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PREM 19/1838

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Part 3

Confidential Filing

The Water Industry:
Structural Change

Constitution of the Welsh Water Authority.

Local Government

Pt 1: March 1981
Pt 3: Dec 1985

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
9/12/85		8-4-86					
10/12/85		10.4.86					
13.12.85		11.4.86					
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17.3.86							
26.3.86							

PREM 19/1838

PART 3 ends:-

MS/MAFF to SS/DOE 21/4/86

PART 4 begins:-

LPC to PM 1/7/86

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister

The Rt Hon Kenneth Baker MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
London
SW1A OAA

21 April 1986

WATER PRIVATISATION: ENVIRONMENTAL PROTECTION

Thank you for your letter of 17 April. I am sorry that I was not able to meet your deadline of 18 April.

Like you, I was disappointed that there was need for me to raise these issues. I have to say that they had virtually all been raised in discussions between our officials. If the solutions you are now proposing had been offered then, it would have avoided the need for correspondence between us on the great majority of points.

I am nevetheless grateful to the further consideration that has now been given to the various points in my letter. In particular I find that the explanation you have given me on water environment protection zones, together with the redrafted paragraph, both clarify the position and resolve my concerns. I am therefore content.

I am also pleased that you have been able to meet most of my other points or provided the necessary reassurances. I still consider it unfortunate that you are unable to agree to the deletion of the reference in paragraph 1.5 of the consultation paper, to the increasing attention to the protection of the marine environment in consultation with our European partners. As I said in my earlier letter I feel this could be taken as endorsing the recent EC draft directive for disposals at sea. If you remain convinced, that this reference is necessary for wider considerations, I will not continue to oppose. But I must warn that the reference may lead us into difficulties at a later date.

The one point on which I do feel that a change is necessary is that the paper should mention the possibility of introducing charges ror the work which our respective Departments carry out in considering applications for discharges. This falls squarely

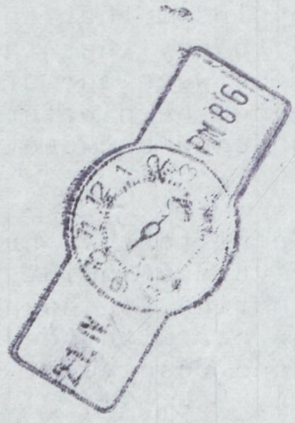
/ within the Polluter ...

LOCAL GOVT
WATER
PT 3

within the Polluter Pays Principle and should not be dismissed until it has received full consideration. If it is then shown impractical, so be it, but I must request that the paper leaves the way open and gives recipients the opportunity to comment.

I am copying this letter to the Prime Minister, Malcolm Rifkind, Paul Channon, David Young, Nicholas Edwards, John Moore and Sir Robert Armstrong.

MICHAEL JOPLING



CCBG.

SECRETARY OF STATE FOR THE ENVIRONMENT

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref: B/PSO/13864/86
Your ref:

17 April 1986

NSR7.

Dear Mr Mark,

WATER PRIVATISATION : ENVIRONMENTAL PROTECTION

Thank you for your letter of 16 April about water privatisation and our environmental consultation paper. As you will know, there has been extensive inter-departmental discussion on earlier drafts of this and we have made considerable efforts to meet the points which we knew were of concern on the agricultural side. It is therefore disappointing that your letter should now be raising so many matters but I will try to meet them in a way which will be satisfactory to both of us.

I cannot agree that we should drop the reference to water environment protection zones, but I think we can present what we mean by these rather better. Introducing these zones does not constitute a "new measure". The powers are all there at present in Section 31(5) of the Control of Pollution Act 1974 which was implemented last year. Other powers do not tackle the risks of pollution arising some distance up stream. The powers to vary discharge consents are of no assistance. The problems arise not from regular consented discharges but from spillages and negligent disposal of wastes and other pollutants. It would not be a satisfactory alternative to implement the powers given to water authorities in section 46(1-3) of COPA. Water authorities regard these powers as burdensome and virtually inoperable, and we are proposing that they should go.

Nor do I believe that the proposals put the voluntary approach to conservation at risk in any way. They are intended to catch practices which are likely to result in criminal offences. We could not defend applying the voluntary principle in such circumstances - especially since the offences can be prevented a good deal more cheaply than their consequences can be remedied. While I do not therefore see grounds to delete this section, I appreciate your concern that, used increasingly, it could damage legitimate agricultural interests. I have therefore recast the section (as attached) in a way which ties it clearly to pollution risks and circumscribes its use to their problems which we clearly need to tackle. I hope you will feel that this reformulation meets your concerns.

Your more detailed points cause me less difficulty: the order below follows that in your letter:

(i) On COPA Section 32 I do not believe we can deregulate and at the same time emphasise continuing control by central guidance. But we will indicate that such guidance will be provided when appropriate.

(ii) Taking paragraphs 4.11 - 4.14 as a whole I do not believe that what we say about compensation for variation of consents will cause difficulties. However, if it will help, I am prepared to say, in the final sentence of paragraph 4.12 "in this case also the payment of compensation might (rather than 'would') not be appropriate".

(iii) I am prepared to amend the text to make it explicit that we would not expect to make regulations under section 31(4) of COPA on any agricultural practices effectively covered by the Code of Good Agricultural Practice (rather than just the two most important - silage and slurry - to which we explicitly refer). But this is on the clear understanding that if the present advisory code is not enough to reduce the current level of pollution incidents within a reasonable period we must look to other measures. I am concerned that the River Quality Survey may soon show that the long-term improvement in water quality has halted or gone into reverse, particularly within the agricultural regions, so we must be seen to have adequate powers available.

(iv) I confirm that I have no present plans to amend Section 39(2) of COPA which allows us jointly to hear appeals in certain circumstances.

(v) I do not think we should at this stage raise the possibility of charging discharges consent applicants for the time your department gives to commenting on certain categories of application on which they are statutory consultees. We would have to extend it to local authorities who see all such consent applications. Such a charging system could quickly collapse under its own complexity;

(vi) I do not believe that a statement that "The Government is giving increasing attention to protection of the marine environment" risks implying any change of stance on disposals at sea. I believe it is the least we can defensibly say on a matter of increasing concern.

(vii) I accept your point about the reference to anti-fouling paints.

It is inevitable that environmental policies affect a wide range of interests, and agriculture more than most. I hope that you will feel the changes I am able to make reasonably meet your main concerns, and that we can now move immediately to publication. As we have to allow 2 months for consultation, and our final instructions have to be sent to counsel in July, it is vital that we publish this month, and if you have any problems about agreeing to my proposals, I must ask that you let me know by Friday at the latest. Other colleagues, as you know, have already agreed the draft. I am copying this to the recepients of yours.

Yours sincerely

KENNETH BAKER

The Rt Hon Michael Jopling MP

3F

Proposed Revision

7.11. But smaller areas are also important. Here the proposed means of protection are the powers in the Wildlife and Countryside Act for the designation of Sites of Special Scientific Interest. Under present plans the Nature Conservancy Council expects that some 9% of the water courses may be so designated. Aquatic plants and animals may however be affected by pollution originating at some distance. In circumstances where pollution injurious to flora and fauna is arising, designation of an SSSI or use of other powers under COPA may not be appropriate. In these exceptional circumstances the Government will consider use of protection zone powers under section 31(5) of COPA (described in section 5 in relation to the protection of sources of water supply) to regulate those activities giving rise to the pollution, whether in the water or on the banks or associated land. This could prove a helpful addition to the existing machinery for conservation of the water environment.

LOCAL GOVT: Water Ind: Pt 3

CCBG

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

NBPM

From the Minister

The Rt Hon Kenneth Baker MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
London SW1

16 April 1986

Dear Ken

WATER PRIVATISATION: ENVIRONMENTAL PROTECTION

Thank you for sending me a copy of your letter of 26 March to Nick Edwards together with a draft of the consultation paper foreshadowed in the Water Privatisation White Paper.

In terms of the overall structure of the paper, it is important to strike the right balance. On the one hand we must be seen in the context of privatisation to be maintaining effective protection for the environment. In addition, the forthcoming legislation will provide a useful opportunity to consolidate and, where appropriate, extend the environmental gains of recent years. On the other hand, any changes must clearly be seen as justified and appropriate. They must take account of the costs to be borne both by the WSPLCs and the individuals affected. They must not be of a nature likely to frighten off potential investors. Finally they must be consistent with our policy on deregulation.

A number of the options outlined in your letter are relevant to my areas of responsibility. I am glad to note that, as a result of discussions between our officials, many of our concerns have been met. The resulting draft which you have circulated now presents a useful basis for preparation of the final version. I do, however, have a few remaining concerns which need to be resolved before the consultation paper is issued and I fully agree with David Young's views on the need for a summary and preliminary compliance cost assessments.

I would like firstly to comment briefly on the overall style of the draft. I accept that we must be as clear as possible about our intentions. Not least, we must show the environmental lobby that there will be no lowering in standards following privatisation. But we must also consider the impression we give to potential investors on whom the success of the whole enterprise depends. I must say that, viewed in this light, I do find the present flavour of the document rather draconian and interventionist.

Turning to points of substance, my principal outstanding concern relates to Chapter 7. Although in general it strikes the right balance by signalling the Government's continued support for adequate

conservation measures, I do not see the need for further protection in the form of Water Environment Protection Zones, which would control activities on water, banks and associated land. The case for new measures of this sort is not made in your letter and it is not clear to me why such additional controls are considered necessary, bearing in mind the existing arrangements, including provisions to vary discharge consents in Section 46 of the 1974 Act, the separate arrangements for Sites of Special Scientific Interest and other provisions in the Wildlife and Countryside Act 1981. The new powers would involve an important element of compulsion and no provision for compensation. This would mark a fundamental change in Government policy, which presently relies upon a voluntary approach to nature and landscape conservation. It might well be seen as running counter to the Government's policy on de-regulation. I believe the creation of these powers would be seized upon by those who wish to argue that the voluntary approach has failed. This is not so. It is important therefore to exclude this proposal from the consultation paper.

My other comments are more on matters of detail. I accept that Section 32 of the 1974 Act can benefit from some changes (Chapter 4 of paper) but we still have reservations over leaving the decision on whether a consent for discharge is necessary to the discretion of WSPLCs. I am therefore strongly in favour of appropriate central guidance being given and believe the consultation paper should state that this will be done, instead of merely referring to it as one option (in paragraph 4.7). Such guidance should incorporate the guidelines agreed last year in respect of agricultural discharges.

In paragraphs 4.11 and 4.12 you discuss the extent to which the existing provisions to vary a discharge consent might be implemented, and I find it helpful that the text clarifies the extent to which compensation is available. However the concluding sentence of 4.12 suggests that compensation would not be appropriate under the new arrangements. This is a delicate issue and I do not consider it appropriate to rule out the possibility of compensation at this stage of the consultation process. I must therefore ask you to adopt a more open wording in this passage so that we are left free to take appropriate decisions in the light of responses to the document.

Paragraph 4.13 proposes the repeal of Sections 46(1) to (3) of the 1974 Act, in view of the new measures in Chapter 7. You may of course wish to reconsider this proposal in the light of my earlier comments on Water Environment Protection Zones.

In chapter 5 you rightly highlight the importance of the Code of Good Agricultural Practice in helping to minimise water pollution from farming activities. Paragraph 5.7 is particularly helpful in suggesting that regulations under Section 31(4) of the 1974 Act are unlikely to be necessary for the storage of silage and slurry (two of the activities covered in the Code). I would suggest however that the reference could be extended to all the activities included in the Code. The Section would then read "... The most important is the Code of Good Agricultural Practice, covering activities described in paragraph 5.4 above. In view of the Code it is unlikely to be necessary to make regulations for such farming

activities, but the Government ...". This is an important statement in that it recognises the role of the Code in avoiding pollution, highlights the Government's view that results are best achieved through the voluntary approach, and makes it clear that we are not looking for changes in respect of agricultural practices so soon after the adoption of the Code and other arrangements made last year.

The section of the paper dealing with Water Source Protection Zones is for the most part acceptable. However, I am uneasy about the proposal to remove the right of an individual to a local public enquiry in advance of controls being imposed. I recognise that the possibility of appeal to you, which might be followed by a public enquiry, would remain as a safeguard. However, in this case, controls which might have a severe impact on, for example, a farm business, would already have come into force. I consider that we should pay careful heed to any representations made on this possible change during the consultation process.

The Control of Pollution Act 1974 presently provides, in Section 39(2), that where there is an appeal against the withholding of a consent for discharge, a certificate can be obtained from this Ministry stating that the activity is good agricultural practice. The appeal is then considered jointly between ourselves. In the absence of any reference to this procedure in the consultation document, I would be grateful for your confirmation that it will continue.

On the fisheries side, my officials are, of course, consulted on a statutory basis on discharges into coastal and estuarine waters and I am glad to note that this provision will continue after privatisation. I also fully support the concept set out in Paragraph 3.6 of the draft consultation paper that you should set objectives and quality standards for estuarial and coastal waters with an appropriate timetable for implementation. I welcome the extension of the polluter pays principle as enshrined in Section 6, which has been developed here through the charges levied under the Food and Environment Protection Act 1985 (FEPA) and through the proposed introduction of charges for authorisations under the Radioactive Substances Act 1960. But I do not think that it goes far enough in that no provision is made in Section 6 for recovery of the costs that our respective Departments incur in considering applications to discharge. While the position may not be entirely straightforward from a legal point of view, I consider that it would be prudent at this stage of the exercise to put up a marker that the Government is considering the concept. Our officials can then look into the position in more depth during the consultation period and, of course, take on board any comments that are made by recipients of the consultation document.

There are also two presentational points on the fisheris side that I would like taken on board. First, despite advice to the contrary by my officials a reference to the marine environment still occurs in paragraph 1.5. I fail to see the relevance of this to the privatisation issue unless it is intended as a reference to water quality standards. If so, the reference should be specifically to that aspect of the marine environment; otherwise I fear that the draft as it stands will be interpreted as a change of stance on

LOCAL GOVT. Water Industry: PE3

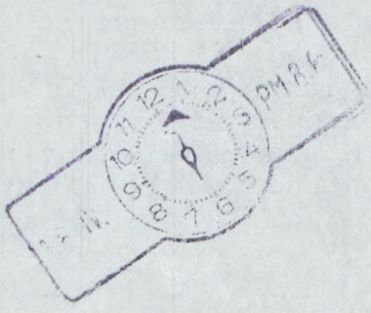
disposals at sea, which would be a particularly unfortunate development, bearing in mind our proposed lin on the draft EC Directive. Secondly I note that a reference to anti-fouling paints has now been introduced at Paragraph 7.6. This gives the impression that existing powers to regulate their use may be adequate. I thought it was clear that the current sanctions under COPA were in fact inadequate and that was why consideration is now being given to controls under Part III of FEPA. In these circumstances, I do not consider the reference to the paints problem to be at all appropriate and would prefer this sentence to be deleted.

I am copying this letter to the Prime Minister, Malcolm Rifkind, Paul Channon, David Young, Nicholas Edwards, John Moore and Sir Robert Armstrong.

Yours ever

M Jopling

MICHAEL JOPLING



CCBA

JU10
Secretary of State for Trade and Industry

DEPARTMENT OF TRADE AND INDUSTRY
1-19 VICTORIA STREET
LONDON SW1H 0ET
Telephone (Direct dialling) 01-215 5422
GTN 215) .....
(Switchboard) 01-215 7877

15 April 1986

The Rt Hon Kenneth Baker MP
Secretary of State for
the Environment
Department of
the Environment
2 Marsham Street
London SW1P 3EB

NBPM

Dear Kenneth.

WATER PRIVATISATION: ENVIRONMENTAL PROTECTION

Thank you for sending me a copy of your letter of 26 March to Nicholas Edwards, which enclosed a draft of the consultation paper you propose to issue on this subject.

Your letter emphasised the need to take account of the concerns of the environmental lobby about the possible implications of the proposed transfer of regulatory functions to private sector companies. As I am sure you recognise, this concern is not confined to environmental interests. Industry too is concerned with the proposal that manufacturers discharging effluent into rivers etc should be subject to regulatory controls exercised by what are in effect competitor companies.

The proposals in your draft consultation document are understandably designed principally to allay the fears of environmental rather than industrial interests. While some are welcome - for example, your proposal to adopt cost recovery charges for pollution control, rather than incentive or distributive charges - others, for example, your proposals to extend regulation in a number of areas are less so. I share your reservations, for example, over the reference in paragraph 6.10 to the possibility that WSPLCs should be required to levy penalty charges where effluent discharge consents are exceeded.

1786 1986 BOARD OF TRADE BICENTENARY

While I am content that the consultation paper should be issued, I must therefore reserve my position on the detailed changes proposed until we have had an opportunity to consider responses from industry and others to the consultation exercise. I should be grateful if your officials could keep officials here in touch with developments.

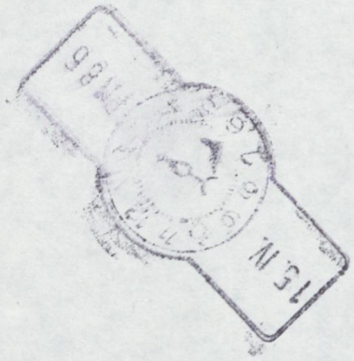
I have one comment to offer on the drafting. The paper includes a large number of proposals in a variety of forms - the bringing into force of some existing statutory provisions, the abolition or amendment of others, and some wholly new powers. I think it would aid the reader greatly if a chapter were to be added listing in summary form the main changes proposed.

I am copying this letter to the Prime Minister, Nicholas Edwards, Michael Jopling, Malcolm Rifkind, David Young, John Moore and Sir Robert Armstrong.

PAUL CHANNON

1786 1986 BOARD OF TRADE BICENTENARY

LOCAL GOVT: Water PPS



cc BR

FROM THE MINISTER FOR LOCAL GOVERNMENT AND THE ENVIRONMENT

SCOTTISH OFFICE
NEW ST. ANDREW'S HOUSE
ST. JAMES CENTRE
EDINBURGH EH1 3SX

The Rt Hon Kenneth Baker MP
Secretary of State for the Environment
2 Marsham Street
London
SW1P 2EB

15 April 1986

NBPM.

Dear Kenneth,

Thank you for copying to Malcolm Rifkind your letter of 26 March and your consultation paper on environmental protection.

As you know we have quite different arrangements in Scotland for the provision of water services and for the protection of the aquatic environment. These arrangements appear to be working very satisfactorily and we have no plans to go for privatisation at this time. Nevertheless we have been watching the development of your proposals on environmental protection with interest. Your officials have helpfully let mine see an earlier draft of the consultation paper and the present version takes account of the points we made. I have therefore no comments to make on the paper itself.

We are conscious, however, that many of your proposals would lead to amendment of the Control of Pollution Act 1974 which generally applies to the whole of Great Britain. There is no need for us to adopt all of these changes but we have identified a number on which it would be helpful and sensible to maintain a common line. I recognise that there will be many demands on the Water Privatisation Bill but I would be grateful for your acceptance that our proposals, which are modest, should be accommodated in the Bill. I am leaving it to my officials to convey the details to yours but I shall, of course, be keeping in touch with developments.

I am sending a copy of this letter to the Prime Minister, Nicholas Edwards, Michael Jopling, Paul Channon, David Young, John Moore and Sir Robert Armstrong.

Yours Michael

MICHAEL ANCRAM

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Local Govt. Water
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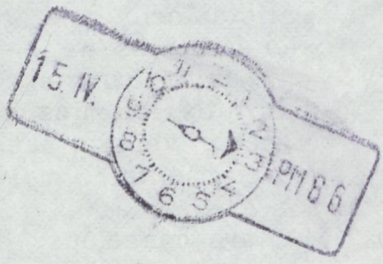
PC-3



NJ[redacted]41

dcbb

SECRETARY OF STATE FOR EMPLOYMENT

Caxton House Tothill Street London SW1H 9NF

Telephone Direct Line 01-213 6460
Switchboard 01-213 3000

The Rt Hon Kenneth Baker MP
Secretary of State
Department of Environment
2 Marsham Street
London SW1

11 April 1986

Dear Secretary of State,

WATER PRIVATISATION: ENVIRONMENTAL CONTROLS

Thank you for copying to me your letter of 26 March to Nicholas Edwards about new regulatory arrangements for the protection of the water environment.

I view with some alarm any consultation document that has seven long and complex chapters. I hope that the final version will carry a summary which distinguishes clearly between new controls that would affect new water companies and those which would directly affect existing industrial and agricultural businesses.

I notice that some of the latter type of new proposals are still tentative, for example 'water source protection zones'. If, as a result of your consultation, you decide to proceed with these it would be most helpful if your officials could provide preliminary compliance cost assessments for the Enterprise and Deregulation Unit.

I am copying this letter to the Prime Minister, Michael Jopling, Malcolm Rifkind, Nicholas Edwards, Paul Channon, John Moore and Sir Robert Armstrong.

Yours sincerely,

(Approved by the Secretary
of State and signed in his absence)

Local Govt; Water Pt 3

CCBG

Y SWYDDFA GYMREIG
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WHITEHALL LONDON SW1A 2ER
Tel. 01-233 3000 (Switsfwrdd)
01-233 (Llinell Union)

WELSH OFFICE
GWYDYR HOUSE
WHITEHALL LONDON SW1A 2ER
Tel. 01-233 3000 (Switchboard)
01-233 (Direct Line)

Oddi wrth yr Is-Ysgrifennydd Seneddol
From The Parliamentary Under-Secretary

CT/4234/86

10 April 1986

Dear Kenneth,

WATER PRIVATISATION - ENVIRONMENTAL PROTECTION

I am replying, in his absence to your letter of 26 March to Nicholas Edwards.

We fully share your view that the protection of the water environment is a matter of the highest importance in the context of Water Privatisation and believe that the environmental lobby are going to prove a difficult group to persuade of the merits of our proposals. I agree that the consultation paper goes a long way towards meeting some of the likely objections they will have. It is necessary, however, to do all we can to demonstrate that our intention to protect the water environment is genuine and I am sure that the national policy proposals, supported by a statutory framework of controls overseen by the Government through an Inspectorate, is the right way forward. I am broadly content with the proposals set out in the paper, although my officials will continue to be in touch with yours on some minor drafting points which need to be addressed.

I am copying this letter to the Prime Minister, Michael Jopling, Malcolm Rifkind, Paul Channon, David Young, John Moore and to Sir Robert Armstrong.

Yours ever,

MARK ROBINSON

The Rt Hon Kenneth Baker MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON

Local Govt: Water Industry Pt 3

CONFIDENTIAL

CCBG

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref: B/PSO/12899/86

Your ref:

8 April 1986

WATER METERING

Thank you for your helpful letter of 17 March.

You are right that the metering of distribution networks and the development of tariff structures for use in the trials can proceed in advance of legislation. Both these things are being done. I fear however that existing powers on building regulations and bye-laws are insufficient to allow us to require new houses to be constructed so as to facilitate meter installation. So we will need provisions on that in our Bill.

I am copying this letter to other members of E(A) and to Sir Robert Armstrong.

KENNETH BAKER

The Rt Hon John Moore MP

LOCAL GOVT

WATER

PT 3

SECRETARY OF STATE FOR THE ENVIRONMENT

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref:

Your ref:

26 March 1986

Dear Nicholas,

WATER PRIVATISATION: ENVIRONMENTAL PROTECTION

As you know, John Patten and I have all along seen protection of the water environment as a matter of the highest importance in the context of water privatisation.

This is partly because transferring a regulatory system to the custody of private companies is unusual, and raises genuine concern to ensure that they operate their powers fairly, and in the public interest. It is partly because of genuine concern that private bodies may not have sufficient regard to the conservation of the environment. It is also because there will be a number of other concerns, justified or otherwise, which the increasingly powerful environmental lobby will bring to the fore as our proposals go forward.

That was why we devoted a whole section of our White Paper to the subject. There has been a muted response to this so far. A recent Times leader questioned whether private bodies ought to be exercising regulatory functions, and there has been a limited amount of press and other public comment in the same vein. There are signs that we can expect more criticism of this kind unless we can show convincingly that our intention to protect the water environment will be given good effect. In the White Paper we promised to produce a consultation paper on this subject and I attach a draft.

This has been produced following very helpful discussions at official level with your own and other Departments. We have tried to reflect a wide variety of departmental concerns and I very much hope that you and colleagues will agree that this has been done. The draft of course builds on section 5 of the White Paper. Its most important recommendations are:

a. retention by Ministers and privatised water authorities of their essential responsibilities, with some development of these where essential;

b. river quality objectives to be given statutory force;

c. greater protection for sensitive areas from which water resources are derived (this would be derived from present legislation);

d. stronger safeguards against accidental pollution;

e. development of the "polluter pays" principle;

f. simplification of effluent discharge consent procedures.

In my view, this set of proposals will provide a much needed measure of improvement in our arrangements for environmental protection. It should go some way to settling the environmentalist's concern, whilst at the same time not imposing any unreasonable burdens - and indeed producing some benefits - for those who use our river system for discharging effluent.

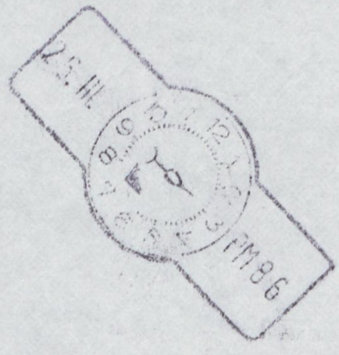
Could I please have any comments by Friday 11 April? I will need to issue it by mid April if we are to take account of public comments in the drafting of legislation.

I am sending a copy of this letter to the Prime Minister, Michael Jopling, Malcolm Rifkind, Paul Channon, David Young, John Moore and Sir Robert Armstrong.

Yours ever,

KENNETH BAKER

The Rt Hon Nicholas Edwards MP



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SECRETARY OF STATE FOR THE ENVIRONMENT

Private Secretaries' Office

N BPM

PS Mr EDWARDS,

WATER PRIVATISATION:
ENVIRONMENTAL PROTECTION.

THE CONSULTATION PAPER REFERRED TO IN THE ABOVE LETTER WAS OMITTED WHEN SENT. PLEASE ACCEPT THIS COPY OF THE PAPER AND MY APOLOGIES FOR THIS OMMISSION.

COPIES OF THIS PAPER GO AS BEFORE.

A.J. Sum
27-3-86.

THE WATER ENVIRONMENT: THE NEXT STEPS

The Government's Consultative Proposals for Environmental Protection under a Privatised Water Industry.

C O N T E N T S

S e c t i o n 1: Introduction
S e c t i o n 2: Environmental Protection: the New Framework
S e c t i o n 3: Environmental Quality Objectives
S e c t i o n 4: Regulation of Discharges
S e c t i o n 5: Reducing Pollution Risks
S e c t i o n 6: Incentives and Charging
S e c t i o n 7: Progress in Conservation

INTRODUCTION

1.1 On 5 February 1986, the Government announced its intention to transfer to the private sector the ten water authorities in England and Wales. The proposals are set out in a White Paper 'Privatisation of the Water Authorities in England and Wales', HMSO, CMND 9734.

1.2 The main elements of the White Paper are as follows:

(a) River basin management of the water cycle will be maintained.

(b) The Water authorities will be converted, with their present boundaries, into Water Services Public Limited Companies (WSPLCs) which will be responsible for all functions of the present authorities with the single exception of flood protection and land drainage.

