

CORPORATE PLAN

2021-27

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FOREWORD BY THE CHIEF EXECUTIVE

Welcome to our Corporate Plan, which sets out our commitments to customers, communities and other stakeholders for the period 2021-27. The plan explains how the Commission will contribute to the transformation that is beginning to take place in the Scottish water industry. The Commission is starting to embed a new regulatory approach, one founded on the principles of Ethical Business Regulation (EBR). We believe that the adoption by Scottish Water and all market participants of Ethical Business Practice (EBP), reinforced by our own move to an EBR approach, will enable the water industry to meet the challenges that lie ahead as effectively as possible, and to do so long into the future. The move will also support the industry as it sets out to deliver the common water industry vision, agreed by all stakeholders.

Scottish Water's Strategic Plan, published in February 2020, was a first step on the journey it will need to make as it seeks to achieve that common industry vision. Scottish Water must now develop a Transformation Plan that outlines the organisational and cultural changes that will be necessary if it is to deliver the long-term vision that it outlined in its Strategic Plan. As part of this, the onus will be on Scottish Water to explain how it will deliver the transformation and communicate this to its customers and communities.

The scale of the transformation required should not be underestimated: Scottish Water will have to more than double its average annual level of investment, become more customer and community centric, and achieve net zero emissions on both its operational and embedded carbon footprints. Perhaps most importantly, Scottish Water should be proposing to its regulators, and to the customers and communities it serves, solutions to potential issues ahead of any concerns ever arising. As such, a robust and ambitious plan will be essential if Scottish Water is to achieve the Scottish Ministers' expectations for the water industry for the future.

As part of its journey it will be necessary for Scottish Water to transition to an EBP approach. This will ensure that the business achieves genuine ownership of its relationship with – and responsibility towards – its customers.

For the Commission the move to EBR will entail a transformation of our own. To support this, the Commission Board has agreed a revised strategy.

The strategy reflects the context in which we are operating and places emphasis on implementing a framework that enables long-term thinking and planning; supports the sector to deliver a world-leading service for customers and communities; and places our work at the cutting edge of economic regulation. This Corporate Plan puts that strategy into effect.

Building on our revised strategy and in preparing this Corporate Plan, we have considered how best to structure our business activities. In particular we recognise that EBR will require the introduction of new approaches, some of which demand new skills. We will continue to invest in the professional development of our staff and to maintain our culture of continuous improvement. We have also determined that the collaborative and flexible ways in which we already work should be more closely reflected in our Corporate Plan.

In the past three years, the Commission has supported the Scottish Government's Hydro Nation Initiative. The income earned contributes towards keeping our costs to customers in Scotland as low as possible. Our work on Hydro Nation projects has provided wider benefits too – for example, offering excellent learning experiences for staff, particularly for those at the start of their career. The work also supports recruitment and retention of key staff, thereby helping us to regulate the water industry in Scotland more effectively.

To implement this Corporate Plan, we will need to continue to attract and retain inquisitive individuals from diverse backgrounds who share a desire to do the best for the industry's customers and communities. For this reason, an important element of the Corporate Plan is our enhanced graduate training and development programme.

In closing, and on behalf of the Water Industry Commission for Scotland, I would like to take this opportunity to thank our wide-ranging water industry stakeholders here in Scotland, in the rest of the UK, and internationally. We look forward to continuing to work together in the forthcoming regulatory control period.

ALAN D A SUTHERLAND
Chief Executive

7 December 2020

1 INTRODUCTION

About this document

This Corporate Plan explains our strategic objectives; the outcomes we are setting out to achieve for customers, communities and other stakeholders; the activities we will need to undertake to deliver these outcomes; and the resources that will be necessary. We also explain how we will structure the way we work so that we are as efficient and effective as possible.

The Commission Board will use the Corporate Plan over the forthcoming regulatory control period to monitor progress against the commitments in the plan. We will also report progress against a more detailed annual work plan in our annual report.

The Corporate Plan aligns with the next regulatory control period, covering the period 2021-27.

Our role

The Water Industry Commission for Scotland was formed on 1 July 2005 under the Water Services etc. (Scotland) Act 2005.

In summary, our statutory duties are to:

- promote the interests of Scottish Water's customers and, in so doing, to have regard to the interests of future customers;
- ensure that customer charges reflect the lowest reasonable overall cost for Scottish Water to deliver the Scottish Ministers' Objectives;
- comment on Scottish Water's reporting of its performance, challenging Scottish Water to become more efficient and sustainable;
- facilitate the entry of retail water and sewerage providers that wish to supply non-household customers in Scotland; and
- support the Scottish Government's vision of ensuring that Scotland is a Hydro Nation, and to meet our obligations under the Water Resource Act 2013.

Accountability

We are accountable, through the Scottish Ministers to the Scottish Parliament and, ultimately, to water and sewerage customers in Scotland. We achieve this accountability by being transparent about our work, by engaging and consulting with others, and by reporting progress against the commitments in our Corporate Plan in our annual report (which is laid before Parliament).

The Commission has a Board consisting of four non-executive board members and the Chief Executive. The Scottish Ministers appoint the non-Executive members of the Board. The Board appoints the Chief Executive. The Board's role is to oversee the governance of the organisation and its strategic direction. The Board is supported in its work by an Audit and Risk Committee.

2 CONTEXT WITHIN WHICH THIS CORPORATE PLAN IS SET

Our approach to date

We are publishing this Corporate Plan at a key moment in the development of regulation of the Scottish water industry. Not only are we preparing for the start of the next regulatory control period (2021-27), but we are also taking steps to ensure that the industry is properly equipped to address the significant challenges ahead and to deliver the Scottish Ministers' vision for the industry.

In response to these challenges the industry has jointly agreed to move to a new and very different regulatory approach, founded on behaviours that are in line with the principles of EBP, underpinned by a regulatory framework that aligns with the principles of EBR.

Within this context the Commission Board has reviewed its strategy and as a result developed and agreed new strategic objectives for the forthcoming regulatory control period.

Before we look ahead to how we will deliver these objectives, it is helpful to take stock of what has been achieved since economic regulation was introduced in the Scottish water sector in 1999. During this time, we have provided critical external challenge and scrutiny of Scottish Water's performance and charges. We have also set fixed charge controls based on our forward-looking assessment of the efficient level of expenditure required to deliver the Objectives set by the Scottish Ministers within their Principles of Charging.

By limiting its cash budget, Scottish Water has had a strong incentive to operate efficiently. This, aligned with stringent performance targets, has delivered significant benefits to Scottish customers.

- Scottish Water's service quality performance has more than tripled since 2002.
- Its customer service and operational efficiency are at least as good as the leading water companies in England and Wales.
- Household bills have fallen by 9% in real terms since 2002 – compared with an average increase of 11% in England and Wales. (The range in England and Wales is from a decrease of 2% to an increase of 24% in real terms.)

A changing environment

As we look to the future, however, it is clear that the sector faces new challenges. In undertaking our duties, we must take this into account as they affect, and will continue to affect, the industry:

- The economic impact of the COVID-19 pandemic will continue to affect businesses and households across Scotland for some time (leading to higher than expected levels of unemployment, poverty and business failures). The pandemic has already resulted in delays to Scottish Water's investment delivery during the current 2015-21 regulatory period, and it appears inevitable that there will be a higher than expected 'carry over' of projects into the next regulatory period. The pandemic will also affect Scottish Water's financial position as well as having significant and wide-ranging impacts on the Scottish economy and on growth. The extent and duration of all of these impacts are difficult to forecast with any accuracy at this stage.
- The water industry will have a vital role to play in helping deliver net zero emissions by 2045, the target declared by the Scottish Government in response to the climate emergency. Scottish Water has a substantial operational and embedded carbon footprint and has been set a highly demanding target by Scottish Ministers to achieve net zero by 2040. The Scottish Ministers have also required Scottish Water to increase the generation of renewable energy that it hosts from double to treble its actual use of energy.

- In future Scottish Water will need to operate, invest in new assets and refurbish and replace its existing assets in an economically optimal way (in other words, in a way that takes account not only of the cash costs, but also of the wider costs and benefits to society and the environment). This will be essential to maintaining service and helping Scottish Water achieve its net zero target. Jointly with Scottish Water we have undertaken innovative work which has identified that expenditure on asset replacement may eventually have to increase three-fold from current levels. Over the next decade there will be a need to replace many shorter life assets that were installed to improve water and wastewater compliance.

