

THE INDEPENDENT WATER COMMISSION'S INTERIM FINDINGS: PRESSURE BUILDS FOR REFORM, BUT A SEA-CHANGE LOOKS UNLIKELY

Following a Call for Evidence that elicited over 50,000 responses, the UK's Independent Water Commission (Commission) has published its [interim findings](#), highlighting five areas it believes to be critical to reforming the UK water industry. The report considers possible reforms to strategic direction and network planning; the current legislative framework; the role of the regulator; the structure and governance of water companies; and the management of infrastructure and asset health. In this briefing, we review the Commission's preliminary recommendations and consider the implications for the industry and investors.

Background

Established in October 2024 and led by Sir Jon Cunliffe, the Commission has been conducting a “root and branch review” of the water industry in England and Wales in an effort to identify potential solutions that will restore confidence in the regulatory framework governing the sector, whilst making it more resilient and attractive to investors (as discussed in our previous article [here](#)). The Commission's initial report - to be followed by final recommendations later in the summer - outlines its preliminary conclusions, intended “direction of travel”, and the scale and nature of the change necessary.

The interim findings come six months after Ofwat published its Final Determinations under the 2024 Price Review (PR24), providing the sector with a £104 billion funding package for the five years to 2030, and setting the amount water companies can charge customers (see our briefing [here](#) for more detail). Whilst the Commission's [Terms of Reference](#) make it clear that the Commission will not make recommendations that impact the PR24 process, its recommendations are likely to have implications for both the asset base and the approach to future reviews. The Commission's report also follows the enactment of the Water Industry (Special Measures) Act 2025 earlier this year, which amended the special administration regime for water companies, and introduced new governance and remuneration measures.

Preliminary findings

1. Strategic direction and planning

The Commission found that, whilst the UK and Welsh governments have sought to provide strategic direction on the growing environmental, social and financial demands of the sector, these can be narrowly expressed, and there has generally been a lack of prioritisation and guidance on how to strike the balance between competing targets. In England and Wales, the Strategic Policy Statements (SPS) are set every five years by the respective governments and are directed solely towards Ofwat. The Commission considers that this means that targets are relatively short-term, do not apply to other water regulators and are not considered in guidance for sectors beyond water. The Commission also observed a different approach to stakeholder involvement in England and in Wales; a more collaborative approach is taken in Wales, where the Price Review Forum brings together government,

water companies, regulators and customer advocates to inform water company business plans and delivery strategies.

The Commission recommends clearer, long-term direction on what the UK government wants from the water system and suggests that “this requires government to set out its priorities and timescales for the system much more clearly than it does at present”. The Commission is considering how to hold actors to account for the delivery of long-term national strategies, and how to ensure progress is measured. For example, these strategies might inform milestones for every price review and apply to all water regulators rather than to the economic regulator alone. These could replace the current SPS to Ofwat and provide guiding principles to support systems and industry planning processes leading into the price review

periods. The Commission will provide further reflections on this in its final report.

In their submissions to the Commission's Call for Evidence, both [Ofwat](#) and industry body [Water UK](#) agreed on the need for a more consistent approach to planning and long-term strategic investment in the sector. Both called for this function to be delivered through a new coordinating unit with clear ownership and oversight. Suggesting that the water sector builds on learning from the energy sector, both cite the National Energy System Operator as a potential model, with Ofwat observing that this kind of "guiding mind" would help it to better plan development and respond more quickly to critical challenges, such as reducing discharges from storm overflows and enabling major new water resources. More specifically, Ofwat proposed the creation of a Strategic Water and Wastewater Planning Unit - a "new holistic, strategic planning function for government and regulators" to facilitate effective collaboration and decision making on long-term strategic investment plans.

Finally, the Commission also found that there is considerable scope to improve and rationalise the process for the planning and funding of water industry investment. In its view, there should be "some degree of assurance on the funding of what is likely to be needed in the following price review period", not just in the immediate price review period.

2. Legislative framework

The Commission found that the legislative framework governing water lacks clarity, and has led to confusion among water companies, investors and regulators. Having evolved in a piecemeal manner, there are currently around 80 pieces of legislation covering the sector. In its submission, Water UK observed that "new environmental legislation has been incrementally added to over time with no common purpose or clear end-goal in mind", giving rise to "inconsistencies and incoherence of the body of law as a whole".

