# FEEDBACK ON SCOTTISH WATER’S DRAFT BUSINESS PLAN FOR SRC 2027-2033

28 August 2025

WICS Economic regulation for Scotland’s water

# Contents

# 1. Executive Summary

## 1.1. Background to WICS and the Strategic Review of Charges 2027-33

1.1.1. The Water Industry Commission for Scotland (WICS) is the economic regulator of Scottish Water. Our role is to challenge Scottish Water to deliver long-term value and high quality levels of service for its customers. We do this by setting a cap on how much Scottish Water can charge through a process called the 'Strategic Review of Charges'. This ensures that customers pay no more than necessary for essential water and wastewater services.

1.1.2. Through the Strategic Review of Charges process, we determine the revenue Scottish Water must collect from customer charges to deliver the policy objectives set by Scottish Ministers at the 'lowest reasonable overall cost'. These policy objectives include the Ministerial Objectives, which set out the outcomes Scottish Water must deliver, and the Principles of Charging, which outline how services are paid for, by whom and the charging arrangements that apply.

1.1.3. The next Strategic Review of Charges covers the six years from 1 April 2027 to 31 March 2033 (SRC27). In December 2024, we published our final methodology for this review, setting out the approach we will take to set charge caps and service level targets. Alongside the methodology, we also published business plan guidance and data tables to request the information from Scottish Water that will underpin our analysis and support the setting of charge caps and service level targets.

## 1.2. Building on the approach in SRC21

1.2.1. The final methodology for SRC27 builds on the long-term approach adopted in SRC21, where stakeholders collaborated to develop a sector vision. WICS set charges of CPI + 2% in 2021-27 as a first step towards ensuring that Scottish Water would make appropriate progress towards maintaining service and achieving net zero emissions by 2040, in line with the sector vision.[1] We also explained that given the need to continue transitioning to increased investment, charges will need to increase by a similar amount in real terms of 1.5% to 2% per annum (equivalent to 9-13% in total over 2027-33) over the 2027-33 regulatory period.[2] This approach sought to protect current and future customers by avoiding sudden price shocks while ensuring that service levels are not compromised. We consider that the long-term approach followed in SRC21 remains an important reference point in considering the draft business plan for the 2027-33 regulatory period.

## 1.3. Scottish Water's draft business plan submission

[1] WICS (2020), 'Strategic Review of Charges 2021-27: Draft Determination', October, pp.65-69.
[2] WICS (2020), 'Strategic Review of Charges 2021-27: Draft Determination', October, p.21.

1.3.1. Scottish Water submitted its draft business plan to WICS on 12 June 2025. Before commenting on the content of the plan, we acknowledge the significant effort made by Scottish Water to reach this important milestone. We also appreciate the contributions of stakeholders to date in the SRC27 process. The draft business plan reflects Scottish Water's position at a specific point in time, and we understand that further analysis is ongoing ahead of the final submission in February.

1.3.2. In summary, Scottish Water contains the following proposals:

- charges increasing in line with Consumer Price Index (CPI) inflation + 4% per annum, equivalent to an increase of 27% above inflation over the 2027-33 regulatory period;
- an investment programme of £8.3 billion (2023-24 prices), which represents a 40% increase in the size of the investment programme that Scottish Water plans to deliver over the 2021-27 regulatory period and a 10% increase in investment compared to the level envisaged for 2027-33 regulatory period in the final determination for SRC21;
- of the £8.3 billion of investment, £5 billion (2023-24 prices) is for asset maintenance, representing a c.30% increase in maintenance compared to that planned for the 2021-27 regulatory period; and
- the remaining £3.3 billion (2023-24 prices) is for enhancement and growth, representing a c.70% increase compared to that planned for the 2021-27 regulatory period.

## 1.4. Strengths of the draft business plan

1.4.1. Overall, WICS considers this draft business plan to be one of the stronger submissions produced by Scottish Water in the context of previous Strategic Reviews of Charges. However, we expect the final business plan to be supported by more substantial evidence in several areas, especially given Scottish Water's proposal for a material increase in charges. This expectation is reflected in the comments set out throughout this feedback document.

1.4.2. WICS welcomes Scottish Water's aspiration for customers to be at the heart of its business plan. We consider that the text boxes with "what our customers have told us about…" throughout the business plan are an effective way of demonstrating that the final business plan is grounded in the priorities of customers.[3]

1.4.3. We note that Scottish Water has completed data tables to a good standard, except for the remaining gaps in asset health information and enhancement benchmarking data. Overall, the detail Scottish Water provides on outputs and outcomes in the business plan data tables will enable WICS to set a baseline and ensure that regulators can hold Scottish Water to account for delivery during the 2027-33 regulatory period.

[3] See for example page 56 of Scottish Water's draft business plan document that sets out *"what our customers have told us about addressing climate change"*, Scottish Water (2025), 'SR27 Draft Business Plan – Investing in Scotland's Future', June.

## 1.5. The needs case underpinning the business plan

### THE NEEDS CASE

1.5.1. As set out in paragraph 1.2.1, in SRC21, WICS explained that, given the need to continue transitioning to increased investment, charges will need to increase by CPI + 1.5% to 2% per annum (equivalent to 9-13% in total over 2027-33) over the 2027-33 regulatory period. Scottish Water must ensure that its final business plan provides this linkage back to the SRC21 final determination and clearly explains the factors it considers justify a deviation from the price profile of CPI + 1.5% to 2% per annum.

1.5.2. Scottish Water has not yet demonstrated that it is unable to deliver the outcomes set out in the Ministerial Objectives with CPI + 1.5% to 2% per annum over the 2027-33 regulatory period. WICS considers the assumptions from the SRC21 period a reference point for the 2027-33 period and that it is for Scottish Water to demonstrate where changes to these assumptions are appropriate.

1.5.3. Scottish Water's long-term strategy includes a directional estimate of around £50 billion in investment in water and wastewater services over the next 25 years. As set out in the feedback on that long-term strategy, stakeholders will require confidence in the assumptions underpinning these forecasts, especially given they are used as context for investment proposed in the 2027-33 regulatory period.

1.5.4. On 7th August 2025, Scottish Water began sharing more detailed information in the form of an investment strategy and sub-outcome summary reports.[4] Scottish Water explains that these documents provide the evidence base and outline the process followed in determining how it proposes to deliver the outcomes of its long-term strategy. WICS continues to review these documents. However, at this stage, we consider that there remain gaps in information on the assumptions underpinning the £50 billion estimate of required investment. This represents a gap in the needs case for investment over the 2027-33 regulatory period.

1.5.5. It is essential for Scottish Water to ensure there is a shared view among stakeholders that the investment plan will meet the Ministerial Objectives.[5] From WICS' perspective, this includes explaining whether the proposed investment aligns with the expectations of both DWQR and SEPA in relation to the Ministerial Objectives that apply to them. We expect the final business plan to clearly set out how this alignment has been tested, and how Scottish Water has ensured the plan has the support of customers and its regulators. If there are areas of misalignment, we expect Scottish Water to provide further information on these

[4] Scottish Water (2025), 'Investment Strategy', August. This document is supported by 21 sub-outcome reports covering areas such as water growth, water pressure and network discharges.

[5] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.18.

areas to enable WICS to issue a determination, e.g. the standard information required on the investment programme if related to investment.

1.5.6. The draft business plan is Scottish Water's proposal for what will ultimately become the regulatory contract between Scottish Water and the people of Scotland. It sets out Scottish Water's proposals for charges and what benefits customers, society and the wider environment can expect from it in return for paying these charges. Recognising the proposed 40% increase in investment, which includes a 70% increase in enhancement and growth investment, and the proposal to raise charges by CPI + 4% each year, WICS considers that Scottish Water should seek to improve the benefits it proposes to deliver to customers and the explanation of the consequences of not delivering or delaying investment.

### CUSTOMER RESEARCH ON THE PROPOSED PATHS

1.5.7. WICS considers that clearly demonstrating the benefits of the business plan proposals was a key theme in customer feedback during the development of the draft plan. WICS notes that Scottish Water tested the following charge paths with customers (research activity 1):

- CPI + 2% a year;
- CPI + 4% a year; and
- CPI + 6.5% a year.

1.5.8. Customer feedback indicated that none of the proposed charge paths offered sufficient value to receive full endorsement from customers. Following this feedback, Scottish Water developed a revised scenario of CPI + 4% which included a rebalanced investment programme and improved outcomes for testing with customers (research activity 3). Scottish Water explains that customers generally felt that the investment programme was more balanced and showed greater ambition. Scottish Water should provide further evidence for why only the CPI + 4% scenario with improved outcomes was tested with customers given that the initial feedback from research activity 1 was inconclusive.

1.5.9. Scottish Water should also examine whether it is feasible to deliver the Ministerial Objectives and improved outcomes with a rebalanced CPI + 2% scenario. If it is feasible, Scottish Water should include CPI + 2% as one of the charge path scenarios (either replacing one of or in addition to the three charge paths in the draft business plan) and seek to test this with customers. This recognises that CPI + 2% was consistent with the long-term price path set out in SRC21. WICS reserves the right to conduct its own research if it considers that the different scenarios for price and service outcomes have not been adequately tested.

## 1.6. Evidencing further the ambition in the draft business plan

## OUTCOMES

1.6.1. In developing the business plan guidance, WICS developed a list of candidate outcome measures based on Scottish Water's current measures, standard industry measures and best practice in asset management. We expect outcome measures to reflect the benefits to customers of the investment, and we are pleased to note that the draft business plan includes 39 of the 44 proposed measures.

1.6.2. WICS also identified outcome measures requiring further development, including:

- sewerage infrastructure discharges
- environmental performance; and
- a communities experience measure.

1.6.3. Scottish Water must demonstrate that it has examined and tested different options for outcome measures in each area. For example, in relation to sewerage infrastructure discharges, WICS notes that Scottish Water proposes to measure the impact of sewerage infrastructure discharges based on the number of unsatisfactory intermittent discharges, which places environmental risk and harm as the focus. Recognising the public interest in this area, we consider that Scottish Water should engage with stakeholders on the different options for a measure (or measures) in this area. If Scottish Water is unable to develop appropriate measures, WICS may decide to add its own measures as part of our draft and final determination to protect the interests of customers and the environment.

1.6.4. WICS' final methodology makes clear that customer research should underpin Scottish Water's proposals for outcome measures and targets in its business plan submission.[6] We note that Scottish Water's forecasts significant improvements in the following measures:

- water supply interruptions;
- meeting peak demand;
- demand in during a worst historic drought;
- lead pipe removal in the public network; and
- drinking water quality risks.

1.6.5. However, we note that for the other outcome measures Scottish Water forecasts that performance will remain broadly stable (e.g. per capita consumption, average minutes lost due to water supply interruption, discharge permit compliance and pollution incidents) or deteriorate (e.g. taste and odour contacts and external sewer flooding).

1.6.6. WICS seeks clarity on how Scottish Water has taken account of the customer research in identifying the priority outcome measures for improvements. For example, we need to

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[6] WICS (2024), 'Strategic Review of Charges 2027-33: Final Methodology, December, p.131.

understand whether the five outcomes listed in paragraph 1.6.4 are consistent with the outcomes that customers value most highly.

1.6.7. As a general observation, WICS questions whether Scottish Water is providing sufficiently stretching forecasts (in line with the principles set out in our methodology) for performance on the outcome measures. If Scottish Water considers that the forecasts are stretching given the external challenges that it faces, then Scottish Water should provide further explanation of these external challenges. Initial feedback from industry stakeholders on Scottish Water's draft business plan suggests that this is a common theme.

1.6.8. WICS has also benchmarked Scottish Water's forecast performance against both Scottish Water's current performance and the performance of the water and wastewater companies in England and Wales, where there are comparable measures. Based on this review, while recognising the forecasts should reflect the priorities of customers, Scottish Water could propose more ambition for some of its outcome measures, including in leakage reduction and customer contacts – see sub-section 4.4, Figure 6 and Figure 7.

1.6.9. As a broader point, we also consider that Scottish Water should engage with the relevant industry stakeholders on the outcome measures and forecasts in developing the final business plan to ensure broad support for them. Scottish Water must also demonstrate complete alignment with the principles for outcome measures from the final methodology.[7]

## EFFICIENCY

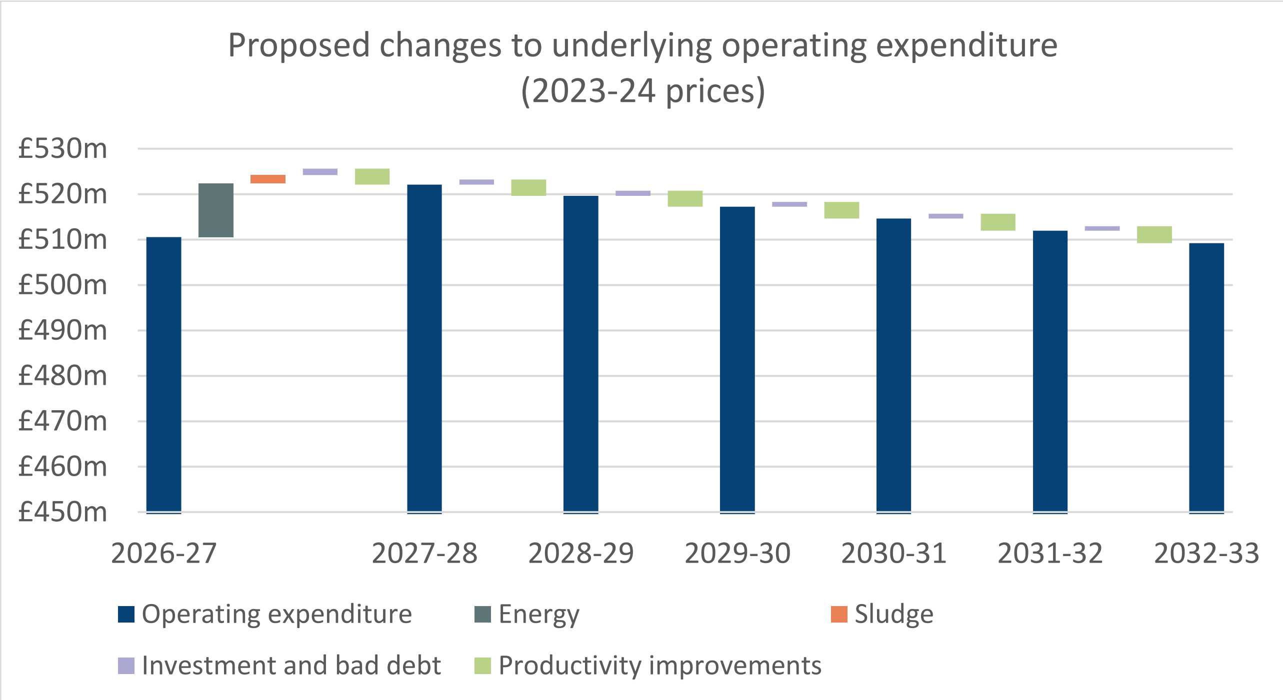
1.6.10. We welcome the engagement with Scottish Water on developing approaches to assess its relative efficiency on operating expenditure compared to the companies in England and Wales. Scottish Water positions itself among the leading companies in Great Britain based on Ofwat's base cost models, after adjusting for differences in capital maintenance levels and the relative rurality of its operating area. In March 2025, we provided additional feedback highlighting areas where the evidence should be strengthened. We note that some of the points raised in our feedback are not yet reflected in the draft business plan, recognising that Scottish Water was preparing to sign off the plan internally ahead of sharing the draft plan with stakeholders in June.

1.6.11. WICS welcomes Scottish Water's long-term strategy commitment to maximise efficiency and minimise the funding required from customers. At an overall level, we note that Scottish Water proposes material additions to operating expenditure in the final two years of the 2021-27 regulatory period, which increases underlying operating expenditure (before the return of wastewater assets upon the expiry of PFI contracts) to £510m. Scottish Water then proposes further additions over the 2027-33 regulatory period with efficiencies bringing operating expenditure back down to £510m by 2032-33, as shown in Figure 1. At an overall

[7] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.133.

level, WICS questions whether the proposed profile of operating expenditure aligns with Scottish Water's commitment from its long-term strategy to maximise efficiency and minimise the funding it requires.

*Figure 1: Proposed changes to underlying operating expenditure over 2027-33*




1.6.12. We also consider that if Scottish Water's operating expenditure increases in line with its proposed forecasts for 2025-26 and 2026-27, it will underperform the forecasts for the efficient level of operating and PFI expenditure set in the final determination for the 2021-27 regulatory period. Furthermore, Scottish Water's operating expenditure would exceed the benchmark level of efficiency based on the operating efficiency of the companies in England and Wales. Taken together, these points lead WICS to question whether these proposed additions represent efficient expenditure.

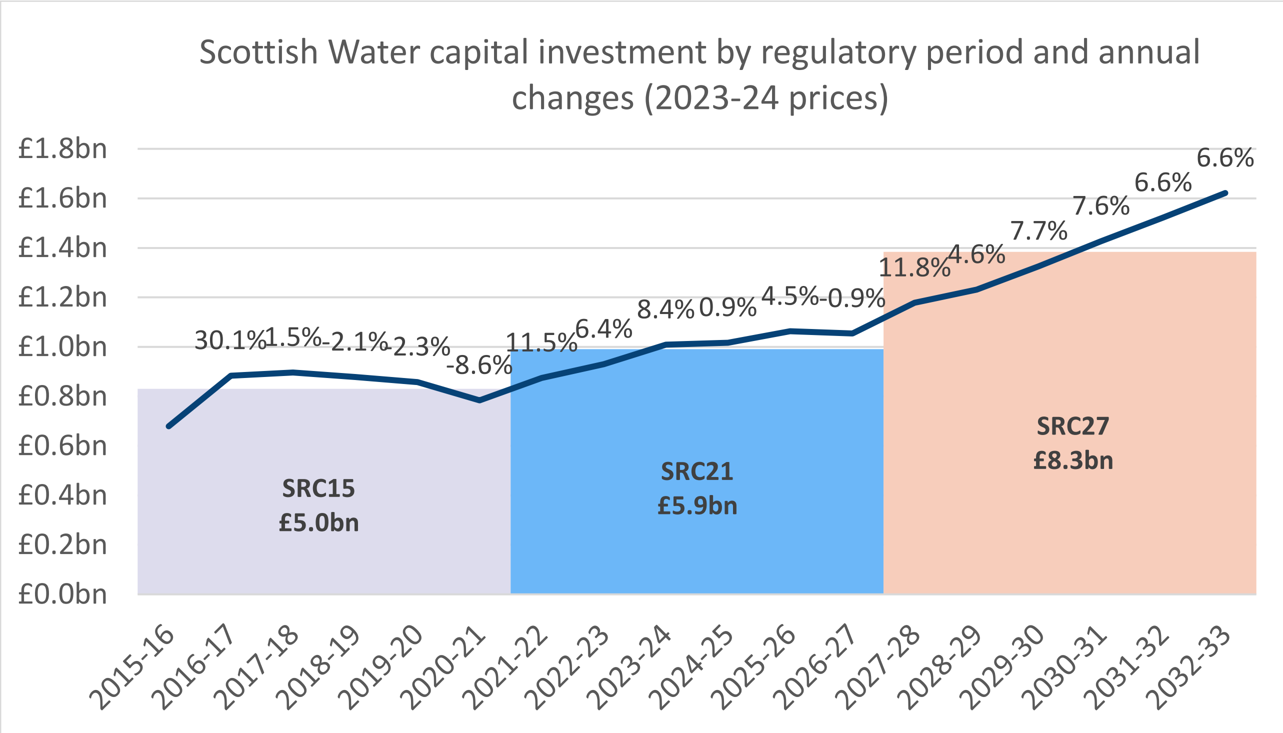
1.6.13. Scottish Water proposes an assumption for productivity improvements of 0.8% per annum. Our starting point remains that the 1% per annum productivity efficiency target will continue to apply unless Scottish Water provides compelling evidence to justify a lower figure. This assumption for productivity improvements of 1% per annum is also consistent with recent regulatory precedent.

## 1.7. Ensuring efficient investment

### DELIVERABILITY OF THE INVESTMENT PROGRAMME

1.7.1. Scottish Water proposes an investment programme of £8.3 billion (2023-24 prices) within its draft business plan with a gradually increasing profile over the 2021-27 regulatory period as shown in Figure 2 below. This represents around a 40% increase compared to the planned investment programme for the SRC21 period of £5.9 billion (2023-24 prices).

*Figure 2: Capital investment by regulatory period*




1.7.2. WICS' final methodology requires Scottish Water to demonstrate that its investment programme is deliverable, considering factors such as the capacity of the supply chain and Scottish Water's internal capacity.

1.7.3. The business plan Technical Appendix 11 (TA011) provides further explanation of Scottish Water's supply chain and procurement of its proposed investment delivery model. This new delivery model will fundamentally change how Scottish Water delivers its investment programme by creating new roles and responsibilities. For example, Scottish Water is developing a new 'primary designer' role, consisting of 1-2 partners from the supply chain who will work closely with existing teams to promote standardisation in asset delivery. WICS notes that this will represent significant organisational and cultural change within Scottish Water, raising further questions over how quickly it could embed the new delivery model and scale up its investment programme, especially noting the 12% increase in investment proposed in the 2027-33 regulatory period shown in Figure 2.

1.7.4. We continue to engage with Scottish Water on the deliverability of the capital investment programme. However, WICS considers that there is insufficient evidence at this stage to demonstrate that the proposed investment programme is deliverable, recognising that the procurement of the new partners remains underway.

## ASSET MAINTENANCE

1.7.5. Scottish Water's draft business plan includes asset maintenance investment of £4,961m, representing a 30% uplift in maintenance investment between 2021-27 and 2027-33 regulatory periods.

1.7.6. As explained above, the final determination in SRC21 marked a change in approach to focusing on the sector's long-term investment needs. This is important as it smooths the profile of charges, while ensuring that service levels are not compromised.

1.7.7. The final methodology builds on the approach in SRC21 by requiring Scottish Water to provide asset condition measures that demonstrate the impact of maintenance activities on its asset base and, as far as possible, translate the impact of these activities into tangible consequences that customers will understand.

1.7.8. WICS welcomes that Scottish Water provides more detailed data on water main condition and performance in the business plan data tables. However, the sewer condition data was not completed at the time of the draft submission, and this remains a notable gap in the information provided. We note that Scottish Water has committed to completing the sewer condition data in line with the guidance for the final business plan and would welcome early visibility of this ahead of the final business plan.

1.7.9. Furthermore, the draft business plan explains that Scottish Water continues to develop an outcome measure for asset health and proposes three options. The draft business plan also suggests working collaboratively on these measures with WICS and other stakeholders with a view of the measure becoming a 'shadow' measure in the 2027-33 regulatory period. Recognising the significant maintenance expenditure proposed for the 2027-33 regulatory period, in line with the final methodology, WICS requires that the business plan includes a tangible measure with forecasts for the 2027-33 regulatory period. Scottish Water should also demonstrate further that it has fully met the requirement from the final methodology to translate the impact of its maintenance activities into tangible consequences that customers will understand.

1.7.10. As part of this evidence, Scottish Water could explain how its maintenance activities over 2021-27 have impacted the asset base and customer outcomes. Such an assessment could help Scottish Water justify maintenance requirements for the 2027-33 regulatory period, especially for asset categories where Scottish Water proposes maintenance investment in line with current levels.

1.7.11. If Scottish Water cannot provide the evidence requested from the final methodology, then WICS will take responsibility for developing an asset health measure during the 2027-33 regulatory period in consultation with Scottish Water.

## INVESTMENT CASES

1.7.12. For projects that involve an element of enhancement or growth and are in the early stages of development (pre-Scottish Water's internal gate 50), the final methodology requires Scottish Water to provide assumptions for indicative costings and outputs.

1.7.13. For projects and programmes of work that are in development (Scottish Water's internal Gate 50 onwards), the final methodology requires Scottish Water to provide standard information as part of an investment case. The final methodology explains that all projects with a whole life cost above £6m must have a separate investment case, with all other investment captured in investment cases for programmes of work.

### Programmes of work and projects in early stages of development (pre-Gate 50)

1.7.14. In the draft business plan, Scottish Water did not provide its assumptions for indicative costings and outputs for projects for investment pre-Gate 50. To further detail our expectations in this area, we expect Scottish Water to set out the rationale for the investment need and the assumptions for benefits and costs. This includes explaining the methodology used to calculate the estimates and providing the underpinning assumptions.

### Programmes of work and projects requiring an investment case (Gate 50 onwards)

1.7.15. The draft business plan includes 14 project investment appraisal (PIAs) documents and 51 management approaches (MAs), which are internal documents that Scottish Water uses to prioritise investment.

1.7.16. From our review of the business plan data tables, we note that Scottish Water provided investment cases for two-thirds of the investment that met the criteria. Table 1 below includes a list of some of the high-value projects and programmes that met the criteria but did not have an investment case as part of the draft business plan submission.

*Table 1: Sample of projects and programmes meeting the threshold without an investment case in the draft business plan submission*

| Unique ID | Description | Proposed cost over SRC27 | Total cost |
|---|---|---|---|
| **Various** | UID Programme[8] | £393.3m | £467.6m |
| **Under£6M-837 (Reference) Scenario A** | To reduce flood risk to customers impacted by repeat high consequence internal sewer flooding when not disproportionately expensive | £108.4m | £145.7m |

[8] WICS notes that the UID programme is not fully past Gate 50, however, it is a high-value programme with some constituent projects being on the Committed List or past Gate 50. As such, we would expect an investment case to be submitted.

| | | | |
|---|---|---|---|
| **Under£6M-532 (Reference) Scenario A** | Improve Water Treatment Works (WTWs) with persistent non-trivial fails (Group 1) (committed / enforced). | £16.2m | £88.7m |
| **Under£6M-835 (Reference) Scenario A** | To reduce flood risk to customers impacted by repeat high consequence external sewer flooding where not disproportionately expensive | £22.6m | £36.3m |
| **Under£6M-533 (Reference) Scenario A** | Improve Water Treatment Works (WTWs) with persistent non-trivial fails (Group 2) | £19.6m | £27.4m |
| **Under£6M-536 (Reference) Scenario A** | Develop solutions at 21 sites (auto shutdown / run to waste) | £15.2m | £19.1m |
| **P5363110201-837 (Reference) Scenario A** | W571 - Dolphin Road Glasgow | £13.7m | £14.5m |

1.7.17. Scottish Water provided some of the standard information required in these areas in response to WICS' queries. We reiterate the requirement for full investment cases for all relevant projects and programmes which meet the final methodology criteria to be provided leading up to and as part of the final business plan.

1.7.18. To provide greater confidence in this area, we require Scottish Water to submit a list of the projects and programmes it expects will meet these criteria by the time of the final business plan by 29 September 2025.

1.7.19. We consider Scottish Water's internal PIAs currently do not cover all of the standard information requested as part of the investment case, including the range of options considered to meet the need for investment. It is for Scottish Water to decide how it meets the requirements from the final methodology; however, as a minimum we expect the standard information requested on investment projects and programmes of work as set out in our final methodology.

## DALDOWIE PFI

1.7.20. Following the return of the Daldowie PFI asset from the operator in 2026, Scottish Water proposes to build an advanced anaerobic digestion (AAD) facility. This is part of a wider strategy for the treatment, recovery and/or disposal of the biosolids (the byproduct of wastewater treatment) in West Central Scotland, which is expected to cost around £460m across the different sites that would use the new facility.[9]

[9] Scottish Water's response to the draft business query number 5 explains that the c.£460m value includes the West Central Bioresource project work at Daldowie for £325 in SRC27, as well as various enabling works at Sludge Treatment

1.7.21. The commissioning letter for the SRC27 regulatory period explains that Scottish Water should "consider the options and costs for the future operation and funding of these assets". The letter then requests that "the Commission undertake a full examination of Scottish Water's approach to establishing the options and costs with an overall assumption that these assets should return to public ownership."[10]

1.7.22. Scottish Water's preferred option is an AAD facility on the existing site of the Daldowie PFI, which would be funded from customer charges and borrowing in 2027-33. WICS notes that this investment accounts for around a quarter of Scottish Water's proposed charge increase for the 2027-33 regulatory period. As such, Scottish Water must demonstrate that the proposed option represents best value for customers, both current customers in the 2027-33 regulatory period and future customers.

