



**Scottish
Water**

Trusted to serve Scotland

Annual Return 2015/16

Overview

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Appendix A –Board Assurance Statement

1. Executive Summary

This overview reports on Scottish Water's performance and activities in 2015/16, the first year of the 2015-21 regulatory period.

In our 2015 Delivery Plan we stated that while the targets were very challenging, we were determined to deliver significant further improvements for our customers and out-perform our commitments. During 2015/16 we have made a positive start to delivering these commitments. Highlights include:

- The water we delivered to our customers' taps during 2015 has been at its highest quality level ever, at above 99.91%;
- The level of customer service we are providing, as measured by the Overall Performance Assessment (OPA) measure is within the upper end of our plan range at 393;
- We introduced our household Customer Experience Measure in April 2015 to ensure that the service experienced by our customers is a key driver of our performance. Our commitment for 2015/16 was to improve on the score of 82.6 (out of 100) in 2014/15. Our actual score was 84.3, a reduction of 10% in points lost from 17.4 in 2014/15 to 15.7 in 2015/16;
- Our customer satisfaction score as measured by the Institute of Customer Service is at a record level. We continue to maintain our leading position within the UK water industry and we are among the leaders across the wider economy in the provision of essential products and services;
- Our reported leakage for 2015/16 is 500 MI/d which is a 44 MI/d reduction on our reported level of 544 MI/d for 2014/15;
- We have been recognised as Scotland's Best Large Employer and accredited as a Living Wage Employer; and
- We are on track to outperform the challenging financial limits set out in the Final Determination 2014.

While our first year of the new regulatory period was successful in many areas there were challenges in terms of our investment delivery. We put in place new investment planning and delivery arrangements that incorporate learning from previous investment delivery approaches. The scale of change associated with this impacted on our rate of investment delivery in the first half of the year and in agreement with the Output Monitoring Group and the Scottish Government, we have re-baselined our investment programme for the 2015-21 period.

In the latter part of the year we have generated momentum in our investment delivery, enabling us to achieve the original Overall Measure of Delivery (OMD) target.

1.1 2015/16 Dashboard

Table 1 shows the 2015/16 year-end position for the key regulatory outputs set out in the Regulatory Contract.

Annual Dashboard – 2015/16			
Measure to be reported	Delivery Plan Target 2015/16	Actual 2015/16	Current RAG Status
Output Delivery			
Investment: Overall Measure of Delivery (OMD) (2015 Delivery Plan)	71 - 75	75	G
Investment: Overall Measure of Delivery (OMD) ¹ (2016 Delivery Plan update)	52 - 54	73	G
Investment: Complete SR10 projects by March 2015	28	22	R
Levels of Service			
Overall Performance Assessment	380	393	G
Household Customer Experience Measure	82.6	84.3	G
Leakage (MI/d)	575	500	G
Water into supply (MI/d) (rolling four quarters)		1,779	
Expenditure			
Total capital expenditure (£m)	509	483	
Operating and PPP Costs – non IFRS (£m)	545	521	G
Operating and PPP Costs – IFRS* (£m)	504	481	G

*IFRS = International Financial Reporting Standard

Table 1 – Annual Regulatory Dashboard – 2015/16

Performance status
Performance below target
Performance on or above target

1.2 Overall Performance Assessment (OPA)

In our 2015 Delivery Plan we set out our commitment to achieve an OPA score at, or above, the threshold for leading water and waste water companies, (380 points in 2015/16 rising to 385 points by 2020/21), and our aspiration to be best in class, achieving an equivalent OPA score at, or above, 400 points.

We exceeded our 2015 Delivery Plan commitment with a score of 393 in 2015/16. When compared against the 2015-21 methodology, our restated 2014/15 score was 396 points. The small OPA reduction from 2014/15 (on a like for like basis) was caused by a small increase in non-compliant waste water treatment works and the more serious water pollution incidents, offset by the improvement to drinking water quality.

¹ The OMD target score and actual for 2015/16 reflects the re-baselined programme in Scottish Water's Delivery Plan update 2016 as approved by the Scottish Government.

1.3 Customer Experience Measure

We introduced our household Customer Experience Measure (hCEM) in April 2015. We set out in our 2015 Delivery Plan our aim to improve on the score of 82.6 (out of 100) achieved in 2014/15. Our score for 2015/16 was 84.3, a 10% reduction in lost points from 17.4 in 2014/15 to 15.7 in 2015/16. This reduction was as a result of improvements in all seven areas of performance measured under CEM. Written customer complaints have been driven down this year to their lowest ever level.

We have developed a separate Customer Experience Measure (nhCEM) that will allow us to focus on improving the service and experience to our non-household customers in 2016/17 and beyond.

1.4 Customer Satisfaction

We agreed with the Customer Forum to build a benchmarking indicator which would track customer satisfaction of Scottish Water alongside other companies in other sectors using the UK Customer Satisfaction Index (UKCSI) survey from The Institute of Customer Service. Our aspiration is to match the levels of customer satisfaction of leading providers of essential goods and services.

The January 2016 UKCSI results confirmed we continue to maintain our leading position within utilities and that we are starting to meet our aspiration of matching the levels of customer satisfaction of leading providers of essential goods and services.

1.5 Leakage

Our reported leakage for 2015/16 is 500 MI/d which is a 44 MI/d reduction on our reported level of 544 MI/d for 2014/15. We continue to target leakage through proactive leakage detection and repair, pressure management and modulation, improvements in repair cycle times and selected mains rehabilitation. In line with the Leakage Assuror's recommendation, we have improved our data in the water balance calculation particularly through studies into the night time household use of water. This has given us a better understanding of our leakage levels.

