



The Scottish Parliament
Pàrlamaid na h-Alba

INFRASTRUCTURE AND CAPITAL INVESTMENT COMMITTEE

AGENDA

12th Meeting, 2014 (Session 4)

Wednesday 30 April 2014

The Committee will meet at 10.00 am in the Mary Fairfax Somerville Room (CR2).

1. **Decision on taking business in private:** The Committee will decide whether to take item 4 in private.
2. **Scottish Water – Strategic Review of Charges 2015-21** The Committee will take evidence from—

Belinda Oldfield, Regulation General Manager, and Alan Scott, Water Service Strategy General Manager, Scottish Water;

and then from—

Peter Peacock, Chair, Customer Forum for Water;

and then from—

Professor Gordon Hughes, Chairman, and Ian Tait, Director of Investment, Water Industry Commission for Scotland.

3. **Subordinate legislation:** The Committee will consider the following negative instruments—

The Road Traffic (Permitted Parking Area and Special Parking Area) (Argyll and Bute Council) Designation Order 2014 (SSI 2014/84)

The Parking Attendants (Wearing of Uniforms) (Argyll and Bute Council Parking Area) Regulations 2014 (SSI 2014/85)

The Road Traffic (Parking Adjudicators) (Argyll and Bute Council) Regulations 2014 (SSI 2014/86)

4. **Scottish Water – Strategic Review of Charges 2015-21** The Committee will consider evidence heard on the next Scottish Water - Strategic Review of Charges 2015-21.

Steve Farrell
Clerk to the Infrastructure and Capital Investment Committee
Room T3.40
The Scottish Parliament
Edinburgh
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The papers for this meeting are as follows—

Agenda Item 2

Background Note ICI/S4/14/12/1

PRIVATE PAPER ICI/S4/14/12/2 (P)

[Scottish Water Draft Business Plan 2015-21](#)

[Water Industry Commission for Scotland - The Strategic Review of Charges 2015-21 Draft Determination](#)

Agenda Item 3

Background note ICI/S4/14/12/3

[The Road Traffic \(Permitted Parking Area and Special Parking Area\) \(Argyll and Bute Council\) Designation Order 2014 \(SSI 2014/84\)](#)

[The Parking Attendants \(Wearing of Uniforms\) \(Argyll and Bute Council Parking Area\) Regulations 2014 \(SSI 2014/85\)](#)

[The Road Traffic \(Parking Adjudicators\) \(Argyll and Bute Council\) Regulations 2014 \(SSI 2014/86\)](#)

Infrastructure and Capital Investment Committee

12th Meeting, 2014 (Session 4)

Wednesday 30 April 2014

Scottish Water – Strategic Review of Charges 2015-21

Introduction

1. The Water Industry Commission for Scotland (WICS) is currently leading a review of Scottish Water charges for water and sewerage services, which are set for periods lasting a number of years, known as regulatory control periods. The next regulatory control period will run from 2015 to 2021.

2. In October 2013, Scottish Water published its draft business plan for 2015-21, and sets out a vision for the improvement of services during this period. See following link:

<http://www.scottishwater.co.uk/about-us/publications/strategic-projections/draft-business-plan-2015-2021>

3. The Infrastructure and Capital Investment (ICI) Committee took evidence from Scottish Water on its Strategic Review of Charges 2015 at its meeting on 20 November 2013. See following link for the Official Report:

<http://www.scottish.parliament.uk/parliamentarybusiness/28862.aspx?r=9044&mode=pdf>

4. In March 2014 2014, the Customer Forum for Water in Scotland published its Draft Determination, with consultation closing on 12 June 2014. The draft determination proposes the following price caps for Scottish Water services. Please see the following link:

http://www.watercommission.co.uk/UserFiles/Documents/Draft_determination_2015-21.pdf

5. The Customer forum has been involved in discussions with key stakeholders throughout the strategic review of charges. This involvement culminated with the Chair of the Customer Forum signing a minute of agreement with Scottish Water dated 30 January 2014. The Minute of Agreement is included in this paper at **Annexe A** (the signed version is also reproduced at Pg. 78 of the Draft Determination).

Next Steps

6. The Committee will take evidence from representatives of Scottish Water, the Customer Forum, and the Water Industry Commission for Scotland on 30 April 2014.

