

PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT

Fourth Delegated Legislation Committee

DRAFT WATER INDUSTRY
(SPECIAL ADMINISTRATION) REGULATIONS 2024

DRAFT WATER INDUSTRY ACT 1991
(AMENDMENT) ORDER 2024

Tuesday 6 February 2024

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The Committee consisted of the following Members:

Chair: MARTIN VICKERS

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|---|---|
| † Coffey, Dr Thérèse (<i>Suffolk Coastal</i>) (Con) | † Longhi, Marco (<i>Dudley North</i>) (Con) |
| † Drummond, Mrs Flick (<i>Meon Valley</i>) (Con) | † Mahmood, Mr Khalid (<i>Birmingham, Perry Barr</i>) (Lab) |
| Duffield, Rosie (<i>Canterbury</i>) (Lab) | † Moore, Robbie (<i>Parliamentary Under-Secretary of State for Environment, Food and Rural Affairs</i>) (Con) |
| † Edwards, Ruth (<i>Rushcliffe</i>) (Con) | † Simmonds, David (<i>Ruislip, Northwood and Pinner</i>) (Con) |
| † Evennett, Sir David (<i>Bexleyheath and Crayford</i>) (Con) | † Slaughter, Andy (<i>Hammersmith</i>) (Lab) |
| † Everitt, Ben (<i>Milton Keynes North</i>) (Con) | † Western, Andrew (<i>Stretford and Urmston</i>) (Lab) |
| † Hardy, Emma (<i>Kingston upon Hull West and Hessle</i>) (Lab) | |
| † Harrison, Trudy (<i>Copeland</i>) (Con) | Chris Watson, <i>Committee Clerk</i> |
| † Hobhouse, Wera (<i>Bath</i>) (LD) | |
| † Lewis, Clive (<i>Norwich South</i>) (Lab) | |
| † Loder, Chris (<i>West Dorset</i>) (Con) | † attended the Committee |

Fourth Delegated Legislation Committee

Tuesday 6 February 2024

[MARTIN VICKERS *in the Chair*]

Draft Water Industry (Special Administration) Regulations 2024

2.30 pm

The Parliamentary Under-Secretary of State for Environment, Food and Rural Affairs (Robbie Moore): I beg to move,

That the Committee has considered the draft Water Industry (Special Administration) Regulations 2024.

The Chair: With this it will be convenient to consider the draft Water Industry Act 1991 (Amendment) Order 2024.

Robbie Moore: It is a pleasure to serve under your chairmanship, Mr Vickers. The two statutory instruments are part of a package that updates the water industry special administration regime legislation. The package is made up of two commencement orders and three statutory instruments. The first commencement order was made on 11 January, and the two affirmative statutory instruments that we are debating today were laid in draft on 15 January. The second commencement order and the negative resolution statutory instrument will follow shortly after the affirmatives are debated.

The purpose of the statutory instruments is to enable the Government to facilitate a more effective water industry special administration regime. They apply both to England and to Wales, and Welsh ministerial consent has been secured where necessary. The Government already have powers in the Water Industry Act 1991 to apply to the High Court for a special administration order. However, updates are required as the current legislative regime is outdated and largely modelled on the Insolvency Act 1986, which has since been modernised. The most notable legislative updates were the Enterprise Act 2002, the Small Business, Enterprise and Employment Act 2015 and the Insolvency (England and Wales) Rules 2016.

Updates to insolvency legislation are not automatically applied to the water industry special administration regime legislative framework. Instead, the Government must assess how to adapt the insolvency law changes to each industry-specific special administration regime, and legislation relating to those regimes is laid periodically. Recent examples are the Payment and Electronic Money Institution Insolvency (England and Wales) Rules 2021 and the Energy Act 2023. It is vital that the Government are prepared for a range of scenarios, particularly regarding the continued provision of public services, which is why an updated the water industry special administration regime is so important.

The two main grounds on which a water company can enter special administration are unchanged by this legislation. Those grounds are: first, insolvency, when

the company may be unable to pay its debts or its liabilities are greater than its assets; and secondly, performance, when the company has failed to carry out its statutory functions or licensed activities to such an extent that it is inappropriate for it to continue holding its appointment or licence. Under a special administration regime, customers' water and waste water services will continue to be provided.

