

Strategic Review of Charges 2010-14

Every four years, we carry out a review of Scottish Water's charges. This strategic review process is designed to provide value for money for customers. Ministers' decide what Scottish Water should achieve over the four year regulatory period by setting objectives. We determine the financing Scottish Water will need to deliver these objectives at the lowest overall reasonable cost. We translate these financing requirements into limits on the prices Scottish Water's customers will pay.

Our last price review was published in November 2005 and covered the period 2006-10. We have already begun working on the 2010-14 price review.

Our current consultation

During May, June and July this year, we published four consultation documents on the methodology we should use to carry out our next review of Scottish Water's charges. Our consultation considers the following issues which all impact on the prices customers pay:

- Scottish Water's financing and governance arrangements.
- The levels of service Scottish Water provides its customers.
- Scottish Water's operating costs.
- Scottish Water's capital expenditure.

Our consultation closes on **19 October** at 5pm.

Stakeholder workshops

In order to make our consultation more accessible, we held a series of eight workshops for stakeholders – four prior to each document being published and four following publication. We hoped to understand what issues stakeholders believe we should be consulting on, and in turn, to explain our proposed approach.

A brief summary of some of the issues discussed is set out below.

Feedback from the workshops

Financing Scottish Water

We asked stakeholders about the level of risk Scottish Water faces, the steps that could be taken to manage that risk, and how risk impacts on customers' bills.

Stakeholders did not believe that, in general, Scottish Water faced risks different to the English and Welsh water and sewerage companies. However, some stakeholders questioned whether Scottish Water's ownership structure distinguished it from private companies – were customers in Scotland better protected from risks, or more vulnerable?

Stakeholders recognised that steps had been taken to protect customers in Scotland from unexpected shocks such as droughts etc, with the establishment of a gilts buffer. The gilts buffer acts as an insurance policy for customers. Stakeholders questioned how this buffer would be managed, how large would it be allowed to grow and how it impacted on customers' bills.

Customer baseline and levels of service

We asked stakeholders about the information we could use to understand how many and what type of customers Scottish Water has. We also sought views on the level of service Scottish Water provides to its customers.

Stakeholders suggested that Local Authority databases could be used as a check on Scottish Water's reported customer numbers. Some stakeholders questioned what the impact of a local income tax would be should it be introduced.

Stakeholders welcomed how Scottish Water had improved its level of service in recent years, but believed more could be done. They suggested the price review should be used to encourage continuous improvements in service.

Stakeholders also questioned whether the views of customers could be better understood in the price review by undertaking more customer research – were customers willing to pay for continuous service improvements?

Scottish Water's operating costs

We asked stakeholders about how we could ensure that the expenditure Scottish Water requires to operate (such as employment costs, fuel costs etc) represents value for money to customers. Could Scottish Water provide more for less money by being more efficient? If so, by how much?

Many stakeholders agreed that we should gauge how efficient Scottish Water is by comparing it with England and Wales, providing our comparisons were fair. Some stakeholders suggested the econometric models we use to make these comparisons were complicated and could be better explained.

Stakeholders recognised that Scottish Water had made significant improvements, but was not yet as efficient as the English and Welsh companies. Some stakeholders suggested it was reasonable to expect Scottish Water to become as efficient as the best company in England and Wales in 2006-07 by 2014.

Scottish Water's capital expenditure

We asked stakeholders how we can ensure that Scottish Water's investment proposals are appropriate and sufficient to deliver Ministers' objectives. We also asked stakeholders how we could ensure that Scottish Water's capital expenditure was no higher than it needs to be.

Stakeholders told us that as the regulatory control period was relatively short at four years, Scottish Water did not have a long planning horizon. This made it difficult for Scottish Water to plan for the future.

Stakeholders from the construction industry told us that they would welcome a longer regulatory period. Greater certainty over Scottish Water's investment requirements would enable the industry to plan ahead and have more resources in place to respond to Scottish Water's requirements.

Some stakeholders were concerned that the investment programme should not be too big. They recognised that too large a programme could be difficult to manage and could create inefficiencies if it had to be delivered in four years. They also expressed concern about the disruption that could be caused to customers and whether the construction industry would 'overheat' if demand was too high.

Stakeholders agreed that consideration should be given to allowing Scottish Water to make an 'early start' on its future investment and providing more time for planning.

Next steps

Following the close of the consultation period on 19 October, we will consider the written responses we have received carefully. We will issue our response on 20 December.

During 2008-09, the focus of our work will turn to working with Scottish Water to define and collect the information we need to implement our approach.

The Scottish Government will also be undertaking important work by consulting on the principles that should underpin Scottish Water's charges, and issuing guidance on the objectives that Scottish Water will be expected to achieve.