



BURGESS
SALMON

Environment and energy briefing from Burgess Salmon published
in the March 2011 issue of The In-House Lawyer:

Water regulation: key developments in 2011

THE 
IN-HOUSE
LAWYER

Water regulation: key developments in 2011

THIS YEAR WILL SEE SIGNIFICANT REFORMS TO the regulation of water in England and Wales with the publication of a Water White Paper, and a major reform of the economic water regulator Ofwat. The changes will affect not only water companies and their customers, but also have implications for wider utilities regulation and climate change adaptation.

The first part of this article considers how water law and regulation in England and Wales has developed in a way that takes relatively little account of the emerging low carbon agenda. It considers ways in which that may change as these two areas of law and regulation converge, and the opportunities for reform, presented by the Water White Paper and the Ofwat Review.

The second part of the article covers proposals to transfer private sewers in England and Wales to water and sewerage companies, and the implications of this for a range of property owners, users and developers.

WATER REGULATION AND THE LOW CARBON AGENDA

Background to water law

In its earliest origins, water law in England and Wales was very much a property issue. It determined who owned rights to water or could use it, for example for fisheries. It was also, in its earliest form, a public health issue. It concerned environmental issues in a general sense but, of course, had nothing to do with wider concerns about climate as these did not exist at the time. Water legislation from the 14th century was concerned with such things as the dumping of animal dung, garbage and entrails from slaughter houses in ditches, rivers and other waters, with bad effects on water quality and air quality. As one piece of legislation from 1388 puts it, 'many maladies and other intolerable diseases do daily happen' as a result.

Victorian water law also developed in response to public health disasters,

notably the London cholera outbreaks of 1832, 1848/49 and 1853/54. Only those with short memories about what London must have been like for much of the Victorian era should be sanctimonious about current conditions in Haiti. The 1858 'Great Stink' from the River Thames brought deliberations in Parliament to a halt, and finally resulted in the legislation allowing the construction of the first intercepting sewers under London.

In environmental terms, too, law has often evolved internationally in response to disasters and acute problems such as the fires in the Cuyahoga River in Ohio, which shocked a nation into passing clean water legislation.

Privatisation legislation

In England and Wales the Water Act 1989 established the basic structure that is in place today, with the National Rivers Authority (now the Environment Agency), Ofwat, and the water and sewerage undertakers, delivering for domestic supply and sewerage services. This privatisation legislation was consolidated in the form of the Water Industry Act (WIA) 1991, the Water Resources Act 1991 and the Land Drainage Act 1991. Despite establishing the principles of the control of pollution and flood defence, and setting up a powerful environmental regulator, there was little in the initial water privatisation legislation that specifically concerned sustainability, climate or the low carbon agenda.

Water legislation developed further with the Environment Act 1995, which set up the Environment Agency, and included in s4 a highly qualified (and curiously drafted) commitment to contributing to the achievement of sustainable development, as that was to be interpreted by ministers. The Water Industry Act 1999 was mainly about water charging and metering. The Water Act (WA) 2003 introduced major



'The government is now beginning to consider seriously how environmental concerns might be better addressed by regulatory reform in the water sector.'

William Wilson, barrister, Burges Salmon LLP
E-mail: william.wilson@burges-salmon.com

changes to regulation, water abstraction and impounding, and also on flood plans and water resources. Environmental protection was definitely part of this regulatory landscape, but there was still relatively little that clearly addressed the issues of climate or the low carbon agenda.

European water law

In the European context, water law has undergone dramatic revision in the past ten years. The Water Framework Directive 2000/60/EC was the most significant revision of European water legislation for 30 years, committing EC waters to achieving ‘good status’ by 2015, a deadline that is now not far away. The related Groundwater Directive 2006/118/EC and Priority Substances Directive 2008/105/EC developed this concept further, and the Marine Strategy Framework Directive 2008/56/EC took the basic structure of the Water Framework Directive and applied its principles to the marine environment. However, even these major European legislative instruments did not fully reflect the emerging international low carbon agenda.

Climate change and the low carbon agenda

Meanwhile, the international response to climate change resulted in the United Nations Framework Convention on Climate Change, the Kyoto Protocol, and the EU Emissions Trading Scheme. The UK has seen ambitious targets on low carbon and renewables being adopted. The EU Renewable Energy Directive 2009/28/EC commits the UK to a legal target of 15% of energy from renewables by 2020. The UK Renewable Energy Strategy 2009 has an aim of requiring 30% of electricity derived from renewables and promises to ‘drive delivery and clear away barriers’.

This agenda has resulted in a strong regulatory and legal response in the UK. The Climate Change Act 2008 led the way with statutory commitments to reduce emissions, the Committee on Climate Change was established, and the UK government set up the Department of Energy and Climate Change. The Flood and Water Management Act (FWMA) 2010 shows a response to the challenges of climate change adaptation. A Water White Paper and a Natural Environment White Paper are now expected this spring.

