

Mandatory water quality and environmental improvement programme 2015-21

This note summarises issues arising from Scottish Water's Service Improvement Reports on the future capital investment required to meet mandatory drinking water and on environmental quality obligations¹. We will comment in more detail on Scottish Water's proposals in these areas which will be set out in its draft Strategic Business Plan (due to be published in October 2013).

Introduction

The Scottish Government determines the high-level environmental, quality and customer service objectives that Scottish Water must deliver through the 'Quality and Standards' process. The Commission's role, and that of the Customer Forum, is to ensure that these objectives are delivered at a reasonable cost for consumers. The environmental and drinking water quality regulators, the Scottish Environment Protection Agency (SEPA) and the Drinking Water Quality Regulator (DWQR) advise the Government. They also monitor compliance with the required standards.

As such the Commission's role is to establish the efficiency of Scottish Water's proposed approach. This could include the timing and pace of the investment programme, the level of innovation, the use of revenue solutions (as opposed to capital expenditure) and the company's overall efficiency.

Summary of the information provided in the reports

In these reports Scottish Water provides a thorough review of:

- the directives that drive current and future investment, in particular the obligations that are imposed on water companies;
- the role of SEPA and the DWQR in monitoring and enforcing these obligations;
- Scottish Water's future requirements under these directives and, in particular, their impact on the investment programme; and
- the indicative solutions that could be employed to ensure compliance.

Scottish Water also sets out its broad assessment of the capital investment it considers will be necessary to meet the directives. In addition it outlines the key drivers for drinking water quality and environmental performance and sets out its view on the impact on customers if it does not meet the required standards. Finally, the reports outline the options the company has for meeting the standards.

The key points to note are set out below.

Drinking water quality

The report principally reviews improvements in drinking water quality achieved in the last several years. It appears less specific about future improvements, but sets out the non-compliance issues to be addressed and the future risks of non-compliance identified through Drinking Water Safety Plans.

¹ The relevant Service Improvement Reports are entitled 'Drinking Water Quality' and 'Improving the Water Environment' dated 12.12.12 and 21.01.13 respectively.

Performance achieved:

- Compliance has improved significantly over the past ten years: 99.28% of samples taken from consumers' taps achieved the standards in 2002, and this has now improved to 99.84% in 2011.
- Performance remains slightly below average performance in England and Wales (currently 99.96%).
- A small number of failures of drinking water standards at customers' taps (230 in 2011), particularly relating to Trihalomethanes (THMs) and cryptosporidium failures, still need to be addressed.

Proposals:

- Under Scottish Water's proposals the risk of failures would be significantly reduced.
- Customers have choices in terms of the extent and timing of the proposed risk reduction.

Environmental performance

Performance achieved:

- Scottish Water's current performance on key environmental legislation such as the Urban Wastewater Treatment Directive and the Water Framework Directive is broadly comparable with that of the water companies in England and Wales.
- Scottish Ministers have set an objective that by 2027, 97% of water bodies in Scotland should achieve 'good' status or higher (the forecast figure for 2015 is around 60%).
- By 2015 no bathing waters will remain where it would be possible to improve the bathing water classification further simply by improving Scottish Water's assets – for these bathing waters, issues such as diffuse pollution from other sources (eg agriculture and private septic tanks) also have an impact.

Proposals:

- Scottish Water is proposing further investment where there is scientific evidence confirming the impacts this investment will have, there is a clear cost benefit, and asset investment is the most sustainable way to meet the required outcome. As such it is proposing that further investment to improve shellfish waters and to improve bathing water quality should not take place until the impacts of that investment are better understood. In the case of bathing water quality this includes understanding the impacts of diffuse pollution.
- The proposals provide for tackling all confirmed discharges that do not comply with the Urban Wastewater Treatment Directive and for meeting Ministers' objectives under the Water Framework Directive.

Issues arising

The reports provide helpful background information on Scottish Water's proposals in these areas. The Commission intends to set out further guidance for the Customer Forum when we receive Scottish Water's draft Business Plan. This will include advice on:

- the overall level of expenditure;
- the use of innovative approaches adopted by Scottish Water (to reduce costs or to improve performance);

- the efficiency of the proposed expenditure; and
- the extent to which this expenditure will impact on customers' bills.

At the current time, the reports do not provide sufficient information for us to comment on the overall efficiency or effectiveness of Scottish Water's proposed approach. There is also very little information provided on how the use of solutions that are innovative and/or revenue based may reduce the resources required from customers. We would expect Scottish Water to provide further comment in these areas.

In our view the Customer Forum could reasonably expect more detail on the trade-offs that have been considered and discounted, the use of innovative solutions, and the improvement in the overall asset base that would result from the proposed enhancement investment.

The Forum may also wish to ask for information on the implications for future operating costs and capital maintenance expenditure of the selected options in order to reassure itself that these matters have been taken fully into account in Scottish Water's appraisals.

In our view, the Customer Forum could also reasonably:

- agree, and require reporting on, the delivery profile for enhancement investment; and
- seek to define clearly what additional improvements in customer service will be delivered as a result of increased spending on enhancement investment (as opposed to, and separate from, benefits accruing as a result of any increased capital maintenance).

Monitoring capital enhancement investment

The Customer Forum could require reporting on:

- the profile of expenditure for enhancement investment – this could be in the form of either additional operating costs or capital expenditure; and
- progress against planned expenditure – this would be by using the overall measure of delivery (OMD) tool that is being used in the current regulatory control period.

The Forum may also seek to ascertain the improvement in efficiency in the delivery of enhancement investment that Scottish Water has achieved over the past several years. The Forum could also seek to ensure that the company's proposals are genuinely incremental to the improved asset performance that has resulted from previous investment in new assets and from the lower levels of leakage that have been achieved.

Monitoring improvements in customer service

Further investment in improved environmental and water quality performance should reduce operational risk, improve customer service, and result in the overall average asset condition being better than it would otherwise have been. In addition to capturing any customer service improvements in a revised OPA, the Customer Forum may consider it appropriate to define how operational risks, which could lead to service interruptions, will have been reduced.

It is likely to be important that Scottish Water defines clearly the service level improvements that will result from its planned enhancement investment. There should not, of course, be any overlap with discretionary improvements in the level of customer service that are decided on by the Customer Forum.

Ensuring underlying asset health

Current customers benefit when Scottish Water borrows to cover some of the initial cost of service or environmental improvements. This is because the bill for these long-lived assets is being shared with future customers, who will also benefit. However, this increases the responsibility of current customers to ensure that the condition and performance of assets does not deteriorate under their stewardship.

If the assets were to deteriorate, this would either increase the costs that have to be borne by future generations of customers or would reduce the level of service available to them. On the other hand, investment should be committed only when it has been properly defined and appraised as to its need both in terms of actual required outcome and its deadline.

The Forum should consider carefully the evidence presented to it on what should be paid by current as opposed to future generations of customers.

Agreeing the final package

We suggest that the Customer Forum should seek to specify clearly the levels of expenditure, risk reduction and customer service enhancement that have been agreed with Scottish Water.

This information should clearly indicate the improvements in these areas that would result from the proposed enhancement investment, alongside but separate from any increase in expenditure on capital maintenance and any agreed discretionary expenditure on improving customer service. The agreed levels should form part of the Customer Forum's agreement with Scottish Water.

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