The draft Water Industry Act 1991 (Amendment) Order 2024 implements hive-down provisions by amending schedule 2 to the 1991 Act. Schedule 2 makes provision about transfer schemes upon the termination of an appointment or the transfer of a licence for a water industry company, and is amended by the order to include provisions about transfer schemes in cases where there is a transfer by hive-down. The amendment is necessary to ensure that the hive-down provisions commenced last month by the Flood and Water Management Act 2010 (Commencement No. 10) Order 2024 are fully operable. Hive-down is a common commercial restructuring practice to ringfence value and attract potential buyers. The amendment allows the administrator to hive down the regulated business to a subsidiary in order to protect its business and facilitate a sale process that may be more attractive to a potential buyer.

The draft Water Industry (Special Administration) Regulations 2024 will disapply and modify general insolvency provisions as they apply in relation to water companies, including licensed infrastructure providers and special administration orders made in respect of water companies under the 1991 Act. The regulations make general modifications to the 1986 Act and other enactments about insolvency provisions, alongside specific modifications to schedule B1 to the 1986 Act. The amendments adapt parts 26 and 26A of the Companies Act 2006 via specific modifications for the purpose of the water industry special administration regime, and amend section 26 of the 1991 Act and schedule 1 to the Water Industry (Specified Infrastructure Projects) (English Undertakers) Regulations 2013.

In addition, the regulations will give the Government the power to lay a negative statutory instrument in the coming weeks that will revoke the Water Industry (Special Administration) Rules 2009, replacing them with updated special administration rules for water companies based on the Insolvency (England and Wales) Rules 2016. Thus, the statutory instruments will upgrade the water industry special administration regime legislation to ensure that if a water company is ever required to go into special administration, a modern, efficient water industry special administration can be implemented.

2.36 pm

Emma Hardy (Kingston upon Hull West and Hessle) (Lab): It is a pleasure to serve under your chairmanship, Mr Vickers.

It is essential that customers enjoy the continuous provision of water services irrespective of how the company that manages their water supply performs, so we support the changes, which will give a degree more security to people's water provision. Unfortunately, the challenges of the water sector are more fundamental than the changes would suggest. I fear that tinkering in this way shows that the Government are failing to grasp

the scale of the issues that face water provision in this country and the state of the crisis at which we have arrived.

We know that sewage is spilling into our waterways and beauty spots at a wholly unacceptable rate. Water companies discharged untreated sewers more than 399,864 times in 2022, which amounted to 1,091 times a day. I am sure the Minister agrees that the consequences of that mismanagement are awful: damage to precious habitats and natural life, reduced access to nature for some of those who face the sternest barriers, and a palpable sense of the sector failing to keep its house in order. He will be aware that we have set out robust solutions to the crisis, including criminal responsibility for water bosses, the introduction of large, immediate fines and the mandatory automatic monitoring of outlets to ensure that every spillage is recorded.

I have no doubt that many of our constituents will struggle with the profound sense of unfairness that runs through this debate. Despite consistently poor environmental performance and racking up huge debts, the water industry continues to pay large dividends and bonuses to shareholders and bosses. It should not be profitable for companies to pollute and fail to meet environmental legislation and for water and sewage infrastructure to be unfit for purpose. It should also not be acceptable for the water industry to pass the cost of legal compliance on to customers—they have already been funded to deliver it.

That legislative changes are necessary reflects the desperate and perilous situation that the sector has reached, with many companies on the precipice. Not only are water companies failing to deliver a clean and safe environment for water users, but many of them are struggling to function as effective businesses and keep their head above their mucky water. Regulators have raised serious concerns about the solvency of Thames Water, and the Government have even discussed temporary nationalisation measures. We also know that Thames Water, Southern Water and South East Water have been using up to 25% of customer bills to service the huge debts they have built up. It is not right that, again and again, customers are leveraged to cover the poor performance of those businesses.

The combination of the public health threat posed by the sewage scandal and the potential threat to taxpayers and customers posed by the instability of water companies demonstrates clearly that a radical rethink of how the water sector, regulators and Government work together is needed. The future of the sector must be based on sustainable finances and driven by a culture that values both customers and the environment. People must be kept safe and the best environmental outcomes must be achieved per pound spent.