These long-term investment and performance outcome challenges are different from those of the past and will require a transformation in the way we approach regulation. They will also require Scottish Water to take full ownership of its strategy and be able to evidence to its customers and communities that it is delivering efficiently and effectively. A cash-based approach constrained by fixed, six-year price settlements is no longer fit for purpose.

Supporting the sector vision

To address the challenges facing the sector, and make the most of opportunities for excellence and shared learning, stakeholders have developed and now own a common industry vision: that the Scottish water sector will be “admired for excellence, secure a sustainable future and inspire a Hydro Nation”. This followed the call from the Cabinet Secretary for Environment, Climate Change and Land Reform for the industry to create a common understanding of what the sector should seek to achieve over the next three decades.

The vision was developed through a collaborative process involving a group that encompassed WICS, Scottish Water, Citizen’s Advice Scotland, the Customer Forum, the Scottish Environment Protection Agency and the Drinking Water Quality Regulator.

The sector vision

- Together we will support the health and wellbeing of the nation. We will ensure that all of Scotland gets excellent quality drinking water that people can enjoy all of the time. Scotland’s waste water will be collected, treated and recycled in ways that generate value and protect the environment. We will enable the economy to prosper.
- We will transform how we work to live within the means of our planet’s resources, enhance the natural environment and maximise our positive contribution to Scotland achieving net zero emissions.
- We will involve and inspire Scotland’s people to love their water and only use what they need. We will promote access to the natural environment and encourage communities to enjoy and protect it.
- We will be agile and will collaborate within the sector and with others to be resilient to the challenges that will face us. We will keep services affordable by innovating and delivering the greatest possible value from our resources, helping those who need it most. We will serve all customers and communities in a way that is fair and equitable to present and future generations.
- We are a vital part of a flourishing Scotland.

This is the first time in the industry’s history that a common vision has been owned by all stakeholders – marking new, collaborative ways of working between Scottish Water, its regulators and others.

Our strategy is focused on how, in a manner consistent with our statutory duties, we can support the sector to deliver this vision.

3 OUR STRATEGY

As we reach the closing stages of the current Strategic Review of Charges, and given the wider context in which we are operating (as set out in section 2), the Commission’s Board took time last year to refresh its strategy. Underpinning the strategy was an acknowledgement that there is substantial value from moving to more flexible, transparent and collaborative ways of working and making decisions.

Our strategic objectives

Through a series of workshops and discussions, the Board identified the following strategic objectives:

- To support the sector to achieve its long-term vision and the Scottish Ministers’ Objectives for the regulatory control period.
- To challenge Scottish Water to achieve best in class levels of service for its customers and communities.
- To become an international leader in the field of economic regulation.

These objectives are focused on ensuring that we continue to meet our statutory obligations to current and future customers. They will also ensure that we contribute fully to the delivery of the industry vision (including the ambition to develop Scotland as a Hydro Nation). This is particularly important given the need to achieve net zero emissions by 2040 and to maintain service levels by repairing, refurbishing and replacing the industry’s assets in a timely way.

Developing a new regulatory approach

Having considered a number of potential approaches to help the sector address the long-term challenges it faces, and to address the limitations of the current regulatory model (including a focus on the short term), we believe that the most appropriate regulatory model going forwards is one based on the principles of EBP and EBR. Over the past 18 months or so we have been working with the Scottish Government, Scottish Water and other industry stakeholders to establish the necessary conditions for EBR and to start the transition. Fully embedding EBR and EBP will take time.

Developing trust and confidence between Scottish Water, the licensed providers, customers and stakeholders lies at the heart of EBR. Its key elements can be summarised as follows:

- Businesses should continually demonstrate evidence of their commitment to fair and ethical behaviour that will support the trust of regulators and enforcers, as well as of all levels of management and employees, customers, suppliers, investors and stakeholders.
- Regulatory systems need to have clear rules or expectations and be based on collaboration if they are to support an open, balanced and altruistic regime, as well as maximising performance, compliance and innovation.
- Where there is unethical behaviour, people expect a proportionate response. This is consistent with strong sanctions for intentional wrongdoing.

We have adopted the principles of EBR before Scottish Water has had the necessary time to implement EBP fully. A key focus for the period covered by this Corporate Plan will be on ensuring that Scottish Water demonstrates to customers, communities and stakeholders how it will transition to EBP through the development and implementation of its Transformation Plan.

Finally, it is worth noting at this point that implicit within our EBR approach is the commitment, on our part, to act in a way that is fully in line with the principles of EBP.

4 HOW OUR WORK DELIVERS FOR CUSTOMERS AND COMMUNITIES

Each of the three strategic objectives is underpinned by three outcomes (see Table 1). The nine outcomes encompass all strands of our work. The activities and resources set out in later sections of this Corporate Plan will be used to deliver these outcomes.

There are clearly many interactions across and between the outcomes, and the delivery of one outcome will frequently support the delivery of another. It is also the case that the outcomes will naturally evolve as customers' expectations, Scottish Government policy and our approach to regulation evolve.

We provide more information about each of the nine outcomes below. Section 5 details the activities we will deliver in order to achieve the outcomes.

For each outcome we provide a key performance indicator (KPI), which we will use to measure success. There are 11 KPIs. Underpinning these KPIs is a single KPI that relates specifically to the progress we make in delivering our annual work plan against all outcomes. We will report performance against this KPI in our annual report.

The KPIs reported here are new and therefore may need to be amended or strengthened in the light of experience of their effectiveness. We will report any changes in our annual workplan as the Corporate Plan period progresses.

KPI 1: By February of each year of the Corporate Plan period, we will set out in an annual workplan the activities which we will undertake during the year. In the following year our Annual Report will include information on progress against our workplan.

Table 1: Our strategic objectives and the outcomes we will deliver

Our strategic objectives		
<p>Strategic objective 1</p> <p>To support the sector to achieve its long-term vision and the Scottish Ministers' Objectives for the regulatory period.</p>	<p>Strategic objective 2</p> <p>To challenge Scottish Water to achieve best in class levels of service for its customers and communities.</p>	<p>Strategic objective 3</p> <p>To become an international leader in the field of economic regulation.</p>
The 9 outcomes we will deliver		
<p>1</p> <p>Supporting Scottish Water to be sustainable over the long term.</p>	<p>4</p> <p>Supporting Scottish Water to become an analytically driven organisation that takes full account of benefits and costs in its option appraisals and decisions.</p>	<p>7</p> <p>Acting as a cutting edge regulator that contributes to developing Scotland as a Hydro Nation.</p>
<p>2</p> <p>Incentivising an efficient and effective Scottish water.</p>	<p>5</p> <p>Acting as a hub of information and expertise to support decision making.</p>	<p>8</p> <p>Ensuring that the office operates as efficiently and effectively as possible.</p>
<p>3</p> <p>Helping ensure that the retail market maximises benefits for customers.</p>	<p>6</p> <p>Promoting customer-centric decision making.</p>	<p>9</p> <p>Sustaining a high-performance team, with a focus on continuous improvement.</p>

Outcome 1: Supporting Scottish Water to be sustainable over the long term

Description

To achieve a water sector that is sustainable in the long term requires Scottish Water to take ownership: doing the right thing for customers and communities, at the right time, and for the right reasons.

Our role is to put in place a regulatory framework that enables Scottish Water to do this. This entails giving Scottish Water the time and space it needs to transform itself as an organisation. We believe that such an approach is the best way to deliver the industry vision and to meet our statutory duty to protect the interests of both current and future customers – as long as Scottish Water is able to grasp the opportunity that the new regulatory approach represents. This is therefore one element of this outcome.

Another element is ensuring that Scottish Water is appropriately funded to protect service levels for customers today and in future generations. Investment will need to be appropriately targeted and timeous if the sector is to achieve and sustain net zero emissions. By way of example, by 2027, 40% of the time available to achieve net zero emissions will have elapsed. Scottish Water should therefore be determined to be more than 40% towards its net zero emissions target by this stage given that the last steps towards net zero are likely to be the most difficult.

In making decisions we must:

- ensure that Scottish Water has the resources it needs to make the investment necessary to protect service levels and to replace assets in an economic and efficient way, while ensuring that customers pay no more than is necessary; and
- determine an appropriate balance of charges between current and future customers.

Our analysis suggests that current levels of investment in the assets are below the level that is likely to be required in the long term. Furthermore, there is a clear need to adopt a longer term, more flexible approach to maintaining and replacing the assets. The resilience of the industry and of the services it provides to customers and communities depends on getting this right.

