

Section 9

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Section 9: Appendix A

Glossary of Terms and Definitions

Access agreement: In common carriage, the legal agreement entered into by the network owner and the party seeking access to the network. The access agreement binds the parties to adherence to the network access code.

Access charges: The charges payable by parties seeking access to the network, as set out in the access code and detailed in specific network access agreements.

Access code: The detailed terms and conditions agreed between the water authority and the new entrant covering technical, legal, scientific, financial and commercial issues relevant to a proposal.

Annual return: The water authorities are required by the Commissioner to prepare an annual return each June to cover their activities in the previous year, and update forecasts. This return provides a framework for the authorities to submit the majority of the information required by the Commissioner to carry out his regulatory duties. This return was developed and brought into a Scottish context from Ofwat's June Return.

Asset lifecycle: The period from when an asset is purchased to when it is decommissioned.

Asset management efficiencies: Efficiencies achieved through improving value for money in the asset management process.

Asset management plan (AMP): Long-term projection of work required to be undertaken to maintain and upgrade the infrastructure assets. The English and Welsh equivalent of the Quality and Standards process.

Barriers to entry: Obstacles that prevent competitors entering the market. They include economies of scale, product differentiation, capital requirements, switching costs, access to distribution channels and government policy.

Backlog expenditure: Expenditure required to renew assets to bring performance up to defined standards of service or to improve condition to an agreed investment profile.

Benchmarking comparison: A method of comparing the performance of different companies. The best performers in a

given area are used as a standard or benchmark for the others.

BOD: Biological oxygen demand – a measure of the pollution potential of raw sewage and treated sewage effluent.

Brokerage: A deal by which water is sold to customers by a third party, or broker, who is not responsible for anything other than the final supply of water to a customer's premises.

Bulk supplies: Supplies of treated or untreated water traded between water authorities. These supplies are often traded under long-term contracts and on non-standard terms.

Capex: Capital expenditure.

Capital efficiency: Achieving the same or better outputs for less capital expenditure.

Capital maintenance: Planned work carried out by the authorities to replace and repair water and sewerage assets to provide continuing services to customers.

Capital programmes: Planned construction work being carried out by the authorities to build new assets such as sewage treatment works and water mains.

Central option: One of three options for future investment levels proposed by the Scottish Executive as part of the 2002-06 Quality and Standards consultation. The central option 'meets the legal standards and makes some improvements to the assets, through only investing enough in the underground infrastructure to prevent further deterioration'¹.

Charges scheme: Charges schemes set out the Scottish water authorities' charging policy and charge levels for each financial year. They are subject to approval by the Commissioner.

Charging year: The year commencing on 1 April.

Codes of Practice: Each water authority is required by the Local Government etc. (Scotland) Act 1994 to produce a Code of Practice detailing the services they offer. The Code includes the authorities' service aims, their Guaranteed Minimum Standard of service, their procedures for handling complaints and when compensation is payable to customers.

¹ Water Quality and Standards, Investment Priorities for Scotland's Water Authorities 2002-2006. Scottish Executive, August 2001

Cost base: A set of standard capital unit costs, designed to reflect the actual work to be carried out by the authorities. These can be benchmarked in order to assess a procurement efficiency gap.

Comparative analysis: The use of a number of different organisations' performance in a given area to assess relative performance of an individual organisation.

Comparator company: A company used as a benchmark, against which an authority's performance is assessed.

Comparative efficiency studies: Comparisons of organisations' operating costs, taking into account factors outside management control which influence costs. Such factors include economies of scale, population density and the nature of the terrain. From these comparisons it is possible to rank or band companies by relative efficiency and to assess relative scope for reducing costs.

Construction operators' price index (COPI): The rate of inflation applying to the construction industry.

Consultative Committee: The 1999 Water Industry Act established three Committees to advise the Commissioner on the promotion of the interests of customers of the three Scottish water authorities. Each Committee is chaired by the Commissioner and consists of between six and nine members. The appointment of members followed the guidance issued by the Commissioner for Public Appointments. Members are unpaid.

