

Annual Return 2012/13

Overview

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**Scottish
Water**

Always serving Scotland

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1. Executive Summary

This overview document reports on Scottish Water's performance and activities in 2012/13, the third year of the 2010-15 regulatory period. 2012/13 proved to be another very successful year for us with performance exceeding our plans across most activities with many measures reaching new heights. Successful implementation of PACE, one of our major change initiatives is contributing to continued improvement in performance.

2012/13 Dashboard

Table 1 shows the 2012/13 year-end position for the key regulatory outputs set out in the Regulatory Contract.

Annual Dashboard – 2012/13			
Measure to be reported	Actual 2012/13	Delivery Plan Target 2012/13 ¹	Current RAG Status
Output Delivery			
Investment – completion of Q&SII/IIIa (Number of remaining projects requiring regulatory sign-off)	9	12	G
Investment – Delivery of Q&SIIIb Outputs (OMD Measure)	205	192	G
Levels of Service			
Customer Service – OPA (rolling four quarters)	368	338	G
Leakage (MI/d) (rolling four quarters)	575	635	G
Water into Supply (MI/d) (rolling four quarters)	1,840		
Expenditure			
Total Capital Expenditure (£m)	487	494	
Operating and PFI Costs (£m)	499	512	G
Financial Strength			
Cash Interest Cover	3.6	3.1	G
Funds from operations to net debt	13.2%	11.4%	G
Gearing	48%	49%	G
Net new borrowing (£m)	100 ²	100	G
Impact of External Factors: Net 'logging' position	See page 26		

Performance Status
Performance below target and not expected to achieve year end target
Performance below target, but expected to achieve year end target
Performance above target or expected to achieve year end target.

Table 1 – Annual Dashboard 2012/13

¹ As per our March 2012 Delivery Plan Update, with the exception of net new borrowing (see note 2).

² Our March 2013 Delivery Plan assumes a total of £535m borrowing will be available from the Scottish Government for the 2010-15 regulatory period. Net new borrowing for Scottish Water in 2012/13 was £100m in line with our latest plan.

Overall Performance Assessment (OPA)

In 2012/13 our OPA performance increased to 368 and exceeded our Delivery Plan target of 338.

Our 2012/13 OPA score represents a 13 point improvement compared with the 355 OPA points scored in 2011/12.

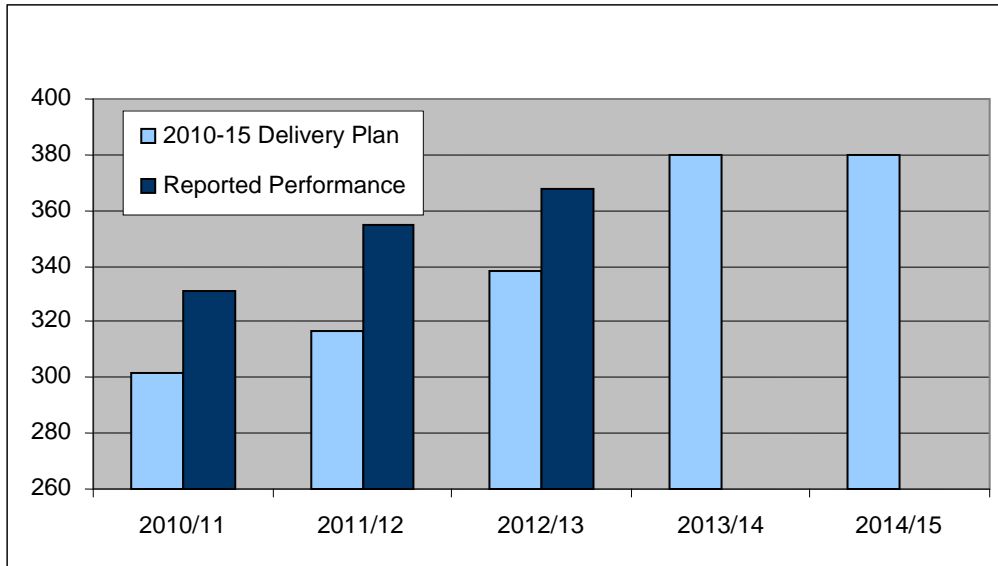


Figure 1 – OPA performance

Leakage

Our MLE reported leakage for 2012/13 is 575 MI/d which is a 54 MI/d reduction on our reported MLE leakage of 629 MI/d for 2011/12, successfully out-performing our 2012/13 Delivery Plan target of 635 MI/d. Scottish Water has also achieved the agreed Economic Level of Leakage (ELL) of 600 MI/d one year ahead of regulatory expectation. Table 1.2 below details the leakage reduction we have achieved in recent years.

Description (ML/d)	2008/09	2009/10	2010/11	2011/12	2012/13
Regulatory Reported leakage (OPA)	802	704	699	629	575
Leakage Target (OPA)	840	730	720	670	635
MLE adjusted leakage	816	738	699	629	575

Table 1.2

Customer Satisfaction

We have been monitoring customer satisfaction since 2010 through a postal survey. Over 50,000 customers have taken part to provide satisfaction tracking and insightful comments about their experience. This valuable information is being used to drive service improvements that are most valued by our customers.

Customer satisfaction has increased again this year and reached a score of 88.3%. This has been achieved through a determined focus on listening to customers, combined with the delivery of a number of considerable improvement projects in our main contact areas, such as those on Sewer Flooding, Repeat Customer Contact and Avoidable Complaints. We continue to focus on customer satisfaction and improve the customer experience further for all our customers.

Compliance

Overall Water Quality Compliance

For the calendar year 2012, overall compliance with water quality standards continued to be of a very high standard with 99.88% of all water quality tests conducted in our sampling programme complying with quality standards.

For OPA purposes, water quality is assessed using the mean zonal compliance of a basket of six parameters. For these parameters performance in 2012 was 99.17% an improvement from 99.02% in 2011.

Wastewater Compliance

Wastewater Treatment Works compliance at 31 March 2013 is reported as 2 failing sites against a Delivery Plan target of 18. This performance, which has been agreed with SEPA, represents an improvement from the 2011/12 performance of 10 failing sites and reduction in environmental impact arising from our operations.

We continue to see significant improvement regarding the number of Environmental Pollution Incidents (EPIs). In 2010/11 there were 824 incidents, which reduced to 500 in 2011/12, and now stands at 331 for 2012/13.

We are utilising improved data and intelligence from the field and we have been able to better allocate resources to avoid EPIs occurring and we continue to work to reduce further the number of incidents.

There are now 33 fewer Unsatisfactory Intermittent Discharges on our sewerage network as a result of our investment programme during 2012/13.

Scotland had 83 bathing waters officially designated under the EU Bathing Water Directive for the 2012 Season, 70 of which could be directly impacted by Scottish Water Assets. Two bathing waters failed for the season (Heads of Ayr and Stonehaven). Scottish Water does not have any assets in the vicinity of Heads of Ayr. Although the failed bathing water at Stonehaven was attributed to periods of persistent and intermittently heavy rainfall, a pollution incident related to a sewer collapse on the Scottish Water network was identified as a possible contributory factor. Scottish Water performance overall remained good.

Capital Programme delivery

During 2012/13 investment totalled £487m, comprising £461m on Q&SIIIb projects and £26m on completion projects.

At the end of March 2013, the Overall Measure of Delivery (OMD) score, which provides a high-level measure of progress in implementing the Q&S3b enhancement investment programme stands at 205 points, 13 points ahead of the baseline target agreed with the Commission.

At the end of the 2012/13 year, we have reduced the overall number of completion projects remaining to be signed off to 9 which is ahead of our delivery plan target of 12. All 9 remaining projects are planned to be completed in 2013/14.

Wholesale Service

Scottish Water provides water and sewerage services to Licensed Providers who in turn provide services to non-household premises. The number of Licensed Providers operational in the market has increased over the period, and with further applicants in the pipeline the number is expected to continue to grow in the coming year. During 2012/13, one Licensed Provider, Satec, exited the market in the period and their customers were reallocated to other Licensed Providers by the Central Market Agency.

