



STRATEGIC REVIEW OF CHARGES 2027-2033: DRAFT METHODOLOGY GLOSSARY

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Glossary of terms

Asset: An item of economic value that Scottish Water owns to help it provide services to current and future customers. They can be physical, such as a network of water pipes and treatment works, or intangible such as intellectual property.

Asset lifetime: The length of time an asset functions before requiring replacement. For example, Scottish Water estimates that its large water mains have an expected asset lifetime of around 100 to 130 years.¹

Asset maintenance: Investment in assets in order to maintain existing service levels to customers. This can comprise fixing an existing asset to ensure it meets its expected life (asset repair), extending the life of an existing asset (asset refurbishment) or replacing the asset outright (asset replacement). This may also be referred to as capital maintenance.

Asset replacement: Investment in the replacement of an asset whether that be equipment, or whole process/site or section of infrastructure. This can occur either at the end of the asset life or when the economic cost of continuing to operate the existing asset (in Net Present Value terms, as defined below) is higher than the cost of replacing the asset over a pre-determined period.

Baseline: The financial and investment delivery forecasts and commitments set out in the Final Determination which underpin the charge caps set by WICS. These forecasts cover three broad categories:

- Sources of cash: the revenue and net new borrowing from the Scottish Government that Scottish Water will receive;
- Uses of cash: the expenditure in each area that Scottish Water will require to efficiently run the business and deliver the investment programme; and
- Benefits delivered: the commitments Scottish Water has made to customers in terms of levels of service performance and measurable deliverables from the investment programme (known as investment outputs).

The baseline is usually provided before the regulatory period begins. During the period, WICS will then compare Scottish Water's reported performance against the forecast values and commitments from the baseline and seek to understand any differences. Such monitoring allows WICS to report on whether Scottish Water has delivered the required efficiencies and the investment programme and, ultimately, to hold Scottish Water to account for delivery.

¹ WICS (2019), 'Strategic Review of Charges 2021-2027: 2019 Decision Paper - Asset Replacement', 1 July 2019, p.24.

Scottish Water will be required to produce a delivery plan following the Final Determination. WICS expects that this will be based on Scottish Water's business plan but reflect any amendments made to Scottish Water's proposals through the Final Determination (e.g. to reflect WICS' assessment for the scope for efficiency). WICS will also require Scottish Water to update its delivery plan each year as a way of capturing changes to the baseline from the Final Determination during the regulatory period.

Blue-green infrastructure: According to the European Commission: "a strategically planned network of natural and semi-natural areas with other environmental features designed and managed to deliver a wide range of ecosystem services, such as water purification, air quality, space for recreation and climate mitigation and adaptation." Introducing these networks of green (land) and blue (water) spaces can deliver benefits such as: better environmental conditions; improved health and quality of life for inhabitants; promoting a green economy; and increased biodiversity.²

Business plan: Economic regulators require robust information from the companies that they regulate to set charge caps. This information covers the company's proposals for the forthcoming six-year period and beyond, covering four broad areas:

- financial forecasts;
- investment projects;
- levels of service performance; and
- how the company proposes to fund its operations during the regulatory period, with implications for charges and borrowing required.

It is common practice for economic regulators to ask for this information in the form of a business plan submission.

Capital enhancement: Investment that results in incremental improvements in levels of service provided or levels of compliance. These could be improvements to the quality of water that customers receive, reductions in the environmental impact that Scottish Water has, or improvements to customer service.

Charge cap: A limit on the charges that Scottish Water can levy on its customers.

Charges Scheme: The way in which Scottish Water proposes to charge customers for the services it provides for the following financial year. These charges must be in line with Ministers' Principles of Charging and within the limits set by the Water Industry Commission for Scotland in its Final Determination.

² European Commission (2021), '*Green and Blue Infrastructures*', updated 27 August 2021, webpage.

Contributions to developers: Payments to recognise that a developer’s capital investment in connecting new customers will result in more revenue for Scottish Water once the customer is receiving water and wastewater services.

CPI: The consumer price index (CPI) measures the proportional change in the weighted average prices of a fixed basket of goods and services which a household typically purchases. Changes in CPI are used to measure price changes associated with the cost of living.

Default retail tariff: The default tariff is a maximum charge that customers pay to licensed providers in the retail market for a defined default level of service. Licensed providers compete in the market either by offering a lower price than the default tariff and/or by offering additional or more tailored retail services to their customers.

DWQR: Drinking Water Quality Regulator for Scotland

EBP: Ethical Business Practice

EBR: Ethical Business Regulation

Embodied carbon: The carbon dioxide or greenhouse gas emissions associated with the manufacture and uses of a product or service.

Efficiency: When considering efficiency, WICS examines operating expenditure together with levels of service. Economic regulators consider efficiency in terms of inputs and outputs:

- inputs in this context could relate to the resources used by the company in order to carry out its activities. It can be measured in terms of materials (e.g. chemicals), labour (e.g. staff costs) and capital, or levels of expenditure; and
- outputs in this context could relate to the quantity and quality of water delivered, the volume of wastewater treated and the quality of treated wastewater discharged into the natural environment. Outputs also cover other aspects of levels of service such as the company’s responsiveness to any contact it receives from customers.

Efficiency can then be considered as one of two things:

- minimising input to achieve the same output; or
- maximising output for a given level of input.

Financing: How expenditure is paid for upfront. This may involve, for example, borrowing money to meet investment needs or letting a contract (such as a PFI contract).