Future priorities

Our main priority will be to ensure that the regulatory framework supports Scottish Water as it develops and implements its Transformation Plan. We expect to maintain an open and constructive dialogue with Scottish Water and will set out our views consistently, including our rationale and the evidence that supports our thinking.

To support the new approach to investment we will also focus on developing our understanding of:

- the industry's long-term investment requirements;
- how investment should be prioritised; and
- the funding required.

As part of this work we will place greater emphasis on our review of Scottish Water's investment appraisals, which should take full account of all of the costs and benefits, not just those that are easily valued in monetary terms. We will also need to be able to draw on better information about the assets and on improved asset management.

We will continue to look outwards at other sectors and industries, bringing best practice back to apply in Scotland, and supporting Scottish Water to implement its Transformation Plan.

How we will measure success

Our success in delivering this outcome will be measured by the following KPI:

KPI 2: We will implement a regulatory framework that enables and supports Scottish Water to take full ownership of its relationship with customers and its decision making. We will report annually to the Board, and in our statutory annual report and accounts, on progress.

To measure success in this area we will ensure that Scottish Water and other stakeholders periodically have the opportunity to identify and suggest amendments to the Commission's regulatory framework and publish the outcome.

Key risks

- If we are unable to engage positively with stakeholders on the benefits of the new regulatory framework then it will not be possible to implement the approach fully.
- If Scottish Water does not take ownership of its transformation then it is unlikely to deliver the sustainable industry vision, including the net zero emissions and asset replacement challenges.

Dependencies

- Scottish Water meeting the milestones set out in the development and implementation of its Transformation Plan.

Control measures

- Regular review of, and commentary on, Scottish Water's reporting of its progress against the milestones in the Transformation Plan.
- Regular engagement with Scottish Water, the Scottish Government and industry stakeholders to understand perceptions of Scottish Water's progress and to identify and raise any issues arising at an early stage.

Outcome 2: Incentivising an efficient and effective Scottish Water

Description

Customers rightly expect Scottish Water to be as efficient and effective as possible and, as a result, to deliver increasingly better value for money. To date we have made sure this is the case by setting Scottish Water tough but credible targets for efficiency. We have then monitored and reported on performance based on the detailed annual data we have required Scottish Water to submit.

Scottish Water has already been through a significant transformation, one that was initiated at its creation in 2002. This saw both year-on-year operating performance improvements and increases in the level of service such that Scottish Water's performance is now in line with that of the best performing companies in England and Wales.

Yet a further transformation is required if Scottish Water is to deliver its net zero emissions target by 2040 in an effective and efficient way. This arguably represents an even greater challenge than the one the business has already overcome.

We are working with Scottish Water as it embraces EBP. Through this change in approach Scottish Water must take ownership for:

- setting its own targets;
- outlining the steps it will take to meet these targets; and
- reporting performance (both the good and not-so-good) to its customers and communities in a transparent and accessible way.

This is very different from the traditional approach of responding to the regulator's demands.

Future priorities

As Scottish Water transitions to a fully EBP approach its customers will still want to have confidence that the company is continuing to seek opportunities to make its operations more efficient and effective.

Our main priority for 2021-27 will therefore be to focus on commenting strategically on Scottish Water's performance reporting and on offering constructive feedback.

This will require us to undertake an increased level of engagement with stakeholders so that we understand their perceptions of Scottish Water's performance and can gauge the level of trust that exists within the industry.

To put its performance into context we will also need to understand how well Scottish Water's performance compares with that of the water companies in the rest of the UK and internationally. We will therefore prioritise looking outwards at other sectors and industries, understanding the potential for further improvement that could be realised in the Scottish water industry.

Ensuring that Scottish Water operates as efficiently as possible is essential to delivering the objectives of the Scottish Ministers in an as affordable way as possible.

How we will measure success

Our success in delivering this outcome will be measured by the following KPI:

KPI 3: By November of each year we will publish our annual reports on Scottish Water's overall performance in delivering the requirements set out in the 2021-27 final determination and identify any gaps that have the potential to impact on the level of trust among its stakeholders.

We will do this by engaging with Scottish Water's stakeholders and by keeping Scottish Water's progress under review. Our assessment of the reporting framework will be set out in a comprehensive annual performance report.

Key risks

- If Scottish Water does not report its performance in an open and transparent manner, then this will erode trust, which in turn could lead to a focus on short-term assurance.
- If we are unable to analyse and benchmark Scottish Water's costs, through either its failure to supply timely information or a loss of our analytical capacity, then we will not be able to comment in a strategic and constructive way on performance.
- If we fail to engage with wider stakeholders, then we will not develop a holistic view of Scottish Water's performance.

Dependencies

- Scottish Water adopting EBP and taking ownership of its transformation.
- Scottish Water reporting its performance comprehensively.
- WICS undertaking effective horizon scanning.

Control measures

- Increase the frequency of stakeholder engagement and ensure that this is at Board level, executive level and senior management level.
- Provide constructive feedback to Scottish Water as part of a 'no blame' culture.
- Integrate our horizon scanning activities more fully within the office.

Outcome 3: Helping ensure that the retail market maximises benefits for customers

Description

The competitive retail market for water and sewerage services in Scotland opened in April 2008. The market is for all non-domestic customers in Scotland, including businesses, public sector bodies and members of the third sector. Thirty providers are licensed in the Scottish market, serving around 160,000 non-domestic customers, with an annual gross value of c.£350 million.

Much of our activity to date has been to manage new licence applications and support the implementation of the Scottish Government's principles of charging. This includes changing the charging arrangements for vacant properties and transitioning to more up-to-date rateable values as the basis for charging unmetered services. More recently we undertook a comprehensive review – involving extensive engagement and consultation – of the retail market; we are now in the closing stages of the process to update the market framework arrangements. These changes will ensure that the market continues to be fit for purpose, to deliver benefits to customers, and to work well for market participants.

Future priorities

In addition to continuing to oversee the steady functioning of the market arrangements, our priorities for 2021-27 are as follows:

- To support the licensed providers to embed the principles of EBP in their businesses and in their interactions with customers, other providers, the Commission and stakeholders. This will require them to demonstrate their commitment to open, fair and honest behaviours.
- To ensure that the lessons of the COVID-19 pandemic are learned and that licensed providers are financially resilient to shocks.
- To improve the transparency of the information that is available to customers, so that they are able to make informed choices.
- To ensure that the market contributes to the industry's common vision and the achievement of the net zero target.

How we will measure success

Our success in delivering this outcome will be measured by the following KPIs:

KPI 4: Working with licenced providers, we will seek to put in place by December 2024 effective measures which ensure that all licensed providers have appropriate financial resilience.

Our annual report will comment on the effectiveness and resilience of the market arrangements.

KPI 5: By April 2023 we will introduce a voluntary market-wide process that allows licensed providers to demonstrate behaviours consistent with EBP.

Working with the licensed providers, we will aim to establish this process by April 2023. We will use the Scotland on Tap website to report on progress.

Key risks

- If a licensed provider suffers financial failure, then this may cause a detriment to Scottish Water and adversely impact on Scottish customers.
- If non-household customers are not sufficiently engaged in the opportunities available from the retail market, then they will not receive the benefits the market offers.

Dependencies

- The licensed providers adopting EBP principles and engaging in an open and honest manner with customers, the Commission and other stakeholders.
- The licensed providers embracing the planned market health checks.
- Control measures
- Review the financial resilience of licensed providers and consider further measures to protect the integrity of the market.
- Develop an engagement plan with the licensed providers on the journey to adopting EBP principles.

Outcome 4: Supporting Scottish Water to become an analytically driven organisation that takes full account of benefits and costs in its option appraisals and decisions.

Description

As part of SRC21 the Commission adapted the regulatory framework to move away from a fixed investment programme for the regulatory period. This change enables Scottish Water to plan and to prioritise its investment programme in a more dynamic way, thereby ensuring maximum long-term value.

Planning and prioritising in a way that maximises the trust of stakeholders requires Scottish Water to develop and clearly explain a benefits framework that quantifies the consequences and impacts of each of its decisions.

Future priorities

Scottish Water has historically defined upfront the areas requiring investment over the regulatory period, supported by a broad allocation of costs. This process has placed an undue short-term focus on ensuring that outputs are added to the list of investments and delivered using a lowest cost engineering approach.

An ongoing process for planning and prioritising investment allows Scottish Water more time to understand the investment needs for each system of assets over the long term. It will allow Scottish Water to assess all financial and non-financial costs and benefits of each investment while allowing for ongoing engagement with customers and communities, so their views are listened to and incorporated into the decision-making process.