In 2012/13, a number of changes were made to market processes which enabled Licensed Providers to select accredited entities to undertake defined work on new connections and temporary disconnections and assisted Licensed Providers in tracking connections applications through a portal facility.

A number of changes were made to Trade Effluent processes, including the launch by Scottish Water of a portal facility enabling Licensed Providers and dischargers to review results of sampling undertaken by Scottish Water.

The Vacancy Charging Admin Scheme was also introduced in the period and Scottish Water considers this initiative, combined with the pre-existing Vacancy Incentive Scheme, to have had a beneficial impact on the market.

Scottish Water is continuing to work with the Commission and market participants in the context of the Commission's Data Alignment project and has developed a Data Assurance Framework for assuring the data for which it is responsible.

A number of fora were established over the year in relation to the development of the competitive market in England. Scottish Water participated in the roadmap Group and the Programme Implementation Board supporting the High Level Group.

Section 29e

During 2012-13 we received two further preliminary Section 29e enquiries from Licence Providers, bringing the number of enquiries received to seven since 2008. Our asset and cost assessment established that none of the circumstances in either case would result in a Section 29e agreement.

Research and Innovation

Innovation is key to sustaining high performance and delivering ever higher service standards. During 2012/13, research and innovation have helped us to deliver improved value, through the installation of an energy recovery system on our water mains at Denny and enhanced performance for our customers, through the use of wastewater pump blockage detection systems. Looking ahead we will further improve our services to customers by focussing our innovation activity to deliver transformational research in three areas:

- Enhancing water quality compliance
- Energy self generation on all wastewater treatment works
- Sustainable rural communities

Alongside this, we are also pursuing single topic issues such as leakage, sewer flooding and carbon reduction through the UKWIR programme.

We continue to find ways to further improve our service and create efficiencies in running the business, either through in-house work or in collaboration with a variety of partners.

Financials

The surplus before tax in the year for Scottish Water was £68.3 million, £5.7 million lower than in 2011/12 (£74.0 million). The regulated surplus before tax of £67.8 million was £6.0 million lower than 2011/12 (£73.8 million), but £6 million greater than our Delivery Plan target (2012 update) of £62 million.

Revenue

Regulated revenue for the year totalled £1,053.0 million (2012 - £1,045.8 million).

Revenue from services supplied to household customers increased by only £5.3 million or 0.7% to £750.9 million reflecting the increase in connected properties and the tariff freeze effective from 1 April 2012.

The benefit to household customers of freezing household charges at a time when applicable RPI was 5.4% was c£40 million.

Revenue from wholesale services supplied to Licensed Providers increased by £2.0 million or 0.7% to £296.7 million. Revenue from other sales decreased by £0.1 million to £5.4 million.

Total costs

Total costs of £830.8 million were £15.6 million higher than in 2011/12.

Operating costs of £499.3 million were £12.4 million higher than 2011/12. Within these costs, regulated operating costs of £349.3 million were 2.7% or £9.1 million higher than in 2011/12 and PFI costs were £3.3 million higher at £150.0 million.

From a regulatory perspective, like-for-like costs actually reduced in real terms by £1.3m or 0.6%. Compared with 2011/12, higher bad debt provision charges of £6.3 million, £7.0 million of inflation, an increase in local authority rates of £3.4 million, increased energy prices of £3.0 million and new operating costs associated with new capital investment of £3.0m were absorbed. These increases were partly offset by lower VR and other restructure costs of £12.0 million.

Depreciation, including infrastructure depreciation, increased by £4.6 million to £333.6 million, primarily as a consequence of the capital investment programme. The gain on sale from asset disposals was £1.4 million higher than in 2011/12 at £2.1 million.

Finance costs

As at 31 March 2013, the weighted average interest cost of the outstanding long-term debt was 5.03%, (2012 – 5.15%). Net interest payable during the year was £154.4 million, £2.4 million lower than in 2011/12.

During the year, net debt increased by £95.5 million to £3,023.8 million (being loans of £3,269.3 million less cash balances of £245.5 million). The increase was driven by a £100.0 million increase in borrowing from the Scottish Government and a £4.5 million increase in cash balances.

Borrowing Limit

Scottish Ministers set Scottish Water's (consolidated) maximum net new borrowing limit at £100.0 million for 2012/13. Actual net new borrowings in 2012/13 were £100.0 million.

Board Changes

In February 2013 Mr Douglas Millican was appointed Chief Executive Officer of Scottish Water, following the death of Mr Richard Ackroyd. The position of Finance Director, is currently awaiting an appointment.

In conjunction with the above changes Mr Peter Farrer was appointed Chief Operating Officer.

On 31st March 2013 Mr Pat Kelly left the Board at the end of his period of appointment, not being eligible for a further re-appointment, resulting in a second Non Executive Board vacancy.

Governance of the Annual Return

We have retained the methodologies and processes used for producing the detailed information in Scottish Water's Annual Return to the Water Industry Commission developed over previous years. Black and Veatch have again audited the information reported in the Annual Return as part of the normal assurance to the Scottish Water Board and consequently the Commission.

This approach has ensured that this submission continues to be based on sound processes and assumptions.

2. Key Outputs and Service Delivery

2.1 Service Outputs and Performance

Overall Performance Assessment (OPA)

In 2012/13 our OPA performance increased to 368 and exceeded our Delivery Plan target of 338.

This is the third year where we have been measured against the new “17 indicator” OPA, which replaced the “12 indicator” measure that was used until 2009/10. Our 2012/13 OPA score represents a 13 point improvement compared with the 355 OPA points scored in 2011/12.

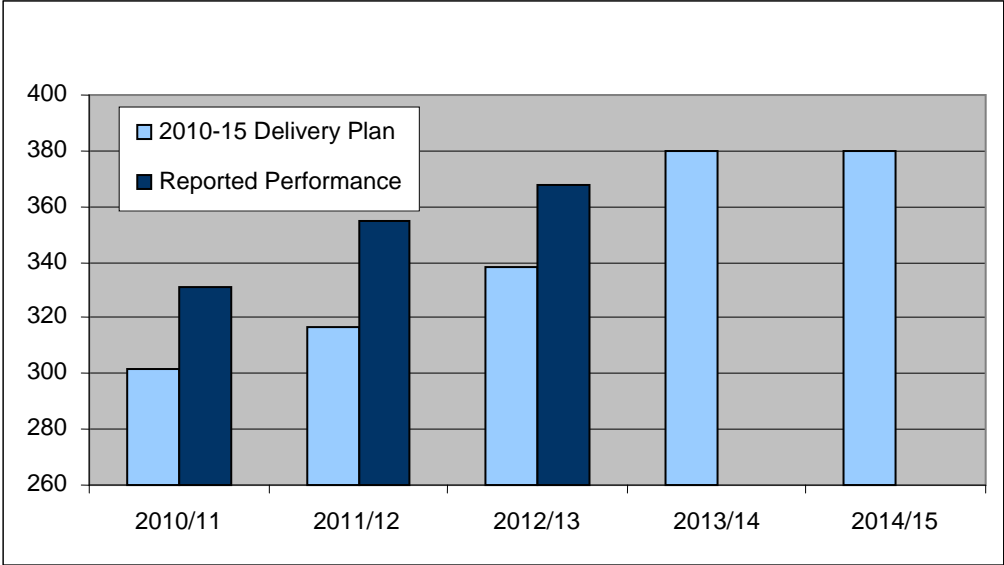


Figure 2.1 – OPA performance

Significant Improvements

The areas in which we made the most **significant** improvement in 2012/13, are:

- EPI Sewage category 1&2 improved from 17.9 to 23.7 points (+5.9 points);
- Drinking water quality improved from 22.4 to 26.6 points (+4.1 points);
- Interruptions to Supply improved from 29.1 to 32.4 points (+3.3 points);
- Sewer Flooding incidents due to other causes (IFOC) improved from 34.8 to 37.2 points (+2.4 points);
- EPI Sewage category 3 improved from 7.3 to 9.3 points (+1.9 points), and
- Low Pressure improved from 35.1 to 37.0 points (+1.8 points).

