they will be wholly-owned by the Secretary of State, who will proceed to float them individually, as rapidly as market conditions and the circumstances of the individual companies allow.

6.3 Preparatory work for the flotation of the WSPLCs will be carried out in parallel with the drafting and passage of legislation. The Government will be discussing with each authority the appropriate restructuring of its balance sheet. It will also be considering the effect of its present policies for rates of return, borrowing and investment to see whether changes are necessary, either in relation to particular authorities or more generally. It is recognised that a WSPLC will not necessarily and appropriately have the same board members as the present water authorities, and the Secretary of State will select new members accordingly as appointments expire. He also intends that the legislation should provide for the possibility of other changes of chairmen and members before flotation.

6.4 As noted in paragraph 3.10, the Government is reviewing the responses it has received to the Green Paper, "Financing and Administration of Land Drainage, Flood Prevention, and Coast Protection in England and Wales" (Cmnd 9449), which was issued in March 1985. The review is being carried out in the light of the Government's commitment to privatisation, and a further announcement will be made following its completion.

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6.5 A consultation paper will be issued shortly on the Government's proposals for modernising water and sewerage law.

6.6 The Government will be holding discussions with the Water Companies Association on the proposals in paragraph 3.5, and will be consulting other interested parties on a number of detailed issues.

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FURTHER INFORMATION

Further information can be obtained from the following publications:

1. Annual Reports and Accounts are published by each water authority and are on sale from their headquarters. Prices range from £2.00 to £5.00.
2. Corporate Plans (published by each water authority, prices range from "no charge" to £10.00).
3. Water Facts (Water Authorities' Association, £3.50).
4. River Quality Survey (HMSO, £5.45).
5. The Water Industry: UK Service and Costs 1984 (CIPFA, 3 Robert Street, London WC2N 6BM, £6.50).
6. Who's Who in the Water Industry (Water Authorities' Association, 1 Queen Annes's Gate, London SW1H 9BT, £13.00).
7. Water Industry Review 1982 (National Water Council, £6.00. Excellent for the history of the water industry).
8. The principal Acts relating to water authority affairs are: The Public Health Act 1936, The Water Act 1945, The Water Resources Act 1963, The Water Act 1973, The Water Charges Act 1976, the Control of Pollution Act 1974, the Water Act 1983.
9. Economic Regulation of Privatised Water Authorities, a report submitted to the Department of the Environment by Professor S C Littlechild.
10. Joint Study of Water Metering: Report of the Steering Group (HMSO).

