

**Minute of the twelfth meeting of the Water Industry Commission for
Scotland
Held on 7 and 8 February 2006 in Stirling**

In attendance

Commission: Sir Ian Byatt (Chairman)
Professor David Simpson (Deputy Chairman)
Professor John Banyard
Dr Michael Brooker
Mr Charles Coulthard
Mr Alan Sutherland (Chief Executive)
Mrs Katherine Russell (Secretary to the
Commission)

Miss Harriet Towler

Apologies for absence: None

Chairman's opening remarks

The Chairman welcomed everyone to the meeting and thanked them for attending.

Minute of previous meeting and review of action points

The Commission agreed that the minute was an accurate account of proceedings. They noted, however, that before minutes were placed on the website, actions should be made anonymous.

The Commission were updated on actions from the previous meeting.

The Chief Executive noted that he had written to Scottish Water regarding a meeting held with them on 11 January on capital procurement. This letter included minutes of the meeting as an annex. It was noted by the Commission that an important point had been omitted from these minutes. They asked that it be recorded that they were concerned that gains made by the Scottish Water Solutions joint venture should not be achieved at the expense of required outputs.

The Commission noted the ongoing task of servicing the high level monitoring group. They noted that this was a priority for the office.

The Commission were informed that Directors and Officers liability insurance was in place and that assurance had been received from brokers that the office was appropriately insured.

The Commission were informed that the draft Rules of Procedure were going through another iteration process. It was agreed that the latest iteration would be presented to the Audit Committee at their meeting on 1 March, and the Commission at their April meeting. **Action**

It was agreed that the risk register (discussed at the January Commission meeting) would be presented to the Audit Committee at their March meeting, and a final register, including the steps taken to mitigate risk, to the Commission in April. **Action**

The Chief Executive advised the Commission that analysis on market codes was in progress, and would be completed in time for the March Commission meeting. **Action**

The Commission agreed that any outstanding actions from each meeting would be carried forward to the next meeting. All actions would be recorded in a rolling register with completion dates noted. **Action**

Update on current issue (Scottish Water delivery plan)

The Commission discussed a request from the Deputy Minister regarding a delivery plan Scottish Water had submitted to its owner, and approved a reply. **Action**

Update on other current issues

The Commission noted that Scottish Water had accepted the Final Determination, and that the Commission could now turn to playing their part in monitoring the achievement of objectives.

The Commission welcomed the fact that Scottish Water, SEPA, DWQR and the WCCP had all signed up to the high level monitoring group.

The Chairman and Chief Executive noted that they had given a successful presentation to the Regulatory Policy Institute in Oxford on 27 January. They were pleased that this had been a well attended event.

The Chief Executive noted that framework agreements for economic, engineering and financial/regulatory accounting consultancy services were in the process of being concluded. The Commission noted that this would materially aid the resourcing position of the office. A note would be written on the new resources available and circulated to the Commission and all staff. **Action**

The Chief Executive informed the Commission that a full audit trail regarding the tendering process for the framework agreements was in place.

The Secretary updated the Commission on the progress with arrangements for the Comiston lecture.

Dr Brooker noted that he would be shortly holding a conference call with Scottish Water to discuss staff incentives. **Action**

The Chairman noted that he had received a letter from Scottish Water regarding its capital procurement using Scottish Water Solutions. The Commission agreed that the Chief Executive should write to Scottish Water in response, noting that the Commission still had concerns about the present arrangements, but recognising that this was a matter for Scottish Water and its owners. The Commission noted that the key indicator of the appropriateness of the present arrangements would be if the ministerial objectives and better customer service were delivered within the constraints set out in the Final Determination. This would be an issue for the high level monitoring group. **Action**

The Commission: working methods

The Commission discussed a paper (CP08-06) drafted by the Chairman on its working methods. The Commission approved the paper and asked that it be circulated to all staff. **Action**

It was noted that all future Commission papers should be labelled consistently with the categories set out in this paper, and include recommendations where appropriate. **Action**

Key messages for annual reports – Investment and Asset Management, Costs and Performance, Customer Service

The Commission welcomed the key messages for the three annual reports tabled at the meeting. They agreed that each report should clearly document those messages.

