

**Minute of the nineteenth meeting of the Water Industry Commission  
for Scotland  
Held on 5 and 6 September 2006 in Stirling**

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Present:

Sir Ian Byatt (Chairman)  
Professor David Simpson (Deputy Chairman)  
Professor John Banyard  
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)  
Dr John Simpson (Director of Analysis) for item 6 and 7.  
Dr Jeremy Atkinson (Director of Licensing) for item 8.  
Mr Ian Tait (Director of Investment and Asset Management) for item 6.

**Chairman's opening remarks**

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

**1. Apologies for absence**

None.

**2. Minute of previous meeting and review of action points**

The Commission agreed that the minute was an accurate account of proceedings.

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

**3. Update on current issues**

**3.1 Working with Stakeholders**

The Chairman reported on his correspondence with the Chair of Scottish Water, Ronnie Mercer (CP137-06). The Chairman noted he was not aware of any decisions made by the Minister regarding the form Scottish Water's retail

entity could take. The Chairman noted he would be meeting with Mr Mercer again on 7 September.

The Chief Executive reported the resignation of Scottish Water's Customer Service Director, Cheryl Black.

The Chief Executive also updated the Commission on legal advice received regarding the Commission's statutory obligations towards Waterwatch. The Commission noted that as a result of this advice, a pay review the same as that conducted for the Commission's in-house staff, would also be carried out for Waterwatch staff. In addition, the Commission noted that its internal auditors would carry out an internal audit review of Waterwatch. The Commission noted that this situation would impact on the role of its Audit Committee.

The Commission were informed of the formation of a small informal working group to discuss common issues in regulatory publicly owned utilities.

The Commission noted CP138-06 regarding monthly meetings with SEPA.

### **3.2 Other Current Developments**

The Chief Executive reported positive progress with Human Resource issues and updated the Commission on the implementation of the appraisal system. The Commission were pleased with the feedback and requested continued updates. **Action**

The Chairman reported that he had continued his programme of meetings with stakeholders across Scotland. This month he had met with representatives from the City Council of Glasgow, Edinburgh, North Ayrshire, North Lanarkshire as well as the Church of Scotland. The primary issues arising from these meetings were development constraints and retail access.

Professor Simpson reported that he would circulate a response to a paper written by a Mr and Mrs Cuthbert on the financing of the Scottish Water industry in the final determination. This response would be published.

Professor Banyard reported two new external appointments. The Commission agreed no conflict of interest involved.

The Chief Executive reported that he would shortly be meeting with representatives from Anglian Water to discuss views on interaction with regulators and retail access.

## **4. Strategy**

The Commission discussed how the governance framework of the water industry in Scotland could be improved (CP140-06). The Commission agreed that the principle that customers should not pay twice, which had underpinned the Strategic Review of Charges 2006-10, should continue to be a

fundamental principle going forward. Furthermore, the Commission agreed that the cost of capital assumed for Scottish Water in the future, should be at the market rate.

The Commission noted that key areas to be discussed in the future would be; gaining greater clarity over responsibilities; an examination of lending options; and the alignment of incentives.

The Commission agreed that advice should be sought from Counsel regarding the interpretation of “lowest overall reasonable cost”. This would be reported at the next meeting. **Action**

## **5. Corporate Affairs**

The Commission noted the information paper on the office workplan (CP 141-06). **Action**

The Commission reviewed the paper on update of framework agreements (CP142-06) and requested that the appropriate director reviews each report and adds a comment. This comment should incorporate views on delivery as well as monetary issues. **Action**

Mr Coulthard, Chairman of the Audit Committee, suggested the process for managing contracts should form part on an internal review. Audit Scotland is to provide guidelines on ensuring value for money of framework contracts. **Action**

The Commission noted CP143-06 on the process and timescale for devising a workplan for the Strategic Review of Charges 2010-14.