(c) Financing and co-ordination of flood protection and land drainage will become the responsibility of special bodies which will have close links with the water authorities.

(d) A Director General of Water Services will be appointed to regulate the main services of WSPLCs through a licensing system. Licences will specify price and service standard controls for the utility services, and can include other requirements, giving them legal force.

(e) The Director General will appoint committees to represent the interests of customers of each WSPLC.

(f) There will be new and strong safeguards for the water environment. Existing statutory duties relating to recreation, conservation, navigation and fisheries will continue.

(g) A Bill will be introduced to give effect to these proposals at the earliest opportunity.

(h) WSPLCs will be transferred to private ownership at intervals thereafter.

1.3 This paper develops the proposals in chapter 5 of the White Paper for the strengthening of safeguards for the water environment.

1.4 An important aspect of unified river catchment management

is that a single body is responsible for protecting rivers and other sources of water supply, including ground water, as well as for supplying to customers water which must reach rigorous standards of wholesomeness. This provides a strong incentive for ensuring that all water resources are properly protected from pollution. The ability to develop the fisheries and recreational potential of rivers and other inland waters, also provides an incentive to effective pollution control and water resource management. Retention of unified river basin management therefore will help to ensure that, under privatisation, the environmental responsibilities of WSPLCs will be properly discharged. This paper considers whether the companies will have adequate powers to discharge that responsibility, and also considers changes which privatisation will itself make desirable.

1.5 The Government has already taken important steps to safeguard and strengthen protection of the water environment. It has implemented Part II of the Control of Pollution Act 1974, which provides for more effective protection of inland surface and underground water, the extension of controls to coastal waters, and public involvement in the control system. It has launched and put its weight behind the initiative to tackle the severe pollution of the Mersey river system on a firm timetable. In co-operation with its partners in the European Community it is giving increasing attention to protection of the marine environment.

1.6 Since their establishment in 1973 the ten water authorities have had the executive responsibility for conserving the water environment in England and Wales. In that period, the quality of rivers has been protected in spite of increasing demands upon them. Plans are in place for the improvement of the main industrial estuaries, and maintenance of current investment levels over the next ten or fifteen years would enable the main sources of sewage contamination of coastal waters to be remedied.

At the same time authorities have reflected, and contributed to, the widening interest in the conservation of landscape, flora and fauna. They have considerably extended the consultation they carry out before undertaking works with a major environmental impact. River corridor surveys have been carried out, conservation officers have been appointed and codes of conservation practice have been written and brought into effect. The Government believes that through integrated river basin management the authorities have succeeded in reconciling these objectives with wider provision for amenity and recreation. The table below and associated map indicate the extent of the commitment which the authorities now make in this area.

Recreational Activities at Water Authority Reservoirs in England and Wales 1985.

Total Number of Reservoirs	530
Number with provision for:	
Fishing	474
Sailing	91
Sailboarding	68
Canoeing	45
Sub-aqua	42
Bird Watching	275
Horse riding	40

1.7 Privatisation means that new measures will be required to ensure that the water industry continues to attach due weight to environmental protection. It also provides an opportunity to consolidate and extend the environmental gains achieved in recent years. In deciding its approach the Government has had the following main objectives in mind:

(a) the need for a clearer framework of national environmental policy within which local decisions and local action on matters such as the protection of particular stretches of river can be taken;

(b) the need for regulatory systems to be simple, clear, justifiable and affordable, with firm safeguards against abuse;

(c) the need for the public to have adequate access to information;

(d) the need for financing and charging systems to allocate costs effectively to those whose actions give rise to those costs.

1.8 This consultation paper is written against that background, to set out in more detail the proposals in chapter 5 of the White Paper. Section 2 describes how the general framework for environmental protection can be improved. The following sections deal with separate elements of the system. The Government invites views from organisations and from members of the public with an interest. Comments should be sent to Mr Adrian Straw, Room A434, Romney House, 43 Marsham Street, London SW1. Comments on aspects of the proposals which may be of special significance in Wales should be copied to the Welsh Office: Mr. L. Pavelin, Welsh Office, Cathay's Park, Cardiff, CF1 3NQ. Comments should arrive no later than 20 June 1986.

ENVIRONMENTAL PROTECTION: RESPONSIBILITIES AND A NEW FRAMEWORK

2.1 Privatisation will make a fundamental difference to the constitution of the Water Industry in England and Wales, and the Government is concerned that when it happens the arrangements for safeguarding the environment and for promoting amenity should be consolidated and strengthened. Changes in these arrangements are in any case necessary because since the Water Act 1973 was enacted there have been important developments in environmental policy: it has had to respond to European Community legislation and it has been necessary to define more clearly a national framework of policies and priorities within which regional policies can be set.

2.2 This section describes new arrangements which the Government proposes to introduce with privatisation. It considers in particular the part to be played by the Secretary of State, the WSPLCs and the Director General of Water Services, and it has these principal objectives:

i. to provide for national environmental policies to be clearly identified.

ii. to ensure that adaquate powers exist to give effect to these policies and

iii. to ensure that WSPLCs act in conformity with national policies and the public interest.

Responsibilities of the Secretary of State: Establishing National Policies

2.3 After privatisation, overall policy for the environment and for setting general objectives and priorities will remain, as it must, the responsibility of ministers answerable to Parliament. It will be their duty to ensure that national policy requirements are met including directives of the European Community. It must therefore ultimately be for ministers to ensure that WSPLCs give due weight to environmental considerations. At present, the Secretary of State's responsibilities are defined by section 1 of the Water Act

1973 under which the Secretary of State for the Environment, the Secretary of State for Wales and the Minister of Agriculture, Fisheries and Food are under a duty 'to promote jointly a national policy for water in England and Wales' and it is the duty of the different ministers to secure the effective execution of that policy in relation to their respective functions. Under privatisation, where Ministers will no longer be responsible for appointing members of water authorities and WSPLCs will be outside the public sector, relationships between Ministers and WSPLCs will need to be more clearly defined, and Parliament will expect that the Secretary of State's own obligations should be more precisely formulated.

2.4 There are two main areas in which this will be necessary. The first is the availability and quality of water resources. At present the duty to initiate and carry through surveys of future demand for water, and surveys of water resources, is placed by section 24 of the Water Act 1973 on the water authorities. Assessments undertaken after the 1973 reorganisation identified regional deficiencies then foreseeable up to the end of the century, and the water authorities have promoted schemes to meet these deficiencies. As the demand for water has increased less steeply than was forecast in the early 1970s, it has not yet been generally necessary to extend water resource planning and to secure further supplies for the future. But this may become necessary from time to time, and the Government must be in a position to see that necessary assessments should be carried out as the need arises. It is therefore proposed that there should be a duty on the Secretary of State to require this to be done as and when it appears to him to be necessary, so that the implications can be fully considered.

2.5 The second main area is the setting of quality objectives and standards to which main surface waters - ie rivers, lakes, streams and other natural water resources - should be maintained or improved. These objectives are at present imposed upon themselves, voluntarily, by the water authorities. They are fundamental to the health of our rivers and therefore

to the entire basis of water protection policy. Imposition by the Secretary of State will ensure that his overall responsibility for the water environment is given direct statutory force, in the area where it matters most. Chapter 3 sets out more fully the background to this proposal and what it would entail.

Powers of the Secretary of State

2.6 If environmental quality objectives are to be clarified and given greater statutory force, it is essential that there are adequate powers to ensure that they can be given effect. Such powers must lie primarily with the Secretary of State, in view of his central responsibility for policy, though adequate powers must also be available to the WSPLCs to enable them to carry out their responsibilities.

2.7 The Secretary of State will require a number of specific powers to discharge his remit. These will include

(a) A power to ensure, subject to Parliamentary procedure, that WSPLCs implement specific national environmental policies:

Inevitably new requirements of national, including European Community environmental policy will from to time arise. Ministers should have powers, subject to Parliamentary procedure, to require that these policies are given effect by WSPLCs.

(b) Powers to prescribe precautions to be taken by anyone with custody or control of substances likely to pollute or impair water resources; and to designate zones within which any activities likely to damage water resources can be regulated;

Maintenance of river water quality can be jeopardised not only be regular discharges but also by accidental spillages and the unintended consequences of normal activities. Adequate powers to control such risks are increasingly important.

Section 5 describes how existing powers in section 31 of the Control of Pollution Act 1974 might be adapted and used to this effect.

(c) A power to establish inquiries on any matter relevant to maintaining the quality of natural waters;

There are already powers for the Secretary of State to establish local inquiries on individual abstractions and discharges and the local application of regulations. These should extend to quality objectives and standards when the arrangements described in section 3 are in place. When executive operation of environmental protection is the responsibility of private bodies the Secretary of State should also have powers to establish inquiries on any matters relevant to maintaining the quality of natural waters to ensure that the public interest can be properly taken into account.

(d) A power to require WSPLCs to furnish such information as Ministers may reasonably need to fulfil their duties.

While water authorities are within the public sector and the members of authorities are appointed by Ministers, exchanges of information with Government are continuous, with little need for formal arrangements. Once the authorities are privatised it will be appropriate that there be formal powers to require WSPLCs to furnish information on environmental matters to the Secretary of State. Existing information requirements will be reviewed with a view to simplification, avoidance of duplication and ensuring that they can be discharged by WSPLCs as cost effectively as possible.

Responsibilities of the WSPLCs

2.8 Historically, the principal means of ensuring water quality has been control over discharges of trade and sewage effluent to rivers, lakes, streams and other natural water courses, a control exercised to a system of formal consents. No such discharge is allowed unless it complies with the conditions set by the water authority (or formerly by the

river authority), and these conditions limit the amount of polluting material emitted from pipe or sewer. This system of controling individual emissions is vital to protection of the water environment and will continue when the water authorities are privatised. Section 4 describes more fully the current system, the role of the Secretary of State in ensuring that it is operated fairly, and proposals for improvement.

2.9 As part of their general responsibility for river basin management water authorities also discharge a wide range of other responsibilities for the protection of water quality. They undertake systematic monitoring of water quality and develop plans for improvement. Their pollution control staff play the principal role in the enforcement of section 31 of the Control of Pollution Act which forbids the entry of polluting matter to water, by policing water areas and undertaking prosections when necessary. They handle pollution emergencies and take appropriate remedial measures when they occur. Water authorities have major responsibilities in the field of conservation. Subsequent sections will explain how all these responsibilities will remain following privatisation, and how in some cases they will be developed.

Monitoring and Enforcement

2.10 The Secretary of State will need adequate powers to ensure that WSPLCs discharge their own duties in relation to pollution control. It will be important to ensure that the monitoring by WSPLCs of rivers and estuaries is carried out adequately and on a broadly consistent basis as to the number of sampling points and frequency of sampling. Sampling of discharges must also be carried out with regard to the requirements of particular areas, but also with regard to sound and broadly consistent criteria.

2.11 Water authority inspectors undertake general supervision and policing of water areas to enforce the controls on dumping, spillages and other entries of polluting matter. This extends to the general planning and management of natural waters. These activities are difficult to quantify or express in terms of output measures, but they are central to the general

management of water areas. WSPLCs will have a continuing interest in and responsibility for undertaking them. While the Government does not see a need for any substantial changes in current practice, its importance to environmental protection means that the Secretary of State should be in a position to impose requirements of a general character as to its scale and nature.

2.12 The Government has a wide range of powers on which it can rely in exceptional emergencies but in most incidents it will be the water authorities on which the obligations will fall. They operate, and review periodically, standard guidelines for dealing with emergencies. The Government will wish to ensure that this continues after privatisation, and to be able to satisfy itself from time to time that the procedures operated are sound. Proposals in a consultation paper 'Water and Sewerage Law' published on 21 March 1986 review certain of the powers of water authorities in relation to their functions for controlling others' operations (eg powers of entry) and these are relevant.

2.13 The above proposals for ensuring that monitoring and sampling are carried out adequately and consistently may most appropriately be implemented through regulations, statutory codes or as conditions of the operating licences under which WSPLCs will be regulated by the Director General of Water Services. Such approaches will allow greater detail and flexibility to be achieved. It will be for the Secretary of State to oversee and support WSPLCs in their role as pollution control authorities. To provide guidance on these matters, and in particular to monitor their own performance as abstractors of water and dischargers of effluent, a small inspectorate will be established within the Department of the Environment and Welsh Office. This will be an important new development.

Expenditure and Charges

2.14 As at present, it will not for the most part be possible for WSPLC's pollution control and environmental service functions to be undertaken on a profit-making basis. Some aspects of pollution control are susceptible of direct charges

(see section 6) and in some areas of recreation there will be greater scope for enterprise activities. Nevertheless a deficit on these activities may need to be accepted in the public interest and it is right that this should be recoverable by WSPLCs from the charges raised from customers of water and sewerage services.

2.15 It is therefore important that investors in the new companies, as well as those who enjoy the non-profit-making services, should be aware of their financial implications. The figures below are extracted from the authorities' 1984/85 accounts. They show how much the 10 water authorities spent on the five environmental services, what income they received from each, and how much support these activities had from environmental services charges - ie from the bills of water customers and users of sewerage services.

£000s

	Water Quality Regulation	Pollution Alleviation	Recreation & amenity	Fisheries	Navigation	TOTAL
Expenditure	17,328	4,445	6,961	8,296	4,346	41,376
Income	115	91	2,630	4,290	1,859	8,985
Support from the Environmental Services Charge	17,213	4,354	4,331	4,006	2,487	32,391

Thus for all environmental services, the extent of support from the Environmental Services Charge in 1984/85 was a little over £32m. The Government is committed to the principle that the costs of these activities should be recovered to the fullest possible extent from those who benefit from them. However the Government also considers it right that they should receive a reasonable measure of support from the main services. At present this support amounts to less than 2 per cent of the authorities' gross turnover. The Government considers this to be a ~~reasonable~~ burden on the consumers of the main services, and intends that the WSPLC's licences should provide for support of this order to be continued.

2.16 The Director General will have a general interest in WSPLC's exercise of environmental functions, but will in particular be concerned with matters of finance and consumer representation. As explained in the White Paper (paragraph 75), he will be given the responsibility of determining from time to time the extent to which the environmental services should be supported from charges raised from customers for water and sewerage services. In this task he will need to take account of obligations WSPLCs may be required to fill by changing national or EC environmental policies and have regard for the interests both of consumers and shareholders. In striking this balance he will be assisted by the decision announced in the White Paper that he should in future appoint the members of Consumer Consultative Committees, including those responsible for environmental matters.

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SECTION 3

ENVIRONMENTAL QUALITY OBJECTIVES AND STANDARDS

3.1 When the water authorities are converted into Water Service Public Limited Companies, they will continue to be the agencies responsible for protecting the water environment - as they must be if the benefits of integrated river basin management are to be preserved. As now, they will be the agents of national policy for the environment, and their efforts in that direction will be governed by a system of environmental quality objectives which, henceforth, will be set on a statutory basis by the Secretary of State.

3.2 The water authorities established under the Water Act 1973 inherited a situation in which many discharges were subjected to standard conditions set by their predecessors unrelated to the effects of the discharges on the receiving waters. Some of the conditions were unnecessarily stringent while others were not stringent enough. Water authorities in carrying out the Secretary of State's duties to restore and maintain its wholesomeness of rivers were not required to produce programmes for improvement of these rivers. This situation led to the National Water Council (NWC), after extensive work and consultation, issuing in 1978 the policy statement "River Water Quality: The Next Stage." The NWC recommended amongst other things that river quality objectives to provide a better basis for setting consents and for planning investment to improve water quality should be determined by water authorities as far as practicable for rivers, canals and major streams. The then Government endorsed the NWC's statement.

3.3 All water authorities have set quality objectives for individual stretches of watercourse directly related to the use or potential use of the water, for example abstraction of drinking water, support of fisheries, recreation, amenity value. They may be short term reflecting current use, or long term representing a target use. The objective for each stretch of river can be expressed in terms of a quality classification, stating broad categories of use which can then be further expressed in terms of limiting quality criteria for such things as biochemical oxygen demand and ammonia content. The NWC produced a classification of river quality in which the highest classification, for example, is Class 1 which applies to water of high amenity value and high quality suitable for abstraction for drinking water and game fisheries. The quality criteria for this class includes a biochemical oxygen demand not greater than 5 milligrammes per litre and an ammonia content not greater than 0.9 mg/l.

3.4 River classification criteria alone however were not sufficiently precise to form a basis for protection of rivers. Water authorities therefore also set quality standards which generally represented the maximum quantity of a substance, for example metals, which could be present in the water if its current or future use has to be maintained or achieved. Discharge consent conditions were then set individually in the light of levels of substances already in the water. This system of limiting the amount of a substance in the water itself rather than applying an across the board limit on the amount permitted in any discharge has added importance in that it can also be used to give effect to the requirements of EEC Directives on water quality.

3.5 As part of the need to restore and maintain the wholesomeness of rivers, water authorities have thus used three mechanisms - the setting of water quality objectives and the complementary water quality standards plus detailed control over discharges through individual consents. Consents are discussed in ~~chapter~~ section 4 and the remainder of this ~~chapter~~ section considers how the existing procedures for objectives and standards should be adopted and built upon in the future.

3.6 Environmental quality objectives and standards have three main functions:

a. they provide a basis for the planning and investment necessary to maintain and improve water quality;

b. they provide an ~~(scientific)~~ explicit framework for controlling discharges of effluent, through discharge consents;

c. if published, they inform the community at large about goals for water quality and permit informed discussion about their adequacy.

Under the present voluntary arrangements they have proved helpful at a regional level. The Government considers that they could also play an important role nationally. If they were laid down centrally, they could help to establish national priorities, such as the Mersey Basin Campaign, for environmental improvement and control. The Government also believes that they could be usefully extended beyond their present application almost solely to inland waters to cover all types of water protected under Part II of the Control of Pollution Act 1974. The Government therefore proposes that the Secretary of State should be empowered to set objectives and quality standards, initially for all significant

inland waters, and subsequently for estuarial, coastal and underground waters, and to specify a timetable within which they are to be achieved. WSPLCs will be required to assess applications for discharge consents in the light of the objectives and standards. Objectives and standards will also be one of the matters which the Secretary of State will take into account in considering the WSPLCs' own applications for discharge consents, and in determining appeals by third parties against their decisions. WSPLCs would, however, be able to set more stringent objectives and standards in the light of local circumstances.

3.7 In order to launch this new system quickly and on a firmly established clear basis the Government proposes to use initially the objectives which the water authorities have already adopted. These objectives are widely understood, have been the subject of local consultation, and can be related to the classifications used as a basis for water quality measurement in the 1980 River Quality Survey. These classifications will again be used in this way in the 1985 Survey due to be published in 1986. Using them at the outset will ensure continuity and provide a good basis for comparison between progress in different WSPLC areas, and between the present situation and any future review.

3.8 Quality objectives for a stretch of river may not be appropriate on a once and for all basis. They will need to be amended to reflect changed circumstances. The Secretary of State will therefore have a power to review objectives at intervals of not less than 5 years. Quality standards will also need to be reviewed, particularly to take account of the requirements of EEC Directives. No restriction on the frequency of reviews of standards is proposed.

3.9 Public participation, backed up by adequate access to information, provides a major stimulus to effective environmental protection. There will therefore be publicity for the reviews of objectives carried out by the Secretary of State. One possibility might be to consult local authorities, WSPLCs and other bodies with a particular interest during the early stages of a review, and then to allow general public comment on a published set of proposals. An alternative might be to consult a specified, but wide, group of environmental, local government and industrial interests. In either case, the Secretary of State would be empowered to hold a public inquiry in connection with any or all of the revised proposals.

3.10 Clearly the relevant information on quality objectives and existing water quality must be publicly available. This could be achieved either by the publication of a special report open to inspection at specified locations, or by the extension of the existing public registers to accommodate this information. The same applies to availability to the public of information on quality standards.

3.11 Thus under the government's proposals the principal day-to-day tasks involved in the protection of the water environment will continue after privatisation to fall to the present authorities, as they must if the benefits of integrated river basis management are to be preserved. But the lynch-pin of arrangements for safeguarding the environment will be the system of environmental quality objectives set, on a statutory basis, by the Secretary of State.

3.12 In summary, such objectives will ensure a consistent basis for national policies and allow the Government's objective of maintaining or improving the quality of river and estuarial waters to be carried forward. They will provide guidelines for WSPLCs in discharging their operational functions and benchmarks against which their performance can be measured. They will provide a clear basis for informal public discussion of water environment policies and resources.

SECTION 4

REGULATION OF DISCHARGES

4.1 Water authorities are charged by statute with exercising a number of responsibilities of a regulatory nature, involving the granting of licences and consents which determine the rights of others to use or enjoy natural waters. These include abstraction licences and fishing permits, but the most important for environmental water quality are the comprehensive controls they exercise on discharges of trade and sewage effluent. They are also of great importance to industry in relation to their ability to dispose effectively and economically of their wastes and effluents.

4.2 The major controls over effluent discharges are contained in Part II of the Control of Pollution Act 1974 which reenacted and extended previous legislation to cover virtually all waters. The 1974 Act also provided for public involvement in pollution control: applications for consent are advertised and comments invited; public registers containing details about water quality and discharge consents have been opened. This ensures that decisions reached and action taken must be publicly defensible. In addition the Secretary of State consents water authorities' own discharges, can call in any application for his own determination and there is a right of appeal to him by third parties against the decisions of water authorities; these three features of the system ensure evenhandness.

4.3 The new powers discussed in the preceding chapters, particularly the Secretary of State's power to set objectives and standards, will build on the 1974 Act provisions to provide a firmer framework of control, also open to public comment capable of safeguarding water quality after privatisation.

4.4 It is desirable for effective environmental management that the granting of consents and the conditions to be attached to them should lie with the bodies responsible for integrated river basin management, but some concern has been expressed that it is inappropriate that such jurisdiction should fall to a private body answerable to shareholders in view of the conflicts of interest that could arise. There could moreover be concern that WSPLCs might be inclined to require higher standards of other discharges than they attain for their own discharges. WSLPLCs could thus shift some expenditure elsewhere. The Government has therefore considered alternative arrangements. One possibility would be to transfer formal statutory responsibility to the Secretary of State and permit the WSPLCs to operate the controls as his agents and subject to the terms of an agency agreement. While this might allay anxieties its practical effect in ensuring equity and even-handedness

would be less than the very considerable safeguards against abuse which have recently been built into the effluent discharge consent system and which will continue after privatisation. In particular the key safeguard - the right of appeal direct to the Secretary of State - would not be exercisable if the body granting the initial consent did so as his agent.

4.5 The Government concludes therefore that it is safer to rely on the present comprehensive safeguards - the power to call-in and the obligation to include all relevant documents in public registers as well as the appeal provision - rather than effect a formal transfer of responsibility which would be of little practical effect.

4.6 There is a case, however, for seeking so far as practicable to simplify and streamline existing procedures so that they are easier to understand and to operate. The rest of this section consider ways in which this might be done.

Special Provisions as to Discharge Consents

4.7 Section 32 of the 1974 Act extended discharge consent requirements inter alia to:

a. discharges of trade and sewage effluent from buildings and fixed plant to land and land-locked ponds and lakes; and

b. discharges of other matter from a drain or sewer to waters controlled by the Act.

The purpose of these provisions was to enable every kind of discharge which might conceivably pollute water to be controlled. In practice however controls in the first category apply to many harmless discharges while controls in the second category apply almost exclusively to rainwater. Control of discharges which do not cause pollution consumes time and resources which could be more effectively used. It is therefore proposed to remove the compulsory control over these discharges and to substitute a discretionary control which could be used in the rare cases where pollution could occur. The Government is considering whether published guidance on the use of the discretionary controls would be helpful.

4.8 Water authorities already have a discretionary control over highway drainage. This would be continued with the new discretionary controls. In both cases WSPLCs would have the power to serve a notice applying the 1974 controls to any specified discharge. There would be the normal right of appeal to the Secretary of State against the refusal of consent or the terms and conditions of any consent given.

4.9 Under EEC directive 80/68/EEC on the protection of groundwater against pollution caused by certain dangerous substances (17 September 1979) significant discharges of certain dangerous substances (eg cadmium and lead) must be controlled even if made indirectly to underground water. It is therefore proposed that the Secretary of State should have power should circumstances prove necessary to prescribe substances the discharge of which, if made into the ground without WSPLC consent, would constitute an offence. Anyone wishing to discharge such a substance would need to apply for consent (unless the discharge were the subject of a waste disposal licence issued under Part I of the 1974 Act) and normal procedures would apply.

4.10 The Secretary of State has the power (under section 37(2) of the 1974 Act) to direct that any consent should be varied or revoked. This power is linked with a duty of water authorities to review consents. Neither the Secretary of State nor the authorities can vary or revoke a consent within a specified period unless the discharger agrees.

4.11 Part of section 38 of the Act which has not yet been brought into force provides for a water authority or the Secretary of State to vary consents early if it is considered necessary to do so for the protection of people likely to be affected by discharges. Where consents are varied early compensation is payable unless the variation is needed as a consequence of a change, which could not have been reasonably foreseen when the consent was granted, in the information available relating to the discharge. Compensation would not be payable, for example, where it was discovered that one discharge was reacting with another to produce a harmful effect if the reaction could not reasonably have been predicted.

4.12 The Government is considering whether to bring this provision into force or whether to limit the power to direct early variation solely to those circumstances where compensation would not be payable under the 1974 Act. The right of appeal to the Secretary of State against the terms and conditions of a varied consent would remain. Another possibility would be to provide that only the Secretary of State could direct an early variation, restricting the grounds for such a variation to the protection of public health or the implementation of essential national policy (for example to give effect to international agreements). In this case also the payment of compensation would not be appropriate.

4.13 Water authorities may also vary consents early when aquatic flora and fauna have been harmed by discharges of effluent (Section 46(1)-(3), also not yet in force). The Government considers that more effective protection for aquatic life can be provided on the basis of the measures described in Chapter 7 below rather than within the framework of the discharge control system. In particular those measures are addressed to preventative as opposed to remedial action. It is therefore proposed to repeal section 46(1)-(3). WSPLCs would however retain the power provided by section 46(4)-(7) to undertake operations to protect or restore flora and fauna. As an additional safeguard the Secretary of State would be empowered to direct the early variation of a consent governing a discharge found to be seriously damaging to aquatic flora and fauna. WSPLCs will inherit the water authorities' duty to take account of the effects of discharge proposals on flora and fauna before setting consent conditions. Early variation is likely only in cases where damage to aquatic life could not have been reasonably foreseen. A question for consideration is whether there should be any provision for compensation in these circumstances.

4.14 There are cases where a discharger wishes to make a discharge for a period less than two years and there is some doubt whether temporary consents can be issued in view of the minimum period specified in the Act. If necessary, there will be provision for consents of less than two years, with the discharger's agreement.

Publicity

4.15 Section 36 of the 1974 Act requires water authorities to advertise applications for discharge consent. An authority may, however, waive the requirement to advertise an application if it intends to give consent and is satisfied that the proposed discharge will have no appreciable effect on the receiving water. If the proposals outlined in paragraphs 4.3 to 4.5 above are adopted most discharges of this nature will no longer be the subject of applications. It is doubtful that any discharge for which an application must be made could be classified as having so slight an effect as to merit exclusion from advertising. It is therefore proposed that all applications should be advertised with the exception of those which are the subject of an exemption certificate issued by the Secretary of State under section 42 of the Act. Dischargers are already required to pay for the advertisement of consent applications. Since all applications would have to be advertised under these proposals it would minimize delays if the discharger placed the advertisement before making a formal application to the WSPLC. Evidence that the proposed discharge had been publicised would then need to be submitted when the application was made. This would be in line with procedures for planning applications.

