



SCOTTISH EXECUTIVE

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Dear Sir Ian

STRATEGIC REVIEW OF WATER CHARGES: 2010 -2014

I am writing to inform you of the broad arrangements that the Executive wishes to be followed in the next Strategic Review of Water Charges (SRoC).

SRoC arrangements: background

The Water Industry (Scotland) Act 2002, as amended by the Water Services etc. (Scotland) Act 2005, places duties on both the Scottish Ministers (Ministers) and the Water Industry Commission (the Commission).

The duties on Ministers include to:

- Specify the time period for the determination of charges (SRoC);
- Specify the date by which the determination must be made;
- *Set the standards and objectives* (statement of objectives) to be achieved by Scottish Water in the provision of core services during the period to be covered by the strategic review; and
- Issue a statement of policy regarding charges (principles of charging), having consulted the Commission, the Convenor of Waterwatch Scotland and Scottish Water.

The duties on the Commission include to:

- Determine the limits on charges for the time period and by the date specified by Ministers. The limits have to be set for each of the years covered by the review period and must be consistent with the principles of charging set by Ministers

- Ensure that, in determining charge limits the revenue from the limits, when taken with the borrowing authorised by the Executive, is sufficient to allow Scottish Water to perform its core functions and meet the stated Ministerial objectives at the lowest reasonable overall cost
- Publish a draft determination, invite representations and have regards to these in the final determination.

SRoC 2010-14: Ministerial Specifications

The following set out the requirements Ministers wish followed in the next Strategic Review of Charges.

Time period of and date of publication for the determination: The Commission is to undertake a strategic review of charges for the four year period 2010 to 2014, consistent with the planning horizon used in the Quality and Standards 3 process and the indicative charge limits provided as part of the Strategic Review of Charges 2006-2010. The determination should be published by the end of November 2009.

Principles of Charging: Ministers will issue a consultation on the principles of charging in November 2007 and confirm the principles of charges to be applied by way of a public statement in April 2008.

Statement of Objectives: The objectives to be achieved by Scottish Water during the next period are those specified in the Explanatory Note attached to the Scottish Water (Objectives for 1st April 2006 to 31st March 2010) Direction 2005¹. These objectives were established by Ministers following advice of the Quality and Standards 3 Board and in-depth public consultation and research. In specifying these requirements Minister recognise Scottish Water's duty under Section 51 of the Water Industry (Scotland) Act 2002 to act in a manner best calculated to contribute to the achievement of sustainable development and we would welcome specific assessment of this issue in the Strategic Review.

I understand that the Commission intends to publish its timetable for the Strategic Review shortly and that as part of the process Scottish Water will be required to submit a first draft business plan at the end of May 2008, with the Commission commenting on it by the of July 2008. This provides a useful evidence base to allow for Ministers to review their statement of objectives and principles of charging. Ministers will either revise or confirm the objectives and the principles of charging by the end of September 2008.

SRoC 2010-14: Arrangements to support greater continuity of investment planning

The development of objectives for the industry which cover more than one regulatory period is, I believe, a positive development toward providing greater continuity in investment planning and delivery of longer term objectives, for instance the Water Framework Directive. Improving the planned delivery of objectives is to the benefit of customers. Nevertheless, it is appropriate to consider whether there are further developments which could assist in this process and remove unnecessary uncertainty.

With this in mind, I would ask that the Commission considers whether there are further opportunities to support greater continuity of investment planning in the current processes. Such options might

¹ <http://www.scotland.gov.uk/Resource/Doc/1057/0022201.pdf>

include arrangements which facilitate an early start to Ministers' objectives, thereby minimising any hiatus between investment, and the ability to take account of delivery requirements which will take longer than any single regulatory period to address. For example, the requirement to address waste water infrastructure issues in the Glasgow area as well as the broader requirements to address sustainable development and climate change issues.

You will be aware that the Q&S3 Board endorsed the Common Framework Approach to assess Scottish Water's requirements for capital maintenance in its report to Ministers and that Ministers accepted that advice. I note that you have advised that you will not be able to apply this approach due to lack of data in the Strategic Review 2010-14. To help avoid unnecessary uncertainty, I would encourage the Commission to work with Scottish Water to develop a suitable interim arrangement whilst continuing to encourage the enhancement of Scottish Water data to a *sufficient level* to support the operation of a Common Framework Approach.

Finally, I wanted to raise with you my plans to develop a longer term vision for the water industry in Scotland. While the objectives for the next review are already stated, it will be necessary to begin consideration of how to develop objectives for subsequent periods so that an acceptable longer term vision for Scottish Water, the service customers receive and the water environment can be established. Such a vision would help further to ensure that the objectives financed by successive reviews contribute effectively to longer term aims. As well as sustainable development and climate change mentioned above, such a vision could take account of the interaction with River Basin Management Planning and Water Safety Plans.

I look forward to receiving regular reports on the progress of the strategic review.

I am copying this letter the Chairman of SEPA, the Drinking Water Quality Regulator for Scotland, the Chairman of Scottish Water, the Convenor of Waterwatch Scotland and the Chairman of the Competition Commission.

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