1.7.23. There may be scope to consider further public-private finance arrangements such as the proposed mutual investment model (MIM) that has been examined by the Scottish Futures Trust.[11] Given the size of the proposed investment and the potential scope for adopting new technologies and innovation relating to resource recovery, the use of a MIM could be considered further as one of the possible options for this project. WICS requests that Scottish Water provides further analysis on the prospect of extending the life of the existing asset to enable greater consideration of potential alternative financing options such as a MIM.

## CAPITAL EFFICIENCY

1.7.24. The final methodology sets out the elements of Scottish Water's proposed efficiency work plan, covering:

- using external consultants to benchmark the direct construction costs;
- benchmarking Scottish Water's overheads against those of other companies in England and Wales;
- benchmarking against Scottish Water's outturn costs of delivering similar projects in previous years;
- benchmarking Scottish Water's enhancement cost forecasts using the data-sets available from econometric modelling of enhancement costs of the companies in England and Wales; and

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sites including Meadowhead, Kinneil Kerse, Galashiels, Dalderse & Cumnock and improvements to the Greater Glasgow Sludge Main. Scottish Water has indicated there have been updates to the business case since the draft business plan submission which will be reflected in the final business plan.

[10] Scottish Government (2024), '2027-33 Commissioning letter', 12 June 2024.

[11] The Scottish Futures Trust examined privately financed, privately classified, revenue funded investment models to support the Scottish Government in delivering its National Infrastructure Mission and recommended the option of a mutual investment model (MIM) that met this requirement. See Scottish Futures Trust (2019), 'An options appraisal to examine profit sharing schemes, such as the Welsh Mutual Investment Model, to secure investment for the National Infrastructure Mission and best value for tax payers', April.

- conducting an external review of a sample of projects from Scottish Water's investment plan.

1.7.25. The final methodology also explains that WICS would undertake a review of a sample of projects and programmes, to understand:

- the investment need as part of the investment case;
- whether the scope of solution is appropriate; and
- the cost efficiency of the solution proposed.

1.7.26. Scottish Water provided early visibility of the findings from its efficiency work plan in February 2025, with WICS providing feedback in March 2025. We note that some of the points raised in our feedback are not yet reflected in the draft business plan, for the same reason as provided in paragraph 1.6.10.

1.7.27. The draft business plan continues to assume that Scottish Water's capital efficiency is broadly in line with the average (based on a median) performance of the companies in Great Britain and that there is no further scope to catch up with best practice. While the draft business plan assumes that there is no scope to catch up to best practice, it assumes ongoing productivity improvements of 0.8% per annum.

1.7.28. As Scottish Water has not yet addressed comments provided in March, we expect further evidence to demonstrate that no further efficiency to catch up with best practice is possible. In addition, the information required to support benchmarking of enhancement costs has not yet been provided, despite concerns raised in both February and March. We require that this information be submitted by 29 September 2025.

1.7.29. Scottish Water proposes an assumption for ongoing productivity improvements of 0.8% per annum. As set out above, our starting point is that a productivity efficiency improvement of 1% per annum from SRC21 should continue to apply unless Scottish Water provides compelling evidence to justify a lower figure. This assumption for productivity improvements of 1% per annum remains in line with the recent regulatory precedent.

## 1.8. Financial assumptions

1.8.1. WICS welcomes its work to date with Scottish Water to jointly develop the financial model for SRC27, which it considers a good example of EBP&R in practice. By using the same financial model to forecast charge caps, both organisations can focus on the material assumptions that impact charge caps over the 2027-33 regulatory period. As set out above, we consider that the assumptions from the SRC21 period are a reference point for the 2027-33 period, and that it is for Scottish Water to evidence where changes to these assumptions are appropriate (e.g. for assumed productivity improvements).

1.8.2. WICS welcomes the commitment from Scottish Water's long-term strategy to do as much as it can to minimise the funding that it needs from customers.[12] In this regard, we consider that Scottish Water should strengthen the evidence in the following two areas:

- operating expenditure; and
- non-household revenues.

1.8.3. WICS considers that based on updated assumptions in these two areas, as well as for other assumptions where the differences between WICS and Scottish Water are less material, continuing with the current charge cap of CPI + 2% could allow for investment of up to £7.9 billion in 2023-24 prices. This investment is around £400m lower than the investment proposed in Scottish Water's draft business plan, suggesting that investment would need to be prioritised further and/or additional efficiencies would be required under if the long-term charge cap of CPI + 2% per annum is adopted over the 2027-33 regulatory period.

## 1.9. Next steps

1.9.1. Based on our feedback on the draft business plan, we clarify some of the requirements from the final methodology in section 6 of this document, such as the expectation for Scottish Water to finalise the delivery plan in February 2027. The delivery plan will set out how Scottish Water plans to meet the requirements of the final determination and will provide a baseline for the 2027-33 regulatory period before the period begins on 1 April 2027.

1.9.2. WICS concludes this feedback by recognising the significant effort Scottish Water has made in reaching this important milestone in the Strategic Review of Charges 2027-33. We look forward to continuing close and constructive engagement with Scottish Water and stakeholders in the lead-up to the final business plan submission and beyond, consistent with the principles of EBP&R.

[12] Scottish Water (2025), 'Our sustainable future together: long-term strategy', May, p.52.

# 2. Introduction

## 2.1. The Strategic Review of Charges 2027-33

2.1.1. The Water Industry Commission for Scotland (WICS) is the economic regulator of Scottish Water. Our role is to challenge Scottish Water to deliver long-term value and high quality levels of service for its customers. We do this by setting a cap on how much Scottish Water can charge through a process called the 'Strategic Review of Charges'. This ensures that customers pay no more than necessary for essential water and wastewater services.

2.1.2. Through the Strategic Review of Charges process, we determine the revenue Scottish Water must collect from customer charges to deliver the policy objectives set by Scottish Ministers at the 'lowest reasonable overall cost'. These policy objectives include the Ministerial Objectives, which set out the outcomes Scottish Water must deliver, and the Principles of Charging, which outline how services are paid for, by whom and the charging arrangements that apply.[13]

2.1.3. The next Strategic Review of Charges involves setting charge caps for the six years from 1 April 2027 to 31 March 2033 (2027-33). In December 2024, WICS published its final methodology for the Strategic Review of Charges 2027-33 (SRC27).[14] The final methodology sets out:

- a detailed timeline for SRC27 that aligns with the key milestones and dates set out in the Commissioning letter of the Scottish Ministers;[15] and
- WICS approach to setting charge caps.

2.1.4. Alongside the methodology, we published business plan guidance and data tables to request the information from Scottish Water that will underpin our analysis and support the setting of charge caps and service level targets in line with the approach set out in the final methodology.[16]

## 2.2. Building on the approach in SRC21

[13] Further information on the role of the Ministerial Objectives and Principles of Charging is provided in WICS final methodology. WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.30.
[14] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, available at: 2027-33 Final Methodology | WICS, last accessed on 30 July 2025.
[15] Scottish Government (2024), 'Commissioning the Strategic Review of Water Charges: 2027-2033', available at: 2027-33 Commissioning letter | WICS, last accessed on 30 July 2025.
[16] WICS (2024), 'Final Business Plan Guidance and Definitions', 12 December 2024, available at: 2027-33 Final Methodology | WICS, last accessed on 30 July 2025.

2.2.1. The final methodology for SRC27 builds on the long-term approach adopted in SRC21, where stakeholders collaborated to develop a sector vision.[17] WICS set charges of CPI + 2% in 2021-27 as a first step towards ensuring that Scottish Water would make appropriate progress towards maintaining service and achieving net zero emissions by 2040, in line with the sector vision.[18] We also explained that given the need to continue transitioning to increased investment, charges will need to increase by a similar amount in real terms of 1.5% to 2% per annum (equivalent to 9-13% in total over 2027-33) over the 2027-33 regulatory period.[19] The approach sought to protect current and future customers by avoiding sudden price shocks while ensuring that service levels are not compromised. The long-term approach followed in SRC21 remains an important reference point in considering the draft business plan for the 2027-33 regulatory period.

## 2.3. Scottish Water's long-term strategy

2.3.1. WICS' final methodology required Scottish Water to develop a business plan set in the context of a long-term water sector vision.

2.3.2. In February 2025, Scottish Water consulted on its long-term strategy covering the period up to 2050. Its strategy provides further detail on Scottish Water's contribution to the long-term sector vision. It sets out the opportunities and challenges ahead for the industry and the proposed outcomes that Scottish Water will deliver over that timeframe.

2.3.3. WICS responded to the consultation on the long-term strategy, highlighting that Scottish Water will need to evidence:[20]

- its estimate of £50 billion of investment required in water and wastewater services over the next 25 years;
- how it has taken account of affordability with the proposed charge increases, particularly if it seeks to deviate from the indicative charge profile for SRC27 provided in SRC21;
- that it has explained the importance of the outcomes that customers will receive from the proposed investment, including the investment in asset maintenance; and
- that the proposed investment programme is deliverable, taking account of Scottish Water's internal capacity and external factors such as capacity of the supply chain recognising the large investment programmes underway in England and Wales as part of the Asset Management Period 8 (AMP8).

[17] The Commissioning letter for the SRC21 regulatory period explained that 'Ministers will look to the water industry to develop and work towards a coherent vision describing the longer term nature of the industry and what it can achieve'. See WICS (2020), 'Strategic Review of Charges 2021-27: Draft Determination', October, p.92.
[18] WICS (2020), 'Strategic Review of Charges 2021-27: Draft Determination', October, pp.65-69.
[19] WICS (2020), 'Strategic Review of Charges 2021-27: Draft Determination', October, p.21.
[20] WICS (2025), 'Response to Scottish Water's draft long-term strategy', letter dated 21 March 2025, available at WICS-Letter-LTS_0.pdf, last accessed on 30 July 2025.

2.3.4. Scottish Water finalised and published its long-term strategy in May 2025.[21]

## 2.4. Efficiency plan

2.4.1. The final methodology required Scottish Water to share initial findings from its efficiency analysis for operating and capital investment by February 2025 ahead of its draft business plan submission in June. Scottish Water shared this initial analysis with WICS in February 2025 with WICS providing its working-level feedback on the initial analysis in March 2025. We welcome the engagement to date on Scottish Water's efficiency position and support the joint work to develop a shared data-set and a common understanding of methodology changes to ensure that the efficiency modelling is appropriate when applied to Scottish Water.

2.4.2. WICS' feedback on Scottish Water's initial efficiency analysis was that further evidence is required to demonstrate it is among the most efficient companies in the industry across operating and capital expenditures and that there is no remaining scope to improve efficiency to catch up with best practice levels.

2.4.3. We also shared more specific feedback on Scottish Water's analysis of operating and capital investment efficiency. We note that some of the points raised in our feedback are not yet reflected in the draft business plan, recognising that Scottish Water was preparing to sign off the plan internally ahead of sharing the draft plan with stakeholders in June.[22] This document refers to this feedback on the efficiency proposals when commenting on Scottish Water's specific proposals for operating and capital investment efficiency.

## 2.5. Scottish Water's draft business plan

2.5.1. Scottish Water shared its draft business plan with WICS on 12th June 2025. The draft business plan provides Scottish Water's view of the funding it requires over the six years from 2027-33 to meet the Objectives of the Scottish Ministers. It sets out:

- the outcomes customers will receive in line with the Objectives of the Scottish Ministers;
- the investment required to deliver those outcomes;
- the efficient level of expenditure;
- the required level of revenue and borrowing;
- proposed charge caps; and
- the assurance that Scottish Water has conducted on the proposals, including assurance on whether its expenditure forecasts are efficient, the proposed charges are affordable, the investment programme is deliverable, and the plan commands customer support.

[21] Scottish Water (2025), 'Our sustainable future together', May, available at: Our Sustainable Future Together - Scottish Water, last accessed on 30 July 2025.
[22] WICS (2025), 'WICS response to the efficiency evidence summary document for sharing ahead of draft business plan submission', letter dated 28 March 2025.

2.5.2. Scottish Water also shared accompanying documents, including:

- eighteen technical appendices;
- data tables and accompanying commentary;
- management approaches and project investment appraisals;
- the report from the Scottish Water independent customer group (ICG) on Scottish Water's customer research programme; and
- consultant reports.

2.5.3. In terms of content, Scottish Water's draft business plan contains the following proposals:

- charges increasing in line with Consumer Price Index (CPI) inflation + 4% per annum, equivalent to an increase of 27% above inflation over the 2027-33 regulatory period;
- an investment programme of £8.3 billion (2023-24 prices), which represents a 40% increase in the size of the investment programme that Scottish Water plans to deliver over the 2021-27 regulatory period and a 10% increase in investment compared to the level envisaged for 2027-33 regulatory period in the final determination for SRC21;
- of the £8.3 billion of investment, £5 billion (2023-24 prices) is for asset maintenance, representing a c.30% increase in maintenance compared to that planned for the 2021-27 regulatory period; and
- the remaining £3.3 billion (2023-24 prices) is for enhancement and growth, representing a c.70% increase compared to that planned for the 2021-27 regulatory period.

## 2.6. WICS feedback on the draft business plan submission

2.6.1. The next stage of SRC27 involves WICS and the industry stakeholders providing feedback on Scottish Water's draft business plan.

2.6.2. WICS recognises the significant efforts of Scottish Water in preparing its draft business plan and welcomes the information provided and accompanying documents. We also acknowledge the vital contributions of industry stakeholders to date in the SRC27 process.

2.6.3. The information provided in the data tables provide a strong foundation for Scottish Water's delivery plan for 2027-33, which we expect to be published in February 2027 and will provide further detail on how Scottish Water will meet the requirements from the final determination.[23] This will ensure that WICS and the industry stakeholders can hold Scottish Water to account for delivery on behalf of customers over the 2027-33 regulatory period.

2.6.4. WICS recognises that Scottish Water's draft business plan reflects Scottish Water's analysis at a point in time and that several areas of the draft business plan will be developed further

[23] For a further explanation of the delivery plan, see page 31 of the WICS final methodology. WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.31 and pp.126-127.

ahead of the final business plan submission. We welcome that Scottish Water has provided some visibility of areas that remain under development. While we recognise that this is the case, our feedback also covers these areas for completeness.

2.6.5. As Scottish Water's economic regulator, our feedback will inevitably focus on areas where the final business plan could be strengthened. This focus is not intended to overlook the strengths of the draft plan but to reflect the importance of this feedback stage in the Strategic Review of Charges process and the materiality of areas that could be strengthened to improve the overall Strategic Review of Charges outcome.

## 2.7. Structure of this feedback document

2.7.1. This document provides WICS feedback, covering:

- strengths of the plan;
- areas requiring further evidence;
- financial assumptions; and
- methodology clarifications and next steps.

2.7.2. This document also includes three appendices, covering:

- financial model assumptions;
- operating expenditure efficiency analysis; and
- other points that WICS identified in its review of the draft business plan and accompanying documents.

# 3. Strengths of the plan

## 3.1. Overview of the chapter

3.1.1. This chapter provides a summary of areas of the business plan that WICS welcomes, covering both:

- The business plan;
- The business plan data tables and commentary.

## 3.2. Business plan

### GENERAL COMMENTS

3.2.1. Overall, WICS considers this draft business plan to be one of the stronger submissions produced by Scottish Water in the context of previous Strategic Reviews of Charges. A key improvement compared to earlier business plans is the inclusion of the Technical Appendices, which have been helpful in aiding understanding, as they provide more detailed explanations. However, we expect the final business plan to be supported by stronger more substantial evidence in several areas, especially given Scottish Water's proposal for a material increase in customer charges.

3.2.2. We welcome that Scottish Water has addressed most of the requirements set out in the 2027-33 final methodology and has been transparent in identifying remaining gaps and areas where further evidence is required. These are covered in section 4.

### CUSTOMER FOCUS

3.2.3. WICS welcomes Scottish Water's aspiration for customers to be at the heart of its business plan. We consider that including boxes with the heading "what our customers have told us about…" throughout the plan is an effective way of ensuring that the business plan reflects the priorities of customers as identified through customer research. While this is the case, WICS has specific comments on the customer research in section 4.

### IDENTIFYING NEW WAYS OF WORKING

3.2.4. As set out in our response to Scottish Water's long-term strategy (see paragraph 2.3.3), WICS recognises several challenges that Scottish Water has identified.

3.2.5. Given these challenges, we welcome Scottish Water's recognition in the draft business plan that continuing to deliver reliable and resilient services at a price that remains affordable to customers will require new ways of working. As explained in the 2027-33 final methodology, a key aspect of this new way of working will involve working with others to find better solutions for customers and the environment. WICS welcomes Scottish Water's recognition of how it can work actively with other organisations, customers, and communities to develop new solutions with lower whole-life costs than standard engineering solutions (e.g., working with customers to reduce demand placed on Scottish Water's services, rather than immediately opting for the standard engineering solutions to increase the water supply or sewer capacity).

3.2.6. While we welcome Scottish Water's recognition of the importance of partnership approaches, WICS considers that Scottish Water could set out more clearly the specific projects or areas where it proposes to pursue a partnership approach in the 2027-33 regulatory period. This will be key in ensuring that services remain reliable and resilient at a price that remains affordable to customers.

3.2.7. In chapter 7 of the draft business plan, Scottish Water also commits to continuing to manage its assets responsibly. Our approach in SRC21 started a journey towards gaining a better understanding of Scottish Water's future maintenance requirements. WICS welcomes that Scottish Water's asset management policy forms part of its plans to work differently. Scottish Water's approach to asset management should play a key role in ensuring that the cost of providing water and wastewater services remains efficient. For example, one crucial way of ensuring that costs remain efficient is for Scottish Water to maximise the useful life of existing assets, which aligns with the Scottish Government's investment hierarchy of maintaining existing assets before building new assets.[24]

### SCOTTISH WATER'S ENGAGEMENT WITH WICS

3.2.8. In developing its draft business plan, Scottish Water has followed the principles of Ethical Business Practice and Regulation (EBP&R), which requires openness and candour in engagement between company and regulator. In general, WICS considers Scottish Water to be proactive in sharing information as it has developed its draft business plan. For example, we welcomed the engagement with Scottish Water on the operating expenditure efficiency models and in developing the joint WICS/Scottish Water financial model. While this is the case in general, there are areas that Scottish Water could have sought earlier engagement with stakeholders, including on the outcome measures and the proposal for West Central Bioresources, as covered in section 4.

## 3.3. Business plan data tables

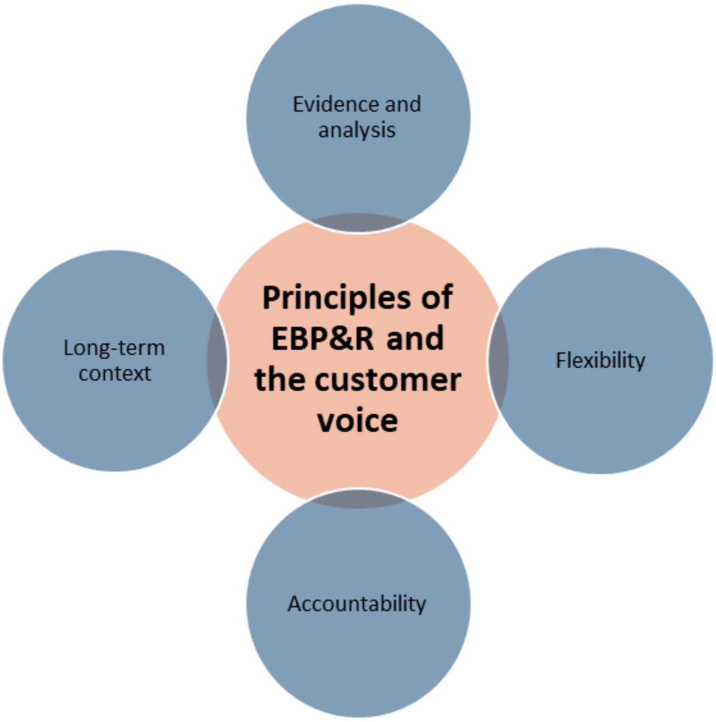
3.3.1. As set out in the final methodology, the purpose of the business plan data tables is to provide WICS with the information it requires to set a baseline covering the financial, investment, and service forecasts over a regulatory period as part of its final determination.[25] The information from the business plan tables provides a strong foundation for what will eventually become Scottish Water's delivery plan for 2027-33, which provides further detail

[24] Scottish Government (2021), 'A National Mission with Local Impact: Infrastructure Investment Plan for Scotland 2021-22 to 2025-26', 4 February 2025, p.25. Available at: https://www.gov.scot/publications/national-mission-local-impact-infrastructure-investment-plan-scotland-2021-22-2025-26/documents/.

[25] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, pp.51-52.

on how Scottish Water will meet the requirements from the final determination and is updated annually to reflect new information during the regulatory period.[26] During the period, WICS will compare Scottish Water's reported performance against the forecast values and commitments from the baseline and seek to understand any differences. This allows us to hold Scottish Water to account for delivery on behalf of customers. The ability to hold Scottish Water to account for delivery during the regulatory period through establishing a clear baseline is one of the five key principles underpinning the approach to SRC27, as summarised in Figure 3.[27]

*Figure 3: Principles of SRC27*




3.3.2. Scottish Water has completed the tables to a good standard, except for the remaining gaps in information on asset health and the enhancement benchmarking data (see section 4). WICS welcomes the additional information Scottish Water provides in the accompanying table commentaries. Overall, the detail Scottish Water provides on outputs and outcomes in the business plan data tables will enable WICS to set a baseline for the 2027-33 regulatory period and ensure that regulators can hold Scottish Water to account for delivery during the 2027-33 regulatory period.

[26] For a further explanation of the delivery plan, see page 31 of the WICS final methodology. WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.31 and pp.126-127.
[27] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.10.

# 4. Areas requiring further evidence

## 4.1. Overview of the chapter

4.1.1. This chapter covers areas which WICS consider requires further evidence, including:

- the needs case for Scottish Water's proposals for SRC27;
- customer engagement and research;
- outcome measures;
- investment;
- operating and PFI expenditure; and
- adjustments following the final determination.

## 4.2. Needs case for Scottish Water's proposals for SRC27

### NEEDS CASE IN THE CONTEXT OF THE LONG-TERM PRICE PATH FROM SRC21

4.2.1. As set out in paragraph 2.2.1, in SRC21, WICS set out a long-term price path of CPI + 1.5% to 2% to enable Scottish Water to make appropriate progress towards maintaining service and achieving net zero emissions by 2040. The final determination set charge caps of CPI + 2% for the 2021-27 regulatory period and explained that to continue the transition towards addressing the challenges of the sector, charges will need to increase by a similar amount in real terms of CPI + 1.5% to 2% per annum (equivalent to 9-13% in total over 2027-33) over the 2027-33 regulatory period.

4.2.2. In the draft business plan, Scottish Water has not explained what has changed since SRC21 to justify deviating from the long-term price path of CPI + 1.5% to 2%. Scottish Water must ensure that its final business plan provides this linkage back to the SRC21 final determination and clearly explains the factors it considers justify a deviation from the price profile of CPI + 1.5% to 2% per annum.

4.2.3. Scottish Water has not yet demonstrated that it is unable to deliver the desired outcomes set out in the Ministerial Objectives with CPI + 1.5% to 2% per annum over the 2027-33 regulatory period. WICS considers the assumptions from the SRC21 period are a reference point for the 2027-33 period, and that it is for Scottish Water to demonstrate where changes to these assumptions are appropriate.

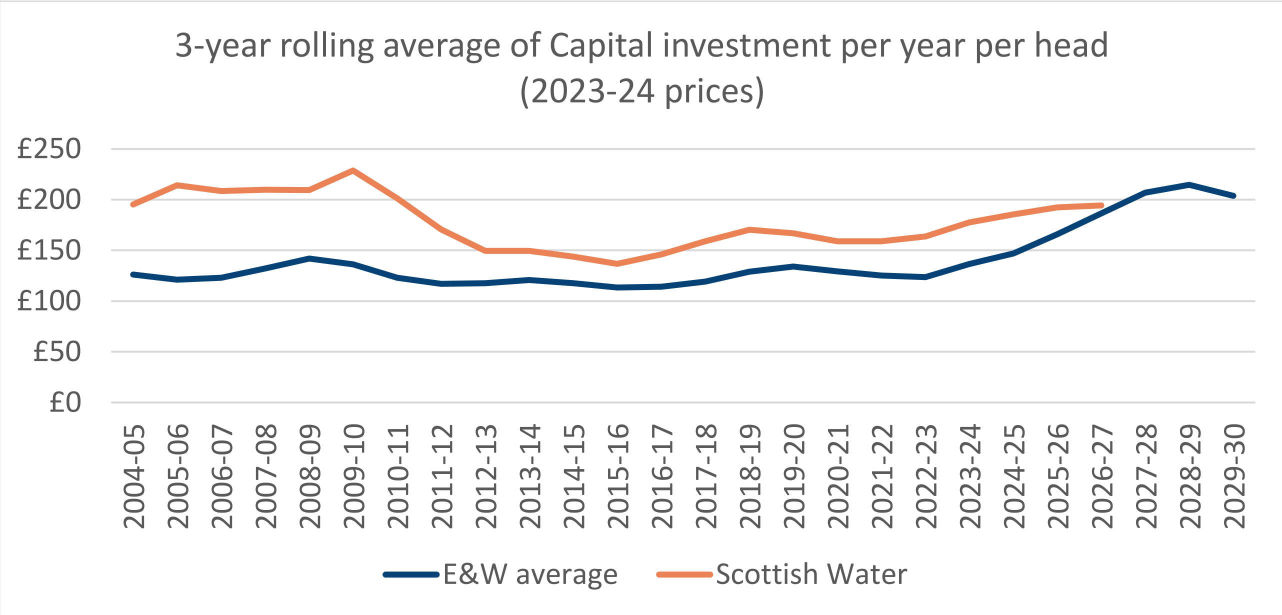
4.2.4. As a further point, WICS notes that Scottish Water compares the change in annual charges proposed in the draft business plan to that in England and Wales over 2025-30. Page 64 of the draft business plan explains:

*"To deliver the investment needed, this will mean bills would rise by CPI +4% each year. By the end of this period, the average customer bill for water and wastewater services will increase 26.5% in real terms over the 6 year period. In comparison, average bills in England*

*and Wales will rise by CPI +19.5% in the first year of PR24, followed by annual increases of CPI +3.2%, a real increase of 36% over their 5-year period."*

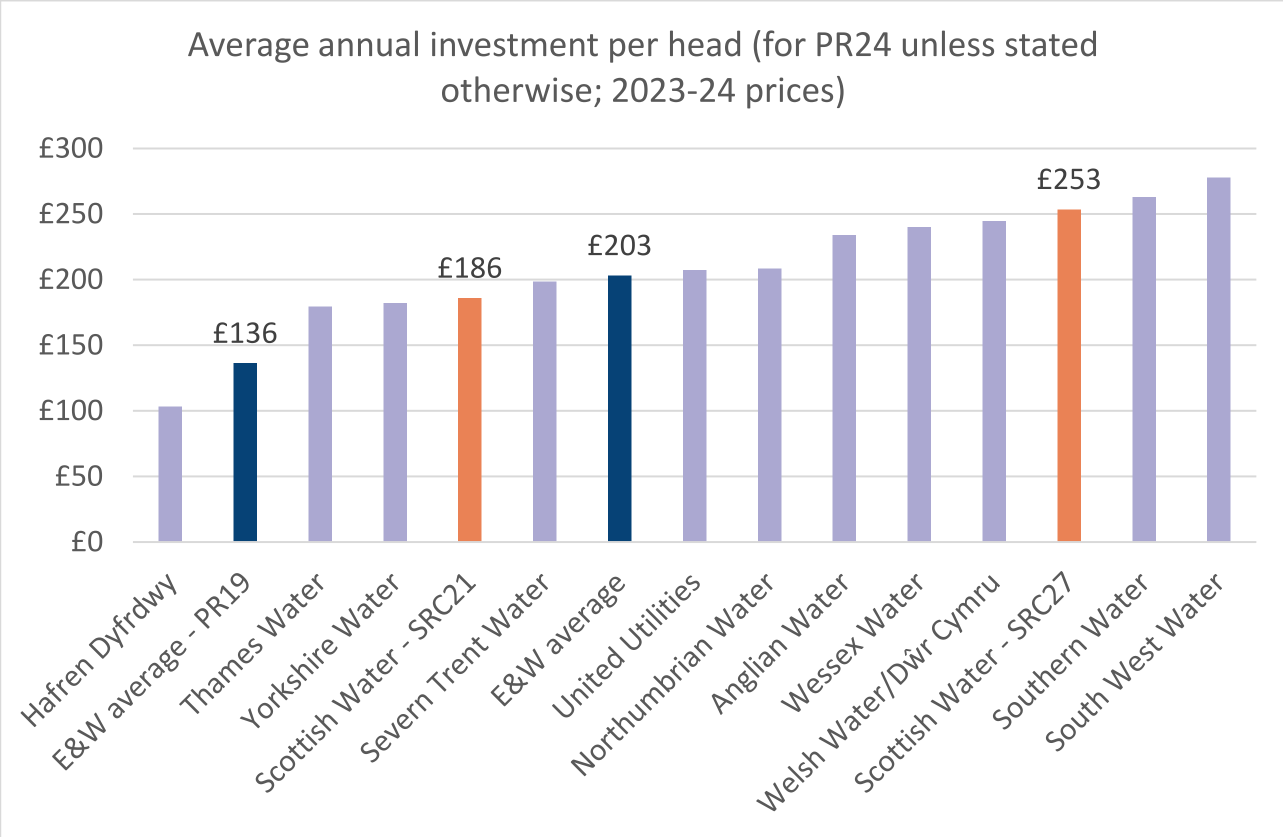
4.2.5. Such comparisons need to be placed in their appropriate context, recognising that Scottish Water began the transition in charges to increased levels of investment earlier than the companies in England and Wales. The figure below shows investment per head of population from 2004-05, including the forecast for Scottish Water to 2026-27 and the forecast in England and Wales from 2024-30. As shown in figure 4, Scottish Water has consistently invested more per head of population than in England and Wales.