Table 2.2 below compares our 2011/12 and 2012/13 performance for each of the 17 indicators: In summary:

- 5 items continued to score full points;
- 1 item increased to maximum OPA points, an additional 1.3 OPA points;
- 7 items showed increased performance, securing 19.6 additional OPA points;
- 1 item maintained its score, and
- 3 items slipped back – which reduced OPA by 7.7 points.

Indicator	AR12 OPA	AR13 OPA	AR12 OPA score	AR13 OPA score	Change
% of properties subject to inadequate water pressure	0.03%	0.01%	35.1	37.0	1.8
Connected properties experiencing unplanned interruptions	0.84%	0.57%	29.1	32.4	3.3
Hosepipe restrictions	0	0	12.5	12.5	0.0
Security of Supply absolute performance	71	74	7.5	7.5	0.0
Security of Supply performance against target	-54.35%	-57.45%	12.5	12.5	0.0
% of water samples that comply with parameters	99.02%	99.17%	22.4	26.6	4.1
Leakage	-6.48%	-10.40%	12.5	12.5	0.0
Water Service (sub-total)			131.7	142.1	10.4
% properties suffering sewer flooding incidents caused by overloading	0.0017%	0.0036%	24.9	23.6	-1.2
% properties suffering sewer flooding incidents caused by other causes	0.0066%	0.0049%	34.8	37.2	2.4
Sewer flooding (at risk)	0.01083%	0.01257%	12.5	12.4	-0.1
Sewerage Service (sub-total)			72.2	73.3	1.1
Customer Contact (Total of complaints and telephone performance)	18.2	18.4	18.2	18.4	0.2
Assessed customer service	8	9	37.5	37.5	0.0
Customer Service (sub-total)			55.7	55.9	0.2
Category 1 & 2 sewage EPIs	18	9	17.9	23.7	5.9
Category 3 sewage EPIs	481	322	7.3	9.3	1.9
Category 1 & 2 water EPIs	1	0	11.2	12.5	1.3
Sewage sludge disposal	0%	0%	12.5	12.5	0.0
% pe served by non-compliant sewerage treatment works	0.39%	1.09%	46.5	40.0	-6.4
Environmental Performance Service (sub-total)			95.4	98.0	2.6
Total			354.9	368.1	13.2

Table 2.2 - OPA Performance

Each of the OPA elements and their scores are discussed below.

Percentage of Properties Subject to Inadequate Water Pressure

A total of 938 properties were removed from the low pressure register over the year, reducing the total number from 1,542 (2011/12 reported value) to 604. 406 of these properties are within 10.5m of the bottom water level of the supplying service reservoir which, under OPA rules, are not included within OPA. Overall the improvement of water pressure for customers has increased our OPA performance by 1.8 points to 37.0 in 2012/13.

Connected Properties Experiencing Unplanned Interruptions

Table 2.3 shows the change in the number of properties that experienced unplanned interruptions compared to last year. While the loss of supply to our customers is regrettable the reduction of almost 5,000 customers experiencing supply losses that lasted more than 6 hours is reflective of our drive to maintain supplies. A total of 14,717 weighted properties, or 0.57% of total population, received a supply interruption greater than 6 hours.

In this reporting year three large incidents caused over 5,816 properties to lose supply for more than six hours.

In August 2012, 1,100 properties were affected by an incident on Allison Street in Glasgow with supply being restored in 11 and a half hours.

In September 2012, 412 properties were affected by an incident in Auchtermuchty, Fife with supply being restored in 7 and a half hours.

In October 2012, 4,304 properties were affected by an incident on Dongola Road in Ayr with supply being restored within 12 hours.

	2011/12	2012/13
Properties interrupted for 6 to 12 hours	14,083	11,267
Properties interrupted for 12 to 24 hours	3,484	1,301
Properties interrupted for more than 24 hours	188	212
Total number of properties interrupted for more than 6 hours	17,755	12,780
Total number of properties interrupted for more than 12 hours	3,672	1,513
Total 'weighted' properties interrupted for more than 6 hours	21,803	14,717

Table 2.3 - Unplanned Interruptions to Supply

The number of properties experiencing unplanned interruptions, as a percentage of total properties, decreased during from 0.84% to 0.57% in 2012/13. This reduction improved our OPA performance by 3.3 points to 32.4 points.

Hosepipe Restrictions

We have maintained unconstrained supplies to customers and have not required any hosepipe restrictions since Scottish Water was formed in 2002.

Security of Supply Index (SOSI)

a) SOSI absolute performance.

Absolute performance is measured on total SOSI score. Our score improved in 2012/13, rising from 71 to 74, retaining our 50-89 SOSI banding and giving us 7.5 OPA points.

b) SOSI performance against target.

We are also measured in terms of our SOSI performance against our annual target. For 2012/13 our target was 51 points. We scored 74 SOSI points in 2012/13 and exceeded our target. Our OPA score for this measure of SOSI remained at the maximum 12.5 points.

Percentage of Water Samples that Comply with Parameters

Water Quality, as measured by mean zonal compliance of 6 parameters, increased from 99.02% to 99.17% in 2012. This increases our OPA component score by 4.1 points, to 26.6 points. Our water quality performance is discussed in more detail in Section 2.2.

Leakage

Our MLE reported leakage for 2012/13 is 575 MI/d which is a 54 MI/d reduction on our reported MLE leakage of 629 MI/d for 2011/12, successfully out-performing our 2012/13 Delivery Plan target of 635 MI/d. Scottish Water has also achieved the agreed Economic Level of Leakage (ELL) of 600 MI/d one year ahead of regulatory expectation.

Our leakage performance is discussed more fully on page 24.

Number of Incidents of Sewer Flooding Caused by Overloading of Main Sewers

In 2012/13 there were 89 Incidents of flooding from overloaded mains sewers that regrettably caused internal flooding of customers' properties. Disappointingly this was an increase from 42 incidents for 2011/12 and was associated with the wet weather throughout last summer. Our OPA performance decreased by 1.2 points to 23.6 points in 2012/13.

Number of Incidents of Sewer Flooding from Other Causes on Main Sewers

In 2012/13 there were 122 incidents of flooding from other causes on main sewers, such as choked sewers, that also caused internal flooding of customers' properties. This was a reduction of 41 incidents from 2011/12. Our OPA performance increased by 2.4 points to 37.2 points in 2012/13.

Sewer Flooding (properties at risk)

The number of properties on the "At-risk of flooding from overloaded sewers" register is 395 in 2012/13. This gives a score of 12.4 OPA points.

	2012/13
At risk of flooding twice in ten years	167
At risk of flooding once (but less than twice) in ten years	228
Total number of properties at risk of flooding at least once in ten years	395

Table 2.4 - Properties at Risk of Flooding from Sewers

The existence of properties on the At-Risk register reflects capacity issues on our network of sewers which cannot be readily and quickly improved. While the increase in 2012/13 is disappointing, it was due to additional premises being identified as a result of the wet weather experienced during 2012-13 as well as the time required to deliver a number of projects aimed at alleviating the network problems for some customers. We will continue to work to reduce the number of customers that live with the risk of sewer flooding.

Customer Contact

The Customer Contact measure consolidates 4 sub-elements as described below.

a) Percentage Written Complaints Responded to within 10 days

Our performance for 2012/13 was 100% with all written complaints responded to within 10 days.

b) Percentage Telephone lines busy

In 2012-13 a total of 4,114 lines were reported as busy, which meant the customer could not make contact with Scottish Water when they called, a significant increase from 593 in

2011/12. This decreased performance from 99.87% to 99.83% over the year. BT experienced an exchange fault in June, which resulted in our system becoming non-operational for a period of 4 hours. This resulted in 4,078 instances where all lines were reported as busy. Excluding this event, there were only 36 other instances during the year.

c) Percentage Telephone calls abandoned

During 2012/13 the total number of abandoned calls, where the customer had to hang up before the call was answered, decreased from 5,335 to 2,191. This increased our performance in this measure from 98.83% to 99.38%.

d) Customer Service Survey

Our telephone customer survey scored 4.69 out of a maximum of 5.00 for 2012/13, an increase from 4.56 in 2011/12.

Assessed Customer Service

Our score decreased from 8 to 9 points in 2012/13 and retained maximum 37.5 OPA points. With the dissolution of Waterwatch in August 2011, Scottish Water has produced an Assessed Customer Service Report for 2012/13.