As the Minister will be aware, a special administration order is intended to ensure that service is not interrupted when a water company becomes unviable. That means customers will continue to be provided with water services. Water companies also have a significant environmental duty, which may be interrupted if a company becomes insolvent. Do the new regulations also guarantee that any special administrator will continue to discharge a company's environmental obligations, including investment commitments under the water industry national environment programme, catchment plans and infrastructure upgrades?

Clarity around the criteria for the introduction of the special administrator is essential to all of this. Unless owners and shareholders believe that there is a genuine risk of them losing their licence, they have no real incentive to promote good corporate behaviour or environmental performance. Reading the 2019 Southern Water enforcement decision, one could be left wondering what it would possibly take for a licence to be removed. If multiple and deliberate breaches of environmental law and repeated deception of the regulator by the provision of falsified performance information is not enough, what fear can those in the sector really have? Ofwat must be much clearer on when owners lose the licence through special administration. Will the Minister commit to setting the bar for special administration in legislation?

As I have set out, we have grave concerns about the ability and motivation of water companies to meet environmental standards and take the crisis of sewage spilling seriously. The Water Industry Act 1991 states that a special administration order may be granted when a company is failing to fulfil its statutory functions. The regulations give the Government the opportunity to clarify that the imposition of a special administration can also be used as the ultimate sanction for water company pollution. That would send a powerful message to water companies and their bosses that the Government were intending to crack down on the issue and that environmental responsibility must be a central pillar of any business plan. Will the Minister confirm that the violation of environmental law constitutes a failure to fulfil a statutory duty under the terms of chapter 2 of the 1991 Act? Does the Minister commit to applying for a special administration order where a company shows consistent and flagrant breaches of its environmental duties?

The changes must go much further to solve the problems in the water sector. The Government must establish a clear, strategic regulatory framework that sets out the long-term vision for the water sector and how that will contribute towards achieving environmental targets and outcomes. More broadly, the Government must give stronger direction on the types of solutions needed and ensure that that is reflected in the regulatory framework to enable the greater uptake and use of catchment and nature-based solutions.

The Government must also recognise the role that years of cuts have played in creating the crisis. The sector is largely operating using a self-reporting model to evidence compliance with legislation. Self-reporting does not work. In 2022, only 48% of serious pollution incidents were self-reported, while many serious incidents were simply downgraded by water companies so as not to affect their environmental score. Ofwat and the Environment Agency must have the necessary resources to deliver a robust monitoring and enforcement regime.

The Opposition will support the changes, but I hope the Government understand the need for further consideration of the environmental responsibilities of water companies, in this legislation and in the future. I look forward to hearing the Minister's response.

The Chair: I remind Members to stick to the scope of the regulations. We are not here to debate the wider issues facing the water industry.

2.43 pm

Wera Hobhouse (Bath) (LD): I hear what you say, Mr Vickers, but we are debating matters that touch on the wider issues in the water sector. The Liberal Democrats will also not oppose the statutory instrument, but I wish to express our wider concerns about the water sector and how it is regulated.

Water company regulation should have three aims. First, we need to protect the water needs of future generations; secondly, we should ensure that the costs of investment in achieving environmental standards are shared fairly; and thirdly, we must ensure accountability and good customer service. Water companies need greater regulation to stop them getting into an administration or insolvency position in the first place.

Government attempts to tackle consistent poor environmental performance from the water industry have not worked. They have failed to address the root cause of the underfunding and under-resourcing of the regulators. There must be a clearer regulatory framework, duties and purposes for regulators, increased funding and greater direction on solutions to protect customers and the environment. New regulations should also guarantee that any special administrator will continue to discharge a company's environmental obligations, including investment commitments under the water industry national environment programme, catchment plans and infrastructure upgrades.

The proposals before us fail to talk sufficiently about the sewage crisis. There needs to be clarity on whether the Government will allow the special administrator to discharge environmental duties. Will the Minister confirm that the special administration order could be imposed as a sanction for sustained sewage pollution? We Liberal Democrats support a public benefit company model for water companies, so that they must consider explicitly economic and environmental policy objectives in particular. Water companies should also put a share of their profits into social tariffs. I have kept my remarks short. I support the statutory instruments, but whether they really tackle the wider crisis in the water sector is questionable.