1.6 Compliance

Drinking water quality compliance

For the calendar year 2015, overall compliance with water quality standards reached our highest ever level with 99.93% of all water quality tests conducted in our sampling programme complying with quality standards. Water quality at customer taps in 2015 increased to 99.91%, also our highest ever level, and significantly above our Delivery Plan commitment of 99.88%.

Waste water compliance

Waste water treatment works compliance is reported as 6 failing works (Dalscone Old, Mauldslie, Newton St. Boswells, Pathhead, Rothienorman and Newmachar) at 31 March 2016; none of which were a failing works in 2014/15. This level of performance compares against our Delivery Plan 2015-21 forecast of 5 works, and a performance in 2014/15 of 3 failing waste water treatment works under serviceability measures and 4 for OPA purposes.

There has been a steady reduction in the number of high risk waste water treatment works from 66 in 2013/14 to 36 in 2015/16.

There has been a small increase in the category 1 to 3 environmental pollution incidents from 250 in 2014/15 (of which 1 was a water pollution incident) to 260 in 2015/16 (of which 3 were water pollution incidents). However, at 260 category 1-3 events, this remains well below the minimum level of service to be maintained in the 2015-21 period of 330 as set out in our Delivery Plan.

We continued to reduce the number of Unsatisfactory Intermittent Discharges (UIDs) on our sewerage network as a result of our investment programme during 2015/16.

2015 was the first bathing season under the revised Bathing Water Directive. We are pleased to note that Scottish Water assets performed as expected and did not contribute to the downgrade of any Scottish bathing waters.

All sewage sludge was recycled in compliance with the regulations during 2015/16.

1.7 Capital programme delivery

We put in place new investment planning and delivery arrangements with strengthened in-house investment planning capability and three new delivery alliances. The scale of change associated with implementing this revised business model and tailored supply chain impacted on our rate of investment delivery in the first half of the year. In agreement with the Output Monitoring Group and the Scottish Government, we have re-baselined our investment programme for the 2015-21 period.

In the latter part of the year we have generated momentum in our investment delivery. As a result of this momentum in 2015/16 we have invested a total of £482.6 million compared to £481.1 million in 2014/15. At 31 March 2016, our Overall Measure of Delivery (OMD) was on target.

We started the 2015-21 period with 37 projects from the previous programme which were due but not completed by March 2015. By the 31 March 2016 we delivered 22 of these projects, against an original target of 28.

1.8 Wholesale service

2015/16 has seen the Scottish competitive market continue to develop rapidly with licences granted to a further six Licensed Providers in the last year. This takes the total number of Licensed Providers able to operate in the retail market in Scotland to 23. Businesses have continued to switch Licensed Providers in significant numbers. The most significant switch was associated with the successful transfer of the public sector contract to Anglian Water Business where 24,000 supply points (SPIDS) transferred on 1 March 2016.

1.9 Research and Innovation

We recognise that innovation is key to sustaining high performance and delivering ever higher service to our customers. We continue to work with academia to develop new knowledge to improve services and with our supply chain to explore better ways to deliver increased value

for customers. Our strategic research and innovation programme is progressing in the following areas:

- Enhancing water and environmental quality compliance
- Value recovery from waste water
- Sustainable rural communities

We are already starting to see benefits from some key innovations we introduced in previous years.

1.10 Expenditure, Performance and Efficiency

Financials

The regulated surplus before tax of £102.8 million was £32.6 million higher than in 2014/15 (£70.2 million).

Revenue

Regulated revenue for the year totalled £1,120.4 million (2015: £1,096.9 million).

Revenue from services supplied to household customers increased by £19.9 million or 2.5% to £820.7 million reflecting the 1.6% tariff increase effective from 1 April 2015 and the increase in properties connected to the network.

Revenue from the wholesale service supplied to Licensed Providers increased to £291.5 million, an increase of £2.3 million (0.8%) from 2014/15 reflecting the project to identify and bring into charge unregistered premises and an average tariff increase of 0.5%, partly offset by a reduction in consumption.

Revenue from other sales increased by £1.3 million to £8.2 million.

Total costs

Total costs increased by £0.3 million to £845.4 million (2015: £845.1 million).

Operating costs of £480.5 million were £15.3 million higher than in 2014/15. Within these costs, regulated operating costs of £367.6 million were 4.1% or £14.5 million higher than in 2014/15 and PPP operating costs were £0.8 million higher at £112.9 million.

The £14.5 million increase in regulated operating costs was primarily due to: a £15.1 million increase in local authority rates charges, reflecting the one-off refund received in 2014/15 (associated with the successful revaluation appeal) and the unwinding of an accrual in 2014/15 that was no longer required (associated with potential retrospective landfill tax charges) of £5.5 million. These variances were partially offset by a reduction of £7.0 million in the bad debt charge for 2015/16. After adjusting for these items, the increase in energy prices, carbon reduction charges and new operating costs associated with capital investment, like-for-like costs, decreased in real terms by 2.4% or £7.1 million.

Depreciation, including PPP depreciation, increased by £6.6 million to £261.0 million, due to the profile of the capital investment in the year. The gain on sale from asset disposals was £4.0 million higher than in 2014/15 at £14.7 million.

