

Staff Paper 4

Number, mix and type of customers

This staff paper has been produced by our office to assist stakeholders in responding to the Draft Determination. The material reflected in this staff paper has informed the preparation of the Commission's proposed conclusions. However, this staff paper does not form part of the Draft Determination. Accordingly, this staff paper should not be relied upon as expanding upon or replacing anything contained in the Draft Determination.

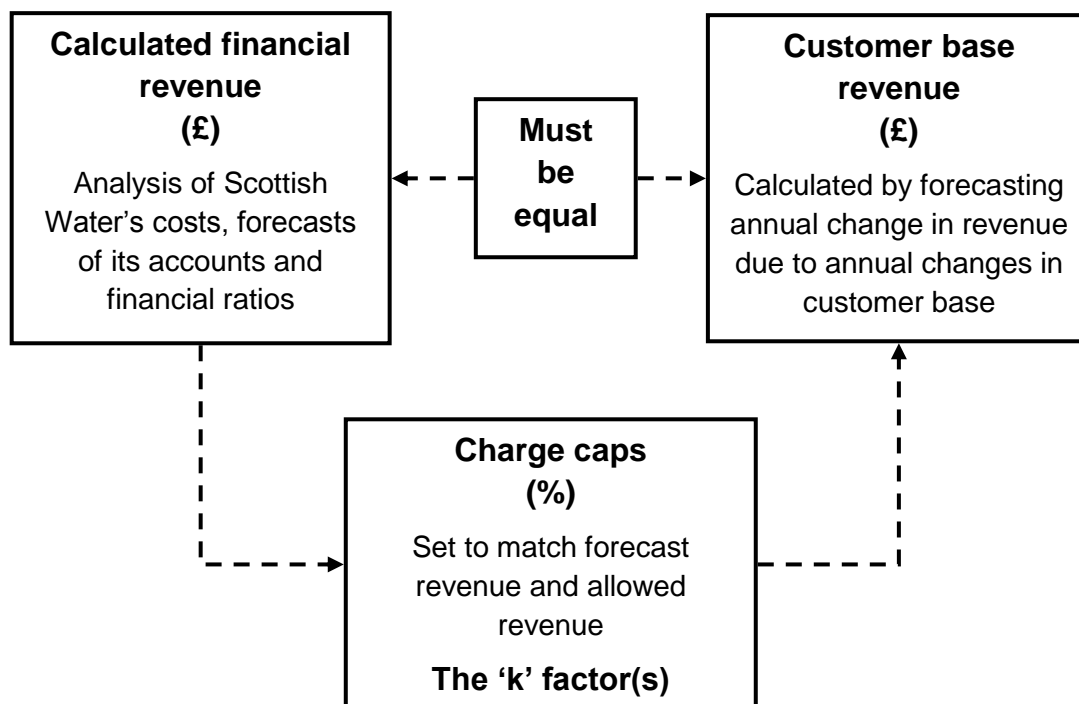
4.1 Introduction

This paper outlines the working assumptions in the forecast of Scottish Water's customer base in the Draft Determination.

The charge caps that the Commission sets for Scottish Water must balance the revenue that Scottish Water requires with the revenue it collects from charges. This means that, once we have calculated the level of revenue to allow for, it is necessary to forecast the number, mix and type of customers that Scottish Water provides services to. Figure 4.1 summarises this process.

This paper summarises how the number, mix and type of customers to whom Scottish Water will provide services have been forecast and explains how this impacts on the proposed charge caps. The financial and tariff basket model is available on CD and at www.watercommission.co.uk.

Figure 4.1: Charge setting process



4.2 Projections of customer base

Given the current economic uncertainty, it is proposed to make lower assumptions about Scottish Water's customer base than otherwise may have been made.

For both household and non-household customers, the projected growth rates that Scottish Water included in its second draft business plan until 2010 have been accepted. For household customers this is a growth rate of 0.6% between financial years 2008-09 and 2009-10 and for business customers, this is a decline of around 1% between 2008-09 and 2009-10.

Projections of household customers

In order to understand potential rates of growth in household premises, historical information on growth rates was examined.

As the overwhelming majority of household customers pay with reference to the council tax band of the property, growth rates of the number of water customers should be similar to that of council tax¹. Table 4.1 sets out the growth in numbers of

¹There are some differences in growth rates as not all council tax payers are connected to the water network and the discounts available to water customers are different from those available for council tax payers. These differences, which influence overall growth rates only negligibly, mean that overall growth rates of council tax payers are slightly below the growth rate of water customers.

council tax 'Band D equivalents' over the last 12 years. The number of 'Band D equivalents' is the total revenue from household customers divided by the 'Band D' charge – it is a way of converting households that may pay different bills into a standard measurement.