The Commission agreed that in September and October of each year, the above reports would be published. They would report on Scottish Water's performance in the previous financial year and Scottish Water's comparative performance in the preceding year (taking account of the availability of information for the English and Welsh industry). For example, September 2007 would compare Scottish Water against expectations for 2006-07, and against England and Wales for 2005-06. Reports for 2006 only would cover three years; 2003-04, 2004-05 and 2005-06, in order to bring current monitoring up to date. Reports for 2006 would be published on the following dates:

- Customer Service – 15 September;
- Investment and Asset Management – 6 October; and
- Costs and Performance – 31 October.

These publication dates should be incorporated into the office workplan. **Action**

Study on wholesale charges/external consultants

The Chairman welcomed Dan Elliott and Rob Francis (from Frontier Economics) to the meeting to discuss a study into wholesale charges which had been agreed at the last Commission meeting. Dr Jeremy Atkinson, Dr John Simpson and Mr Craig Mackenzie were also welcomed to the meeting.

It was noted that since the last meeting, a letter had been sent to Scottish Water inviting it to take part in the study.

The Commission held a wide-ranging discussion about wholesale charging. A briefing note (CP10-06) had previously been circulated to aid discussion. It was agreed that the study would approach wholesale charges by assessing overall wholesale costs and then identifying areas where costs may diverge significantly from the average. A number of different areas where costs may diverge were identified. For water, factors to be considered were; infrastructure usage; peak versus base usage; seasonal usage; day/night usage; and interruptible. For waste water, the components of the Mogden formula would be used as a starting point. It was agreed that the relative importance of each factor, and any others arising, would be assessed

The Commission emphasised the importance of ensuring that work by consultants was appropriately monitored. The Chief Executive undertook to provide the Commission with bi-monthly updates about the progress of work undertaken by these consultants. **Action**

Update on the office workplan

The Commission were informed on progress and welcomed the construction of a detailed workplan, closely integrated with the work of the Commission. The Commission believed the plan should engage all members of staff and be closely aligned with performance management. Charles Coulthard, Chair of the office's working group on performance management noted that a proposal scheme would be ready to be tabled before the Remuneration Committee at their next meeting. **Action**

It was emphasised that it would be important that procedures were in place to deal with unexpected events and changes to the plan. The Commission noted that the plan involved a heavy workload for the office, and were comforted by the option to draw on experts from the newly appointed framework agreements.

The Chief Executive would report on progress with achieving the workplan at each Commission meeting and advise of any areas where prioritisation is required. **Action**

A Corporate Affairs workplan to complement that of the analytical work of the office would be prepared by the end of March. **Action**

In thinking about the workplan, the Commission reviewed the lessons of the past and concluded there could be merit in:

- extending the period for charges to 5 years in a process similar to Ofwat;
- developing the idea of an indicative set of prices for the subsequent 5 years; and
- emphasising the importance of maintaining an efficient capital programme which would be unlikely to exceed £400-£500m per annum.

These ideas would be discussed with the Scottish Executive at an early stage.

Action

An information paper on the process for interim determinations would be written for the Commission. **Action**

The Chief Executive informed the Commission of his plans for recruitment. The Commission noted and welcomed the proposed policy of focussing recruitment where high quality candidates are available. They thanked Professor Simpson for his involvement in the process.

Update on retail access

The Commission agreed the drafting of a letter to Scottish Water setting out the requirements for the award of either a provisional or permanent licence. This letter would be sent following the meeting. **Action**

The Commission noted a meeting would be held with Scottish Water on 23 February to discuss issues arising from Scottish Water's role as wholesale supplier in the new retail market, and the formation of its retail entity. Members were invited to attend. A briefing note would be prepared for attendees. **Action**

In advance of this meeting, an agenda would be prepared in consultation with Scottish Water. **Action**

The Commission were minded that there should always be a default price for all suppliers (in line with the Final Determination). However, such a default price would not obviate the need to have an undue discrimination clause in licences. This issue would be discussed further with the office's economic consultants. **Action**