Environmental Pollution Incidents (EPIs)

All EPIs shown below have been agreed with SEPA.

a) Wastewater Category 1&2 EPIs

We reported a decrease in Category 1&2 incidents in 2012/13 from 18 to 9. This increased our OPA performance by 5.9 points.

b) Wastewater Category 3

We reported a decrease in the number of Category 3 incidents in 2012/12, from 481 to 322. This increased our OPA performance by 1.9 points.

c) Water Category 1&2

In 2011/12 there was 1 water pollution incident, but we had no water pollution incidents in 2012/13. This increases our OPA performance by 1.3 points and back to maximum points of 12.5.

Sewage Sludge Disposal

All sewage sludge from Scottish Water is disposed of through approved routes in compliance with all relevant legislation.

Percentage of Population Equivalent Served by Non-compliant Sewage Treatment Works

The compliance of Scottish Water's waste water treatment works decreased significantly in 2012/13. In 2012/13 a maximum of 1.09% of the connected population equivalent was served by a non-compliant works, this decrease is due to a failing sample at Ardoch WwTW which has a population equivalent of 57,753. This number is subject to confirmation by SEPA. Our OPA performance decreased by 6.4 points to 40.0 points in 2012/13.

2.2 Drinking Water Service

Compliance - Water Quality Compliance

Overall Water Quality Compliance

Overall compliance with water quality standards continues to be of a very high standard for the 2012 calendar year, with 99.88% of all water quality tests conducted in our sampling programme complying with quality standards (2011: 99.86%; 2010: 99.86%; 2009: 99.83%).

Microbiological Quality

Microbiological standards apply to water leaving treatment works, in service reservoirs and supplied at customers' taps.

a) water leaving treatment works

In 2012, 27,305 samples were taken for faecal and 27,306 for total Coliform analysis. Compliance with the faecal coliform standard was 99.99% and with the total coliform standard was 99.88%.

b) water in service reservoirs

In 2012, 52,230 samples were taken for faecal and total Coliform analysis. Compliance with the faecal coliform standard was 99.99% and the total coliform standard was 99.79%.

c) water at customers' taps

In 2012, 14,214 samples were taken for faecal coliforms and 14,215 for total coliform analysis. Compliance with the faecal coliform standard was 99.99% and the total coliform standard was 99.57%.

Microbiological compliance remains very high despite a slight dip in coliform compliance in 2012 at customer's taps (99.57%) compared with 2011 (99.58%), however there has been an overall improving trend in microbiological compliance, as can be seen in table 2.5.

The following summary table highlights performance in microbiological water quality from 2009 to 2012 based on regulation samples:

		2009 fails	2009 compliance	2010 fails	2010 compliance	2011 fails	2011 compliance	2012 fails	2012 compliance
Treatment Works	Coliforms	30	99.90%	44	99.85%	49	99.83%	33	99.88%
	Faecal Coliforms	6	99.98%	8	99.97%	5	99.98%	3	99.99%
Service Reservoirs	Coliforms	138	99.74%	107	99.79%	122	99.77%	109	99.79%
	Faecal Coliforms	12	99.98%	9	99.98%	13	99.97%	7	99.99%
Customer Taps	Coliforms	66	99.54%	69	99.52%	60	99.58%	61	99.57%
	Faecal Coliforms	4	99.97%	2	99.99%	2	99.99%	2	99.99%

Table 2.5 - Microbiological quality of water

Chemical Sampling

Physical and chemical quality standards apply to water supplied at customers' taps. 118,328 tests were carried out at customers' taps for all parameters during 2012. Of these 99.87% were compliant with regulatory standards (99.84% in 2011).

The following summary table highlights the performance of the key chemical parameters for 2009 to 2012.

	2009 fails	2009 compliance	2010 fails	2010 compliance	2011 fails	2011 compliance	2012 fails	2012 compliance
THM Total	89	94.59%	59	96.39%	42	97.33%	42	97.30%
Iron	49	99.06%	32	99.38%	46	99.09%	34	99.34%
Colour	12	99.77%	7	99.87%	3	99.94%	0	100%
Manganese	24	99.54%	31	99.40%	28	99.45%	32	99.38%
Aluminium	7	99.87%	12	99.77%	11	99.78%	2	99.96%

Table 2.6 - Chemical Quality of Water

THM

Trihalomethanes (THM) are by-products of the disinfection stage that is used in some of our water treatment processes. These result from the reaction between chlorine and any organic material which is not removed in the treatment process. THMs are traditionally associated with upland sources and we are investigating the reasons why we are finding increased levels of organic materials in some of our water sources. During 2013 we will continue to work hard to reduce THM precursor levels by further optimising and automating processes, and where required progressing with new initiatives including aeration of treated water or looking at chloramination.

Manganese

Overall compliance has decreased slightly to 99.38% from 99.45% in 2011 (28 failures). During 2012, we continued with our extensive network improvement programme which is due for completion in 2015. Through this programme, improvements in water quality and customer contacts have been seen, particularly in the Muirdykes zone where work was substantially complete by the end of 2012. In addition to the programmed network improvement work we have also instigated a flushing programme, initially undertaking work in small zones, but also assessing hot spot areas within larger zones. It is anticipated that this will have a positive impact on manganese compliance in 2013 and beyond.

For OPA purposes, water quality is now assessed using the mean zonal compliance of a basket of six parameters. For these parameters performance in 2012 was 99.17%, an improvement from 99.02% in 2011.

Abstraction Licensing

This is the fourth year we have submitted our annual Water Resource data return to SEPA. This covers 378 measurement points covering abstraction and impoundment activities authorised under the Controlled Activities Regulations (CAR) in approximately 300 Water Use Licences. It is a legal requirement of the Water Use Licence to provide SEPA with our abstraction and compensation data to enable SEPA to monitor our compliance against the conditions of the licence – typically maximum abstraction limits from our sources and minimum compensation flow requirements from our reservoirs. In addition 2012 was the first year that SW performance was assessed under SEPA's Compliance Assessment Scheme (CAS) for Water Resources

We continue to work with SEPA to analyse the data and discuss final CAS assessments in the coming months through a joint SW-SEPA water resources Task and Finish Group to address a number of issues.

Water Resource Strategic Studies

In SR06 we undertook water resource strategic studies in 78 Water Resource Zones to understand the impact of new standards associated with the Water Framework Directive on our abstractions and impoundments. Any changes to operational regimes were also implemented where this was required and agreed with SEPA. By March 2013 we had gained Regulatory sign-off for all 78 WRZ's.

During 2010-2015 we studied a further 26 supply systems and as a result:

- 10 systems required no action
- 3 systems resulted in either a reduced abstraction or increased compensation and associated licence variation
- 13 systems are being promoted for investment for resolution or further study.

In addition, studies were undertaken to assess the feasibility of improving fish passage at 10 impoundments. Options have been proposed for these sites and promoted for the next investment period for further assessment and potential construction.

Sustainable Land Management

Scottish Water is taking an innovative approach to delivering high quality drinking water by seeking to protect the quality of raw waters in 6 catchments across Scotland. In 2012 we introduced an incentive scheme for farmers and land managers in these 6 catchments, whereby payments will be made to those who take actions to protect drinking water sources to levels beyond that normally required by the General Binding Rules. To date, the incentive scheme has been actively promoted in 2 of the 6 catchments, with a total of 80 applicants. In 2013-14 we intend to continue this work and promote the scheme in all 6 catchments. We continue to gather data in these catchments and have a rolling programme of sampling and analysis to characterise catchments and identify hot-spots of diffuse pollution that impact on sources of drinking water.

Building on the experience gained through this work, we have also undertaken a number of catchment assessments for raw waters in other areas of Scotland, to identify sources of diffuse pollution and are embedding sustainable land management further into our business-as-usual approach for the protection and improvement of drinking water quality. We are also considering catchment management as a solution to future investment needs and where possible to mitigate risks before the need arises.