Finance costs

As at 31 March 2016, the weighted average interest cost of the outstanding long-term debt was 4.73%, (2015: 4.86%). Net interest payable during the year was £149.6 million, £8.4 million lower than in 2014/15. The finance costs total is net of the foreign exchange gain of £1.2 million (2015: £1.4m loss) in respect of the forward Euro currency contracts.

PPP finance costs were £1.0 million lower at £22.6 million.

During the year, net debt decreased by £23.2 million to £3,055.7 million (being loans of £3,424.3 million less cash balances of £368.6 million). The decrease was driven by a £23.2 million increase in cash balances, with no net new borrowings from the Scottish Government.

1.11 Board Changes

Ronnie Mercer CBE retired as Chair at the end of his term of office on 31 May 2015, with Lady Susan Rice CBE assuming the Chair on 1 June 2015. Donald Emslie ended his term of office with the Scottish Water Board on 31 March 2016.

1.12 Recognition

As well as being recognised as Scotland's Best Large Employer and accredited as a Living Wage Employer, Scottish Water also received recognition for its achievements in the areas of health and safety, customer service and procurement.

1.13 Looking Forward

Our Delivery Plan for 2015-21 is ambitious and sets out to build on our success to date. Over the remainder of the regulatory period our focus remains on providing our customers a leading service while at the same time reducing our charges in real terms.

1.14 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. We also retained Black and Veatch to audit the information reported in the Annual Return as part of the normal assurance to the Scottish Water Board and consequently the Commission. Our process for preparing the Annual Return achieved ISO9001 accreditation in March 2015 and was reassessed as part of the BSI audit in January 2016. Our approach continues to ensure that the Annual Return submission is based on sound processes and assumptions, and is subject to continuous improvement.

Please find our Board assurance statement at Appendix A.

2. Key Outputs and Service Delivery

2.1 Customer Service

Overall Performance Assessment (OPA)

In 2015/16 our OPA performance exceeded our Delivery Plan target of 380. This was though 3.21 points lower than our 2014/15 performance when assessed against the methodology used for the 2015-21 period.

Table 2.1 below compares our 2014/15 and 2015/16 performance for each of the 17 indicators.

Indicator	2010-15 methodology	2015-21 methodology		
	AR15 OPA score	AR15 OPA score	AR16 OPA score	Change
% of properties subject to inadequate water pressure	37.38	37.38	37.38	0
Connected properties experiencing unplanned interruptions	35.02	35.02	35.76	0.74
Hosepipe restrictions	12.5	12.5	12.5	0
Security of Supply absolute performance	11.25	11.25	11.25	0
Security of Supply performance against target	12.5	12.5	12.5	0
% of water samples that comply with parameters	42.64	40.54	43.6	3.06
Leakage	12.5	12.5	12.5	0
Water Service (sub-total)	163.79	161.69	165.49	3.8
% properties suffering sewer flooding incidents caused by overloading	25	25	24.91	-0.09
% properties suffering sewer flooding incidents caused by other causes	37.5	37.5	37.5	0
Sewer flooding (at risk)	12.5	12.5	12.5	0
Sewerage Service (sub-total)	75.00	75.00	74.91	-0.09
Customer Contact (Total of complaints and telephone performance)	18.51	18.4	18.59	0.19
Assessed customer service	37.5	37.5	37.5	0
Customer Service (sub-total)	56.01	55.9	56.09	0.19
Category 1 & 2 sewage EPIs	24.4	24.4	22.95	-1.45
Category 3 sewage EPIs	10.29	10.29	10.16	-0.13
Category 1 & 2 water EPIs	11.22	11.22	8.69	-2.53
Sewage sludge disposal	12.5	12.5	12.5	0
% pe served by non-compliant sewerage treatment works	47.75	46.00	43.00	-3.00
Environmental Performance Service (sub-total)	106.16	104.40	97.29	-7.11
Total	400.96	396.99	393.79	-3.20

Table 2.1: OPA Performance 2015/16

Figure 1 below shows the changes in OPA score for each indicator from 2014/15 to 2015/16, on a like for like basis.