As such, our first priority will be to work with Scottish Water as it develops the way in which it prioritises and appraises investment to ensure that all costs and benefits are integrated and monetised in a transparent manner. This will help ensure that Scottish Water gets best value for every pound of customers' money that it spends.

Although quantifying and costing the impact of carbon will be the immediate focus given Scottish Water's net zero emissions target, this work extends to all social, environmental and financial benefits and externalities. This will form a key element of our involvement in the new Investment Planning and Prioritisation Group (IPPG) process.

How we will measure success

Our success in delivering this outcome will be measured by the following KPI:

KPI 6: Our annual reports on Scottish Water's overall performance will include an assessment of its progress in ensuring that project appraisals encompass a full assessment of the economic costs and benefits of investment. This assessment should include aspects such as the carbon impact, and of natural and social capital.

Key risks

If Scottish Water fails to respond appropriately to our engagement in this area, then it will be unable to realise the benefits of becoming an analytically driven organisation.

Dependencies

- Scottish Water's ability to make optimal decisions based on rigorous analysis of all of the relevant costs and benefits.
- Scottish Water's ability to evidence all of the relevant costs and benefits.

Control measures

- Scottish Water's key milestones during the development, and in the implementation, of its Transformation Plan.

Outcome 5: Acting as a hub of information and expertise to support decision making

Description

As economic regulator, we are asked to provide analytical assistance and/or advice drawing on our expertise in economics, regulation, commercial strategy, asset management and the water industry more generally.

Examples include:

- analysis on policy areas such as charging policy for the retail market; and
- analysis on the Scottish Government's assistance measures to respond to the COVID-19 crisis.

In the spirit of EBR, we believe that we have an important role to play in sharing our expertise; doing so will ultimately secure better outcomes for customers and the environment in the water sector in Scotland.

In line with the Scottish Government's Hydro Nation programme, we also recognise that effective governance and regulation of the water industry can have a real impact on people's lives and wellbeing. It is therefore important that we share information and expertise on economic regulation with our international partners wherever possible (see Outcome 7 below).

Future priorities

Looking forward, as the industry starts its journey towards realising its ambitious vision, we anticipate that the need for such information and expertise will increase. We are therefore seeking to put our role as a hub of information and expertise on a more formal footing.

We also need to continue building our corporate knowledge and expertise so that we can provide valuable contributions. Our future horizon scanning and Hydro Nation work is essential in this regard.

Performing this role provides much wider benefits in terms of developing and retaining our people and ensuring that effective succession planning takes place across our organisation (see Outcome 9, below). This occurs, for example, through providing opportunities to conduct analysis in interesting areas (such as rural development) and by working collaboratively with industry stakeholders and international partners.

How we will measure success

Our success in delivering this outcome will be measured by the following KPI:

KPI 7: We will report annually on requests for regulatory advice and information and expertise from industry stakeholders and international partners, and on the nature of support we have provided.

Key risks

- If we do not have the resources we need (in terms of information, knowledge or capacity) to support advice and requests then we may not be able to provide effective support and our reputation could be adversely impacted.

Dependencies

- Scottish Water reports its performance comprehensively (for example through the Annual Return, Regulatory Accounts and other submissions).
- We continue to update and maintain our UK-wide and international information databases.
- We attract and retain talented analysts to ensure that we have capacity to provide such support.

Control measures

- If necessary, and in line with an EBR approach, use our powers to request information that Scottish Water has not provided through its reporting.
- Position ourselves as an employer of choice by providing opportunities for training, development and progression.

Outcome 6: Promoting customer-centric decision making

Description

We have a statutory duty to promote the interests of all customers, whether they are households or non-household customers, and current or future customers.

Our regulation in line with EBR principles will provide both Scottish Water and the licensed providers the time and space they need to engage and listen to customers and communities. We will continue to make sure that, as the industry adopts EBP and takes ownership of its decisions, this is done in a way that is in the best interests of customers.

EBR follows on from and responds to the adoption of EBP by the companies or entities subject to regulation. As noted previously, implicit within the EBR approach we are taking is the assumption that we will adhere to the principles of EBP in our own behaviour.

Future priorities

Our primary focus will be to support Scottish Water as it transforms the way in which it works with customers and communities, to ensure that its investment decisions maximise long-term customer value.

This includes supporting the business as it develops its approach to engaging with customers as it further understands investment needs and appraises investment. Customer views should have as much authority as the more traditional engineering input.

The outcome of this approach is that customers can have confidence that what is being done reflects their priorities. To be clear, this is not about undertaking more or better-quality research; rather, it is about living the community view, ensuring that decisions are taken having given proper regard as to what customers and communities would think. This encompasses their views not only on what is to be delivered or how it is to be delivered, but on the process that was adopted to allow these decisions to be taken.

We also expect licensed providers to take ownership for high standards of conduct with their customers and to act in an open and honest manner with stakeholders at all times. This involves upholding their customer service commitments and communicating these in a clear and transparent way. We expect licensed providers to take individual and collective responsibility for an appropriately functioning market and to work collaboratively together, subject to competition rules, to ensure that the market continues to work in the best interests of customers.

How we will measure success

Our success in delivering this outcome will be measured by the following KPI:

KPI 8: Our annual reports on Scottish Water's overall performance will include an assessment of its progress in ensuring that customers and communities are involved in decision making. This will encompass assessing the extent to which customers could reasonably have confidence that their views are being heard and acted upon.

We will achieve this by working closely with representatives of Scottish Water's customers.

To measure our success in this area we will ensure that customer representatives periodically have the opportunity to identify and suggest amendments to the Commission's regulatory framework. We will also publish the outcome of our review.

Key risks

- If Scottish Water and licenced providers do not engage appropriately with customers and communities, the customer and community view will be less well reflected in future government policy and service levels will likely fall short of what could be achieved.
- If the input from customers is skewed towards a vocal minority, then decisions may not be in the overall customer interest.

Dependencies

- The ability and desire of each company to operate under EBP.
- The ability of each company to understand customers on an ongoing basis and for these views to influence decisions.

Control measures

- Work with Scottish Water to develop a strategic assurance process of customer and community involvement.
- Undertake an engagement programme with licensed providers to ensure they embed the EBP principles.

Outcome 7: Acting as a cutting-edge regulator that contributes to developing Scotland as a Hydro Nation

Description

We support the Scottish Government's Hydro Nation initiative, which is setting out to build partnerships, share knowledge and expertise, to develop relationships and to undertake joint research. The aim in doing so is to use Scotland's reputation and expertise internationally in order to improve global water management.

We have already delivered a number of highly successful projects through our Hydro Nation work, collaborating with economic regulators and government agencies in Europe and more widely. Initial projects often lead to further requests for support and to date this has been the case in both Romania and New Zealand.

Our activities involve assisting international partners to build capacity and develop strong leadership and expertise. We do this by developing appropriate information framework and analytical capabilities, and by delivering bespoke training programmes to senior management.

It should be noted that our involvement in Hydro Nation work has not been to the detriment of the role we undertake in Scotland; rather, it provides a number of real benefits that ensure that we are a more effective regulator of Scottish Water.

Our involvement helps ensure that we stay at the forefront of regulatory best practice and promote the Commission's international reputation by acting as an independent adviser and critical friend. Our participation in international projects also provides development opportunities to members of staff, bringing valuable insights, contributing to the office's learning and supporting staff recruitment and retention. In addition, our Hydro Nation activities provide analytical work that provides meaningful training and professional development for all of our trainee analysts, helping them learn much faster than they would otherwise have done. Finally, while some of our work is provided on a pro-bono basis, much of it is charged for – bringing in additional income to the Commission. The levy that we receive from licensed providers and from Scottish Water is lower as a consequence of our Hydro Nation activity.

Future priorities

Our international work has grown organically, based on the connections and contacts we have made to date. Looking ahead, there is a clear opportunity for us to:

- formalise and restructure our approach to identifying and selecting opportunities;
- develop a stakeholder management plan and engage in a proactive way to communicate our successes;
- pursue further growth in this area.

We plan to target up to four countries, in accordance with our Hydro Nation strategy criteria, where we will focus our efforts to establish a pipeline of future projects. This is likely to include Romania and New Zealand (where we have already completed successful projects and have developed strong relationships), along with two other countries (potentially from within eastern or central Europe). There may also be opportunities to work as part of a consortium on Hydro Nation activities in future.