Since November 2012, the SLM team has undertaken 10 catchment assessments to determine how land management can help improve water quality. This work is based on river and catchment walks, which identify breaches in General Binding Rules (GBRs) for land management and poor land management practices. Following each visit a report is produced which summarises the findings and gives recommendations which will lead to improvements in source water quality. Catchments where these assessments have taken place in the last 12 months include Orkney, Craignure, Lochenkit, Colonsay, Gigha and Teangue.

We plan to embed sustainable land management further into our business-as-usual approach to improving drinking water quality. We are also incorporating catchment management as a potential solution into our future investment priorities for 2015 -2021.

2.3 Wastewater Service

Compliance - Wastewater Serviceability

Wastewater Treatment

Wastewater Treatment Works compliance figures at 31 March 2013 are reported as 2 failing sites against a Delivery Plan target of 18. This performance, which has been agreed with SEPA, is an improvement on the 10 failing works in 2011/12.

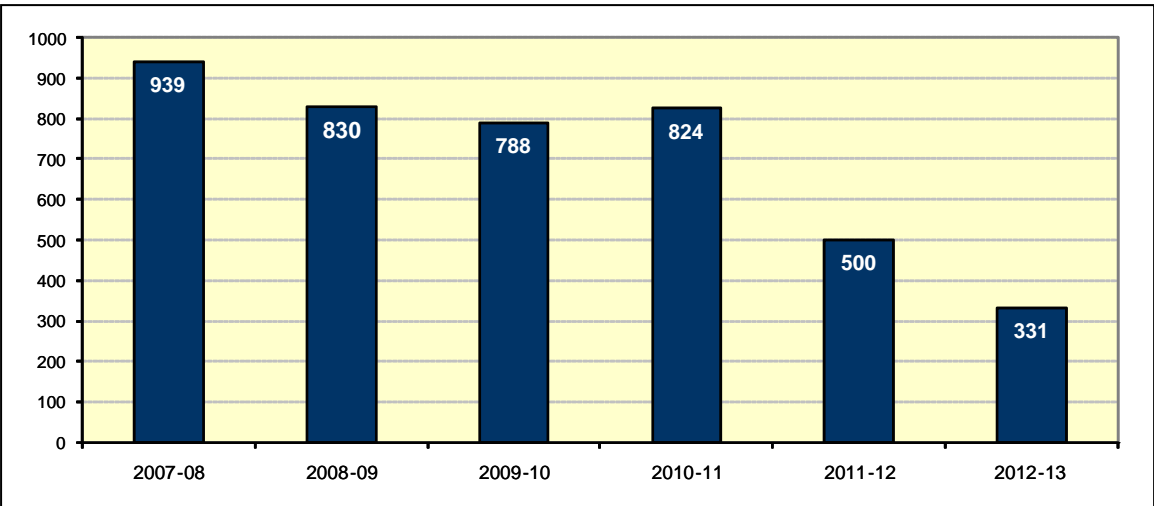
Scottish Water continues to focus on improving processes and alignment of operational and investment activities. This is supported and driven by a functional structure, which ensures the appropriate focus and continuous improvement in compliance.

Bathing Waters

Scotland had 83 bathing waters officially designated under the EU Bathing Water Directive for the 2012 Season, 70 of which could be directly impacted by Scottish Water Assets. Two bathing waters failed for the season (Heads of Ayr and Stonehaven). Scottish Water does not have any assets in the vicinity of Heads of Ayr. Although the failed bathing water at Stonehaven was attributed to periods of persistent and intermittently heavy rainfall, a pollution incident related to a sewer collapse on the Scottish Water network was identified as a possible contributory factor. Scottish Water performance overall remained good.

Pollution Incidents

There has been continual improvement in our performance with regards to Environmental Pollution Incidents (EPI), demonstrated below.



During 2012/13 as agreed with SEPA there were a total of 331 EPI events, another stepped improvement beyond that achieved last year. A total of 9 category 1&2 incidents and 322 category 3 wastewater incidents were reported during the year. No category 1&2 incidents were reported at water assets in 2012/13 (1 in 2011/12). There is close liaison between Scottish Water and SEPA with weekly teleconference calls to agree EPI numbers

We are utilising improved data and intelligence from the field and we have been able to better allocate resources to avoid EPIs occurring and we continue to work to further reduce the number of incidents.

Unsatisfactory Intermittent Discharges (UIDs)

During 2012/13, Scottish Water has delivered a further 12 Q&S3a UID outputs. A total of 300 UIDs have now been improved, leaving only 6 to be delivered under this programme. The outputs comprise physical improvement, operational interventions, and those where modelling has confirmed no need for physical intervention. A further 21 UIDs have been resolved in 2012/13 through the Q&S3b programme bringing the total improved under this programme to 59.

Glasgow

Scottish Water is committed to improving the Greater Glasgow wastewater system to deliver a modern, sustainable drainage system. In February 2013, we launched our strategy to deliver the key objectives published in our Glasgow Wastewater Strategy. This strategy has taken 4 years develop and will help us to play our part in improving services to customers in Glasgow, reducing flooding and improving the environment of the River Clyde and its tributaries.

We have worked closely with external stakeholders throughout this process. We have undertaken extensive and complex modelling of the five drainage area catchments to produce robust evidence and analysis on which to base decision making to ensure strategy-led investment.

The investment planned will support the Scottish Government's objectives to comply with the Urban Waste Water Directive and to achieve Water Framework Directive 'Good' Ecological Status or 'Good' Ecological Potential for the River Clyde and its tributaries. It will also help Greater Glasgow continue to grow and prosper, supporting delivery of economic growth and benefiting the area's economy and environment for generations to come.

Commonwealth Games 2014

In 2012/13 we made a number of improvements to our water and wastewater infrastructure ahead of the Commonwealth Games and all remaining projects will be complete by December 2013 to ensure no disruption to Glasgow and its environs leading up to the games. We continue to support a successful Glasgow Commonwealth Games in 2014 and we will ensure that our investment addresses needs in the catchment surrounding the games. Glasgow City Council has introduced an April 2014 construction embargo. We have adopted an earlier target for completion of works of December 2013 to reduce the risk that projects are not completed in sufficient time.

2.4 Capital Programme Delivery

The capital programme is monitored quarterly by the Outputs Monitoring Group, and the associated Working Group, with progress reported to Scottish Ministers.

Investment

During 2011/12 investment totalled £487m, comprising £461m on Q&SIIIb projects and £26m on completion (Q&S2 and Q&S3a) projects.

Completion Programme (Q&S2 and Q&S3a)

At the start of the 2010-15 regulatory period a total of 313 Q&S2 and Q&S3a projects were still to be completed. A further 20 projects have been completed or removed over the year, reducing the number of projects still outstanding to 9, 3 projects better than our Delivery Plan target of only 12 projects remaining at this stage.

	Projects remaining at end of 2009/10	Projects remaining at end of 2010/11	Projects remaining at end of 2011/12	Projects remaining at end of 2012/13
Q&S2	62	16	6	1
Q&S3a	251	46	23	8
Total	313	62	29	9

Table 2.7 – Completion projects remaining

Q&S3b

2010/11 saw the introduction of the Overall Measure of Delivery (OMD) which provides a high-level measure of progress in implementing the Q&S3b enhancement investment programme financed in the 2010-15 period. At the end of March 2013, the OMD score stands at 205 points. This is 13 points ahead of the baseline agreed with the Commission.

As shown in table 2.8 below we have consistently out-performed against our quarterly OMD target throughout 2012/13.

OMD Measure	Q1	Q2	Q3	Q4
Target	147	159	177	192
Actual	168	178	187	205

Table 2.8 - OMD

Our Delivery Plan forecast the delivery of outputs across 26 programmes by the end of 2012/13. At the end of 2012/13 we had delivered outputs on 30 programmes. 17 of the programmes had delivered more outputs than forecast, while 4 programmes are in line with forecast. 6 programmes have been completed on or ahead of time, while only 3 delivered fewer outputs than forecast. Table 2.9 shows the output sign-off position of each of the 33 programmes.