*Figure 4: Rolling average of capital investment per head*




4.2.6. Figure 5 shows that the increase in charges in England and Wales has enabled the companies to increase investment from around £140 per head per year (2023-24 prices) on average in PR19 to around £200 over the 2025-30 period (based on Ofwat's allowances in its price review 2024 (PR24)), which is around the level of Scottish Water over the 2021-27 regulatory period (£190 per head per year).

*Figure 5: Average annual investment per head for PR24*




4.2.7. Given these points, Scottish Water should examine whether it is feasible to deliver the Ministerial Objectives with a charge path of CPI + 2% and, if so, include it as one of the charge path scenarios (either replacing one of or in addition to the three charge paths in the draft business plan).

## NEEDS CASE IN THE CONTEXT OF SCOTTISH WATER'S LONG-TERM STRATEGY

4.2.8. Scottish Water's long-term strategy includes a directional estimate of around £50 billion in investment in water and wastewater services over the next 25 years, of which half relates to investment in maintaining the existing asset base. While WICS recognised the "directional" nature of these long-term cost estimates, stakeholders will require confidence in the assumptions underpinning these forecasts.[28]

4.2.9. WICS notes that Scottish Water appears to be using the £50 billion as a reference point for justifying investment over 2027-33.

4.2.10. For example, page 71 of the draft business plan explains:

[28] WICS (2025), 'Response to Scottish Water's draft long-term strategy', 21 March 2025.

*"In SR27, we plan to invest £8.3 billion, which will contribute 16% of the £50 billion required to achieve our Long-Term Strategy over the next four regulatory periods"*[29]

4.2.11. A further example is provided on pages 37 to 38 of Technical Appendix 1 (TA001), which explains:

*"For Water Quality, the projection will see a near doubling in expenditure from SR27 to SR45 from ~£1,581m to ~£2,806m…the above [figures comparing water quality investment by regulatory period] demonstrates that our SR27 plans is a proportionate and incremental step to achieving the ambitions of our Long-Term Strategy."*[30]

4.2.12. On 7th August 2025, Scottish Water began sharing more detailed information in the form of an investment strategy and sub-outcome summary reports.[31] Scottish Water explains that these documents provide the evidence base and outline the process followed in determining how it proposes to deliver the outcomes of its long-term strategy. WICS continues to review these documents. However, at this stage, we consider that there remain gaps in information on the assumptions underpinning the £50 billion estimate of required investment. This represents a gap in the needs case for investment over the 2027-33 regulatory period given that SRC27 is the next step towards achieving Scottish Water's long-term ambitions.

## NEEDS CASE FOR INVESTMENT IN THE CONTEXT OF THE MINISTERIAL OBJECTIVES

4.2.13. WICS sets charge caps based on our assessment of the lowest reasonable overall cost incurred by Scottish Water in delivering the Ministerial Objectives, consistent with the Principles of Charging for the industry. To fulfil our role in setting charge caps, we require clear evidence of how the Ministerial Objectives are translated into the proposed investment programme. This ensures that charge caps fund only the investment necessary for Scottish Water to meet the Ministerial Objectives. There must also be a shared view among key stakeholders that delivery of that investment programme will be consistent with Scottish Water meeting the Ministerial Objectives during the regulatory period.

4.2.14. In the Commissioning letter that the Scottish Ministers issued to WICS in March 2024, Ministers explained that the draft Ministerial Objectives and Principles of Charging will be an evolution of those that currently apply during the 2021-27 regulatory period and that WICS and Scottish Water should take these as a starting point in undertaking SRC27.[32] To recognise this, the Commissioning letter included the current Ministerial Objectives and

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[29] Scottish Water (2025), 'SR27 draft business plan – investing in Scotland's future', 12 June 2025, p.71.

[30] Scottish Water (2025), 'SR27 Draft Business Plan: Water Quality Technical Appendix', 12 June 2025, pp. 38-37.

[31] Scottish Water (2025), 'Investment Strategy', August. This document is supported by 21 sub-outcome reports covering areas such as water growth, water pressure and network discharges.

[32] The Commissioning letter launches the Strategic Review of Charges (SRC) process and also sets the duration of the regulatory period, the preferred approach and a high-level timeline for the SRC. The Commissioning letter for SRC27 is included as appendix 3 in the WICS final methodology. WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024.

Principles of Charging with minor amendments as annexes. We refer to these Ministerial Objectives as the pre-draft Ministerial Objectives and Principles of Charging throughout this document.

4.2.15. The draft business plan could explain more clearly how Scottish Water has interpreted the requirements of the pre-draft Ministerial Objectives and explain how the reference scenario of CPI + 4% in the draft business plan meets the pre-draft Ministerial Objectives. These points also apply to the two alternative charge paths of CPI + 3% and CPI + 5% per annum. At this stage, it is unclear how much more or less progress each of the alternative charge paths makes towards achieving the Ministerial Objectives.

4.2.16. For example, the draft business plan provides a summary table of Scottish Water's assessment of investment plans against these pre-draft Ministerial Objectives.[33] However, this assessment could be enhanced to include a version of the analysis of the February 2025 scenarios against the draft Ministerial Objectives in Technical Appendix 8, Annex F, updated for the three scenarios proposed in the draft business plan.

4.2.17. WICS recognises that by the time Scottish Water finalises its final business plan for publication in February, it will have visibility of the draft Ministerial Objectives and Principles of Charging. As such, Scottish Water must demonstrate the linkage between the draft Ministerial Objectives and the proposed projects and programmes that comprise the proposed investment programme. We expect this to feature prominently in the business plan submission.

4.2.18. It is essential for Scottish Water to ensure there is a shared view among stakeholders that the investment plan will meet the Ministerial Objectives.[34] From WICS' perspective, this includes explaining whether the proposed investment aligns with the expectations of both DWQR and SEPA in relation to the Ministerial Objectives that apply to them. We expect the final business plan to clearly set out how this alignment has been tested, and how Scottish Water has ensured that the plan has the support of customers and its regulators. If there are areas of misalignment, we expect Scottish Water to provide further information on these areas to enable WICS to issue a determination, e.g. the standard information required on the investment programme if related to investment.

4.2.19. WICS will update the template for data Table 5 for Scottish Water to indicate which is the primary Ministerial Objective that the investment line is contributing to, as described in paragraph 6.11.9.

4.2.20. Ahead of the draft determination, WICS will also seek feedback from SEPA and DWQR on whether they agree that the proposed investment programme is consistent with the

[33] Scottish Water (2025), 'SR27 draft business plan – investing in Scotland's future', 12 June 2025, pp. 62-63.
[34] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.18.

elements of the MOs that apply to them. We are exploring the timing of when SEPA and DWQR could provide such feedback.

4.2.21. Besides the requirement to meet the Ministerial Objectives, Scottish Water has other obligations it must fulfil. One set of those obligations is to comply with its duties as a designated public body/authority. Such duties include complying with the Consumer Scotland Act 2020 which places a statutory duty on specified public authorities[35] to have regard to consumer interests when making decisions of a strategic nature about how to exercise their functions.

4.2.22. WICS requires Scottish Water to provide alongside the final business plan submission any impact assessments or other relevant publications on how it is performing its statutory duties as a designated public body.

### OVERALL ASSESSMENT ON THE NEEDS CASE

4.2.23. The draft business plan is Scottish Water's proposal for what will ultimately become the regulatory contract between Scottish Water and the people of Scotland. It sets out Scottish Water's proposals for charges and what benefits customers, society and the wider environment can expect to receive in return for these charges over the 2027-33 regulatory period.

4.2.24. Recognising the proposals summarised in paragraph 2.5.3, WICS considers that Scottish Water should seek to improve the benefits and the explanation of the consequences of not delivering or delaying investment. For example, as explained in section 4.4 on outcomes below, Scottish Water could demonstrate more ambition in its performance measures and forecasts based on comparisons to current performance and the performance improvements set for the other water and wastewater companies in Great Britain.

4.2.25. These points are also apparent when reviewing Scottish Water's proposed charge paths (4% as the reference scenario, with 3% and 5% as variations) and the proposed outcomes and forecast performance that Scottish Water proposes to deliver for each charge path. There is limited variation in either the levels of service or the explanation of the level of risk associated with each outcome.[36] This raises a question of whether the benefits of the reference scenario of CPI + 4% per annum relative to the charge path of CPI + 3% scenario are worth the additional costs and a further 1% on charges in each year of the 2027-33 regulatory period.

## 4.3. Customer engagement and research

[35] Scottish Water is specified as a relevant public authority in The Consumer Scotland Act 2020 (Relevant Public Authorities) Regulations 2024.

[36] In the reference scenario of CPI + 4%, Scottish Water forecasts improved performance for five outcomes, which increases to six outcomes in the CPI + 5% scenario.

4.3.1. The final methodology builds on the approach to customer involvement in SRC21 by establishing a Memorandum of Understanding (MoU) among WICS, Scottish Water and Consumer Scotland.[37] Under the MoU, Scottish Water has established a Customer Challenge Group, known as the Independent Customer Group, to help ensure its business plan reflects customers' views. This is central to WICS reaching a final determination of charges that commands customer support.

4.3.2. The MoU involves three pillars of work: evidence, challenge, and confirmation. Consumer research will provide evidence for the Independent Customer Group to challenge Scottish Water's decision-making as it develops its business plan. Consumer Scotland will undertake the final confirmation stage, which will involve asking consumers whether Scottish Water's final business plan commands their support.

4.3.3. The final methodology also requires Scottish Water to work openly and collaboratively with both Consumer Scotland and WICS on the design and development of customer research through a multi-stakeholder coordination group. This will include undertaking a deliberative research programme to understand strategic prioritisation and customers' acceptability of the business plan.

4.3.4. As set out in the draft business plan and Technical Appendix 9 (TA009), WICS notes that the collaborative SR27 customer research involves 5 activities, the first 3 of which have been completed so far:

- Activity 1: Establishing customer expectations, and understanding their views around SRC27 charging and investment scenarios
- Activity 2: Understanding expectations from Licensed Providers
- Activity 3: Gathering customer feedback on updated investment scenarios and charging trajectories
- Activity 4: Further research on a more final version of investment scenarios using a nationally representative sample of customers
- Activity 5: Consumer Scotland's Longitudinal Deliberative Research

4.3.5. During activity 1, customers were presented with three different scenarios for the levels of charging (CPI + 2%, CPI + 4% and CPI + 6.5%) and resulting investment at a high level. It was recognised in appendix 9 that none of the scenarios *"offered enough value for wholehearted endorsement from customers."*[38]

4.3.6. This response led Scottish Water to further develop the CPI + 4% investment scenario, with the intention of rebalancing investments to enable improvements to outcomes. Activity 3 involved reconvening customers to discuss this plan alongside a discussion on charging

[37] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, pp.17-18.
[38] Scottish Water (2025), 'SR27 draft business plan: Technical Appendix 9 – Customer Research', p. 21.

trajectories. Scottish Water has explained that an improved CPI + 2% scenario was not retested with customers since, in Scottish Water's view, they had clearly rejected this scenario in activity 1. However, as none of the scenarios were endorsed in activity 1, WICS considers that Scottish Water could have retested the three scenarios with customers.

4.3.7. Based on WICS' review of the research to date, Scottish Water should provide further evidence for why only the CPI + 4% scenario with improved outcomes was retested with customers in Activity 3, given that the initial feedback from research activity 1 was inconclusive. WICS considers that customers could have expressed a preference for CPI + 2% with improved outcomes; however, they do not appear to have received that choice.

4.3.8. Scottish Water should also examine whether it is feasible to deliver the Ministerial Objectives and improved outcomes with a rebalanced CPI + 2% scenario. If it is feasible, Scottish Water should include CPI + 2% as a charge path (either replacing one of or in addition to the three charge paths in the draft business plan) and seek to test this with customers. This recognises that CPI + 2% was consistent with the long-term price path set out in SRC21. WICS reserves the right to conduct its own research if it considers that the different scenarios for price and service outcomes have not been adequately tested.

4.3.9. WICS notes Scottish Water's statement that "*our plan is affordable*".[39] While we recognise that the draft business plan represents a point in time and that further research and analysis are underway, we consider that additional evidence is required to substantiate this statement.

## 4.4. Outcome measures

### OVERVIEW OF SUB-SECTION

4.4.1. WICS considers that Scottish Water should strengthen the evidence in the following areas:

- ensuring alignment with the principles from the final methodology;
- choice of outcome measures; and
- level of ambition in outcome measures.

### ALIGNMENT WITH THE PRINCIPLES FROM THE METHODOLOGY

4.4.2. WICS' final methodology required Scottish Water to commit to the following principles in developing the outcome measures for the draft business plan.[40]

- The measures should align with both the outcomes outlined in the Scottish Ministers' Objectives and the outcomes Scottish Water is expected to deliver as part of the water sector vision to help track progress towards achieving the water sector vision.

[39] Scottish Water (2025), 'SR27 draft business plan – investing in Scotland's future', 12 June 2025, pp.63-64
[40] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.133.

- The annual targets should be stretching while maintaining the incentive for outperformance.
- Scottish Water should engage with stakeholders to ensure that they have confidence in the measures and targets.
- The measures should allow Scottish Water to demonstrate its progress against its current commitments (e.g. Scottish Water's target to reduce operational emissions by at least 75% by 2030).
- Scottish Water has a measure (or measures) covering asset condition, to allow stakeholders to understand the impact of maintenance activities on the asset base.
- Comparisons with performance over time should be retained, where appropriate (e.g. in relation to drinking water quality measures).
- Scottish Water should propose annual targets or commitments on the performance measures in its business plan, taking account of the investment programme proposed in the plan (recognising that this may change) and historic performance.
- WICS and Scottish Water should assess performance against the measures set out in the final determination with any management or employee incentives aligning with these measures, notwithstanding that Scottish Water may track other measures (e.g. health and safety).
- Outcome measures should cover all benefits that customers receive, and these measures should be mapped to the Scottish Government's National Performance Framework (NPF). We consider that Scottish Water should identify whether there are gaps between outcome measures and the NPF and seek to fill these gaps.

4.4.3. WICS considers that Scottish Water is yet to demonstrate that it has met several of the principles including:

- that the forecasts are stretching;
- engaging with stakeholders to ensure that they have confidence in the measures and targets; and
- confirming that the management or employee incentives will align with the outcome measures and targets.

4.4.4. Indeed, WICS notes that the draft business plan proposes developing a weighted basket of outcome measures for the 2027-33 regulatory period, similar to the outcome performance assessment (OPA) measure currently in place in the 2021-27 regulatory period. Scottish Water proposes to use this measure for reporting and incentivising Scottish Water employees and notes that other outcome measures "on the WICS list and LTS will be reported separately and not enter the main framework for SW Incentives Scheme."[41] We request clarification on whether this approach aligns with the final methodology, which

[41] Scottish Water (2025), 'SR27 draft business plan: Technical Appendix 14 - Performance Monitoring', p.39

requires that any management or employee incentives are based on the outcome measures set out in the final methodology and that will underpin the final determination. For the avoidance of doubt, WICS is not expecting a new OPA-type higher-level measure that does not align with the outcome measures in the business plan. Having two sets of measures (one set from the business plan and a separate OPA-type higher-level measure that does not align with the outcomes from the business plan) could undermine the legitimacy of the performance framework and would not be in the customers' interests.

## CHOICE OF OUTCOME MEASURES

4.4.5. In developing its final methodology and business plan guidance and data tables, WICS developed a list of candidate outcome measures drawing on:

- existing outcome measures;
- standard industry measures in place in other jurisdictions, where benchmarking could be appropriate; and
- best practice in asset management.

4.4.6. The outcome measures and forecasts should capture the benefits to customers of the investment programme and reflect the priorities of customers as identified through research.[42]

4.4.7. As such, the final methodology explained that Scottish Water may decide to propose alternative outcome measures based on the composition of the investment programme or the findings from its extensive customer research programme.

4.4.8. WICS is pleased that Scottish Water's draft business plan includes 39 of the 44 outcomes set out in WICS business plan table guidance.

4.4.9. We welcome that the draft business plan included proposals for two additional measures, recognising that they remain at an early stage of development and do not include any forecasts.

4.4.10. We also identified outcomes requiring further development, explaining that "these are set out as placeholders in the table below for Scottish Water to propose in its business plan submission".[43] These placeholders covered the following areas:

- sewerage infrastructure discharges;
- environmental performance; and
- a communities experience measure.

[42] WICS (2024), 'Strategic Review of Charges 2027-33: Final Methodology, December, p.131.
[43] WICS (2024), 'Final Business Plan Guidance and Definitions', 12 December 2024, pp. 11-12. Available at [Final Business Plan Guidance and Definitions | WICS]

4.4.11. WICS set an expectation that these outcomes should be developed through engagement between Scottish Water and other stakeholders. We are unaware of engagement taking place with Scottish Water and other stakeholders on the outcome measures and forecasts. As such, Scottish Water should engage with the relevant stakeholders on these measures and forecasts in preparing the final business plan.

4.4.12. If Scottish Water is unable to develop appropriate measures and forecasts in these areas (e.g. sewerage infrastructure discharges), WICS may decide to add its own measures as part of the draft and final determination to protect the interests of customers and the environment.

4.4.13. The remainder of this sub-section covers each of the three areas above.

### Sewerage infrastructure discharges

4.4.14. In the business plan tables, guidance and definitions,[44] WICS identified sewerage infrastructure discharges as one of the outcomes requiring further development. The draft business plan Technical Appendix 14 (TA014) explains:

*"Unsatisfactory Intermittent Discharge (UID) (Table 1 line 32): A UID is a Combined Sewer Overflow (CSO) that is not operating as expected. UIDs are a subset of CSOs that are prioritised by SEPA for intervention by Scottish Water because of their environmental impact. While there is an interest in All Combined Sewer Discharges in the regulatory framework in E&W, Scotland has adopted an approach which focusses on those that cause the most material environmental impact. We consider improvement in UIDs to be the most appropriate performance measure of 'sewerage network environmental impact. this puts environmental risk / harm as the focus."*[45]

4.4.15. Recognising the public interest in this area, Scottish Water should provide further evidence that it has examined alternative measures or engaged with stakeholders on the appropriate measure(s) covering performance in this area.[46] There are a range of possible measures that could be considered in this area, including:

- Overflow events from sewerage infrastructure overflows (number of events and/or duration)
- Overflow events from a subset of overflows such as:
    - those that Scottish Water is required to report to SEPA as part of its consent;

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[44] WICS (2024), 'Final Business Plan Guidance and Definitions', 12 December 2024, pp. 11-12. Available at Final Business Plan Guidance and Definitions | WICS

[45] Scottish Water (2025), 'SR27 draft business plan: Technical Appendix 14 - Performance Monitoring', p.38

[46] WICS recognises that Scottish Water has provided further information in the query 13 response on 23 July 2025 but the engagement it cites pre-dates final methodology expectations on further engagement. WICS also questions whether there was full consideration of options for measures in this area and engagement with stakeholders on them.

- those that have licence requirement for monitoring or are monitored but do not require reporting to SEPA;
- overflow events from UID that were identified by SEPA as high and medium priority, given that these are the focus for investment in the 2021-27 and 2027-33 regulatory periods.

4.4.16. Scottish Water should address this area when preparing the final business plan.

## Environmental performance

4.4.17. One of the three long-term outcomes set out in Scottish Water's long-term strategy is "The quality of our rivers and seas has improved, and our communities are protected from sewer flooding, through collaboration with others."

4.4.18. WICS included a placeholder for a river water quality measure (1.33) in the business plan guidance with expectation that "Measure(s) to be developed through engagement with Scottish Water and other stakeholders".[47]

4.4.19. Scottish Water has not proposed an outcome measure covering its impact on the bathing waters or river water quality explaining that it is not "appropriate to forecast or set outcomes for river water quality as this issue sits within the remit of SEPA."[48] Scottish Water also indicates that "Overall, river water quality is measured by SEPA. A metric will be considered, with SEPA, alongside the forthcoming River Basin Management Programme (RBMP4) to find a suitable measure for River Water Quality specific to Scottish Water."[49]

4.4.20. Scottish Water should provide further clarity on the options for such a measure. If such a measure will not be developed for the final business plan, then Scottish Water should provide detailed milestones and timescales for developing one. WICS considers that it is critical for Scottish Water to demonstrate the impact that it has on the natural water environment.

## Communities experience measure

4.4.21. Based on feedback from stakeholders, the final methodology highlighted the need for Scottish Water to cover the benefits to customers and communities, as a refinement or complement to the customer experience measures, and the impact of Scottish Water's partnerships with customers, communities and other stakeholders (e.g. demand side initiatives such as information campaigns). As such, WICS identified this as an outcome requiring further development (see paragraph 4.4.10).

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[47] WICS (2024), 'Final Business Plan Guidance and Definitions', 12 December 2024, p. 23. Available at [Final Business Plan Guidance and Definitions | WICS]
[48] Scottish Water (2025), 'SR27 draft business plan: Table 1: Performance Commentary', p. 5.
[49] Scottish Water (2025), 'SR27 draft business plan: Technical Appendix 14 - Performance Monitoring', p. 10.

4.4.22. WICS notes that the draft business plan does propose a measure in this area and explains:

> *"While we continue to monitor information across our communities we do not have an additional measure as yet. Scottish Water considers this measure to be repetitive of data already collected through the currently reported CEMs and through the inclusion of the UKCSI measure. Further benefit may come from the development of a new 'Awareness' measure that would measure progress aligned to our Long-Term Strategy."*[50]

4.4.23. Based on the draft business plan, it is unclear whether the CEMs, UKCSI and the awareness measure[51] addresses the need highlighted in the final methodology. In developing the final business plan, Scottish Water should engage with stakeholders to obtain wider views on whether the awareness measure, in particular, will capture the impact of Scottish Water's engagement with communities.

## LEVEL OF AMBITION IN THE FORECASTS

4.4.24. In keeping with the principle from the SRC27 final methodology (see paragraph 4.4.2), WICS expects Scottish Water to demonstrate that its forecasts are stretching while maintaining the incentive for outperformance.

4.4.25. WICS' final methodology explains that customer research should underpin Scottish Water's proposals for outcome measures and targets in its business plan submission. Scottish Water's forecasts significant improvements in the following measures:

- water supply interruptions (outcome 1.14);
- meeting peak demand and demand during a worst historic drought (outcomes 1.15 and 1.16); and
- lead pipe removal in public network (outcome 1.19); and
- drinking water quality risks (outcome 1.22).

4.4.26. However, we note that for the other outcome measures, Scottish Water forecasts that performance will remain broadly stable, exhibiting only marginal improvements or deterioration during the regulatory period (see Table 2 below).

[50] Scottish Water (2025), 'SR27 draft business plan: Table 1: Performance Commentary', p. 4.

[51] For example, Scottish Water explains that the awareness measure *"would combine qualitative survey on trust and awareness with quantitative assessments of outputs like proactive communications and outcomes like PCC and blockages"*. See Scottish Water (2025), 'SR27 draft business plan: Technical Appendix 014 - Performance Monitoring', pp. 32-33.

*Table 2: Outcomes with stable or small changes in performance*

| Line reference | Level of Service | Base year | Base value | Year 6 2032-33 | Change |
|---|---|---|---|---|---|
| 1.05 | UKCSI UK customer Satisfaction Index | 2026/27 | 77.9 | 77.9 | No change |
| 1.10 | Three-year average per capita consumption* | 2026/27 | 177 | 174 | 1.7% reduction |
| 1.12 | Unplanned interruptions greater than 6 hours, excluding 3rd party | 2026/27 | 6750 | 6750 | No change |
| 1.13 | Average minutes lost due to water supply interruptions (over 3 hours)* | 2026/27 | 15.00 | 15.00 | No change |
| 1.24 | Number of internal sewer flooding incidents* | 2026/27 | 1.57 | 1.48 | 6% decrease |
| 1.25 | Number of properties at risk of internal flooding | 2026/27 | 1.51 | 1.51 | No change |
| 1.26 | Number of external sewer flooding | 2026/27 | 10.50 | 11.24 | 7% increase |
| 1.27 | Number of properties at risk of external flooding | 2026/27 | 11.35 | 11.881 | 5% increase |
| 1.28 | Percentage compliance with SEPA discharge permits | 2026/27 | 96.37% | 96.37% | No change |
| 1.30 | The total number of pollution incidents from a sewerage asset affecting the water environment* | 2026/27 | 34.8 | 34.8 | No change |

4.4.27. WICS seeks clarity on how Scottish Water has taken into account the customer research in identifying the priority outcome measures for improvements. For example, it would be useful to understand whether the five outcomes listed in paragraph 4.4.25 are consistent with the outcomes that customers value most highly.

4.4.28. WICS has also benchmarked Scottish Water's forecast performance against both Scottish Water's current performance and the performance of the water and wastewater companies in England and Wales, where there are comparable measures.

4.4.29. Based on this review, while recognising the forecasts should reflect the priorities of customers, WICS questions whether Scottish Water is providing sufficiently stretching forecasts (in line with the principles set out in our methodology) for performance on the outcome measures. If Scottish Water considers that the forecasts are stretching given the external challenges that it faces, then it should provide further explanation of these external challenges. Initial feedback from industry stakeholders on Scottish Water's draft business plan suggests that this is a common theme.

## Benchmarking against current performance

4.4.30. Technical Appendix 14 explains that most of the forecasts for the outcome measures in table 2 are based on a forecast level of performance in 2026-27. Based on comparing the forecast level of performance in 2026-27 to current performance, Scottish Water's forecast of performance in 2026-27 is lower than its current performance in 2024-25 for some measures (see Table 3 below). WICS notes that comparing performance over the regulatory period 2027-33 to a lower starting point in 2026-27 risks overstating the improvements Scottish Water is proposing over 2027-33 and the level of ambition in the business plan.

*Table 3: Outcomes with actual performance in 2024-25 better than forecast 2026-27 base*

| Line reference | Level of Service | 2024-25 (actual) | 2026-27 | 2032-33 |
|---|---|---|---|---|
| 1.01 | dCEM Developer Customer Experience Measure | 82.90 | 81.99 | 83.04 |
| 1.02 | nhCEM Non Household Customer Experience Measure | 89.30 | 88.78 | 89.43 |
| 1.11 | Number of properties on the low pressure register | 22 | 30 | 26 |
| 1.12 | Unplanned interruptions greater than 6 hours, excluding 3rd party | 5047 | 6750 | 6750 |
| 1.13 | Average minutes lost due to water supply interruptions (over 3 hours)* | 10.60 | 15.00 | 15.00 |
| 1.17 | Taste and odour contacts* | 0.50 | 0.51 | 0.53 |
| 1.21 | Total drinking water compliance | 99.932% | 99.930% | 99.950% |
| 1.24 | Number of internal sewer flooding incidents* | 1.05 | 1.57 | 1.48 |
| 1.25 | Number of properties at risk of internal flooding | 1.17 | 1.51 | 1.51 |
| 1.26 | Number of external sewer flooding | 6.12 | 10.50 | 11.24 |
| 1.27 | Number of properties at risk of external flooding | 11.48 | 11.35 | 11.88 |
| 1.28 | Percentage compliance with SEPA discharge permits | 97% | 96% | 96% |
| 1.29 | Number of serious pollution incidents* | 4 | 8 | 5 |
| 1.30 | The total number of pollution incidents from a sewerage asset affecting the water environment* | 34.06 | 34.80 | 34.76 |

4.4.31. Scottish Water should set out its current performance on the outcome measures and explain and evidence its forecasts for 2026-27, especially where Scottish Water forecasts a deterioration in performance.