In addition, we have started to discuss with the Scottish Government whether or not there would be benefits in the Commission establishing a separate division of WICS, 'WICS international', as the natural progression of the work we have done to date. This would ensure transparency of reporting and robust governance arrangements of our international activities.

How we will measure success

Our success in delivering this outcome will be measured by the following KPI:

KPI 9: We will support the Scottish Government's Hydro Nation initiative by delivering projects and assistance, providing a minimum annual net contribution to our income from this work of £300,000.

We will achieve this by assisting international partners through training and by offering appropriate information framework and analytical capabilities; we will also recover the full costs of our activity.

We will measure our performance in this area by the volume of activity we are invited to be involved in. If we generate a contribution to costs that is in excess of that included in our budget, we will either rebate this surplus to Scottish Water and the licensed providers or will support other Hydro Nation activity of the Scottish Government (for example, its work in Malawi).

Key risks

- If the costs we incur in undertaking international activities are not recovered, then this could be to the detriment of Scottish customers.
- If our international activities are not properly appraised, well managed and resourced then this could have a negative impact on our other core functions.

Dependencies

- Have access to a talented and skilled pool of analysts to support our Hydro Nation activities.
- Maintain our reputation as a leading economic regulator by horizon scanning for best practice within the global water industry.

Control measures

- Governance and assurance arrangements to ensure full recovery of costs incurred in Hydro Nation activities, including overheads and business development costs.
- Appropriate project and resource management for international projects to ensure that the Commission uses resources effectively and efficiently and to allow equal access to learning opportunities for members of staff.
- Limited budgeted revenue from Hydro Nation activity.

Outcome 8: Ensuring that the office operates as efficiently and effectively as possible

Description

With a staff of 24 people we are responsible for regulating an industry with an annual turnover of more than £1.2 billion that provides a vital service to the people and economy of Scotland. We carry out our role at a cost of around 37 pence per person in Scotland each year.

As a public body we are very conscious of our obligations to deliver value for money. We monitor our expenditure with care, and by maintaining robust financial authorisation, expenditure scrutiny and procurement processes, we ensure maximum cost effectiveness. We review the way in which we achieve our objectives on an on-going basis to ensure that the results of our spending are as targeted and effective as possible. In doing so, we look to learn lessons from other analytical and regulatory processes in other industries and jurisdictions.

Future priorities

We continue to seek ways to be as efficient and effective as possible. Our experience of remote working during the COVID-19 pandemic has allowed us to develop our thinking on how staff might work more flexibly, in ways that maximise our efficiency. We are also focused on taking all opportunities to minimise our environmental impacts by allowing for more flexible travel arrangements and reducing the need for a large office.

In line with our strategic objectives, we intend to expand our international work in a way that provides cost benefits for water customers in Scotland through earning revenue that makes a meaningful contribution to office overheads.

How we will measure success

Our success in delivering this outcome will be measured by the following KPI:

KPI 10: We will ensure that our income and costs remain within budget targets over the regulatory control period and will report our financial performance on a regular basis to the Commission Board.

To deliver this we will ensure that appropriate cost benefit analysis is carried out in procurement, including in securing consultancy resources. We will also seek to outperform wherever possible and in so doing seek to return excess finances to Scottish Water and licensed providers. Finally, we will make sure that our Hydro Nation activities make a positive financial contribution to the costs of the office.

Key risks

- If we do not control our office costs carefully then we will not meet our financial targets, resulting in an overspend and a reduced ability to deliver the objectives.
- If the office is not structured appropriately to meet the opportunities and challenges presented by the strategic objectives, then we will be unable to deliver the Corporate Plan.

Dependencies

- The budget set for the Corporate Plan period is sufficient to meet the strategic objectives.
- The income from Scottish Water, licenced providers and Hydro Nation activity is in line with expectations.
- Our proposals to restructure the office to meet the strategic objectives are able to proceed as planned.

Control measures

- Maintain the Commission's comprehensive financial control mechanisms, including internal approval mechanisms, the oversight of the Commission Board and the Audit and Risk Committee on financial performance, and the internal and external audits.
- Executive oversight of progress with delivering the office structure plans to meet the strategic objectives, including through monitoring progress with the office KPIs.

Outcome 9: Sustaining a high-performing team, with a focus on continuous improvement

Description

One of our biggest challenges in delivering our objectives is to make sure that we are able to attract and retain the best talent and that our employees have the skills and expertise they need. As we transition to the EBR approach and develop our international work further we need to ensure that our pool of high-quality analytical and corporate talent is maintained.

In particular, in recent years it has sometimes been difficult to attract high-quality graduate applicants and to retain graduate analysts for more than two years. Our corporate team is more established but will benefit from ongoing training and development.

Future focus

Our activities in this area will focus on ensuring that we have the right people, skills and experience in place to deliver our overall strategy and objectives now and in the future. This will involve succession planning at all levels in the organisation and an ongoing commitment to training and development of staff. In particular, the transition to EBR will require staff development across the office.

A key element of this will be improving our graduate offering. It is important that we are seen as an attractive and supportive place for graduates to begin their careers. To promote the Commission as a first-choice graduate employer, we will further develop our graduate offering so that it comprises a structured training and development programme. Our offer will also include competitive remuneration, a package of wider benefits, and opportunities to work internationally.

To support our recruitment strategy, and as a key component of our communications strategy, we will invest in more extensive recruitment marketing. We are also developing our corporate website so that it more fully reflects the interesting and rewarding work that we do.

Our aim is to increase the volume of high-quality applications we receive each year, so that we are ultimately able to build a permanent analytical team of 10-12 people. We should see a consistent stream of new recruits being enrolled into our development programme and an increasing number of recruits staying for four years or more. In the longer term, the intention is that this programme will support our succession planning. We will also continue to invest in the professional development of our staff. This is something we believe is very important as it ensures the continuous improvement of the office, enables employees to achieve all that they are capable of, and helps them develop new skills and expertise.

How we will measure success

Our success in delivering this outcome will be measured by the following KPI:

KPI 11: We will achieve the desired structure for the office by 2025 and ensure that progress remains on track in the interim.

Key risks

- If we do not develop or invest in our staff training needs, then we will be unable to retain them.
- If we do not engage with universities and participate in graduate fairs, then we will be unable to attract graduate recruits or remain competitive with graduate programmes offered by others.

Dependencies

- High-quality training and development programmes with clear opportunities for progression for all staff.
- Delivery of the Commission's communications strategy, including developing engaging online content and promotional materials for graduate recruitment.
- Maintaining our leadership and management capabilities.

Control measures

- Appropriate work-planning and resource management for all of our core activities.
- Putting in place a training and development plan for new recruits.
- Implementing our communications strategy, including ongoing evaluation.

5 HOW WE WILL DELIVER THESE OUTCOMES

We have identified a number of activities which, taken together, will deliver the outcomes described in the previous section.

Many of these activities contribute to more than one outcome, and any specific project that we work on may require a number of different activities. We intend to reflect this level of integration in our future operational model/office structure.

These activities are necessarily high level given the length of time that is covered by this plan. We will publish more detail about our planned activities and budget at the start of each year. Our performance in delivering this annual list of activities is one of our key performance indicators.

The activities that we will undertake in the period covered by this Corporate Plan are as follows:

Implement or support the Scottish Government's policy initiatives

- Provide support to the Scottish Government as it develops policy measures in response to COVID-19.
- Support the implementation of process changes to the retail market framework to reflect the Ministers' Statement on the Principles of Charging.
- Understand the costs of connecting rural communities to Scottish Water's network and compare these with the costs of monitoring and supporting private water supplies.
- Review the charging arrangements for developers as required under the Ministers' Principles of Charging to ensure that developers pay appropriately for the infrastructure services that they are provided with by Scottish Water.
- Improve understanding of the drivers of costs of property and highway drainage and how best to recover those costs given the industry's challenge to achieve net zero emissions by 2040.

Embedding the trust and confidence model

- Ensure that all WICS staff understand the principles of EBR and the associated behaviours and values and put these into practice through engagement with experts in the field.
- Encourage Scottish Water and other stakeholders to use experts in the field of EBP to discuss the concept and to help them implement the associated behaviours and values within their organisations.
- Identify best practice and influence future communication between Scottish Water and stakeholders through the use of real examples provided by stakeholders where things have worked well, and ensure that lessons are identified and communicated in cases that have not worked so well.
- Establish a forum for regular discussion of what has gone well and what has gone less well in implementing EBR and EBP.
- Identify test cases of good and less good practice to gather stakeholders' views, including through workshops.
- Undertake ongoing engagement with stakeholders through, for example, an annual review of the model and by holding individual sessions with stakeholders.