OMGWG Grouping	Quarterly monitored programme areas	Q4 2012/13 Target	Q4 2012/13 Actual	Q4 2012/13 Position
Drinking Water Quality	Km of mains rehabilitated to improve drinking water quality	1,320	1,938	Ahead of target
	Number of WTW receiving improved disinfection control	12	20	Ahead of target
	Number of WTW improved to meet quality standards	2	2	On Target
	Number of sites with reduced risk from cryptosporidium	7	12	Ahead of target
	Number of zones with reduced lead levels	41	49	Ahead of target
	Number of DMA subject to investigations	143	143	Complete
	Type A Raw water supplies provided with treatment	0	1	Ahead of target
	Number of raw water sample points installed	0	86	Ahead of target
	Number of lead comms pipes removed	0	0	No outputs forecast
	Number of backflow prevention devices installed	126	249	Ahead of target
	Number of sites covered by drinking water safety plans	174	196	Complete
	Number of tanker fill points installed	14	14	Complete
	Number of sites with increased security	346	375	Ahead of target
	Number of WRZs receiving company standard for security of supply (under 7 stage)	0	4	Ahead of target
	Number of WRZs receiving company standard for security of supply	1	1	Complete
Environmental Protection	Improvements to the Wastewater Network (properties)	15	15	Complete
	Number of properties with environmental improvements to support the 2014 Commonwealth Games	0	32	Ahead of target
	Number of UIDs improved (under 7 stage)	27	46	Ahead of target
	Number of UIDs improved (excluding 7 stage)	8	13	Ahead of target
	Number of dual manhole systems upgraded	3	2	Behind Target
	Number of WWTW discharges improved to meet new licence requirements	54	36	Behind Target
	Number of WWTW upgraded to meet existing licence requirements	19	19	On target
	Number of WWPS upgraded to comply with existing licence requirements	16	16	On target
	Number of WWTW brought into compliance with licence non-sanitary requirements	20	24	Ahead of target
	Number of wastewater network assets made compliant with licence requirements	78	78	On target
	Number of surface water systems upgraded	0	0	No outputs forecast
	Number of environmental studies undertaken	112	92	Behind Target
Malodour	Number of sites where malodour is reduced	2	3	Ahead of target
Customer Service	Properties removed from low pressure register	1,704	2,343	Ahead of target
	Properties removed from low pressure register (Exclusions under 1980 Act)	108	515	Ahead of target
Flood Management	Number of assets protected from flood risk	16	17	Ahead of target
	Number of models to support the Flooding Bill	0	0	No outputs forecast
	Number of flooding asset risk assessments	269	294	Complete

Table 2.9 Q&S3b Output sign-off

The OMG was aware that two programme areas, WWTW discharges improved to meet new licenses and the number of environmental studies undertaken, would not achieve the year-end targets. Discussions are ongoing with SEPA in relation to sign-offs in the Dual Manhole systems programme.

2.5 Wholesale Service

Scottish Water provides water and sewerage services to Licensed Providers who in turn provide services to non-household premises. The number of Licensed Providers operational in the market has increased over the period, and with further applicants in the pipeline the number is expected to continue to grow in the coming year. During 2012/13, one Licensed Provider, Satec, exited the market in the period and their customers were reallocated to other Licensed Providers by the Central Market Agency.

All new Licensed Providers were offered a one-day training session on the practical and operational aspects of inter-working with Scottish Water after signing the Wholesale Services Agreement.

In 2012/13, a number of changes were made to market processes which enabled Licensed Providers to select accredited entities to undertake defined work on new connections and temporary disconnections and assisted Licensed Providers in tracking connections applications through a portal facility.

A number of changes were made to Trade Effluent processes, including the launch by Scottish Water of a portal facility enabling Licensed Providers and dischargers to review results of sampling undertaken by Scottish Water.

The Vacancy Charging Admin Scheme was also introduced in the period and Scottish Water considers this initiative, combined with the pre-existing Vacancy Incentive Scheme, to have had a beneficial impact on the market.

Scottish Water is continuing to work with the Commission and market participants in the context of the Commission's Data Alignment project and has developed a Data Assurance Framework for assuring the data for which it is responsible.

A number of fora were established over the year in relation to the development of the competitive market in England. Scottish Water participated in the roadmap Group and the Programme Implementation Board supporting the High Level Group.

Section 29 e

During 2012-13 we received two further preliminary Section 29e enquiries from Licence Providers, bringing the number of enquiries received to seven since 2008. Our asset and cost assessment established that none of the circumstances in either case would result in a Section 29e agreement.

3. Expenditure, Performance and Efficiency

HCA financial results

The table below compares the Historical Cost Accounting results for Scottish Water's activities to 31 March 2013 excluding subsidiaries. The financial results below exclude all of the statutory adjustments required under the International Accounting Standards (IAS), including IAS 19 'Employee Benefits'.

	2012/13	2011/12	Change
	£m	£m	£m
Turnover	1,053.0	1,045.8	7.2
Operating costs	499.3	486.9	-12.4
Depreciation / amortisation	333.6	329.0	-4.6
Gain on sale of assets	-2.1	-0.7	1.4
Total costs	830.8	815.2	-15.6
Operating surplus before interest	222.2	230.6	-8.4
Net interest	154.4	156.8	2.4
Profit before tax – Regulated	67.8	73.8	-6.0
Profit before tax – Non Regulated	0.5	0.2	0.3
Profit before tax – Scottish Water	68.3	74.0	-5.7
Taxation charge / (credit)	-3.4	-0.5	2.9
Profit after tax	71.7	74.5	-2.8

Table 3.1

For the year ending 31 March 2013 Scottish Water's costs (excluding subsidiaries and statutory adjustments under IAS) totalled £830.8 million. Costs included in tables E1 (£397.1 million), E2 (£280.2 million) and E3 (£153.7 million) total £831.0 million. The £0.2 million difference relates to costs recharged to Business Stream under Service Agreements. These costs have been netted off Scottish Water's expenditure in line with group inter-company transaction reporting.

The surplus before tax in the year for Scottish Water was £68.3 million, £5.7 million lower than in 2011/12 (£74.0 million). The regulated surplus before tax was £6.0 million lower at £67.8 million.

Revenue

Regulated revenue for the year totalled £1,053.0 million (2012 - £1,045.8 million) and is analysed by category in table 3.2 below:

	2012/13	2011/12	Change
	£m	£m	£m
Household	750.9	745.6	5.3
Wholesale	296.7	294.7	2.0
Other	5.4	5.5	-0.1
Total regulated revenue	1053.0	1045.8	7.2

Table 3.2

Revenue from services supplied to household customers increased by only £5.3 million or 0.7% to £750.9 million reflecting the increase in connected properties and the tariff freeze effective from 1 April 2012. The benefit to household customers of freezing household charges at a time when applicable RPI was 5.4% was c£40 million. Revenue from wholesale services supplied to Licensed Providers increased by £2.0 million or 0.7% to £296.7 million. Revenue from other sales decreased by £0.1 million to £5.4 million.

Total costs

Total costs of £830.8 million were £15.6 million higher than in 2011/12.

Operating costs of £499.3 million were £12.4 million higher than 2011/12. Within these costs, regulated operating costs of £349.3 million were 2.7% or £9.1 million higher than in 2011/12 while PFI costs were £3.3 million higher at £150.0 million.

From a regulatory perspective, like-for-like costs actually reduced in real terms by £1.3m or 0.6%. Compared with last year there were higher bad debt provision charges of £6.3 million, £7.0 million of inflation, an increase in local authority rates of £3.4 million, increased energy prices of £3.0 million and new operating costs associated with new capital investment of £3.0m. These increases were partly offset by lower VR and other restructure costs of £12.0 million. Table 3.3 below summarises this movement:

	2012/13	2011/12	(inc)/dec	
	£m	£m	£m	%
Regulated Operating Costs	349.3	340.2	-9.1	-2.7%
VR costs and other restructure costs	-3.5	-15.5	-12.0	
Average inflation (3.1%)	-	7.0	7.0	
Carbon Reduction Commitment	-2.8	-3.0	-0.2	
New operating costs	-3.0	-	3.0	
Bad debt	-29.2	-22.9	6.3	
Like for Like costs	310.8	305.8	-5.0	-1.6%
Power price	-3.0	-	3.0	
Local Authority rates charges	-61.7	-58.3	3.4	
SEPA and WIC costs	-14.9	-15.0	-0.1	
Like-for-like real controllable costs	231.2	232.5	1.3	0.6%

Table 3.3

Depreciation, including infrastructure depreciation, increased by £4.6 million to £333.6 million, primarily as a consequence of the capital investment programme. The gain on sale from asset disposals was £1.4 million higher than in 2011/12 at £2.1 million.