4.16 At present advertisements must be placed in the London Gazette as well as local newspapers. It has been suggested that this involves additional expense for the discharger which is not warranted by a comparable increase in the audience reached. While it is true that applications for discharge consents will be of most interest to local people who are likely to consult local papers it is also the case that many national organisations, particularly environmental bodies, will wish to be aware of proposed discharges. It is doubtful however if this amounts to a sufficient justification for the requirement to advertise in the London Gazette, and it is proposed that this should be discontinued.

Public Registers

4.17 Since July 1985, when the water authroities instituted registers under the Control of Pollution Act, 1974, records have been available for public inspection of discharge consents and their conditions - ie what water authroities or others are permitted to discharge into rivers and other controlled waters; and the results of monitoring each discharge for compliance with consent conditions. Thus these registers enable the public to keep an informed eye on the way in which dischargers are complying with what is required of them. The Government's aim is that registers should make a substantial contribution to protecting water quality. There have been suggestions, from various quarters, that extra information should also be recorded in registers; eg particulars of aquatic flora and fauna, or data on river flows, or factual records of incidents giving rise to pollution. The Government would like at this stage to consider seriously the possibilities for improving the value of registers; and before moving to make the registration of further information obligatory, the Government would wish to satisfy itself that the extra information fulfilled a valuable purpose, and that this value was not outweighed by considerations of practicality or cost. The Government would welcome proposals which helped it to take these various considerations into account.

Minor Amendments

4.18 The Government is also considering revision of the following matters:

Specified underground water: the existing definition requires a water authority to specify the use to which underground water are being or will be put. This has proved a practical difficulty and it does not fit well with the requirements of EEC Directives. The type of map required by the Act has also proved restrictive and less useful and informative to the public

than expected. The current definition may therefore be inadequate to identify the underground water which needs protection. One possibility might be to redefine it in terms of water in underground strata as in the Water Resources Act 1963. This however might be too wide a definition in cases of casual pollution covered by section 31 of the 1974 Act. The Government would welcome advice from water authorities and others on the best approach.

Restricted waters: these are defined as waters in tidal rivers designated by regulations and water in other areas prescribed by the Secretary of State where vessels are moored in close proximity to one another; no regulations or prescriptions have yet been made. Restricted waters appear in Part II of the 1974 Act in two contexts. People are prohibited from dumping solid waste in restricted waters, and there are controls on wastes discharged from vessels. The former controls seem of little real value, since there is adequate protection in the Food and Environment Protection Act 1985 and private harbour legislation. For the latter it would be possible to apply the powers to make byelaws controlling vessels (section 33) automatically to tidal rivers thus obviating the need for regulations. References to restricted waters would be repealed.

Solid refuse from mines and quarries: section 31(3) of the 1974 Act provides a defence against the charge of causing or permitting pollution if the offence charged results from the entry of mine or quarry waste deposited on land with the consent of the water authority. It is unclear whether this provision is still of relevance and the Government would welcome information about the number of consents issued for this practice and the need for the defence to be continued.

Controlled waters: portions of certain estuaries fall outside the present definition of controlled waters and therefore cannot be protected under the 1974 Act. The Government intends to remedy this by extending the Secretary of State's power to prescribe additional parts of the sea as controlled waters.

Sewage effluent: the definition of sewage effluent covers all effluent from the sewerage works of a water authroity and thus includes surface water discharges. Other surface water discharges are not classed as sewage effluent. The Government is considering whether this should be amended to place water authorities' surface water discharges under the same controls as other surface water discharges.

Water authorities' areas: the definition contained in section 56(4) taken with provisions in the Thames Water Authority Constitution Order 1973 means that the greater part of the Thames estuary falls within the areas of three water authorities. Amending legislation will be necessary to restore pollution control in the estuary to the sole jurisdiction of the Thames Water Authority. All discharges to the estuary made by WSPLCs will continue to be controlled by the Secretary of State.

SECTION 5

REDUCING POLLUTION RISKS

5.1 Whilst there are effective systems to control regular effluent discharges, there have until recently been few comparable arrangements to prevent damage from pollution incidents arising from other sources. There has been a steady rise, for some years, in pollution from occasional spillages and other accidents and these can do serious damage to surface and ground water sources. The Government has considered that this is the most important area in which to strengthen water pollution policy and therefore brought into force last year a number of powers within the Control of Pollution Act relevant to these problems. This section explains how the Government expects them to be used after privatisation.

Increase in pollution Incidents

5.2 Pollution incidents represent a continuing risk to surface and underground waters:

- The number arising from industrial sources continues to show some increase. In Severn Trent WA area there were 2014 in 1984-5 - the highest number yet recorded. While the great majority were minor, incidents such as those recently on the River Dee in Wales show the continuing risks of widespread pollution of supplies, especially since 30% of water supplies still come from river abstraction, often direct without bankside storage;

- The rate of growth of significant incidents from agricultural sources has been even more marked - to nearly 3000 last year. While the increase may partly reflect increased water authority vigilance and changes in reporting practices there is widespread recognition, both within the agricultural community and more widely of the need to reduce pollution from such sources.

- These problems have their cost. They consume a rising proportion of water authority pollution control resources - now about 30%. Although in absolute terms the costs may not be large, it is desirable to reduce them if that can be achieved in ways which are cost effective both for the authorities and the community at large.

5.3 Until recently water authorities have had to depend largely on informal and voluntary arrangements to protect their resources. Some have prepared valuable Aquifer Protection Policies but these rely ultimately on persuasion and voluntary co-operation. Others have been led to purchase extensive tracts of the gathering grounds they consider need protection. Others have relied heavily on local by-laws: while effective, it is doubtful if in the longer term they will represent the best way of tackling what are often general rather than local problems.

5.4 The Government has already taken a number of measures recently to reduce pollution incidents. In particular, the Code of Good Agricultural Practice, made under Part II of the Control of Pollution Act 1974 recommends practices relating to the use of fertilizers, manures, farm wastes, silage and pesticides, which, if followed, would largely avoid water pollution arising from these sources. Additionally the Ministry of Agriculture, Fisheries and Food has introduced new provisions for capital grants on various environmentally attractive investments and arrangements whereby water authorities are consulted at an early stage in respect of those investments that have a high pollution potential, for example silage storage facilities. Beyond this the Agricultural Development and Advisory Service continues to provide advice through a wide range of scientific, technical and business management services including ways of minimising the risks of pollution.

5.5 Nevertheless the Government considers that especially after privatisation, there should be enforceable powers addressed specifically to the avoidance of pollution incidents. Below are set out the ways in which the Government envisages using three of the 1974 Act powers brought into force last

year: section 31(4) which provides for the making of regulations dealing with precautions people must take to prevent harmful material from polluting waters; section 31(5) which provides for the prohibition or restriction of potentially polluting activities in designated areas; and section 46(4) to (7) which empowers a water authority to remedy of forstall the entry of poisonous, noxious or polluting matter into water.

General Precautions

5.6 Section 31(4) is an important general power. While some Planning and Health and Safety legislation can reduce pollution risks, this is the only provision for general precautions specifically against water pollution. It should provide a major instrument of water environment policy after privatisation, and the Government will consider whether any amendment or widening of its terms is appropriate.

5.7 The precautions must be specified in regulations. These should be relevant generally rather than to particular kinds of area. While there is no restriction on what the regulations can cover, so long as the purpose is to protect the water environment, the Government considers that they will primarily be applicable to the location, construction and maintenance of storage facilities. This might include provision for adequate bunding, or an impermeable base, for such substances as fuel, oil, liquid and solid chemicals and biocides. Regulations may also be relevant to the disposal of surplus chemicals and their containers to the extent that other statutory provisions are not relevant. On a number of these matters the Government has published advisory codes in recent years. The most important is the Code of Good Agricultural Practice, which, amongst other things, makes provision for storage of silage and slurries. In view of this code it is unlikely to be necessary to make regulations to cover silage and slurries but the Government will be prepared to consider making regulations on these if it is clear that advisory codes are not proving successful in reducing pollution risks.

Water Source Protection Zones

5.8 In the Government's view section 31(5) - which allows regulation of specified activities in designated areas - will mainly be useful for the protection of sensitive water resources, for example underground water used for abstraction, from the indirect pollution which can be caused by normal, everyday practices.

5.9 At present the power can be applied only in specified locations, and there is provision for a local inquiry to be held when a new location is proposed. The power could be useful but there is at present no power to apply controls on a more generic basis for the protection of particular kinds of water source. Aquifers, stretches of major rivers from which there is direct abstraction and the gathering of grounds of reservoirs are cases in point. General powers of designation of this kind could largely supersede existing by-laws, make existing informal policies for resource protection more effective and provide a common and simplified regime for key areas at risk. This would be helpful both to environmental protection generally and to WSPLCs in maintaining protection of the resources on which they depend.

5.10 Since Parliament enacted the Control of Pollution Act a good deal of research by water authorities and others has been done on common causes of pollution, the routes which polluting substances take through water courses and aquifers, and the areas over which controls may need to operate to be effective. Most authorities have identified about three rivers where major stretches may merit particular attention. One authority, particularly dependent on aquifers for supply has about /‾X‾/ boreholdes of major importance where special precautions against pollution risks may be justified within a radius of perhaps 1 km or 50 day's travelling time for polluting substances. Only in the upland gathering grounds of major reservoirs might extensive areas of control appear necessary. Controls may be necessary on storage of oils and chemicals; mining; oil and gas drilling; and the location of farm waste storage, for example silage effluent tanks and slurry stores.

5.11 In the circumstances the Government considers that it may be desirable to amend section 31(5) to facilitate designation of protection zones for major water sources on a standard and simplified basis. The two main features would be:

(a) a power to designate areas without individual local inquiries; and
(b) the application of common regulatory regimes, including a requirement for the consent of the WSPLC to specified activities.

5.12 At present the Act requires that any regulations proposed under section 31(5) should be advertised and objections considered. If objections are not withdrawn the Secretary of State must hold a local inquiry. Once regulations are made the consent of the water authority must be obtained and any reasonable conditions observed if the activities specified in the regulations are to be undertaken. There is a right of appeal to the Secretary of State and until the appeal is determined the consent conditions are not binding. Either a further local inquiry or a hearing must be held if the appellant requests.

5.13 The requirement to hold an inquiry if there are objections to the regulations is necessary where proposals are purely local in effect and raise issues peculiar to a specific location. Water Source Protection Zones would, however, be designated on a generic basis covering kinds of activities known to cause pollution and types of area known to be at risk. Local inquiries would be inappropriate because uniquely local issues would not arise. There remains, however, the need to protect individuals whose livelihood may be affected by excessively stringent use of controls on activities which would otherwise be unrestricted. This is provided by the requirement that consent to undertake or continue an activity must not be withheld unreasonably and by the right of appeal to the Secretary of State. The appellant's right to require a hearing or inquiry will also remain.

5.14 An effective protection zone policy would be a major advance in water pollution control policy. It would be a discriminating control over particular water sources and particular risks, without the need for cumbersome and repetitive local designations. Protection zone policies are widely used in our EEC partner countries and experience there will be helpful in the detailed planning if, in the light of comments, the Government concludes that it would be sensible to extend use of section 31(5) in the way proposed.

Tackling Emergencies

5.15 The provisions of section 46(4) to (7) are of great importance and are already proving their worth. They provide authorities with the power to undertake any operations necessary to prevent polluting matter from entering inland, underground and coastal waters or to clear up and dispose of such matter if it is already in the water. The power includes operations to restore water and the flora and fauna in it. The cost can be recovered from the person who was likely to cause or who caused the pollution to occur. While these are wide ranging powers for private bodies to posses, they must be available to WSPLCs after privatisation. The Act requires that any costs should be incurred necessarily and unnecessary costs can be challenged so there is protection against abuse.

SECTION 6

INCENTIVES AND CHARGING

6.1 In line with Council Recommendations of the OECD in 1972 and of the European Community in 1975, successive governments have for some years been committed to the Polluter Pays Principle, that is that those who cause pollution or whose activities make protective or remedial measures necessary should bear the resulting costs. That is the only fair approach; and gives actual or potential polluters the incentive to find ways to minimize the harm or damage they cause; thus it also promotes responsible practice. This section describes how the Government proposes to introduce charging, where practical, to the main areas of pollution control. Charges will apply both to authorised regular discharges and to pollution incidents.

Charging for Sewage and Trade Effluent Discharges

6.2 Water authorities at present levy charges to cover the costs of trade effluent discharges to sewer. The primary purpose of this is to cover the costs of treatment within the authority's sewage treatment system. No corresponding service is provided by the authority in the case of direct discharges to rivers and estuaries, and for this reason any proposal to charge for direct discharges has been unpopular with industry. Section 52 of the Control of Pollution Act 1974 empowers authorities to levy charges in respect of discharges to rivers but has not hitherto been implemented.

6.3 Effluent discharges to water nevertheless impose appreciable costs on pollution control authorities. These extend beyond the administrative costs of processing consent applications to include in particular the costs of monitoring the discharge and its impact on the receiving waters; and any survey costs which may be entailed by the initial consideration of the consent application.

6.4 Some member countries of the EEC have wide-ranging systems of charging direct dischargers and following a recommendation in the Tenth Report of the House of Lords Select Committee on the European Communities (1982/3 Session) to do so, the Government has reviewed arrangements in other member states and their possible implication for Britain. (The research report considered during this review can be obtained at cost from Environmental Resources Ltd, 106 Gloucester Place, London W1H 3DB).

6.5 There are 3 main options:

a. Incentive charges: make the polluter pay towards any damage his effluent may cause to the environment. This applies even where such effluent is within existing consent conditions. The aim is to give the polluter an incentive to reduce his effluent further where it is cost-effective to do so. Such charges would be based on the amount of harmful substances in effluents, and if possible also on the vulnerability of the local environment. To be fair they would have to be levied on all direct discharges, including those from WSPLC sewage treatment works.

b. Distributive charges: are the same as incentive charges in most respects except for what happens to the charges. These are collected by a central agency and returned to dischargers as subsidies for improved pollution control, typically as a percentage subsidy on investment in new control equipment.

c. Cost recovery charges: remove from direct dischargers only the costs directly attributable to the control of water quality, such as costs of:

- granting and administering discharge consents

- monitoring compliance with consents

- preventing or cleaning up after pollution incidents where direct dischargers accidently or otherwise greatly exceed their consents.

6.6 The first two options depend on some assessment of the relative costs imposed by the toxicity or other harmful effects of the various substances discharged. This is complex and requires much work in estimating the relative polluting effects of different substances and the degree to which concentrations and quantities of substances should be taken into account in the charging formula, while some experience in Europe suggests that acceptable and practicable formulae can be established, it is doubtful whether early conclusions could be reached which would command general confidence.

6.7 Although distributive charges may appear the more acceptable course given their more direct contribution to reducing water pollution, both incentive or distributive charges might be seen as a tax on direct dischargers' uses of the water environment which until now have been regarded as a right granted free of

harge, within the consent conditions laid down by the water authorities. It will not be appropriate for WSPLCs to levy charges of this nature both because they will be privately owned companies and because they would be liable to pay the charges on their own discharges. The Government does not propose to adopt either of these options at present.

6.8 The third option, which the Government proposes to adopt, has the merit of relating charges directly and clearly to costs incurred by the water authority or WSPLC. It is much simpler and less controversial than incentive or distributive charges, although these also have advantages. Where a discharge is particularly noxious, particularly large, or not effectively controlled, this will be partly reflected in the WSPLC's costs which will be passed on to the discharger under the proposed cost recovery system. It will provide an incentive for improvement.

6.9 In the light of the responses to this consultation paper, the Government will develop and discuss with water authorities, and other interested parties, detailed criteria and scales of charges which are fair, equitable and can be properly audited.

6.10 It has also been suggested that pollution control authorities (ie Government Departments in respect of discharges by WSPLCs, and the WSPLCs in respect of all other discharges) should be required to levy penalty charges where effluent discharge consents are exceeded. Imposition of penalties could not be discretionary and penalties would have to be at a relatively high level if they were to be effective. So this would be a major innovation.

6.11 There are practical difficulties in such a system. Sampling and monitoring arrangements would have to be standardised and relatively inflexible, and any penalties imposed would have to be subject to challenge in the courts. It could nevertheless be an effective deterrent and the Government will therefore consider the issues further. At this stage, however, it seems doubtful if such powers would be appropriate to pollution control authorities and it is difficult to see how they could be made to relate satisfactorily to existing remedies through the courts against non-compliance with consents.

Costs of Pollution Incidents

6.12 As described in Chapter 5 the number of pollution incidents, from industrial and agricultural sources, has risen rapidly in recent years and now accounts for about 30% of pollution control costs. In July last year the Government brought

into force section 46(5) of the Control of Pollution Act 1974 to enable water authorities to recover from those responsible the costs of preventing pollution incidents or of remedying their effects. These cost recovery powers must be used in a fair and reasonable manner and the Act requires that the Authority be able to show that costs were not incurred unnecessarily. In view of this protection there is no reason why the powers should not be retained by WSPLCs after privatisation.

Other Costs

6.13 Much of the work on pollution control, inspection and sampling is concerned with the general condition of rivers and estuaries and does not relate to individual discharges. The costs involved could be apportioned amongst industrial dischargers but this would be unfair in that they are incurred for the benefit of the whole community. They should instead be covered by main service charges, along with any other pollution control costs which cannot be allocated to particular polluters. As described in Section 2, the Director General will be able to take such costs into account in reviewing the price formula in the operating licence.

SECTION 7

7. PROGRESS IN CONSERVATION

7.1 All the measures discussed in the earlier sections of this paper are relevant to conservation. This reflects its essential character. It cannot be confined to a particular set of actions or policies. With utility services in particular it is an attitude or approach which must influence all its operations. Recognising this the Government in the Wildlife and Countryside Act 1981 extended water authorities' obligations under the Water Act 1973 to have regard to the desirability of conserving the natural environment to a wider duty to perform all their functions so as to further conservation. The Government continues to support this approach - not only for habitats, but also for landscapes and the archaeological and historical heritage - and therefore proposes to ensure existing statutory duties continue after privatisation.

7.2 While such general obligations can be valuable, arrangements in four particular areas will be critical for ensuring further progress in conservation. The key questions are:

- Will controls on polluting discharges harmful to aquatic life be under full and effective control?

- Will good practices be followed in regulating conflicting recreational and other uses likely to hinder conservation?

- Will there be adequate powers for the special protection of particular habitats and landscapes?

- How can good conservation practice be ensured in water supply, sewerage, drainage and other functions of WSPLCs?

The Government's proposals to ensure continuing progress in each of these areas are summarised below.

Protection from Pollution

7.3 With the withdrawal of COPA exemptions announced by the Environment Minister on there will be comprehensive control of polluting discharges and section 4 described how their effectiveness would be maintained. In particular Ministers will be provided with effective means to ensure that polluting discharges to beaches and coastal waters can now be brought progressively under control.

7.4 The Government recognises however that controls on casual entries of polluting matter - spillages and dumping - are not quite complete. In particular, water which is land-locked and does not discharge into other water - ponds and some lakes - have generally been excluded from pollution controls. Part II of COPA only protects such enclosed waters from dischages of trade and sewage effluent made from buildings or fixed plant, although individual ponds and lakes and enclosed waters of a specified type could be protected by means of regulations made under section 56(3). Ponds and lakes constitute a valuable habitat and source of food for a rich and varied range of animal and plant life, and there is some evidence that this environment may be under increasing threat from pollution. The Government therefore proposes to consider, in the light of responses to this consultation, whether section 31 of the 1974 Act should be extended to make it an offence to cause or permit any poisonous, noxious or polluting matter to enter any enclosed water.

Conflicting Uses

7.5 As indicated earlier the Government believes that water authorities have a good, and steadily improving, record in managing conflicting recreational and other uses of water and reconciling them with conservation. The decision to privatise authorities on their present integrated basis - allied with their general duty to further conservation - will enable this to continue, but the Government has considered whether it could be assisted by any further specific measures.

7.6 On balance recent experience of the difficult problems associated with anti-fouling paints on boats suggest that existing powers for regulations and by-laws, for exceptional problems of this kind, may be adequate. It is however for consideration whether there are adequate powers for the general control of the boats and pleasure craft now drawn in increasing numbers to attractive areas of water, including tidal waters which are rich in flora and fauna. Controlling boats, and in particular discharges of sewage effluent from them, is important to conservation.

7.7 Sections 33,47 and 48 of COPA, which deal with those matters, have not so far been brought into force. They provide:

(a) a power for water authorities to make by-laws prohibiting or regulating the use on non-tidal rivers of boats with sanitary appliances which discharge into water;

(b) a prohibition, originally to take effect after 1978, on all boats with sanitary appliances discharging into non-tidal rivers;

(c) a power for Ministers, by order, to extend the prohibition to tidal waters and areas where vessels are moored in close proximity;

(d) a duty for water authorities to arrange for the collection of waste from vessels prohibited from discharging into water and to provide washing out facilities for such vessels;

(e) a power for water authorities to provide sanitary and washing facilities for boat users;

(f) a power for water authorities to make by-laws prohibiting non-registered boats from specified inland waterways;

(g) a right for people on registered vessels to use facilities provided by water authorities free of charge.

7.8 During the 10 years that these provisions have remained unimplemented, little evidence has been drawn to the Government's attention of the need for them. Many of them

would apply in areas where they are not needed, and would require a cumbersome procedure to ensure that they are applied in areas where they are needed. Enforcement would be very difficult. WSPLCs would have to provide facilities, the costs of which could only be recovered by punitive charges and this would discourage observance of the controls. In the end the costs would come back to all those paying water charges. In the absence of clear need, the Government considers on balance, that these provisions can be repealed with the exception of the by-law provision ((a above) in section 33(1) which is valuable and should now be implemented.

7.9 This by-law making power could ensure proper regulation in places where it was needed. It could be consolidated with other by-law making powers to provide a general power dealing with the regulation of activities likely to cause pollution. It should also be extended to cover the tidal reaches of rivers. If a WSPLC failed to make by-laws where these were clearly necessary, the Secretary of State could designate a water protection zone.

Areas for Special Protection

7.10 Some water areas are of exceptional importance for conservation because of their special landscapes, flora or fauna, and the Government will continue to ensure they receive exceptional treatment. For instance, it proposes to introduce at the earliest possible opportunity a Bill to provide a strengthened Broards Authority for better conservation of this unique area.

7.11 But smaller areas are also important. Here there are the existing procedures for Sites of Special Scientific Interest, but the Government proposes that there should be scope for further protection, where necessary, by use of the recently implemented powers of section 31(5) of the Control of Pollution Act. In effect these make possible, inter alia, designation of the Water Environment Protection Zones where activities likely to pollute water - and hence damage the flora and fauna dependent upon it - can be regulated

by a requirement that they be undertaken only with the consent of the water authority. The controls can be applied to activities conducted either on the water or on the banks and associated land, so it is a measure of considerable potential significance for conservation.

7.12 Designation under this provision is by the Secretary of State, on his own initiative or after representations from WSPLCs, the nature Conservancy Council, the Countryside Commission or other interested bodies. Operating the controls would impose some limited costs on WSPLCs which would, like some of the other environmental protection activities, be recovered through main service charges.

Promoting Good Practice

7.13 Effective conservation of the water environment depends not only upon how WSPLCs can continue to regulate the actions of other users of water space, but also upon how they conduct their own operations of water supply, sewerage and drainage.

7.14 A number of water authorities have in recent years developed codes of practice on conservation, in consultation with the Nature Conservancy Council, the Countryside Commission and other conservation bodies. Privatisation provides an opportunity to consolidate and extend progress in this area. The Government proposes to invite the water authorities, the NCC and the Countryside Commission to review these codes and so to develop a model which could be imposed on all WSPLCs. This might be done on a statutory basis or through the operating licence. The code will have to follow the best of current practice and to focus (without unnecessary detail) on matters important to environmental protection in general and to special flora, fauna and natural habitats in particular. It should provide for consultation with a broad range of conservation interests on matters of general concern and with the NCC and other relevant bodies on detailed matters affecting particular species or habitats.

7.15 The Government recognises the important and positive role played by the various conservation bodies, both nationally

and local, in helping to safeguard the environment, and recognises that this has in many cases already involved working closely with the Water Authorities. The proposals above should enable this partnership to continue and develop. The views of conservation bodies will be of particular interest both on developing the code of practice mentioned above, and also more generally on the matters canvassed in this consultation document.

7.16 While the Government will stand ready to take such further measures as may prove necessary, action in the four areas described above should provide a firm basis for ensuring that recent progress in conservation of the aquatic environment is maintained.

2812/27

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CCBG

FINANCIAL SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Kenneth Baker Esq MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

17 March 1986

Prime Minister!
Agree that the Chief Secretary's suggestion look well worth considering? DRS 18/3

Dear Kenneth,

WATER METERING

I have read your minute of 11 March to the Prime Minister and agree that the course you outline is the most sensible way forward. It would be a great pity if metering were discredited through precipitate action. As you say, the privatised industry will have every incentive to introduce metering where it is cost effective and I think it would have an adverse impact both on our privatisation proposals and upon the introduction of metering if it were to be seen as a centrally imposed burden.

There are, however, two important areas where progress can be made before the legislation required for compulsory metering trials reaches the statute book. First, we should develop our thinking about the suitable tariff structures and with this in mind I agree that the metering of distribution networks should proceed as quickly as possible. Secondly, bylaws are required to ensure that building regulations require new houses to be constructed so as to facilitate meter installation. If, as I expect, the results of the trials are positive, the introduction of more wide spread metering can then be implemented as quickly and cheaply as possible. I think that your Department should therefore regard the establishment of the necessary bylaws as a priority.

I am copying this letter to other members of E(A) and to Sir Robert Armstrong.

Yours ever

John

JOHN MOORE

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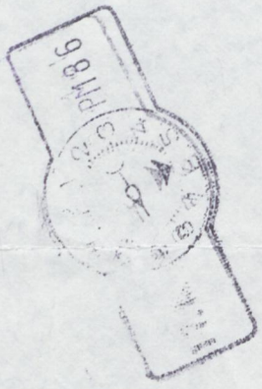
Local Govt: Water Industry Pt 3



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Ree JA

cc Prof Griffiths

10 DOWNING STREET

From the Private Secretary

17 March 1986

WATER METERING

The Prime Minister was grateful for your Secretary of State's minute of 11 March about plans for taking forward the development of domestic water metering following the Watts Report.

The Prime Minister agrees - albeit reluctantly - that the proposals set out in the minute represent an acceptable way forward.

I am copying this letter to Private Secretaries to members of E(A) and to Michael Stark (Cabinet Office).

(David Norgrove)

Robin Young, Esq.,
Department of the Environment.

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BG

Prime Minister

Agree that these proposals represent an acceptable way forward?

DHW
14/3

PRIME MINISTER

WATER METERING

My minute of 3 December set out my plans for taking forward the development of domestic water metering following the Watts Report. You suggested firmer proposals, such as a power for the Government to require the phased introduction of compulsory water metering.