7. Members will consider the evidence heard, and consider whether to make representations to Cabinet Secretary for Infrastructure, Investment and Cities.

Kelly Forbes
Assistant Clerk
25 April 2014

ANNEXE A

SCOTTISH WATER AND THE CUSTOMER FORUM

Minute of agreed modifications to Scottish Water's draft business plan for 2015-21

INTRODUCTION

1. The formal document setting out the procedures for the setting of charges for water in Scotland – "Strategic Review of Charges 2015-21: Innovation and Choice" issued by the Water Industry Commission for Scotland, had at its heart an invitation to Scottish Water and the Customer Forum for water to agree the business plan the Water Industry Commission would consider in determining charges for 2015-21. This Minute of Agreement represents the agreement reached and as sought in the formal procedures for the Strategic Review of Charges 2015-21.
2. This minute of agreement should be read in the context of Scottish Water's draft business plan for the 2015-21 period. Scottish Water's draft business plan is agreed by the Customer Forum unless, and to the extent, modified by this minute of agreement. For completeness, by 28 February 2014, Scottish Water will update its draft business plan for all the matters set out in this minute of agreement to create "the agreed business plan".
3. Where the term 'Customer Forum' is used throughout this document and referring to matters beyond the current process for the price review and current powers to agree, this reference is not intended to imply that a decision has been taken on the future of the Customer Forum and any future role it may have. This is simply a short-hand for consistency and identifies areas where customer input to discussions and arrangements will be appropriate and important, whatever the particular form of that customer body.

DELIVERING FOR CUSTOMERS

Overall Performance assessment (OPA)

4. Scottish Water and the Customer Forum aspire for Scottish Water's performance to be 'best in class', and this is reflected in the agreed approach towards OPA where a three tier approach is agreed, based around the following thresholds:

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21
Best in class performance threshold	400	400	400	400	400	400
Leading companies performance threshold	380	381	382	383	384	385

- Scottish Water aspires to be best-in-class, achieving an equivalent¹ OPA score at, or above, 400. It is recognised by the Customer Forum that this is unlikely to happen consistently based on the experience from England and Wales.
 - Scottish Water plans to be leading, achieving an OPA score at, or above, the leading companies' threshold in every year. It is acknowledged by the Customer Forum that, occasionally, this may not be achieved because of significant events.
 - In recognition of this occasional risk to delivering a leading level of customer service, Scottish Water commits to achieving an average OPA score across the 2015-21 period that exceeds the leading companies' performance threshold (i.e.: an average score across 2015-21 that exceeds 382.5).
5. The following detailed points with regard to the OPA have been agreed in addition to those identified for the drinking water quality measure and the waste water treatment compliance measure in the draft business plan:
- Exclusions: the current exclusions that apply to OPA are to continue during 2015-21. Scottish Water to identify and report the exclusions to the OPA calculation to an annual performance review meeting with the Customer Forum.
 - Response to formal complaints: the period for a substantive response to formal complaints to be reduced from 10 days to 5 days.
 - Independent verification of the OPA: Scottish Water to continue to undertake an annual independent audit and verification of its OPA score

Customer Experience Measure (CEM)

6. A separate Customer Experience Measure (CEM) will be introduced for each of household and business customers. The non-household CEM is to include Licensed Providers, businesses and developers. Scottish Water will work with the Customer Forum on the development of the measures for agreement and implementation by March 2015.
7. The following detailed points with regard to the introduction of a Household Customer Experience Measure (CEM) have been agreed:
- Perception survey: the perception survey is to constitute 30% of the qualitative element of the household CEM.
 - The qualitative survey elements of CEM to be conducted independently of Scottish Water.
 - Timetable: Scottish Water to operate the household CEM on a shadow basis from April 2014 with a view to establishing a baseline level of performance during 2014/15 and a CEM improvement plan by March 2015.
 - Affected non-contact customers: A commitment from Scottish Water to work with the Customer Forum in developing for implementation by March 2015 a separate component (weighting to be agreed) element of household CEM covering the customer experience of Scottish Water's response to planned and unplanned

¹ The equivalent score reflects that, given the revised scoring being introduced for drinking water quality and Scottish Water improvement plans for SOSI, Scottish Water's equivalent score will be between 3 and 4 points below that recorded in England & Wales. Only one company has achieved an equivalent score above 400 points.

