

Stakeholder Workshop 6: Capital Maintenance

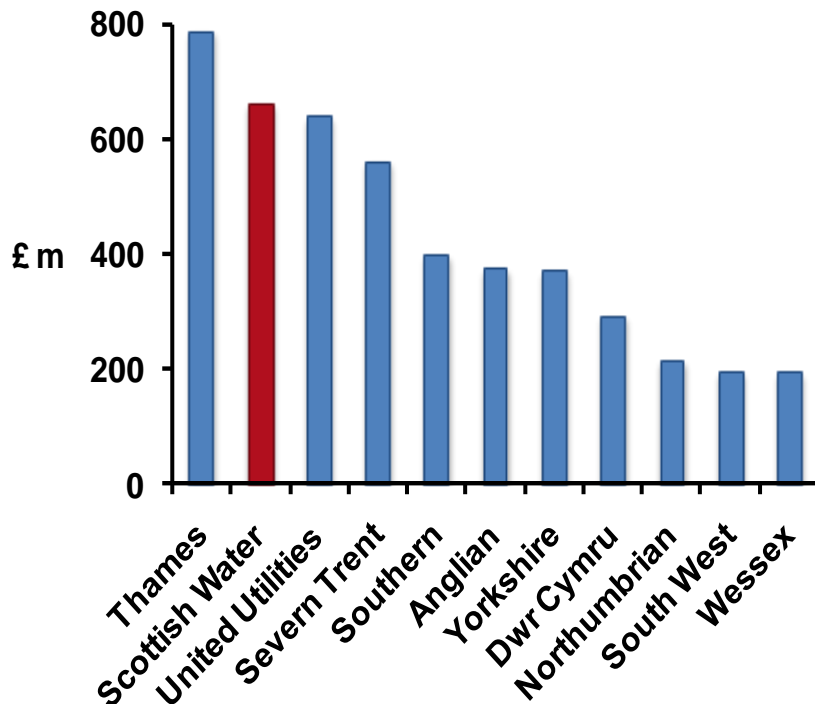
Strategic Review of Charges 2010-14: 2009 workshops
Stirling, 30th April 2009

Programme for the morning...

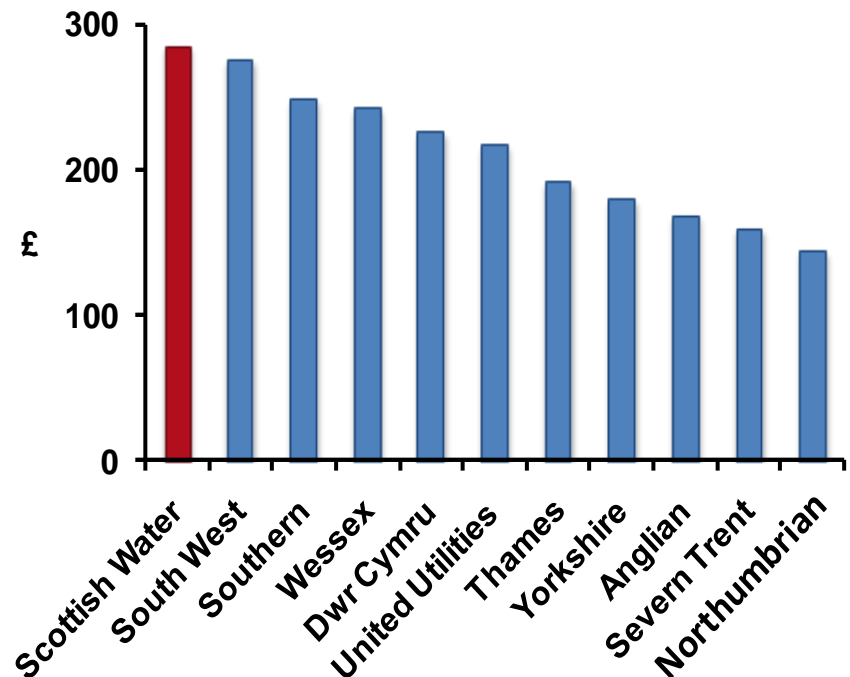
- The scale of historic investment in Scotland;
- Defining capital maintenance;
- Establishing the allowance for capital maintenance;
- Some key questions for stakeholders; and
- Your views

Scottish Water is currently tasked with delivering a very large capital programme....