It is obviously right in principle that people should pay for what they take and be made fully aware of the value of the service they are getting.

Roy Watts' report represents a major advance, in that it has established for the first time that in some circumstances domestic metering of whole areas could be cost-effective. That is so in particular where peak demand is currently at levels which would require major investment before long to increase supply capacity.

Of course, in much of England and Wales, water is abundant and the marginal cost of changes in demand is low. The study which Coopers and Lybrand carried out for Watts suggested that installation of meters for every household would cost over £1 billion. This compares with total annual income of water companies and water authorities (net of income already based on measured volumes) which is running at less than £1.9 billion a year. We need to be very confident that such an investment would give value for money before imposing it on the industry.

Told spark on cigarettes? Alcohol?

The Coopers study concludes that, on present information, 'metering the average consumer would lie on the borderline of economic viability'. Coopers' estimates are, inevitably, tentative and they, and Watts, recommend that they are tested. But they do make allowance, drawing in particular on extensive foreign experience, both for likely economies of scale in meter production and installation and for likely reductions in consumption.

That is why John Patten and I agree with Watts that the next step must be a series of controlled large-scale experiments to establish where and how we can get good value out of metering. We simply do not know enough yet, for example, about how consumers would respond to consumption-based charging and about the pros and cons of simple meters operating with simple tariff structures and more sophisticated ones which would permit high charges at times of peak demand.

We need new powers to allow for compulsory metering of houses in the trial areas. The installation programme, and our testing of costs, cannot therefore begin until the privatisation Bill receives Royal Assent next year. But we can press ahead in the meantime with putting meters at key points in the distribution network. That will give us essential information about present patterns of consumption. It will then take a year or two for customers to adjust to the new regime before we can assess the impact of metered charges on their consumption.

You suggested that we should require meters to be installed in all new dwellings, rather than provide for them to be constructed so as to facilitate meter installation. I fear however that that would set back rather than advance the cause of consumption-based charging. Metering scattered over new properties would be conspicuously costly and would thus tend to discredit the policy. The major prospect of economies of scale lies in metering all properties within compact areas. Only in that way will we bring the unit costs of installing the meters and reading and billing right down; the scope for savings is much greater here than it is in the production of the meters themselves, particularly if we can apply successfully the emerging technology of customer telemetry.

Our privatisation proposals also have a bearing on the issue. In future, with their prices and standards under firm regulation, the water undertakers will be looking to greater efficiency as the

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main source of profit for their shareholders. More cost-effective charging arrangements could have an important part to play in this, and there will therefore be every incentive on the WSPLCs and water companies to introduce metering wherever it makes good commercial sense. With that motivation in the industry and until we have the results of the experiments, I do not consider that we should take powers to compel them to introduce one method of charging rather than another.

I hope that you agree that my proposals represent an acceptable way forward. I shall be working up the details in consultation with the industry and consumer interests in the coming months.

I am copying this letter to the other members of E(A) and to Sir Robert Armstrong.

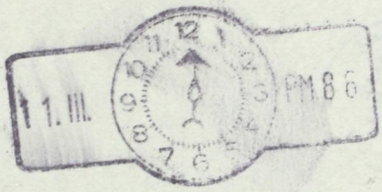
Personally — but it's not worth fighting about considered against other matters.

K.B.

K B

11 March 1986

Local Govt; Water Ind. Pt 3



CCBC

MM

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SECRETARY OF STATE FOR THE ENVIRONMENT

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434
My ref: B/PSO/11843/86

Your ref:

28 February 1986

NBPM

THAMES WATER AUTHORITY AUDIT: ARTHUR ANDERSEN & CO

Thank you for your letter of 18 February attached. I agree that the Treasury Solicitor should be consulted about how the reappointment exercise is carried out, and my officials will make the necessary arrangements.

Copies of this letter go to recipients of yours.

KENNETH BAKER

The Rt Hon Sir Michael Havers QC MP

LOCAL GOVT

Water PTS

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ROYAL COURTS OF JUSTICE
LONDON, WC2A 2LL

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01-936-6020

18 February 1986

The Rt Hon Kenneth Baker QC MP
Secretary of State for the Environment
2 Marsham Street
LONDON S W 1

Dear Kenneth,

THAMES WATER AUTHORITY AUDIT : ARTHUR ANDERSEN & CO

Thank you for your letter of ~~11~~ attached February 1986 indicating your intention to reappoint Arthur Andersen as auditors for the Thames Water Authority.

I accept that there are policy reasons that justify your desire to reappoint Arthur Andersens as auditors and I note your intention to impose the condition that no member of the firm who was engaged upon the audit of De Lorean should have any contact with this audit.

However, as the litigation with Arthur Andersens is still in progress and the Treasury Solicitor has the conduct of this, I think it would be desirable to ensure that he is consulted about how the reappointment exercise is carried out. As I indicated in my letter of 30 April 1985 to Norman Tebbit, particular care has to be exercised in such situations.

Copies of this letter go to Tom King, Paul Channon, on colleagues on E(NI), Sir Robert Armstrong, the Head of the Government Accountancy Service and to the Treasury Solicitor.

Yours ever, Michael.

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LOCAL GOVT

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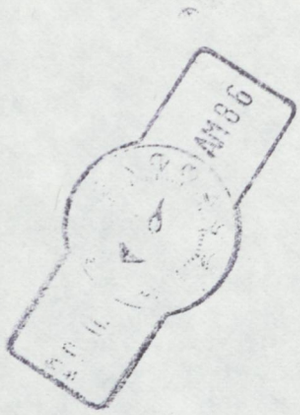

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CONFIDENTIAL

SECRETARY OF STATE FOR THE ENVIRONMENT

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref:

Your ref:

11 February 1986

Dear Michael.

THAMES WATER AUTHORITY AUDIT: ARTHUR ANDERSEN & CO

I feel that I should let you know that, because of special circumstances, I am intending to reappoint Arthur Andersen as auditors for the Thames Water Authority.

In the context of forthcoming privatisation it will be necessary to obtain an accountant's report of the financial position and results of the Water Authority over the last five years. It would be highly awkward to have to appoint new auditors, who would have to do that within their first year of appointment. The advice of the Head of the Government Accountancy Service is that, in these circumstances, it would not be in the public interest to involve another firm at this stage, given that Arthur Andersen have performed well on this particular audit. I shall, of course, impose the condition that no member of the firm who was engaged upon the audit of De Lorean should have any contact with the audit of Thames Water.

I am copying this letter to Tom King, Paul Channon, other colleagues on E(NI), Sir Robert Armstrong and the Head of the Government Accountancy Service.

Yours ever

Kenneth

KENNETH BAKER

The Rt Hon Sir Michael Havers QC MP

cc Questions
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STATEMENT BY THE SECRETARY OF STATE FOR THE ENVIRONMENT

PRIVATISATION OF WATER AUTHORITIES

With permission, Mr Speaker, I will make a statement about the future of the water authorities in England and Wales.

On 7 February 1985, the then Minister for Housing and Construction my hon. Friend the Member for Eastbourne, announced that the Government would examine the prospects for privatisation in the water industry. A discussion paper followed in April. In the light of the responses, and of professional advice on the financial issues, the Government has now decided to transfer the ten water authorities in England and Wales to private ownership; already, 25% of water is supplied by private sector water companies.

With my rt.hon. Friends, the Secretary of State for Wales and the Minister for Agriculture, Fisheries and Food, I have today presented to Parliament a White Paper setting out our proposals. Legislation will be necessary, and we shall put the water authorities on the market as soon as possible thereafter.

Our privatisation programme already covers a wide range of businesses. But transferring water to the private sector will offer unique opportunities and challenges. The water authorities are not merely suppliers of goods and services. They are managers of natural resources. They safeguard the quality of our rivers. They control water pollution. They have important responsibilities for fisheries, conservation, recreation and navigation. These functions are inter-dependent and inseparable.

We will maintain the principle of integrated river basin management and we will maintain existing boundaries. The water authorities will be privatised with all their existing responsibilities but for the one exception of land drainage and flood protection. Financing and co-ordination of that function will remain a public sector responsibility.

The authorities are largely natural monopolies. The public will, rightly, expect us to set up a firm regulatory framework. We will

appoint a Director General for Water Services. He will control the authorities through an operating licence. This will lay down strict conditions on pricing and on service standards. The system of promoting the interests of consumers will take into account a report which I am publishing today from Professor Littlechild of Birmingham University. Under the Director General there will also be strong machinery for representing consumer interests and investigating complaints.

Water authorities are responsible in England and Wales for the implementation of national policy for the water environment. Necessary existing safeguards - including appeals against water authority decisions on discharges and Government controls on the authorities' own discharges - will continue. And we shall strengthen the system of pollution control in two main ways; first, we shall legislate to make their river quality objectives subject to Ministerial approval; second, we shall provide for any new requirements to be laid down through a Parliamentary procedure. In this way we will use the opportunity of privatisation to improve environmental standards on a continuing basis.

Mr Speaker, over the last seven years considerable progress has been made in improving the management efficiency of water authorities. Their operating costs have been reduced in real terms, even while the demand for their services has been growing. Manpower has been reduced by 20%. The number of Board appointments has been reduced even more dramatically - from 313 to 123. In 1979 their investment was falling; in real terms it is now above its 1979 level and it is rising. In the last six years we have made the water authorities fit and ready to join the private sector. And, as reported to the Public Accounts Committee, the quality of water services has been improving in almost all regions.

Privatisation is the next logical step. It will bring benefits to customers, to the industry itself and to the nation as a whole in improved quality, more efficient service, greater commitment of the staff to the work they are doing, and greater awareness of customer preference.

With the disciplines and freedoms of the private sector I expect the industry to move from strength to strength. I know these proposals will be welcomed.

With permission, Mr Speaker, I wish to make a statement about the privatisation of the Welsh Water Authority.

As my Rt Hon Friend, the Secretary of State for the Environment, has told the House, the Government have decided to transfer the water authorities in England and Wales to private ownership and a White Paper setting out our proposals has been presented to Parliament.

The House will be aware that the Water Authorities in England and Wales were established so that a single body controls water and sewerage in river catchment areas; and that the Welsh Water Authority excludes that part of mid Wales which drains into the Severn but does cover those parts of England that drain into the Wye and Dee.

During the consultation that followed the publication of our discussion paper last April the Welsh Water Authority urged that the present integrated river basin management should continue if the industry was

privatised. We agree with that recommendation and the Authority will therefore be privatised with its existing boundaries and functions intact, with the exception of the co-ordination and financing of flood defence and land drainage.

The privatised Welsh Water company will operate under a licence from the new Director General of Water Services who will lay down strict conditions on pricing and service standards. The Director General will appoint a Regional Consumer Committee representing all consumer interests and in Wales this Committee will be assisted by divisional committees.

The privatisation of the WWA will for the first time enable employees and customers in Wales to have a direct stake in the industry.

The regulatory regime will provide general powers with regard to the supply of water in bulk between undertakings. The right of appeal will remain when water 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 as apply

to other aspects of charging policy in that charges should be cost related and should not be discriminatory.

Considerable progress has been made since the Authority was reorganised in 1982. Services and efficiency have been greatly improved and a large investment programme undertaken. I pay tribute to the Chairman, Board and employees for these achievements. I believe that privatisation will enable them to get on with their job with greater freedom and without the constraints on financing which public ownership imposes. Customers will benefit from the improving service that will result.

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NBPM.

FINANCIAL SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

Miss Sue Vandervord
Private Secretary to the
Secretary of State for the Environment
Department of Environment
2 Marsham Street
LONDON
SW1P 3EB

5 February 1986

Dear Sue

PRIVATISATION OF WATER AUTHORITIES: STATEMENT / With PM

Your letter to David Norgrove dated 31 January enclosed the draft statement on water authority privatisation that your Secretary of State intends to make this Wednesday.

As I told you on the telephone, the Financial Secretary has the following comments:

(i) the draft says that land drainage and flood protection will remain in the public sector. It is not however intended that operational activities related to these responsibilities will remain and the statement should refer to "decisions on the financing of land drainage and flood protection" remaining.

(ii) The statement emphasises that water authorities are natural monopolies. This is of course true for most of their activities in most places but the possibility of competition should not be ruled out. The statement should say "largely natural monopolies".

(iii) The draft says that the regulatory system for promoting the interests of consumers will be based on Professor Littlechild's report. This goes too far given that Ministers have not yet considered the detail of the report and the statement should say no more than "the system of promoting the interests of consumers will take into account advice contained in a report ...."

CONFIDENTIAL

(iv) In talking about strengthening the system of pollution control, the statement says that "We shall provide for new requirements to be laid down through a Parliamentary procedure". This could be taken as meaning that all sorts of new requirements are waiting in the wings and it would be better to say "We shall provide that any new requirements will be laid down through a Parliamentary procedure".

(v) The statement says nothing about the Government's intentions towards water companies. There will be quite a lot of interest in this, not least in the market, and they deserve an explicit mention.

I am sending a copy of this letter to David Norgrove at No 10, to the Private Secretaries to members of E(A), to the Private Secretaries of the Lord President and of the Chief Whips of both Houses and to Michael Stark in Sir Robert Armstrong's office.

Yours

Vivien

VIVIEN LIFE
Private Secretary

FILE

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10 DOWNING STREET

From the Private Secretary

3 February 1986

Dear Sue,

PRIVATISATION OF WATER AUTHORITIES: STATEMENT

The Prime Minister has seen the draft statement attached to your letter to me of 31 January, and is content, subject to the views of colleagues. The Prime Minister found it admirably clear.

I am sending copies of this letter to the Private Secretaries to members of E(A), Joan MacNaughton (Lord President's Office), Murdo Maclean (Chief Whip's Office), David Beamish (Government Whips' Office, Lords) and Michael Stark (Cabinet Office).

Yours ever

David.

(David Norgrove)

Miss Sue Vandervord,
Department of the Environment.

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cc CWO WSO CST
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LPO DTI CO
HMT CSL PGO
NIO DTM
DTN MAFF
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SECRETARY OF STATE FOR THE ENVIRONMENT

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref:

Your ref:

31 January 1986

Prime Minister

Another good draft statement. Content?

DLV
3/2

Excellent MF

Dear David

PRIVATISATION OF WATER AUTHORITIES: STATEMENT

I attach the draft of a statement which my Secretary of State is to make on Wednesday about the privatisation of water authorities.

The Secretary of State will be working on it over the weekend but, as time is pressing, I thought it might help if I circulated this text now to see if there are any points which you or copy recipients wish to have taken on board. I should be grateful for comments on Monday 3 February if at all possible.

I understand that the Secretary of State for Wales is also to make a statement. The draft as written covers both England and Wales. We will need to consider this aspect of handling next week, and perhaps Colin Williams could contact me on Monday about that.

I am sending a copy of this to the Private Secretaries to members of E(A), to the Private Secretaries of the Lord President and of the Chief Whips of both Houses and to Michael Stark in Sir Robert Armstrong's office.

Yours sincerely

Sue Vandervord

MISS SUE VANDERVORD
Private Secretary

David Norgrove Esq

DRAFT STATEMENT BY THE SECRETARY OF STATE

PRIVATISATION OF WATER AUTHORITIES

With permission, Mr Speaker, I will make a statement about the future of the Water authorities in England /~~and~~ Wales_/.

On 7 February 1985, the then Minister for Housing and Construction, my hon. Friend the Member for Eastbourne, announced that the Government would examine the prospects for privatisation in the water industry. A discussion paper followed in April. In the light of the responses, and of professional advice on the financial issues, the Government has now decided to transfer the ten water authorities in England and Wales to private ownership.

With my rt hon. Friends, the Secretary of State for Wales and the Minister for Agriculture, Fisheries and Food, I have today presented to Parliament a White Paper setting out our proposals. Legislation will be necessary, and we shall put the water authorities on the market as soon as possible thereafter.

Our privatisation programme already covers a wide range of businesses, from motor manufacturing to telecommunications. But transferring water to the private sector will offer unique opportunities and challenges. For water authorities are not merely suppliers of goods and services. They are managers of natural resources. They safeguard the quality of our rivers. They control water pollution. They have important responsibilities for fisheries, conservation, recreation and navigation. These functions are inter-dependent and inseparable.

With one exception - land drainage and flood protection, which will remain in the public sector - we will privatise the authorities with all their existing responsibilities and on their existing boundaries.

The authorities are, of course, natural monopolies. The public will, rightly, expect us to set up a firm regulatory framework.

We will appoint a Director General for Water Services. He will control the authorities through an operating licence. This will lay down strict conditions on pricing and on service standards. The system of promoting the interests of consumers will be based on a report which I am publishing today from Professor Littlechild of Birmingham University. Under the Director General there will also be strong machinery for representing consumer interests and investigating complaints.

Water authorities are responsible in England and Wales for the implementation of national policy for the water environment. Necessary present safeguards - including appeals against water authority decisions on discharges and Government controls on the authorities' own discharges - will continue. And we shall strengthen the system of pollution control in two main ways; first, we shall legislate to make their river quality objectives subject to Ministerial approval; second, we shall provide for new requirements to be laid down through a Parliamentary procedure. In these ways water environment policy will be both more effective and more explicit than before.

Mr Speaker, when we came to power in 1979 the water authorities showed signs of public-sector-itis. Since then their operating costs have been reduced in real terms, even while the demand for their services has been growing. Manpower has been reduced by 20 per cent. The number of board appointments has been reduced even more dramatically - from 313 to 123. When we came in, investment was falling; it is now above its 1979/80 level and rising. In 1979/80 (half) their investment was financed by borrowing; next year they will be 90 per cent self-financing. In the last six years we have made the water authorities fit and ready to join the private sector. And, as reported to the Public Accounts Committee, the quality of water services has been improving in almost all respects in almost all regions.

Privatisation is the next logical step. It will bring benefits to customers, to the industry itself and to the nation as a whole.

With the disciplines and freedoms of the private sector I expect the industry to move from strength to strength. I know these proposals will be welcomed.

31. I.
PM 5 6

FILE DA

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10 DOWNING STREET

From the Private Secretary 29 January 1986

Dear Robin,

WATER PRIVATISATION - WHITE PAPER

The Prime Minister has seen the revised version of the White Paper on Water Privatisation attached to your Secretary of State's minute of 22 January, and has noted that the aim is to publish it on Wednesday 5 February.

I am copying this letter to the Private Secretaries to members of the Cabinet, Murdo Maclean (Chief Whip's Office), David Beamish (Government Whips' Office, Lords) and Michael Stark (Cabinet Office).

Yours ever

David.

(David Norgrove)

Robin Young, Esq.,
Department of the Environment.

2155/34

CONFIDENTIAL

NBPN.

Treasury Chambers, Parliament Street, SW1P 3AG

John Patten Esq
Minister for Housing, Urban affairs
and Construction
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

24 January 1986

Dear John

WATER PRIVATISATION: DRAFT WHITE PAPER

FILE WITHDRAWN

Thank you for your letter of 21 January. I have now seen the revised draft covered by Kenneth Baker's letter to the Prime Minister of 22 January and am very content with the way in which the points I raised earlier have been handled.

Kenneth drew attention to a change in the reference in paragraph 3.9 to the public bodies which would assume responsibility for flood defence after privatisation. On the understanding that this leaves quite open our eventual decision on the precise type of body to be set up, I can support, and indeed would prefer, the new formulation.

I understand that our officials have agreed a number of small drafting points on this draft. Only one difficulty now remains to be resolved. In paragraph 4.17, "threat of takeover" is described as a spur to efficiency. Until our thinking is clearer on the circumstances in which we would regard takeovers as acceptable and those in which we would regard them as objectionable, I think that it would be wiser to drop this reference. It will, I feel, simply, raise te spectre of foreign takeovers and of diminished competition between authorities as a result of amalgamation which I do not think would be helpful until we are clearer about the appropriate riposte if indeed we decide in due course that takeover is desirable. It may also cause problems in relation to wider share ownership and employee involvement.

I am copying this letter to the recipients of Kenneth Baker's.

Yours ever

JOHN MOORE

CONFIDENTIAL

LOCAL GOUT

WATER

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CCBG

Prime Minister 4

To note the two points marked below.

DRS

24/1

PRIME MINISTER

WATER PRIVATISATION - WHITE PAPER

With my minute of 23 December I enclosed a copy of the draft of the White Paper on Water Privatisation. Your Private Secretary wrote in response on 13 January, and I have also had helpful comments from a number of colleagues.

Generally, we have been able to accept colleagues' points and I am writing to them individually to explain how we have handled the issues of substance which they have raised. We have also made our own revisions, to tighten the drafting and in particular to spell out more clearly the benefits which will arise from privatisation. The text is much improved.

I should draw attention to one point where I am now proposing to draw back from what we agreed in E(A), namely on the future arrangements for a public body to finance land drainage and flood protection. I believe we should keep our options open on this pending advice from officials in the Interdepartmental group on the Financing and Administration of Flood Defence, and have written to Michael Jopling accordingly.

We aim to publish the White Paper on Wednesday 5 February and delay must be avoided if we are to meet our timetable for legislating in the next session. I am circulating this revised text in the expectation that colleagues will not be seeking further changes. If they do, however, I must have them please by midday on Friday 24 January. If we do not hear by then, we will assume colleagues are content.

I am sending a copy of this to members of the Cabinet, John Wakeham, Bertie Denham, Sir Robert Armstrong and Brian Griffiths.

K.B.

K B

22 January 1986

DRAFT WHITE PAPER

PRIVATISATION OF THE WATER AUTHORITIES IN ENGLAND AND WALES

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1: INTRODUCTION

1.1 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 published a discussion paper, to which responses have been received from the water industry and others. After studying the reponses and examining the issues, the Government has now decided to transfer the ten water authorities in England and Wales to private ownership.

1.2 This White Paper sets out the reasons for the decision and the basis for the legislative proposals which the Government intends to put to Parliament as soon as possible.

Why private ownership?

1.3 The Government believes that the privatisation of the water authorities will benefit their customers and employees, and indeed the nation as a whole, in the following ways:

* the authorities will be free of Government intervention in day to day management and protected from fluctuating political pressures;

* the authorities will be released from the constraints on financing which public ownership imposes;

* access to private capital markets will enable more cost-saving investment and higher standards of service to be achieved than would otherwise have been possible;

* the financial markets will be able to compare the performance of individual water authorities against each other and against other sectors of the economy. This will provide the financial spur to improved performance;

* a system of economic regulation can be designed to ensure that the benefits of greater efficiency are systematically passed on to customers in

the form of lower prices and better service than would otherwise have occurred;

* measures will be introduced to provide a clearer strategic framework for the protection of the water environment;

* private water authorities will have greater incentive to ascertain the needs and preferences of customers, and to tailor their services and tariffs accordingly;

* private authorities will be better able to compete in the provision of various commercial services, notably in consultancy abroad;

* privatised authorities will be better able to attract high quality managers from other parts of the private sector;

* there will be the opportunity for wide ownership of shares both among employees and among local customers;

* most employees will be more closely involved with their business through their ownership of shares, and motivated to ensure its success.

1.4 The Government has therefore decided to seek from Parliament 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 the 400,000 that have already been transferred to the private sector.

Who will benefit from private ownership?

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

1.6 Customers in particular will benefit from the prospect of higher standards, greater efficiency in the provision of services, a charging policy designed 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 over charges, and levels of service will be defined. Drinking water quality standards are already laid down.

1.7 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 for other industries that have been privatised. Water authority pensions form part of the Local Government Superannuation Scheme, and the Government will consult the industry about future arrangements. Employees will be entitled to preserve pension rights already accrued in the Local Government Scheme.

1.8 The environment will benefit from a new system of Government approval for the objectives set for each river and estuary, defining the standards to which each is to be maintained or improved.

1.9 By setting explicit objectives for drinking water quality for river quality, and for other key service standards before the authorities are sold into private ownership, the Government will protect the consumer and the public. Prospective shareholders will also be able to take stock of obligations inherent in explicit objectives, when assessing the businesses in terms of assets, worth, and profitability.

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

The new shape of the water industry

1.11 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. The water

authorities will be privatised on the basis of their existing boundaries. The Government intends that the water authorities should continue to carry out their responsibilities for the management of rivers, control of pollution, fisheries, environmental conservation, recreation and navigation. Special arrangements will be made for land drainage and flood protection, and these are discussed in paragraph 3.8-3.10. An overall aim will be to keep the structure of the industry as simple as possible.

1.12 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 WSPLCs act even-handedly.

1.13 To protect the interests of the customer, the Government will appoint a regulator to prevent the abuse of monopoly power through charges, to see that standards are observed and to be responsible for consumer consultation.

1.14 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.

1.15 The proposals in this White Paper represent a significant extension of the Government's successful programme of privatisation, and will 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.

SECTION 2: THE WATER AUTHORITIES NOW

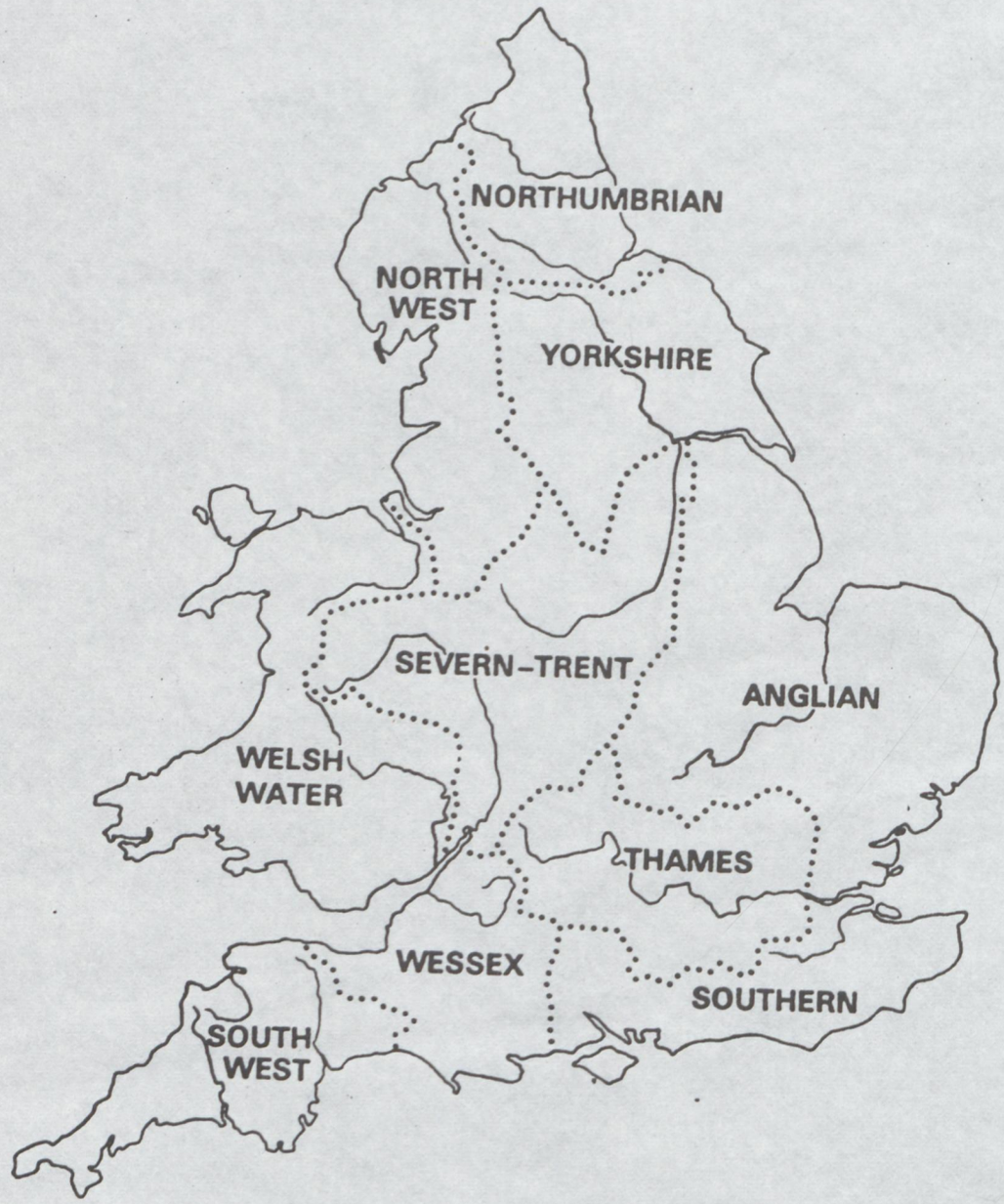
Integrated River-Basin Management

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 undertakings had been responsible for water services. There were inevitable working difficulties and conflicts of interest, which the water authorities were created to overcome. The authorities assumed responsibility for water supply, sewerage and sewage disposal, as well as for water-resource planning, pollution control, fisheries, flood protection, navigation, water recreation and environmental conservation. The area of each authority comprises one or more river basins; boundaries are shown on the map opposite.