Scottish Water service events from those customers who are likely to have been affected but have chosen not to contact Scottish Water.

- SPSO complaints upheld: These are given a weighting of 1000 times 'unwanted' contacts within the CEM. Scottish Water will also report on escalated and SPSO complaint levels in the annual performance review meeting (see note 17).
 - 'Calls Abandoned' and 'All Lines Busy': to be included within the quantitative element of CEM.
 - Independent verification of the CEM: Scottish Water to seek independent audit and verification of its CEM score.
8. It is agreed that the disaggregated elements of the household CEM can and will be benchmarked with the Service Incentive Mechanism (SIM) in England and Wales as it is constituted currently. It is noted that SIM is currently under review and any changes to SIM which would affect comparability with CEM will be discussed with the Customer Forum to assess any effect on the understanding of CEM this might have.
9. Scottish Water and the Customer Forum will keep the relative weightings of the components of the CEM under review.
10. Scottish Water and the Customer Forum recognise that further steps could be taken to achieve a better understanding of business customers' perceptions of the service outcomes they experience and agree that they will, together, seek to conclude discussions with all relevant parties aimed at developing a non-household CEM by March 2015 to capture:
- Licensed Providers' views as a customer of Scottish Water.
 - Scottish Water component of business users' experience.
 - Scottish Water service to the Developer community.
11. Scottish Water are taking steps to develop improved working relations with business customers where that is relevant to matters specifically under the direct control of Scottish Water and which may facilitate business growth. Scottish Water will engage with the Customer Forum in reviewing progress on this strand of work.

High Esteem Test (UKCSI)

12. Scottish Water and the Customer Forum agree that benchmarking Scottish Water's customer satisfaction against other utilities and companies in other sectors would be of value. Scottish Water and the Customer Forum have agreed that Scottish Water will bring forward its proposals for building a robust benchmark tracking survey to the Customer Forum for agreement and implementation by March 2015.

Additional Service Activity Measures

13. Scottish Water will work with the Customer Forum to agree separate service activity measures in the following areas for implementation from April 2015.

- external flooding due to hydraulic overloading.
- the annual number of properties externally flooded.
- visible leakage.
- carbon footprint reduction.
- extreme weather events excluded from OPA.
- SPSO escalated complaints and upheld complaints.

Customer engagement:

14. Scottish Water and the Customer Forum are committed to working together throughout the 2015-21 period on deepening customer engagement. Each year, as appropriate, a wider programme of research into customers with particular service requirements will be conducted. This work may encompass, for example, vulnerable customers, customers within particular geographic areas, customers with particular service improvement needs, research to inform future customer driven priorities and long term issues such as lead pipe replacement, rural sewerage provision, and private water supplies.

Customer education:

15. Scottish Water and the Customer Forum agree that there is more that can be done to get close to customers and to help customers co-produce outcomes for themselves and the water and waste water system as a whole, through more comprehensive customer education, care and support arrangements.
16. Building on work done to improve customer education on blockages to sewers caused by customer behaviours, Scottish Water will engage with the Customer Forum during 2014/15 with a view to developing potential approaches to education, care and support programmes, and the subsequent trialling and evaluation of such programmes.

Annual review meeting

17. The Customer Forum and Scottish Water agree that there will be an annual meeting between Scottish Water and the Customer Forum specifically for the purpose of looking at levels of service and performance as represented by: OPA; the CEM; the High Esteem Test (UKCSI); Wholesale KPIs - and the component parts of each; and other agreed service activity measures under development. Following any such meeting the Customer Forum undertakes to write to Scottish Water identifying any issues it considers relevant to the question of service level and wider performance monitoring, and Scottish Water agrees to consider the issues raised.

CUSTOMER PRICES

18. The financial modifications and mechanisms set out in this minute of agreement are intended to achieve the following prices for customers.

