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Water services and agriculture: key issues and strategic options

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2 Water privatisation - so what has really changed?

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INTRODUCTION

Even those in the UK water industry who were against or doubted the sense of water privatisation have changed their minds. I believe the privatisation of the 10 water and waste-water businesses in England and Wales has been the most successful UK privatisation judged first by the provision of benefits for customers and second by providing value for money. With hindsight the 10 water and waste-water businesses were probably the most appropriate candidates for privatisation of all the utilities, since these 10 companies had competed with each other from their formation as separate authorities in 1974. Such competition was not the case for the regional electricity companies that had always been divisions of the Electricity Council, nor for British Gas, British Telecom and the electricity generating companies who were, and to a reducing extent remain, big national, monolithic businesses.

But it has not all been roses. The emotion that water arouses, combined with the increase in water and waste-water charges since 1989 of around 60%, has fuelled criticism of the companies and criticism of the whole idea of water privatisation. And these criticisms remain in spite of universal improvements in the standards of clean water delivered, the standards of dirty water treatment programmes, compliance with EC and UK directives for clean and waste water, and improved services for contact with customers. The old days of 'stop-go' financing by Government have gone - when Government had to choose whether to commit its limited finance to demands often more compelling than sewage treatment, or to demands for funds for

hospitals, schools, transport and other social services. Of course the £28 billion required for the water industry for the 10 years to 1999 would not have survived such Public Service Borrowing Requirement (PSBR) bargaining. It remains the greatest benefit from privatisation that the Government released the 10 companies to find the finance at an 'affordable' price although at increased prices to our customers. But we must remember just how much money the Government put into the water companies at the time of privatisation: money that I believe kept charges to the present reasonable levels. The contribution provided by Government to eliminate the accrued debts of the 10 companies just about matched the £5.2 billion which came from investors who bought the equity of the 10 companies. Had this cash injection not happened then I would see little chance that the 10 companies could have complied, as they do and will, with the water standard requirements of the EC and with the legitimate improved service standards expected for domestic, industrial and agricultural customers. In the company I work for, Wessex Water which is fairly typical, 28% of the payment made by each customer up to 1989 was used by us to pay interest on the accrued debt we had inherited on formation as the then Wessex Water Authority in 1974 when we were derived from 99 separate river, drainage, water supply and municipal waste treatment boards who brought with them a debt which added up to £140 million.

BENEFITS OF PRIVATISATION

The three principal benefits from privatisation of the 10 companies have been:

- (i) the availability of funds to the companies to put right years of neglect and to comply with new standards;
- (ii) competition by comparison, not least the drive for profits to employ on the capital spend (as well as paying dividends) as a result of an enterprise and efficiency culture not found before 1989;
- (iii) the separation of operation of the companies from the regulation of those same companies.

REGULATION AND STANDARDS

The separation of operation from regulation has provided the greatest benefit for agriculture in all its forms.

Before the formation of the National Rivers Authority (NRA) in April 1989, I well remember how unfair it was that once each month our Board considered industrial and farming pollution incidents. It was unfair because I knew that very occasionally our own Wessex Water sewage treatment works caused pollution of water courses and yet we

never prosecuted ourselves. We did however prosecute farmers where there was clear neglect. That inequity has gone and Wessex Water is now treated by the NRA just as roughly or as fairly as the circumstances demand.

Self regulation is not as effective as independent regulation. Both the Director General (DG) of the Office of Water Services (OFWAT) and the NRA have done, on the whole, a good job. That is not to say that we do not or should not criticise them. Between our two main regulators the water companies try to reconcile the sometimes unreconcilable views of the NRA who want ever higher standards and seem not to consider enough the costs of achieving those standards; and the DG who supports customers, sometimes too much, although on the issue of costs in relation to benefits I believe the DG is being more sensible than the NRA. The recent complex paper from the Secretaries of State for the Environment and for Wales on this subject is a fair attempt to balance costs to customers against standards and impact on the environment, but I hope the interpretation of the paper by the NRA, OFWAT, and the industry, will be agreed, otherwise it could create even more uncertainty.

Compliance with the drinking water standards (not something with which the NRA is concerned except for water resource management) is the responsibility of the Drinking Water Inspectorate (DWI), which remains part of the Department of Environment (DOE) - Wessex Water's compliance is 99.7%. The cost of achieving 100% compliance (which is practically impossible anyway), is many millions of pounds and the benefit of achieving the last 0.3% compliance is questionable and certainly would not be noticed by our customers. On this standard and on some other standards we have to be realistic.