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 6,500 discharges from industry and 450 discharges from the Authority's own 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 regulated and managed to ensure that discharges do not pollute water supplies and abstractions do not lower the level of the river and put at risk natural life or the enjoyment of those who use the river for recreation.

2.3 As the water authorities control and regulate all the uses to which their rivers are put, they have generally been able to meet 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. During the drought of 1984, when rainfall in its region was less than half the average for 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

WATER AUTHORITIES IN ENGLAND AND WALES



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REGISTER MARKS ARE TO SHOW 'SQUARENESS'. NOT FOR ANY OTHER PURPOSE

prohibited the Authority was able to maintain supplies without resort to water rationing, and without detriment to the rivers themselves and the natural life they support. Water shortage of a different kind will be overcome by the Southern Water Authority by another application of the principle of integrated river basin management. 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, so 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. It has been recognised 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 retain the structure of the water authorities essentially as they stand in the transfer to private ownership.

Constitution and Functions

2.5 The water authorities are large undertakings. They employ some 51,000 people; their annual turnover is about £2,600m; and their capital investment for 1986/7 will exceed £900m. Their assets include 137,000 miles of water mains, 141,000 miles of sewers, 6,500 sewage treatment works and 1000 water treatment works. An analysis of the authorities' capital and operating expenditure is shown in Figures 1 and 2.

2.6 Until 1983, the authorities were run by large boards with a majority of local authority representatives. The Water Act of 1983 set up the present boards, which are smaller and more business-like. All members are appointed by Ministers.

2.7 Over 99% of the population of England and Wales is connected to a public water supply. The water authorities supply about 75% themselves; the privately owned statutory water companies supply the remainder. About 96% of the population is connected to a public sewer. The water authorities own and are responsible for the sewers, and undertake all sewage treatment and disposal. Before the 1973 Water Act, local authorities built and maintained the sewers, and in most areas district councils continue to do so on an agency basis.

OPERATING EXPENDITURE: WATER AUTHORITIES
England & Wales Inc. Land Drainage 1984/85

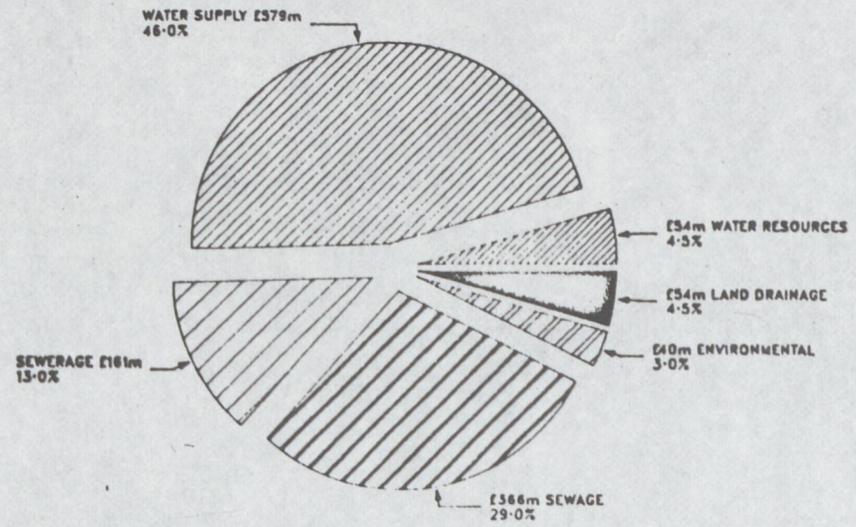

Figure 1

CAPITAL EXPENDITURE: WATER AUTHORITIES
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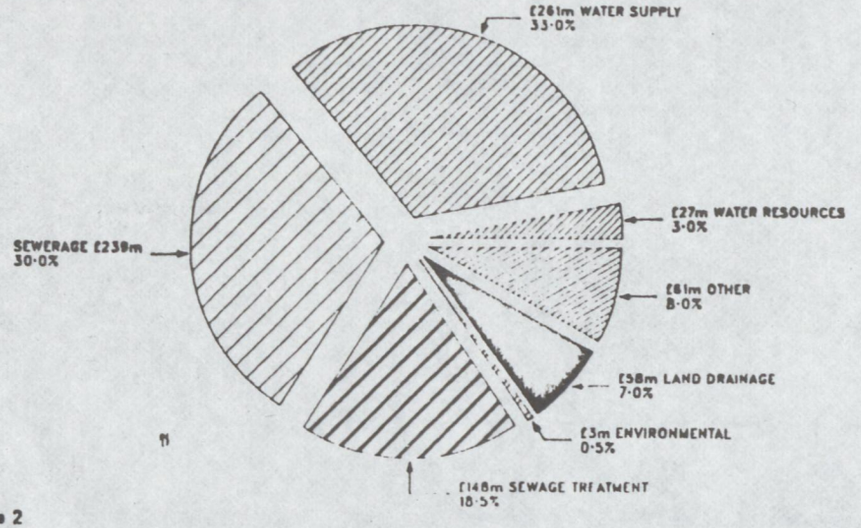

Figure 2

2.8 In addition to providing these main services, water authorities also regulate other users of water. They control through a licensing system the abstraction of water from rivers and other sources. Their consent is needed for the discharge of effluent into lakes, rivers and other places where water might be contaminated by the discharges. They grant licences and consents in the light of the standards of quality for each stretch of river and coast. 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.

2.9 Water authorities are also responsible for environmental conservation, fisheries, navigation, flood defence and land drainage. These account for less than 10% of the authorities' operating expenditure but are important areas of activity.

Present State and Progress of the Industry

2.10 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

2.11 Between 1961 and 1971, domestic water supply rose from 2,400 million gallons a day to 3,100 million gallons a day. By 1984, it had increased to 3,600 million gallons a day. In addition, about 6,600 million gallons 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.

2.12 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 was 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 provided 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 it to transfer supplies to many areas of acute shortage. It has now extended the grid to serve fully the conurbations of West Yorkshire and South Yorkshire. All the authorities mobilised resources of finance, management and engineering to tackle shortages in ways which would have been impossible before the 1973 Water Act.

- **Water Quality**

2.13 The quality of water supplied has been maintained and in some cases improved. In the Summer of 1985, in accordance with the Drinking Water Directive of the European Community, the Government completed a review of the quality of all drinking water supplies and an assessment of the shortcomings. 90% of supply areas 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 nitrates, manganese, iron and other standards, where it is satisfied that there is no risk to health.

- **Sewerage**

2.14 In the last decade, the industry has developed sophisticated techniques of sewer survey and renewal by remote control. Although much has been said about the need for heavy investment in the renovation of Britain's sewers, about half the 140,000 miles of sewers in England and Wales have been built since the Second World War, and less than a quarter predate 1914. Properly laid and maintained, sewers last a very long time, and it is not generally realised that most failures are due to blockage rather than collapse. The Water Research Centre's Sewerage Rehabilitation Manual has codified the best available techniques for dealing with sewer dilapidations and the problem is now technically manageable. So substantial progress has been made, but much also remains to be done to establish the scale of the problem and to make good the dilapidations of the past.

- **Pollution Control**

2.15 River quality lies at the heart of the water authorities' performance of their functions. The benefits of clean rivers for the local environment and for making an area more attractive to potential investors are immense. The authorities have tackled pollution both by controlling their own discharges and those of others. The discharge of raw sewage into rivers such as the Tyne and Mersey has

been a major cause of pollution. In many areas, the sewage works inherited by water authorities were small, outdated and inefficient. Where possible, authorities have updated or replaced them in projects such as Severn-Trent Water Authority's Black Country strategic sewage treatment scheme, which will significantly improve the quality of the River Tame. The North West Water Authority has started 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.

2.16 The last national survey of river quality showed that grossly polluted rivers had been reduced in length from 792 miles in 1975 to 506 miles in 1980, while lengths of "grossly polluted" and "poor" tidal river were reduced by 21% and 47% respectively in the same period. The indications are that this improvement has not been sustained in the last two years. A comprehensive new survey will be carried out in 1986.

2.17 Many authorities are taking action to prevent the pollution of bathing waters by sewage, in accordance with standards laid down by the European Community 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 brought into service 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

2.18 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.

2.19 Consultants who reviewed the water authorities' budgets for 1981/2 and 1982/3 found scope for reducing costs without damaging standards of service. In addition, the Monopolies 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 contain 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. 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. Numbers rose between 1976 and 1979, but since 1979 there has been a saving of nearly one-fifth. At the same time, standards of service have been maintained and improved.

2.20 With improved financial performance, the water authorities have become more self-financing, and capable of standing independently as commercially viable entities. When the authorities were set up in 1974, internal finance contributed little to capital expenditure, but by 1980/81, when authorities' capital expenditure was £692 million, only 41% was financed from borrowing and by 1986/87, with planned capital expenditure having risen to £942 million, about 10% only is to be financed from borrowing.

Investment Needs and Plans

2.21 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.

2.22 The present position is as follows:

a. Water Resources

Water resources in most regions will meet demands (expected to grow by about 1% per annum 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.

TABLE 1

WATER AUTHORITY - MANPOWER (AT 31 MARCH EACH YEAR)

	1976	1979	1982	1985	30 September 1985
Anglian	6726	6978	6700	5549	5388
Northumbrian	2279	2448	2151	1759	1707
North West	9005	9379	8782	8166	8096
Severn-Trent	10464	11240	10502	9269	9080
Southern	4120	4207	3948	3336	3281
South West	2315	2551	2276	2023	1989
Thames	11810	12061	11753	9089	8981
Welsh	5330	5594	5677	4709	4799
Wessex	2260	2425	2291	2050	2029
Yorkshire	6340	6338	6506	5835	5680
TOTAL	60649	63221	60586	51785	51030

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: £ millon 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	278.0
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	867.0

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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CAPITAL EXPENDITURE BY PURPOSE (1984/85)

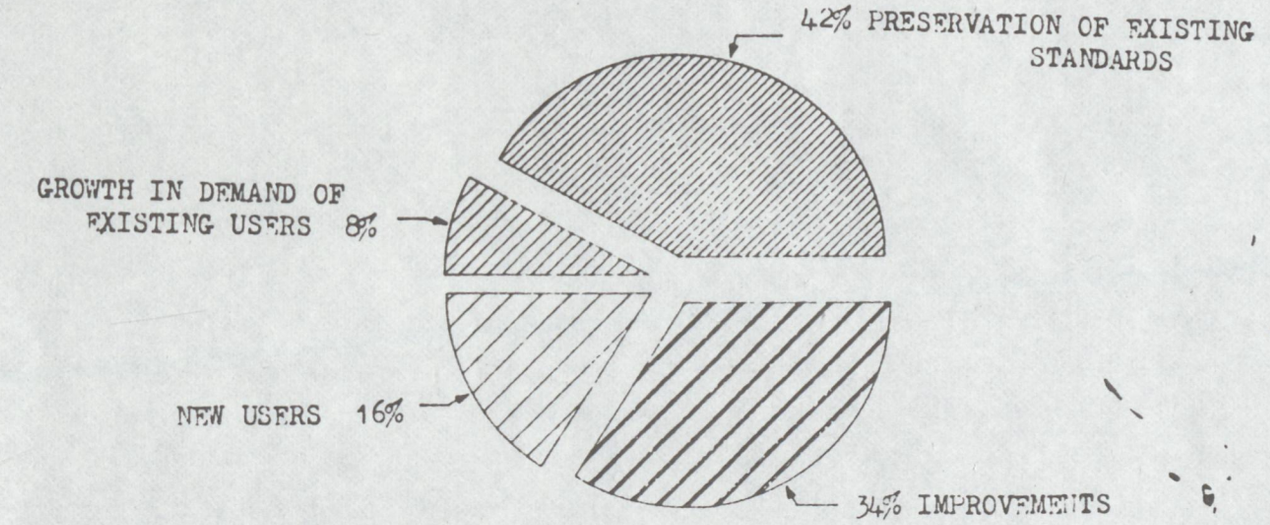


Figure 3

b. Water Supply

In a number of areas water mains need to be replaced and enlarged to accommodate increasing demand. The authorities will be spending about £345m on water supply investment in 1986/87, and good progress is being made in dealing with the problems that have been identified.

c. Sewerage and Sewage Treatment

Investment has increased from about £200m in 1980/81 to about £325m in 1986/87 and the Government expects expenditure at the present level or above to continue in the foreseeable future. The need for investment in treatment and disposal will be affected by future quality objectives for rivers and coastal waters.

d. Flood Protection and Land Drainage

Substantial expenditure is likely to be necessary on flood protection schemes over the next 4 years and there will be a continuing need for such work into the 1990s. The financing of flood protection will, however, remain in the public sector.

The Government considers that the present level of planned investment is adequate to maintain the delivery of services and to effect improvements where these are most needed. The water authorities' consider that a somewhat higher level would be justified, and they bid in their recent corporate plans for an investment level in 1988/89 no more than 13 per cent in real terms above the provision for 1986/87 (ie £910 million). In future, WSPLCs will be free from the constraints of public expenditure control. They will be free, therefore, to make their own plans for meeting the required levels of service, which they are expected to do more quickly that would otherwise have been the case, and to increase the rate at which cost-saving technology is introduced.

2.23 The nationalised water industry in England and Wales has been transformed into ten modern businesses. The finances of the industry have been considerably strengthened, a great deal of worthwhile investment has been carried

out, efficiency and performance have been substantially improved. The industry is now in a state where it can be privatised. This will enable it to achieve further improvements in service more easily than it could in the public sector. Private enterprise is both more flexible and readier to pursue energetic and innovative approaches than the public sector. The demands of the market will give management and staff the impetus they need to secure greater efficiency. Freeing the authorities from the constraints imposed by state ownership will help them to carry out their tasks with vigour and imagination.

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 while 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, so as 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 ten new water services public limited companies (WSPLCs) and to transfer them to the private sector with their present functions largely intact. This Section explains the reasons for the organisational and company structure chosen, the changes 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 does not believe 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.

Statutory Companies or PLCs

3.4 At present there are twenty-eight statutory water companies supplying water to about a quarter of the population of England and Wales. They provide a precedent for

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. PLC status under the Companies Act 1985 on the other hand would provide a framework within which enterprise can flourish. It would afford all the normal protection of company law, and would automatically be kept up to date as that law was revised. If necessary, additional safeguards can be made, as in previous privatisations, through Government ownership of a "special share" for purposes defined in the WSPLCs' articles of association.

Statutory Water Companies

3.5 Under the Water Act 1973, some water authorities discharge their water supply functions in parts of their areas through the statutory water companies. Financial controls are written into the companies' statutes, limiting the maximum rate of dividend, the size of reserves, and the amount of balances that can be carried forward from one year to another. The Government sees advantage in ending the constitutional 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 will apply to 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 that this would offer. The Government will be discussing these proposals further with the 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 interests of efficiency nor would it be consistent with the principle and practice of integrated water management. It would also 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 a year. 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 needs by new arrangements for the financing of flood defence activities through public bodies which will make the fullest possible use of WSPLC expertise. 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 (Cmnd 9449) issued in March 1985.

Franchising and Competition

3.11 The Government has considered, as an alternative to full-scale privatisation, the possibility of requiring the water authorities to franchise out the whole of their main operational functions, for which potential franchisees would bid. This system is widely practised in France, and has been advocated as a means of introducing competition into a monopoly situation. It is difficult, however, to see competition arising from this approach in an effective form. Competition on this model would only arise when the franchise came up for renewal, and because of the high cost of termination, such franchises would need to be granted for

substantial periods - say 25 years. In addition, there would be little incentive to invest in new equipment and infrastructure, particularly during the later part of the franchise period. Operating franchises, where the franchisee leases the assets could be renewed more frequently - at up to 10 year intervals - but the division of responsibility between owner and operator would be prejudicial to a properly planned programme of maintenance, renewal and replacement.

3.12 The Government does not rule out and indeed favours franchising or contracting out by the WSPLCs themselves. In some cases this may well produce significant operational and financial benefits. However, the Government does not propose to put WSPLCs under a duty to enter into such arrangements. The regulatory system described in Section 4 provides continuing incentives for the industry's managers to find the most efficient ways to achieve standards and make profits. They can be expected to franchise operations, where this is cheaper and more effective than doing the job themselves.

Regulatory Responsibilities

3.13 In safeguarding water resources, the authorities impose costs and constraints on other parties. At the same time, they are actual or potential dischargers and abstractors themselves. The statutory basis of regulatory control will ensure that WSPLCs deal with abstractions and discharges even-handedly and in the public interest, and the existing rights of appeal to the Secretary of State on individual cases will be reinforced.

Environmental Services

3.14 The water authorities' responsibilities for fisheries, pollution control and monitoring, navigation, recreation and amenity services cannot be discharged on a straightforward commercial basis. All these services receive some support from the present Environmental Services Charge. Expenditure amounts to no more than 2.5% of any authority's income. The future financing of these services is described in paragraph 4.22 below.

3.15 To summarise, the Government proposes to make only those minimum changes to the structure of the industry which are necessary to secure the privatisation of the water authorities as public limited companies, or to enable the present statutory water companies to come within a similar corporate and regulatory

framework. 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.

SECTION 4: REGULATION AND CUSTOMER PROTECTION

The Need for Regulation

4.1 The water authorities are for the most part natural monopolies. The work required to create their infrastructure makes it more efficicient for the services to be provided by one company than by several. The services they provide are essential to public health, as well as to the protection of the environment. Therefore, safeguards are obviously necessary to prevent the WSPLCs from overcharging or providing a low standard of service, while not inhibiting their enterprise.

4.2 Although similar in its local distribution networks, 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. This offers scope for competition, even though each authority is responsible for the provision of main services within its area. Authorities will be competing in the capital market for funds, and there are increasing opportunities for competition in services such as overseas consultancy and recreation. The Government would expect that WSPLCs would expand such entrepreneurial activities considerably. The regulatory system will enable comparison of performance to be made between WSPLCs, and this will both act as an impetus to improvement and - by providing a yardstick for investors to make judgements - facilitate competition between WSPLCs 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 will limit what customers can be charged and set requirements about standards of service. The Director General's principal duty will be to safeguard the interests of the customers and ensure at the same time that the companies have every incentive to

perform well in the interests of their shareholders. He will also be responsible for setting up and maintaining the consumer consultative arrangements described in paragraph 4.24. The costs of the Director General and his staff will be met by fees changed for the granting of licences. 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 separately.

4.5 The licence will formally designate the WSPLCs as bodies licensed to provide water supply and sewerage services, to conserve rivers and other water resources, to do so for profit, but with attendant obligations. The licences will not replace existing statutory duties, but they 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. 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 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). The price formula would, however, 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 the Director General to make interim changes under special circumstances with the agreement of the licensee. In the absence of agreement, proposals for change would be referred to the Monopolies and Mergers Commission. 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.

4.8 The terms of the licence would be enforceable in the courts. In extreme circumstances the licence could be revoked, and the company taken over - for example by another WSPLC. It will also be necessary to ensure that there are adequate contingency schemes for responding to emergencies and for civil defence provision. WSPLCs, like other private technology-based organisations, will need a sound research and development capability. The licence would require WSPLCs to carry out or obtain adequate research and development for their responsibilities.

Limiting of Charges to Customers

4.9 Charges to customers can be limited in two main ways. The method with which the water industry is most familiar is that applied to the statutory water companies, where the principal control is a limit to the rate of dividend that may be paid to their shareholders. However, profit controls of this kind provide no incentive to efficiency, since increases in expenditure are allowed to feed through directly into prices.

4.10 Price controls are more attractive. They provide an incentive to efficiency and are therefore to be preferred. A precedent has been established with the privatisation of British Telecom and the proposed privatisation of British Gas. It is for further consideration what formula should be applied to the water industry. Price controls would need to cover the main services of WSPLCs, in which they have a monopoly. It is for consideration whether a single price formula should be applied to these services (water supply, sewerage, and sewage disposal), or whether separate formulae should be applied to each. 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.

4.11 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. WSPLCs could also compete to provide other WSPLCs with services, such as laboratory analysis or sewage treatment, if these were franchised out. In some instances, WSPLCs might compete directly for customers situated on the borders of their areas.

4.12 It would not be right to allow competitive kinds of business to be sustained by hidden subsidy from the customers of the main services. So it will be necessary to ensure that such businesses are run at arm's length from the main services. The Director General, the competitors and the public will be better able to satisfy themselves that there is no unfair subsidisation, if unregulated, non-monopoly business is carried out by a subsidiary company.

Service Standards

4.13 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 will be allowed only in exceptional circumstances with specific Government authorisation.

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

4.15 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 connection, reliability of water supplies and the incidence of sewer failures. They provide a basis for setting targets for key aspects of service quality, and for monitoring progress. Progress has been made against almost every indicator in each area. It could be a requirement of the licences that WSPLCs should continue to publish their

performance against such indicators. For some indicators, specific targets could be set by the Director General on a common basis for all WSPLCs. In some instances, these targets would be the basis for the improvement of services over a period of years.

4.16 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

4.17 In applying price controls and target standards, there is a choice between:

i. tailoring standards and price controls individually to each WSPLC, taking account of its geography and investment needs; and

ii. setting uniform standards and price controls throughout the industry.

The first allows for greater flexibility, but would involve the Director General in complex and repeated 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 demonstrate even-handedness between the regulated companies. The second method has the advantage of simplicity once it is in operation. The variations in their situation would be reflected in their capital structures and the prices they command on the market. By encouraging direct comparisons between authorities by investors, it would also promote efficiency by means of competition. The threat of takeover would become a spur to poor performers as would sanctions available to the Director General himself. If the price formula were set to reflect changes in the average performance of the industry as a whole, it would provide two further advantages: it would pass on to the customer the benefit of the average cost reduction, and would give WSPLCs an incentive to be more effective than the average, and so to be more profitable.

Charges

4.18 While the rate of increase in the average level of water charges would be governed by price control, the general principle now expressed in Section 30 of the Water Act 1973 that charges for water services should be cost-related and non-discriminatory between classes of customers would still be applicable.

4.19 Most domestic customers still choose to be charged for water services on the basis of rateable value. In the Green Paper 'Paying for Local Government' the Government has proposed that the present system of domestic rates should be phased out within ten years, starting in 1990, in favour of a community charge levied as a flat rate on all resident adults. This suggests that it would in any case be necessary to discontinue the use of domestic rateable value as the basis for water charges, at least as regards new or substantially modified properties.

4.20 There are obvious attractions in principle in charging for water services on the basis of consumption, particularly where private-sector companies are selling to customers. At present, all industrial and many commercial customers are already metered for consumption, but few domestic consumers have so far seen sufficient advantage in this method of charging to be prepared to incur the cost of having a meter installed. The recently published report of the Watts Committee, however, suggests that in some circumstances compulsory domestic metering of whole areas, installation costs being met in the first instance by the WSPLC, could be worthwhile. This would secure economies of scale in the purchase, installation and administration of meters. By reducing demand, it would tend to reduce, or defer, the need for new investment in supply capacity. This Committee recommends legislation to make more extensive trials possible. The Government will make provision accordingly in its privatisation Bill. It would clearly be premature to require from the outset universal reliance on metering for domestic charges, but this is an option which could be considered by the Director General in due course if the results of the trials were to justify it.

4.21 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 as apply to other aspects of charging policy - that charges should be cost-related and should not be discriminatory.

4.22 As a general principle, WSPLCs should aim for the maximum possible cost recovery for those services which currently receive a contribution from the Environmental Services Charge (ie fisheries, pollution control and monitoring, navigation, recreation and amenity services. Some areas of enterprise could well be undertaken on a profit-making basis. However, some desirable activities may have to continue to be run at a loss. WSPLCs will be able to meet the net cost of these services from main service charges. The size of the contribution, which is at present no higher than 2.5% in any part of the country, would be determined by the Director General, after consultation with the appropriate advisory committees. There is no question of repealing duties, whether general or specific, currently placed upon water authorities in this area of activity. The duties and obligations of the WSPLCs will have to be taken into account by the Director General in assessing the reasonableness of the subsidy proposed.

Customers

4.23 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.

4.24 It believes, however, that they should be strengthened in various ways so that consumer bodies can assume an additional responsibility after privatisation. It therefore proposes that in future consumer consultation, which is organised divisionally at present, should be simplified and based on regional consultative committees. The regional committees will be independent of the water authority they monitor and will report to the Director General. They will be financed from the licence fee charged to WSPLCs. 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 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 Commission for Local

Administration (the local Ombudsman). The Directors General's office will, however, be subject to investigation by the Parliamentary Commissioner for Administration (the Parliamentary Ombudsman).

4.25 Privatisation itself will encourage the WSPLCs to compete effectively in fields where they can do so. 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 Director General will be able to ensure that services are not only maintained, but improved, and customers benefit. Customers will also benefit from the system of price-control, which keeps 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.

SECTION 5: SAFEGUARDING THE ENVIRONMENT

5.1 The Government has placed great emphasis on the conservation and improvement of the water environment, and on promotion of the recreational opportunities it provides. Last year, in particular, it implemented Part II of the Control of Pollution Act 1974. This section describes how the Government will ensure that sound environmental policies continue after privatisation and the part which WSPLCs will play in them.

Environmental Water Quality

5.2 Rivers provide both a source of water supply and a means of disposing of sewage and other liquid wastes. So the conservation of rivers lies at the heart of the water authorities' activities. As explained in Section 3, the Government has decided that the privatised water authorities should retain executive responsibility for the protection of rivers and other natural waters from pollution.

5.3 The responsibilities for water pollution control and monitoring are important, but they do not consume enormous resources. For instance, the Thames Water Authority, which has been notably successful in cleaning up the Thames, 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 some £500 million.

5.4 The steady improvement in water quality in recent decades has been 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 to show what discharges can be safely permitted. The authorities' inspectors monitor individual effluent discharges against the limits that have been set, and they also monitor the river water quality. The inspectors play a critical role in the prohibition of dumping and spillages of polluting matter.