Core business: The supply of water through pipes including discharge of waste water. It is the only aspect of the business that is regulated in England and Wales. In Scotland, economic regulation applies to all activities, whether core business or not.

Cost-reflective pricing: Charges are based on the cost to the service provider of actually providing that service to a customer.

Council Tax bands: The use of the value of a domestic property to set the level of Council Tax and water charges paid by domestic customers.

Cross-subsidy: The subsidy of a particular customer group by another group. The former pays less than the actual cost of providing the service and the latter pays more.

Cryptosporidium: A waterborne parasitic micro-organism, believed to originate from livestock. Cryptosporidia have been identified as being responsible for a small number of acute diarrhoea cases (cryptosporidiosis).

Cubic metres: 1,000 litres.

Current cost accounting: A method of accounting originally designed to deal with the problem of showing the effect of inflation on business profits. Instead of showing assets at their historic cost (i.e. their original purchase price), less depreciation where appropriate, the assets are shown at their current cost (replacement cost) at the time of producing the accounts. This method of accounting is used in tandem with historic cost accounting (HCA) in the water industry because of the importance of capital assets and the fact that historic costs do not reflect the asset's true worth.

Debt premium: The debt premium is that part of an interest rate that represents the corporate risk of the debt instrument above the risk free rate. Investors therefore require the premium to compensate them for the additional risk of the debt instrument over government securities.

Depreciation: Depreciation is a measure of the consumption, use or wearing out of an asset over the period of its useful economic life.

DEFRA: Department for Environment, Food and Rural Affairs.

Discharge consent: Permission granted by the Scottish Environment Protection Agency to an organisation discharging sewage or trade effluent to controlled waters. The permission sets out the conditions under which the organisation may make the discharge.

Domestic properties: Properties used as single domestic dwellings (normally occupied), receiving water and/or sewerage services for domestic purposes only.

Econometric modelling: The use of regression and other statistical techniques to model the relationships that underlie economic and financial results.

Economic leakage level: The point at which further leakage control activity would cost more than alternative means to bridge the gap between supply and demand.

Economic life: The economic life of an asset is the period for which an asset remains useful.

Economies of scale: Economies or savings resulting from the use, management or production of goods in large quantities. A lower cost per unit of output is achieved than would have been the case if smaller quantities were produced.

Efficiency gap: The difference between the current level of efficiency of a water authority and the assessed level of efficiency of the benchmark comparator.

Enhanced option: One of three options for future investment levels proposed by the Scottish Executive as part of the 2002-06 Quality and Standards consultation. The enhanced option 'allows substantial progress towards modernising all assets. It is also the only option that includes significant resources for removing development constraints and first time connections'².

External Financing Limit (EFL): A limit placed on the authority's new debt borrowings by Scottish Ministers.

Financial indicators: Certain financial ratios specified in appointed business licences of English and Welsh companies, such as gearing, interest cover and dividend cover. These are used to measure financial performance.

Financial model: A computer model, which uses historical financial data together with a series of assumptions and scenarios to predict the future incomes and expenditures (and, hence, the revenue caps) of the water authorities.

Financial Reporting Standards (FRSs): Statements of accounting standards as issued by the Accounting Standards Board.

Gaming: Strategic behaviour by companies, aimed at benefiting shareholders by influencing regulation; in particular, the submission of costs for inclusion in the regulatory asset value which are relatively higher than those put into the profit and loss account, thus artificially raising regulatory asset value and earning a higher return.

Gearing: A company's net debt expressed as a percentage of its total capital (i.e. the ratio of net debt to net debt plus equity expressed as a percentage).

Guaranteed Minimum Standards: The minimum level of customer service customers should expect of West, East and North of Scotland Water Authorities set by the Commissioner. If the authorities fail to meet these standards a compensation payment is made.

Highway drainage charge: The part of the surface water drainage charge that covers the drainage of roads.

Historic cost accounting: The traditional form of accounting, in which assets are shown in balance sheets at their cost to the organisation (historic cost), less any appropriate depreciation.

Incumbent: The water undertaker required to provide statutory water services within a geographically defined area. In Scotland these are the three Scottish water authorities.