The Commission sees a strong case for review, rationalisation and consolidation of existing legislation, to simplify the framework, create greater flexibility for regulators, update standards, and broaden objectives. Noting that this is a major exercise and beyond the Commission's scope, the Commission undertook to consider priority areas for review in its final report. However, it noted in its preliminary findings that changes to the Water Environment (Water Framework Directive) (England and Wales) Regulations 2017 would be needed given there is no statutory deadline for environmental improvements relating to good ecological or good chemical status after 2027, and observed that the growth of recreational water use means there is a strong case to include public health alongside the current scope of the regulation. It also noted that the Urban Wastewater Treatment (England and Wales) Regulations 1994 should be a priority for

review to ensure that public health continues to be protected from existing and emerging contaminants.

The Commission also undertook to consider two issues further in its final report: first, whether "proportionate provision for constrained discretion" of regulators could give greater focus on outcomes; and second, whether the concept of "extended producer responsibility" could apply to the water sector to better support the management of pollutants upstream. Whilst the case for legislative review is clear, the industry may be keen to avoid an open-ended, lengthy review process, which might result in further uncertainty for the sector.

3. The role of the regulator

The Commission noted the range of public bodies involved in regulating the sector: Ofwat, as economic regulator; the Environment Agency in England and Natural Resources Wales in Wales, as environmental regulators; the Drinking Water Inspectorate, as drinking water regulator; and the Consumer Council for Water, a non-departmental public body representing consumer interests.

The Commission heard evidence that public trust in the current regulatory framework as a whole has been "severely eroded", leading to "falling confidence in the adequacy of the planning and regulatory framework for the sector, and in its ability to hold companies to account to comply with their obligations". Stakeholders noted that Ofwat price reviews had become complex and over-reliant on econometric based modelling, focused on examining "comparability" - benchmarking companies against one another to assess efficiency and justify customer bills - when networks may not be directly comparable (e.g. due to the age of infrastructure). It also heard that the ability of the environmental regulators to enforce compliance with standards has been compromised by capacity, capability and cultural challenges. The Commission acknowledged high levels of satisfaction with the Drinking Water Inspectorate, which was seen as highly effective.

In relation to economic regulation, the Commission reached the view that, given material differences between water companies, the benchmarking model cannot be relied upon alone to accurately assess the reasonableness of an individual company's costs, efficiency, and overall performance. It will also comment in its final report on a number of detailed issues such as how base, enhancement and WACC allowances are set. The Commission also questioned the constructiveness of fines for underperformance at a time when the industry needs to attract significant investment. The Commission believes a fundamental strengthening and rebalancing of Ofwat's regulatory approach is needed to redress these limitations and recommends the introduction of a "supervisory approach", (as found in sectors such as financial services) alongside Ofwat's econometric benchmarking

function. A supervisory approach would help regulation to become more specific to the relevant water company. By providing a deeper understanding of the company's circumstances and finances, it will facilitate intervention before issues arise and enable incentives and penalties to be set realistically to improve the company's performance over time. Ofwat itself has welcomed the Commission's recommendation to move to a supervisory approach. The Commission will however be considering whether Ofwat requires stronger and/or additional "tools to direct companies and intervene in changes of ownership". It remains to be seen the extent to which the Commission will draw on the Financial Conduct Authority for inspiration as a model in this regard.

In the context of environmental regulation, the Commission reached the view that a stable and consistent approach to funding will be essential to provide certainty on regulatory functions, and restore public trust in the level and endurance of regulatory oversight. It will also be necessary for a capable regulator to be equipped with the appropriate technology and skills to enable innovative solutions that deliver the greatest environmental benefits and ensure that the effective delivery of its functions will endure. The Commission also noted the need for proportionate action where companies failed to comply with requirements and welcomed the introduction of civil penalties under the Water Industry (Special Measures) Act 2025 to enable swifter enforcement. The Commission will consider whether any further interventions should be made to support swifter enforcement as part of its final report.

The report also identifies a need for major reform in relation to the structure of the regulatory framework. The Commission found that the multiple water regulators have overlapping remits for oversight and enforcement. This impedes the ability of the regulatory system to form a consistent view of a firm's overall performance and challenges, and take cohesive enforcement action. It is considering options for significant streamlining and alignment of the regulators to address this issue, and will make recommendations on this in its final report.

4. Company structures, ownership, governance and management

The Commission examined the ownership, governance and management of water companies. It noted a broad range of investors in both publicly listed and private water companies, including international infrastructure companies, private equity funds, and institutional investors.

In its preliminary conclusions, the Commission noted that it is still evaluating whether there is a link between ownership models and performance. Its current view is that "listed models may score more highly on public trust, due perhaps to greater

transparency, and that, in the past, private equity models have led to higher levels of gearing". This issue will be examined further in the final report. We note that consideration of public ownership models was outside of the scope of the Commission's Terms of Reference.