5.5 The authorities' regulatory functions will be retained by WSPLCs. The recent implementation of Part II of the Control of Pollution Act 1974 has put the regulatory system on a firmer footing. The system will work as follows. Applications by third parties will normally be decided by WSPLCs. Their own applications for discharge consents will, as now, be decided by the Secretary of State. As now, there will be a system of appeal by third parties to the Secretary of State and, as now, applications may be called in by the Secretary of State, who may hold a public inquiry. The WSPLCs will inherit their predecessors' expertise in dealing with such matters, and their need to abstract water for their own supply will provide a continuing incentive to them to maintain the quality of rivers and groundwater.

5.6 Certain changes will be necessary to underpin the exercise of these functions by private bodies. A clearer strategic framework of national policy for the water environment will be needed (paragraphs 5.7-5.9), along with public involvement (paragraphs 5.16-5.18) and a satisfactory system of finance and management for environmental purposes (paragraphs 5.19-5.21).

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

i. 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. The Director General's licence will provide targets and performance measures for the achievement of quality objectives. The aim will be for the Secretary of State to approve these long-term river quality objectives before prospectuses are issued for the sale of of the WSPLCs. This will enable guidance to be given to investors about the cost implications of river improvements, 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. the Control of Pollution Act allows water authorities to require other parties to take precautions and to regulate their activities in order to avoid water pollution. These powers will provide a protective regime for the water resources on which WSPLCs will depend and for those areas of the water

environment of particular importance to nature conservation. These provisions will supersede authorities' present byelaw making powers and provide a more effective means of tackling sources of pollution not susceptible to regulation through discharge consents.

5.8 At present the Secretary of State has the duty under the Water Act 1973 to give effect to a national policy for the restoration and maintenance of wholesome of rivers and for related environmental purposes. 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 advice and guidance given less formally.

5.9 These public sector arrangements will need revision before 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. A wide power of general direction is clearly inappropriate. It will however be necessary for the Secretary of State to have a power, subject to Parliamentary procedure, to require WSPLCs, in their capacity as pollution control authorities, to give effect to European Community and national environmental policies. The legislation will be drafted accordingly, and will include the provisions described in paragraphs 5.20 and 5.21 below to enable WSPLCs to recover the costs arising from their environmental functions and responsibilities.

Environmental Services

5.10 These arrangements will enable the Government's long-standing commitment to maintain and improve water quality to be carried forward effectively after privatisation. They will also provide a sound basis for meeting objectives for the environmental services which are dependent upon it.

- Wildlife and Conservation

5.11 The Water Act 1973, the Control of Pollution Act 1974, and the Wildlife and Countryside Act 1981, require water authorities to have regard to the conservation of the natural environment and to exercise their other functions so as to further

conservation. 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.

5.12 The Government intends that the various activities undertaken by water authorities to support nature conservation and protect amenity should be continued. The privatisation of the water industry will provide an opportunity to consolidate their achievements and carry them forward within a new statutory and administrative framework. The measures described in paragraph 5.7(ii) will provide a basis, when necessary, for special protective regimes for particular areas.

- Fisheries

5.13 Water authorities have a statutory duty to maintain, develop and regulate fisheries for salmon, trout, eels and freshwater fish. They are required to consult affected interests through statutory fisheries advisory committees. These duties 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, since the health of fish provides a sensitive indicator. It is the Government's intention that the WSPLCs should retain the full range of fisheries responsibilities. The Minister of Agriculture, Fisheries and Food and the Secretary of State for Wales will continue to 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

5.14 In common with certain other private and public bodies, three water authorities at present exercise extensive navigation responsibilities set out in local acts in relation to a public right of navigation. The Government accept that these responsibilities can pass to their successor bodies either through

the amendment of existing statutes or by establishing 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

5.15 Water authorities already provide wide opportunities for enjoyment of the water environment. They have a statutory duty to make the waters they control, and any associated land, available for recreation, as far as reasonably practicable. As a result there has been a dramatic increase in recent years in opportunities for active water-based recreation. These opportunities must be preserved. Conditions within the operating licence will provide for the maintenance of the existing range and level of facilities, including those for private clubs. There will remain many opportunities to expand and develop the recreational potential of the water environment. The Government considers that WSPLCs 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 that they are free to do this.

Public Information and Consultation

5.16 The Government recently implemented the public register provisions of the Control of Pollution Act, which ensure public 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. In the light of the arrangements proposed for privatisation the Government will consider how to extend the provisions for registers to include information on the receiving waters, their quality objectives and incidents.

5.17 The Government proposes 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, which is undertaken every five years, this information will provide a full account of changes in environmental water quality and a basis for reviewing the effectiveness of environmental protection measures.

5.18 Arrangements for consultation on environmental matters will be maintained, and it will be the responsibility of the Director General to ensure that a reasonable balance is struck between the provision of recreation and conservation facilities and the costs to shareholders and customers.

Management and Finance

5.19 Government approval of local water quality objectives (paragraph 5.7(i)), provisions for the protection of water resources (paragraph 5.7(ii)), and the specific Ministerial power of direction in matters of pollution control (paragraph 5.9) will ensure a consistent framework for environmental policy. The development of public information (paragraphs 5.16-5.18) will provide a stimulus to action. WSPLCs themselves will have every reason on the grounds of efficiency to improve their expertise, and they will be free, as private companies, to use and sell their skills at home and overseas.

5.20 Investors in the new companies will be concerned about the financial implications of their environmental duties. The expenditure is 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 and other dischargers should be given a direct incentive to help maintain and improve water quality. The Government will therefore work out in consultation with the water industry and other interests how the costs of monitoring and controlling effluent discharges can be assigned to those who make them, and the costs of averting or remedying pollution incidents can be assigned to those whose actions make that necessary.

5.21 There must also be a sound general basis 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.

SECTION 6: NEXT STEPS

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 with an eye to the future as appointments expire. He will no longer consider himself committed to appoint members nominated by local authorities or who possess local government experience. He also intends that the legislation should provide for the possibility of other changes in membership and chairmanship 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.

6.5 Consultation papers will be issued shortly on the Government's proposals for modernising water and sewerage law, and on the arrangements for environmental protection.

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.

ANNEX

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 are 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: United Kingdom 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 Anne's Gate, London SW1H 9BT, £13.00).

7. Water Industry Review 1982 (National Water Council, £6.00.)

8. Sewerage Rehabilitation Manual 1983 (Water Research Centre, PO Box 85, Frankland Road, Blagrove, Swindon, Wilts, SN5 8YR).

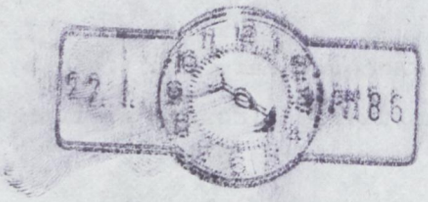
9. The principal Acts relating to water authority affairs are: the Public Health Act 1936, the Water Act 1945, the Water Resources Act 1963, the Water Act 1973, the Control of Pollution Act 1974, the Salmon and Freshwater Fisheries Act 1975, the Water Charges Act 1976, the Drought Act 1976, the Land Drainage Act 1976, the Water Act 1983.

10. Joint Study of Water Metering: Report of the Steering Group 1985 (HMSO £5.85).

11. Economic Regulations of Privatised Water Authorities, a report submitted to the Department of the Environment by Professor S C Littlechild.

LOCAL GOUT

WATER PIT



CONFIDENTIAL

cc BG

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister

NBPM.

The Rt Hon Kenneth Baker MP
Secretary of State for the Environment
2 Marsham Street
London SW1

January 1986

Dear Secretary of State

WHITE PAPER: PRIVATISATION OF THE WATER AUTHORITIES IN ENGLAND AND WALES

FILE WITH DRN

Thank you for your letter of 22 January in which you suggest a change in the arrangements that we had agreed in E(A) for flood defence and land drainage. You also refer to this in your minute to the Prime Minister of the same date.

As you say in your letter, the issue that you raise is of importance especially to the agricultural industry. In E(A) last November you told the Committee that it would be important to retain the flood defence and large drainage functions within the public sector through reconstituted Regional Land Drainage Committees. E(A) supported these arrangements, and I would be strongly opposed to altering them. Although you advance arguments for doing so, it is clear that the arrangements you have in mind would cause us severe difficulties - and particularly me as Minister of Agriculture.

Moreover this is a matter which we must resolve before we publish the White Paper. We shall at once be asked what we mean, and we cannot possibly say that we have not decided. I am afraid therefore that I cannot agree to the change you propose.

I am copying this letter to members of the Cabinet, John Wakeham, John Moore, Bertie Denham, and to Sir Robert Armstrong.

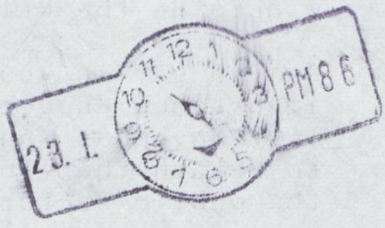
Yours Sincerely

for MICHAEL JOPLING
(approved by the Minister
and signed in his absence)

LOCAL GOUT

WATER

PT 3



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CCBG

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

The Rt Hon Kenneth Baker MP
Secretary of State for the Environment
2 Marsham Street
LONDON SW1

22 January 1986

NBPM.

Dear Kenneth

WATER PRIVATISATION

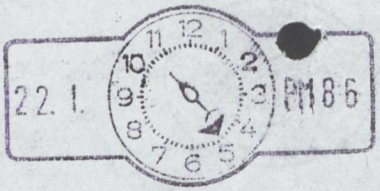
I have read your White Paper with great interest. Both the British Airports Authority and water authorities are continuing monopolies and we therefore have similar, but very far from identical problems, in applying "RPI-X" formulae. I shall shortly be commissioning consultants to advise me, and I think it will be useful if our officials keep in contact in order to see that we benefit from each other's work.

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

Yours ever

Nicholas

NICHOLAS RIDLEY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PJ

CONFIDENTIAL

cc BG

Department of the Environment
2 Marsham Street London SW1P 3EB
Telephone 01-212 7601

NB 2 PP's

Minister for Housing, Urban Affairs and Construction

My Ref: B/PSO/10278/86

21 January 1986

NBPM

WATER PRIVATISATION - DRAFT WHITE PAPER

Thank you for your letter of 10 January about the White Paper on water privatisation.

I think we have been able to meet all your points adequately. We will be circulating a revised text in the next day or two, and you will find that explicit reference to RPI-X is no longer a feature, although we do refer - as I think we must - to the fact that there are precedents for price control formulas in the Telecoms and Gas cases. I agree that a good deal more work needs to be done in working up a model appropriate to the water industry.

On committees, the draft now includes a sentence that our overall aim will be to keep the structure of WSPLCs as simple as possible. We no longer refer to separate recreation and conservation committees and I accept that we will need to look, interdepartmentally, at the arrangements for all the functions you mention to ensure that simplicity is, if possible, achieved.

On research and development, we think it is important (and we will be under a good deal of pressure in the House of Lords Select Committee on Science and Technology and elsewhere if we do not say this) that the WSPLCs should be able to carry out themselves, or to have carried out, adequate research and development to fulfil their responsibilities. We have dropped the reference to environmental and long-term issues, though there will be cases, undoubtedly, where work on such matters will be necessary.

So far as directions are concerned, we will certainly need a mechanism for ensuring that EEC directives and pressing pollution control requirements arising in a national context, can be brought into effect. The Secretary of State will retain his environmental protection duties, including those laid on him by section 1 of the Water Act 1973, and he must have a means of discharging those duties in such a crucial area as water pollution. Nevertheless, I accept your point about the possible alarm which the exercise of direction

powers by future Ministers might cause in the mind of potential investors. The revised draft is therefore couched in terms of powers subject to Parliamentary procedure and I hope that this will give the arrangements the protection you feel is necessary.

Officials have discussed your more detailed points and I believe that the Treasury is satisfied with the way we have handled them.

I am sending a copy of this letter to those who received yours.

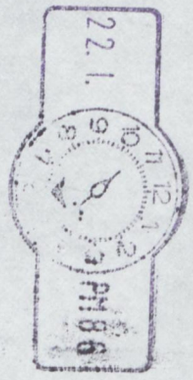
Yours ever, John

JOHN PATTEN

John Moore Esq MP

2F

LOCAL GOVT: Water Ind. PE3.



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CONFIDENTIAL

CC BG

Department of the Environment
2 Marsham Street London SW1P 3EB
Telephone 01-212 7601

Minister for Housing, Urban Affairs and Construction

Ref: B/PSO/10280/86

21 January 1986

Dear Richard.

NBBR.

WATER PRIVATISATION - WHITE PAPER

Thank you for your letter of 10 January to Kenneth Baker about Water Privatisation.

I recognise that we will have to have our arguments ready to explain the differences between our consumer arrangements and those which apply in the Telecommunications and Gas cases. The main reason why each Water Services Public Limited Company is to have its own Consumer Council is that each will be independent of the others and operating in a different part of the country. The degree to which there will be common issues, requiring a common consumer approach, will be limited.

The role of the Director General of Water Services will also be different in significant respects from those for Telecom and Gas cases. In particular, he will be concerned (and indeed responsible, through the licensing mechanism) with issues of service provision and standards of service which will be a crucial part of our regulatory mechanism. This will bring him into close contact with a wider range of issues of concern to consumers, and we consider it appropriate for the Director General to make appointments to the Consumer Councils. They will be his regional watchdogs.

I appreciate what you say about creating a new series of quangos. That was one of the considerations in our minds when we set up Consumer arrangements for water authorities under the Water Act 1973 on the basis that each water authority would appoint its own on a Ministerially approved models. But has it been established that bodies appointed by a Director General are in fact quangos? In any event, we cannot leave responsibility for appointing Consumer committees in the hands of the bodies themselves once they have been privatised. It was difficult to gain acceptance for the present consumer committees given their system of appointment; under a privatised regime it would be impossible.

CONFIDENTIAL

Of the other changes you propose, I think we can agree to the proposed merger of consumer and recreation/conservation committees. The latter were not in our original proposals when the Water Act 1983 was in Parliament but there was strong pressure from the environmental recreation lobbies for their establishment. To abandon separate committees now would be difficult. Nevertheless I am prepared to adopt your proposal in the interests of efficiency. We have adopted your amendment to the text, which is not specific on this point, but our intention is as I have stated it.

I believe we can present our proposals as a significant reduction in bodies and bureaucracy. At present there are 59 committees in all. Under the new proposals there would be 13. Even if the 59 do not count against the quango total I am sure we can put forward these figures with advantage.

Copies of this letter go to recipients of yours.

Yours ever. John

JOHN PATTEN

The Rt Hon Richard Luce MP

LOCAL GOVT; Water Ind: R3.

CONFIDENTIAL

CCBC

SECRETARY OF STATE FOR THE ENVIRONMENT

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref:

Your ref:

24 January 1986

NBPM

Dear Norman,

WATER PRIVATISATION - WHITE PAPER

Thank you for your letter of 6 January. attached

I am grateful for your comments on the draft. I agree with you that we can put more forcefully the argument that privatisation is the best way to improve efficiency and service standards in the water industry, and that we can make a better sales pitch for our very positive policy of legislating to allow full-scale trials of compulsory water metering to go ahead. I hope you will find the final text an improvement in both respects.

I fear however, that I cannot go all the way with your comments on price controls. It is crucial that we should allow the shareholder to benefit from any improvement in efficiency, and it is hard to see what incentive the privatised authorities would have to cut the costs of their services if we were to reward their efforts only by putting a tighter clamp on the prices they could charge in future. There will be further opportunities to consider the detail of the regulatory regime, and a number of important issues will need to be resolved. For the moment, I would prefer to stick to the very generalised description of our intentions given in the present text.

Copies of this letter goes to the receipients of yours.

Yours ever,

KENNETH BAKER

The Rt Hon Norman Tebbit MP

LOCAL GOVT P13

Water

CONFIDENTIAL

SECRETARY OF STATE FOR THE ENVIRONMENT

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref:

Your ref:

21 January 1986

Dear Leon,

WATER PRIVATISATION - DRAFT WHITE PAPER

Thank you for your letter of 13 January about water privatisation.

Detailed arrangements for customer protection, and the inter-relationship of the various bodies you refer to, will certainly need to be the subject of further discussion between officials. A national water consumer consultative committee is not envisaged as such in the White Paper and I can foresee difficulties (eg Richard Luce has commented on the dangers of quango-creation) but this point also can be considered in further discussion.

I am copying this letter to recipients of yours.

Yours ever,

KENNETH BAKER

The Rt Hon Leon Brittan QC MP

LOCAL GOVT RB

Water

SECRETARY OF STATE FOR THE ENVIRONMENT

CCBG

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref:

Your ref:

21 January 1986

Dear Norman,

WATER PRIVATISATION - DRAFT WHITE PAPER

Thank you for your letter of 14 January about water privatisation.

Your letter raises important points which will need to be explored between officials. I have asked my officials to get in touch with yours in due course. Meanwhile, you can be assured that we will take what you say into account in handling any responses to the White Paper.

I am copying this letter to the recipients of yours.

Yours ever,

KENNETH BAKER

The Rt Hon Norman Fowler MP

LOCAL GOVT PT3

Water

cc BG

DEPARTMENT OF HEALTH & SOCIAL SECURITY

Alexander Fleming House, Elephant & Castle, London SE1 6BY

Telephone 01-407 5522

From the Secretary of State for Social Services

NBPR.

The Rt Hon Kenneth Baker MP
Secretary of State for the
Environment
Department of the Environment
2 Marsham Street
London SW1

14 January 1986

Dear Ken.

WATER PRIVATISATION: WHITE PAPER

Norman Tebbit's letter of 6 January has alerted us to one aspect of the White Paper on which we need to settle a clear line before its publication.

The White Paper rightly makes it clear that the proposed new structure will encourage efficiency and improved standards of service and the cost to the consumer will be regulated. Nevertheless costs may rise in some areas and the provision to experiment with metering of domestic supplies explicitly refers to the possible advantages of compulsory meter installation.

There are likely to be questions on what protection will be available to low income households who might be affected by these changes. It will have to be made clear that there is no provision for additional expenditure through social security. Moreover, the changes to supplementary benefit set out in the White Paper on Social Security and shortly to be published in the Social Security Bill will not provide scope in future for compensating low-income householders for above average charges.

The current position is that supplementary benefit recipients are directly reimbursed for their actual weekly water charges irrespective of whether these are billed on a standard rateable value or metered basis. However, on the introduction of the income support scheme, this arrangement will cease. Instead, a standard amount towards average water charges will be taken into account when benefit rates are set.

On the question of installation of water meters there is no separate provision at present to meet the cost for low income householders. Again the changes to be implemented through the Social Security Bill, which will replace the existing single payments provisions with a Social Fund

for making repayable loans and grants, would not in our view provide the means in future for assisting households with the cost of installing meters.

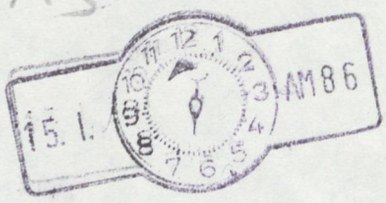
It is important therefore to make clear in any Government response to comments on the White Paper that the safeguards for consumers, including households with low income, lie in the scope for increased competition and efficiency and the proposed framework for regulation and not through increased social security expenditure.

I am copying this letter to the Prime Minister, Members of Cabinet, John Wakeham, Bertie Denham, Sir Robert Armstrong and Brian Griffiths.

NORMAN FOWLER

LOCAL GOVT PC3

WATER



CCBG

JU130
Secretary of State for Trade and Industry

DEPARTMENT OF TRADE AND INDUSTRY
1-19 VICTORIA STREET
LONDON SW1H 0ET
Telephone (Direct dialling) 01-215 5422
GTN 215) .....
(Switchboard) 01-215 7877

13 January 1986

CONFIDENTIAL

The Rt Hon Kenneth Baker MP
Secretary of State
for the Environment
Department of the Environment
2 Marsham Street
London SW1P 3EB

Dear Kenneth,

WATER PRIVATISATION: WHITE PAPER

Thank you for copying to me your minute of 23 December to the Prime Minister enclosing a draft of your White Paper.

I think that the draft generally sets out well the case for privatisation on the agreed basis that integrated river management should be preserved. I am sure that it is right at this stage to leave open some of the details, so that these can be considered in the light of reactions to the White Paper.

It will be important to ensure that the final arrangements contain adequate powers to achieve the objectives set out in the White Paper. My officials will need to be particularly closely involved in the working up of the detailed arrangements for regulation and customer protection, and the relationship between the new Director General of Water Services, the Director of Fair Trading, and the Monopolies and Mergers Commission. One possibility which we shall need to look at is some form of co-ordination at national level between the proposed regional consumer consultative committees.

I am copying this letter to the Prime Minister, Members of Cabinet, John Wakeham, Bertie Denham, Sir Robert Armstrong and Brian Griffiths.

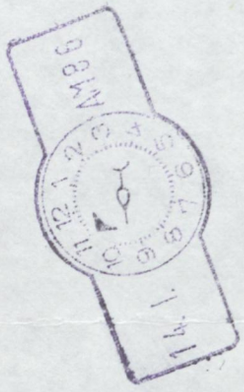
Yours,
Leon

LEON BRITTAN

999-1

LOCAL GOVT PT3

Water Industry.



FROM:
THE RT. HON. LORD HAILSHAM OF ST. MARYLEBONE, C.H., F.R.S., D.C.L.

LORD CHANCELLOR

HOUSE OF LORDS,
LONDON SW1A 0PW

CCBG

13 January 1986

CONFIDENTIAL

NDPR.

My dear Kenneth, Water Privatisation - White Paper

Thank you for copying to me your minute of 23 December 1985 to the Prime Minister. I have no particular points to make on the draft White Paper, save to suggest that the economic case for privatisation is perhaps argued somewhat weakly. For example, paragraph 4.2 points out that regulation of prices will remain a permanent feature of the water industry, yet competition on price is the most normal form of competition, the virtues of which are referred to elsewhere in the draft.

In this regard, I entirely agree with Norman Tebbit that the draft should contain some provision so that customers in lower-cost areas are given some guarantee that their charges will reflect the above-average performance of the water supplier in their area.

I am copying this letter to the Prime Minister, Members of Cabinet, John Wakeham, Bertie Denham, Sir Robert Armstrong and Brian Griffiths.

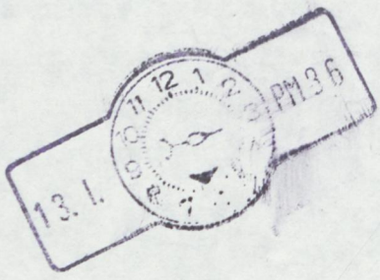
Yrs.

The Right Honourable
Kenneth Baker MP
Secretary of State for
the Environment
Department of the Environment
2 Marsham Street
London SW1

LOCAL GOVT

WATER

PT 3



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OA

bc BG.

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

OA

CONFIDENTIAL

CC BG

Cabinet Office

MANAGEMENT AND PERSONNEL OFFICE

From the Minister of State
Privy Council Office

The Rt Hon Richard Luce MP

Great George Street
London SW1P 3AL
Telephone 01-233 8610

The Rt Hon Kenneth Baker QC MP
Secretary of state for the Environment
2 Marsham Street
LONDON SW1P 3EB

10 January 1986

NBPM

Dear Kenneth,

file with DN

WATER PRIVATISATION - WHITE PAPER

I have seen your minute to the Prime Minister of 23 December and the attached draft White Paper on Water Privatisation.

As you know I have responsibility for policy on NDPBs, and I am therefore interested in the arrangements envisaged for protecting consumer interests (paragraphs 4.24 and 4.25). I should like to raise two points.

As currently drafted, the arrangements differ from the OFTEL and OFGAS models. You propose a network of regional consumer councils with members appointed by the Director General of Water Services. In both the OFTEL and OFGAS case there is a national consumer council, with regional representatives. Members are appointed by the Secretary of State. I believe that your officials see good reasons for the differences in approach, but we shall need to be ready to explain why the alternative model is not right for the water industry.

My second point is that the White Paper proposals appear to result in an increase of 20 in the quango count. Paragraph 4.25 proposes that consultative committees (on water matters) should be set up at authority level and that recreation and conservation committees (RCCs) should be retained. I understand that members of the RCCs and divisional consultative committees on water are currently appointed by the Water Authorities but that, after privatisation, all their members will be appointed by the DG of Water Services. As such, all these bodies will then count as NDPBs. As you know, our policy is to resist setting up NDPBs wherever possible. I accept that these will not, strictly speaking, be new bodies. But they will come into the quango count for

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the first time and there is no denying that the change in the appointment arrangements gives them a closer relationship to central Government. I wonder therefore whether this is in an area that you could look at again to see if alternative arrangements could meet the need for consumers' interests to be represented without this unwelcome increase in the numbers of quangos.

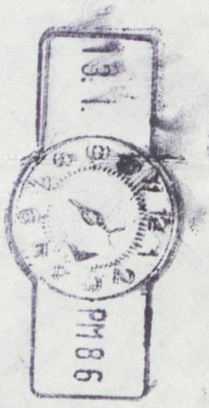
Leaving appointments to these bodies in the hands of the water authorities would of course achieve this. I realise though that this may be seen as prejudicing their independence from the water authorities and you are better placed than I am to judge how strong an objection this is in practice. If that option had to be ruled out, an alternative would be to have one body in each area rather than two; or, if one body could not adequately cover both aspects, you might consider whether an existing body, with appropriate changes to its terms of reference and membership (e.g the Countryside Commission) could represent consumer interests in relation to recreational and conservation issues.

I do not want to delay publication of your White Paper while this subsidiary issue is looked into. If the bracketed phrase "(in parallel with the English recreation and conservation committees which will be retained)" were removed from paragraph 4.24, this would leave us sufficient flexibility to explore options for the best structure for consumer representation. I think the final sentence of paragraph 4.24 gives the necessary assurance that customers' interests will be properly looked after.

I am copying this to the Prime Minister and other recipients of your minute of 23 December.

RICHARD LUCE

local Auth; Water Ind. Pt 3



2159/7

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cc BG

FINANCIAL SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

10th January 1986

The Rt Hon Kenneth Baker MP
Secretary of State for the Environment
2 Marsham Street
LONDON SW1

NRBM

Dear Kenneth.

WATER PRIVATISATION: WHITE PAPER at flap WITH DRN

Thank you for copying to the Chancellor your minute of 23 December to the Prime Minister and the draft of the White Paper. I agree with Norman Tebbit's view (his letter of 6 January) that it makes a good case for privatisation of the Authorities in their present form and that it meets very adequately the argument that privatisation would jeopardise the interests of consumers and the environment. I am also grateful for the efforts your officials have made in keeping my people here at the Treasury closely in touch during the drafting of the Paper.

I think that Chapters 2 and 3 read well and that the balance has been struck satisfactorily in explaining why there are limits on the extent to which further improvements can be achieved within the public sector without denigrating those very real achievements which have been made by the Authorities since the reorganisation in 1974.

I remain, however, slightly concerned by the extent to which we appear to be committing ourselves to an RPI - x type formula in Chapter 4. There is a great deal of work to be done on the nature of the regulatory framework following publication of the White Paper and the precise mechanism of the formula could easily be left more open, for example in 4.12 where there is a firm steer towards RPI-X.