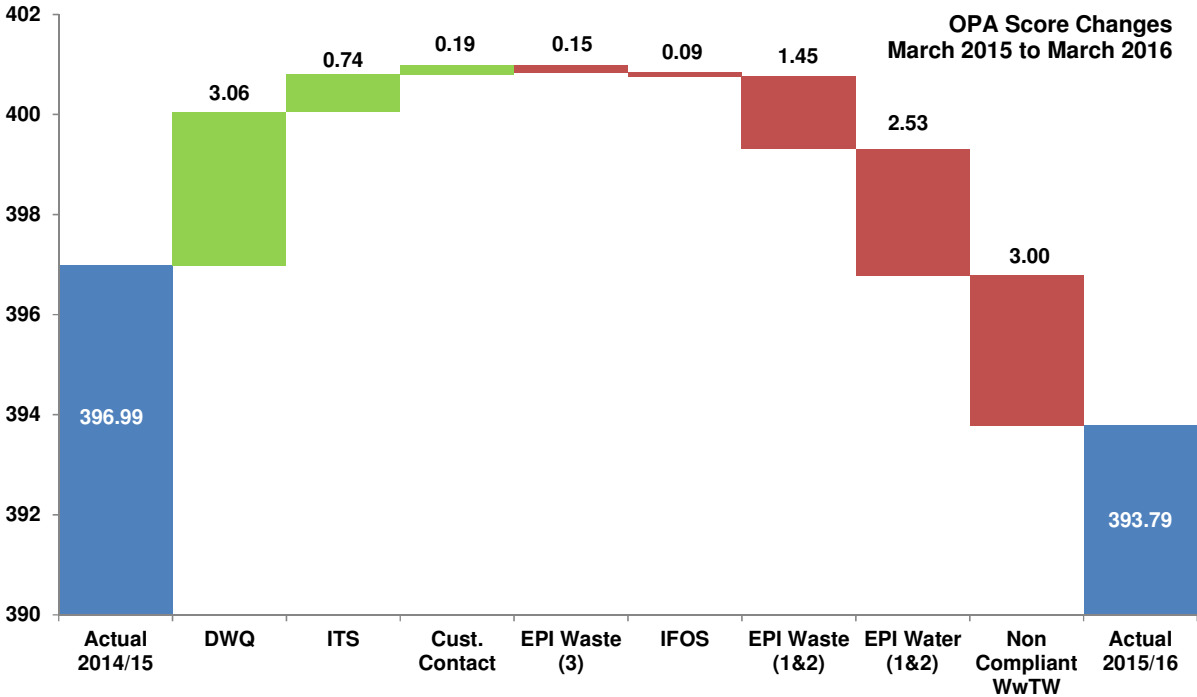


Figure 1 – Movement in OPA scores 2015/16

The change in methodology for the 2015-21 period was made to align the measures to customer impact and to give greater transparency to what the quality regulators report about Scottish Water’s performance. The changes comprised:

1. An amendment to waste water treatment works to balance priority on compliance across all works. We have moved away from the position where compliance is based on a percentage of the population receiving service from a compliant treatment works, to an absolute number of failing works. The agreed amendment will band failing works as follows:
 - 1 - 5 failing works: 1 point lost from each failing works
 - 6 - 10 failing works: 2 points lost from each failing works
 - 11 - 20 failing works: 3 points lost from each failing works

This change has been agreed with SEPA to reflect the environmental importance of complying with all discharge licenses. The definition of a failing works remains unchanged.

2. An amendment to the drinking water quality service measure to align with the DWQR’s measurement of overall compliance at customer taps. This increases the number of quality parameters being considered and reduces the over-emphasis previously placed on small water supply zones with relatively few samples. Parameters for taste and odour have also been included. The agreed amendment measures performance based on a linear range from a minimum performance level of 99.42%, achieving 5 points, to a maximum performance level of 100% achieving 50 points.

3. An amendment to the customer contact measure. We have reduced the period for a substantive response to formal complaints from 10 days to 5 days to align to our Guaranteed Service Standards.

Significant movements against the OPA indicators are explained below.

Connected Properties Experiencing Unplanned Interruptions

Table 2.2 shows the reduction in the number of properties that experienced unplanned interruptions compared to last year. A total of 7,318 weighted properties, or 0.28% of total population, received a supply interruption greater than 6 hours.

	2014/15	2015/16
Properties interrupted for 6 to 12 hours	7,626	5,718
Properties interrupted for 12 to 24 hours	482	632
Properties interrupted for more than 24 hours	81	84
Total number of properties interrupted for more than 6 hours	8,189	6,434
Total number of properties interrupted for more than 12 hours	563	716
Total 'weighted' properties interrupted for more than 6 hours	8,914	7,318

Table 2.2: Unplanned Interruptions to Supply 2013/14 and 2014/15

In this reporting year 6 large incidents caused 2,118 (2,268 aggregate) properties to lose supply for more than 6 hours:

- In May 2015, 610 properties were affected by an incident in Stoneybridge, South Uist with supply being restored within 11 hours 4 minutes.
- In July 2015, 202 properties were affected by an incident in Redmoss Road, Aberdeen with supply being restored within 9 hours 45 minutes.
- In February 2016, 581 properties were affected by an incident in Dunfermline with supply being restored within 9 hours 35 minutes.
- In February 2016, 375 properties were affected by an incident in Braehead Road, Paisley with supply being restored in 8 hours 20 minutes.
- In February 2016, 300 properties were affected by an incident in Seafield, Bathgate with supply being restored in 7 hours 9 minutes.
- In February 2016, 1,050 properties were affected by an incident in Bridge of Earn and Forgandenny, Perth. A burst occurred on a 300mm diameter main, the location of which was difficult, across farmland and down a steep river bank. In addition, the burst was located at a bend which complicated the repair. While almost all properties had their supplies restored in less than 6 hours, 50 properties in Forgandenny could not be fully supplied by tankers or rezoning due to the height of the properties and network restriction, with supply being restored in 41 hours 42 minutes. Bottled water was deployed to the community.

Percentage of water samples at customer taps that comply with parameters

In 2015/16 our OPA performance for the percentage of water samples at customer taps that comply with parameters increased from 40.54 points to 43.6 points, when measured on a like for like basis. Our water quality performance is discussed in Section 2.3 below.

Waste Water Category 1&2 EPIs

In 2015/16 there were 10 Category 1&2 incidents, an increase from 8 in 2014/15. This decreased our OPA performance by 1.45 points to 22.95 points for this indicator.

Water Category 1&2 EPIs

There were 3 Category 1 and 2 water pollution incidents during 2015/16 (compared to 1 in 2014/15). This decreased our OPA performance by 2.53 points to 8.69 points for this indicator.

Non-compliant Sewage Treatment Works

The methodology within this measure has changed from the % population equivalent served by non-compliant works to the number of failing treatment works. In 2014/15 a total of 4 failing works were recorded for OPA purposes, which would have scored 46.0 OPA points based on the new methodology. In 2015/16 we recorded 6 failing works, which reduces our score to 43.0 points.