Supporting licensed providers to implement the principles of EBP in the retail non-household market

- Undertake an extensive engagement process with licensed providers (this may involve a pilot project, facilitated by experts in the field).
- Introduce a voluntary market-wide process that allows licensed providers to demonstrate behaviours consistent with EBP.

Reviewing and commenting on performance

- Comment strategically and publicly on Scottish Water's performance each year as a minimum or more frequently if there is benefit to customers, communities and other stakeholders in doing so.
- Understand how Scottish Water is delivering the Ministers' Objectives by attending and contributing actively to quarterly Delivery Assurance Group meetings.
- Work with international experts to understand Scottish Water's progress as it implements its Asset Management Transformation Plan.
- Comment strategically and publicly on Scottish Water's activity as a wholesaler, each year as a minimum or more frequently if there is benefit to licensed providers and customers in doing so.
- Keep under review the growth in population and population migration within Scotland.
- Keep under review the impact of macro-economic factors such as cost and price inflation, and interest rates on Scottish Water's business.

Reviewing costs

- Undertake a bottom-up review of Scottish Water's wholesale costs across geographical areas and the value chain. This work will help ensure that future charging arrangements support the behaviours necessary to achieve the Ministers' Objectives.
- Review the default tariffs and the margins that are available in the non-household retail market (e.g. trade effluent).
- Keep under review how Scottish Water allocates costs between expenditure that is subject to the financial tramlines (such as operating costs and asset repairs) and the investment that is subject to investment prioritisation.

Ensuring appropriate incentives

- Keep under review the regulatory framework to ensure that it provides appropriate incentives for Scottish Water to deliver Ministers' Objectives as effectively and efficiently as possible.

Understanding investment requirements

- Review the way in which Scottish Water currently appraises investment and help to develop a more comprehensive 'economic toolkit' for appraising future investment.
- Attend and engage constructively with Scottish Water's Investment Advisory Group to help the pricing of externalities and societal/environmental costs and benefits ('capitals').
- Conduct a periodic review of the long-term asset replacement requirements with better and more up-to-date information on Scottish Water's assets.
- Develop a deeper understanding of the way in which Scottish Water is prioritising the investment required to meet Ministers' Objectives at IPPG.

Understanding and acting on the views of customers

- Ensure that the customer and community voice is embedded within Scottish Water's decision-making process and that they are able to demonstrate that they have taken due account of these in the decisions they take.
- Support Scottish Water in carrying out research – including behavioural insights – in order to gain a better understanding of the preferences of customers.

Developing the SRC 2028-34 methodology

- Take due account of Scottish Water's transformation during the early years of the period, and develop the methodology for the 2028-34 price review.

Undertaking horizon scanning

- Review regulatory frameworks in other countries to identify best practice that may be applied to the model in Scotland or more widely through our Hydro Nation work.
- Undertake proactive review of innovations in other asset-intensive industries and review innovative practices within the water industry in order to inform our commentary on Scottish Water's performance.
- Understand the techniques for valuing concession arrangements and changes in market value over time.
- Engage with international organisations such as OECD NER/WAREG/IWA/ EU Commission in order to maintain an up to date knowledge of regulatory approaches and identify best practice.

Managing and administering the non-household retail market

- Review and process any new licence application, licence revocation and licence transfer.
- Review and where relevant implement proposed changes to the market codes and other refinements to the market framework as part of the CMA Technical Panel process or following a Commission-led consultation process.
- Review the financial resilience of licensed providers. Consider further measures to protect the integrity of the market to ensure that licensed providers are operating on a sustainable basis and are resilient to future shocks.
- Review and monitor customer retail-related enquiries.
- Review any alleged licence breach and where appropriate undertake formal investigations.
- Monitor the market through frequent engagement with licensed providers and the CMA.

Supporting the Hydro Nation initiative

- Undertake to deliver projects in Europe and internationally by providing strategic and analytical support, and through offering appropriate training programmes (with the relevant high-quality supporting materials).
- Seek new opportunities for business development through activities such as developing our partnerships and exploring links with potential contractors.
- Explore with the Scottish Government the pros and cons of developing a separate legal entity for our Hydro Nation activities.
- Maintain MOUs with other international regulatory bodies.
- Develop relationships with countries that we have identified as potential future partners.
- Continue our active membership of WAREG and other international organisations.
- Support the Hydro Nation scholars by providing training.
- Seek out secondment opportunities for staff to work externally and for external contacts to be seconded into WICS.

Undertaking performance management

- Ensure that we have appropriate procedures and policies in place in relation to governance, budgeting and resources, to support the successful delivery of our strategic objectives.
- Report performance against our corporate plan KPIs and annual work plan to the Commission Board and in our Annual Report.

Delivering IT services and cyber resiliency

- Ensure that our systems are cyber resilient through our people-focused approach, by strengthening our defences in line with the Scottish Government Cyber Resiliency Framework, and by remaining compliant with the Cyber Essentials Plus standards.
- Provide stable, secure and flexible IT services to support the IT and telecommunications requirements of the office.
- Build on our existing approach to incident management and business continuity planning.

Managing our finances

- Ensure that policies and procedures are in place that are in line with the Scottish Public Finance Manual.
- Prepare annual accounts in line with the Financial Reporting Manual.
- Monitor and report on expenditure against budget, highlighting areas of concern.

Recruiting and retaining staff

- Develop and keep under review our overall graduate recruitment strategy, including an assessment of our recruitment requirements.
- Undertake promotion and engagement activity.
- Deliver induction training and manage our graduate training and development programme. This includes opportunities for inward and external secondments.
- Manage our staff development and assessment framework.

Engaging with our external and internal stakeholders

- Develop and agree our communications strategy, which will describe our key stakeholders, their interests and motivations, our approach to engagement and the tools and resources required.
- Implement our communications strategy by using a wide range of tools to communicate with our external and internal stakeholders. These stakeholders are wide-ranging and encompass national and international stakeholders, the licensed providers, household and non-household customers, MSPs and the media, and current and potential employees.
- Publish information documents as appropriate in order to support understanding and transparency; this would include our annual report and the documentation relating to current and future Strategic Reviews of Charges.

Information management

- Promote best practice records management.
- Ensure compliance with legislation in relation to FOI, GDPR, and data protection.
- Handle enquiries and complaints in a timely and relevant way.
- Facilitate information provision to the Commission Board.

Risk management

- Manage the corporate risk register and operational risks.
- Identify risk and implement mitigations and review.

Work planning and resourcing

- Develop forward plans to ensure that we deliver against our KPIs and in support of our strategic objectives.
- Prepare our annual work plan and monitor and report progress against it.
- Undertake resource planning to support our work plan, deploy resources as appropriate, and provide project management support.
- Make arrangements for future staff working that draw on the experience and lessons learned from operating during lock-down.

6 RESOURCES

Future organisation

We have identified that delivering our future strategy will require our organisation to change significantly. In particular, transitioning to a fully EBR approach will inevitably require us to develop a new range of skills and capabilities. The way we worked in the past will not be able to deliver the new regulatory framework, which is based on trust and confidence, rather than the traditional regulatory 'parent-child' approach.

The EBR approach will require us to:

- behave in a way that is consistent with the principles of EBP;
- identify and promote best practice across the industry;
- closely tune in with stakeholders' views and levels of confidence;
- be prepared to call out inappropriate behaviour and performance and engage in open and robust dialogue;
- focus on the long-term delivery of benefits for customers and the environment, rather than short-term target setting and monitoring;
- be capable of delivering high-quality work to overseas customers.

As outlined under Outcome 9, in planning for the next regulatory period, we also need to take account of succession management, recognising the need to bring through talent at all levels and develop the next generation of leaders. This will build on the progress made during the current Corporate Plan period to strengthen our senior leadership team.

We have identified six key areas of internal organisational development

Establishing **robust recruitment and retention approaches**, particularly at the graduate recruitment level. We need to ensure an ongoing throughput of high-quality talent into the organisation.

Growing the **management capability of the senior team** within the organisation to manage effectively an expanding organisation with an increased throughput of junior analytical staff who will require supervision, coaching and development.

Providing **leadership development for the senior team** to ensure executive succession for the future; recognising that experience tells us that we will need to grow this capability from within the organisation.

Developing **understanding and capability** across the office of the new behaviours and approaches required to deliver economic regulation under EBR/EBP.