Household customers

19. There will be an overall household price cap of CPI-1.75% across the 2015-21 period – this is the overall price control that is consistent with achieving annual nominal price increases of 1.6% in 2015-21 assuming that actual CPI adheres to the assumptions given in note 22 below. This mechanism protects both customers and Scottish Water from actual inflation differing from that assumed in this note of modifications. The overall household price cap will be operated in accordance with the following three principles:

- a. A fixed nominal price increase of 1.6% pa in each of 2015/16, 2016/17, and 2017/18 for household customers only, albeit that any over/under recovery of revenue in these three years may be adjusted for in 2018-21 under the price cap arrangements. This follows a limiting of the household price increase in 2014/15 to 1.6% in light of the pricing intention for 2015-18.
- b. An indicative nominal price increase of 1.6% pa in each of 2018/19, 2019/20 and 2020/21 for household customers only, that will be subject to assessment at the time based on out-turn and forecast CPI.
- c. If the application of the price cap methodology would require household prices in 2018-21 to exceed the indicative price increase of 1.6% pa then, prior to the application of such an increase, Scottish Water, the Customer Forum, and the Commission will consider whether any, or all, of the increase above 1.6% can be off-set by overall favourable external factors, re-phasing of IR18 allowances to after March 2021, or by returning any early sustainable out-performance to customers.

20. Affordability: Scottish Water agree to commence work with the Scottish Government and other stakeholders, including the Customer Forum, by April 2015 to investigate if more can be done to support vulnerable customers within the principles of charges laid down by Scottish Ministers.

Wholesale customers

21. There will be a target annual wholesale price change in 2015-21 of CPI-0.3%, but this would be subject to annual adjustment to reflect actual growth and CPI so that Scottish Water's revenue complies with the annual wholesale revenue cap as adjusted for out-turn CPI.

OTHER FINANCIAL CHANGES

Inflation assumptions

22. The inflation assumption forecasts are modified as follows:

- CPI for prices will be reduced to 1.9% pa in line with the Bank of England's inflation forecast of November 2013.²
- The annual differential between CPI and RPI will be reduced to 0.75%.
- In light of the falling forecasts for RPI, the RPI cost assumptions for 2013/14 and 2014/15 shall be reduced to 2.8% and 2.65% respectively.

This is set out, for clarity, in the table below.

	2013/14	2014/15	Each year from 2015/16 to 2020/21
Modified CPI for prices	-	-	1.9%
Draft business plan CPI for prices	-	-	2.0%
Modified RPI for costs	2.8%	2.65%	CPI+0.75% (i.e.: 2.65%)
Draft business plan RPI for costs	3.0%	2.9%	CPI+0.9% (i.e.: 2.9%)

Household growth

23. The Commission set out in note 22 that household growth may exceed that set out in our draft business plan. In response to this, the assumption on household growth has been increased from an average of 0.67% pa in the draft business plan to an average of 0.74% pa. This revised average growth assumption is based on an assumed rising annual growth from 0.6% in 2015/16 to 0.9% in 2020/21. The assumed financial consequences arising from this additional growth (in out-turn revenues and costs) are:

	£m
Additional customer revenue	11
Additional infrastructure charge income	7
Additional investment in strategic infrastructure	(4)
Additional reasonable cost contributions	(11)
Additional investment in strategic capacity	(13)
Net cash cost in 2015-21	(10)

24. To the extent that growth exceeds the assumptions set out in our draft business plan, as amended above, the further net additional costs (investment in excess of additional revenue) would require further re-phasing of IR18 investment allowances to after March 2021, beyond those set out in note 27 below.

²www.bankofengland.co.uk/publications/pages/inflationreport/2013

Investment levels and priorities

Updates to draft business plan forecasts

25. Cash provision is being made for the £61million SR10 investment risk provision that was highlighted in the table commentary accompanying the draft business plan but omitted from the accompanying financial model projections. This cash provision is essential in the context of the Commission's guidance to lower significantly the closing cash balance at March 2021.
26. Recognition, but no overall net cash adjustment, is being made for two compensating understatements in the draft business plan that were identified by the Commission through their business plan review process, which are:
- a cost increase of £21million to correct for an understatement in relation to reasonable cost contributions (RCC).
 - infrastructure charge income is increased to reflect an under-statement by £3-4m a year. This will provide additional income that off-sets the additional RCC, albeit that part of this may need to be invested in additional strategic infrastructure capacity.

IR18 allowances

27. To create a positive cash balance of £20million at March 2021, £40million (2012/13 prices) of IR18 allowances need to be re-phased to after March 2021. The impact on the phasing of IR18 is set out below.