Secondly, the reference to new committees (eg in paragraph 4.25) gives the rather misleading impression that there will be an elaborate new committee structure accompanying privatisation. The proposals, for consumer consultative committees at authority

level which will replace the original divisional committees, for recreation and conservation committees and fisheries committees may be acceptable but I am sure that the structure should be kept as simple as possible and that this should be a stated aim.

Thirdly, it is proposed (paragraph 4.7) that the licence should require WSplcs to make an adequate contribution to R&D. This is an unusual licence condition and while I can understand your concern that underinvestment in research would, in practice, take place without such a licence requirement, I feel it may be unwise to include such a specific reference when so many details of the regulatory regime remain open. At the very least the reference to "contributions" could be dropped, so that the licence would require WSplcs "to maintain an adequate research and development capacity". This leaves the question slightly more open.

Fourthly, it is proposed in Chapter Five that the Secretary of State should retain a general power of direction with respect to their responsibility as polution control authorities (5.10). I am not convinced that it is practicable or desirable for future Ministers to have such a power of direction over private sector companies. Whilst I quite appreciate the need for control, I do feel it would be more appropriate for it to be exercised through a proper statutory system or through a neutral third-party (eg the Director-General) rather than through ad hoc powers of Ministerial direction. The idea that future Ministers should have unconstrained powers of direction over future private sector companies makes me very uneasy.

I have annexed a number of more detailed drafting points which I think could usefully be incorporated and I would be grateful if our officials could agree how these should be handled.

Copies of this letter to go to recipients of yours.

JOHN MOORE

ANNEX

DETAILED COMMENTS ON DRAFT WHITE PAPER ON WATER PRIVATISATION

1.3. As the benefits listed do not relate exclusively to the consumer, as is now implied, the first sentence could be revised to "The Government believes that the nation will benefit from privatisation of the Water Authorities in the following ways:"

1.5-1.10. In a number of cases (eg environmental protection) it is probably worth mentioning improved arrangements under more than one heading as they benefit more than one group.

1.13. 2nd sentence, delete "also" as it is redundant.

2.11. It is rather unhelpful to refer to flood defence in the context of the importance of integrated management over the whole river catchment area, as it is not a function which will be retained by the WSplcs.

2.22. Last sentence. The reference to real profits is rather obscure. Amend to "since 1979, the Government has stimulated them to more effective management by requiring the authorities to achieve a rising real rate of return, more in line with that of the private sector as a whole."

2.25d. The statement about future levels of expenditure on flood protection and land drainage are more quantified and pre-emptive than for the other areas of expenditure discussed in this paragraph. As neither flood protection nor land drainage are being proposed for the privatisation cost this commitment seems unnecessary. The first two sentences should therefore be amended to read "The Water Authorities have planned to incur capital expenditure of £200-250m over the next 4 years to prevent flooding and there will be a continuing need for such work into the 1990s."

2-Tables. As chapter 2 concentrates on achievements since the 1973 Act, it would be appropriate for the tables to date from then. Table 3 does not state the year to which it refers.

3.4. Last sentence. Insert "WSplcs" before "articles of association".

3.9. The possibility of making the direct beneficiaries pay or developers contribute to expenditure on land drainage and flood protection is under consideration but the opening part of this paragraph rather gives the impression that there is a commitment to fund all expenditure from the public purse. It would be better to say "The Government proposes to reconcile these opposing ideals by new arrangements for the financing and co-ordination of ....."

4.2. Although it is correct to say that the water industry differs from Telecommunications and Gas in the extent to which competition is possible, it is similar in its local distribution networks. To this extent it is consistent to treat water similarly and it would be useful to make this point here.

4.3. and 4.13. Both give "consultancy" as main example of the scope for competition in services. This sells us short. There is scope for competition over a wide range of leisure services and 4.13 is more diffident than is necessary on the scope for competition on laboratory analysis, sewage treatment and competition for customers on authorities' borders.

4.19(ii). The reference to the various situations being reflected in their "flotation prices" may give rise to the misleading impression that the Government would be prepared to sell certain authorities at a larger discount than others.

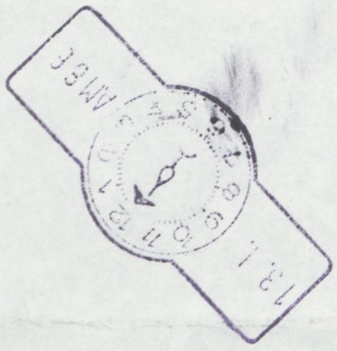
4.20. Delete reference to "the formula described" and insert "a price control formula of the type described".

4.23. This paragraph, which explains how the cost of services currently funded by the Environmental Service Charge will be met, is slightly opaque and gives over-heavy emphasis to the consultative process which the Director General would undertake in coming to a decision about the appropriate subsidy. Perhaps it could be revised to read "the Government will expect efforts to be made for the maximum possible recovery for those services currently funded by the Environmental Service Charge. Some areas of new 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 and, as described in paragraph 3.15, WSplcs will be able to meet the net cost of those services currently funded by the Environmental Service Charge from the Charges for their main services. The size of the contribution which is at present no higher than 2.5% in any part of the country would be determined, after appropriate consultation, but the Director General. There is no question of repealing obligations.....".

5.6. Last sentence: delete "and tradition of public service" as it may invite the comment that a better way of preserving this tradition would be to retain the authorities in the public sector.

LOCAL GOVT PTS

WATER INDUSTRY



Prime Minister

Agree to write as proposed? – No – leave it alone. There are more important things.

(Malvern, by the way, has had water metering for more than a century!)

DKV 10/1

PRIME MINISTER

10 January 1985

WATER PRIVATISATION

This draft White Paper is admirably clear and well-written. It proposes:

1. privatisation of all 10 Water Authorities;

2. transformation of the authorities into PLCs;

3. retention by the authorities of almost all their present functions (so that they remain responsible for management of the entire water systems in their areas, except for the financing of land drainage and flood protection);

4. establishment of a Director General, who will license the authorities, control their charges and ensure that they meet set standards of quality;

5. establishment of a new independent consultative committee for each authority, reporting on any complaints to the Director General;

6. permission for the authorities to undertake compulsory metering experiments (forcing the inhabitants of given areas to instal meters);

7. the setting of new 'quality objectives' for drinking and river water;

8. clear powers for the authorities to control pollution;

9. permission for the (small) private water companies to become PLCs and to act in their own right; (at present, these are statutory companies that act only as agents for the Water Authorities);

10. establishment of a new appeal system for companies whose activities are regulated by the Water Authorities to ensure that they are treated even-handedly.

Comments

1. The paper gives the impression of introducing a substantial amount of regulation of the water industry in order to protect the environment and to ensure quality and efficient performance. But it in fact does little more than convert existing regulation to fit the new framework. The balance seems about right.

2. The Paper is weaker when it deals with the advantages of emulation between water authorities. This is not even mentioned in the principal sections on competition. But the Paper does clearly propose linking the RPI-X price control to a moving average of all the water authorities performances (para 4.12). This will ensure that the most effective companies will make the largest profits, and will therefore encourage all of them to be more efficient.

3. The Paper rightly makes clear that the Government is in favour of improving water quality and reducing pollution; but it leaves the impression that this is something which the Government would wish to improve ad infinitum. That is dangerous. True, the Mersey must be brought up to the Thames' new standard; but there is less reason for expensive improvements beyond that level. Everyone wants tap water of good drinking quality, but few may wish to pay for continually rising standards of purity. The paper does not, in fact, say in so many words that standards should be raised indefinitely, but care will need to be taken to ensure

that this impression is not given during the debates in the House.

4. The one major defect of the White Paper is the section on water metering (para 4.21). It pays lip service to the benefits of compulsory meter installation but only proposes legislation for experiments in compulsory metering. It fails to include three vital items mentioned in your Private Secretary letter of 9 December:

   i. a timetable for the trials;

   ii. legislation enabling compulsory water metering to be extended by Affirmative Order once the experiments have been completed;

   iii. compulsory installation of water meters in all new dwellings.

Conclusion

We recommend that you should:

- welcome the White Paper; but

- ask for changes on water metering, to bring the proposals into line with your Private Secretary letter of 9 December; and

- ask for greater emphasis to be placed on the emulation and efficiency gains that would be caused by a clever pricing mechanism of the kind suggested.

OLIVER LETWIN

PETER WARRY

CC BG

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister

KBaker.

The Rt Hon Kenneth Baker MP
Secretary of State for the Environment
2 Marsham Street
London SW1 2EB

10 January 1986

Dear Ken

I have now seen a copy of the White Paper on Water Privatisation, and I can confirm that I would be content to sponsor the paper jointly with you and Nicholas Edwards.

You rightly mention in your minute the work that we need to do on the administration and financing of flood prevention and land drainage. Decisions in this area are long awaited, but they could only sensibly be taken once a decision to privatise water authorities had been initiated. I hope that you and my colleagues will urge their officials along with mine to give priority to this review so that we can reach decisions in the Spring and any necessary legislation can be introduced in the 1986/87 session. This will enable the arrangement to link smoothly with the programme for water authority privatisation and show the importance that we all attach to flood defence.

I am copying this letter to the Prime Minister, colleagues on E(A) and Sir Robert Armstrong.

Yours

Michael

MICHAEL JOPLING

LOCAL GOVT

WATER INDUSTRY

PT 3

CC/BG

NBB7

SECRETARY OF STATE FOR THE ENVIRONMENT

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434
My ref:

Your ref:

8 January 1986

Dr Nick.

WATER PRIVATISATION

Thank you for your letter of 23 December.

It is of course important that the White Paper should give full recognition to any special features of the situation in Wales, and my officials will be in touch with yours to ensure that this is done. Meanwhile, we will seek to improve the detailed drafting and would be glad of any specific suggestions you may have to make. Again, our officials can discuss.

I am copying this letter to the recipients of yours.

Yours ever

Kenneth

KENNETH BAKER

The Rt Hon Nicholas Edwards MP

Local Govt; Water Industry Pt 3

CONFIDENTIAL

CABINET OFFICE,
WHITEHALL, LONDON SW1A 2AS

Chancellor of the Duchy of Lancaster

Tel No: 233 3299
7471

6 January 1986

The Rt Hon Kenneth Baker MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON
SW1

Dear Kenneth.

WATER PRIVATISATION - WHITE PAPER

Thank you for the copy of your minute of 23 December to the Prime Minister, enclosing a draft of the White Paper.

The draft makes a good case for privatisation of the industry on the basis of integrated river management, and sets out well the ways in which the interests of the customer and the environment are to be safeguarded.

There are three points, however, where the draft needs particularly to be presented convincingly. The first is the point (para 2.26) at which the argument is made that privatisation is now the best means of continuing and enhancing a process of improved efficiency and service generated since 1979. We must make clear that providers of private capital are both more flexible, and inclined to the enterprising and innovative approach, than public providers of capital. They will give the now-improved management and staff the impetus they need for greater efficiency. And, in practical terms, state ownership imposes constraints which the authorities' managements wish themselves to be free of.

The second, and related, point concerns water metering. The draft should be more positive in its approach. Charging by reference to rateable values will increasingly be anachronistic; and charging by reference to consumption is much preferable for a private sector company engaged in selling a service to its customers.

The third point concerns price controls. A price control set by reference to changes in average performance on costs provides safeguards for customers in higher-cost areas, but does not guarantee to customers in lower-cost areas that their charges adequately reflect the above-average performance achieved in their

area. Some provision should be made for this. We might also stress that the price of a commodity should be expected to reflect the change in performance of producers in the industry and the average cost of its inputs. One safeguard, however, should be not necessarily to allow companies to pass on directly in full changes in costs which are within their control, eg some pay increases, nor entirely to be able to pass on changes in the cost of capital, which must be reflected, in part, on the rate of return to equityholders.

I am copying this letter to the Prime Minister, Members of Cabinet, John Wakeham, Bertie Denham, Sir Robert Armstrong and Brian Griffiths.

NORMAN TEBBIT

LOCAL GOVT PCB

WATER INDUSTRY

CONFIDENTIAL

SECRETARY OF STATE FOR THE ENVIRONMENT

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.

CONFIDENTIAL

CONFIDENTIAL

SECRETARY OF STATE FOR THE ENVIRONMENT

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.

S Wanderson

for

K B

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

CONFIDENTIAL

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;

* 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

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

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.

SECTION 2: THE WATER AUTHORITIES NOW

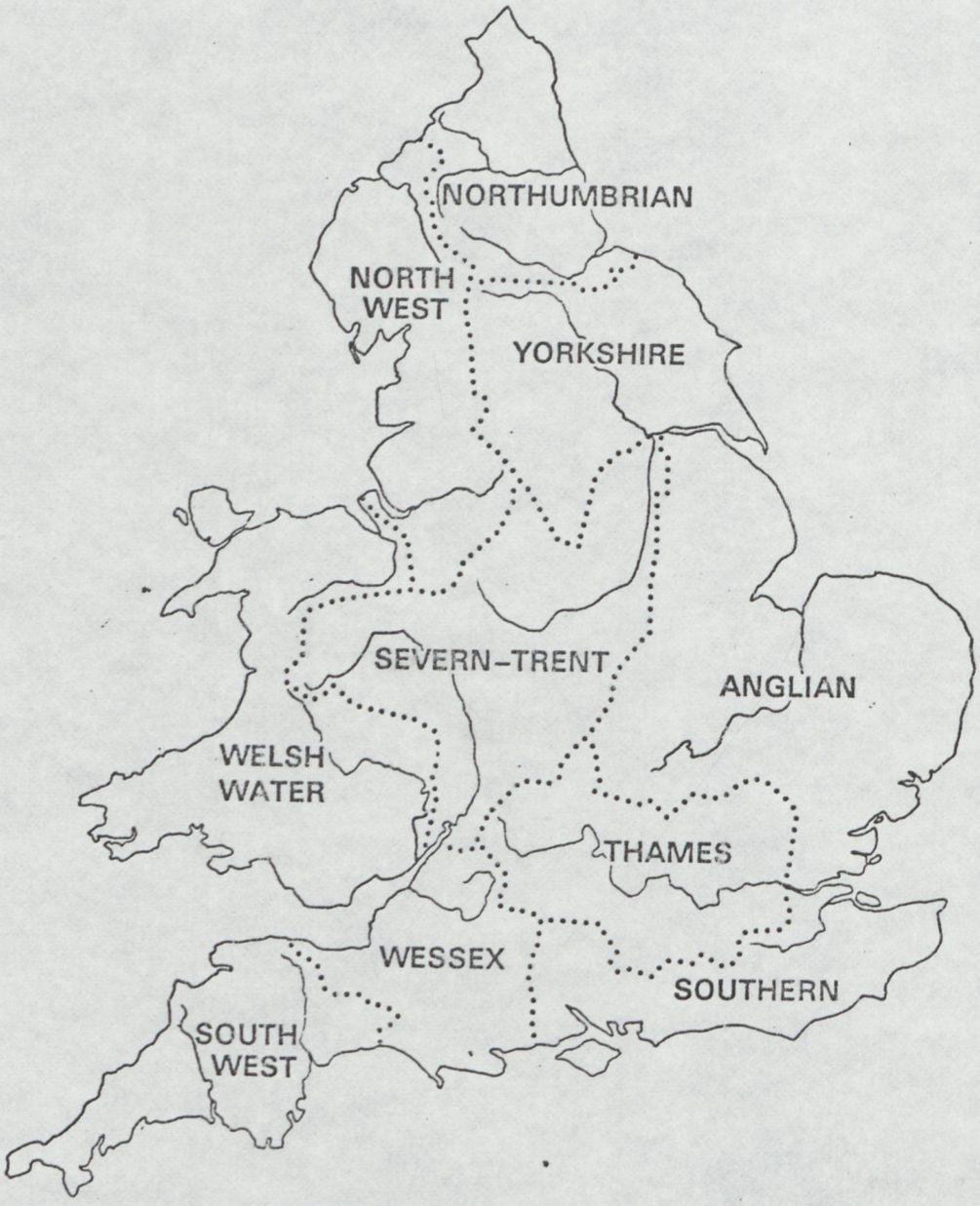
Integrated River-Basin Management

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

WATER AUTHORITIES IN ENGLAND AND WALES



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

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.

OPERATING EXPENDITURE: WATER AUTHORITIES

ENGLAND & WALES INC LAND DRAINAGE 1984/5

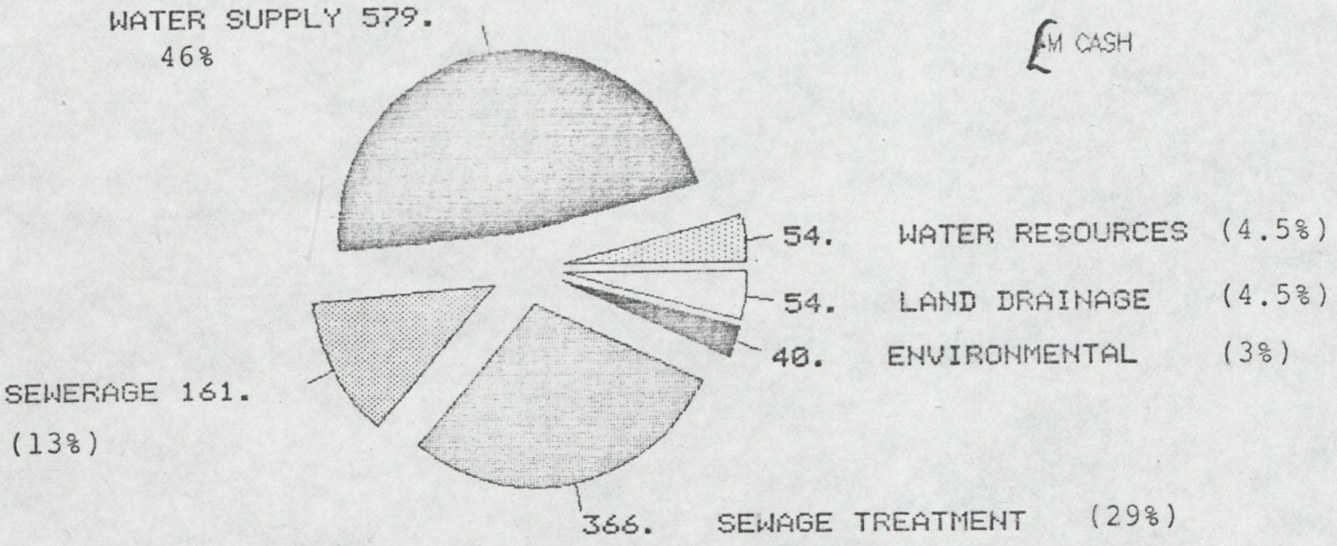


Figure 1

CAPITAL EXPENDITURE: WATER AUTHORITIES

ENGLAND & WALES INC LAND DRAINAGE 1984/5

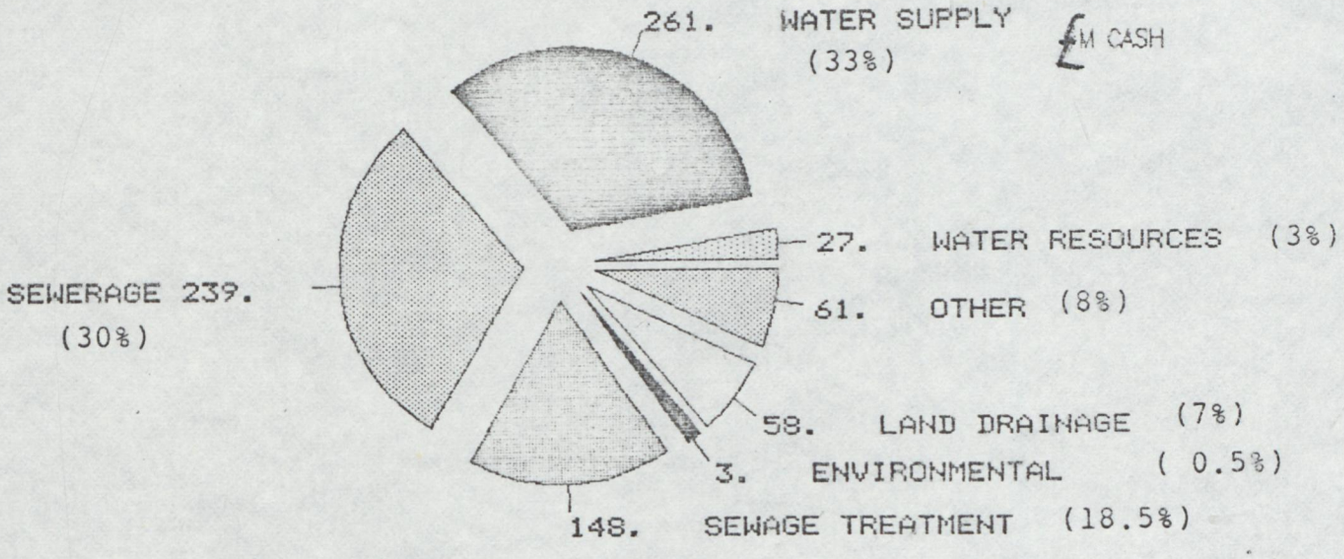


Figure 2

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

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

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, onwhich 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

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.

TABLE 1

WATER AUTHORITY - MANPOWER (at 31 March each year)

	1976	1979	1982	1985	30 September 1985
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
Total	60649	63204	60586	51785	51030

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: £ millon 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

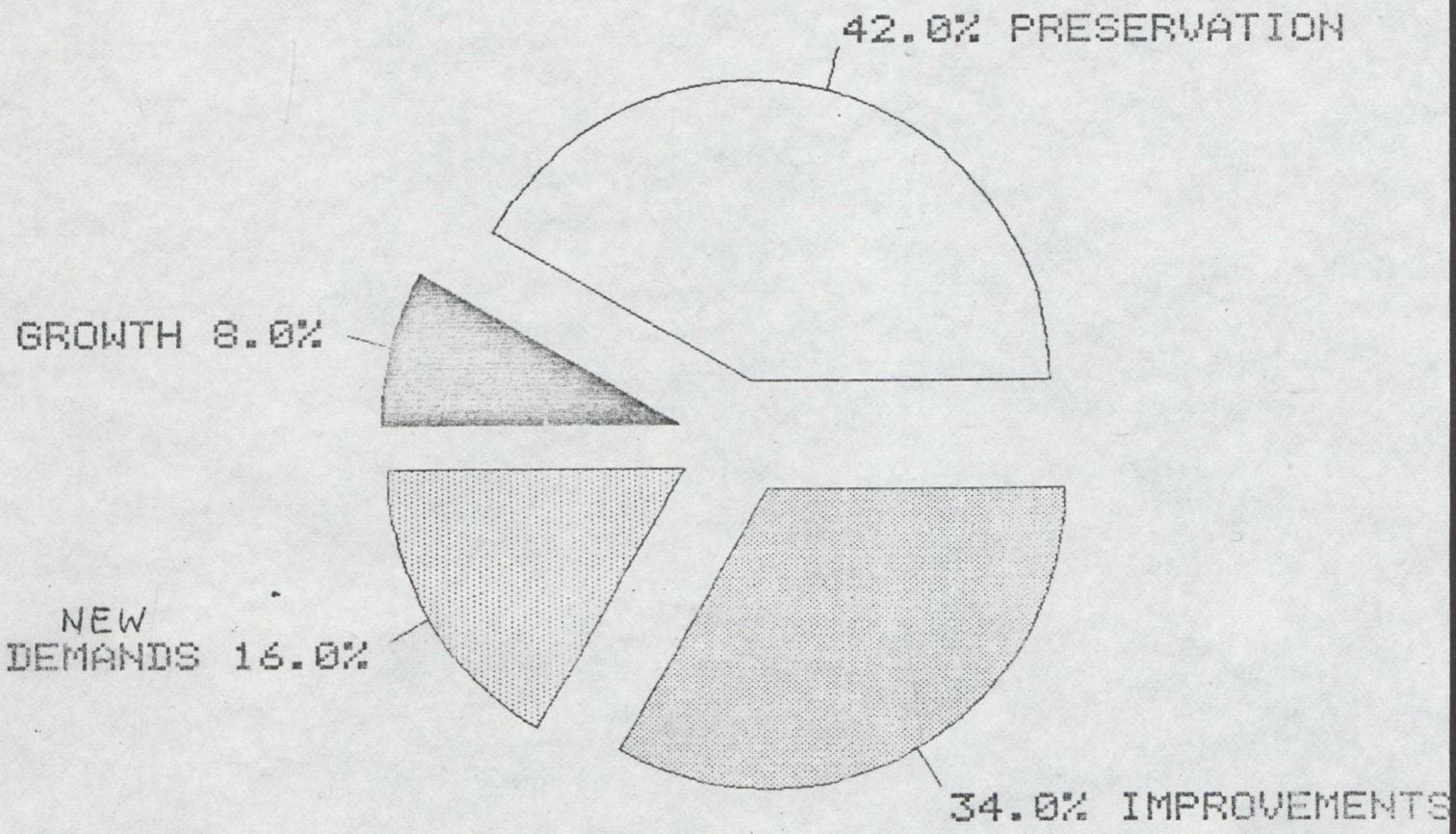

FIGURE 3

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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.

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.

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

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 (Cmnd 9449) issued in March 1985.

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

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

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.

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 responsibe 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 - for example by 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.

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

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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

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 Director-General 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

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,

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

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 Governments'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.

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.

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

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

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.

- 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

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

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

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.

SECTION 6: NEXT STEPS CONFIDENTIAL

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.

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.

ANNEX

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).

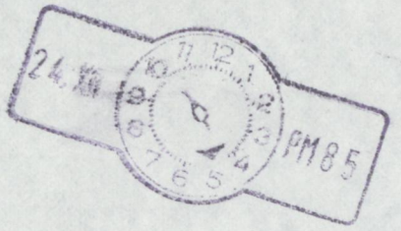
6. Who's Who in the Water Industry (Water Authorities' Association, 1 Queen Annes's Gate, London SW1H 9BT, £13.00).

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).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From The Secretary of State for Wales

The Rt Hon Nicholas Edwards MP

23 December 1985

Dear Secretary of State,

NBPM.

WATER PRIVATISATION - WHITE PAPER

I understand from my officials that you have issued instructions for the draft White Paper to be sent to the Prime Minister.

You will appreciate that, as the draft only reached me today, I have only had a very quick look at it. My officials have drawn my attention to a number of issues having a Welsh dimension, including consumer representation where separate provision for Wales may well be desirable. I must therefore reserve my position until we have reached agreement on such issues. In terms of drafting it needs a good deal of sharpening and the general argument for privatisation needs to be better presented.

I am copying this to the Prime Minister, colleagues on E(A) and Sir Robert Armstrong.

Yours sincerely,

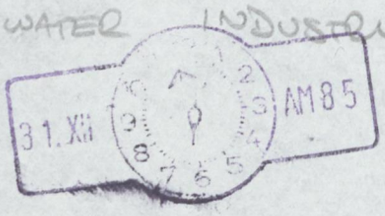
Peter

(Approved by the Secretary of State and signed in his absence)

The Rt Hon Kenneth Baker MP
Secretary of State for the Environment
2 Marsham Street
LONDON
SW1 2EB

Local Govt Pt 3

THE WATER INDUSTRY



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PAY IN CONFIDENCE

CCM

2 PP's

Treasury Chambers, Parliament Street, SW1P 3AG

John Patten Esq MP
Minister for Housing, Urban Affairs
and Construction
Department of the Environment
2 Marsham Street
London
SW1P 3EB

NBPM.