The Commission discussed key issues relating to the formulation of a communication strategy. The Commission emphasised the need for two-way engagement with stakeholders. A draft communication strategy, which will keep an ongoing track of important information regarding stakeholders, will be discussed at the next meeting. **Action**

## **6. Investment**

The Commission noted CP145-06 on the challenges faced by Scottish Water in delivering the remaining Quality and Standards II outputs. The Commission noted the potential range of the remaining outputs and the factors contributing to this. The Commission requested to be kept informed about the remaining outputs in the coming year. An update report following receipt of the Annual Return in 2007 would be presented to the Commission. **Action**

The Commission agreed that the Scottish Executive should be kept informed about the status of the overhang. The Commission requested a number of amendments to draft letter to the Scottish Executive in this regard (CP146-06). The Commission agreed a copy of the amended letter should be forwarded to Scottish Water. **Action**

The Commission noted the update on the Scottish Executive's current thinking on how the process for Quality and Standards IIIb might work (CP147-06). A letter would be sent to the Scottish Executive confirming that in the Commission's view, current objectives do not require revisiting. **Action**

The Commission noted the paper on the report into the duplication of Quality and Standards II schemes (CP148-06). and confirmed that the findings reflected the Faber Maunsell report. A meeting would be held with Arup to clarify further their conclusions before a meeting with DWQR and Scottish Water. **Action**

The Commission approved the report on the Executive Summary for Investment and Asset Management (CP149-06) but noted some amendments.

## **7. Costs, Performance and levels of service**

The Commission noted the update on the wholesale charging project (CP150-06) and noted the importance of timely consultation by the Scottish Executive on charging.

The Commission noted the paper on the process for the Scheme of Charges 2007-08 (CP151-06).

The Commission discussed Scottish Water's operating cost baseline for 2005-06 (CP152-06). The Commission noted the distinction between core and non-core costs and wholesale and retail costs.

The Commission considered the update on the regulatory information review being conducted by the office. The Commission noted that there would be a material net reduction in the amount of information required from Scottish Water (CP153-06). A final report on these issues was agreed to be completed for the November meeting. **Action**

The Commission approved key themes for the Costs and Performance report (CP154-06).

## **8. Licensing**

The Commission received a general update on progress with regard to current issues surrounding licensing. The following key points were discussed.

- The Chief Executive informed the Commission of the timeline for the opening of the retail market.
- The Commission noted the form the retail entity should take was still to be decided.
- The Commission noted the considerable amount of work being carried out on the codes.

- The Chief Executive informed the Commission that the provisional licence for Scottish Water Business Stream (SWBS) would expire on 31 March 2007.
- The Chief Executive would write to Scottish Water and the Scottish Executive regarding the provisional licence. **Action**
- The Chairman noted that following the grant of the provisional licence he would write to the Deputy Minister, Rhona Brankin regarding the commencement of the relevant sections of the 2005 Act to allow the Commission to grant permanent licences.

The Commission noted the paper on the minutes of the first two meetings of the Licensing Framework Implementation Group (LFIG) (CP155-06).

The Commission approved the terms of reference of the Licensing Framework Implementation group (CP156-06).

The Commission agreed that CP157-06 on the role of codes and agreements and CP158-06 on the role of the Central Market Authority (CMA) should be combined and posted on the website as an information paper, with the addition of a short introduction. **Action**

The Commission were informed that the office would be undertaking procurement work to set up the Central Market Authority (CP159-06). The Commission confirmed that it would be prepared to use its Section 11 direction powers to require Scottish Water to take responsibility for the set-up of the CMA.

The Commission approved the approach to assessing Section 29E departures (CP160-06) but requested an alteration to the benefit-sharing ratio be made, with a full explanation included. The Commission delegated authority to the Chief Executive to finalise the detail of the consultation. **Action**

The Commission discussed a proposed consultation on the licensing fees scheme that would apply to Scottish Water Business Stream (CP161-06). The Commission noted that the figures used should be cost reflective and therefore robust to challenge. The Commission approved the consultation on the fees outlined.

The Commission agreed the procedure outlined in CP162-06 to determine disputes over the cost of discontinuation

The Commission discussed the procedure which it must follow in considering the provisional licence application of SWBS (CP163-06). The Commission approved the proposed procedure.

## **9. Any other business**

Mr Coulthard drew the Commission's attention to a letter received from the Independent Review of Regulation, Audit, Inspection and Complaints

Handling of Public Services. The Commission took account of the letter but agreed that no action was to be taken.

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**Minute approved on:**

**Minute authorised by:**