

**Minute of the thirtieth meeting of the Water Industry Commission for
Scotland**

Held on 4 September 2007 in Stirling

Present:

Sir Ian Byatt (Chairman)
Professor David Simpson (Deputy Chairman)
Mr Charles Coulthard
Dr Michael Brooker
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 item 5.
Miss Suzanne Baylis (Analyst) for item 6.
Mr Richard Khaldi (Analyst) for item 6.
Mr Cameron McKean (Analyst) for item 6.
Mr Craig Mackenzie (Analyst) for item 7.
Mr Cesar Raffo (Analyst) for item 7.
Dr Jeremy Atkinson (Chief Executive, CMA Scotland) for
item 3.3

Chairman's opening remarks

The 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

I. Minute of last meeting (07/07)

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

II. Review of action points (AP07/07)

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

3. Update on current issues

I. Working with stakeholders

The Chief Executive reported that:

- He had recently welcomed representatives from the Korean Water and Wastewater Works Association to the office.
- The office had recently welcomed a secondee from the Northern Ireland Authority for Utility Regulation (NIAUR).
- The office would shortly hold its annual away day. A number of stakeholders had been invited to join the event and express their views on the industry.
- On-going liaison with Scottish Water and the Scottish Executive continued to work well.
- The office would shortly be investigating the extent of separation between Scottish Water and Scottish Water Business Stream.
- The Drinking Water Quality Regulator had recently published his annual report.

The Chief Executive thanked Waterwatch Scotland for inviting the Commission to hold its seventh stakeholder workshop for the next price review at its away day. He hoped attendees had found it a useful event.

The Chairman reported that he had held useful meetings with Stephen Noon, Des McNulty MSP, Brian Saunders (Chair of the Central Market Agency) and Ronnie Mercer (Chair of Scottish Water).

The Chairman also reported that he had been invited to present at a European Policy Forum event on competition.

II. Other current issues

Professor Simpson reported that research part funded by the Commission into how Scottish Water's regulatory model could be applied to other areas of the Scottish public sector, would shortly be completed and presented at a David Hume Institute event.

Mr Coulthard thanked the office for briefing the Independent Water Review Panel for Northern Ireland, of which he is a member, on the water industry in Scotland.

The Commission noted that there had been a recent cryptosporidium incident in Langholm.

III. Update on the Central Market Agency (CMA)

The Chairman welcomed Dr Jeremy Atkinson, Chief Executive of the CMA to the meeting. Dr Atkinson updated the Commission that administration arrangements for the CMA were progressing well, and that its board was expected to hold its first meeting on 26 September. Dr Atkinson noted that the Commission's contract with Gemserv, the service provider for the CMA, was expected to shortly transfer to the CMA. A due diligence exercise would be carried out on the contract prior to its transfer.

4. Corporate Affairs

I. Update on the office workplan (CP111-07)

The Commission noted the update on the office's workplan.

II. Update on framework contracts (CP112-07)

The Commission noted the update on its framework contractors. The Commission welcomed the action that the office was taking to effectively manage its contractors. The Commission requested that future updates provide more information on the steps taken to manage these contracts.

III. Update on stakeholder workshops 5 and 6 (CP113-07)

The Commission noted and welcomed the summaries of its fifth and sixth stakeholder workshops for the 2010-14 price review.

IV. Update on Waterwatch Scotland

The Chief Executive reported that whilst a strategy for ensuring Waterwatch Scotland's operational independence from the Commission had been devised, action had yet to be taken by the Scottish Executive. The Chief Executive also reported that the Scottish Executive was currently drafting a letter in respect to his responsibilities as accountable officer for the Commission, and any future responsibility for Waterwatch Scotland.

The Commission noted this update.

V. Update on the Comiston lecture 2008

The Chairman reported that he had invited a speaker for the 2008 Comiston lecture, and hoped they would accept.

The Commission noted this update.

5. Investment

I. Update on Scottish Water's leakage performance (CP114-07)

The Commission were updated about Scottish Water's performance against the pragmatic leakage targets it had set in May 2006. It had been previously reported to the Commission that Scottish Water's reported leakage for 2006-07 was 1,004 MI/day, some 44MI/day above the target agreed. Furthermore, the Reporter had found that around 60MI/day of the reported reduction was attributable to changes in assumptions about unmeasured consumption. The Commission emphasised the importance of reducing actual leakage, and ensuring that leakage is measured on a consistent basis. The Commission noted that Scottish Water is undertaking a programme to improve its measurement of leakage. Scottish Water had also requested a meeting with the Chief Executive to discuss this issue further. The Commission requested a further update once this meeting had taken place.