Indexation: The policy of connecting prices, costs, wages, taxes etc to rises in the general price level, retail prices or other measures of inflation.

Infrastructure assets: Mainly underground assets, such as water mains and sewers and also lochs, dams and reservoirs. A distinction is drawn between infrastructure and non-infrastructure assets because of the way in which the assets are managed, operated and maintained.

Infrastructure renewals charge: An annual accounting provision for expenditure on the renewal of infrastructure assets charged to the income and expenditure account.

Input regulation: Monitoring of the method of delivering required outputs, for example monitoring the number of kilometres of water mains renewed for a given expenditure (see Output regulation).

² Water Quality and Standards, Investment Priorities for Scotland's Water Authorities 2002-2006. Scottish Executive, August 2001.

Interest cover: The number of times a company's profits, before interest and tax, cover interest due on all its borrowings.

June Return: The framework used by Ofwat for the submission of regulatory information by the English and Welsh water and sewerage companies.

Large users: Industrial and commercial customers using significant annual amounts of water, usually more than 100 million litres per year, or the equivalent in sewerage services or trade effluent disposal.

Licence: The water (and sewerage) companies in England and Wales operate under licences granted by the Secretaries of State for the Environment and for Wales, or by the Director of Ofwat, to provide water and sewerage services. The licences impose conditions on the companies, which the Director is required to enforce.

Load: A measure of strength and quantity of waste water, usually expressed in Kg BOD per day.

Megalitre: one million litres, or 1,000 cubic metres.

MI/day: one megalitre per day.

Minimum option: One of three options for future investment levels proposed by the Scottish Executive as part of the 2002-06 Quality and Standards consultation. The minimum option 'meets the standards set by regulations on water and sewage treatment. This option has low-cost solutions and does not tackle the state of fast deteriorating existing assets, such as treatment plants, water mains, sewers and so on³.

Modified historic cost: A basis for valuing assets by increasing the asset cost by inflation each year to represent a more realistic cost level.

Net present value: The economic value of a project, at today's prices, calculated by netting off its discounted cash flow from revenues and costs over its full life.

Network charge: The fixed charge assigned to cover the cost associated with supplying water through the network. This charge is linked to meter size.

Network: The physical assets downstream of production and bulk storage facilities owned by the Scottish water authorities which are essential for the supply of water to customers up to the boundary stopcock of customer premises.

Non-core business: Anything other than core business, for example consultancy services, plumbing, recreation, farming and waste management.

Non-domestic properties: Properties receiving water and/or sewerage services which are used exclusively for public, business, trade or manufacturing purposes, or domestic dwellings also used for commercial purposes.

Non-infrastructure assets: Mainly above ground surface assets such as water and sewage treatment works, pumping stations and company laboratories, depots, workshops and equipment.

Off-network: A privately owned water supply or waste water treatment and disposal system.

Ofgem: Office of Gas and Electricity Markets, regulator of the electricity and gas industries in Great Britain.

Ofwat: Office of Water Services, regulator of the water and sewerage companies in England and Wales.

One-off costs: Costs appearing in the accounts that are not regular occurrences. Examples include redundancy payments, drought costs and unusual legal fees.

Operating costs: Operating expenditure plus capitalised maintenance of assets.

Operating expenditure: The day-to-day cost of running the water and sewerage service, excluding capitalised maintenance of assets.

Opex: Operational expenditure.

Output regulation: Monitoring the results of the method of capital investment, for example the improvements in the drinking water quality index resulting from new water mains being laid (see Input regulation).

³ Water Quality and Standards, Investment Priorities for Scotland's Water Authorities 2002-2006. Scottish Executive, August 2001

Per capita consumption: The estimated amount of water used by each individual and any internal plumbing losses.

PFI: Private Finance Initiative, precursor to Public Private Partnership.

Population equivalent of sewage treatment works: The capacity of sewage treatment works is measured in terms of the amount of organic material that can be treated. It is assumed that one person is equivalent to a load of 60g of biological oxygen demand (BOD). This measure includes industrial waste water treated at works. Hence, the capacity of a works can greatly exceed the population served in the catchment, especially if a large volume of industrial effluent is also treated by the works.