2.45 pm

Robbie Moore: I am grateful to the hon. Members for Kingston upon Hull West and Hessle and for Bath for their important contributions, although I must say it was good that they eventually came back on to the script, so to speak. The statutory instruments will enable the Government to facilitate a more effective and efficient water industry special administration regime, ensuring that they are prepared in all eventualities to ensure uninterrupted provision for vital public services.

Let me briefly address some of the questions and points raised by the hon. Member for Kingston upon Hull West and Hessle. Before I get into the detail, I should say that I was pleased to hear her reference self-monitoring, because that was brought in by the Labour party when it was in power, in a water industry Act. We have increased the amount of monitoring that we are doing from 7% in 2010 to the 100% that we saw rolled out in 2023.

I will get back to the point. We are taking clear and decisive action to improve water quality. Our plan for water is delivering more investment, stronger regulation and tougher enforcement for our water system, and we

are clear that water companies must not profit from environmental damage. Through that plan, we will transform our management of water systems, deliver cleaner water for nature and people, and secure a plentiful water supply.

The hon. Member for Kingston upon Hull West and Hessle made reference to storm overflows, so let me clarify the amount of investment going into them. Our plan for water sets stringent targets on companies to improve storm overflows, which will drive the largest infrastructure programme in water company history, with £60 billion of capital investment over 25 years. We are clear that the volume of sewage being discharged into our waters is utterly unacceptable. However, storm overflows cannot just be switched off, as some have suggested; they are an automatic feature designed to stop sewage backing up into our properties.

We introduced the statutory instruments to update the existing regulations set in place under the 1991 Act so that, should we get to a scenario in which we need to utilise the special administration regime, we are in a position to do so. I will clarify that since privatisation the private water sector model has unlocked about £215 billion of investment; I raise that point because the hon. Member for Kingston upon Hull West and Hessle referenced nationalisation. Since privatisation that has been equivalent to about £6 billion being invested annually, which is almost double the pre-privatisation level.

Emma Hardy: Will the Minister give way?

Robbie Moore: I will carry on for now.

The hon. Lady quite rightly asked how customers may be impacted should a special administration regime be put in place. We will always act to protect customers as a priority, and any intervention that would put pressure on the public purse would be considered seriously and as a last resort. Dividends are an important part of the investor return and should provide an adequate return that reflects company performance. If a company did not pay its dividends, it would struggle to access the finances to fund investment, impacting on the service for future customers.

In each year since privatisation in 1989, investment has been greater than the dividends paid, but a sustained level of investment in the water industry will continue only if the shareholders of companies can expect a fair return. Companies must pay for new investment up front, so need to secure a large amount of funding to pay for that. To avoid customer bills increasing drastically to pay for that, companies may secure money by raising debt or equity, or through shares in the company or investors.

The hon. Lady also asked whether a company in special administration will have to adhere to the same standards as the rest of the sector. The answer simply is yes. The special administrator will manage the affairs, business and property of the company according to the same statutory obligations as any other water company.

To build on that, the hon. Lady also asked for clarity on whether a water company could be placed in special administration. In general, special administration can be applied for on insolvency grounds, when the company might be unable to pay its debts or when liabilities are greater than its assets—as I said in my opening

remarks—or in instances where water companies are in serious breach of their principal statutory duties or an enforcement order.

Emma Hardy: The Minister mentioned the failure to fulfil statutory duties, but will he confirm whether a violation of environmental law constitutes a failure to fulfil statutory duties?

Robbie Moore: Every water company is specifically regulated by the Environment Agency, as well as Ofwat. The Environment Agency will have powers if water companies are owned and operating under the regime they operate under now, or should they enter special administration.

On the hon. Lady's point about Ofwat, it is clear from Ofwat's performance report that there has been marked decline in performance over the past year. That has

been driven by company-specific factors, but also by the effects of extreme weather, including the unusually hot and dry summer we had. The Environment Agency and Ofwat have powers of enforcement, and those powers will not change under a special administration regime.

I have addressed the points that were made, so I commend the draft statutory instruments to the Committee.

Question put and agreed to.

**Draft Water industry Act 1991
(Amendment) Order 2024**

Resolved,

That the Committee has considered the draft Water Industry Act 1991 (Amendment) Order 2024.—(*Robbie Moore.*)

2.53 pm

Committee rose.