4.4.32. WICS will amend the table 1 template for the final business plan to include new columns for 2024-25 actual values alongside 2025-26 and 2026-27 forecasts.

## Benchmarking against performance in England and Wales

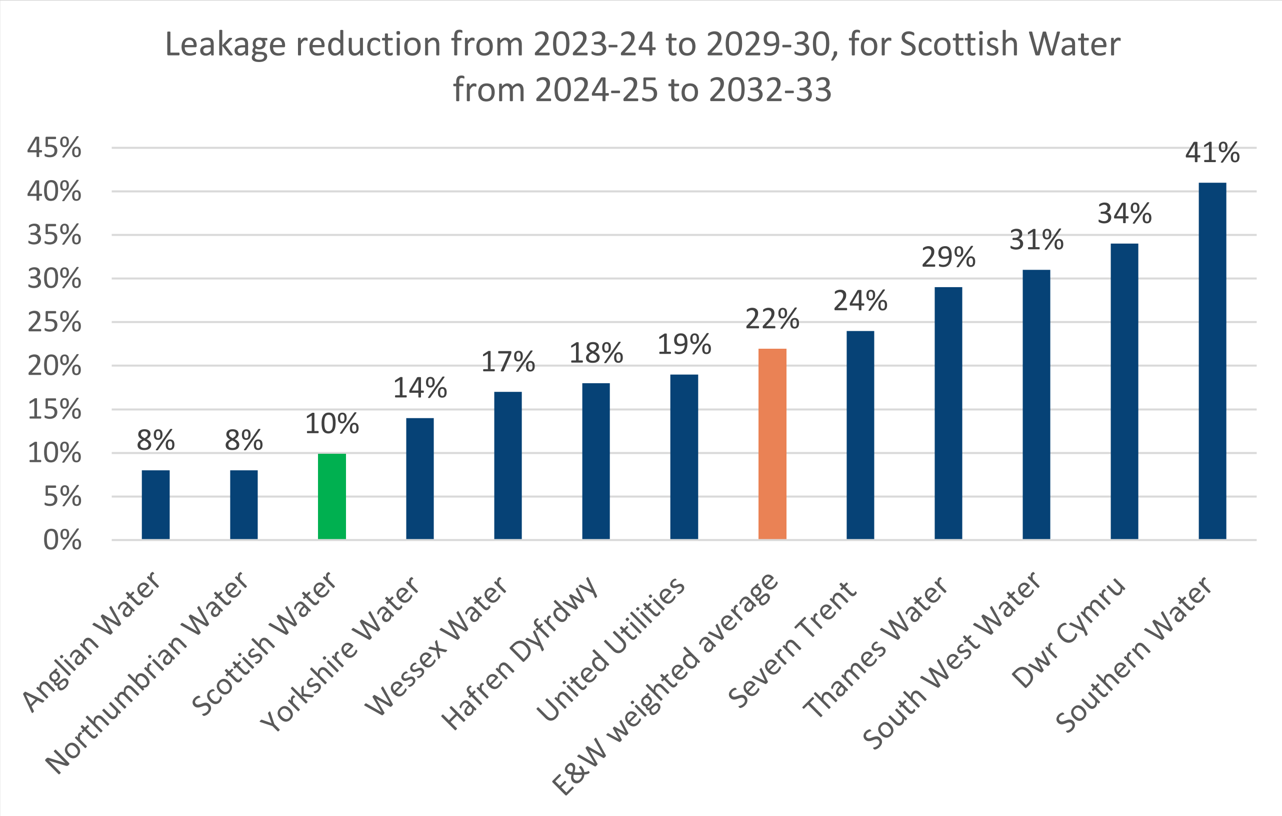
4.4.33. WICS has compared Scottish Water's forecast performance over the 2027-33 regulatory period to the forecast performance of the companies in England and Wales over 2025-30 for the comparable measures.

4.4.34. Based on these comparisons, the proposed level of improvement is lower in leakage reduction, complaints about water quality and the reduction in per capita consumption.

4.4.35. **Leakage:** Scottish Water currently has one of the highest levels of leakage when expressed as a percentage of distribution input at 25% (2023-24), with only two water companies having a higher level of leakage, and most companies having a level below 20%. Scottish

Water forecasts 9.9% reduction in leakage by 2032-33 compared to baseline of 2024-25, i.e. over eight years. In England and Wales, the water and wastewater companies are expected to reduce the level of leakage by 22% from the level in 2023-24, i.e. over six years. Nine of the eleven companies are expected to reduce it by more than 14% as shown in Figure 6.

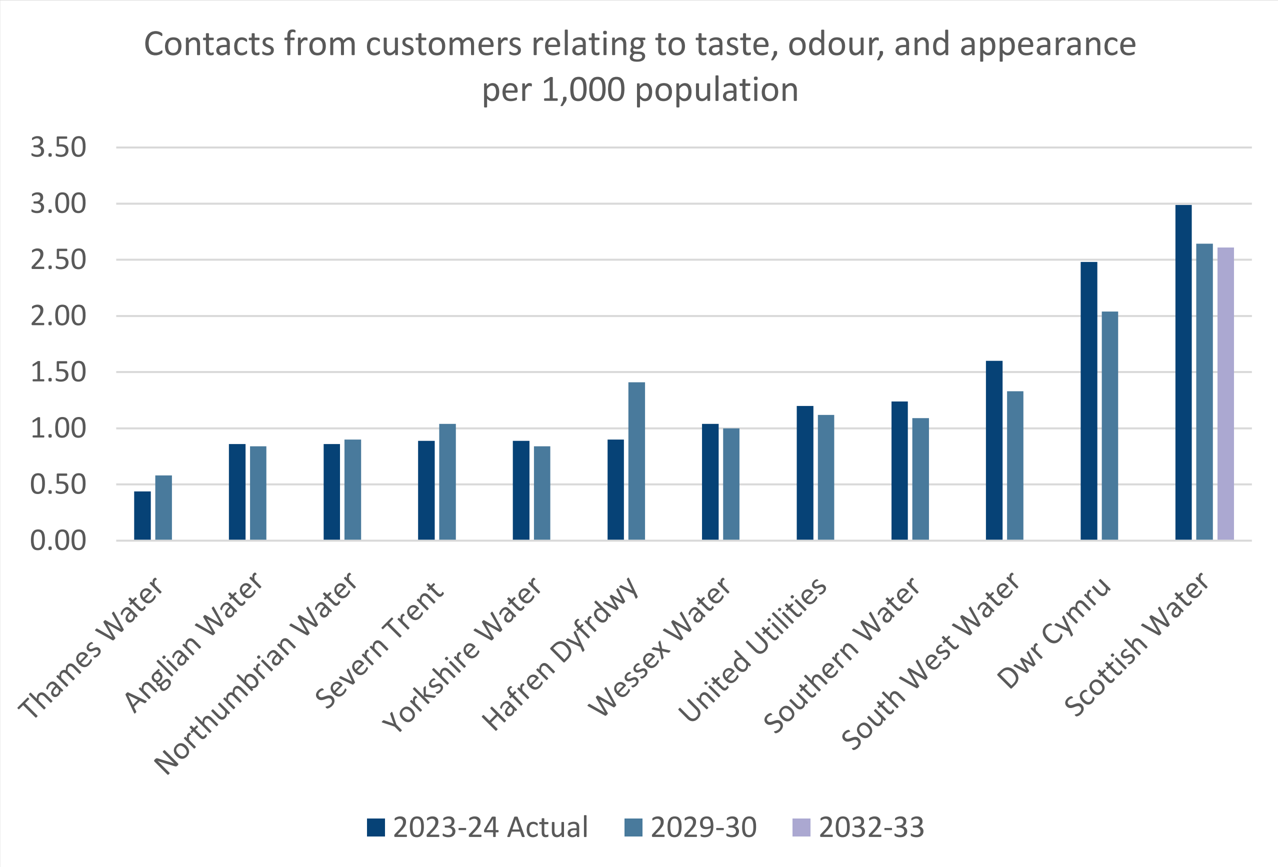
*Figure 6: Leakage reduction comparison*




4.4.36. **Customer contacts about water quality** (appearance, odour and taste):[52] WICS notes that customer contacts in this area are higher than that of any other water company in Great Britain as shown in Figure 7. The draft business plan also proposes that performance remain at that level, with slight deterioration in taste and odour contacts. Scottish Water should explain both its current performance and why it does not forecast improved performance in this area.

[52] As covered in the business plan data table, lines 1.17 and 1.18.

*Figure 7: Contacts from customers relating to taste, odour, and appearance per 1,000 population*




4.4.37. **Per capita consumption (PCC)**: Scottish Water proposes maintaining per capita consumption at 174 litres per person per day (l/p/d), despite PCC in Scotland being the highest in Great Britain (see Figure 8 below). Appendix 14 explains that “There is limited change in per capita consumption, as there is no investment targeted in this area, and we forecast a gradual return to working in offices in Scotland.” While Scottish Water may not have as many mechanisms available as the companies in Great Britain to reduce per capita consumption, WICS notes that:

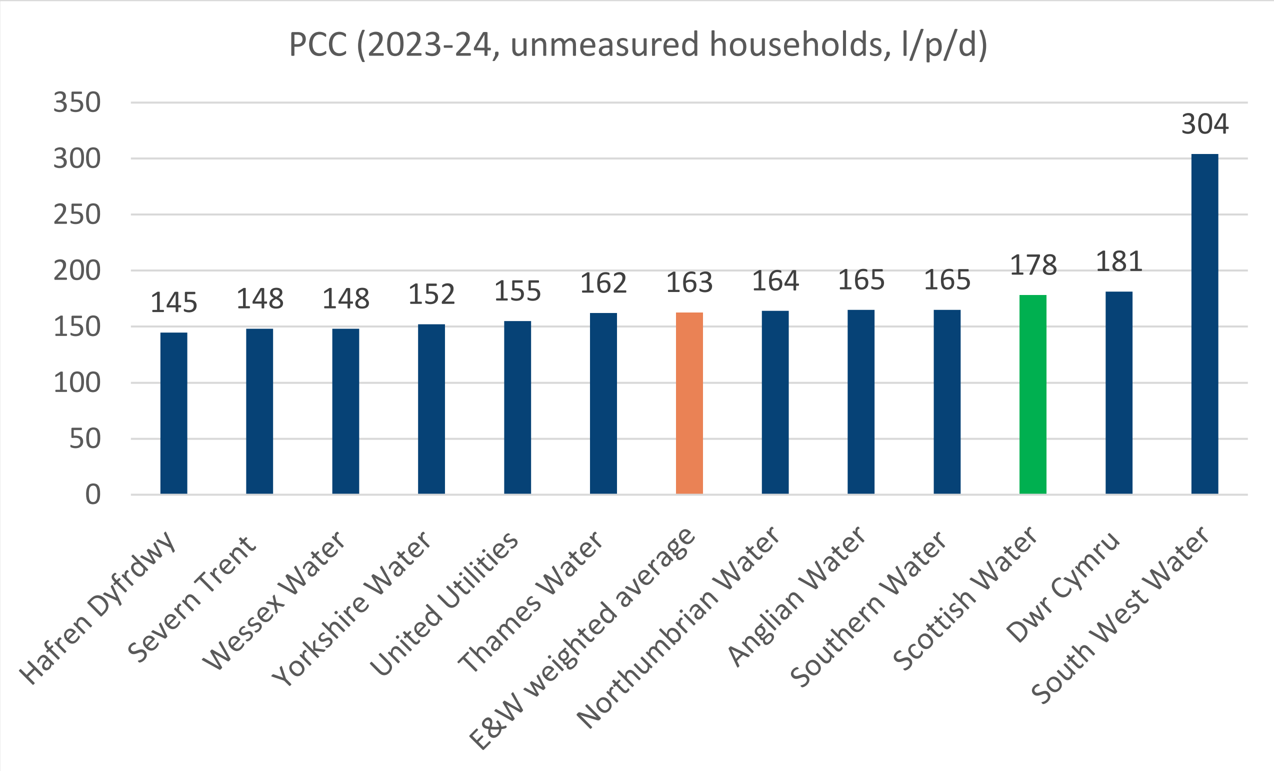
- In 2018-19, the Scottish Water PCC was about 166 l/p/d, and the weighted average PCC in unmeasured household properties in England and Wales was around 158. In 2023-24, these values were 178 and 163 in Scotland and England and Wales, respectively. The per capita consumption in unmeasured household properties has broadly returned to pre-pandemic level in England, but it remains elevated in Scotland.
- The latest data on the subject from ONS shows that in 2022 England had higher proportion of homeworking of 33.1% than 30.6% in Scotland.[53]

[53] ONS, 2022, Homeworking in the UK – regional patterns, available at: [Homeworking in the UK – regional patterns - Office for National Statistics]

- The draft business plan forecasts that PCC will take until 2038-39 to return to 2018-19 levels. [54]

Scottish Water should explain further why it will not be able to reduce per capita consumption back to the pre-pandemic levels and the current level for unmeasured properties in England without significant investment over the SRC27. Scottish Water should also explain the other initiatives that it is pursuing to mitigate the recent increases in per capita consumption.

*Figure 8: Per capita consumption levels in Great Britain 2023-24*




## 4.5. Investment

### OVERVIEW OF SUB-SECTION

4.5.1. WICS considers that Scottish Water should strengthen the evidence in the following areas:

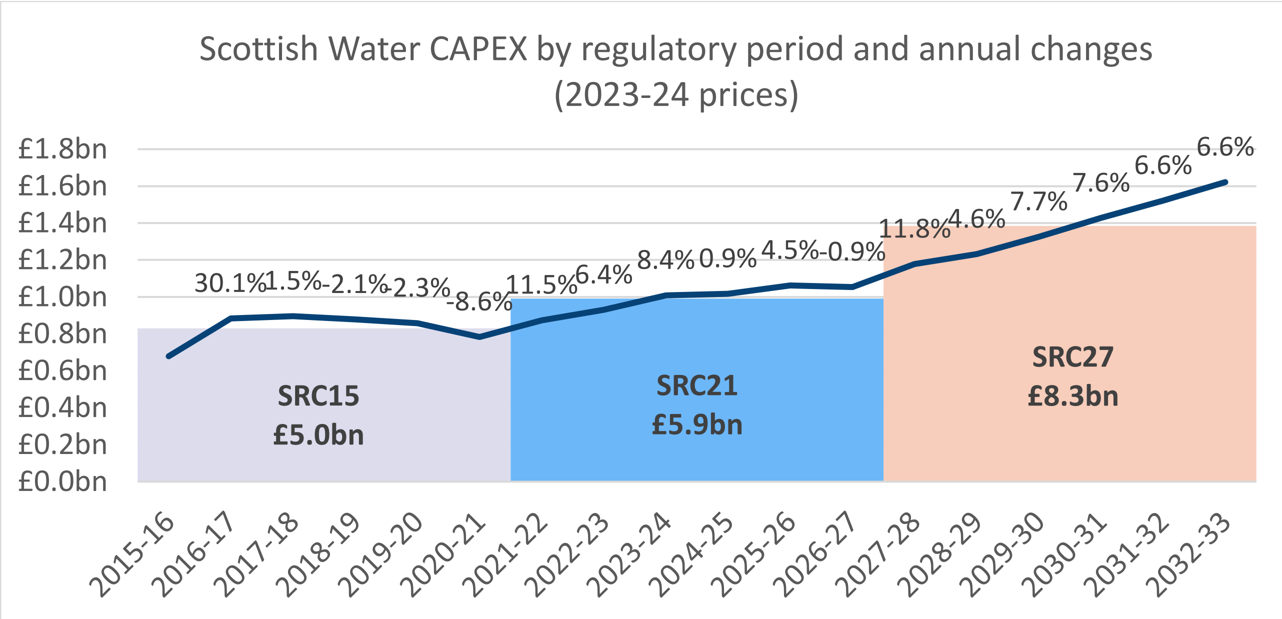
- deliverability of the investment programme;
- asset maintenance;
- investment cases;
- efficiency and benchmarking data; and
- approach to SRC21 completion investment.

[54] Table 1 provides forecast of 165l by end of SRC33 period, 2018-19 PCC is reported as 167l.

## DELIVERABILITY OF THE INVESTMENT PROGRAMME

4.5.2. Scottish Water proposes an investment programme of £8.3 billion (2023-24 prices) within its draft business plan with a gradually increasing profile over the 2021-27 regulatory period. This represents around a 40% increase compared to the planned investment programme for the SRC21 period of £5.9 billion (2023-24 prices), as shown in figure 9 below. This proposed increase in investment over a single regulatory period is unprecedented in the water industry in Scotland.

*Figure 9: Scottish Water CAPEX by regulatory period and annual changes (2023-24 prices)*




4.5.3. The final methodology identifies that the deliverability of Scottish Water's proposed investment plan is an important consideration for SRC27. As such, WICS required the Scottish Water Board to provide assurance within its assurance statement that its business plan is "deliverable, considering factors such as the capacity of the supply chain in Scotland to deliver the proposed investment programme".[55]

4.5.4. WICS notes that Scottish Water's Board assurance report does not provide a statement on the deliverability of the investment programme.[56] However, the draft business plan explains that the investment programme is deliverable with further information on Scottish Water's procurement of its proposed new investment delivery model (i.e. the Delivery Vehicle 4 Enterprise Model) provided in the associated Technical Appendix 11 (or TA011).

4.5.5. Technical Appendix 11 provides an overview of the known planned infrastructure investment across the UK and Scotland in particular over the next 10-15 years and outlines expected constraints in the market such as wage inflation, increases in materials prices, lead

[55] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.15.
[56] Scottish Water (2025) ), 'SR27 draft business plan – investing in Scotland's future', 12 June 2025, pp.8-9.

times and labour availability. Scottish Water explains there is some existing unutilised capacity within its existing delivery routes, which could support delivery in the 2027-33 regulatory period. Most of the Appendix explains the structure of the proposed new investment delivery model and the process for developing it.

4.5.6. This new delivery model will fundamentally change how Scottish Water delivers its investment programme by creating new roles and responsibilities. For example, Scottish Water is developing a new 'primary designer' role, consisting of 1-2 partners from the supply chain who will work closely with existing teams to promote standardisation in asset delivery. WICS notes that this will represent significant organisational and cultural change within Scottish Water (as identified in sub-section 3.6 'Risk and mitigations' in TA011), raising further questions over how quickly it could embed the new delivery model and scale up its investment programme, especially noting the 12% increase in investment proposed in the 2027-33 regulatory period shown in Figure 9.

4.5.7. WICS has commissioned work to examine the capacity of the supply chain and Scottish Water's internal capacity to deliver the investment programme proposed in the draft business plan, and to provide an estimate of the size of the investment programme that Scottish Water could deliver efficiently. As part of that analysis, WICS and Turner and Townsend have examined Scottish Water's analysis presented in TA011 through further information requests and interviews. WICS notes that the work remains underway and welcomes that Scottish Water has agreed to provide further analysis of the capacity of its proposed new investment delivery model in August 2025 as it reaches a further milestone in procuring the new arrangements.

4.5.8. Taking account of these factors, there is insufficient evidence at this stage to demonstrate that the proposed investment programme is deliverable, recognising that the procurement of the new partners remains underway.

## ASSET MAINTENANCE AND HEALTH

4.5.9. The WICS SRC21 draft and final determinations marked a change in approach to asset maintenance compared to previous regulatory periods. Overall, the approach placed greater focus on infrastructure resilience to address the long-term challenges facing the industry (see sub-section 2.2).

4.5.10. This change in approach has also been recognised by the Independent Water Commission in its final report on the review of the water sector in England and Wales (also referred to as 'the Cunliffe review', named after the chair of the Commission, Sir Jon Cunliffe).[57] One of the

[57] Independent Water Commission (2025), '*Independent Water Commission: Final Report*', 21 July 2025. Available at: https://assets.publishing.service.gov.uk/media/687dfcc4312ee8a5f0806be6/Independent_Water_Commission_-_Final_Report_-_21_July.pdf

key recommendations in the final report relates to the need for setting a forward-looking infrastructure resilience framework and standards at a national level for England and Wales.

4.5.11. The SRC21 approach is also aligned to the Scottish Government Investment Hierarchy which requires that infrastructure organisations should maximise the useful life of existing assets by prioritising maintaining and enhancing them over building new ones.[58] This is reflected in Scottish Water's own SRC21 Investment Hierarchy where asset maintenance and enhancement (Categories 1, 2 and 3a) is generally prioritised over building new assets (Category 3b).[59]

4.5.12. The final methodology builds on the SRC21 approach, and sets out the requirements for capturing the asset maintenance and health forecasts in the draft business plan. These included:

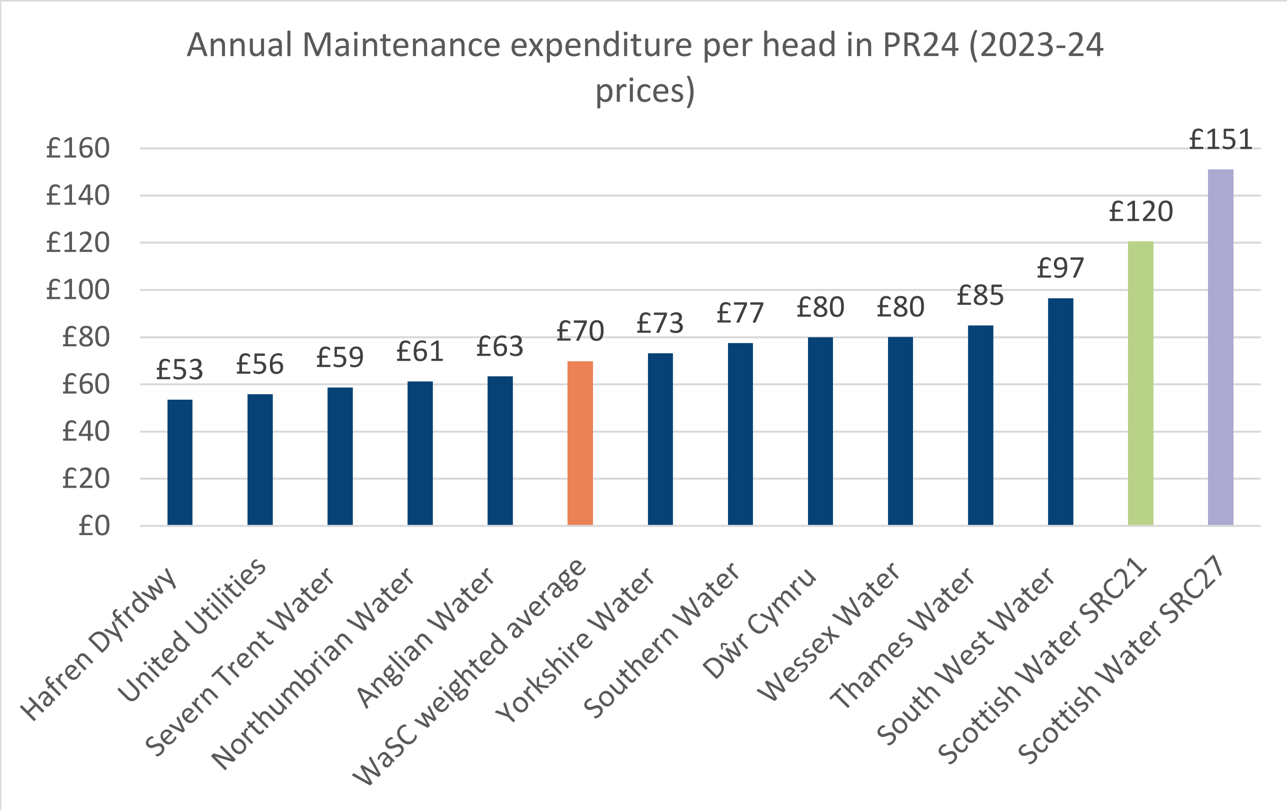
- expectations on Scottish Water developing an asset condition measure or measures;
- continuing to improve its knowledge of its asset base and long-term replacement costs; and
- providing detailed bottom-up evidence for future asset replacement needs including an investment baseline with clear descriptions of expected measurable outcomes across different asset categories and how these investments will impact the condition and performance of the asset base, and other requirements.

4.5.13. Scottish Water's draft business plan includes asset maintenance investment of £4,961m, which represents a 30% uplift in maintenance investment between 2021-27 and 2027-33 regulatory periods.

4.5.14. WICS compares Scottish Water's proposed asset maintenance investment for the 2027-33 regulatory period to that of the companies in England and Wales over PR24. When expressed on an annual basis per head of population, Scottish Water's SRC27 asset maintenance investment is around 120% higher than the England and Wales average and around 60% higher than that of the company with the highest maintenance investment, as shown in Figure 10 below.

[58] Scottish Government (2021), 'A National Mission with Local Impact: Infrastructure Investment Plan for Scotland 2021-22 to 2025-26', 4 February 2025, p.25. Available at: https://www.gov.scot/publications/national-mission-local-impact-infrastructure-investment-plan-scotland-2021-22-2025-26/documents/.
[59] Scottish Water (2025), 'SR27 draft business plan: Technical Appendix 008 – Investment Planning', 12 June 2025, p. 33.

*Figure 10: Annual Maintenance expenditure per head in PR24 (2023-24 prices)*




4.5.15. WICS recognises that there are factors that can help explain some of these differences, with these factors having both positive and negative impacts on maintenance investment. For example, the difference in the approach to asset maintenance could result in Scottish Water having higher maintenance expenditure per head of population relative to other companies. However, using PFI contracts involving third parties operating and maintaining 21 wastewater treatment facilities would result in Scottish Water having lower maintenance expenditure per head of population relative to other companies. As such, given the additional maintenance investment in Scotland, WICS requires confidence in both the efficiency of the proposed expenditure and the impact of the maintenance investment on the condition of the asset base.

4.5.16. The rest of the sub-section focuses on the main areas which WICS considers Scottish Water should further develop and strengthen the evidence in preparing the final business plan.

## Long-term replacement costs

4.5.17. The final methodology requires Scottish Water to develop detailed bottom-up information on future asset replacement needs, to complement the top-down analysis of long-term replacement costs undertaken for SRC21.[60] As set out in the final methodology, WICS

[60] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.88.

expects Scottish Water to continue building an understanding of these long-term replacement costs based on the analysis in SRC21.

4.5.18. WICS welcomes that Scottish Water has provided the detailed bottom-up information on the maintenance interventions and expenditure, as requested in the business plan guidance and data tables.

4.5.19. On the top-down analysis of long-term replacement costs, Scottish Water sets out how it has taken forward the analysis from SRC21 in Technical Appendix 8 (TA008).[61]

4.5.20. As Scottish Water is aware, during 2021 both WICS and Scottish Water participated in a cross-jurisdictional project examining how companies and regulators can gain a better understanding of long-term replacement costs in the water industry.[62] The work identified several areas that Scottish Water's analysis in SRC21 could be taken forward, covering:

- Further disaggregating asset types (e.g. civil structures versus mechanical, electrical equipment) and broadening the analysis to consider large civil structures; and
- Incorporating the interaction between repair and refurbishment (life extending activities) versus end of life replacement into the analysis.

4.5.21. Scottish Water then took this work forward with companies in England and Wales. WICS does not expect Scottish Water to have addressed all of these points. However, one material area that requires further clarity is how Scottish Water has considered the balance between repair and refurbishment investment, versus asset replacement. This understanding is essential to ensure that the asset base is being managed as efficiently as possible.

4.5.22. For example, Scottish Water's draft business plan proposes repair and refurbishment investment of £2,415 million,[63] which represents a 10% uplift in investment compared to the SRC21 period. This is nearly the same amount of investment as the proposed £2,546 million for asset replacement, which is around 49% higher compared to the SRC21 period.[64]

4.5.23. WICS expects the final business plan to explain how Scottish Water has sought to achieve an appropriate balance between repair and refurbishment and asset replacement investment in 2027-33, and how Scottish Water has factored the increase in repair and refurbishment

[61] Scottish Water (2025), 'SR27 draft business plan: Technical Appendix 008 – Investment Planning', 12 June 2025, pp.67-76.