2.2 Customer Satisfaction

2.2.1 Customer Experience Measure (CEM)

We introduced our household CEM in April 2015 to ensure that the level of service experienced by our customers sits at the heart of what we do and is a key driver of our performance improvement. Performance is measured against a number of quantitative and qualitative indicators and combined to produce an annual score out of 100, which is made up of the elements summarised below in Figure 2 below:

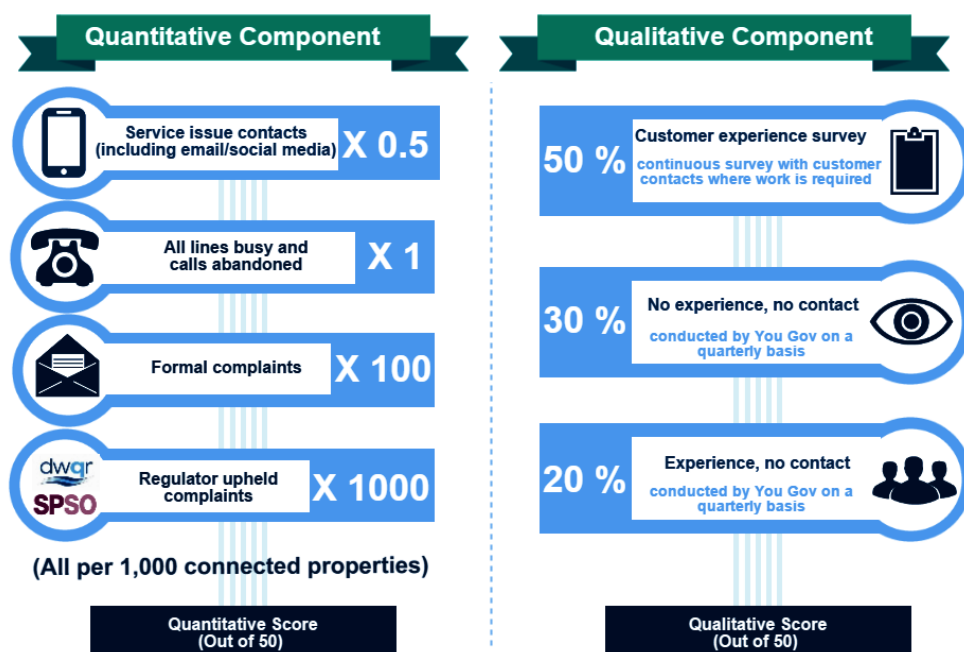


Figure 2 – Component elements of the household Customer Experience Measure

The score is improved by driving down unwanted service contacts, abandoned calls and complaints and by increasing customers' satisfaction with their experience of Scottish Water.

We set out in our 2015 Delivery Plan our aim to improve on the score of 82.6 (out of 100). Our score for 2015/16 was 84.3 - a 10% reduction in lost points. This was achieved primarily by driving down the number of complaints we receive and driving up the customer satisfaction of the service we delivered. Details of the component elements of the household Customer Experience measure and the number of points lost on each are shown below in Table 2.2.1

Measure	2014/15		2015/16	
	Input	Points lost	Input	Points lost
Quantitative elements				
Service issue contacts	298,962	5.06	291,401	4.89
All lines busy and calls abandoned	3,932	0.13	3,582	0.12
Written complaints	1,310	4.43	1,145	3.85
Regulatory upheld complaints	2	0.07	1	0.03
Qualitative elements				
Customer experience survey	87.7%	3.60	89.5%	3.06
No experience - no contact	92.6%	2.78	94.0%	2.65
Experience - no contact	76.2%	1.30	77.1%	1.05
Total points lost		17.37		15.65

Table 2.2.1 – Household Customer Experience Measure – points lost 2014/15 and 2015/16

In December 2015, our customer contact centre received the lowest in-month number of calls in the history of Scottish Water. Increasingly, our customers are choosing to enquire about services using social media and, in the last year, we have seen our number of Twitter followers increase from around 12,500 to around 17,500.

Written customer complaints have been driven down to their lowest ever level, with a 13% reduction in 2015/16.

We have developed a separate Customer Experience Measure that will allow us to focus on improving the service and experience to our non-household customers. We are trialling the measure during 2016/17.

2.2.2 UK Customer Satisfaction Index

We agreed with our customers to build a benchmarking comparison which would track customer satisfaction of Scottish Water alongside other companies in other sectors using the UK Customer Satisfaction Index (UKCSI) survey from The Institute of Customer Service. Our aspiration is to match the levels of customer satisfaction of leading providers of essential goods and services.

The January 2016 UKCSI results confirmed we continue to maintain our leading position within utilities (as shown in Figure 3) and we are starting to meet our aspiration of matching the levels of customer satisfaction of leading providers of essential goods and services in Scotland (as shown in Figure 4).

