

Methodology Information Paper 19: Reviewing the baseline capital programme

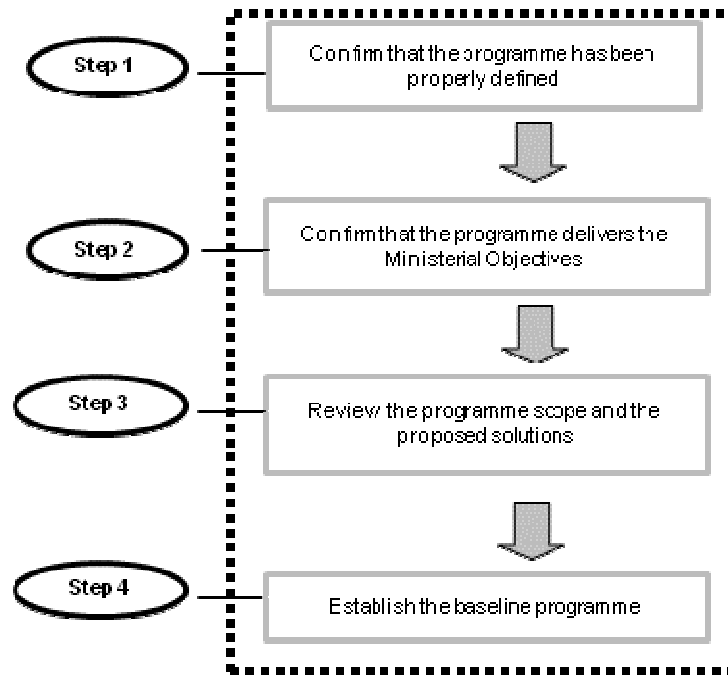
Introduction

This information paper sets out our proposed approach to reviewing Scottish Water's capital expenditure proposals. Our aim is to establish whether Scottish Water's proposals will deliver Ministers' objectives at the lowest reasonable overall cost. We will seek confirmation from the other industry regulators that Scottish Water's proposals will meet, but not exceed, Ministers' objectives.

The outcome of our review will be an agreed baseline investment programme against which Scottish Water's performance in delivering the programme can be monitored.

Reviewing the programme

Once Scottish Water has submitted its business plan, we intend to go through the following stages:



Step 1: Ensuring that the programme is properly defined

We will seek confirmation from the Reporter that Scottish Water has defined its investment programme adequately and met the requirements set out in our business plan guidance.

If there is insufficient information about elements of the programme, we will ask Scottish Water to provide clarification. Where insufficient information is provided, we may need to draw our own conclusions on the level of capital expenditure to allow for. We would base our conclusions on empirical and/or comparator information.

Step 2: Confirming that the proposed capital programme delivers ministerial objectives

We will seek confirmation from the Reporter and other industry regulators (the Scottish Environment Protection Agency (SEPA), the Drinking Water Quality Regulator (DWQR) and Waterwatch) that, if delivered in full, Scottish Water's investment proposals will meet the ministerial objectives. It will also be important to ensure that we do not finance any proposed outputs that are not consistent with the objectives.

Step 3: Reviewing the programme scope and the proposed solutions

We will ask the Reporter to examine Scottish Water's proposals in detail. We also propose to seek independent engineering advice on any aspects of Scottish Water's proposals where we consider that there may be scope for savings.

We will ask the Reporter to place particular emphasis on:

- The scope of requirements.
Is the scope of the proposed requirements consistent with meeting the ministerial objectives at the lowest reasonable overall cost?
Are strategic solutions employed?
Are best practice approaches being used?
- The technical solutions proposed.
Are the solutions employing the most appropriate technology?
Are better solutions available through the use of operational measures?
Has due account been taken of Scottish Water's obligations to ensure sustainable development?
- The profile of delivery.
Is the profile of delivery reasonable?
Has due account been taken of the impact of any overhang of investment from the previous period?

We will also ask the Reporter to analyse Scottish Water's approach to costing the investment programme. We will seek confirmation that Scottish Water's costing of its capital investment programme is

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consistent with both its out-turn costs for delivering the 2006-10 investment programme and the costs provided in Scottish Water's 'cost base'¹ submission.

The Reporter may identify aspects of the programme where there is insufficient evidence that Scottish Water's proposals meet the ministerial objectives at the lowest reasonable overall cost. We may seek independent advice in this instance.

This is consistent with our approach to the Strategic Review of Charges 2006-10. At that time the Reporter identified concerns about the scoping of aspects of Scottish Water's proposals, including the programme for water treatment works and improvements to unsatisfactory intermittent discharges (UIDs). We therefore commissioned independent engineering consultants Faber Maunsell to review those elements of Scottish Water's proposals in detail. We also asked Ofwat to compare Scottish Water's proposals for water treatment works and UIDs with those of the companies in England and Wales. Through this work, we identified significant over-scoping of requirements and an over-reliance on capital expenditure solutions when lower cost operational solutions were available. As a result, we made substantial reductions in Scottish Water's planned level of capital expenditure.

Step 4: Establishing the baseline programme

The output of our review will be a properly costed, fully defined list of capital investment projects, which, if delivered in full, will meet the objectives set out by Ministers for the regulatory control period.

Once the baseline programme has been established we will assess the scope for efficiency. This process is set out in Information Papers 24 and 25 'Capital Efficiency' and 'The Cost Base Approach'.

Related documents

'The Strategic Review of Charges 2006-10: The draft determination', Volume 5, Water Industry Commissioner for Scotland, June 2005.

'The Strategic Review of Charges 2006-10: The final determination', Water Industry Commission for Scotland, November 2005.

¹ In the Strategic Review process we use the 'cost base' approach, which was developed by Ofwat. The approach compares companies' costs for a range of benchmark projects to establish relative efficiency. It is important to establish that Scottish Water's cost base submission is consistent with the actual costs used in its investment plan.