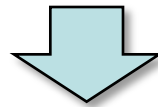
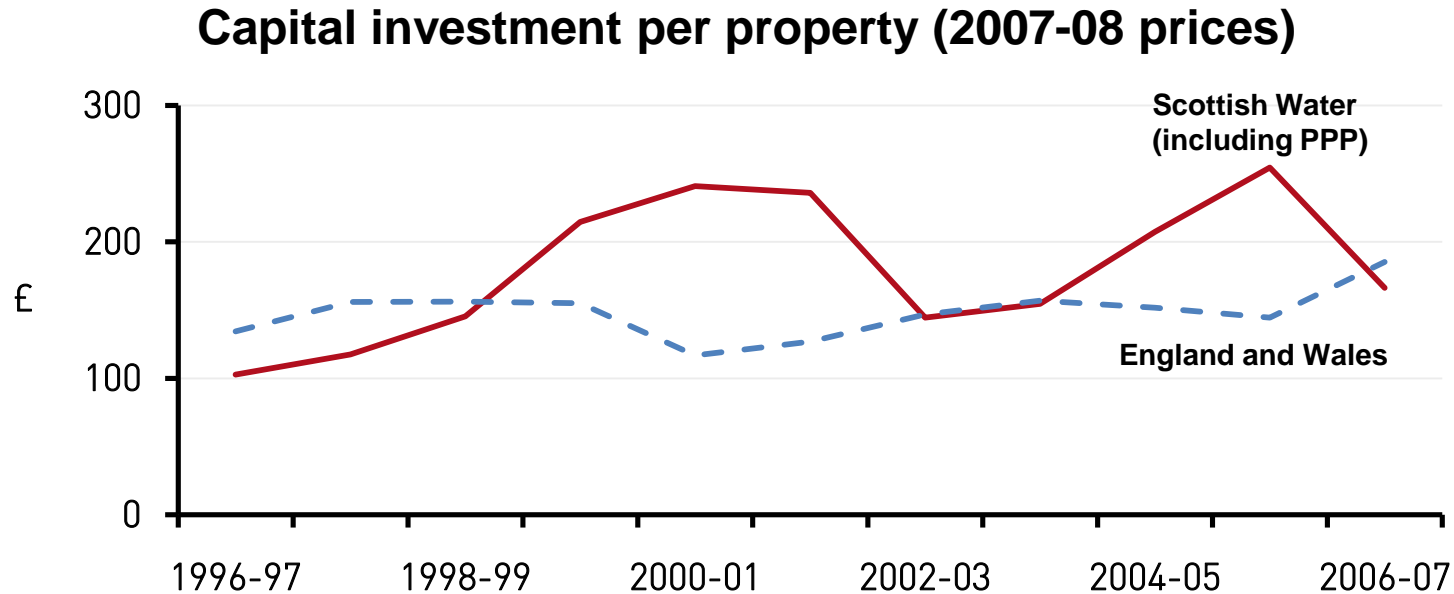
Total investment per year 2005-10
(2007-08 prices)



Investment per property per year
(2007-08 prices)



Levels of investment in Scotland have generally been higher than those in England and Wales in recent years



Even after adjustments for relative efficiency, the level of spending in Scotland has been relatively high.

In their draft statement, Ministers have set Scottish Water objectives in the following areas...

- Capital maintenance and service standards
- Strategic capacity for new developments
- Drinking water quality and water resources
- Environmental protection

The totality of capital investment identified in Scottish Water's business plan is £2.2 billion (07-08 prices)

It comprises:

- £1,047m for capital enhancement
- £928m of capital maintenance (including “exceptional items” of around £103 million)
- Overhang from Q&S2 & 3a of £169m
- Q&S4 ‘early start’ of £74m

Scottish Water have proposed £88m of ‘early start’ investment prior to the Q&S3b period and £140m after, leaving £2.2 billion to be financed in 2010-14.

So what is 'capital maintenance' ?

It is the investment needed to replace or refurbish existing water and waste-water assets (and the associated support systems) so that they continue to function and perform as intended.