Action:

The Commission noted this update.

II. Key messages for the Investment and asset management report (CP115-07)

The Commission noted that analysis had been undertaken for its Investment and asset management report 2006-07. The Commission considered the key messages this analysis suggested. The Commission agreed the report should highlight that a significant increase in project delivery is required if Ministers' objectives are to be met. The Commission also agreed the report should set out that if investment delivery does not significantly increase, it may be required to discuss with the Minister whether a re-phasing of elements of the investment programme would be in the interests of customers.

The Commission approved these revised key messages.

6. Competition

I. Application for licences by Aquavitae (UK) Limited (CP116-07)

The Commission considered an application submitted by Aquavitae (UK) Limited for permanent water and sewerage licences. The Commission agreed that it was minded to grant licences to Aquavitae (UK) limited, subject to representations received from third parties.

The Commission agreed to delegate authority to the Chairman and Chief Executive to make any further and final decisions concerning the

grant of such licenses and the issuing of any related directions, waivers or consents, providing there were no material changes in circumstances.

II. Principles of governance for Scottish Water Business Stream (CP117-07)

The Commission noted that governance is one the three tests that it had agreed Scottish Water Business Stream must pass in order to be awarded with permanent water and sewerage licences. The Commission noted that the structure of Scottish Water and Scottish Water Business Stream is complicated. Scottish Water (as the holding company) has a legitimate interest in Scottish Water Business Stream, however, in order to ensure a level playing field in the market, Scottish Water Business Stream must be demonstrably separate and free from Scottish Water's influence over its business strategy.

The Commission agreed that a governance code should be introduced to govern Scottish Water and Scottish Water Business Stream's relationship. The Commission approved the proposed principles that should underpin this code. The Commission noted that this code would be enforced as part of Scottish Water Business Stream's licence conditions. The Commission requested consideration be given to using a Section 11 Direction to clarify Scottish Water's requirement to adhere to the code. This issue should be discussed with Scottish Water and Scottish Water Business Stream, and a draft code presented to the Commission at its next meeting.

Action

III. Codes and service directions (CP118-07)

The Commission noted that a series of minor amendments to core market documents had been proposed since they had been approved by the Commission in May. The Commission understood that these changes resulted from technical discussions with relevant parties and consistency checks. The Commission agreed that these changes were not inconsistent with its statutory duty under the Water Services etc (Scotland) Act 2005, to ensure that the introduction of competition should not be to the detriment of Scottish Water's core functions. The Commission noted that these proposed changes would be consulted on.

The Commission agreed to delegate authority to the Chief Executive to finalise the codes and directions following a period of consultation, and to issue them, providing no further material changes were made.

7. Costs, performance and levels of service

I. Key messages for the Customer service report (CP119-07)

The Commission noted that analysis for the Customer service report 2006-07 had been undertaken. The Commission considered the key messages suggested by this analysis.

The Commission approved the key messages proposed, but requested that the importance of incentives be emphasised, and changes in Scottish Water's Overall Performance Assessment score be expressed in terms of the service customers receive.

II. Key messages for the Costs and performance report (CP120-07)

The Commission noted that analysis for the Costs and performance report 2006-07 had been undertaken. The Commission considered the key messages suggested by this analysis.

The Commission agreed a simplified version of the proposed key messages.

III. Update on Scottish Water's quarterly financial performance (CP121-07)

The Commission were updated on Scottish Water's financial performance for Quarter 1 of 2006-07.

The Commission noted that Scottish Water's revenue was in line with that assumed in the Final Determination of Charges for 2006-10, and that Scottish Water was on target to outperform on operating costs for the period. However, the Commission noted with concern that capital expenditure was lower than anticipated.

The Commission noted this update.

IV. Update on whether Scottish Water has requested an interim determination

The Commission noted that Scottish Water had not requested an interim determination of charges be carried out for 2008-09 (by the 1st September deadline).