[62] This work was undertaken through an asset replacement group comprising WICS, Scottish Water, Northumbrian Water and Sydney Water.

[63] WICS infers that the £2,415 million of asset repair and replacement also includes expenditure on asset inspections. WICS requests Scottish Water to explicitly explain in the final business plan how much expenditure on inspections it proposes and where that has been reported within the data tables. WICS will look to understand the underlying trends in asset repair and refurbishment without inspections.

[64] Percentage comparisons to SRC21 are based on the total SRC21 values in 2023-24 prices from the draft Annual Return 2024-25 table G1 using the CPI cost inflation in table G10. The SRC21 comparison for asset repair and refurbishment also includes the expenditure on inspections.

investment in its top-down analysis of long-term replacement costs considering some of this investment will extend the life of assets and thus defer the need for full end-of-life asset replacement.

### Measure(s) for asset health

4.5.24. The final methodology requires Scottish Water to provide a measure (or measures) of asset condition across its asset base and, as far as possible, translate the impact of maintenance activities on asset condition into tangible consequences that customers will understand.[65]

4.5.25. WICS requires Scottish Water to provide several types of data in this area within the business plan data tables:

- an overall outcome measure (or measures) for asset health in Table 1;
- the Equipment Health Index (EHI) metric using current "basic" methodology considering only asset age as a proxy for asset health for c.30% of the asset base (based on asset value) in Table 3b; and
- an analysis of the length of water mains and sewers split by material type/function and by condition grade based on the number of bursts/collapses in Table 4.

4.5.26. Regarding Table 1, Scottish Water could not finalise an overall outcome measure (or measures) for asset health in time for the draft business plan submission. It proposed to work collaboratively with WICS and other stakeholders to develop this for the final business plan, noting that it would likely be a "shadow" measure in the SRC27 period.[66] It has identified 3 main options: an EHI-based metric for all asset categories using only age, an EHI-based metric for 10 Management Approach categories using both age and condition, and a combination of service-related metrics across relevant areas (e.g., burst rates, AC main replacement, MEICA mean time to fail).[67] Scottish Water also wants to consider developments in measuring asset health within the industry and align to best practice.[68]

4.5.27. Scottish Water should take ownership of developing the measure as the asset owner with the necessary expertise. Recognising the significant maintenance expenditure proposed for the 2027-33 regulatory period, WICS requires that the business plan include a tangible measure with forecasts for the 2027-33 regulatory period. Scottish Water should also demonstrate further that it has fully met the requirement from the final methodology to translate the impact of its maintenance activities into tangible consequences that customers will understand.

[65] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.119.
[66] Scottish Water (2025), 'SR27 draft business plan: Technical Appendix 14 - Performance Monitoring', p.56.
[67] Scottish Water (2025), 'SR27 draft business plan: Technical Appendix 14 - Performance Monitoring', p.21.
[68] Scottish Water (2025), 'SR27 draft business plan: Technical Appendix 14 - Performance Monitoring', p.53.

4.5.28. As part of this evidence, Scottish Water could explain how its maintenance activities over 2021-27 have impacted the asset base and customer outcomes. Such an assessment could help Scottish Water justify maintenance requirements for the 2027-33 regulatory period, especially for asset categories where Scottish Water proposes maintenance investment in line with current levels.

4.5.29. Regarding Table 4, Scottish Water has provided the required condition data for distribution water mains and the accompanying commentary provides further explanation of the methodology followed including assumptions and caveats. However, Scottish Water has not completed the required condition data for sewers. The Table 4 Commentary (p. 12) explains that this is because the "the Level 2 wastewater asset risk model (WWARM) was not developed at function or material level". We note that Scottish Water has committed to completing the sewer condition data in line with the guidance for the final business plan and would welcome early visibility of this ahead of the final business plan.

4.5.30. If Scottish Water cannot provide the evidence requested from the final methodology, then WICS will take responsibility for developing an asset health measure during the 2027-33 regulatory period in consultation with Scottish Water.

### Asset health data improvement plans

4.5.31. The final methodology requires Scottish Water to provide an improvement plan to address gaps in data and knowledge of the condition of its assets in its business plan.[69]

4.5.32. Scottish Water has provided this improvement plan for activities to improve its understanding of the health of its assets and to further develop the EHI measure by April 2027 in Technical Appendix 8, Annex A, section A5. There are further asset health/condition improvement plans in Table 3b Commentary (sub-sections 4.5, 4.6 and 4.7) and Table 4 Commentary (sub-sections 2.6, 3.6, and 4.9), which outline the activities Scottish Water will undertake between draft and final business plan and beyond the final business plan.

4.5.33. However, WICS expects the improvement plan to be more detailed, covering the expected milestones and the due dates for making the proposed improvement activities that Scottish Water could be held accountable for meeting. We also request that for each improvement activity Scottish Water indicates when the information would be reported to WICS with reference to the annual return submission in a specific year. This will allow us to assess whether Scottish Water is making appropriate progress in improving the gaps in its data and knowledge of the condition of its assets.

4.5.34. WICS appreciates that Scottish Water has provided additional plans for improving its data and analytic capabilities to enable better investment decision-making. These have been outlined in Technical Appendix 8 (Annex A, section A4) and the commentaries for Table 2

[69] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.119.

(sub-section 3.4), Table 3a (section 8) and Table 5 (section 5). We would welcome further details around milestones and due dates for these improvements.

## INVESTMENT CASES

4.5.35. For projects and programmes of work that involve an element of enhancement and growth which have not reached Gate 50 of Scottish Water's internal development process (those considered "pre-development"), the final methodology requires Scottish Water to explain its assumptions for the indicative costings and outputs in the draft business plan.

4.5.36. For projects and programmes of work that involve an element of enhancement and growth which have passed Gate 50 (those considered "in-development" and post-commitment), the final methodology requires Scottish Water to provide individual investment cases covering standard information for all projects. The final methodology requires Scottish Water to provide this information for projects with a whole life cost above £6m and programmes of work for projects below this threshold. This would provide WICS with visibility of the full investment programme.[70]

4.5.37. The final methodology set out the standard information for both projects and programmes of work to cover:

- the range of options considered (both traditional and non-traditional) to meet the need for an investment including the risk of not doing anything, recognising that a 'do nothing' option still has an associated cost. We also acknowledge that in some cases Scottish Water may have less flexibility in deciding how and when to deliver investment outcomes, particularly if the situation is urgent and/or poses high risk to public health;
- whether the investment has the support of the quality regulators, DWQR and SEPA;
- how the investment will support climate change adaptation and align with the Scottish Government's policy development work;
- the cost-benefit analysis undertaken to select the proposed solution, taking account of factors such as the level of risk associated with the different options and benefits in terms of what the investment is expected to achieve. Scottish Water should also consider non-financial costs and Strategic Review of Charges 2027-2033: final methodology 123 benefits such as the carbon impact (both operational and embodied carbon), natural and social capital;
- evidence that the proposed costs for the proposed solution are efficient, which could be evidenced through different methods such as comparisons to past projects or the use of industry cost benchmarks (efficiency is covered in more detail below) or external assurance on the robustness of the cost estimates;

[70] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, pp.122-124.

- whether the investment involves partners, recognising the expectation in the Commissioning letter for Scottish Water to continue working closely with partners to identify more sustainable solutions (such as the adoption of blue-green infrastructure and utilising existing legislation such as section 29e to explore innovative solutions) and, if so, how costs will be shared with the partners including the funding arrangements;
- if Scottish Water has already engaged with communities in terms of project design, how those community views have informed the choice of the proposed solution; and
- the output(s) and benefits that will be delivered from the proposed solution and the outcomes that the investment will contribute to in the context of the Objectives of the Scottish Ministers and Scottish Water's contribution to the sector vision.

4.5.38. The final methodology also places additional requirements on two specific categories of projects:

- large projects, defined as projects with a total project value above £100m; and
- Private Finance Initiative funded projects, recognising that Ministers have requested WICS undertake a full examination of Scottish Water's approach to establishing the options and costs of the 4 PFI contracts maturing in the 2027-33 regulatory period.

4.5.39. For these projects, WICS requires Scottish Water to provide external assurance on the proposed approach and the robustness of the cost estimates.

4.5.40. The final methodology explains that investment in development will still need to progress through the revised investment governance process and that project scope and costs may change during the development of these projects. However, WICS will continue to review these proposals for efficiency to set an investment baseline in our final determination and set charge caps. That baseline will then provide the reference point for investment that progresses through the revised investment governance process.

4.5.41. Scottish Water has sought to provide the standard information requested as part of the investment cases by providing its internal project investment appraisals (PIAs) and management approaches. As part of Scottish Water draft business plan submission, it provided 14 Project Investment Appraisal (PIA) documents and 51 Management Approach (MA) policy documents, the latter of which should provide supporting evidence for investment cases for the programmes of works and projects which are beyond Gate 50 but are less than £6m (as explained on page 64 of TA008). WICS has mapped the submitted PIAs and MAs to the relevant lines in Table 5 (where MAs were mapped based on all the investment needs they cover). The total SRC27 value in column 29 of all 125 lines associated with a PIA or an MA is £4.55 billion or c.55% of the proposed £8.3 billion investment in SRC27.

4.5.42. WICS has four overall comments on the standard information requested as part of the investment case:

- Scottish Water has not sufficiently explained the assumptions for costing and outputs for those investments pre-Gate 50;
- Scottish Water has not provided an investment case for all investment that meets the current criteria for projects and programmes of work post-Gate 50 in the final methodology;
- Scottish Water has not provided the additional information requested for large projects above £100m and the projects related to the return of PFI assets upon expiry of the PFI contracts; and
- The information that Scottish Water has provided in PIAs does not cover all of the standard information requested as part of the investment case.

4.5.43. WICS covers each of these areas in turn.

### Programmes of work and projects in early stages of development (pre-Gate 50)

4.5.44. On the first area in paragraph 4.5.42, Scottish Water did not provide its assumptions for indicative costings and outputs for projects for investment pre-Gate 50.

4.5.45. For example, as part of its queries on the draft business plan, WICS requested information to support the investment case, where readily available, for several projects and programmes of work which are pre-development but have a significant estimated spend in SRC27. We welcome that Scottish Water has provided information to support the investment cases for some of these in its response. We further welcome Scottish Water's intention to update the standard requirements of future PIA documents so that they automatically meet WICS' SR27 requirements. The queried investments include but are not limited to the following lines from draft business plan data Table 5:

- Line "P5363112309-807 (Reference) Scenario A" "West Central Bioresource" with total SRC27 expenditure of £325m ;
- Line "AR3-575 (Reference) Scenario A" "Maintenance activities on water mains to reduce the risk to service" with total SRC27 expenditure of £256m;
- Line "AR3-574 (Reference) Scenario A" "Maintenance activities on sections with recurring interruptions to supply" with total SRC27 expenditure of £182m;
- Line "P5363112574-811 (Reference) Scenario A" "Persley Growth from Aberdeen Strategy" with total SRC27 expenditure of £48m; and
- Line "P5363112576-811 (Reference) Scenario A" "Nigg Growth small option" with total SRC27 expenditure of £48m.

4.5.46. Two specific programmes of work which WICS requested further information in its queries are a programme allocation for asset replacement, repair and refurbishment (AR3) of returning PFI assets[71] with total SRC27 expenditure of £284m, and the programme for the

[71] Draft business plan data Table 5, line "AR3-SR27009 (Reference) Scenario A" "AR3 associate with PFI return sites"

non-household smart metering rollout[72] with total SRC27 expenditure of £43m. Following Scottish Water's response, we do not consider it has sufficient evidence on the options considered, the forecast benefits and costs and the assumptions underpinning their calculation. WICS expects further information on these in the final business plan recognising that they are material to the outcome of the Strategic Review of Charges.

4.5.47. Finally, WICS queried Scottish Water on some potentially material investment requirements identified on page 32 of Technical Appendix 1 (TA001) for a number of WTW with a Letter of Commitment for Haloacetic Acids, WTW with persistent non-trivial failures, and for addressing needs at Daer WTW as per other Letters of Commitments which Scottish Water indicated are not included within the reference scenario investment plan. In its response to the query, Scottish Water explained it is in the early stages of developing solutions for these sites and, as such, it is not able to provide reasonable estimates. We are concerned that could be material investment arising during the regulatory period which will reduce available funding for investment in other areas currently in the plan. WICS recognises this is an inherent feature of the rolling investment programme. However, Scottish Water could better explain the risks associated with not including allocations for these investments within the plan (noting that for example there are material indicative costings for the AR3 associated with PFI return sites as mentioned in paragraph 4.5.46. It could also be useful to provide an order of magnitude estimate of the cost, to provide stakeholders with a greater understanding of the risk in this area.

4.5.48. Based on these observations of the information submitted by Scottish Water in the draft business plan, we expect Scottish Water to clearly explain the rationale for the investment need as well as the assumptions for the benefits and costing of investment pre-Gate 50 within the final business plan submission. This includes explaining the methodology used for calculating the estimates as well as the underpinning assumptions. Example programmes include the UID programme (discussed in the next sub-section) and the AR3 programme for returning PFI assets where Scottish Water should explain how the programme costs have been calculated, e.g. if the costing are based on unit costs, then WICS would want to understand what those unit costs are and how they have been derived.

### Programmes of work and projects requiring an investment case (Gate 50 onwards)

4.5.49. On the second area in paragraph 4.5.42, there are 45 lines in Table 5 of the draft business plan which meet the threshold criteria and require an investment case,[73] having a total SRC27 expenditure of £703m (2023-24 prices). WICS expected Scottish Water to provide 33

[72] Draft business plan data Table 5, line "P940-940 (Reference) Scenario A" "Meter installation for all first time registered non domestic premises as per policy and provides meters for domestic occupants -Top down adjustment"

[73] The 45 lines are those which are categorised as being "Investment in-development/pre-commitment" or "Committed List Named Project" in column 15 "Committed status", i.e. post Gate 50.

investment cases to cover these lines.[74] However, only 14 of these 33 investment cases have been submitted in the form of 10 PIAs and 4 MAs. These have a total SRC27 expenditure of £471m which is two-thirds of the investment that met the criteria for an investment case. As such, Scottish Water has not fully met the criteria for providing investment cases.

4.5.50. Furthermore, in one of our queries, WICS requested Scottish Water to provide the investment case for the Unsatisfactory Intermittent Discharges (UID) programme of works. We recognise that the UID programme is not fully past Gate 50; however, it is a high-value programme with some constituent projects being on the Committed List or past Gate 50. The estimated total SRC27 expenditure of the UID programme is £393 million, which makes it the highest value expenditure item.

4.5.51. Some examples from the investment cases not submitted are listed in Table 4 below. WICS welcomes that Scottish Water has provided information to support the investment cases for some of these in its response to our draft business plan queries, including the UID programme. We continue to expect the full investment cases for all relevant projects and programmes which meet the final methodology criteria to be provided either in advance of the final business plan or alongside the final business plan.

*Table 4: Sample of projects and programmes meeting the threshold without an investment case in the draft business plan submission*

| Unique ID | Description | Proposed cost over SRC27 | Total cost |
|---|---|---|---|
| Various | UID Programme | £393.3m | £467.6m |
| Under£6M-837 (Reference) Scenario A | To reduce flood risk to customers impacted by repeat high consequence internal sewer flooding where not disproportionately expensive | £108.4m | £145.7m |
| Under£6M-532 (Reference) Scenario A | Improve Water Treatment Works (WTWs) with persistent non-trivial fails (Group 1) (committed / enforced). | £16.2m | £88.7m |
| Under£6M-835 (Reference) Scenario A | To reduce flood risk to customers impacted by repeat high consequence external sewer flooding where not disproportionately expensive | £22.6m | £36.3m |
| Under£6M-533 (Reference) Scenario A | Improve Water Treatment Works (WTWs) with persistent non-trivial fails (Group 2) | £19.6m | £27.4m |

[74] 14 of the 45 lines relate to projects for benchmarking and, as such, Scottish Water explains in Table 5 Commentary (PDF page 10) that these have been excluded from the process of grouping into a programme of works line because they require separate inputs in Blocks K and M of the data table. These 14 projects cover 2 investment needs and, therefore, WICS expects could be covered by 2 separate investment cases.

| Unique ID | Description | Proposed cost over SRC27 | Total cost |
|---|---|---|---|
| Under£6M-536 (Reference) Scenario A | Develop solutions at 21 sites (auto shutdown / run to waste) | £15.2m | £19.1m |
| P5363110201-837 (Reference) Scenario A | W571 - Dolphin Road Glasgow | £13.7m | £14.5m |

4.5.52. WICS must ensure that it has the information required to review Scottish Water's investment proposals and set a baseline. As such, WICS requests that Scottish Water provides a list of the projects and programmes that it expects will meet the final methodology criteria by the time of the final business plan by 29 September 2025.

4.5.53. For the investments which have passed Gate 50, we expect Scottish Water to provide the investment cases as per the threshold requirements in the final methodology. In its responses to the draft business plan queries, Scottish Water has applied further thresholds to reduce the number of cases it proposes to submit. WICS does not agree with the application of the criterion for at least 50% of the total project/programme investment expenditure to be planned for SRC27, and so expects any investment meeting the existing final methodology criteria to be covered by an investment case.

4.5.54. WICS expects Scottish Water to provide the data in Table 5 of the final business plan as requested by the final methodology and business plan table guidance with any identified projects that have a total project value of at least £6m reported in a separate line. We note that this appears not to have been the case in the draft business plan submission. For example, in its response to one of our queries, Scottish Water notes that one of the projects included in programme "Under£6M-837 (Reference) Scenario A" "To reduce flood risk to customers impacted by repeat high consequence internal sewer flooding where not disproportionately expensive" is project for internal sewer flooding with investment code 5363110205[75] with a total SRC27 value of £6.2m.

## Information on large projects or projects related to the return of PFI assets

4.5.55. The draft business plan does not include the requested information or external assurance on large projects above £100m and the projects related to the return of PFI assets upon expiry of the PFI contracts (the third area in paragraph 4.5.42). WICS requires this information and the results from its external assurance in the final business plan to ensure confidence in the proposed approach and robustness of the cost estimates.

[75] Scottish Water's query response provides the project name which is the property address with internal sewer flooding problems. For privacy purposes, the project name has been substituted for the associated investment code provided in Table X, which has been shared with WICS for information alongside the draft business plan submission.

### Standard information

4.5.56. The information provided in the Scottish Water internal PIAs does not cover all of the standard information in paragraph 4.5.37. For example, the final methodology requires Scottish Water to provide information on the range of options considered to meet the need for investment. However, we note that the PIAs does not include all options considered.

4.5.57. It is for Scottish Water to decide how it meets the requirements from the final methodology; however, as a minimum we expect the standard information requested on investment projects and programmes of work as set out in our final methodology.

## CAPITAL INVESTMENT EFFICIENCY

### Approach to capital efficiency

4.5.58. The final methodology set out the elements of Scottish Water's proposed efficiency work plan, which involves a combination of different techniques, including:[76]

- using external consultants to benchmark the direct construction costs;
- benchmarking of Scottish Water's indirect and on-cost levels against those of companies in England and Wales, supported by three external cost consultants;
- benchmarking against Scottish Water's outturn costs of delivering similar projects in previous years;
- benchmarking Scottish Water's enhancement costs forecasts against data from companies in England and Wales using Ofwat's econometric benchmarking of enhancement costs; and
- conducting an external review of a sample of projects from Scottish Water's plan.

4.5.59. Furthermore, the final methodology set out that WICS would undertake a review of a sample of projects and programmes to understand:

- the investment need as part of the investment case;
- whether the scope of the solution is appropriate; and
- the cost efficiency of the solution proposed.

4.5.60. The final methodology also set out that reviewing the sample of projects and programmes would become an important step in the process for defining the investment programme on a rolling basis throughout the 2027-33 regulatory period.

4.5.61. As set out in section 2.4, Scottish Water provided early visibility of its findings from its benchmarking analysis in February 2025. WICS provided feedback on these findings in March 2025.

[76] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, pp.124-125.

4.5.62. WICS notes that some of the points raised in the feedback are not yet reflected in the draft business plan, recognising that Scottish Water was preparing to sign off the plan internally ahead of sharing the draft plan with stakeholders in June.

4.5.63. Scottish Water considers that its capital efficiency is broadly in line with the median companies in the water industry in Great Britain and that there is no further scope to catch up with the best-performing companies. Scottish Water uses the industry median company as a benchmark to reflect regional differences that may impact costs and uncertainty in the cost estimates.

4.5.64. While Scottish Water considers that it is already an efficient company, Scottish Water's draft business plan includes an annual efficiency challenge of 0.8% a year to reflect the scope for productivity improvements. Scottish Water has not, at this stage, proposed an adjustment to reflect that its capital costs could increase at a rate different from general economy-wide inflation, as measured by the consumer price index (CPI) inflation.

4.5.65. The remainder of this subsection considers:

- WICS further comments on Scottish Water's cost benchmarking assessment;
- the enhancement benchmarking models;
- the proposed productivity improvement; and
- WICS review from the sample of projects and programmes proposed in the draft business plan.

### Cost benchmarking

4.5.66. Scottish Water has provided one report from an external consultant who benchmarked Scottish Water's direct construction costs, and three reports from external consultants who benchmarked Scottish Water's indirect cost, or on-costs. Technical Appendix 12 (TA012) provides Scottish Water's summary of these reports and its own assessment and proposal that no catch-up efficiency challenge is applied to its capital expenditure in SRC27. Scottish Water's summary and explanation in TA012 contains minor updates and clarifications compared to those provided by Scottish Water to WICS in February 2025. Scottish Water has also provided a peer review report by First Economics on the approach and results of the efficiency analysis of capital and operating expenditure.

4.5.67. WICS' feedback from March 2025 on the evidence provided in February 2025 noted that "Regarding the evidence provided from the consultant reports on the benchmarking of direct and indirect costs, we are not convinced that the evidence presented fully supports Scottish Water's provisional statement that no catch-up efficiency is required" (p. 5). WICS outlined its more detailed observations and questions on the methodology used by the consultants in an appendix to the feedback letter.

4.5.68. The draft business plan has not addressed most of the points from WICS' March 2025 feedback on efficiency evidence. WICS recognises that this is due to the short timeframe Scottish Water had available between receiving WICS' feedback and submitting the draft business plan for internal approvals prior to submission. As such, we continue to consider that further evidence is required to demonstrate that WICS should not set a catch-up efficiency challenge for capital costs for SRC27.

4.5.69. In particular, WICS will consider applying an efficiency challenge to expenditure related to civil engineering non-infrastructure assets based on the current evidence that Scottish Water's expenditure for that asset category is 11.5% above the industry average benchmark. We acknowledge that Scottish Water will continue investigating the reasons for this high variance and will consider factors such as data availability and exceptional circumstances around timing and location of costs.[77] The First Economics peer review report also notes that it is possible there is scope for a catch-up efficiency challenge in this area pending these further investigations.[78]

4.5.70. Some of the remaining material gaps in evidence as identified in the March 2025 feedback include:

- whether wastewater infrastructure asset direct costs are included in the overall analysis (updated for the 'Level 0' models). The original analysis results for this expenditure had the highest positive variance compared to the industry benchmark and these assets represent the largest proportion of the value of the total asset base. As such, the costs for this asset category could have a material impact on the overall efficiency position;
- providing more evidence to support the use of the industry median rather than the industry upper quartile as the most appropriate benchmark. WICS notes that the First Economics peer review report supports the use of the industry median/average rather than the upper quartile;[79]
- more detailed explanations of the methodology used for both the direct costs and indirect costs benchmark analyses; and
- more detailed explanations of the reasons for the results of the indirect costs benchmark analysis such as for differences in Scottish Water's efficiency position relative to the industry benchmark between the three consultant reports or for differences between client and contractor on-costs.

4.5.71. In our assessment of the scope for a catch-up efficiency challenge for indirect capital costs, WICS will consider the findings of engineering consultants WSP, who are reviewing Scottish Water's proposed level of overheads for 2027-33.

[77] Scottish Water (2025), 'SR27 draft business plan: Technical Appendix 12 - Efficiency', p.14-15.
[78] First Economics (2025), 'SR27 Benchmarking: Peer Review', 14 March 2025, p.3.
[79] First Economics (2025), 'SR27 Benchmarking: Peer Review', 14 March 2025, p.3.

### Enhancement benchmarking models

4.5.72. WICS requested information on 12 enhancement areas as candidates for benchmarking in the business plan tables. In the draft business plan, Scottish Water did not provide sufficient information on nine out of the 12 enhancement areas for benchmarking purposes. WICS requested this information through its query process on the draft business plan submission. Table 5 provides a summary of the remaining gaps following the query process.

*Table 5: Gaps in completing information for enhancement benchmarking purposes.*

| Ref. | Enhancement area | Current status following the queries | Next steps |
|---|---|---|---|
| **5.K** | Phosphorus removal | Scottish Water did not provide information on historical consents.<br><br>Scottish Water did not provide an allocation of expenditure between phosphorous removal and sanitary permits. | Provide data on historical consents.<br><br>Report the investment on phosphorous removal and sanitary permits as separate rows in Table 5. |
| **5.L** | Sanitary permit | Scottish Water did not provide an allocation of expenditure between phosphorous removal and sanitary permits. | Report the investment on phosphorous removal and sanitary permits as separate rows in Table 5. |
| **5.M** | Storm overflows | Scottish Water explained that it will be able to provide this information once the projects are at a more advanced stage of development (Scottish Water internal Gate 50). | Provide the data for projects that are already post-Gate 50. |
| **5.N** | Water resources | Scottish Water explained that it will be able to provide this information once the projects are at a more advanced stage of development (Scottish Water internal Gate 50). | Provide the data for projects that are already post-Gate 50. |
| **9.1** | Leakage | There remains an inconsistency between the data reported in Table 2, Table 5 and Table 9. | Report mains replacement data for leakage reduction purposes only in Table 9. |
| **9.2** | Investigations | Scottish Water explained that there are no relevant projects. | No further action at this stage. |
| **9.3a** | Lead, communication pipes | Inconsistency between the data reported in Table 2, Table 5 and Table 9. | Ensure that the data is consistent across all tables. |
| **9.3 b&c** | Lead, internal and external pipes | Information reported incorrectly in the draft business plan, as explained in response to the queries. | Provide the corrected values. |
| **9.4** | Metering | Inconsistency between the data reported in Table 2, Table 5 and Table 9. | Ensure that the data is consistent across all tables. |
| **9.5** | Continuous river water | Scottish Water explained that SEPA is responsible and Scottish Water does not have any planned interventions. | No further action at this stage. |

| | | | |
|---|---|---|---|
| | quality monitoring | | |
| **9.6** | Flow monitoring at WWTW | Scottish Water did not provide the number of flow monitoring schemes applied and installed, which is the cost driver in the model. Scottish Water explained that this information will be available once it has completed the surveys that are underway. | Provide timescales for completing the surveys and then the data once the surveys are complete. |
| **9.7** | Event duration and flow monitors | Scottish Water provided this information | No further action required at this stage. |
| **9.8** | Chemicals removal | Scottish Water explained that there are no relevant projects in the response to the queries. | No further action required at this stage. |

4.5.73. As shown in Table 5, several gaps in information remain in relation to the enhancement cost benchmarking data. For example, Scottish Water explains that projects for storm overflows and water resources are before its internal Gate 50 stage when it has further data on the scope of solution and proposed costings. However, we note that the following storm overflow projects are post-Gate 50 and therefore should have the data available:

- P5363113420 UID- Arboretum Ave CSO 2
- P5363113453 UID - Valleyfield CSO Assessment
- P5363113459 UID - Torryburn SPS CSO Valleyfield
- P5363113464 UID - St Bridgets Brae CSO Dalgety Bay
- P5363113454 UID - Picnic Site SPS CSO Fochabers 2022
- P5363113419 UID - Murrayfield - Corstorphine Road CSO
- P5363113460 UID - Mill Farm CSO Invergowrie
- P5363113468 UID - Lochloy Road CSO Nairn
- P5363113472 UID - Kirkhill CSO Penicuik
- P5363113467 UID - David Dale CSO Stewarton
- P5363113465 UID - 2 Kirkford Bridge Stewarton

4.5.74. Recognising that the information requested should be available for these projects, we require that Scottish Water provide this data along with the other outstanding information to address the remaining gaps highlighted in Table 5. Given that we have previously highlighted concerns in this area in both February and March, we require that this information be submitted by 29 September 2025.