PPP: Public Private Partnership: An agreement between an authority and a private contractor for the building and operation of a waste water treatment works. The assets are owned and run by the contractor, but the land they are built on is usually leased from the water authority. The water authorities pay the contractor a set tariff per cubic meter of treated sewage and sludge. The contractor bears all the construction, maintenance, operating and financial risks associated with the project.

Priority register: An initiative intended to address the needs of customers who may have particular difficulties in the event of an interruption to supply, or who have special needs in terms of information provision. The concept is to create a register, possibly in conjunction with other utilities, of these customers and their needs, so that they receive the service they require.

Privatisation: To transfer the production of goods or services from the public sector of an economy into private ownership and operation.

Procurement efficiencies: Increased value for money achieved through minimisation of the whole life costs of new assets.

Quality and Standards: The standards set by the Scottish Executive and the Scottish Environment Protection Agency to ensure Scotland receives safer drinking water and a cleaner

environment. The standards are determined largely by the policies of Scottish Ministers, which are underpinned by standards agreed within the European Union. The Quality and Standards Process sets out the environmental and drinking water standards that the Scottish water authorities must meet and estimates the investment that is required to meet them. The Quality and Standards programme for 2002-06 was announced by the Minister for the Environment and Rural Development on 29 August 2001.

Quality performance audits: A system of monitoring the performance of the water authorities in handling contacts from customers in terms of compliance with standards and codes, and particularly quality.

Rate of return: The annual income and capital growth from an investment, expressed as a percentage of the original investment.

Rateable value: Commercial property valuation as defined in Section 74 of the Local Government Finance Act 1992.

Regulatory Information: Financial, customer and engineering data collected by the regulator for monitoring, benchmarking and financial analysis.

Regulatory letters: Letters requesting regulatory information from the water authorities by the Commissioner.

Reporters: Independent engineering consultants who are under a duty to report to Ofwat on the accuracy of the English and Welsh companies' annual returns and their delivery of outputs.

Resource accounting and budgeting (RAB): An accounting basis which assists the planning, controlling and reporting on public expenditure. The main changes to accounting practice on a RAB basis is the revaluation of fixed assets to a more realistic cost basis. It is on this cost basis that depreciation is charged. This is known as revaluing assets on a modified historic cost basis. It involves increasing asset cost by inflation each year to represent a more realistic cost level.

Retail price index: The rate of inflation applying to a basket of retail prices over a period of time.

Revenue cap: The revenue cap is the maximum increase in revenue that a water authority can receive through customer charges in any one year.

Scottish Executive: The devolved government in Scotland and their civil service support.

Secondary water and sewerage charges: Charges for any service provided by the water authority, other than for the supply of water and the removal of waste water. For example secondary charges include the charge for connecting to mains water and sewerage, building water supply, field troughs and desludging septic tanks.

SEPA: Scottish Environment Protection Agency. Established in 1996 as the national public body responsible for environmental protection and improvement in Scotland. SEPA regulates potential pollution to land, air and water, the storage, transport and disposal of controlled waste and the keeping and disposal of radioactive materials.

Special factors: Factors taken into account when setting the authorities' operating expenditure targets. An example would be the remoteness of many customers in the North of Scotland.

Specialised quality performance assessments: Water Industry Commissioner for Scotland audit of the performance of a water authority in handling contacts from customers on a particular subject.

Spend to Save: Spend to Save expenditure is spending now to save money later, for example redundancy payments now reduce wage bills in the future.

Supplier of last resort: This supplier has to ensure that basic water and sewerage services are available in the event of a new entrant failing to meet its obligations.

Supply/demand balance: The balance between the amount of a company's available water resource and the demand for water by customers. Any imbalance between supply and

demand can be met via resource enhancement or demand management strategies (e.g. selective metering and leakage control).

Surface water drainage charge: The part of the waste water charge that covers the cost of removing and cleaning impurities and pollution from rainwater from roofs and private lands, as well as from roads and other public areas.

Trade effluent: Industrial waste water other than that produced through normal domestic systems such as sinks and toilets.

WICS: Water Industry Commissioner for Scotland.