17th December 1985

Dear John,

BOARD MEMBERS' PAY 1985: BRITISH WATERWAYS BOARD

Thank you for your letter of 3 December about the pay of the Chairman, Deputy Chairman and members of the British Waterways Board (BWB).

In view of your comments about BWB performance and the fact that there was no 1984 pay review, I am content with your proposals for 1985 increases of 8 per cent for the Chairman and 10 per cent for the Deputy Chairman and Members. This gives the following revised salaries from 1 July 1985:

	Part-time Salary Paid	Notional Full-time Salary
	£	£
Chairman Sir Leslie Young (2.5 days a week)	16,038	32,076
Deputy Chairman Dr A Robertson (1.5 days a week)	6,600	22,000
Members (2 days a month)	3,300	-

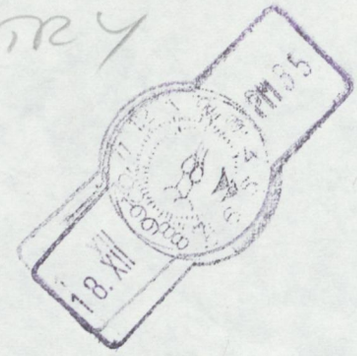
I am copying this letter to the Prime Minister, other members of E(NI), and to Sir Robert Armstrong.

Yours ever,

JOHN MacGREGOR

PAY IN CONFIDENCE

LOCAL GOVT
WATER INDUSTRY
PT 3



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CHIEF SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Kenneth Baker MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
London
SW1P 3EB

16 December 1985

Dear Kenneth,

WATER CHARGES AND INVESTMENT

Thank you for your letter of 13 December. We must obviously sort this out quickly.

I have no problems with much of what you say. I entirely agree that there is a widespread hope amongst our supporters for lower water charge increases in future years. But we must not confuse hopes with reality and the plain fact is that we do not yet know what future financial target path and price levels may be necessary. It would not make sense to hold out a hope which we might find we could not deliver, or delivery of which was damaging to our privatisation strategy. I see nothing in the totally non-committal approach I suggested which would give grounds for accusations of fattening up the authorities in advance of privatisation. In fact, the present order with its lower average target than the 1.7 per cent earlier announced is itself adequate rebuttal of this.

I cannot therefore agree that the original line which you proposed is satisfactory. I can only repeat that it is both an unnecessary hostage to fortune and unfair to colleagues in the presumptions it creates. If you believe that the alternative formulation I suggested relies too much on privatisation (although it says nothing more than has already been said and makes a point which will certainly appeal to our supporters in the House), then I remain clear that you can go no further than indicating, without commitment, that water authorities future financing, in common with that of all other nationalised industries, will be considered during next year's public expenditure round.

I am copying this letter to the Prime Minister, other membersof the Cabinet and Sir Robert Armstrong.

Yours ever,

JOHN MacGREGOR

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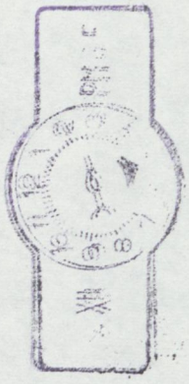
LOCAL GOVT

WATER INDUSTRY

PT 3



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SECRETARY OF STATE FOR THE ENVIRONMENT

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref:

Your ref:

13 December 1985

NRPN.

Dear Chief Secretary,

WATER CHARGES AND INVESTMENT

I am sorry to prolong correspondence on a matter which I thought had been satisfactorily resolved in MISC 120 but your letter of 10 December and the imminent debate on the Rate of Return Order leave me no option.

You will recall that the policy decided by E(NI) in 1984 would have required water authorities' average financial targets to rise from 1.4% in 1985/6 to 1.7% in 1986/7 and 1.9% in 1987/8, implying charges increases of about 11½%, 10% and 9% respectively. I argued in this year's PES that this prospect was politically untenable and I believe that you and other colleagues broadly accepted my view. Indeed the Lord President said, after we had reached an agreement which would allow the 1986/7 increase to come down to about 8%, "I would not mind if the charges increase were rather lower...".

There is little doubt in my mind that colleagues want, and expect, a lower charges increase next year. That hope is of course widely shared by our supporters in Parliament. For John Patten to say that he hopes we shall be able to maintain the more favourable trend is no more than the truth.

Your formulation on the other hand appears to me to rest too heavily on the possibility of privatisation, on which no announcement will have been made. It would moreover give no comfort to our supporters who may fear that the E(NI) policy of 1.9% for 1987/8 announced last year still holds; and it will expose us to the accusation that we are planning to fatten up the water authorities at the expense of water consumers in preparation for privatisation. That would damage the privatisation programme and discredit the Government.

I hope on reflection you will agree that the words we proposed would better meet the situation.

As for the substance of the review which is to take place early next year, our officials need to discuss the details further. But MISC 120 recorded that it would cover "future financial strategy for the water authorities" (Not "every aspect of water authorities operations"). As

we have no policy for water authorities financial targets in 1987/8 at present I do not see how it can avoid dealing with that question. We shall also now need to take into account the cost of metering trials.

I am copying this letter to the Prime Minister, other Members of the Cabinet and to the Chief Whip and Sir Robert Armstrong.

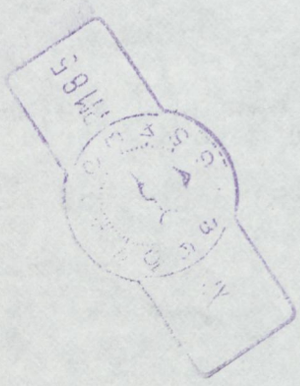
Yours sincerely

for

KENNETH BAKER

(Approved by the Secretary of State and signed in his absence)

The Rt Hon John MacGregor OBE MP



Local Govt:
Water Industry Act 3

10 DOWNING STREET

Prime Minister

pa

Water metering

The Watts report on water metering is already in the bookshops and publication cannot easily be postponed.

However the proposed PQ looks acceptable: it keeps open options for faster change.

Content with the PQ?

DHS
10/12

Yes

MT

SECRETARY OF STATE FOR THE ENVIRONMENT

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434
My ref:

Your ref:

10 December 1985

Dear David,

My Secretary of State has seen your letter of 9 December, setting out the Prime Minister's views about the line to take on publication of the Watts Report on water metering.

In the light of the Prime Minister's desire to react more favourably to the idea of extending domestic water metering, the Secretary of State has revised the text of the announcement which we propose to make tomorrow. I enclose a copy of the revised text which is phrased to respond more positively to the Watts Report.

Your letter raises a number of new policy issues to which the Secretary of State will respond without delay.

Yours sincerely

Sue Vanderson

SUE VANDERSON Private Secretary

David Norgrove Esq.

ANSWER

The report of the Joint Study Group under the chairmanship of Mr R Watts, Chairman of the Thames Water Authority is being published today by Her Majesty's Stationery Office.

The Government welcomes the report. It presents a new view of the economic aspects of domestic water metering. Unlike earlier studies, it concludes that in some circumstances charging households by means of water metering may be cost-effective.

This radically alters the options: and justifies undertaking the extensive trials which the report calls for.

We shall legislate at the earliest suitable opportunity to make progress possible. But before responding to all the recommendations in detail I intend to seek the views of water consumers and others who may be affected. I shall work out with the industry a programme of follow up action.

CC BSC

NBPM.

Treasury Chambers, Parliament Street, SW1P 3AG

CONFIDENTIAL

Rt Hon Kenneth Baker MP
Secretary of State for the Environment
2 Marsham Street
LONDON
SW1P 3EB

10th December 1985

Dear Kenneth,

WATER CHARGES AND INVESTMENT

I am not happy with your letter to me dated 2 December proposing that John Patten should look forward to "a more favourable trend" in future water charges when the 1986-87 rates of return Order is debated.

I have seen an extract from John's proposed speech and I am pleased that he will be justifying our decisions for 1986-87 by announcing that water charges will increase rather less than had been expected, by about 8%, while water investment will increase rather more, by about 10%. However, I understand that he then intends to announce that he is "hopeful we shall be able to maintain the more favourable trend in water charges and water investment for 1987-88."

In my view, the expectations that this statement will arouse will be such as to pre-empt effectively our public expenditure discussions next year and I cannot accept this. It is not yet possible to say what will need to be done from 1987-88.

Nor does it seem to me necessary to say anything along these lines. The possibilities we are considering for privatisation offer a very reasonable line to take about prospects for the future. I suggest that the relevant passage is replaced with one along the following lines:

> "As for the future , we are considering the possibilities for privatisation which would of course mean reviewing

every aspect of water authorities operations."

This passage reflects the point I have consistently made over the last few months that, if it is decided to proceed with water privatisation the whole financial regime applied to water authorities will necessarily have to be reconsidered. I have also said that it does not make sense to separate this out from other work on privatisation and I am not happy with your officials' suggestion that a separate formal review of water authorities' financial targets for 1987-88 should be initiated.

Consideration of the future regime of water authorities should be an integral part of work on privatisation over the next few months and separating it out not only risks wrong decisions but will give the wrong signals to water authorities and others. I cannot therefore agree to this. As long as some water authorities are in the public sector, all decisions that affect their public expenditure requirements will have to be subject to our normal processes.

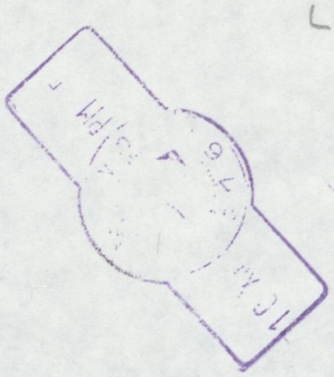
I am copying this letter to the Prime Minister, other members of the Cabinet and to the Chief Whip, and to Sir Robert Armstrong.

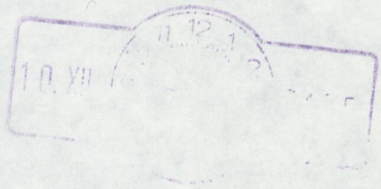
Yours ever,

JOHN MacGREGOR

Local Govt Pt 3

The Water Industry





CONFIDENTIAL

Rite SRW

CC BG x2

10 DOWNING STREET

From the Private Secretary

9 December 1985

Dear Robin,

WATER METERING

The Prime Minister has seen your Secretary of State's minute of 3 December in which he set out the line he proposed to take on publication of the "Watts Report" on water metering.

The Prime Minister strongly disagrees with the proposed approach. She also believes that it is not in accord with the views expressed by colleagues at E(A) when water privatisation was discussed. She believes that it would be right to come forward with much firmer proposals for the introduction of water metering. The present system in her view leads to waste and is inequitable (because some people have to pay for the wasteful behaviour of others).

The Prime Minister points out that the reason why so few meters have been installed is that the meters themselves, and installation, are still expensive. There is a need to start a programme going in order to win economies of scale. It is not enough to provide for all new dwellings to be constructed to "enable" simple meter installation . Meters should be required, in order to encourage mass production. The Prime Minister further questions whether a proxy for water consumption is likely to continue to be available even if rateable value is not, (paragraph 1 of the attachment) and she has noted that the number of losers from a change to metering would be reduced to the extent that people then wasted less water (paragraph 2a). The Prime Minister questions whether it is right to maintain two bases for setting water payments and suggests that it should not be left to companies to decide whether and how far to extend general use of charging by measure.

The Prime Minister would be grateful if your Secretary of State could come forward with firmer proposals for the introduction of water metering. These should include a timetable for the trials. Your Secretary of State might also consider a provision in the privatisation bill for the Government to bring in phased compulsory water metering, by affirmative order. No doubt there are also other possibilities for ensuring faster progress towards metering of water.

BF //

CONFIDENTIAL

I am copying this letter to Private Secretaries to members of E(A).

Yours ever

David

(DAVID NORGROVE)

Robin Young, Esq.,
Department of the Environment

JA1AFF

PRIME MINISTER

WATER METERING

I suspect you may find the recommendations in Mr Baker's minute unacceptably dilatory. He proposes to make it easier to introduce water metering, to encourage trials, and to provide for all new dwellings to be constructed to enable simple metering installation.

The effect is that the water authorities will have available to them the results of the trials. But it will be up to individuals and to the water authorities to decide how quickly metering comes in. The water authorities themselves may well not be attracted to the idea: I know little about them, but there is some risk that they will be size and output oriented.

The main argument against more rapid extension of water metering is that the economics are not proven.

Do you want to ask Mr Baker to come back again with firmer proposals for the introduction of water metering? You might invite him to include a firm timetable for the trials and to consider provision in the privatisation bill for the Government to bring in phased compulsory water metering, by affirmative order, once the results of the trials are known.

Proceed in this way?

DNW

David Norgrove

6 December 1985

CONFIDENTIAL

CC BG

70 WHITEHALL, LONDON SW1A 2AS

01-233 8319

From the Secretary of the Cabinet and Head of the Home Civil Service

Sir Robert Armstrong GCB CVO

Ref. A085/3190

6 December 1985

NBPM.

Dear Robin

The Financing and Administration of Land Drainage Prevention of Flooding, and Coast Protection in England and Wales

In a minute of 5 February to the Minister of Agriculture, Fisheries and Food, Sir Robert Armstrong said that he would be willing to provide a chairman and 'lead' secretary from the Cabinet Office for a group to consider the responses to the Green Paper on this topic. The suggestion for this arrangement had come from the then Secretary of State for the Environment.

The decision in principle taken at E(A)(85) 22nd meeting about the privatisation of water authorities had broadened the context for further work in this field, and I understand that, at official level, your Department, the Treasury and the Ministry of Agriculture, Fisheries and Food all agree that issues arising from the Green Paper should now be processed between Departments in the normal way within that wider context.

Unless he hears to the contrary, therefore, Sir Robert Armstrong will assume that the previous wish for a Cabinet Office chairman and secretary for this exercise has lapsed, though he would be glad to consider providing Cabinet Office services to help resolve any problems that may arise in this field. If Machinery of Government considerations arise, the Machinery of Government Division in the Cabinet Office (MPO) should of course be consulted in the normal way.

I am sending copies of this letter to David Norgrove in the Prime Minister's Office, and to the Private Secretaries to the Secretaries of State for Scotland and Wales, the Minister of Agriculture, Fisheries and Food, the Chief Secretary, Treasury, the Secretary of State for Northern Ireland and the Minister of State, Privy Council Office.

Yours ever

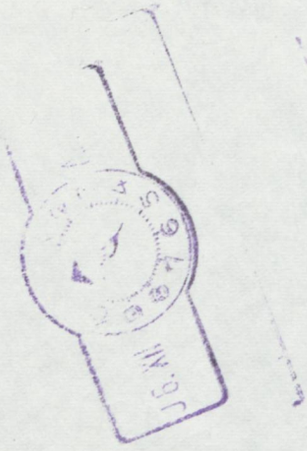
Michael

(M C Stark)
Private Secretary

R U Young Esq

CONFIDENTIAL

LOCAL GOVT : Water Industry : Pt 2.



PD

CJBG

SECRETARY OF STATE FOR THE ENVIRONMENT

Prime Minister

PRIME MINISTER

WATER METERING

E(A) noted on 18 November my intention to publish the "Watts Report" on water metering in the near future. John Patten is arranging for the report to be published on 11 December. I attach a note on the issues raised and the next steps.

I propose:

a. to bring forward legislation, in the water privatisation Bill if that is agreed, to remove legal doubts about compulsory metering trials;

b. to encourage trials of metering, initially to establish consumption patterns but later with a view to trials involving charging by measure once powers are available;

c. to provide, in byelaws, for all new dwellings to be constructed to enable simple meter installation.

require

Unless you or other E(A) colleagues raise objections I shall proceed as above.

but not require.

The point about requiring meters in new homes is to get some mass production not

K.B.

K B

3 December 1985

SG

WATER METERING

Basis of Water Charges

1. About a third of water consumption is already charged for by measure, mainly industrial and commercial. About two thirds, mainly domestic, is charged for by the rateable value of the property supplied. This proxy for consumption produces "rough justice" for some customers which is only somewhat tempered by the effect of minimum or standing charges. All customers can opt to have a meter but only 1 in a 1000 households has done so. Collection of unmeasured charges is cheap and water undertakings make customers opting for meters bear the full cost. A radical change is not inevitable as a result of local Government finance reform. Some form of proxy for water consumption, eg size of property or possibly number of occupants, is likely to continue to be available even if rateable value is not.

2. A change to charging by measure is attractive, and the project of privatisation makes it more so. Two other important considerations are:

a. gainers and losers: a change from a proxy for consumption to measured consumption as a basis for charges will shift their incidence. The new pattern will be more equitable and more efficient as consumers become aware of the cost of consumption. However around half of consumers will pay more - detailed estimates cannot be made because present consumption patterns and likely changes in consumption are

not known. But large families in low RV properties are likely to pay more if metered. There is bound to be a political downside in this area;

b. economic efficiency of metering: a commercial case for metering will depend upon the circumstances of an individual water undertaking: whether consumption is rising, the effect of charging by measure on the particular consumption patterns, adequacy of existing water resources and supply capacity, and other factors. Previous reports identified the high cost of installing and operating meters and smaller savings likely if charging by measure led to reduced water use. The Watts Report advances the argument. Average cost is estimated at around £4.75 per property per year, somewhat below earlier estimates due to economies of scale. Savings are put much higher than previously reported but are less certain to arise and more variable between areas. Only where investment in new water resources, or additional water supply capacity is planned and can be deferred if overall or peak demand for water is reduced by metering, will significant savings in investment costs be made to the ultimate benefit of consumers. Reducing peak demand may make the biggest savings but only if effective measured tariffs relecting peak costs can be devised. The savings may then compare with the costs of metering but they will occur over a much slower timescale than the costs of meter installation, so there will be a large initial financing requirement.

Charging by measure is done and is a right. — How does S7 S justify less than difficult measured payment?

Facilitating metering

3. Under the Water Act 1973, water authorities are free to fix charges on any basis they see fit, provided they are related to costs and are non-discriminatory between classes of consumer. Charging by measure is possible provided classes of consumer are treated consistently. The Attorney General queried the need for legislation to introduce domestic metering, but he accepted that compulsory metering trials (or the phased introduction of general metering) might give rise to legal challenges depending upon the circumstances. The Watts Report recommends that these doubts are removed and other powers to facilitate the introduction of metering are provided.

Trials

4. There are two major gaps in the information needed to assess the economic merits and feasibility of domestic metering:

- consumption patterns and the effect of charging by measure;

- the costs and practical problems of a general compulsory meter installation programme, including use of different technologies.

The introduction of general metering

5. Individual water undertakings decide what form of charges to make. It will in practice be for the post-privatisation companies to decide whether and how far to extend general use of charging by measure. To do so they will need the benefit of the powers and information from trials referred to above. It is too early to presume that

Need for legislation

universal compulsory metering would be their commercial decision.

Proposals

6. In the light of the Watts Report and the above considerations, I propose:

a. to encourage debate by inviting comments following publication of the report;

b. to bring forward legislation, in the water privatisation Bill, if that is agreed, to remove legal doubts about, and otherwise facilitate, compulsory metering trials and the extension of metering;

c. to provide in byelaws for all new dwellings to be constructed to enable simple meter installation;

d. to encourage trials of metering initially to establish existing consumption patterns without charging by measure but later with a view to trials of charging by measure once powers are available.

KT

010

CONFIDENTIAL

CC 3/6

Department of the Environment
2 Marsham Street London SW1P 3EB
Telephone 01-212 7601

Minister for Housing, Urban Affairs and Construction

NBPM

3:XII:85

Dear John:

I have been looking at the remuneration of the Chairman, Deputy Chairman and members of the British Waterways Board. Only the Chairman's pay was increased in 1983, and there was no pay award for any of the Board in 1984.

I now want to reward the Board for their achievements since the new Chairman, Sir Leslie Young, took office in July 1984. We also need to keep sufficiently close to comparable salaries to avoid any difficulties in the future.

I would like to propose an increase of 8% for Sir Leslie Young. Since his appointment he has changed BWB attitudes and policies in line with Government objectives, transferring them into a more cost-conscious organisation working to a realistic Corporate Plan with energetic marketing and profit improvement plans. He has set targets for increased income, manpower reductions and productivity improvements which require urgent action by all parts of BWB. The freight side has responded well despite adverse trading conditions: in particular it has dropped two heavy loss-makers (Weston Point Dock and Brentford Lighter Fleet). The engineering side is reviewing canal maintenance standards in relation to actual use levels and estates division are on target in netting about £1m per annum from a disposal programme for non-operational holdings. The leisure side has particular potential and Sir Leslie is obtaining consultants' advice on a range of possibilities including prospects for a tenfold increase in angling income.

The Chairman's salary was settled in July 1983 and there was no increase when Sir Leslie took office. I believe that a new notional salary of £32,076 would be an adequate response to his achievements: it would still be below that for the smaller water authorities. Sir Leslie's present time input is 50% and we do not propose to change that.

CONFIDENTIAL

CONFIDENTIAL

The Deputy Chairman, Dr Robertson, and other Board members have ably supported the Chairman in his redirection of BWB policies. However, their salaries have not been increased since July 1982, although the members were notified that the increase was to last them until July 1984. In view of the time lapse since the last awards I would propose an increase of 10% taking effect on 1 July 1985. This would bring Dr Robertson's notional salary to £22,000 giving an actual salary of £6,600. Members' new salary would be £3,300 pa.

I hope you can let me have your agreement as soon as possible in order to complete the 1984/85 pay round for my nationalised industries. I am copying this letter to the Prime Minister, other members of E(NI) and Sir Robert Armstrong.

Yours ever, John.

JOHN PATTEN

CONFIDENTIAL

The Rt Hon John MacGregor OBE

2F

CONFIDENTIAL

CLBG

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref:

Your ref:

2 ~~November~~ December 1985

NBPM

Dear Ian,

WATER CHARGES AND INVESTMENT

Thank you for your letter of 25 November.

The hostages to fortune we need to be concerned about are the figures for water authorities' rates of return up to 1987/8 which Ian Gow gave to the House last February. Happily we have been able to ease back the 1986/7 figure from 1.7% to 1.6%. However as Early Day Motion No 129 shows, our supporters are more concerned about 1987/8. There will inevitably be questions about this if our Order is debated and we should do what we can to reassure backbenchers about the prospects. If there has been no announcement about water privatisation, it will not be possible to refer to that so it will be all the more important for John Patten to have something positive to say about the charges prospect, and it is in that context that I believe it will be necessary to refer to our review. Whether or not there is a debate, I will be bound to tell the water authority Chairmen what we have in mind.

I suggest that our officials should be in touch to agree a suitable passage for inclusion in the Government speech in the debate on the Order.

I am copying this letter to the Prime Minister, other members of the Cabinet, the Chief Whip and Sir Robert Armstrong.

Yours ever,
Kenneth

KENNETH BAKER

The Rt Hon John MacGregor OBE MP

LOCAL GOVT

WATER

PT 2

SECRETARY OF STATE FOR THE ENVIRONMENT

Private Secretaries' Office

Kenneth Baker wrote to John MacGregor on 2/12 about water charges and investment. Unfortunately the letter was dated 2 November. I would be grateful if this could be amended.

PJ01/DOE

2/12/4252

3/12

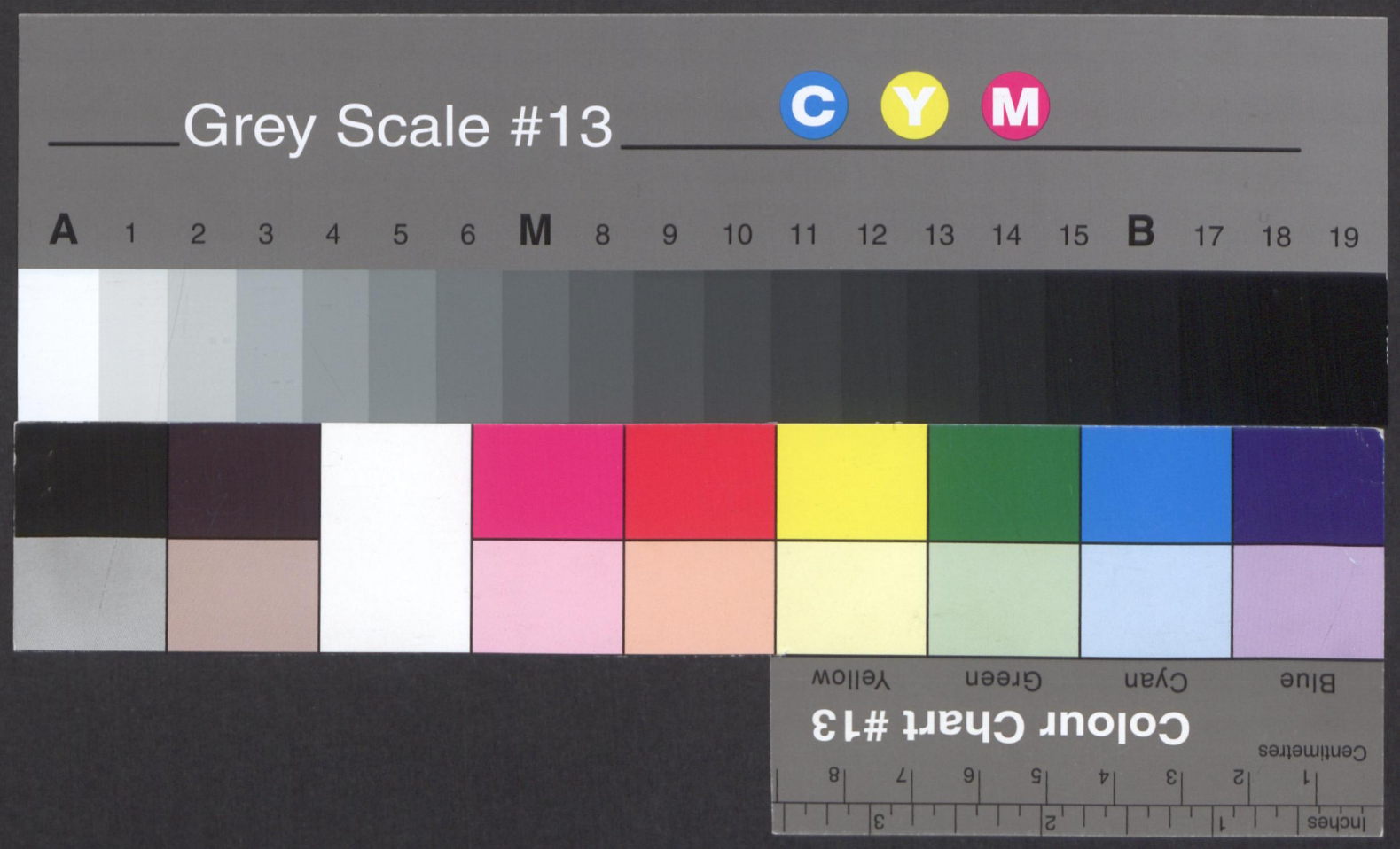
NB Copied as before.

PART 2 ends:-

DN to Environment 26.11.85

PART 3 begins:-

S/S Environment to John McGregor
2 Dec 1985.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