### Proposed productivity improvements

4.5.75. SRC21 accepted a 1% productivity improvement to expenditure, as explained in the final determination[80]. WICS notes that Scottish Water considers that it is on track to deliver this 1% efficiency challenge on operating and other recurring expenditure.[81]

4.5.76. As Scottish Water recognises, in recent regulatory decisions, regulators have assumed a higher efficiency challenge to reflect the scope for productivity improvements, including Ofwat's PR24 final determinations.[82] Following Scottish Water sharing its draft business plan, Ofgem has also proposed applying a similar efficiency challenge of 1% per annum to electricity and gas transmission companies and gas distribution companies.[83]

4.5.77. We recognise that the 0.8% frontier shift proposed by Scottish Water in its draft business plan aligns with the most ambitious levels proposed by the water and wastewater companies in England and Wales in their PR24 business plans. However, our starting point remains that the 1% per annum productivity efficiency target should continue to apply unless Scottish Water provides compelling evidence to justify a lower figure. This assumption for productivity improvements of 1% per annum remains in line with recent regulatory precedent.

4.5.78. WICS notes that increasing the assumption for productivity improvements from 0.8% to 1% per annum would reduce the cost of the investment programme by around £60m over the 2027-33 regulatory period.

### WICS review from the sample of projects and programmes

4.5.79. Given the materiality of the proposed investment programme, WICS commissioned a technical review of a sample of 2 projects and 2 programmes of work from Scottish Water's draft business plan as well as a review of Scottish Water's proposed level of overheads for 2027-33.

4.5.80. The scope of the review of the sample projects and programmes of work covered:

- whether Scottish Water had considered all reasonable solutions and their risks and costs, including a 'do nothing' option;
- the extent to which Scottish Water has considered risk levels and how Scottish Water's risk tolerance compares to that of other water companies;
- whether the proposed solution is appropriately scoped and, if not, what would be an appropriate scope challenge;

[80] WICS (2020), '2021-27 Final Determination', 10 December 2020, p.9.
[81] Scottish Water (2025), 'SR27 draft business plan – investing in Scotland's future', 12 June 2025, p.66.
[82] Ofwat (2024), 'PR24 final determinations: Expenditure allowances', 20 December 2024, p.261.
[83] Ofgem (2025), 'RIIO-3 Draft Determinations Overview Document', 1 July 2025, p.90.

- whether the proposed solution is appropriately costed compared to similar solutions by other water companies and, if not, what would be an appropriate cost challenge; and
- whether overall the proposed solution would meet the desired outcome most effectively.

4.5.81. The scope of the review also covered whether Scottish Water's analysis of in-direct and on-costs is robust.

4.5.82. WICS engaged with DWQR and SEPA and selected the following sample of projects and programmes for the review:

- Project 1: "SR21 ES Black Esk WTW" (unique ID within Table 5 of the draft business plan: "P5363113084-532 (Reference) Scenario A"). This is a water-related project with a total SRC27 expenditure of £9.6m and total overall expenditure of £103.5m (2023-24 prices).
- Project 2: "North Berwick WwTW – UWWTD Compliance" (unique ID: "P5363112902-809 (Reference) Scenario A"). This is a wastewater-related project with a total SRC27 expenditure of £74.6m and total overall expenditure of £79.8m (2023-24 prices).
- Programme 1: "Maintain treated water storage" (unique ID: "AR3-529 (Reference) Scenario A"). This is a water-related programme with a total SRC27 expenditure of £391.2m and total overall expenditure of £397.6m (2023-24 prices).
- Programme 2: "To reduce flood risk to customers impacted by repeat high consequence internal sewer flooding where not disproportionately expensive" (unique ID: "Under£6M-837 (Reference) Scenario A"). This is a wastewater-related project with a total SRC27 expenditure of £108.4m and total overall expenditure of £145.7m (2023-24 prices).

4.5.83. This sample accounts for £0.58 billion of the proposed £8.3 billion SRC27 investment programme.

4.5.84. We welcome that Scottish Water has engaged in a positive manner with the consultants undertaking the work. The engineering report is still being finalised at the time of issuing this feedback.

4.5.85. There are several themes beginning to emerge from the draft report, including:

- the solutions for the two projects examined appear generally technically sound and appropriate given the investment need;
- there is potential for optimisation of the treated water storage programme; and
- there is a need for more robustness and transparency over the assumed unit rates and cost allocation/categorisation for the programmes of work and the review of overheads.

4.5.86. WICS and Scottish Water continue to review the draft report at the time of providing the draft feedback. We will share the findings with Scottish Water and water industry stakeholders once finalised.

4.5.87. As a general observation, we note several examples of Scottish Water not providing details on the assumptions underpinning its cost estimates, including:

- how the costs for investments pre-Gate 50 have been estimated in the draft business plan;
- the assumptions and methodologies used in the direct and indirect cost assurance reports that require further explanation, as set out in our feedback;
- the assumptions underpinning the £50 billion estimate of required investment from the long-term strategy, investment strategy and sub-outcome summary reports;
- for the assumptions underpinning the WSP review of the sample of projects and programmes (e.g. the unit rates used within the Treated Water Storage programme).

4.5.88. We consider that understanding how costs have been estimated is crucial in justifying the proposed investment.

### COMPLETION INVESTMENT

4.5.89. For investment that spans both the 2021-27 and 2027-33 regulatory periods, our final methodology explains that we "require Scottish Water to clearly set out the completion investment and the source of funding for this investment, to ensure that customers receive the benefits they have paid for".[84]

4.5.90. In the final business plan, Scottish Water must set out how its treatment of such investment is consistent with the requirements of the final methodology, to ensure that customers are not asked to pay twice for investment that should have been delivered in the 2021-27 regulatory period.

## 4.6. Operating expenditure and PFI

### OVERVIEW OF SUB-SECTION

4.6.1. WICS considers that Scottish Water should strengthen the evidence in the following areas:

- evidence for SRC21 efficiency challenge;
- operating expenditure profile;
- operating expenditure efficiency;
- additional operating expenditure from returning PFI assets;
- evidence case for West Central Bioresources;

[84] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.16.

- evidence and assurance for returning PFI options;
- operating-based solutions and partnership approaches; and
- transformation.

### EVIDENCE FOR SRC21 EFFICIENCY CHALLENGE

4.6.2. The final methodology requires Scottish Water to provide evidence on: [85]

- whether it has achieved the Tier 1 efficiency challenge of 1% per annum from SRC21; and
- where those reductions in expenditure have been made with respect to the individual components of Tier 1 expenditure.

4.6.3. Scottish Water explains that they expect a 5.5% reduction in tier 1 costs in SRC21, marginally lower than 5.85%, or 1% per annum.[86] WICS encourages Scottish Water to continue working on further efficiency reductions to achieve the commitment.

4.6.4. Scottish Water should provide further evidence explaining where those reductions in expenditure have been made with respect to the individual components of Tier 1 expenditure, as required in the final methodology.

### OPERATING EXPENDITURE PROFILE

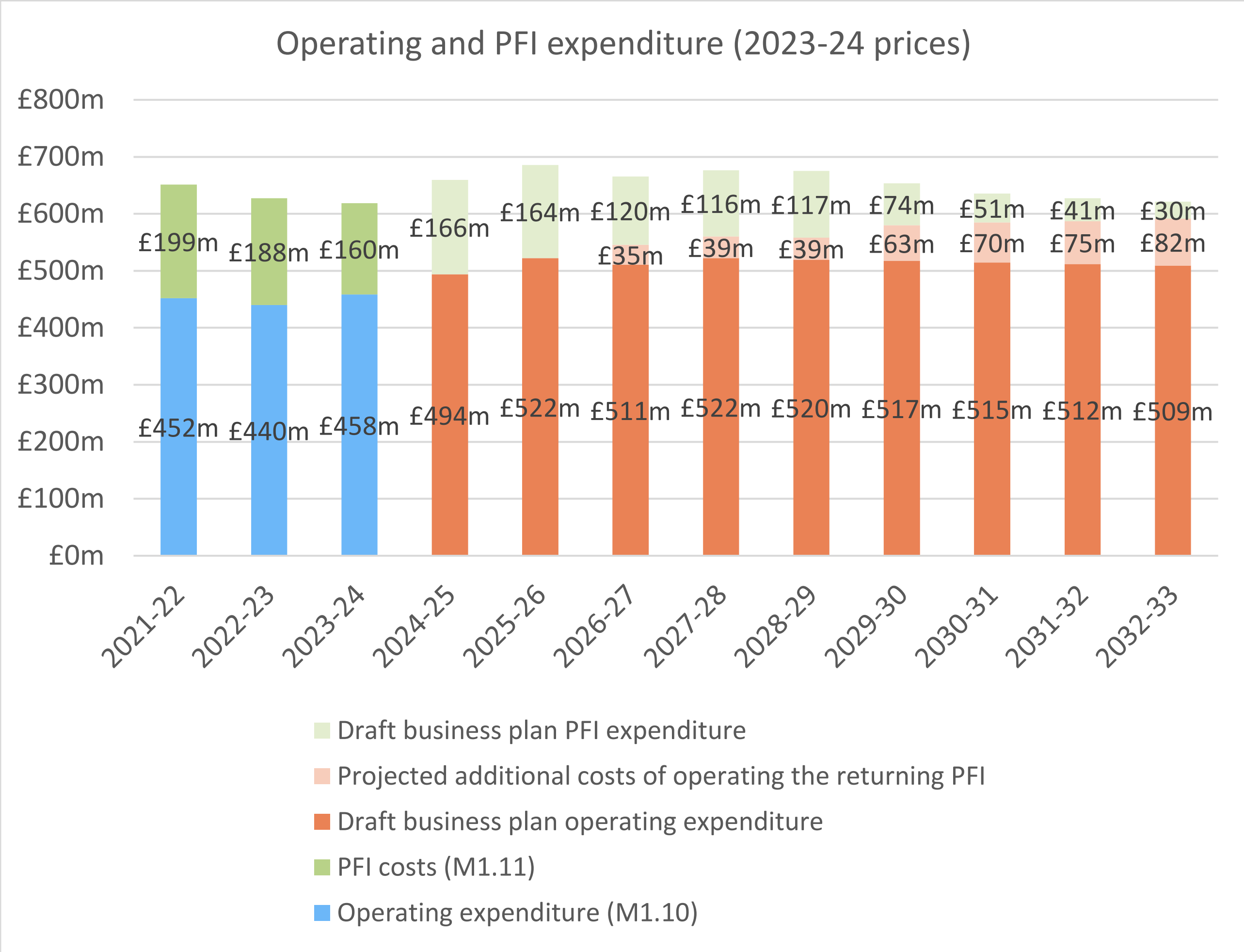
4.6.5. The final methodology requires Scottish Water to provide forecasts for operating and PFI expenditure covering each of the following areas:[87]

- the operating expenditure arising from the return of PFI contracts;
- the adoption of operating-based solutions, rather than capital solutions to deliver improvements;
- spend-to-save or transformation initiatives; and
- the scope for efficiency improvements.

4.6.6. Scottish Water's draft business plan proposes that operating expenditure will increase from £494m in 2024-25 to around £590m as shown in Figure 11, with around £80m relating to the operating expenditure arising from the return of PFI assets upon expiry of the PFI contracts.[88] Figure 11 also shows that expenditure related to the fees to the PFI operators will decrease from around £170m in 2024-25 to £30m by 2032-33.

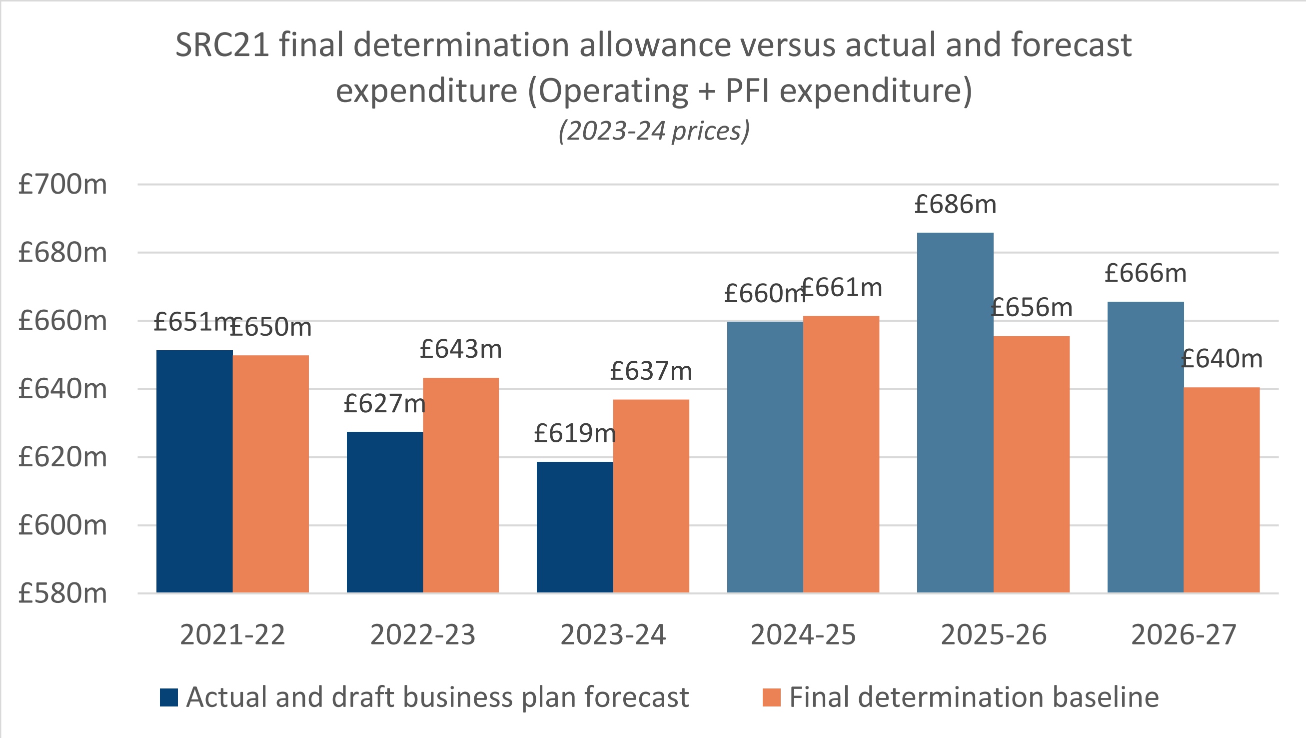
[85] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.103-104.
[86] Scottish Water (2025), 'Transformation & Innovation Technical Appendix', 12 June 2025, p.7.
[87] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.104-105.
[88] Scottish Water (2025), 'SR27 draft business plan: Table 7. Other costs and assumptions', 12 June 2025.

*Figure 11: Operating and PFI expenditure profile*




4.6.7. WICS notes that the proposed additions would result in Scottish Water exceeding the operating and PFI expenditure forecasts underpinning the WICS final determination for SRC21. As shown in Figure 12, Scottish Water's forecast for operating expenditure and PFI fees exceeds the allowance set in the SRC21 final determination by £30 million in 2025-26 and £26m in 2026-27.

*Figure 12: SRC21 final determination operating and PFI expenditure versus draft business plan*



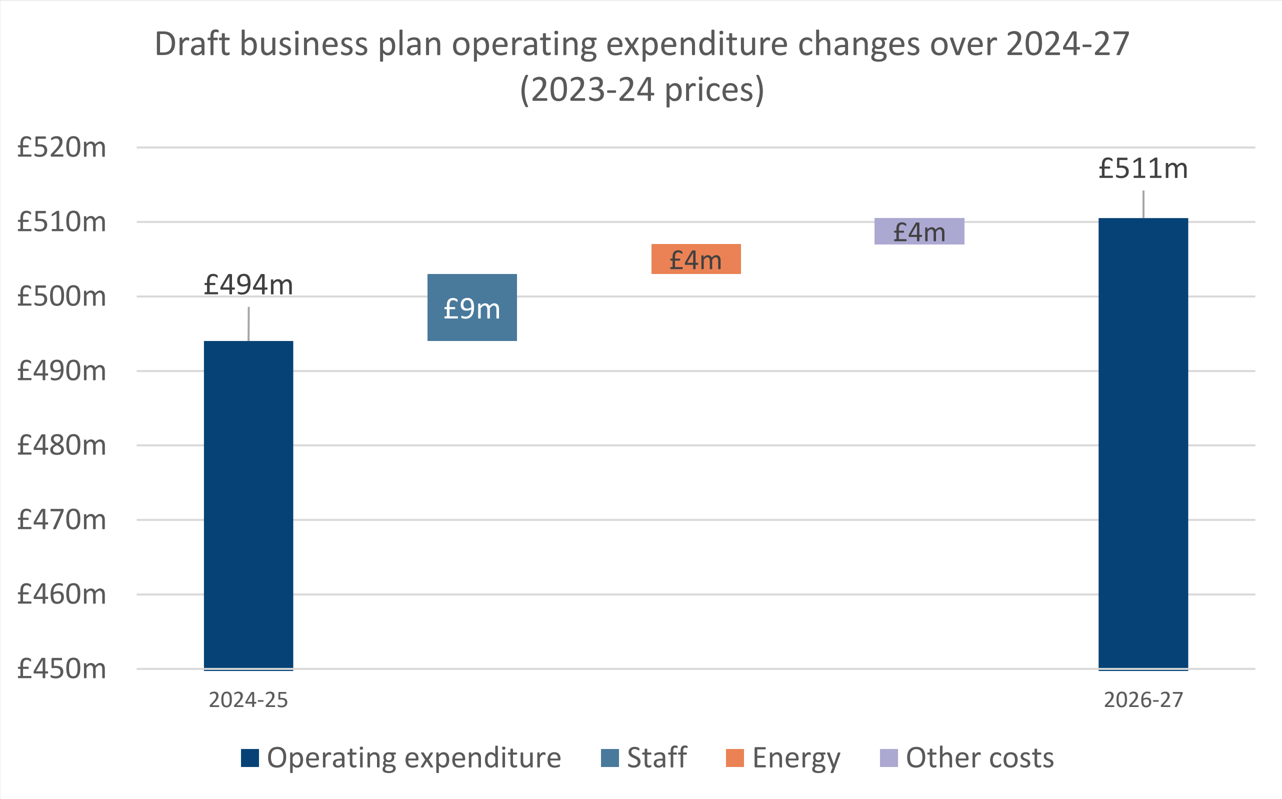

4.6.8. Scottish Water's proposed profile for operating expenditure suggests that it expects to underperform the forecasts in the WICS final determination for SRC21, which the draft business plan does not cover.

4.6.9. The remainder of this sub-section focuses on underlying operating expenditure before the return of wastewater assets upon the expiry of PFI contracts.

### Changes to operating expenditure in 2025-26 and 2026-27 and impact on efficiency

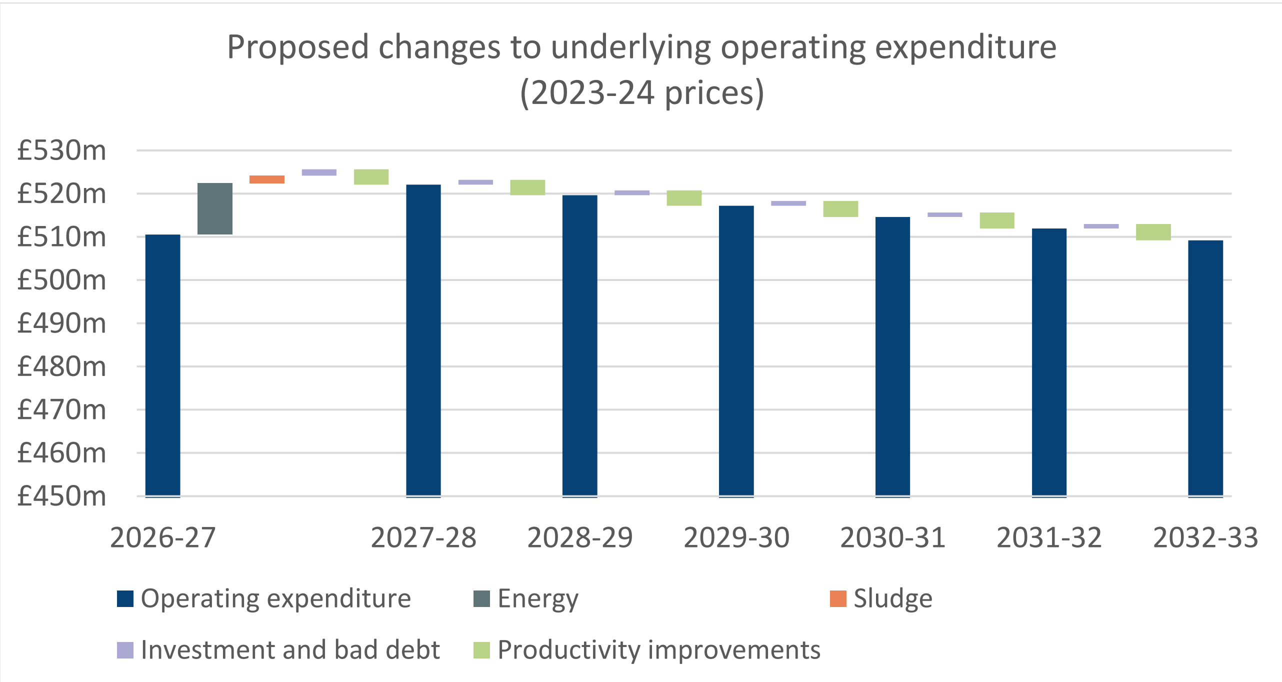
4.6.10. WICS welcomes Scottish Water's long-term strategy commitment to maximise efficiency and minimise the funding required from customers. At an overall level, we note that Scottish Water proposes material additions to operating expenditure in the final two years of the 2021-27 regulatory period, which increases underlying operating expenditure to £510m, as shown in figure 13 below.

*Figure 13: Draft business plan SRC21 operating expenditure additions*




4.6.11. Scottish Water then proposes further additions over the 2027-33 regulatory period with efficiencies bringing operating expenditure back down to £510m by 2032-33, as shown in Figure 14 below.

*Figure 14: Proposed changes to underlying operating expenditure changes over 2027-33*



4.6.12. At an overall level, WICS questions whether the proposed profile of operating expenditure aligns with Scottish Water's commitment from its long-term strategy to maximise efficiency and minimise the funding it requires.

4.6.13. The proposed SRC21 underperformance and the reduction in efficiency ahead of SRC27 require further review by Scottish Water in preparing its final business plan.

## OPERATING EXPENDITURE EFFICIENCY

4.6.14. As set out in the final methodology, there are two elements to efficiency:[89]

- Catching-up to best practice; and
- Ongoing productivity improvements.

4.6.15. Catching up to best practice, or catch-up efficiency, is the reduction in operating expenditure to catch up with the leading performing company (i.e. the 'frontier') on operating expenditure performance after adjusting for differences in operating characteristics across companies. The scope for catch-up efficiency is measured as a snapshot based on historic and current operating expenditure across companies.

4.6.16. Ongoing productivity improvements, or frontier shift, recognising that even the leading performing company (i.e. the 'frontier') should continue to improve its operating efficiency in future years due to technological improvements. This improvement should also be seen in companies that need to catch up to best practice.

4.6.17. There are also real price effects (RPEs) which relate to inflationary pressures above general economy wide inflation as measured by the Consumer Price Index (CPI) measure of inflation. WICS' feedback does not cover RPEs given that Scottish Water did not propose an adjustment for RPEs in its draft business plan. As such, the remainder of this sub-section focuses on catch-up efficiency and ongoing productivity improvements.

### Catch-up efficiency

4.6.18. WICS welcomes its engagement with Scottish Water on developing a shared understanding of the data set and methodological adjustments required to run these models for Scottish Water.

4.6.19. As explained in section 2.4, and highlighted in TA012, WICS commented on Scottish Water's efficiency approach ahead of the draft business plan. Our comments included:

- Scottish Water could seek to develop its own operating expenditure-only efficiency models further.

[89] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.99.

- Scottish Water should provide further evidence on the impact of geographical dispersion on Scottish Water's costs. If Scottish Water considers that revised operating expenditure-only efficiency models do not appropriately account for Scottish Water's geographic dispersion, it could propose a post-modelling adjustment analogous to a 'special factor' adjustment.[90]

4.6.20. Scottish Water is still to address these points from our draft feedback.

4.6.21. In Technical Appendix 12 (TA012), Scottish Water explains how it has used the base expenditure models created by Ofwat for the price review in 2024 (PR24) to assess its efficiency on operating expenditure.[91]

4.6.22. The base cost models exclude expenditure outside of management control such as local authority rates and service charges (such as abstraction licences paid to SEPA). In line with this, PFI fees have been excluded to examine the underlying operating expenditure that Scottish Water has control over.

4.6.23. Based on this analysis, Scottish Water considers itself among the leading water and wastewater companies in Great Britain in terms of operating expenditure efficiency, once it accounts for its higher levels of spending on asset maintenance and the relative rurality of its operating area.[92] Table 6 shows the results from Scottish Water's analysis of applying Ofwat's base cost models on an operating expenditure-only basis.

*Table 6: Scottish Water base cost models re-run as operating expenditure only relative to benchmark*

| Models re-run using operating expenditure only | |
|---|---|
| **Scottish Water water efficiency score relative to median[93]** | 1.00 |
| **Scottish Water water efficiency score relative to upper-quartile** | 1.04 |
| **Scottish Water wastewater efficiency score relative to median[94]** | 0.88 |
| **Scottish Water wastewater efficiency score relative to upper-quartile** | 0.99 |

4.6.24. Scottish Water's results suggest that its operating expenditure efficiency is broadly in line with the company average level in Great Britain (based on the median) for the water service and the leading companies (based on the upper quartile) for the wastewater service excluding PFI assets and expenditure.[95]

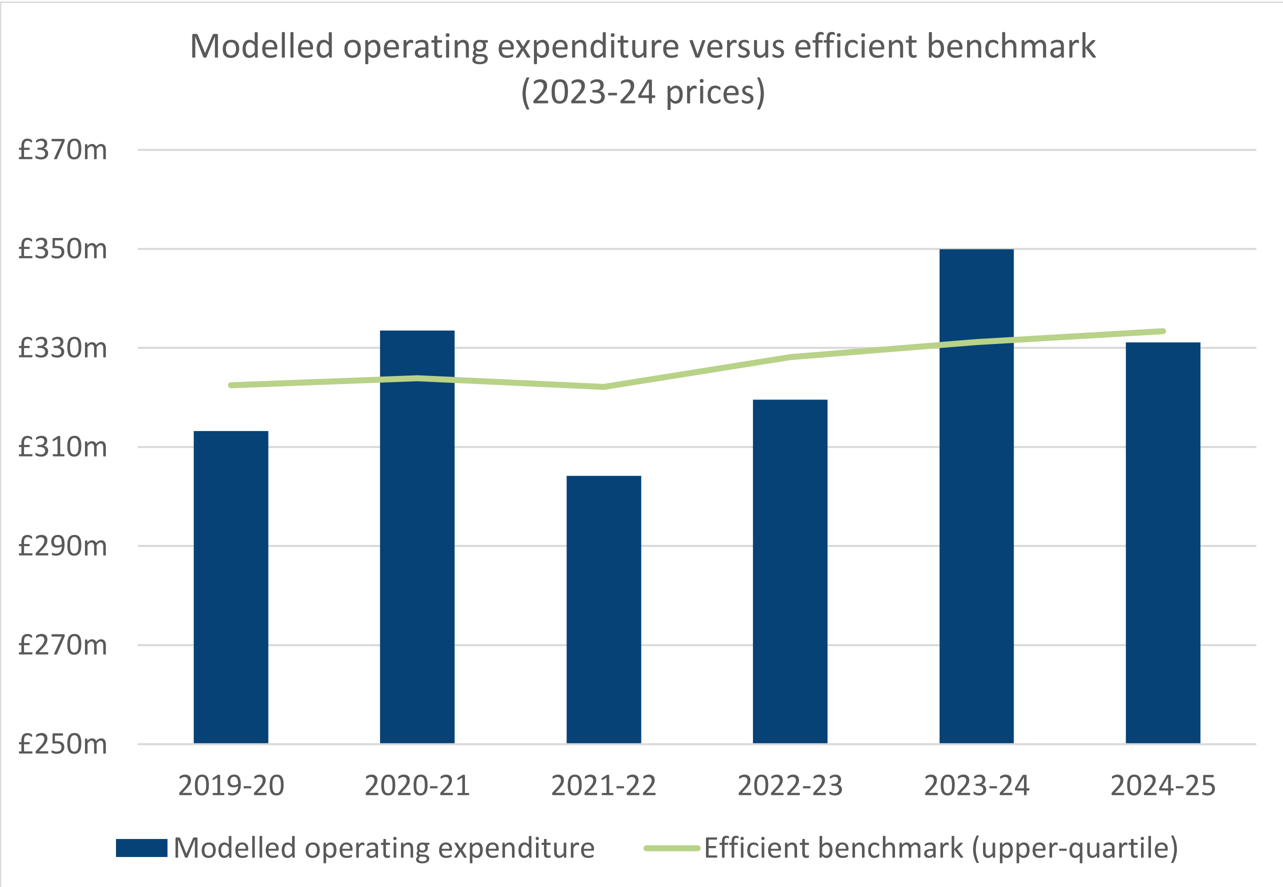
[90] For an explanation of special factors see WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, pp.99-100.
[91] Scottish Water (2025), 'SR27 draft business plan: Technical Appendix 12 - Efficiency', p.9-10.
[92] Scottish Water (2025), 'SR27 draft business plan – investing in Scotland's future', 12 June 2025, p.67.
[93] Scottish Water (2025), 'SR27 draft business plan: Technical Appendix 12 - Efficiency', p.65.
[94] Scottish Water (2025), 'SR27 draft business plan: Technical Appendix 12 - Efficiency', p.87.
[95] The median is the middle ranking company when companies are arranged from most to least efficient. The upper quartile is the top-performing 25% of companies.