‘It is expected that the forthcoming Water White Paper will reflect some aspects of industry demands for the competing demands of regulators to be balanced, with Ofwat undergoing major regulatory reforms.’

All aspects of climate change adaptation as presently envisaged by Defra have a major water element to them. This can be seen in the scenarios for 2030 for cityscapes, coastal areas, countryside, future farms, domestic houses and major infrastructure released by Defra in September 2010.

Implications for water regulation

One important aspect of the reforms proposed will be the review of the functions of the water regulator Ofwat. As Caroline Spelman put it in her speech on 26 August 2010:

‘We need to make sure the regulator is in good shape to help the industry prepare for a changing climate and a growing population, at the same time as keeping bills affordable.’

The review is to be led by David Gray, former managing director of networks at Ofgem. If we consider how Ofgem has changed fundamentally in response to the low carbon agenda, it must be wondered whether similar upheavals are to be expected for Ofwat. Ofwat’s Climate Change Policy Statement ‘Preparing for the Future’ notes that:

‘The operational activities of the (water and sewerage) sectors contribute about 1% of the UK’s greenhouse gas emissions, which shows the scale of the challenge.’

The government is now beginning to consider seriously how environmental concerns might be better addressed by regulatory reform in the water sector. The Ofwat Review – A Call for Evidence (Defra, August 2010) indicated that the Review would consider:

- the government’s objectives for independent economic regulation of the water sector;

- the boundary of responsibility between Ofwat and ministers;
- Ofwat’s statutory duties – government guidance and its decision making;
- Ofwat’s contribution to sustainable development – its relations with other regulators and water companies, and its role with the Consumer Council for Water; and
- Ofwat’s value for money – its governance arrangements, its approach to minimising the burdens of its regulatory activity, and its scope for learning from good practice or other economic regulators.

One part of the challenge will be to try to integrate the agenda of the enforcement agencies and regulators for achieving environmental protection, and that with achieving the low carbon agenda set by the government.

For example, the Environment Agency has a clear mandate for seeking environmental protection, but in pursuing its own statutory responsibilities and those given to it under many EC Directives, it may be asked how it has ‘joined up’ the low carbon agenda and how far it is prepared, or able, to seek a balance between that and its statutory functions.

The Drinking Water Inspectorate set five strategic objectives for 2010-15, but there is no mention of working with other regulators or balancing investment and public health protection. It could be argued that the government and key regulators of the water industry do not yet do enough to work together and to balance the demands of the environmental, health and consumer protection with those of investment, controlling water bills and reducing emissions.

This argument was developed in an important report by Severn Trent Water, 'Changing Course', published in April 2010. This report noted that:

'Industry debt now stands at around £33bn in total... bills to customers had risen faster than inflation... carbon emissions are increasing due largely to higher, more energy-intensive treatment standards being adopted.'

The report argued for flexible implementation of the Water Framework Directive, developing competition through water trading, a more flexible approach to consents, an improved price setting process, companies driving innovation and prioritising national outcomes to deliver this strategy.

Further developments are expected in the future as this regulatory balance is considered in more detail by the government. For example, the government will consider whether there are any regulatory obstacles to the development of wind energy on water company land and how they can be removed.

There is much to do to remove regulatory obstacles to the development of hydropower, where 4,000 sites around the country have been identified but developments are frequently frustrated by regulatory obstacles. However, the Environment Agency is showing some signs of a new determination to address these problems.

The development of anaerobic digestion and co-digestion requires much more progress to achieve a regulatory framework that facilitates these technologies and enables the use of the resulting digestate. At the moment some investments are tangled up with arguments on the use of regulated assets, financing and the regulation of sludges from sources outside assets regulated under the Urban Wastewater Treatment Directive. Ofwat and the Office of Fair Trading have now announced a joint study into the organic waste market and how to enable it to realise its potential.

Water abstraction licence trading has been promised for several years, but is not encouraged by clear regulation and has yet to take full effect. Effective development of a market for water abstraction licences

would certainly be assisted by specific legislation.

The valuation of water as a separate resource has much further to go, although the Royal Institute of Chartered Surveyors (RICS) has made an important start with its information paper in January 2011. Burges Salmon participated in the steering group leading to the production of this paper, alongside representatives from the National Farmers Union, Chartered Institution of Water and Environmental Management, RICS, and others. The status of the RICS document as an information paper reflects the fact that this is the beginning of a process which may now develop into more formal guidance for surveyors. It tackles such questions as how water is valued as a resource, or for amenity, and what factors affect that valuation, such as water scarcity or water legislation and regulation, and begins to address the question of what methods surveyors should adopt or consider.