All figures £m (2012/13 prices)	2018-21	2021-24	Total
Modified IR18 allowances	259	280	539
Draft business plan IR18 allowances	299	240	539
Re-phasing of IR 18 allowances	(40)	40	-

Additional investment priorities

28. Any additional priorities for investment including lead pipe replacement pilots, private water supplies and sewerage provision to rural communities, acceleration of Water Framework Directive actions, and reduction in the economic level of leakage will be considered under the rolling investment review in December 2017 taking account of the available financing in relation to section 19 of this agreement. To the extent that financial provision is required for further additional investment priorities the value of the IR18 re-phasing to after March 2021 set out in note 27 above would need to increase further.

Improving resilience of water supplies

29. The Customer Forum has sought a robust methodology for assessing the risks, costs and benefits associated with large projects to improve resilience within the system. The procedure set out by Scottish Water in January 2014 provides the basis for such robust assessments and sets out how Scottish Water will consult and seek the support of the Customer Forum on these issues over time. This procedure will be incorporated into appendix 6 to "the agreed business plan".
30. Scottish Water and the Customer Forum agree that part of the assessment process to be undertaken by Scottish Water into the issues of resilience will include developing a risk assessment to facilitate discussion with customers and allow them to come to judgements about the scale of risk to assets and how it is assessed and the priority for addressing these risks.

Price Promise and Guaranteed Standards

31. Scottish Water and the Customer Forum have agreed a simplification and enhancement of Scottish Water's Price Promise and Guaranteed Standards of Service.
32. Scottish Water has committed to merging the two schemes, promoting them to customers using Plain English both in its publications and on the website; and taking a more proactive approach to offering rebate and compensation payments. Scottish Water has agreed that higher levels of payment should be made available and that they will be implemented from April 2015 as follows;
- all the financial payments are uprated in light of inflation since they were last uprated.
 - on unplanned interruptions to supply to move to give a rebate of 25% to 100% of annual water charge for between 2 and 5 incidents in future, rather than 3 and 6.
 - where a customer suffers from internal sewage flooding, the rebate will be increased to a minimum of Band D level of household waste water charges.

Cash balances

33. The forecast closing cash balance, including the financial reserve, at 31 March 2021 is reduced to £20million.

Financial performance

34. Scottish Water and the Customer Forum agree that the description in 'Innovation and Choice' that outperformance could potentially be used to "reduce charges, provide additional customer service improvements, improve the condition or performance of the assets in place, or build up its financial reserve" are the appropriate areas for engagement between Scottish Water and the Customer Forum.

35. The Customer Forum accept that "outperformance would be shared at the discretion of Scottish Water at this point, provided its financial strength did not exceed the upper limit of the tramlines", and both parties accept that that "if Scottish Water's financial strength reaches the upper limit and is forecast to stay there for the remainder of the price control period, the company would use the proceeds over that limit to the benefit of customers, subject to the agreement of the Water Industry Commission for Scotland (the Commission) and the Scottish Government".
36. Both parties recognise that Scottish Water will seek to trigger discussions with the Customer Forum, Commission and other stakeholders when the circumstances indicate this would be either beneficial or necessary, with the Commission having the power to determine when discussions under the tramlines should take place if this is not already happening voluntarily. Scottish Water and the Customer Forum recognise that the Scottish Government as owners of the company would have to be party to any agreement on the use of outperformance.

Summary of the forecast out-turn cash impact of the financial changes and limiting of price increases

37. For completeness, tabulated below are each of the financial adjustments and their impact on the forecast closing cash balance at March 2021.

Modification	Cash impact of modification £m	Closing cash balance at 31 March 2021 £m
Cash (including financial reserve) balance in draft business plan		117
Additional net investment requirements arising from omissions from draft business plan financial model	(61)	56
Impact of reduction in household price increase in 2014/15 from 3% in draft business plan to 1.6%.	(97)	(41)
Reduction in 2015-21 prices to 1.6%.	(72)	(113)
Reduction in forecast RPI for costs:		
• arising from reduction in 2013/14 from 3% to 2.8%.	18	
• in the annual differential between RPI and CPI from 0.9% to 0.75 in 2014-21	46	
• arising from a reduction in forecast CPI by 0.1% to 1.9%	<u>31</u>	
	<u>95</u>	(18)
Impact of increase in assumed average household growth from 0.67% pa to 0.74% pa	(10)	(28)
Rephasing of IR18 allowances to after March 2021 (£40m 2012/13 prices)	48	20