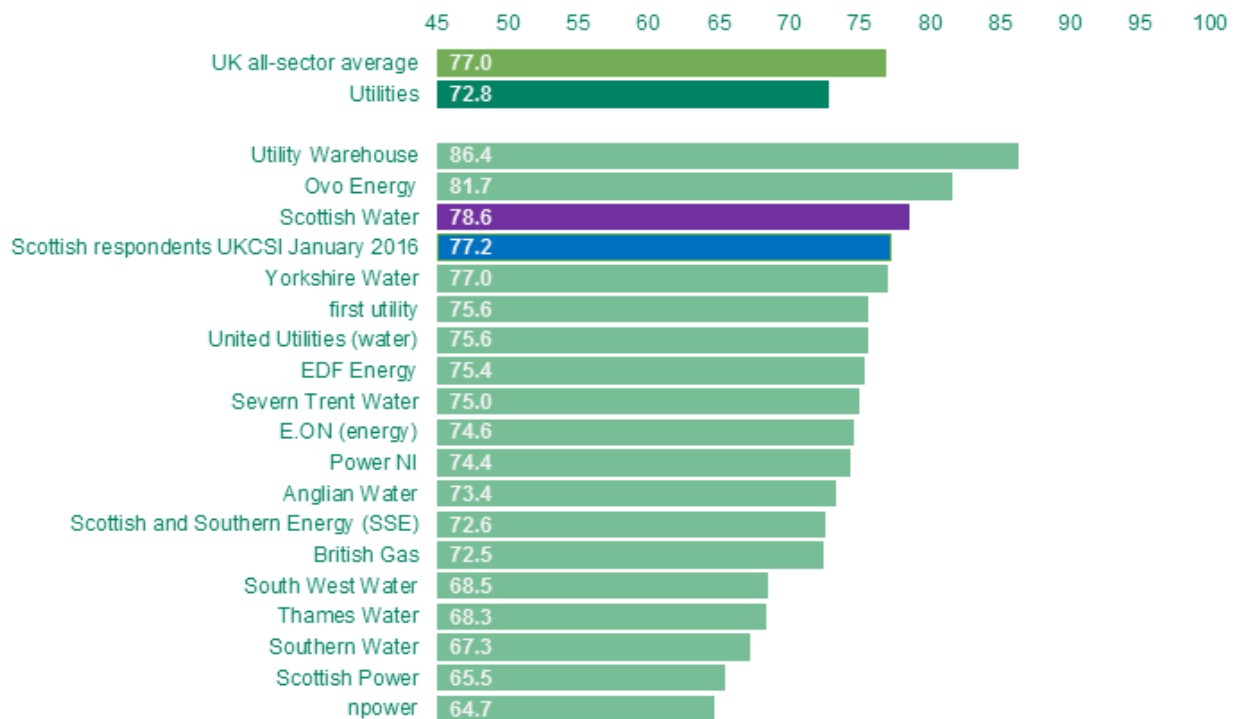


Figure 3 – UK Customer Satisfaction Index (UKCSI) – Utility Sector, January 2016

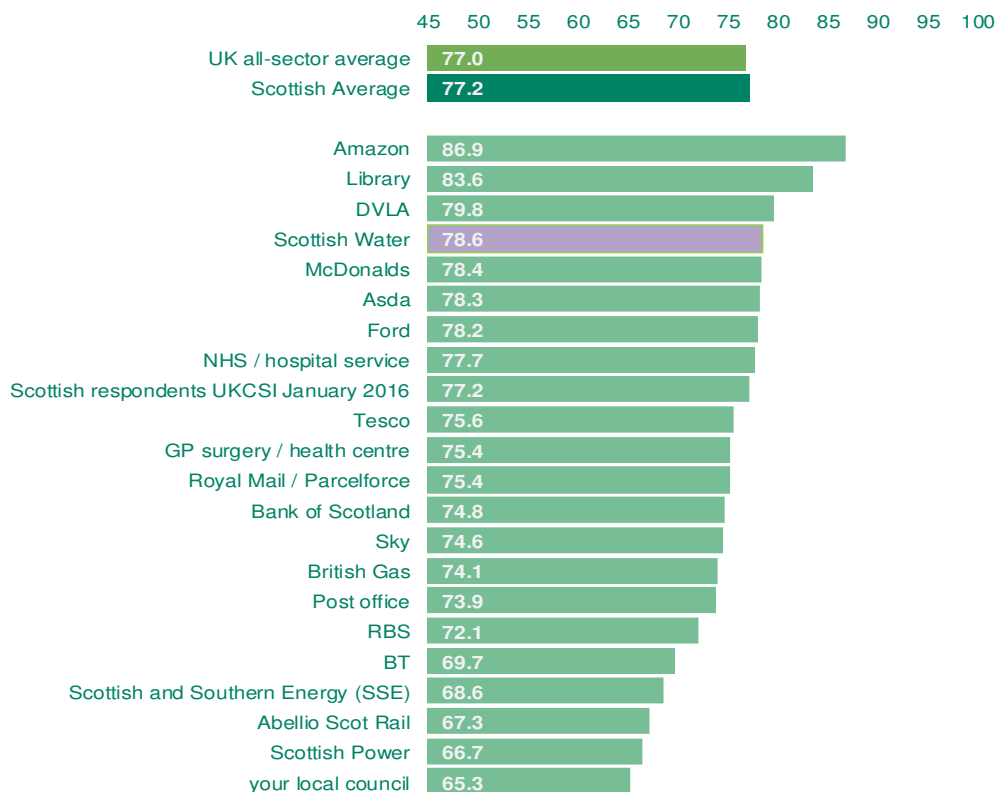


Figure 4 – UK Customer Satisfaction Index (UKCSI) - Scottish survey results, January 2016

2.2.3 Leakage

Our reported leakage for 2015/16 is 500 ML/d which is a 44 ML/d reduction on our reported level for 2014/15. We continue to target leakage through proactive leakage detection and repair, pressure management and modulation, improvements in repair cycle times and selected mains rehabilitation. In line with the Leakage Assuror's recommendation, we have improved our data in the water balance calculation particularly through studies into the night time household use of water. This has given us a better understanding of our leakage levels and reduced reported leakage by around 30 ML/d. Table 2.2.3 details the leakage reduction we have achieved since 2010.