4.6.25. Scottish Water's analysis is based on its historical performance from 2019-20 to 2023-24. Recognising Scottish Water proposes a material increase in operating expenditure in 2025-26 and 2026-27, WICS considers it important to examine the profile of operating expenditure over the remainder of the 2021-27 regulatory period and into 2027-33 regulatory period based on the forecasts from the draft business plan.

4.6.26. WICS has conducted its own benchmarking of Scottish Water's operating expenditure to the expenditure of the other water and wastewater companies in Great Britain using Ofwat's base cost models on an operating expenditure only-basis.

4.6.27. Figure 15 compares Scottish Water's actual operating expenditure used for benchmarking purposes (as shown by the blue bars) to an efficient benchmark based on an upper quartile level of efficiency (as shown by the green line) from 2018-19 to 2024-25.[96] This figure shows that Scottish Water's operating expenditure efficiency was broadly aligned with the efficient benchmark over this period, which is consistent with Scottish Water's findings. Scottish Water's operating expenditure used for modelling was £325m (2023-24 prices) on average over the 2019-20 to 2024-25 period, with the efficient benchmark being £327m (2023-24 prices) on average over the same period.

*Figure 15: Actual operating expenditure versus efficient benchmark*

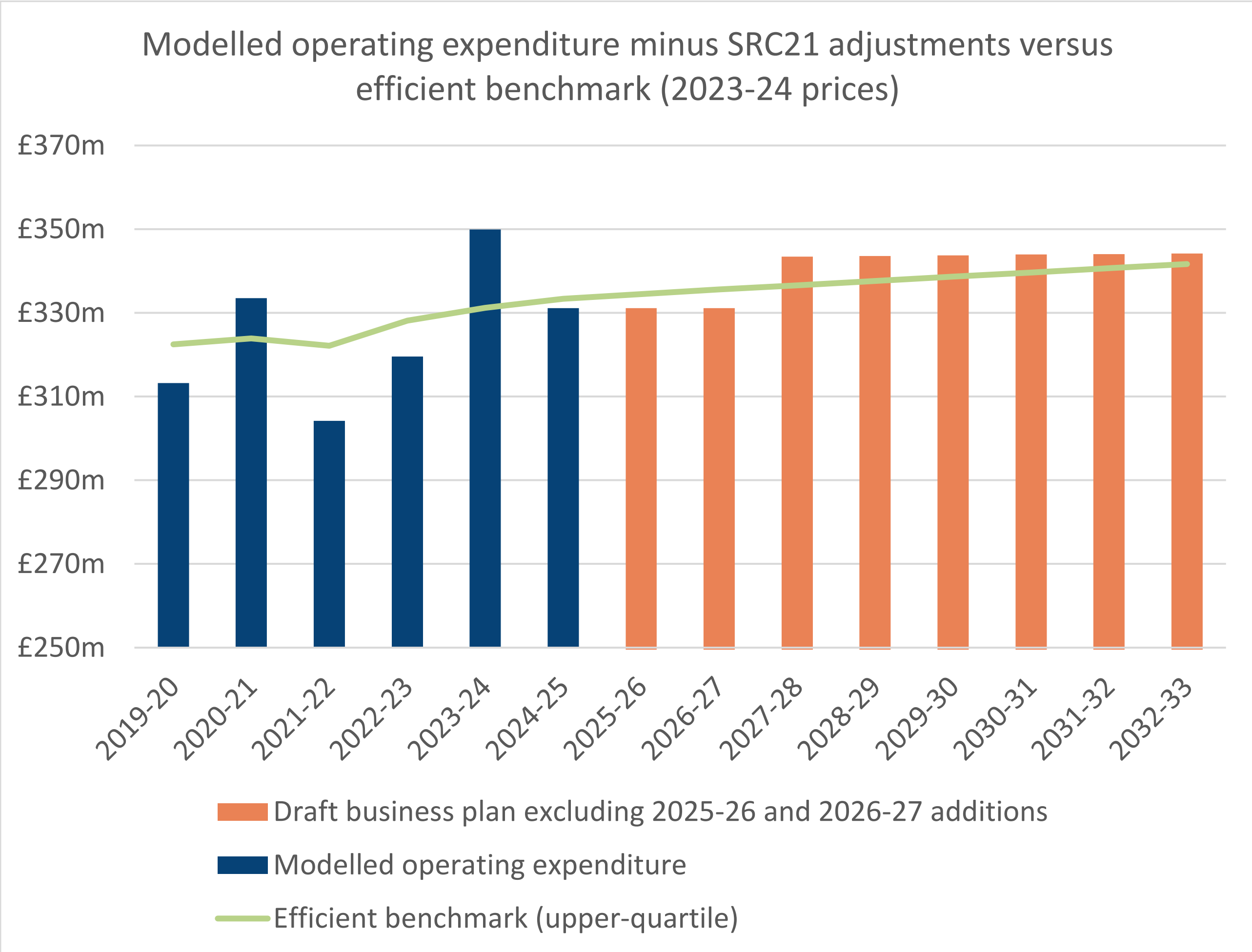



[96] The expenditure used for benchmarking excludes costs outside of management control such as local authority rates.

4.6.28. We expand this figure to include Scottish Water's forecast operating expenditure from the draft business plan (shown by the orange bars in the figures below). To understand the impact of Scottish Water's proposed additions in 2025-26 and 2026-27, we first exclude these proposed additions (Figure 16) and then include them (Figure 17). The additional operating expenditure as a result of operating the returning PFI sites has been excluded so that expenditure is considered in a consistent manner. The expenditure associated with PFI sites is covered separately below.

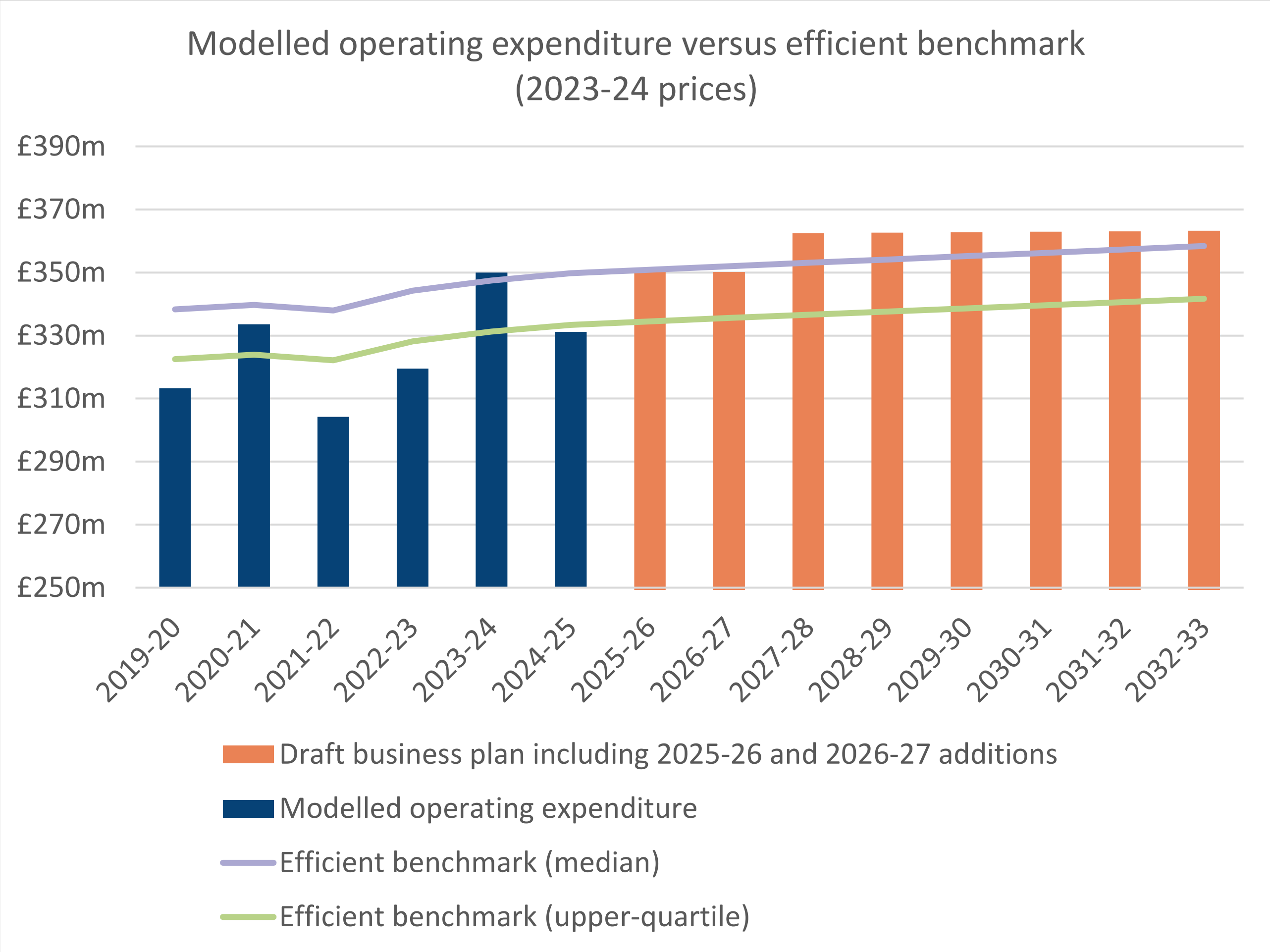
4.6.29. Figure 16 shows the forecast excluding Scottish Water's proposed additions for 2025-26 and 2026-27. Without Scottish Water's proposed additions for 2025-26 and 2026-27, Scottish Water would remain broadly in line with the efficient benchmark over the 2027-33 regulatory period.

*Figure 16: Modelled operating expenditure minus SRC21 adjustments versus efficient benchmark*



4.6.30. Figure 17 repeats the previous figure but now includes Scottish Water's proposed additions for 2025-26 and 2026-27. Scottish Water's forecast operating expenditure is now above the efficient benchmark based on the leading companies and the company average level in Great Britain (as shown in the purple line).

*Figure 17: Modelled operating expenditure (including SRC21 adjustments versus efficient benchmark)*




4.6.31. WICS considers that this analysis may also overstate Scottish Water's efficiency because Scottish Water has increased the level of overheads allocated to capital projects.[97] We will examine this area further with Scottish Water before the final business plan. We also continue to review the merit of the proposed increases over the 2027-33 regulatory period.

4.6.32. In summary, WICS questions whether these proposed additions in 2025-26 and 2026-27 represent efficient expenditure based on:

- the comparison of Scottish Water's forecast operating expenditure against the assumptions in the final determination from SRC21; and

[97] Scottish Water (2025), 'M Tables – Regulatory Accounts Commentary', p.14.

- the efficiency benchmarking against the other water and wastewater companies in Great Britain.

4.6.33. As such, this is an area that requires further evidence in the final business plan and, at this stage, we have not included the proposed additions for 2025-26 and 2026-27 in our financial modelling in section 5. WICS provides further detail on this analysis in appendix 2.

### Ongoing productivity improvements (Frontier shift)

4.6.34. Scottish Water proposes an assumption for ongoing productivity improvements of 0.8%, but has excluded operating expenditure outside of its control, including SEPA fees, business rates and bad debts. As a result, the effective efficiency factor applied to the total operating expenditure reduces to 0.66% per annum.

4.6.35. WICS' starting point is a productivity efficiency improvement of 1% per annum from SRC21 should continue to apply unless Scottish Water provides compelling evidence to justify a lower figure.

4.6.36. As discussed in the sub-section on capital investment efficiency (paragraphs 4.5.58 to 4.5.78), the 1% productivity improvement is consistent with recent regulatory precedent. Such an efficiency challenge would equate to an effective efficiency challenge of 0.80% per annum after excluding SEPA fees, business rates and bad debts.

## ADDITIONAL OPERATING EXPENDITURE FROM RETURNING PFI ASSETS

4.6.37. Scottish Water sets out the proportion of the annual service fee it expects to incur to operate each of the PFI sites after their return.[98] Prior to the draft business plan submission, Scottish Water shared the analysis underpinning this with WICS.

4.6.38. Scottish Water acknowledges that there is uncertainty around the forecast operating costs for the returning PFIs. For example, Scottish Water explain that:

- "To estimate the cost of operating the returning PFI sites we have undertaken a detailed analysis of each site based on available information and at cost category level (e.g. employment costs, chemicals, power etc). Where no information is available, we have used estimates." [99]
- "On a risk aware basis reflecting uncertainty of the asset condition on return, once all four [PFIs] have returned to Scottish Water, operating costs will increase by £55m (which is more than offset by the decrease in PFI fees…)." [100]

[98] Scottish Water (2025), 'SR27 Draft Business Plan: Table 7 – Other Costs and Assumptions Commentary', 12 June 2025, p.5.
[99] Scottish Water (2025), 'SR27 Draft Business Plan: Table 7 – Other Costs and Assumptions Commentary', 12 June 2025 p.4.
[100] Scottish Water (2025), 'SR27 Draft Business Plan: Technical Appendix 013 – Financial Strength', 12 June 2025, p.6.

4.6.39. WICS continues to review Scottish Water's analysis, and its initial review has raised several questions and comments. Some of these comments include that:

- there are various assumptions that WICS does not understand or seeks explanation on how these reconcile to annual return data.
- there are some assumptions for which WICS does not have visibility of the source of the data used and/or how values are calculated.
- the rationale and justification for various assumptions have not been fully explained. For example, the years Scottish Water has chosen to estimate power costs at PFI sites.

4.6.40. One area that WICS is examining relates to using the Ofwat base models on an operating expenditure-only basis to estimate the predicted operating expenditure from returning PFI assets. However, this analysis remains at an early stage and is an area that WICS will consider further ahead of the draft determination.

## EVIDENCE CASE FOR WEST CENTRAL BIORESOURCES

4.6.41. The draft business plan includes the proposal to build an advanced anaerobic digestion (AAD) facility on the site of the current Daldowie PFI, following the return of the asset from the PFI operator in 2026. This is part of a wider strategy for the treatment, recovery and/or disposal of the biosolids (the byproduct of wastewater treatment) in West Central Scotland, which is expected to cost around £460m across the different sites that would use the new facility.[101]

4.6.42. The commissioning letter for the SRC27 regulatory period explains:

"Ministers recognise that 4 PFI contracts (Seafield, Tay, Moray and Ayrshire) mature in 2027-33 regulatory period. Highland and North East have already returned and Daldowie and Dalmuir return in 2026 with Levenmouth the final PFI due to complete in 2040. Scottish Water has been asked to consider the options and costs for the future operation and funding of these assets. Ministers request that the Commission undertake a full examination of Scottish Water's approach to establishing the options and costs with an overall assumption that these assets should return to public ownership." [102]

4.6.43. In the draft business plan, Scottish Water's investment scenario includes its preferred option of an AAD facility on the existing site of the Daldowie PFI that would be funded from customer charges and the available Government borrowing of £1,030m for 2027-33. Given the magnitude of investment associated with Scottish Water's preferred option, the implication of proceeding with this option is that charges would need to increase and/or

[101] Scottish Water's response to the draft business query number 5 explains that the c.£460m value includes the West Central Bioresource project work at Daldowie for £325 in SRC27, as well as various enabling works at Sludge Treatment sites including Meadowhead, Kinneil Kerse, Galashiels, Dalderse & Cumnock and improvements to the Greater Glasgow Sludge Main. Scottish Water has indicated there have been updates to the business case since the draft business plan submission which will be reflected in the final business plan.

[102] Scottish Government (2024), '2027-33 Commissioning letter', 12 June 2024.

there is less funding available to spend on other areas of the investment programme (e.g. removal of sewerage infrastructure discharges). For example, we note that this investment accounts for around a quarter of Scottish Water's proposed charge increase for 2027-33. As such, Scottish Water needs to demonstrate that its preferred option represents best value for customers, especially for customers in 2027-33 who would meet most of the cost of the investment.

4.6.44. There may be scope to consider further public-private finance arrangements such as the proposed mutual investment model (MIM) that has been examined by the Scottish Futures Trust.[103] Given the magnitude of the investment and the potential scope for adopting new technologies and innovation relating to resource recovery, the use of a MIM could be considered further as one of the possible options for this project.

4.6.45. As such, WICS considers that extending the life of the existing asset could provide further time to consider the different options at the Daldowie site. WICS requests that Scottish Water provides further analysis on the prospect of extending the asset life for these reasons.

## EVIDENCE AND ASSURANCE FOR RETURNING PFI OPTIONS

4.6.46. WICS' final methodology set specific requirements for external assurance of the proposed approach and the robustness of the cost estimates for large projects above £100m and for projects relating to assets returning to Scottish Water upon the PFI contract expiry.[104]

4.6.47. WICS notes that Technical Appendix 3 provides some high-level information for the remaining PFI contracts and the optioneering undertaken by Scottish Water when developing the investment forecasts. However, we do not consider that Scottish Water has provided sufficient evidence to meet the requirements from the final methodology or the Commissioning letter.

4.6.48. WICS welcomes that Scottish Water has provided further information as part of the responses to the draft business plan queries. This consists of the West Central Bioresources Project Investment Appraisal. However, Scottish Water has not provided detailed explanation of the assumptions underpinning the calculation of benefits and costings for other pre-development projects and programmes of work related to potentially returning PFI sites.

[103] The Scottish Futures Trust examined privately financed, privately classified, revenue funded investment models to support the Scottish Government in delivering its National Infrastructure Mission and recommended the option of a mutual investment model (MIM) that met this requirement. See Scottish Futures Trust (2019), 'An options appraisal to examine profit sharing schemes, such as the Welsh Mutual Investment Model, to secure investment for the National Infrastructure Mission and best value for tax payers', April.
[104] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024.

### OPERATING-BASED SOLUTIONS AND PARTNERSHIP APPROACHES

4.6.49. The final methodology recognises that Scottish Water may be able to deliver some drinking water, environmental or other levels of service improvements through alternative operating-based solutions, or through partnership approaches. Such solutions may increase Scottish Water's operating expenditure but bring wider environmental and social benefits such as increased biodiversity.[105] The draft business plan does not propose operating-based solutions, which Scottish Water also confirmed in response to WICS queries on the draft business plan. Scottish Water should evidence that it has fully considered the opportunities for operating-based solutions.

### TRANSFORMATION

4.6.50. WICS considers that some questions remain about transformation spending and its effectiveness. The transformation activity rows are not populated in the draft business plan summary tables. In response to our query, Scottish Water explained that the information is not provided as transformation activity is expected to more than pay for itself within the period. In table 6 of the final business plan and its commentary, we will require further explanation of the expected costs and savings associated with transformation initiatives. We have updated the tables and guidance accordingly.

## 4.7. Adjustments following the final determination

4.7.1. This sub-section covers three areas relating to adjustments following the final determination:

- adjustments to the charging profile from the profile assumed in the final determination;
- Scottish Water's proposals for managing uncertainty; and
- the timing of the delivery plan, which will be used to understand changes during the 2027-33 regulatory period.

### ADJUSTMENTS TO THE CHARGING PROFILE

4.7.2. The methodology requests that Scottish Water set out the circumstances in which it might propose deviating from the charge profile of the final determination.

4.7.3. In Technical Appendix 13 of the draft business plan, Scottish Water explains that "such a proposal would only be in circumstances which are materially different with respect to the financial projections, where we judge it would be of benefit to our customers, both present and future."[106] Scottish Water then explains that examples of such circumstances include low inflation, or another cost-of-living crisis.

[105] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.102.
[106] Scottish Water (2025), 'Scottish Water Draft Business Plan: Technical Appendix 013 – Financial Strength', August, p.9.

4.7.4. WICS expects to see further explanation of the circumstances in which it might choose to deviate. If such a deviation is proposed, we expect Scottish Water to demonstrate a clear understanding of the implications for future charges, investment, levels of service, and the progress towards delivery of the longer-term expectations of the industry such as meeting net zero targets and the transition to increased levels of investment.

## SCOTTISH WATER'S PROPOSAL FOR MANAGING UNCERTAINTY

4.7.5. On page 70 of the draft business plan, Scottish Water identifies three areas as an "area of uncertainty". These are areas that Scottish Water believes could be more effective if WICS were to allow for annual adjustments. These areas are the implementation of RPEs, pension fund uncertainties and a reduction in revenue as a result of the rollout of smart metering for non-household customers. Each of these three items is covered in turn below.

### Implementation of RPEs

4.7.6. Scottish Water suggests two options for implementing RPEs: a "cost-focused" adjustment, where the final determination accounts for RPEs on an ex-ante basis for the period, and a "revenue-focused" adjustment, where RPEs are accounted for through in-period adjustments to the charge profile. WICS does not currently have regulatory powers to make in-period adjustments to charges to account for RPEs unless Scottish Water were to meet the criteria for an interim determination of charges.[107]

### Pension adjustments

4.7.7. Scottish Water proposes that adjustments are made through the 2021-27 regulatory period should its employees' pension funds change from a surplus to a balanced or deficit position. This approach deviates from how WICS has treated this risk in the past given that it has never been subject to in-period adjustments. It also differs from regulatory precedent, whereby the company is responsible for managing the risk of the pension fund moving from a surplus to a deficit on an ongoing basis. We do not understand the rationale for changing the current approach. Furthermore, WICS does not currently have regulatory powers to make in-period adjustments to charges to account for Scottish Water incurring higher pension contributions, unless Scottish Water were to meet the criteria for an interim determination of charges.

### Non-household smart metering revenue adjustment

4.7.8. The draft business plan explains that "whilst we are assuming a c10% fall in consumption from the full roll out of smart metering for non-household customers, we have not modelled any impact on revenue, based on the assumption that wholesale charges will be realigned to ensure they continue to be cost reflective".[108]

[107] For further information see WICS (2015), 'Information note 4: How charge caps could change between Strategic Reviews: interim determinations', August 2015.
[108] Scottish Water (2025), 'SR27 draft business plan – investing in Scotland's future', 12 June 2025, p.70.

4.7.9. WICS has concerns with the proposed approach. In our view, if smart metering reduces consumption such that operating costs and/or capital costs are reduced, then non-household charges will remain cost reflective. While there may be timing differences, with the potential for revenues to reduce before any reduction in costs is achieved, WICS considers that consumption reductions because of smart metering should not be adjusted for.

## TIMING OF THE DELIVERY PLAN

4.7.10. The final methodology set out that WICS "will require Scottish Water to produce a delivery plan showing how it proposes to meet the requirements of the final determination and an annual delivery plan refresh before each financial year capturing, in a clear and transparent manner, the changes to the investment baseline each year as endorsed at the revised SGIG (investment prioritisation) process. This revised baseline will then form the basis of our monitoring through the information we receive from Scottish Water in the annual return."[109]

4.7.11. Scottish Water explains on page 3 of Table 5 commentary that the SRC27 baseline would be based on the Annual Return 2026-27 submission.

4.7.12. WICS' expectation is that the SRC27 baseline will be established by the delivery plan for 2027-28. We require Scottish Water to finalise that delivery plan in February 2027 to set the baseline before the regulatory period begins on 1 April 2027.

4.7.13. WICS will issue further guidance on the expectations for the delivery plan in 2026 drawing on the information requested in the business plan data tables.

[109] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.126.

# 5. Financial assumptions

## 5.1. Overview of the chapter

5.1.1. As noted in the methodology, in SRC27 WICS will continue to apply a cash-based approach to setting charge caps for Scottish Water. This approach involves balancing the cash inflows and outflows for the period, ensuring Scottish Water has the funding and financing available to deliver the Objectives of Scottish Ministers, while ensuring customers receive value for money from the service they receive. This chapter assesses the assumptions driving these cash inflows and outflows.

5.1.2. The chapter covers:

- the financial model;
- modelling assumptions; and
- scenario and sensitivity analysis.

## 5.2. The Financial Model

5.2.1. WICS and Scottish Water have worked closely to jointly develop a financial model for the 2027-33 regulatory period. The aim has been to produce a financial model that allows WICS to perform its regulatory duties while enabling Scottish Water to meet its internal and regulatory reporting requirements. Developing and using a joint financial model is an example of EBP&R in practice since it ensures that any differences in calculated charge paths are due to different input assumptions, rather than the underlying model mechanics. This promotes transparency and enables the engagement between both organisations to focus on the material differences in input assumptions, as set out in the following sub-section.

5.2.2. The financial model has been constructed to enable the cash-based approach to setting charges. The main inputs are used to calculate the cash inflows (primarily customer charges and borrowing) and operating outflows (primarily operating and PFI expenditure, interest, and taxation) to calculate the funding available for investment.

5.2.3. Scottish Water used the joint financial model in the development of its draft business plan. We welcome that Scottish Water shared the financial model used to produce the financial forecasts in the business plan with us ahead of its draft business plan submission, allowing us to ask questions on some of its updated assumptions.

## 5.3. Modelling assumptions

5.3.1. In Technical Appendix 13, Scottish Water provides its assumptions used in the financial model for the 2027-33 regulatory period. As explained above, we consider that the assumptions from the SRC21 period are a reference point for the 2027-33 period, and that it is for Scottish Water to evidence where changes to these assumptions are appropriate (e.g. for assumed productivity improvements).

5.3.2. WICS welcomes the commitment from Scottish Water's long-term strategy to do as much as it can to minimise the funding it needs from customers.[110] In this regard, we consider that Scottish Water should provide further evidence if it uses the same forecasts in its final business plan in the following two areas:

- operating expenditure; and
- non-household revenues.

5.3.3. While WICS has questions on the evidence underpinning some of the remaining assumptions, we focus on the two assumptions above given that they account for most of the difference in the financial forecasts of WICS and Scottish Water at this stage. For completeness, the assumptions for SRC21 are shown in appendix 1 for ease of reference.

## MODELLING OF OPERATING EXPENDITURE

5.3.4. Our feedback on Scottish Water's approach to forecasting operating expenditure is covered in detail in sub-section 4.6. Based on this feedback, we have applied different modelling assumptions compared to Scottish Water's reference scenario in the following areas:

- the efficiency challenge;
- adjustments to operating costs; and
- the expiry of PFI contracts.

5.3.5. These are covered in turn below.

### Operating expenditure efficiency challenge

5.3.6. As explained in paragraph 4.6.34, Scottish Water applies an effective efficiency challenge of 0.66% per annum to operating expenditure to reflect the scope for productivity improvements over the 2021-27 regulatory period. However, we note that Scottish Water has not applied an efficiency challenge for the remainder of the 2021-27 regulatory period.

5.3.7. As set out in paragraph 4.6.35, WICS' starting point is a productivity efficiency improvement of 1% per annum from SRC21 should continue to apply unless Scottish Water provides compelling evidence to justify a lower figure. We consider that Scottish Water should continue to assume the efficiency challenge from the final determination for SRC21. As a result, we assume an efficiency challenge of:

- 1% per annum for the remainder of the 2021-27 regulatory period in line with the WICS final determination for SRC21; and

[110] Scottish Water (2025), 'Our sustainable future together: long-term strategy', May, p.52.

- 1% per annum through the 2027-33 regulatory period, which equates to an effective efficiency challenge of 0.8% after excluding operating expenditure outside of Scottish Water's control.