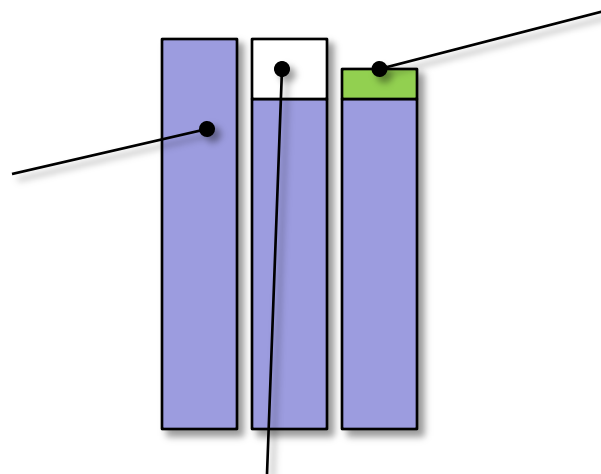
The aim of this capital maintenance investment is to provide customers with a broadly stable level of service.

Our challenge is setting the right of capital maintenance by taking account of

- past historical capital maintenance investment in Scotland;
- how this compares with what is allowed for in England & Wales companies;
- the natural deterioration of asset performance with age and use; and
- the steady uplift in capital maintenance as more assets are built to fulfil higher standards, meet growth etc.

There are three key considerations in reaching our initial conclusions on the correct level of investment for Capital Maintenance

What is the appropriate, baseline level of service?

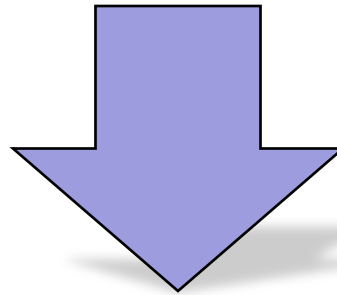


What additional account, if any, is required for any step changes in capital maintenance requirements?

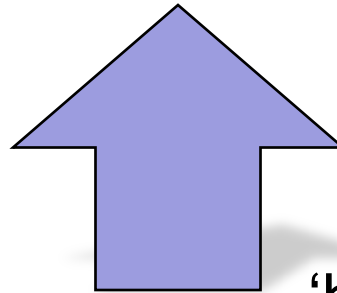
What is the scope for efficiency in delivering this baseline?

We establish the right amount of capital maintenance by reviewing the programme from two perspectives

high level
'top down'
approaches



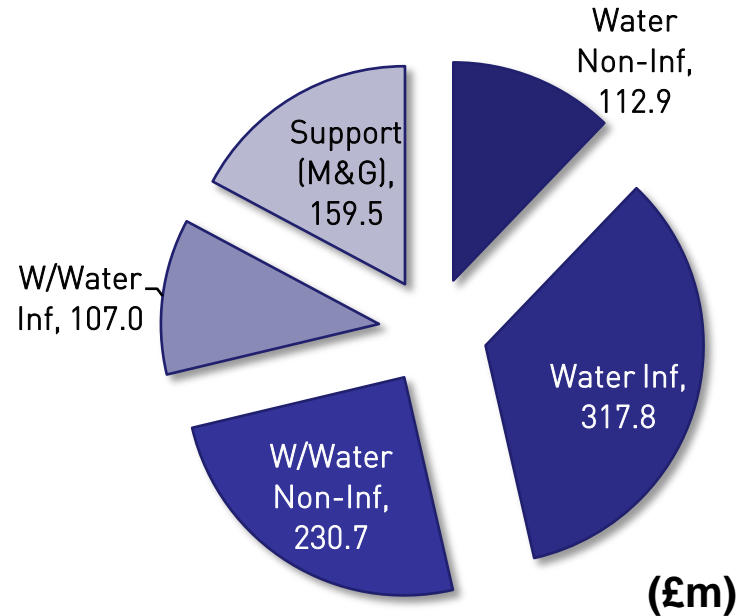
£ x million



detailed
'bottom up'
approaches

For the 'bottom up' assessment we will examine every element of the £928m Capital Maintenance proposal

- Water Infrastructure
- Water Non-Infrastructure
- Wastewater Infrastructure
- Wastewater Non-Infrastructure
- Support Services (management & general)