The average number of employees during the year increased by 48, or 1.5% to 3,272 (including SWS / SWS2 secondees).

Finance costs

As at 31 March 2013, the weighted average interest cost of the outstanding long-term debt was 5.03%, (2012 – 5.15%). Net interest payable during the year was £154.4 million, £2.4 million lower than in 2011/12.

During the year, net debt increased by £95.5 million to £3,023.8 million (being loans of £3,269.3 million less cash balances of £245.5 million). The increase was driven by a £100.0 million increase in borrowing from the Scottish Government and a £4.5 million increase in cash balances.

Taxation

Scottish Water's tax credit was £3.4 million (2012 – £0.5 million). This was due primarily to the favourable impact of the change in UK corporation tax rate from 24% to 23% that will be effective from 1 April 2013 which meant the re-measurement of deferred tax balances.

Borrowing Limit

Scottish Ministers set Scottish Water's (consolidated) maximum net new borrowing limit at £100.0 million for 2012/13. Actual net new borrowings in 2012/13 were £100.0 million.

Potential Regulatory Financing adjustment

In June 2011 we outlined the potential for a minor regulatory financing adjustment to take account of circumstances that differ from those set out in the Final Determination. We have updated this information to take account of changes in 2012/13. Many of these circumstances are still subject to further change and we currently envisage that any required adjustment will be undertaken as part of the 2015-2021 strategic review of charges.

At 31 March 2013 the principal items that may need to be considered are:

- **Freezing of household charges in 2012/13 and restriction of charge increase in 2013/14** – as a result of these decisions we expect to deliver out-performance back to customers early by not using our full entitlement to increase household prices by the household K factor of -5% across 2010-15.
- **Non-Domestic Rates Revaluation** - The impact of the 2010 rates revaluation which increases operating costs by £133m for the 2010-15 period. An increased Opex charge of £130m and increased PFI costs of £3m has been included in the Delivery Plan March 2013 Refresh.
- **Carbon Reduction Commitment Charges** - Carbon Reduction Commitment Costs was introduced for 2011/12 and may impact by around £3.5m per year out to 2014/15. An additional charge of £14m was included in the Delivery Plan March 2013 Refresh to reflect this item.
- **Taxation Changes** - Changes in Corporation Tax rates and capital allowances have been introduced by the UK Government in budgets since June 2010 and adjustments have been made in the Financial Statements in the Delivery Plan Update.
- **Changes in the OMGWG Register** - Changes to the investment programme as set out in the OMGWG change register.

4. Supporting Information

Water Resources, Supply and Demand and Security of Supply Index

This year we have continued to provide unconstrained services with none of the population affected by hosepipe restrictions.

The SOSI is an indicator of the extent to which a company is able to guarantee provision of its planned level of service. Our SOSI score has continued to improve year on year as a result of the positive effects of the leakage reduction programme, growth and other water quality projects. Our SoSI score is now reported as 74.

Leakage

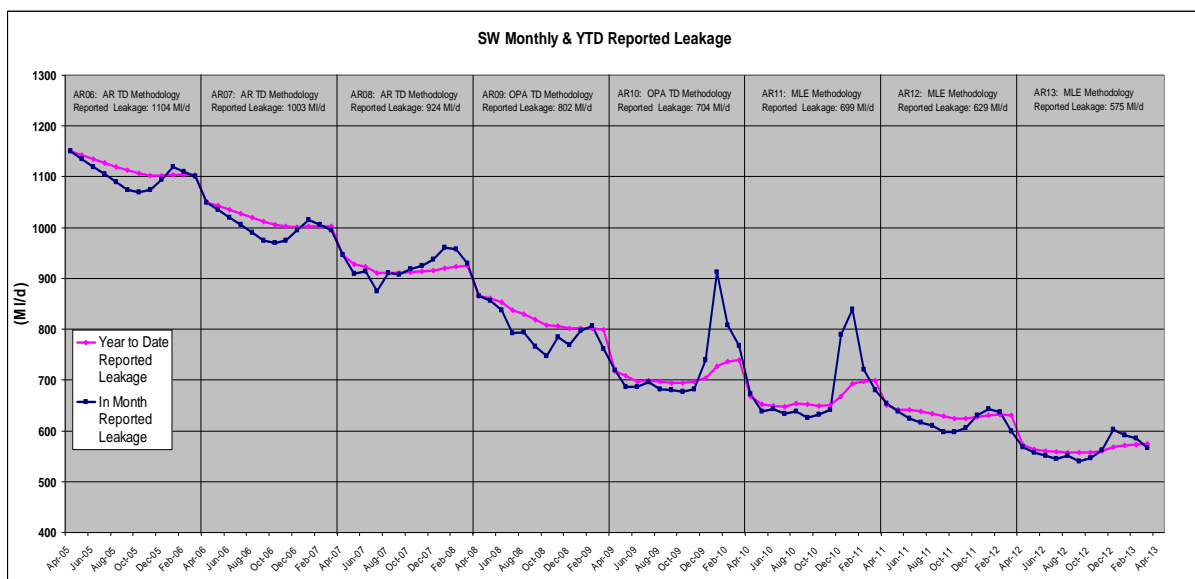
Our MLE reported leakage for 2012/13 is 575 MI/d which is a 54 MI/d reduction on our reported MLE leakage of 629 MI/d for 2011/12, successfully out-performing our 2012/13 Delivery Plan target of 635 MI/d. SW has also achieved the agreed Economic Level of Leakage (ELL) of 600 MI/d one year ahead of regulatory expectation. Table 4.1 below details the leakage reduction we have achieved in recent years.

Description (ML/d)	2008/09	2009/10	2010/11	2011/12	2012/13
Regulatory Reported leakage (OPA)	802	704	699	629	575
Leakage Target (OPA)	840	730	720	670	670
MLE adjusted leakage	816	738	699	629	575

Table 4.1 - Leakage

Figure 4.1 below demonstrates the improvements in leakage over previous years. The spikes in late 2009 and 2010 correspond with the extreme winter weather that caused extensive disruption across Scotland and caused operational challenges for us.

Figure 4.1 – Leakage Profile back to 2005/06



Customer Satisfaction

We have been monitoring customer satisfaction since 2010 through a postal survey. Over 50,000 customers have taken part to provide satisfaction tracking and insightful comments about their experience. This valuable information is being used to drive service improvements that are most valued by our customers.

Customer satisfaction has increased again this year and reached a score of 88.3%. This has been achieved through a determined focus on listening to customers, combined with the delivery of a number of considerable improvement projects in our main contact areas, such as those on Sewer Flooding, Repeat Customer Contact and Avoidable Complaints. We continue to focus on customer satisfaction and improve the customer experience further for all our customers.

Climate Change

The Climate Change (Scotland) Act sets a duty on public bodies to contribute to the Government's goals for carbon reduction and adapting to climate change. We have continued to take action over the past year to meet these expectations.

Our Delivery Plan for 2010-15 includes a number of projects focussed on climate change adaptation and carbon mitigation, notably to install 25GWh of hydropower, and pilot sustainable treatment options.

The climate adaptation projects were completed in 2012-13 and have helped us to determine adaptation measures for the next investment period. The studies identified a need for improved long term monitoring of the environment and our assets, which we are seeking to progress in Q&S4. This will help us to better understand the way in which the climate is changing, its effects on our service, and reduce the uncertainty presented by Climate Change models in order to make appropriate adaptation choices.

We have completed the majority of carbon mitigation studies and are working closely with SEPA on the remaining two, which involve field trials into more sustainable treatment options. A key project delivered was the carbon assessment tool which provides the capability for investment planners and capital delivery teams to quantify the operational and embodied carbon associated with capital projects.

We have been reporting our annual operational carbon footprint (CFP) for six years. Over that time there have been improvements in data but also changes in method and in carbon factors, making direct year-to-year comparisons difficult. We undertook an exercise to allow direct comparison with previous years, adjusting to take account of chemicals, grid emission factor and previously missing data. We are pleased to report that this shows our operational carbon emissions have fallen by 10% since 2007/08. This is in spite of continued quality enhancement, which has in the past driven up electricity consumption.