Increasing **flexibility, knowledge and communication** across the office by integrating functions and avoiding 'silos' through training staff to operate effectively across analytical, investment, retail and Hydro Nation functions. In this regard the recent establishment of a Central Office will play a key role.

Enhancing our **external communication capability**, both to improve our outward communication (including the website and social media presence) and to maintain an ongoing active dialogue with key stakeholders to understand their perceptions.

Consultants

We have been reducing our reliance on consultancy time over the past few years and intend to continue to use less and less of this resource.

The Commission requires wide-ranging advice to make appropriate assumptions about the reasonable costs that it should allow for in setting prices. Its assumptions must be robust to external challenge, particularly as Scottish Water has the right to require the Commission to make a reference to the Competition and Markets Authority.

We must also ensure that our processes and decisions can withstand judicial scrutiny. Supplementing the Commission's expertise with that of outside experts provides significant reassurance of the quality and independence of our work.

At the start of the regulatory control period, we will competitively tender and award a legal framework contract and an economics and finance framework contract. These will allow us to access appropriate economic, financial and legal advice. This will ensure that we can respond flexibly and cost-effectively to the demands of the Strategic Review. We plan to award these contracts for an initial three-year period, with the option for an extension of a further three years. The individuals and consultancy firms that we engage will be recognised experts in their fields.

7 BUDGET

Background

As part of the process for planning the next regulatory control period, we are required to provide an indicative budget of the expenditure needed to achieve our objectives as agreed by the Scottish Government.

The Commission is funded by a levy paid by Scottish Water and the licensed providers that participate in the non-household retail market. Following approval by Ministers of the Commission's Strategic Corporate Plan, our Sponsor Directorate instructs Scottish Water to pay the amount determined to the Commission on a monthly basis and we invoice every licensed provider each quarter, based on their share of the market.

Agreeing the budget for a full regulatory control period provides Scottish Water and the licensed providers with a degree of certainty over future fees and our ability to achieve on the objectives outlined in this plan.

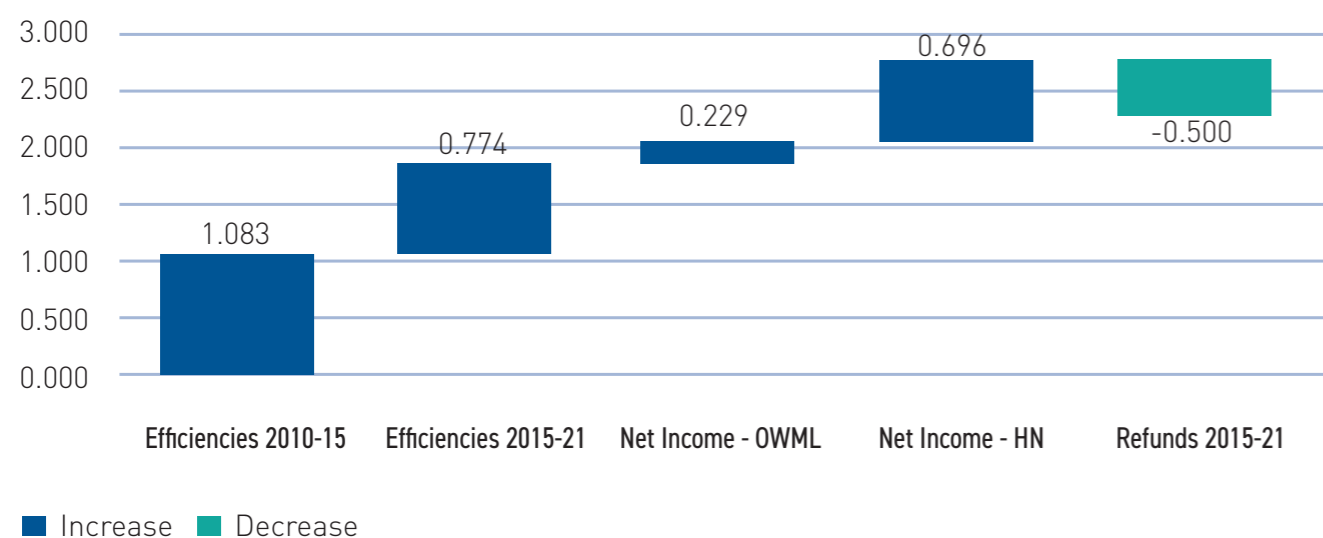
Current regulatory control period

We agreed a budget of £21.8m for the current six year regulatory control period, of which just over half related to anticipated remuneration costs, 27% to consultancy costs and the remaining amount to other operational costs, such as office accommodation, information technology and recruitment. We estimate that we will have incurred in the region of £21.0m by the end of the period, which is 3.6% below the agreed budget. Included in this estimate is the absorption of a significant increase in employer pension contributions from 1 April 2018, which in itself cost over £300,000.

Expenditure category	Agreed income/ income received (£m)	% age of total	Estimated actual expenditure (£m)	% age of total
Staff Costs	11.468	53%	11.081	53%
Consultants	5.840	27%	5.172	25%
Customer Forum	-	-	0.885	4%
Operational Costs	4.450	20%	3.846	18%
Total	21.758		20.984	

We have received a considerable contribution to our net income (£0.8m) from the provision of external services to Open Water Market Ltd in relation to the development of the retail market in England and from our international activities, predominantly European Commission funded work with the Romanian regulator.

Cashflow 2015-21 (£m)



We began the regulatory control period with a cash balance of £1.2m (£1.083m from efficiencies made in the regulatory period 2010-15 and £0.138m net income from OWML). During the current regulatory control period we repaid £0.25m each to Scottish Water and the licensed providers. Notwithstanding having already repaid £0.5m, we are currently forecasting a cash balance at the end of the current financial year of £2.282m. In agreement with Scottish Ministers through this Corporate Plan, we will agree a suitable method of repayment of a further £1.3m of the estimated cash balance at 31 March 2021. We outline our repayment proposal at the end of this section.

Proposed budget 2021-27

The table below outlines the proposed income, high level categories of expenditure and the anticipated cashflow over the regulatory period.

£m	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
Income						
Scottish Water levy	2.26	2.28	2.30	2.32	2.35	2.37
Licensed Provider's levy	1.67	1.72	1.77	1.82	1.88	1.93
Total levy income	3.92	4.00	4.07	4.15	4.23	4.31
Expenditure						
Remuneration	2.47	2.74	2.84	2.97	3.10	3.24
Consultancy	0.53	0.54	0.54	0.54	0.54	0.54
Operational costs	0.55	0.57	0.78	0.80	0.82	0.83
Total expenditure	3.56	3.84	4.16	4.30	4.46	4.60
Cash balance brought forward	0.08	0.45	0.61	0.52	0.37	0.14
Net surplus/(deficit)	0.37	0.16	(0.09)	(0.15)	(0.23)	(0.30)
Cash balance carried forward	0.45	0.61	0.52	0.37	0.14	(0.16)
Proposed net contribution from international activities	0.15	0.15	0.17	0.23	0.30	0.30
Revised net surplus/(deficit)	0.52	0.31	0.08	0.08	0.07	0.00
Revised end cash balance	0.60	0.91	0.99	1.07	1.14	1.14

For the coming 2021-27 regulatory control period, we propose a 1% nominal annual increase to the fee paid by Scottish Water, in line with the allowed for increase in their 'Tier one' expenditure in our draft determination for 2021-27. We propose to increase the licensed provider's levy by 3% nominal each year, on the basis that this is a lesser increase than the extent to which their gross retail margin will increase under the proposals set out in our draft determination. Taking account of the upfront refunds to Scottish Water and the licensed providers, as outlined at the end of this section, neither Scottish Water nor the licensed providers will see an overall nominal increase in the overall net amount of their contributions to WICS over the period of this plan.

Under these proposals, our income and expenditure are projected to be in balance in the final year of the coming regulatory control period.

This is possible because we are committed to achieving a contribution (income less any direct costs incurred) in the region of £1.3m from international projects.

Remuneration costs

Our revised regulatory approach under EBR, as set out earlier in this document, will inevitably require more regular and more detailed interaction with Scottish Water. EBR is based on open, transparent and regular information sharing, along with higher quality reporting of appraisals, performance and progress.

We have also identified a number of major projects that will require more resource on an on-going basis. These relate to issues such as wholesale cost allocation for tariffs, monetisation of externalities and accounting separation of licensed providers' activities in Scotland and in England (where markedly different rules apply).