5.3.8. We have also broadened the scope of operating expenditure subject to the efficiency challenge to include expenditure associated with cloud computing from 2024-25 onwards.[111]

### Adjustments to operating costs

5.3.9. As explained in sub-section 4.6, WICS questions whether the proposed additions to operating expenditure in 2025-26 and 2026-27 represent efficient expenditure. For this reason, we have not applied Scottish Water's adjustments to operating costs in these years.

### Expiry of PFI contracts

5.3.10. Two PFI contracts will expire in 2026, and four more will expire during the 2027-33 regulatory period. Our final methodology explains that we expect the reduction in PFI fees to be larger than the increase in operating expenditure, due to several factors such as the fees covering the financing costs of the PFI company, which Scottish Water would no longer incur.[112]

5.3.11. Scottish Water assumes that the operating expenditure arising from the return of the PFI sites upon contract expiry is consistent with existing PFI fees less a percentage ranging from 12% for Daldowie and 72% for Tay.

5.3.12. For modelling purposes, WICS instead applies a uniform reduction to PFI fees at all PFI sites to recognise the underlying uncertainty in the operating expenditure that Scottish Water will incur at the PFI sites, and WICS' questions and comments on PFI return in sub-section 4.6. WICS sets this assumption at 50%, broadly consistent with the average reduction across all sites as modelled by Scottish Water.

## MODELLING OF NON-HOUSEHOLD REVENUES

5.3.13. In the financial model, non-household revenues are driven by the annual growth rate in the number of non-household properties and the change in consumption by non-household properties. WICS' assumptions for these model inputs are explained below.

### Non-household growth rate

5.3.14. Scottish Water proposes an annual non-household growth rate of 0.2% whereas WICS calculates the average non-household property growth rate between 2018-19 and 2023-24 to be 0.8%. We calculate a growth rate of 0.8% based on the average growth rate in

[111] For the 2024-25 report year, a change was made to the regulatory accounting of cloud expenditure. Such expenditure moved from being accounted as capital expenditure to operating expenditure. Scottish Water has modelled cloud expenditure separately. Taking this approach means that cloud expenditure is not subject to an efficiency challenge
[112] WICS (2024), 'Strategic Review of Charges 2027-33: Final Methodology', December, p.101.

connected non-household properties as Scottish Water has reported in the Annual Return to WICS over the period 2018-19 to 2023-24. This data is provided below.

*Table 7: Historic non-household growth rate (calculated using lines P2.20, P2.63, P2.118, P2.146 of the P-tables)*

| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | Average |
|---|---|---|---|---|---|---|---|
| **NHH growth rate (P-tables)** | -0.05% | 0.69% | 0.47% | 1.16% | 2.06% | 0.51% | 0.81% |

5.3.15. Scottish Water's analysis suggests that recent growth has been elevated due to the identification and subsequent connection of gap sites and that it expects this to end.

5.3.16. However, we consider it unlikely that the number of properties connected as former gap sites will fall to zero immediately. Instead, we expect the number of former gap site properties to gradually reduce in line with the principle of diminishing returns. As a result, we have modelled a non-household growth rate of 0.5% – the mid-point between WICS and Scottish Water's calculated growth rate. This is in line with the rate of growth associated with the identification of gap sites reducing by half, recognising that there will inevitably be some reduction in new properties identified.

5.3.17. For the final two years of the 2021-27 regulatory period, WICS assumes a non-household rate of 0.75%. This is in line with the assumption of the final determination for SRC21.

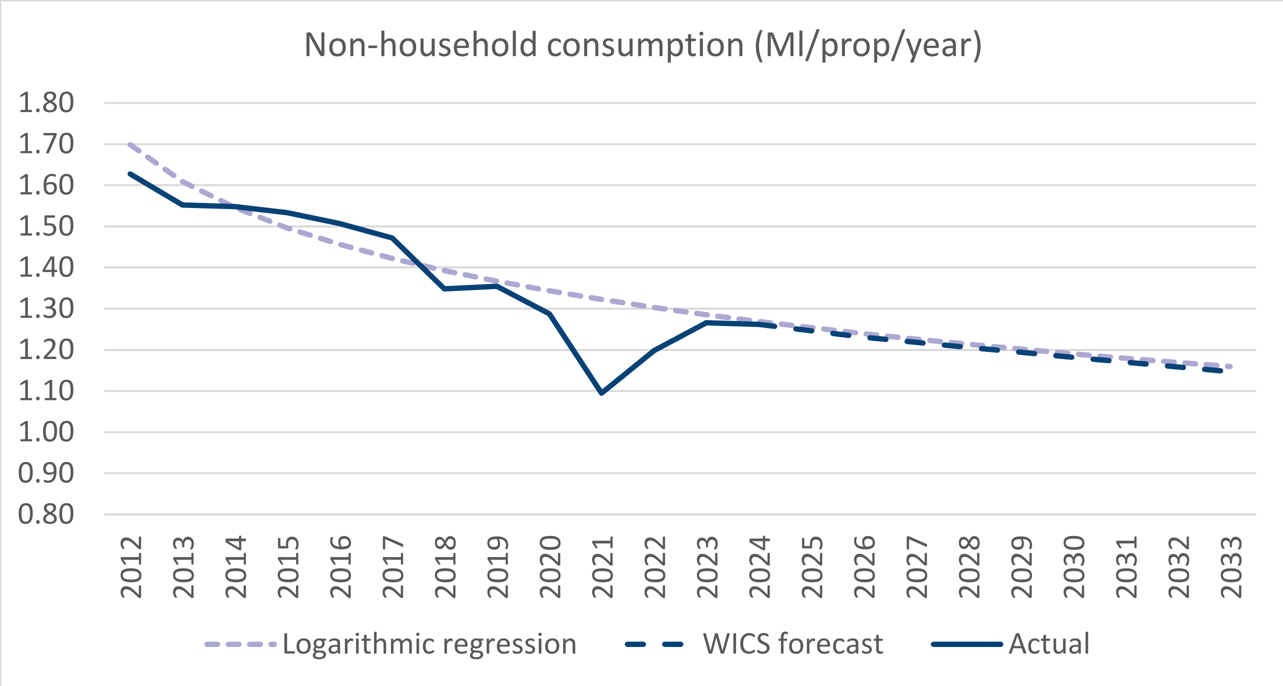
## Non-household consumption

5.3.18. Scottish Water proposes that non-household consumption will decline by 1.5% per annum over the 2027-33 regulatory period. Scottish Water suggests that this is consistent with the average decline over the last 5 years.

5.3.19. WICS' calculation considers the change in non-household consumption per property since 2011. Recognising the temporary reduction in consumption as a result of the COVID-19 pandemic, our analysis suggests that sustained reductions are unlikely to continue at the same rate as has been the case in the last 10-15 years. As a result, we currently assume a 1.0% annual reduction in consumption through the SRC27 period.

5.3.20. Figure 18 shows the profile of non-household consumption we have used to forecast future reductions. WICS considers that the reductions in average consumption per property follows a logarithmic profile, with the reductions gradually flattening out, excluding the years 2020-22 which were impacted by the Covid-19 pandemic. We consider that this profile is broadly consistent with consumption reducing from 1.5% per year on average to 1% per year on average over the 2027-33 period.

*Figure 18: Actual and forecast non-household consumption per property*




## 5.4. Scenario and sensitivity analysis

5.4.1. Recognising the longer-term challenges facing the industry, WICS' approach in SRC21 involved a gradual transition in charges to increased levels of investment over time. This led to our final determination for SRC21 of setting a charge cap of CPI + 2% on average for each year of the 2021-27 regulatory period, which is consistent with a cumulative charge cap of CPI + 12.6% for the period. We also explained that given the need to continue transitioning to increased investment, charges will need to increase by a similar amount in real terms of 1.5% to 2% per annum (equivalent to 9-13% in total over 2027-33) over the 2027-33 regulatory period.

5.4.2. Continuing this approach, WICS has used the financial model and updated assumptions to forecast the amount of cash available for investment in SRC27 based on a scenario of CPI + 2% per annum.[113]

5.4.3. Based on the assumptions above and in appendix 1, continuing with a current charge cap of CPI + 2% over the 2027-33 regulatory period could allow for investment of up to £7.9 billion in 2023-24 prices. This investment is around £400m lower than the investment proposed in Scottish Water's draft business plan, suggesting that investment would need to be prioritised further and/or additional efficiencies would be required under if the long-term charge cap of CPI + 2% per annum is adopted over the 2027-33 regulatory period.

[113] The updated assumptions include those described in section 5.3 and those in appendix 1.

5.4.4. A summary of this scenario is shown in the table below.

*Table 8 – Detailed summary of WICS CPI+2% scenario in 2023-24 prices*

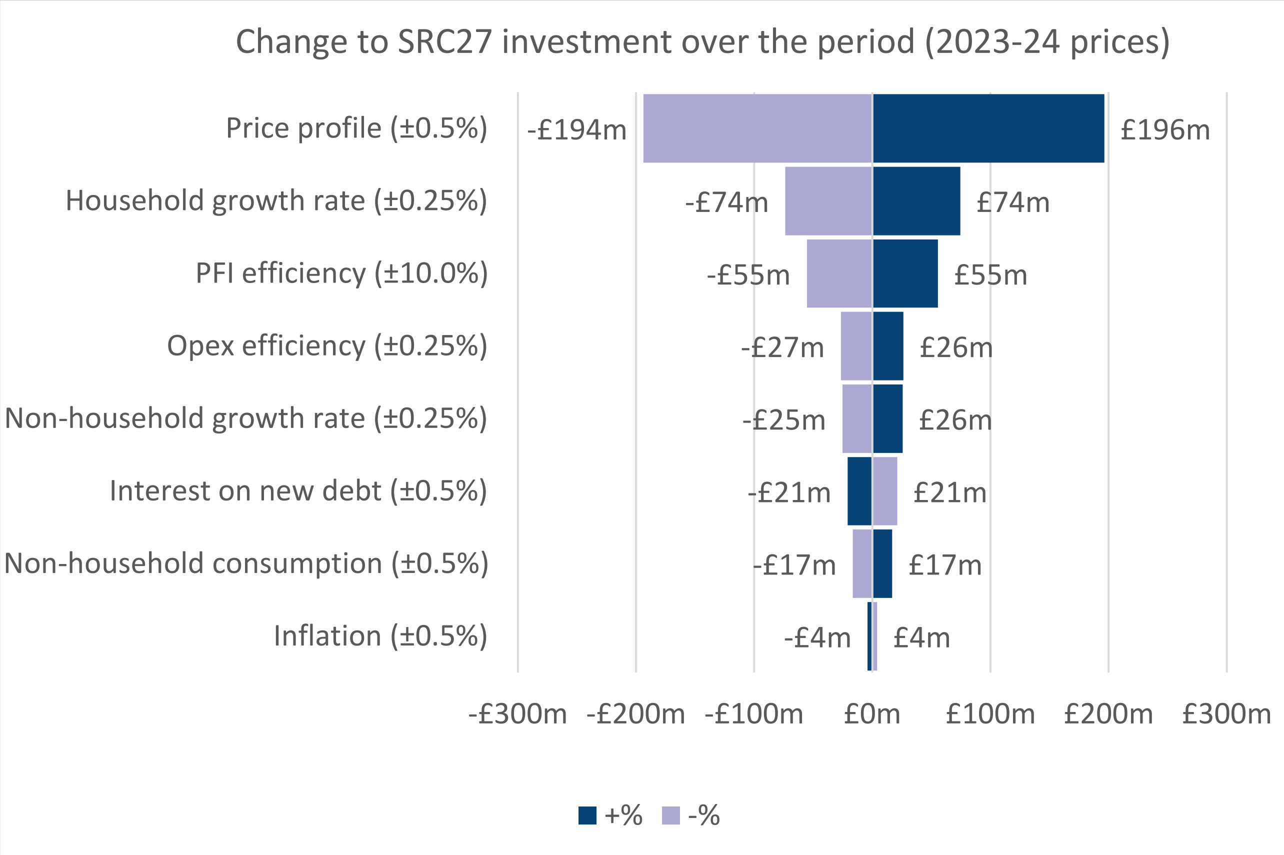
| | *2027-28* | *2028-29* | *2029-30* | *2030-31* | *2031-32* | *2032-33* | *SRC27 total* |
|---|---|---|---|---|---|---|---|
| Cost inflation | 1.90% | 2.00% | 2.00% | 2.00% | 2.00% | 2.00% | |
| Inflation index to 2023-24 prices | 1.100 | 1.122 | 1.145 | 1.167 | 1.191 | 1.215 | |
| Household revenue | 1,335.7 | 1,372.9 | 1,413.8 | 1,455.9 | 1,499.3 | 1,544.0 | 8,621.5 |
| Non-household revenue | 469.7 | 478.8 | 489.0 | 499.5 | 510.2 | 521.1 | 2,968.4 |
| Other revenue | 16.3 | 16.6 | 17.0 | 17.3 | 17.6 | 18.0 | 102.8 |
| **Total revenue** | **1,821.8** | **1,868.3** | **1,919.8** | **1,972.7** | **2,027.1** | **2,083.1** | **11,692.7** |
| Infrastructure charges income | 17.3 | 17.2 | 17.2 | 17.2 | 17.2 | 17.2 | 103.4 |
| Disposal proceeds | 2.5 | 2.5 | 2.5 | 2.5 | 2.5 | 2.5 | 15.0 |
| **Total** | **1,841.5** | **1,888.0** | **1,939.5** | **1,992.4** | **2,046.8** | **2,102.8** | **11,811.1** |
| Net new borrowing | 156.0 | 153.0 | 150.0 | 147.0 | 144.2 | 141.3 | 891.6 |
| **Total cash inflows** | **1,997.6** | **2,041.0** | **2,089.5** | **2,139.5** | **2,191.0** | **2,244.1** | **12,702.6** |
| Operating costs | (520.3) | (517.2) | (536.1) | (544.8) | (546.7) | (549.6) | (3,214.7) |
| PFI costs | (115.8) | (116.7) | (73.9) | (50.8) | (40.9) | (28.8) | (426.8) |
| Net interest | (159.2) | (163.3) | (165.8) | (167.9) | (171.4) | (173.4) | (1,000.9) |
| Taxation | 0.0 | 0.0 | 0.0 | (1.1) | (4.2) | (7.5) | (12.8) |
| **Total operating expenditure** | **(795.2)** | **(797.2)** | **(775.7)** | **(764.5)** | **(763.3)** | **(759.3)** | **(4,655.2)** |
| RCCs | (35.5) | (35.5) | (35.5) | (35.5) | (35.5) | (35.5) | (212.9) |
| Completion | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| **Gross SRC27 investment (incl. repairs)** | **(1,193.5)** | **(1,214.3)** | **(1,284.3)** | **(1,345.4)** | **(1,398.2)** | **(1,455.4)** | **(7,891.1)** |
| Grants and contributions | 6.0 | 6.0 | 6.0 | 6.0 | 6.0 | 6.0 | 35.9 |
| **Net SRC27 investment (incl. repairs)** | **(1,187.5)** | **(1,208.3)** | **(1,278.3)** | **(1,339.4)** | **(1,392.2)** | **(1,449.4)** | **(7,855.2)** |
| Change in working capital | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Change in cash | (20.7) | (0.0) | 0.0 | 0.0 | 0.0 | 0.0 | (20.7) |

5.4.5. Recognising that these forecasts are based on assumptions, WICS has performed sensitivity analysis to test the materiality of each assumption. The assumptions tested are as follows:

- Charging profile
- Household and non-household property growth rates
- Non-household consumption reduction
- Inflation
- Interest rates
- Opex and PFI efficiency

5.4.6. Figure 19 below shows how changes to individual assumptions impact on the level of investment over the 2027-33 regulatory period, using WICS' scenario of CPI + 2% per annum as the central estimate.

*Figure 19: Sensitivity analysis around WICS' CPI + 2% scenario*



# 6. Methodology clarifications

## 6.1. Overview of the chapter

6.1.1. Following our review of Scottish Water's draft business plan, we provide further explanation as to what some of our final methodology expectations mean in practice.

6.1.2. This chapter covers the most material of these areas, including:

- delivery plan and baseline for 2027-28;
- testing alignment on the Ministerial Objectives;
- supporting information for investment;
- asset health measure;
- improvement plans;
- balance between repair, refurbishment and replacement;
- additional charge path;
- the financial model;
- operating-based solutions; and
- changes to the business plan data tables and guidance.

## 6.2. Delivery plan and baseline for 2027-28

6.2.1. The final methodology set out that WICS "will require Scottish Water to produce a delivery plan showing how it proposes to meet the requirements of the final determination and an annual delivery plan refresh before each financial year capturing, in a clear and transparent manner, the changes to the investment baseline each year as endorsed at the revised SGIG [investment prioritisation] process. This revised baseline will then form the basis of our monitoring through the information we receive from Scottish Water in the annual return".[114]

6.2.2. Scottish Water explains on page 3 of Table 5 commentary that the SRC27 baseline would be based on the Annual Return 2026-27 submission.

6.2.3. WICS' expectation is that the SRC27 baseline will be established by the delivery plan for 2027-28. We require Scottish Water to finalise that delivery plan in February 2027 to set the baseline before the regulatory period begins on 1 April 2027.

6.2.4. WICS will issue further guidance on the expectations for the delivery plan in 2026 drawing on the information requested in the business plan data tables.

## 6.3. Testing alignment on the Ministerial Objectives

[114] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.126.

6.3.1. It is essential for Scottish Water to ensure there is a shared view among stakeholders that Scottish Water's investment plan will meet the Ministerial Objectives. [115] From WICS' perspective, this includes explaining whether the proposed investment aligns with the expectations of both DWQR and SEPA in relation to the Ministerial Objectives that apply to them. We expect the final business plan to clearly set out how this alignment has been tested, and how Scottish Water has ensured that the plan has the support of customers and its regulators. If there are areas of misalignment, we expect Scottish Water to provide further information on these areas to enable WICS to make a determination, e.g. the standard information required on the investment programme if related to investment.

6.3.2. Ahead of the draft determination, WICS will seek feedback from SEPA and DWQR on whether they agree that the proposed investment programme is consistent with the elements of the MOs that apply to them. WICS is exploring the timing of when SEPA and DWQR could provide such feedback.

## 6.4. Supporting information for investment

6.4.1. In sub-section 4.5, WICS sets out four overall comments on the standard information requested as part of the investment case:

- Scottish Water has not sufficiently explained the assumptions for costing and outputs for those investments pre-Gate 50;
- Scottish Water has not provided an investment case for all investment that meets the current criteria for projects and programmes of work post Gate 50 in the final methodology;
- Scottish Water has not provided the additional information requested for large projects above £100m and the projects related to the return of PFI assets upon expiry of the PFI contracts; and
- The information that Scottish Water has provided in project investment appraisals (PIAs) does not cover all of the standard information requested as part of the investment case.

6.4.2. Based on the observations of the information submitted by Scottish Water in the draft business plan set out in the investment cases part of sub-section 4.5, WICS issues the following clarifications.

6.4.3. WICS expects Scottish Water to clearly explain the rationale for the investment need as well as the assumptions for the benefits and costing of investment pre-Gate 50 within the final business plan submission. This includes explaining the methodology used for calculating the estimates as well as the underpinning assumptions. Example programmes include the UID programme and the AR3 programme for returning PFI assets where Scottish Water should

[115] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.18.

explain how the programme costs have been calculated, e.g. if based on unit costs, then WICS would want to understand what those unit costs are and how they have been derived.

6.4.4. WICS must ensure that it has the information required to review Scottish Water's investment proposals and set a baseline. As such, we request that Scottish Water provides a list of the projects and programmes that it expects will meet the final methodology criteria by the time of the final business plan by 29 September 2025.

6.4.5. For the investments that have passed Gate 50, WICS expects Scottish Water to provide the investment cases as per the threshold requirements in the final methodology. In its responses to the draft business plan queries, Scottish Water has applied further thresholds to reduce the number of cases it proposes to submit. We do not agree with the application of the criterion for at least 50% of the total project/programme investment expenditure to be planned for SRC27, and so expect any investment meeting the existing final methodology criteria to be covered by an investment case.

6.4.6. WICS expects Scottish Water to provide the data in Table 5 of the final business plan as requested by the final methodology and business plan table guidance with any identified projects that have a total project value of at least £6m reported in a separate line. We note that this appears not to have been the case in the draft business plan submission. For example, in its response to query 20 on page 7 Scottish Water notes that one of the projects included in programme "Under£6M-837 (Reference) Scenario A" "To reduce flood risk to customers impacted by repeat high consequence internal sewer flooding where not disproportionately expensive" is project for internal sewer flooding with investment code 5363110205[116] with a total SRC27 value of £6.2m.

## 6.5. Asset health measure

6.5.1. The final methodology requires Scottish Water to provide a measure (or measures) of asset condition across its asset base and, as far as possible, translate the impact of maintenance activities on asset condition into tangible consequences that customers will understand.[117]

6.5.2. Scottish Water should take ownership of developing the asset health measure as the asset owner with the necessary expertise. Recognising the significant maintenance expenditure proposed for the 2027-33 regulatory period, WICS requires that the business plan include a tangible measure with forecasts for the 2027-33 regulatory period. Scottish Water should also demonstrate further that it has fully met the requirement from the final methodology

[116] Scottish Water's query response provides the project name which is the property address with internal sewer flooding problems. For privacy purposes, the project name has been substituted for the associated investment code provided in Table X, which has been shared with WICS for information alongside the draft business plan submission.
[117] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.119.

to translate the impact of its maintenance activities into tangible consequences that customers will understand.

6.5.3. As part of this evidence, Scottish Water could explain how its maintenance activities over 2021-27 have impacted the asset base and customer outcomes. Such an assessment could help Scottish Water justify maintenance requirements for the 2027-33 regulatory period, especially for asset categories where Scottish Water proposes maintenance investment in line with current levels.

## 6.6. Improvement plans

6.6.1. The final methodology requires Scottish Water to provide an improvement plan to address gaps in data and knowledge of the condition of its assets in its business plan.[118] Scottish Water has provided several improvement plans as outlined in paragraph 4.5.32.

6.6.2. However, WICS expects the improvement plan to be more detailed, covering the expected milestones and the due dates for making the proposed improvement activities that Scottish Water could be held accountable for meeting. We also request that for each improvement activity Scottish Water indicates when the information would be reported to WICS with reference to the annual return submission in a specific year. This will allow us to assess whether Scottish Water is making appropriate progress in improving the gaps in its data and knowledge of the condition of its assets.

6.6.3. WICS appreciates that Scottish Water has provided additional plans for improving its data and analytic capabilities to enable better investment decision-making. These have been outlined in Technical Appendix 8 (Annex A, section A4) and the commentaries for Table 2 (sub-section 3.4), Table 3a (section 8) and Table 5 (section 5). As per paragraph 6.6.2, we would welcome further details around milestones and due dates for these improvements.

## 6.7. Balance between repair, refurbishment and replacement

6.7.1. WICS expects the final business plan to explain how Scottish Water has sought to achieve an appropriate balance between repair and refurbishment and asset replacement investment in 2027-33, and how Scottish Water has factored the increase in repair and refurbishment investment in its top-down analysis of long-term replacement costs considering some of this investment will extend the life of assets and thus defer the need for full end-of-life replacement.

## 6.8. Additional charge path

6.8.1. In line with expectations of Scottish Ministers, last year WICS requested that Scottish Water provide alternative charge paths for services in SRC27.

[118] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.119.

6.8.2. WICS required Scottish Water to set out a range of possible charge paths that demonstrate the extent of progress towards the Ministerial Objectives and the levels of risk of service failure associated with different levels of investment in the short, medium, and long-term. We specified that these charge paths be referred to as 'Reference Scenario A' and Scenario B and Scenario C. We also provided guidance on completing the business plan data tables for these scenarios

6.8.3. Scottish Water should examine whether it is feasible to deliver the Ministerial Objectives with a charge path of CPI + 2% and, if so, include it as one of the charge path scenarios (either replacing one of or in addition to the three charge paths in the draft business plan). This recognises that CPI + 2% is consistent with the long-term price path set out in SRC21.

6.8.4. If Scottish Water decides to provide this new scenario in addition to its existing scenarios, it should update the business plan tables accordingly to accommodate it.

## 6.9. Financial model

6.9.1. WICS requests that Scottish Water formally submit the financial model for each price scenario alongside the final business plan. To support this, Scottish Water should provide a commentary document which explains the assumptions behind the inputs to the financial model.

## 6.10. Operating-based solutions

6.10.1. The final methodology recognises that Scottish Water may be able to deliver some drinking water, environmental or other levels of service improvements through alternative operating-based solutions, or through partnership approaches. Such solutions may increase Scottish Water's operating expenditure but bring wider environmental and social benefits such as increased biodiversity.[119]

6.10.2. Scottish Water should evidence that it has fully considered the opportunities for operating-based solutions.

6.10.3. Scottish Water should explain its specific plans for operating-based solutions in its final business plan and indicate where each of these solutions are included, if at all, in the final business plan data tables.

## 6.11. Changes to business plan data tables and guidance

### TABLE 1 OUTCOMES

6.11.1. Table 1 will be updated to include new columns for the following:

- Reporting year basis (calendar or financial year);

[119] WICS (2024), 'Strategic Review of Charges 2027-2033: Final Methodology', 12 December 2024, p.102.

- Base year indication;
- 2024-25 (actual) value;
- 2025-26 forecast; and
- 2026-27 forecast.

6.11.2. The guidance will be updated to specify that Scottish Water should set out its current performance on the outcome measures and explain and evidence its forecasts for 2026-27, especially where Scottish Water forecasts a deterioration in performance.

6.11.3. The updated guidance will also require Scottish Water to indicate in the commentary when each forecast was set, to provide an audit trail and to help stakeholders to understand how the final business plan forecasts relate to those elsewhere.

6.11.4. Outcome definitions with changes agreed before the draft business plan submission will be updated.

## TABLE 3A AND 3B MAINTENANCE EXPENDITURE AND ASSET HEALTH

6.11.5. Tables 3a and 3b will be updated to require Scottish Water to report repair and refurbishment expenditure separately given the split between repair and refurbishment is material in the financial modelling.

6.11.6. The templates will be updated to standardise the functional activity categories between Table 3a and Table 3b. This change was proposed by Scottish Water on page 2 of the Table 3a commentary.

6.11.7. Table 3a will be updated to include replacement expenditure of lead communication pipes in the column 32 (Cumulative surplus/deficit (£m) in SRC27) total formulas in lines 3a.31 and 3a.85.

## TABLE 5 SRC27 PROJECTS PROGRAMMES

6.11.8. Table 5 will be updated to require Scottish Water to provide the percentage allocation of expenditure to repair and refurbishment separately. Similarly, Table 5 will be updated to split out repair and refurbishment interventions.

6.11.9. Table 5 will be updated to include an additional column for Scottish Water to indicate the primary Ministerial Objective that each investment line is contributing to.

6.11.10. Table 5 will be updated to require Scottish Water to indicate the primary supply chain Delivery Vehicle it will use to deliver each investment line.

6.11.11. The drop-down menu for column 5.126 will be updated to three storm overflow project types to reflect the changes in Ofwat’s final determination model. In addition, columns 132 to 135 will be removed.

6.11.12. The updated guidance will note that information on four enhancement areas is requested as candidates for benchmarking in blocks K to N of Table 5, covering: phosphorus removal; sanitary permits; storm overflows; and water resources. The updated guidance will specify that if a project covers more than one enhancement area such as phosphorus removal and addressing sanitary permits, Scottish Water should allocate the proposed expenditure to these different areas and report the allocated expenditure and corresponding cost drivers in separate lines.

## TABLE 6 TRANSFORMATION INITIATIVES

6.11.13. The updated guidance will require Scottish Water to indicate in the commentary how much of the initial expenditure for each transformation initiative brings about operating expenditure savings.

## TABLE 7 OTHER COSTS AND ASSUMPTIONS

6.11.14. Table 7 will be updated to remove “transformation” from the line titles for lines 7.4a and 7.4b, to rename line 7.5 as “Efficiency - catch-up” and to remove line 7.7 "Efficiency - from Enhancement, Growth and Transformation".

6.11.15. The updated guidance will require Scottish Water to indicate in the commentary how much of the catch-up and frontier shift efficiency result from transformation projects.

6.11.16. Table 7 will be updated to include non-household properties in addition to supply points.

## TABLE 8 SUMMARY COSTS

6.11.17. Table 8 will be updated to require Scottish Water to report repair and refurbishment expenditure separately.

6.11.18. Table 8 will be updated to remove the summary cost lines for transformation activities.

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