In relation to investor appetite, however, the Commission is clear in its view that the water industry is likely to be best served by investors that take a long-term, low return, low risk investment approach. It considers that this will require restoring investor confidence in the predictability and stability of the regulatory system, and a move to a more positive and balanced presentation of the water industry given the challenges it faces, such as the increase in standards, climate change and population growth. The Commission is also exploring regulatory mechanisms to narrow the variability of returns in order to attract lower risk/return investors, although it recognises that such changes could reduce incentives for improvement.

In relation to corporate governance and accountability, the Commission noted major reforms with water companies making changes to their articles of association to incorporate the public interest as a purpose and it is considering whether this could be strengthened by including a requirement in licence conditions, or via board leadership, transparency and governance principles. It did not consider that a "public interest" board representative was justified in the context of current governance arrangements. However, the Commission is examining whether senior managers should be held more accountable and will include views in its final report on whether some, or all, of the Senior Managers Regime applicable in the financial sector could be introduced for water companies. The final report will also consider options to improve financial supervision to support companies' resilience.

5. Infrastructure and asset health

Operating in an environment of climate shocks, rising demand and ageing infrastructure, the Commission and a number of industry stakeholders agree that there is insufficient understanding of the condition and overall resilience of the industry's asset base (e.g. its pipes, treatment plants and pumping stations). Consequently, a clear view of the condition, and past renewal and maintenance, of water assets cannot be formed. The Commission noted that, due to a lack of prescription in the associated legislation and regulatory framework, assets have not been fully mapped and there is variation between companies in how they assess asset health, ranging from "map as you go" during routine maintenance to reactive mapping only when failures occur. Similarly, the roadmap published by Ofwat for improving understanding of asset health is not mandatory and the level of engagement with it by water companies is unclear.

This uncertainty and inconsistency across the sector has made planning for supply chains, logistics, and funding for long-term asset replacement and renewal challenging, and the Commission notes that “funding for renewal and capital maintenance by Ofwat continues to be based primarily on previous capital maintenance and incidence of asset failure” rather than “a prognostic, longer-term assessment that takes into account future stress on assets such as from climate change and population growth”. During the consultation, the majority of water companies reported that, as a result, Ofwat’s funding methodology has failed to fund sufficiently the longer-term maintenance and renewal of their assets.

In relation to supply chains in particular, the Commission heard that limited understanding of supply chain constraints has resulted in deficient sequencing, coordination of supply chain capacity and, therefore, delayed delivery of infrastructure. Numerous stakeholders have expressed concerns that the supply chain does not have the capacity to assume the increased investment obligation set out in PR24.

To address this, the Commission’s current view is that there is a strong case for the implementation of a comprehensive infrastructure resilience framework across all water companies in England and Wales (which was also a recommendation of the National Infrastructure Commission). This would include the establishment of resilience standards and requirements for companies to assess and report on asset health, at set intervals, to regulators (such assessments would also inform company plans and funding in price reviews). Resilience standards would be outcome-focused so that companies do not just fix assets when they fail, but plan for the long-term condition and resilience of these critical assets, also factoring in asset redundancy or back-up into the assessment. This approach would be combined with a more supervisory role of the regulator.

Water and sewerage companies are reportedly broadly supportive of these proposals, noting that resilience standards are useful in classifying assets, managing future risks (e.g. in the context of extreme weather), and forward-planning for investment. In particular, Water UK has called for outcome-based resilience standards to be introduced by the end of 2026 and to be put on a statutory footing. The Commission intends to return to these issues in its final report.

Next steps

Whilst the Commission’s interim report provides a helpful insight into the direction of travel, there is more work to be done ahead of publication of the final report this summer. As well as the further examination of a number of issues covered in the interim report, the Commission will also consider gaps in environmental regulatory oversight and options for improving approaches to environmental performance in its final report. Importantly for the sector, the final report will also provide more consideration of what a supervisory approach should involve and deliver, conclusions regarding the price review process, as well as consideration of the Special Administration regime and customer bills and protections. It will then be for the Secretary of State to respond to the Commission’s report and proceed with implementation of the recommendations, as appropriate. Given the tone of the Commission’s interim report, regulatory reform should be expected. The time required to implement reforms will depend on the nature and extent of the Commission’s recommendations that are taken forwards. Where primary legislation is required, it may potentially take up to two years to enter into force.

The Commission is clearly navigating a delicate policy balancing act of reconciling the objective to attract private investors in the sector whilst also protecting the interests of customers and members of the public. The preliminary recommendations do appear to recognise the importance of the former objective in achieving an effective and resilient water industry, which can, in turn, underpin public interest objectives. Striking the right balance in the Commission’s final report will be key to maintaining confidence in the UK’s water sector.

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