Funding: Compared to financing, funding is about who ultimately pays. Such funding can only come from the customers of the service (current and future) or from the tax payer (by way of grants from Government).

Growth investment: Investment that relates to expanding the water supply and enhancing the capacity for wastewater and surface water drainage to meet new demand for these services. This investment could either be in the expansion of existing capacity or it could be in investment in new connections for household or non-household customers. The latter results in additional revenue for Scottish Water.

Intervention: Activity carried out by Scottish Water on an asset.

IPPF: Investment Planning and Prioritisation Framework

IPPG: Investment Planning and Prioritisation Group

Leakage: Water losses from Scottish Water's system before reaching customers (e.g. due to bursts in pipes). The economic level of leakage is the point where the cost saving of reducing leakage is equal to the economic cost of the water lost (including externalities such as carbon).

Licensed providers: Suppliers who operate in the non-household retail market, competing for the custom of non-household customers in Scotland.

Modern Equivalent Asset Value (MEAV): The gross MEAV represents the equivalent replacement cost of the asset and should reflect both the most technically up-to-date new asset and the most technically up-to-date method of constructing that asset.

Natural capital: Elements of nature that directly or indirectly produce value to people, including ecosystems, species, freshwater, land, minerals, the air and oceans.³

Net present value: The net present value of a project is the total benefits achieved over the life of the project minus the total costs, discounted at an appropriate rate.

Net zero emissions: The state at which any emissions emitted by a company are offset by the removal of an equivalent amount of greenhouse gases from the atmosphere.

Nominal/Outturn prices: Values expressed including inflation.

OECD: Organisation for Economic Cooperation and Development

³ Natural Capital Committee (2013), *The state of natural capital: towards a framework for measurement and valuation*, 1 April 2013.

Operational carbon: Greenhouse gas emissions produced each year in the course of running the organisation.

Operating expenditure: Spending on ongoing, day-to-day activities required to provide water and wastewater services. Operating expenditure includes:

- employment costs;
- electricity and other utility costs;
- local authority rates and taxes;⁴
- vehicle running costs;
- the costs of billing and serving customers (including bad debt); and
- the cost of buying materials such as chemicals for water treatment.

Outputs: Tangible deliverables provided by an investment, driven by legislative or other requirements, which will contribute toward meeting investment drivers or outcomes.

Outcomes: Higher-level objectives that customers and society value – for example, a clean water environment.

Per capita: Per person

PFI: Private Finance Initiative contracts. There are different forms of such contracts but these typically involve a private provider providing an asset or service in return for regular payments over the duration of the contract.

Real terms: Values expressed excluding the impact of inflation.

Refurbishment: Investment in a renovation or overhaul of older or damaged equipment or replacement of parts within a piece of equipment to bring the asset back to a workable condition to extend the expected life of the asset.

Regulatory period: The 6-year period over which WICS sets charges for water and sewerage services.

Repairs: Investment in fixing an asset to ensure that it can continue to operate.

Resilience: The ability to withstand/recover from unexpected changes without adverse effects.

Revenue: The income generated from collection of water and sewerage charges.

⁴ This covers non-domestic (or business) rates which are a tax on non-domestic properties to help pay for local authority services such as education, social care, waste management etc.

RPI: Retail Price Index measure of inflation

Sector vision: A shared long term vision for the Scottish water sector both developed and owned by stakeholders. This vision represents a common understanding of what the sector is seeking to achieve.^{5 6}

SEPA: Scottish Environmental Protection Agency

SGIG: Scottish Government Investment Group. This group ensures that the water industry is developing a sufficient programme of investment to meet the Objectives that Ministers set and that the industry is delivering on these objectives. The Scottish Government chairs the SGIG.⁷

Social capital: Social capital is commonly used to describe the relationships and building of trust that help contribute to the success of an organisation.

SRC15: The Strategic Review of Charges 2015-2021

SRC21: The Strategic Review of Charges 2021-2027

SRC27: The Strategic Review of Charges 2027-2033

Tier 1 expenditure: Tier 1 refers to Scottish Water’s broadly recurring costs such as operating expenditure, PFI contract fees, interest costs, taxation and reasonable cost contributions to developers. WICS intends to move away from aggregating expenditure into Tier categories in SRC27. It intends to assess expenditure at a more disaggregated level instead.

Tier 1a expenditure: Tier 1a refers to responsive repair and refurbishment expenditure. WICS intends to move away from aggregating expenditure into Tier categories in SRC27. It intends to assess expenditure at a more disaggregated level instead.

Tier 2 expenditure: Tier 2 refers to expenditures associated with enhancement, growth, asset replacement and planned repair and refurbishment investment. WICS intends to move away from aggregating expenditure into Tier categories in SRC27. It intends to assess expenditure at a more disaggregated level instead.

Unit cost: Expenditure incurred to produce, store, and sell one unit of a particular good or service.

⁵ Scottish Government (2020), *‘The Scottish Water (Objectives: 2021 to 2027) Directions 2020’*, 7 December 2020.

⁶ Scottish Government (2024), *‘2027-33 Commissioning letter’*, 12 June 2024.

⁷ Scottish Government (2024), *‘Water Industry: Scottish Government Investment Group’*, webpage.

Whole-life cost analysis: Whole-life cost analysis involves assessing the total cost of an asset over its lifetime. This includes consideration of the initial cost of the asset as well as the cost of its operation, maintenance and subsequent replacement or disposal.



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