When considering how much capital maintenance (CM) to allow for in prices ‘bottom up’ we consider

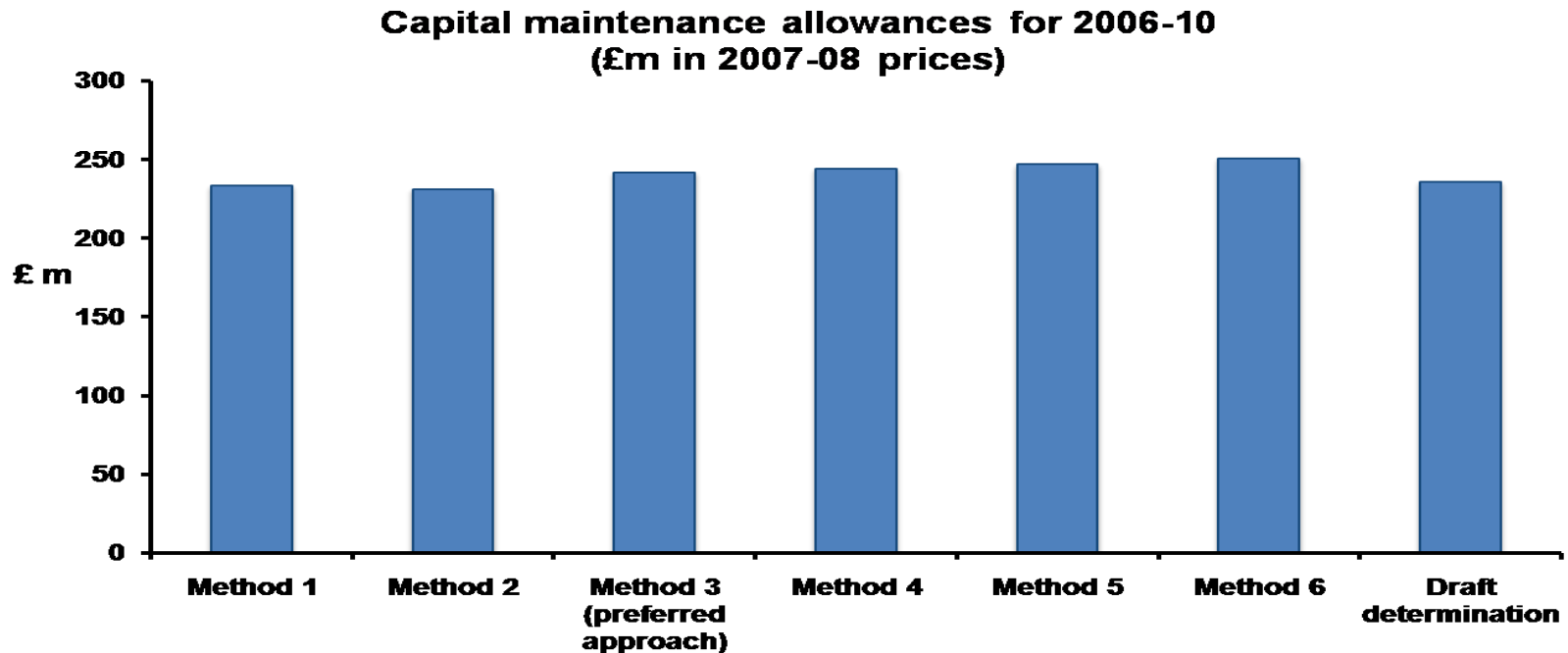
- the views of the Reporter;
- the views of the environmental and drinking water regulators;
- the views of other stakeholders;
- the current asset performance for customers; and
- the quality of Scottish Water’s information underpinning its proposals, and its knowledge of the asset base (‘asset intelligence’)

Summary of Capital Maintenance

Capital Investment Categories	Base	Exceptional
	(£millions)	
Water Non-Infrastructure	92.1	20.8
Water Infrastructure	246.9	70.9
Wastewater Non-Infrastructure	223.8	6.9
Wastewater Infrastructure	102.3	4.7
Support Services	159.5	0.0
Sub Total	824.6	103.3
TOTAL	927.9	

‘Base maintenance’ will, in many cases, be asset specific (targeted) or left undefined. Most of this will be driven by pro-active (planned) maintenance requirements with some reactive (emergency) work.