Our CFP for 2011/12, the most recently reported year, was 464,990 tonnes of carbon dioxide equivalent (tCO_{2e}), and includes for the first time the emissions associated with chemical use. This creates an apparent increase on the previous year but in fact masks a reduction on a like for like basis. We reduced grid electricity use (the main source of our emissions), and of natural gas; the latter is likely to be due to the milder winter experienced in 2011/12 compared with 2010/11. Leakage management has continued to be a key element in reducing carbon. The report was produced in-house and verified by Carbon Trust accredited consultants.

Board Changes

In February 2013 Mr Douglas Millican was appointed Chief Executive Officer of Scottish Water, following the death of Mr Richard Ackroyd in 2012. The position of Finance Director, is currently awaiting an appointment.

In conjunction with the above changes Mr Peter Farrer was appointed Chief Operating Officer.

On 31st March 2013 Mr Pat Kelly left the Board at the end of his period of appointment, not being eligible for a further re-appointment. The two vacant Non-Executive positions are currently being recruited.

The current Board therefore consists of:

- Ronnie Mercer - Chair
- Douglas Millican - CEO
- Andrew Wylie – Non-Executive Director
- Alan Bryce - Non-Executive Director
- James Spowart - Non-Executive Director
- Donald Emslie - Non-Executive Director
- Mrs Lynne Peacock - Non-Executive Director
- Chris Banks – Commercial Director
- Peter Farrer – Chief Operating Officer
- Geoff Aitkenhead – Asset Management Director

Governance

We have retained the methodologies and processes used for producing the detailed information in Scottish Water's Annual Return to the Water Industry Commission developed over previous years. Black and Veatch have again audited the information reported in the Annual Return as part of the normal assurance to the Scottish Water Board and consequently the Commission.

This approach has ensured that this submission continues to be based on sound processes and assumptions.

Please find our Board assurance statement at Appendix 1.

5. Looking Forward

During 2012/13 we continued to transform the way we deliver service to customers and to drive through further improvements to our services during 2010-15.

Delivery Plan Update 2010-15

We are committed to delivering and outperforming the 2010-15 regulatory contract and remain confident about the pace and effectiveness of our delivery. Achieving out-performance will enable Scottish Water to progress considerably towards our vision. Improvements are being driven through three major initiatives.

National Operations Centre

Our new National Operations Centre in Stepps, Glasgow will provide office accommodation for 600 Glasgow based workers and house our new Intelligent Control Centre. This energy efficient building will be completed and operational by late summer 2013. The change supports Scottish Water's move from a reactive to a more planned environment by enabling access to the information our people need to make the right decision at the right time to improve the service we deliver to our customers

Research and Innovation

Innovation is key to sustaining high performance and delivering ever higher service standards. During 2012/13, research and innovation have helped us to deliver improved value, through the installation of an energy recovery system on our water mains at Denny and enhanced performance for our customers, through the use of wastewater pump blockage detection systems. Looking ahead we will further improve our services to customers by focussing our innovation activity to deliver transformational research in three areas:

- Enhancing water quality compliance
- Energy self generation on all wastewater treatment works
- Sustainable rural communities

Alongside this, we are also pursuing single topic issues such as leakage, sewer flooding and carbon reduction through the UKWIR programme.

Research engagement

During 2012/13, Scottish Water has continued to develop its research portfolio to support the strategic focus of the business. Working with Scottish and UK universities we are:

- Working in partnership with Glasgow University to analyse trends in water supply data to identify when there is going to be an interruption to our service. This will aid the development of procedures which will ultimately help minimise disruption to customers.
- Investigating with the University of Exeter the opportunity to vary the quality of discharges from waste water treatment works to match the environmental capacity of the receiving waters. This has the potential to allow us to reduce the treatment costs (through reduced energy and chemical use) when there are high flows in the water environment.
- Researching with Birmingham, Cranfield and Newcastle universities the extent that phosphorous (a valuable nutrient for agriculture) can be recovered from waste water processes by currently known and emerging methods.

- Working with the universities of Strathclyde and Edinburgh to develop statistical predictive models to determine the condition of our assets.
- Participating in the S3C partnership led by the University of Strathclyde on developing an asset sensor system for monitoring long-life assets such as dams or pipes.
- Supporting 9 engineering doctorate projects through STREAM, the industrial doctorate programme for the water sector led by Cranfield Water Science Institute.

European research programme

We continue to seek European partnerships through the EU Framework Programme that support our strategic aspirations. In 2012/13 we commenced a pan-European partnership project. This project will benefit customers and service providers by developing a supply and demand software system that more effectively links consumption patterns of our customers to the production of water at the treatment works.

Technology development

During 2012/13 we have been working with Scottish-based technology companies to develop:

- A low-cost, small-scale ozone generation unit. This unit has potential for rural or point-of-use applications.
- A new treatment system for small scale applications in drinking water production.

We are also working in-house on the development of a device to protect drinking water supplies from potential cross-contamination from industrial applications.

Innovation in action

Scottish Water and our customers are already starting to see benefits from some key innovations we have introduced during 2012/13.

Our pump blockage detection system, developed in partnership with a Scottish-based control systems company, is helping to reduce blockages in our waste water network and save operational costs and reduce impact on our customers.

We have achieved a UK-first in a network pressure management and energy recovery system (Difgen) at Denny. This helps minimise bursts, reduce leakage and converts the kinetic energy from the water supply network to electricity in the process.

A study into the opportunities to generate value from waste water systems has highlighted energy generation opportunities on some of our medium-sized treatment works.

Future activity

We have recently re-focused our research and innovation activities to deliver a practically focused research programme that we believe will interest the wider utility and academic community in the coming years.

We have identified 3 strategic initiatives that will help us to deliver our vision through focusing on exemplary compliance, sustainable rural communities and self-generation of energy at waste water treatment works.

We will use these initiatives to engage more effectively and build strategic relationships with academia and research providers. We will also continue to work with the enterprise community to develop relationships with suppliers which can help us achieve our aspirations over the short, medium and long term.

Through the UK Water Industry Research (UKWIR) Programme, we will work collaboratively with the wider industry on common research programmes to reduce leakage, prevent sewer flooding and reduce our carbon footprint.

Appendix 1

Annual Return 2012/13 ASSURANCE STATEMENT

Background

The Board is required to confirm that it has endorsed the Overview to the Annual Return.

The Board has charged the Chief Executive, with the responsibility to establish and maintain sound systems of internal control that support the completion of the Annual Return submission to the Water Industry Commission.

The systems of internal control that support completion of the Annual Return are designed to ensure:

- The accuracy and consistency of reporting
- That soundly based assumptions and judgements are used
- Audit trails are maintained for origination and approval of all data in the Annual Return
- The identification, understanding and reporting on material data exceptions
- The reliability of information for decision making and for performance assessment.
- Compliance with applicable regulatory and legislative reporting requirements.

The systems of control are designed to reduce the risk of material error and to provide effective assurance on the completion of the Annual Return.

Process

The Board gains assurance as to the effectiveness of internal control through:

- the controls and assurance process put in place by the Executive Directors to ensure that the Annual Return is consistent with the requirements of regulatory reporting;
- a signed assurance statement from the Chief Executive concerning the operation of the systems of internal control;
- reporting from Executive Directors on associated matters;
- the results of both internal and external audit, and other internal and external review agencies;
- the adequacy of management response to issues identified by audit and review activity; assurances relating to the corporate governance requirements for the organisation; and
- the operation of anti-fraud policies, whistle-blowing processes, and arrangements for special investigations.

Outcomes

Based on the Board's knowledge of the effectiveness of the systems of internal control, that support the completion of the Annual Return, the Board has endorsed the Overview to the Annual Return. The Board has been assured that the assumptions, judgements and confidence grades used are appropriate, reasonable and consistent with the requirements of regulatory reporting.


SIGNED
(On behalf of the Board of Scottish Water)

CHIEF EXECUTIVE OFFICER

Date 29/5/13