38. An updated financial appendix containing all of these changes will be provided in 'the agreed business plan'.

Signed

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Peter Peacock
On behalf of the Customer Forum

30 January 2014

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Douglas Millican
On behalf of Scottish Water

30 January 2014

Infrastructure and Capital Investment Committee

12th Meeting, 2014 (Session 4), Wednesday, 30 April 2014

Subordinate legislation

Title of Instruments

Road Traffic (Permitted Parking Area and Special Parking Area) (Argyll and Bute Council) Designation Order 2014 (SSI 2014/84)

Parking Attendants (Wearing of Uniforms) (Argyll and Bute Council Parking Area) Regulations 2014 (SSI 2014/85)

Road Traffic (Parking Adjudicators) (Argyll and Bute Council) Regulations 2014 (SSI 2014/86)

Type of Instruments

Negative

Laid Date

SSI 2014/84 28 March 2014

SSI 2014/85 28 March 2014

SSI 2014/86 28 March 2014

Minister to attend the meeting

No

SSI's drawn to the Parliament's attention by Delegated Powers and Law Reform Committee

No

Reporting Deadline

SSI 2014/84 22 May 2014

SSI 2014/85 22 May 2014

SSI 2014/86 22 May 2014

Purpose

1. The purpose of the three Scottish Statutory Instruments (SSI) together is to introduce a decriminalised parking regime within the Argyll and Bute Council area.

2. To date, 12 Scottish local authorities have introduced de-criminalised parking regimes. This enables them to administer their own parking penalty schemes, and to retain the penalties collected to finance parking enforcement procedures and other traffic management measures.

Road Traffic (Permitted Parking Area and Special Parking Area) (Argyll and Bute Council) Designation Order 2014 (SSI 2014/84)

Background

3. The effect of the designation order is that specified offences will be decriminalised in the parking area, such as breaches of orders relating to free on-street parking places or orders prohibiting or restricting waiting, loading and unloading. Enforcement will be carried out by parking attendants (see SSI 2013/385) and a system of parking adjudicators will deal with disputes (see SSI 2013/386).

The Parking Attendants (Wearing of Uniforms) (Argyll and Bute Council) Regulations 2014 (SSI 2014/85)

Background

4. This SSI stipulates that a parking attendant must be wearing an identifiable uniform when carrying out the duties associated with a parking attendant in the Argyll and Bute Council area.

The Road Traffic (Parking Adjudicators) (Argyll and Bute Council) Regulations 2014 (SSI 2014/86)

Background

5. This SSI provides for the adjudication process to be followed where a motorist believes that a penalty charge notice has been incorrectly issued in the Argyll and Bute Council area.

Procedure

6. Negative instruments are instruments that are “subject to annulment” by resolution of the Parliament for a period of 40 days after they are laid. All negative instruments are considered by the Delegated Powers and Law Reform Committee (on various technical grounds) and by the relevant lead committee (on policy grounds). Under Rule 10.4, any member (whether or not a member of the lead committee) may, within the 40-day period, lodge a motion for consideration by the lead committee recommending annulment of the instrument. If the motion is agreed to, the Parliamentary Bureau must then lodge a motion to annul the instrument for consideration by the Parliament.

7. If that is also agreed to, Scottish Ministers must revoke the instrument. Each negative instrument appears on a committee agenda at the first opportunity after the Delegated Powers and Law Reform Committee has reported on it. This means that, if questions are asked or concerns raised, consideration of the instrument can usually be continued to a later meeting to allow correspondence to be entered into or a Minister or officials invited to give evidence. In other cases, the Committee may be content simply to note the instrument and agree to make no recommendation on it.

Consideration by the Delegated Powers and Law Reform Committee

8. At its meeting on 22 April 2014, the Delegated Powers and Law Reform Committee considered the instruments and determined that it did not need to draw the attention of the Parliament to the instruments on any grounds within its remit.

Recommendation

The Committee is invited to consider any issues that it wishes to raise in reporting to the Parliament on these instruments.

**Myra Leckie
Committee Assistant
25 April 2014**