Following a successful recruitment campaign in September 2020, we have hired four trainee analytical employees. We hope to fill another four trainee analyst vacancies, bringing the total number by the end of the regulatory period to 12 analysts (including trainees) at any one time. This increase in headcount and associated remuneration costs will also allow us to respond both to the additional project oriented works foreseen under EBR and also more flexibly to income earning Hydro Nation projects as and when these become available to us.

During the early part of the next regulatory control period, the Deputy CEO plans to retire. Experience tells us that it is very challenging to appoint at such a senior level from outside, albeit we continue to remain open to this option if there are indications this has changed. As part of our succession planning, we have been investing in our cohort of Assistant Directors and expect to see them graduate to more senior roles, taking on further responsibilities around the time when the Deputy CEO retires.

As part of the assumptions used in proposing our remuneration costs for the next regulatory control period, we have allowed for salary increases to include progression in line with our performance management framework and for a basic award which will be based on the guidance outlined in the annual Scottish Government's Pay Policy.

The underlying salary budget is increasing at 3.6% a year in real terms over the 2021-27 regulatory control period. Adjusted for headcount, it implies a 1.3% real increase in average annual remuneration, including the costs of promotions.

The increase in the proportion of our expenditure being incurred on remuneration costs is offset by a decrease in our use of consultants. We are proposing to cut our use of consultants by over 30%. More details on anticipated consultancy costs are provided in the next section.

A further material factor in our salary budget is the last triennial valuation of the Falkirk Council Local Government Pension Scheme. This resulted in a significant increase in the employer's contribution to the staff pension scheme. From 1 April 2018, the employer's contribution rate increased from 19.1% to 28.3% which was in the region of an additional cost of £140k per year. The next valuation will take effect from 1 April 2021 and early indications are that the contribution will increase once again. Our budget allows for an increase in employer's pension contribution of up to 30%.

Consultancy costs

As explained earlier, the Commission requires access to sound advice relating to the economics, legal, finance, accounting and engineering of water and sewerage provision in Scotland.

The Commission's role is similar to that of other regulators in the UK, but it does not enjoy the same potential for economies of scope or scale. Even these much larger regulators with their additional scope and scale advantages make significant use of external consultants. Expert, independent advice not only provides expertise in areas – such as legal advice and HR – that are not core skills of the office but can also carry additional weight with stakeholders and can be more robust to challenge than expertise drawn from within a regulator's own office.

We plan to reduce our use of external consultancy for our price setting activities during this Corporate Plan period. During the current regulatory control period our expenditure on consultancy is estimated to reach £5.2m (25% of total expenditure). Our total planned consultancy expenditure over the next 6 years is proposed to be £3.2m (12% of total expenditure), as outlined in the table below.

Description of service	Total for the period (£)
Provision of economic advice	1,200,000
Provision of legal advice	1,200,000
Legal support (QC)	240,000
HR and compliance support	185,000
Other consultants – assurance activities	450,000

Operational costs

Operating costs include all costs that do not relate to salary or consultancy. These are now fully consistent with the business case for allowing the lease on our offices at Moray House to be transferred. As such, it includes the costs associated with home working for the next two years followed by the potential costs of a move to a new base, should this be considered to be desirable.

Capital expenditure

The Commission has no planned capital expenditure over the period, other than routine replacement of IT equipment.

International work

Any income and expenditure related to business development or funded international work will be ring-fenced in an appropriate way, to allow for full scrutiny of activity in this area.

The office of the Commission will provide all the resources required to perform international work, including staff time, travel and accommodation requirements and sourcing any external consultancy required.

Any direct disbursements will be allocated to the international 'division' and staff deployed on international work will be charged to the division at a charge-out rate which will cover full remuneration costs of the employees involved. To this end, we will deploy an effective time-allocation mechanism to ensure any time spent on international activities is captured.

The level of activity in this developing area is difficult to forecast but we have made our best estimate at the volume of funded international work we will be able to achieve during the regulatory period and the level of business development activities required to achieve this.

We will bill based on time-spent and any direct costs will be directly re-charged. The aim would be for the international activities to make a contribution to overheads during this regulatory control period of up to £1.3m. This contribution will be after the subtraction of all direct disbursements related to international activity. Any surplus in excess of the planned contribution, which arises from international work will either be returned to Scottish Water or licensed providers or may, in part, be used to support other Scottish Government Hydro Nation initiatives. The Commission will alert the Scottish Government to any such surplus.

Budget management

We propose that the Commission should maintain its ability to transfer budgets between budget lines and between financial years.

A formal review of the budget will be carried out after the third year of the regulatory period for submission to the Scottish Government.

The Commission operates under a tight budget constraint adhering to formal financial processes and procedures. We expect to meet all foreseeable costs from the budget outlined in this Plan. However, if there were substantial legal proceedings, there would need to be a separate provision.

Cash refunds

As a result of our careful management of customers' money and the income that we have generated from our hydro-nation activities during the current regulatory period, we propose the following use of our projected year end surplus as at March 2021:

Stakeholder	Amount	Rationale
Scottish Water	A refund of £1,000,000	This amount reflects income generated from Hydro Nation activity and savings achieved against our base budget, principally reflecting savings in staff costs from operating below agreed head-count. There have also been savings achieved during home working. This refund will be made at the start of the regulatory period and is not included in the cash balance brought forward for the period.
Licensed Providers	A refund of £300,000	This amount reflects savings achieved against our base budget, principally reflecting savings in staff costs from operating below agreed head-count. It is proportionately slightly less than the refund to Scottish Water. This reflects the higher level of activity required in responding to the pandemic. This refund will also be made at the start of the regulatory period and is not included in the cash balance brought forward for the period.
Hydro Nation research projects (to be defined)	An allocation of £300,000	This amount is available as a result of income generated, net of all disbursements, from Hydro Nation income to date. This amount will be ring-fenced and is not included in the cash brought forward for the period.
Hydro Nation network building	An allocation of £600,000	This amount is available as a result of income generated, net of all disbursements, from Hydro Nation income to date. This amount will be ring-fenced and is not included in the cash brought forward for the period.

The allocations for Hydro Nation research projects and network building will contribute to the wider development of the Hydro Nation initiative, and therefore to the scope for future income for the office from this source. Future income from the office's Hydro Nation activities will help offset future levy costs and hence ultimately benefit customers.

8 GOVERNANCE AND ACCOUNTABILITY

The broad framework within which we operate is set out in the Framework Document, a document agreed between the Commission and Scottish Ministers.

The Framework Document defines the key roles and responsibilities which underpin the relationship between the Commission and the Scottish Government. While this document does not confer any legal powers or responsibilities, it forms a key part of the accountability and governance framework. The Commission's governance framework establishes the processes required to monitor activity and the achievement of our objectives.

The Commission Board provides leadership, direction, support and guidance to ensure that the Commission delivers and is committed to delivering its functions effectively and efficiently and in accordance with the aims, policies and priorities of the Scottish Ministers.

As part of our corporate planning process, we have identified the performance indicators we consider appropriate to measure our success over the regulatory control period. We will report on our performance against these performance indicators as part of the annual reporting process.

Our contribution to the Scottish Government's purpose

The overall purpose of the Scottish Government's National Performance Framework (NPF) is to focus government and public services on creating a more successful country, with opportunities for all of Scotland to flourish, through increasing sustainable economic growth. The NPF provides a clear vision for Scotland, with broad measures of national wellbeing covering a range of economic, health, social and environmental indicators and targets.

Table 1 highlights the elements of the NPF where we consider we are able to make a contribution.

Table 1: Alignment of this Corporate Plan with the NPF: How our strategic objectives contribute

NPF elements	Our strategic objectives		
	1: To support the sector to achieve its long-term vision and the Scottish Ministers' objectives for the regulatory control period.	2: To challenge Scottish Water to achieve best in class levels of service for its customers and communities.	3: To become an international leader in the field of economic regulation.
We respect, protect and fulfil human rights and live free from discrimination.			✓
We have a globally competitive, entrepreneurial, inclusive and sustainable economy.	✓	✓	✓
We are open, connected and make a positive contribution internationally.			✓
We tackle poverty by sharing opportunities, wealth and power more equally.			✓
We live in communities that are inclusive, empowered, resilient and safe.	✓		
We grow up loved, safe and respected so that we realise our full potential.			
We are well educated, skilled and able to contribute to society.			✓
We have thriving and innovative businesses, with quality jobs and fair work for everyone.	✓	✓	✓
We are healthy and active.	✓		
We value, enjoy, protect and enhance our environment.	✓	✓	
We are creative and our vibrant and diverse cultures are expressed and enjoyed widely.			

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