Description (ML/d)	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16
Regulatory reported leakage (OPA)	699	629	575	566	544	500

Table 2.2.3 – Leakage levels for the 2010 to 2016 period

2.3 Drinking Water Service

Overall Water Quality Compliance

For the calendar year 2015, overall compliance with water quality standards reached our highest ever level with 99.93% of all water quality tests conducted in our regulatory sampling programme complying with quality standards (2014: 99.90%). Water quality at customer taps in 2015 increased to 99.91%, also our highest ever level.

Microbiological Quality

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

a) water leaving treatment works

In 2015, 25,840 samples were taken for *E.coli* and coliform analysis. Compliance with the *E.coli* standard was 100% and with the total coliform standard was 99.94%.

b) water in service reservoirs

In 2015, 50,306 samples were taken for *E.coli* and coliform analysis. Compliance with the *E.coli* standard was 99.99% and the total coliform standard was 99.87%.

c) water at customer taps

In 2015, 14,067 samples were taken for *E.coli* and coliform analysis. Compliance with the *E.coli* standard was 99.99% and the total coliform standard was 99.76%.

Table 2.3.1 highlights performance in microbiological water quality for 2014 and 2015 based on regulation samples:

		2014 fails	2014 compliance	2015 fails	2015 compliance
Treatment works	Coliforms	40	99.85%	16	99.94%
	<i>E.coli</i>	2	99.99%	0	100%
Service reservoirs	Coliforms	104	99.80%	63	99.87%
	<i>E.coli</i>	2	99.99%	5	99.99%
Customer taps	Coliforms	63	99.55%	34	99.76%
	<i>E.coli</i>	2	99.99%	1	99.99%

Table 2.3.1 - Microbiological quality of water

Chemical Sampling

Physical and chemical quality standards apply to water supplied at customer taps. 116,825 tests were applied to samples taken from customer taps to test for all parameters during 2015.

Table 2.3.2 highlights the performance of the key chemical parameters for 2014 and 2015.

	2014 fails	2014 compliance	2015 fails	2015 compliance
Trihalomethanes (THMs)	16	98.95%	2	99.87%
Iron	19	99.63%	28	99.45%
Colour	1	99.98%	0	100%
Manganese	15	99.70%	13	99.74%
Aluminium	1	99.98%	3	99.94%

Table 2.3.2 – Key Chemical Parameters

Water Resources Licensing

We submitted our annual Water Resource data return to SEPA for the 2015 calendar year, which covers abstraction and impoundment activities authorised under the Controlled Activities Regulations (CAR) and includes data for 275 abstraction and 102 compensation activities. It is a legal requirement of our Water Use (CAR) Licences to provide SEPA with data on our abstraction and compensation activities to enable them to monitor our compliance against the conditions of the licences we hold – typically maximum abstraction limits from our sources and minimum compensation flow requirements from our reservoirs.

There were 4 sites reported as non-compliant against abstraction limits most or all of the time during 2015. All 4 sites have been identified previously and 3 sites now have increased abstraction licences which should ensure compliance in 2016. The other site is due to be addressed during 2016/17. For compensation flows, overall performance has improved during the year, with 41 sites now fully compliant in 2015, up from 28 in 2014. The main issue with compensations has been the availability of data to enable compliance to be assessed. Improvements in data reporting during 2015 has led to better visibility of the flows that are being released and now the focus can move to identifying and resolving the issues that are causing them to be non-compliant.

Resilience

Our customers have told us that improving resilience of water supplies is a priority area for service improvement in order to reduce the likelihood of long term interruptions to supply. Our customers also asked us to consider further the appropriate level of investment to be made in

this area and the benefits this would deliver. We are planning further customer research to understand the levels of resilience customers desire which will help prioritise improvements.

We have developed a structured approach to assessing supply system resilience, and have completed 50% of the field work on the 17 largest systems.

Our pilot assessment identified the Ayrshire system as requiring improvement and to achieve this we are developing a strategic connection to the Glasgow system, which will deliver resilience and water quality improvements. The scheme is being delivered in three phases; the first phase is currently mobilising on site and two thirds of the pipes have been delivered, the other two phases are going through detailed route development.

The key resilience schemes set out in our business plan; South Edinburgh resilience and the duplication of the Glenhove Pumping Station to Dalnacouter Service Reservoir are progressing. We have developed the South Edinburgh scheme and it is now going through detailed route selection, while the Glenhove scheme is due to commence on site early in 2016/17.

2.4 Waste Water Service

Compliance – Waste water serviceability

Waste water treatment

Waste water treatment works compliance is reported as 6 failing works (Dalscone Old, Mauldslie, Newton St. Boswells, Pathhead, Rothienorman and Newmachar) at 31 March 2016, none of which were a failing works in 2014/15. This level of performance compares against our Delivery Plan 2015-21 target of 5 works, and a performance in 2014/15 of 3 failing waste water treatment works under serviceability measures and 4 for OPA purposes.

Failure prevention plans are in place for all high risk works to address performance issues. The number of high risk works has shown a steady reduction from 66 in 2013/14 to 36 in 2015/16.

Bathing Waters 2015

Scotland had 84 bathing waters officially designated for 2015, of which 72 could potentially be affected by Scottish Water assets. Scottish Water undertakes extensive pre-season inspections of assets that may impact bathing waters to identify any issues and ensure they are managed to minimise the risk to the bathing water.