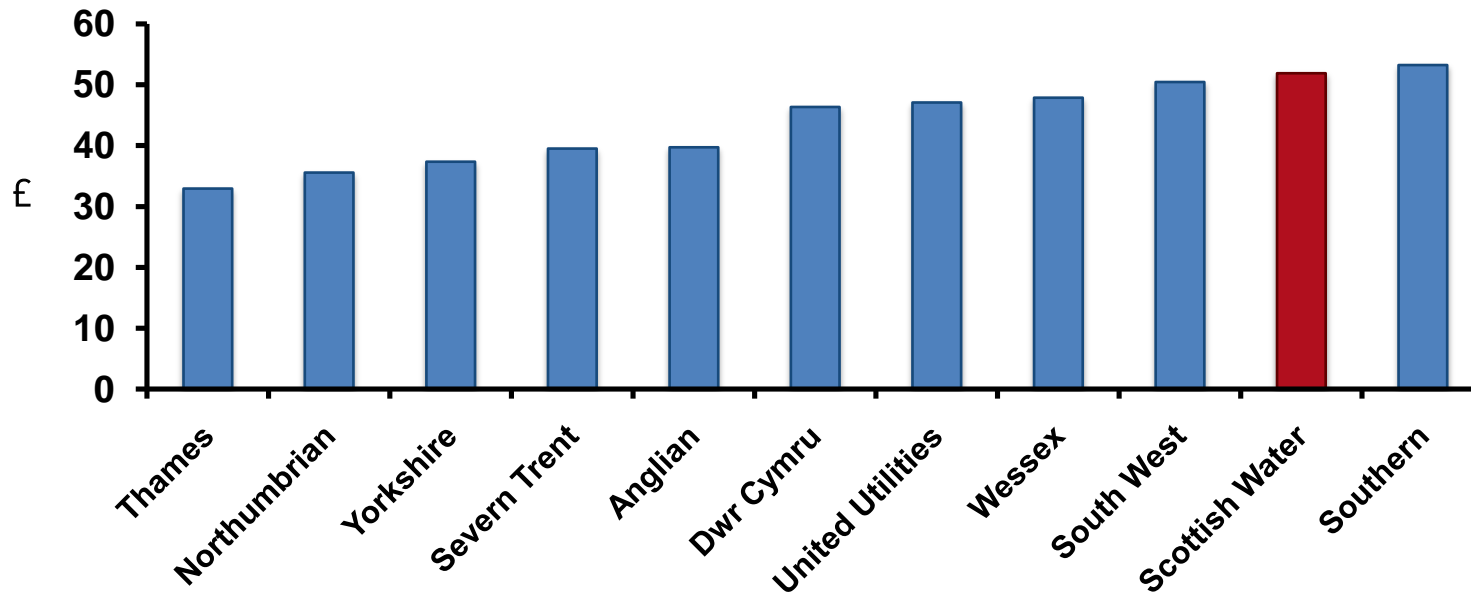
For the 'top down' assessment we are likely to use an array of comparison tools including econometrics to compare the levels of CM activity in Scotland with England & Wales. This is similar in approach to the 2006-10 Price Review.



At the last price review we allowed for £240m per year (in 2007-08 prices) of capital maintenance based on this form of assessment, taking account of the 'bottom up' view.

These allowances compared favourably with those made by Ofwat

2005-10 Allowance for annual capital maintenance expenditure per head of population (2007-08 prices)



Going forward, for the 2010-14 Price Review, we will need to consider whether the historic level of capital maintenance is appropriate taking account of the scope for further efficiencies and consideration of any step-changes in requirements

Some key questions for stakeholders with regard to the 2010-14 investment period. We invite your views on the following?

- (1) What do other stakeholders see as the Capital Maintenance priorities ?**
- (2) What are stakeholder views about the importance of the “exceptional items” (disinfection, network monitors accelerated maintenance, leakage)?**
- (3) What are the residual concerns, if any, of stakeholders in our determination of the capital maintenance allowance for 2010-14?**

**For more information on the price review please go
to:**

www.watercommission.co.uk/view_future_prices.aspx