Table 4.1: Growth in Band D equivalents

	Number of Band D equivalent properties (thousands)	Percentage growth
1996-1997	1,794	-
1997-1998	1,807	0.7%
1998-1999	1,819	0.7%
1999-2000	1,837	1.0%
2000-2001	1,851	0.8%
2001-2002	1,868	0.9%
2002-2003	1,884	0.9%
2003-2004	1,901	0.9%
2004-2005	1,922	1.1%
2005-2006	1,943	1.1%
2006-2007	1,965	1.1%
2007-2008	1,988	1.2%

Over the period, the growth rate of Band D equivalents averaged around 0.9%. However, an annual growth rate of 0.7% has been assumed for each year covered by the review. This is the lowest annual growth rate observed over the period and is considered to be prudent given the current economic uncertainty. It is also lower than the around 1% per year assumed by Scottish Water in its business plan.

The customer bases that have been assumed for household water and household wastewater revenue purposes are set out in Table 4.2.

Table 4.2: Projections of household Band D equivalents

	Water		Wastewater	
	Number of Band D equivalents	Percentage change in Band D equivalents	Number of Band D equivalents	Percentage change in Band D equivalents
2007-2008	1,908,122	-	1,815,179	-
2008-2009	1,929,781	1.1%	1,834,654	1.1%
2009-2010	1,941,691	0.6%	1,846,087	0.6%
2010-2011	1,955,282	0.7%	1,859,010	0.7%
2011-2012	1,968,969	0.7%	1,872,023	0.7%
2012-2013	1,982,752	0.7%	1,885,127	0.7%
2013-2014	1,996,631	0.7%	1,898,323	0.7%
2014-2015	2,010,608	0.7%	1,911,611	0.7%

In adjusting Scottish Water's projections, only the projections for the revenue base were altered. The growth component of its investment proposals have not been adjusted. This means that the Commission is proposing to finance the addition of around 23,100 more household water properties over a four-year period and around 31,200 more over a five-year period than it has assumed will generate revenue for Scottish Water.

Projections of non-household premises

It is more difficult to establish historical trends for non-household premises than for household premises. Scottish Water's historic information was of poor quality and given the variable uses that businesses have for water, there is not a useful external information source.

The Commission remains concerned that Scottish Water's non-household customer base may be materially understated. It therefore intends to introduce a new incentive for licensed providers to locate non-household customers that are not presently being billed for water or wastewater services. This is further discussed below. However, the the impact of this has not been taken into account in the proposed charge caps, meaning that Scottish Water may be able to outperform.

Scottish Water projected in its second draft business plan that there would be three main impacts on its customer base after 2010. These are: large user volume decline, moderate growth in numbers of relatively low water users, and declines in revenue as a consequence of its compulsory metering programme. The Commission understands that Scottish Water has based its expectations on forecasts of changes in the economy and how these impact on water consumption.

Scottish Water's non-household customer base forecasts were used in setting charge caps. These projections are summarised in Table 4.3.

Table 4.3: Projections of non-household customer base

	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
Water						
Number of connected premises	120,838	120,779	121,526	122,197	122,776	123,133
Volume (MI)	155,482	155,691	156,254	156,770	157,260	157,675
Foul sewerage						
Number of connected premises	95,549	95,489	96,262	96,953	97,546	97,910
Volume (MI)	54,118	54,183	54,357	54,516	54,668	54,796
Surface drainage						
Surface and highway drainage RV (£m)	2,807	2,806	2,813	2,819	2,825	2,828
Trade effluent						
Number of connected premises	1,493	1,493	1,493	1,493	1,493	1,493
Volume (MI)	38,735	37,943	38,198	38,396	38,489	38,476
Impact of the above on Scottish Water's revenue base		-0.4%	-0.5%	+0.3%	+0.3%	+0.3%

4.3 Incentives on licensed providers

The Commission is concerned that not all non-household customers are registered with the Central Market Agency (CMA).² It therefore plans to introduce an incentive on licensed providers to locate customers that are not presently registered and to begin billing these customers for water and sewerage services.

The Commission will include firm proposals for this in its Final Determination. It will need to ensure that it does not inadvertently create an incentive for customers not to register with a licensed provider when they occupy premises. There are three ways that such an incentive might work, these are:

- linking the incentive to reasonable cost payments;
- reducing wholesale charges; or
- granting the licensed provider a time limited monopoly to serve the customer.

4.4 Summary

The Commission has made prudent assumptions in assessing Scottish Water's customer base, given the current economic uncertainty. These assumptions on changes to Scottish Water's customer base are included in the proposed charge caps. The Commission will shortly publish a consultation on how to encourage retailers to identify premises that are in receipt of a water and/or sewerage service but who are not currently being billed.

² The Central Market Agency administers the market and operational codes, calculates wholesale bills and registers switches of suppliers by customer.