All of this, of course, takes place against a backdrop of very significant cuts in public expenditure and rising water bills at a time of austerity. Overall, it is expected that the forthcoming Water White Paper will reflect some aspects of industry demands for the competing demands of regulators to be balanced, with Ofwat undergoing major regulatory reform and the government determined to extend the reach of the low carbon agenda, but also addressing the real opportunities that now exist for bringing these two areas of regulation into closer alignment.

TRANSFER OF PRIVATE SEWERS TO WATER AND SEWERAGE COMPANIES IN ENGLAND AND WALES **Draft regulations and proposals**

The UK government in England and the Welsh Assembly Government for Wales are proposing to use powers under WIA 1991, as amended by WA 2003, to transfer private sewers and lateral drains connected to the public sewerage system into the ownership of the statutory water and sewerage companies. The transfer of private sewers and lateral drains will bring about the biggest change in responsibility for sewerage services since 1937 and it is estimated that it will affect 184,000 km of private sewers and 36,000 km of private lateral drains that connect to the

public system. If the proposals go ahead as planned, regulations to implement the change will enter into force on 1 April 2011, and the vesting of the private sewers and drains would take place on 1 October 2011. The proposals have wide implications for householders, builders and developers, drainage companies, Crown land, water and sewerage companies, and many others.

Private sewers and lateral drains are currently the responsibility of their owners, who are generally the owners and occupiers of the properties served. What has often happened is that householders have not been aware of their legal responsibilities for private sewers or lateral drains, or both, where these serve a property, even when it continues beyond the boundary of their property. This has led to problems of unanticipated expense and responsibility for repairs, with disputes over contributions between properties with shared services. The proposed response in this legislation would result in a wholesale transfer of responsibility to the water and sewerage companies.

The coalition government has decided, after consultation, that all sewers and lateral drains that drain to the public sewerage system will transfer into the ownership of the sewerage undertakers on a single date, 1 October 2011. This will include sewers and lateral drains draining both residential and commercial premises. At a later date, some 33,000 pumping stations necessary to link those sewers and lateral drains will be transferred to the ownership of the sewerage undertakers as well. There will be no criteria relating to the condition of the sewers for them to qualify for the transfer, so the sewerage undertakers will be taking on a very mixed collection of assets.

These proposals apply to surface water sewers only where they are drained directly to the public sewerage system, and not otherwise. They will not apply where the householder has their own arrangement, such as a cesspit.

Unusually, a decision has been taken to exempt Crown land from the transfer proposals, but with provision being made for private sewerage systems on Crown land to be volunteered for adoption at a later stage. The government has thereby sidestepped all the complications of access rights

over Crown land, which is actually used or managed by or on behalf of the Duchies or the Royal Family, and certain government departments where access rights could also be an issue, such as the Ministry of Defence and the HM Prison Service.

Following the transfer, householders and other property owners will no longer be responsible for drains and sewers that drain to the public sewerage system outside the curtilage of their property and any sewers within the curtilage. Householders and other property owners whose drains ultimately drain to the public sewerage system will retain responsibility for that part of the drain that serves only their property and is within the curtilage of their property. Pumping stations on a drain that serves only single premises and within the curtilage of the premises that it serves will also remain the responsibility of the property owner, at least until further proposals are brought forward.

These are very wide-ranging proposals, which will have a major effect on sewerage companies and the resources available to them to undertake responsibility for this whole new network. There may be employment issues such as the transfer of staff from local authorities formerly engaged on the maintenance of private sewers to whom the Transfer of Undertakings (Protection of Employment) Regulations

'The transfer of private sewers and lateral drains will bring about the biggest change in responsibility for sewerage services since 1937. It will affect 184,000 km of private sewers and 36,000 km of private lateral drains.'

will apply. It is understood that many of the sewerage companies will plan to contract out the work of maintenance of this new network, which also has major implications for procurement and contracting. Industries affected include the private drainage maintenance companies whose work has consisted in large part of the maintenance of private sewerage networks.

Sewer records for the networks being transferred are less than ideal, and it has been estimated that the cost of carrying out a full exercise to map and survey private sewers and drains would be around £1bn, so this has not been taken forward.

Significantly, powers under the FWMA 2010 will be used to require that mandatory adoption and mandatory building standards will be delivered, so that for new developments, new sewers will be required to be built to a standard that will allow their mandatory

adoption into the sewerage company's network.

CONCLUSION

This year should see important changes to the framework of water regulation with which the industry has become familiar. Water companies are being asked to take on important new responsibilities and will look to pass on their costs as far as possible. The affordability of water bills cannot be taken for granted at a time of economic hardship for many people and it will remain a prime concern for the economic regulator Ofwat. At the same time, however, there is increasing recognition that economic and environmental regulation, and an effective response to climate change, need to be brought together and addressed coherently, representing not just a problem, but also an opportunity.

*By William Wilson, barrister, Burges Salmon.
E-mail: william.wilson@burges-salmon.com.*