

**Minute of the twenty-fourth meeting of the Water Industry Commission
for Scotland
Held on 6 and 7 March 2007 in Stirling**

Present:

Sir Ian Byatt (Chairman)
Professor David Simpson (Deputy Chairman)
Dr Michael Brooker
Mr Charles Coulthard
Mr Alan Sutherland (Chief Executive)

In attendance:

Mrs Katherine Russell (Director of Corporate Affairs and
Secretary to the Commission)
Miss Harriet Towler (Corporate Affairs Manager)
Mr Ian Tait (Director of Investment and Asset
Management) for items 4.9 and 6.
Dr John Simpson (Director of Analysis) for items 4 and 8.
Mr Craig Mackenzie (Analyst) for item 8.

Chairman's opening remarks

The Deputy Chairman welcomed everyone to the meeting and thanked them for attending.

1. Apologies for absence

Professor John Banyard

2. Minute of previous meeting and review of action points

The Commission agreed that the minute was an accurate account of proceedings. However, the Commission noted that one action point from the last meeting had been omitted. The Commission had requested that the Reporter be asked to verify the delivery of a sample of outputs from Scottish Water's investment programme. **Action**

The Commission were updated on other action points from the previous meeting and noted it was a satisfactory position.

3. Update on current issues

Professor Simpson reported that a group had been formed to discuss the regulation of public services in conjunction with the David Hume Institute. This group had recently submitted a request to the Commission for funding. As members of the David Hume Institute, Professor Simpson and Mr Coulthard declared an interest in this item. The Commission agreed that the group's aims were consistent with its remit of promoting customers' interests. As such, a donation should be made, but the level of funding would be at the discretion of the Chief Executive.

The Chief Executive reported that he would give a lecture to the UNESCO (United Nations Educational, Scientific and Cultural Organisation) Centre for Water Law, Policy and Science on World Water Day (22 March). He also reported that an interview would shortly be published in Utility Week.

The Chief Executive updated the Commission on a meeting he had recently held with the Scottish Executive on the next price review. He also reported that the separation review of Scottish Water Business Stream had commenced.

The Chief Executive was pleased to report that the office had successfully recruited four new analysts to the office and one intern. The Commission welcomed this news.

The Secretary to the Commission reported that the programme of liaison meetings with Scottish Water was progressing well. She also reported that Fiona Pethick, Head of Corporate Affairs at Ofwat, would shortly visit the office and provide a briefing to staff.

The Chairman reported that he had recently led a discussion at the European Policy Forum. He had also attended a dinner for those interested in the Scottish water industry which had prompted some interesting discussion.

The Chairman updated the Commission on a meeting he had recently held with the Chairman of Scottish Water.

The Commission noted CP18-07, an update on the Chairman's programme of meetings with stakeholders in the Scottish water industry.

4. Strategy

The Commission reviewed draft executive summaries of Volume 1 and 2 of its planned methodology consultation (CP19-07, CP20-07). The Commission set out a number of minor amendments, but otherwise approved both documents. The Commission agreed that both documents should be published, and supporting chapters be placed on its website.

The Commission discussed possible approaches to providing rolling incentives to Scottish Water at the next price review (CP21-07). The Commission agreed that its preferred approach, subject to consultation, would be to measure outperformance through payments to the gilts buffer. The

Commission agreed that in order to do so effectively, clear rules for the operation of the gilts buffer would need to be set out.

The Commission discussed possible approaches to establishing Scottish Water's customer and revenue baseline (CP22-07) as part of the overall methodology consultation. The Commission noted the proposed approach of providing Scottish Water with the incentive to provide accurate information on customer numbers by only allowing Scottish Water to count any "declared" additional customers at half their value. The Commission noted the rationale for this proposed approach, but believed it would be important to capture stakeholders views on the proposed mechanism.

The Commission discussed its proposed approach to metering for the methodology consultation (CP23-07). The Commission noted that at the next review, the extent of household metering may need to increase. The Commission noted that should the penetration of household metering increase, then it could have a "toppling effect" – that is, as higher council tax banded customers begin to switch to a meter, there will be a greater incentive for lower council tax banded customers to do the same. This could lead to a broader switch to meters. The Commission recognised that this may be inconsistent with ministerial policy on social inclusion. However, the Commission agreed that Ministers Principles of Charging would specify how households should be charged.

The Commission discussed the approach to tariff baskets it would propose in the methodology consultation (CP24-07). The Commission supported the proposed reduction in tariff baskets, subject to stakeholders' views.

The Commission discussed possible approaches to the treatment of growth (CP25-07). The Commission agreed that the methodology consultation should propose an approach which treated growth as a discrete element of the capital programme.

5. Corporate Affairs

The Commission noted the update on the office workplan (CP26-07).

The Commission noted the update on the office's framework contracts (CP27-07). The Commission re-iterated the importance of managing these contracts effectively.

The Commission agreed the oral update on Waterwatch should be referred to its Remuneration and Audit Committees.

6. Investment

The Commission considered a statement setting out its procedure for making Reasonable Cost determinations (CP28-07). A draft of this statement had previously been consulted on. The Commission considered responses to the consultation, and approved the statement in its revised form. The Commission

requested a letter be sent to the Scottish Executive setting out its position.

Action

The Commission considered a proposed mechanism for improving monitoring of Scottish Water's delivery of investment outputs. The Commission welcomed the approach, but noted that further improvements could be made. The Commission requested that Scottish Water be consulted on the tolerance limits that should be used, prior to the approach being submitted to the Output Monitoring Group for consideration. **Action**

7. Licensing

The Commission noted the minutes of the last meeting of its Licensing Implementation Framework Group (LFIG) (CP30-07).

The Commission noted the update on the progress being made in the development of the Central Market Authority (CMA) (CP31-07). The Commission requested that the key milestones on the project be set out, and updates provided. **Action**

The Commission considered CP32-07, a request to grant delegated authority to the Chief Executive to issue a 'Section 11 direction' to Scottish Water Business Stream. The Commission noted the urgency for Scottish Water Business Stream to provide the CMA services provider with data and information. The Commission agreed to delegate authority to the Chief Executive to issue a Section 11 direction if Scottish Water Business Stream did not address the services provider's data request adequately.

The Commission considered a request to delegate authority to the Chief Executive to issue 'The Water Services (Central Market Authority and Interim Arrangements) Directions 2007' to Scottish Water Business Stream (CP33-07). The Commission agreed that authority should be delegated.

The Commission considered a fees scheme to cover the costs associated with processing licence applications (CP34-07). The Commission approved the scheme for submission to Scottish Ministers.

8. Costs, performance and levels of service

The Commission noted CP35-07, an update on its wholesale charges project. The Commission welcomed the work that had been undertaken by John Simpson and Craig Mackenzie on the project. The Commission noted that Scottish Water's wholesale charges scheme would shortly be placed on its website. The Commission noted the importance of communicating the wholesale charges scheme effectively and requested a series of information notes be written. **Action**

The Commission considered CP36-07, a request to delegate authority to the Chief Executive to approve an interim wholesale charges scheme for Scottish

Water to levy on Scottish Water Business Stream until July 2007. The Commission agreed to delegate authority.