I have referred to the separation of regulation from operation, and to the ability of the industry to finance the investment required to put right 100 years of neglect whilst in the public sector at a price to customers which is affordable. And it is affordable for just about the best service in Europe. UK water and waste-water charges are half those of the old West Germany and two thirds of those in France. The UK privatised industry provides good value to houses, factories and farms.

FINANCE AND MANAGEMENT

What else has changed? A number of changes have been cultural - for instance until 1989 we referred to 'customers' as 'consumers'; we had little incentive to save on operating costs; and we had no ability to invest 'profitably', an important qualification, outside of our regulated activities by using our own core skills. The companies are adjusting to a commercial environment instead of being protected as monopoly

suppliers in the public sector. Gone are the days of spending capital whether necessary or not, just so that the next year's capital allowance was not imperilled by an underspend in the current year. This still happens in the public sector and it is but one of the questionable practices and inefficiencies of the public sector system.

As the companies passed resource management, pollution control, river management, land drainage and sea defences to the NRA in April 1989 so the connection between the water and waste-water companies and agriculture reduced. But there are still important links - not least because agriculture is a major user of our services and you, the farmers, are most important customers for the water industry. We charge farms on a measured basis including the notorious cattle troughs. If we know cattle troughs are not being used then we will not charge for them but you must tell us. As our industry moved into the private sector so your attitudes have changed. Some, very few, farmers now question necessary access to land to lay water supply or waste-water pipes where the period of notice required under the 1989 Water Act was lengthened from 21-28 days to 3 months for a new pipeline, and to 42 days for a replacement pipe. But even now, in most cases earlier entry is often gained through negotiation with the landowners and farmers. Also under the 1989 Act a statutory code of practice was introduced to govern the way pipelaying and other works are completed on farmland. The National Farmers' Union (NFU) and the Country Landowners' Association (CLA) had agreed an arrangement with Wessex Water before privatisation so for us there has been little change here. But again in a few cases there is a problem of compensation between the farming and land owning communities with the water companies. Before and after privatisation compensation for works by water companies on land was, and is, assessed on the statutory basis of actual loss incurred. Since privatisation, with the well publicised profits the water companies are making, some landowners and farmers believe they should receive greater and excessive compensation. This has been, should be, and always will be, resisted by the industry.

I have already recognised the good work of the NRA, OFWAT and the DWI, but in some respects I believe they are too expensive. For instance, the NRA still duplicates most of the required analysis of river and waste water which has to be done anyway by the water companies. The cost of having so many laboratories taking so many parallel samples is excessive and it is only in the water industry that the regulator does not accept that the operator performs the day-to-day analyses. Of course you have to trust the operator, and the NRA must, and do, have the right to random audit, check and police proper sampling and proper analysis of all samples. The saving from eliminating this and other duplication would be millions of pounds and would have some impact

on reducing the ever-increasing costs of the NRA. NRA costs for the Wessex region have increased from £940 thousand in 1989 to a forecast by NRA for 1993 of £1.820 million - an increase of 93.6%. For abstraction charges and discharge consents the increase is from £1.045 million in 1991/92 to a forecast for 1993/94 of £2.010 million, an increase of 92.3%.

WORKING WITH OFWAT

OFWAT is also expensive. In 1989/90, the OFWAT licence for Wessex Water cost the company an actual £156 thousand - for next year, 1993/94, the forecast is £366 thousand, an increase of 134.6%. OFWAT like Government is not sure about whether we should instal meters or not. And on the matter of metering, there are differences of opinion between the Customer Services Committees who represent OFWAT in each of the regions - the differences are about meters versus banding charges. The industry broadly agrees and accepts the sense of more metering but knows universal metering is a nonsense and thinks the council tax banding system provides a crude but acceptable judgement of house value, which should be used as a basis for charging domestic customers for water. As ever those who will gain keep quiet - those who will lose complain.

But OFWAT causes costs in other ways. The number of all customer contacts in my company has risen from 399 000 a year to 800 000 in 1993. Every one of these contacts costs money. Most of these contacts are by telephone and relate to changes of address, questioning of bills etc. But OFWAT's view, more often than not, is to ask the companies to support the customers with too little regard for costs. For instance we are encouraged by OFWAT to provide cash payment facilities for slow payers with instalments even on a per week or per fortnight basis. It is not just that the cost of cash payments by such instalments is expensive to manage and means the water company loses money in slow collection and poorer cash flow, but over two thirds of the instalment systems collapse within 2 months so they are an ineffective way of securing payment anyway. OFWAT does not concern itself enough with these problems and it does affect, and will increasingly affect, the level of charges not just to domestic customers but to you farmers as well as to industry. Problems of slow payment mean that the many who pay promptly pay a little extra for those who pay slowly.

RESEARCH AND DEVELOPMENT

What else has changed? Attitudes to research and development have changed. The water industry has challenged the role that research and

development can play in improving the performance of the business. Many research organisations have suggested that insufficient money has been deployed by the industry to research and development. We in Wessex Water, spend over £1 million a year carrying out targeted research. This research money is dispersed through support for the Foundation for Water Research, specific contracts with the Water Research Centre, and internationally with the American Waterworks Research Foundation. In the end, we can only make the business case to support research and development where it enhances customer and shareholder value.

SERVICES TO AGRICULTURE

What has changed for the farming community? Driven by the companies themselves as well as independent regulation you are receiving better quality water; you are receiving higher standards of service as our customers; and as I have explained, your charges have gone up less than they would have done had we not been privatised. The farmers and the agricultural industry are being consulted more than they were. The company I work for researches farmers specifically each year. You are key users of our services and, as a largely rural water and waste water company, Wessex Water pays careful attention to your views, greater attention than the company you have to use ever took before. Standards have improved because of stricter regulation which we must each applaud. Stricter regulation has affected you as well as us. It has encouraged higher quality and it is beneficial to our environment.

DEVELOPMENT OF RESOURCES AND TREATMENT OF SEWAGE

For water supply we are happy to be under increased pressure to consider and solve environmental issues and particularly issues from abstracting water. This means that we are looking for other more environmentally sound sources of water; we are encouraging river flow; and there is more pressure for us to reduce the leakage which inevitably is prevalent throughout the UK because so little money has been spent for many, many years replacing water pipes.

Incidentally the DOE paper - *'The Quality Framework'* which replies to the OFWAT paper *'Paying for Quality'* - is of much interest to farmers. On the matter of low flow rivers and abstraction it says:

'In one or two exceptional cases of withdrawing abstraction licences the cost to the water undertaker will be considerable. If the undertaker agrees, the cost falls to that undertaker. If the undertaker does not agree, the NRA must pay compensation and the cost will be reflected in abstraction charges to all abstractors in the area concerned.'

So farmers who abstract could be charged by the NRA for the consequences of changes to abstraction licences. We must be careful.

The treatment of sewage sludge has become more of an issue since privatisation. Releasing poorly treated sewage sludge to sea has stopped in many places. This means we have to treat more sewage sludge through primary, secondary and tertiary stages so that more has to go to land or be burned or, as is the case with Wessex Water, digested sewage sludge is heated and dehydrated and emerges as granules looking much like coffee, but not tasting quite like coffee. These biogranules have many properties such as slow release of nutrients. They are ideal for use as a soil conditioner. We are selling the product well.

Since 1989 the participation of the UK in the EC water and waste-water discussions has been strengthened both by Government and by the industry itself. This is a spin-off plus from privatisation because the companies do not now rely upon Government for funds and for interpretation of the rules. So we are independently interested in, for instance, the proper preparation of EC directives. We consider before the directive is drafted, the health and environmental solutions as well as the cost consequences.

With the farming community the waste-water industry needs to ensure that recycling properly treated and digested sewage sludge remains open to us. There was talk in the EC of classifying sewage sludge as 'hazardous waste' in which case an alternative means of disposal would have had to be found for the nutrient many of you put back to the land.

CONCLUSIONS

For our water industry we need continuing cooperation with the farming and landowning interests to ensure that we protect the place of water in our relatively unpolluted country. For instance source protection with the NRA is an interest we must all share. I know the farming community is aware of its responsibility for proper control of pesticides and herbicides which are not yet a problem but there is evidence that we must take great care. Your industry is responsible on the use of pesticides and responsible on all environmental issues. We thank you for that as we have common interests and it is essential that we have a continuing dialogue together to reconcile cost, benefit, time, and proper care for water and waste water in your countryside.