All 72 Scottish Water influenced bathing waters recorded minimum sample performance of 'sufficient' for the 2015 Bathing Season, which was characterised by generally dry and warm weather, with short periods of excessive rainfall. Overall performance was good and operational issues were managed by the agreed response and reporting protocols with SEPA to ensure compliance.

Pollution Incidents

With regards to waste water Environmental Pollution Incidents (EPIs) substantial improvements took place since 2010 when a new focus and dedicated team was established to better understand and improve our performance on environmental pollution incidents. A key

focus is to improve data and understand the root causes of EPIs in order to better deploy resources to prevent incidents occurring. The trend in overall waste water EPI performance (Categories 1-3) is shown in Figure 5 below, noting the objective in the Delivery Plan to remain below 330 incidents per annum:

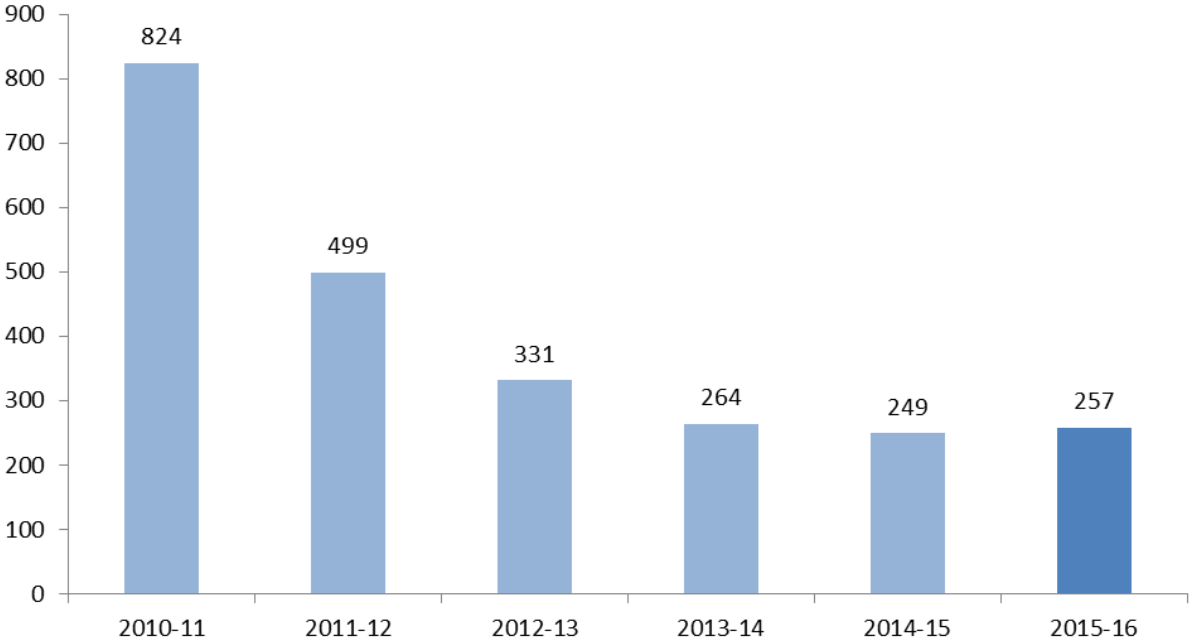


Figure 5 – Number of Environmental Pollution Incidents (Category 1-3)

Performance remained broadly steady during 2015/16 with a total of 260 Environmental Pollution Incidents reported. These include 3 category 1&2 water incidents, 10 category 1&2 waste water incidents and 247 waste water category 3 incidents.

With respect to water assets there were 3 Category 1&2 water pollution incidents reported in 2015/16, two of which were a result of inappropriate draw down of reservoirs by contractors working for Scottish Water.

Waste water sludge

Each year, we are required to submit a register detailing our activities in relation to sludge recycling to agricultural land. The register is based on a calendar year and reports each recycling event, the sludge volumes, quality and soil conditions of the receiving farmland to demonstrate that it contributes to the soil nutrient and organic condition. The 2015 register identifies that all recycling activities complied with the Sludge (Use in Agriculture) Regulations, which specify the safe levels of potential contaminants such as metals.

During 2015 we recycled 67,896 tonnes of sludge to agricultural land in full compliance with the Sludge (Use in Agriculture) Regulations 1989.

Unsatisfactory Intermittent Discharges

We continued to reduce the number of Unsatisfactory Intermittent Discharges (UIDs) on our sewerage network as a result of our investment programme during 2015/16, with the completion of a further 28 outputs.

Sewer Flooding

Reducing flooding from sewers is one of our customers' highest priorities and we have been making progress on delivering our commitment to address internal sewer flooding for those customers at highest risk, i.e. those customers with a 10% chance or greater per annum of being flooded internally.

We have started to address internal sewer flooding for those customers who have been on our register for over 4 years. Such flooding instances tend to be costly to resolve, such as the two-year project to tackle frequent severe sewer flooding in Elmvale Row, Glasgow, where 34 properties have experienced recurring problems with flooding for a number of years.

New problems continue to be found resulting in further additions to the internal sewer flooding register with 79 properties being added this year. 11 properties in Aberdeen were added to the register during 2015/16. We have identified a potential solution to mitigate the impact of further flooding to these properties and remove them from the register. A permanent solution to increase resilience further will require significant investment and implementation timescales to resolve. An emerging sewer flooding issue at a shopping centre in Greenock was confirmed resulting in 30 commercial properties being added to the register to reflect each individual unit in the shopping centre. We are continuing to work with Aberdeen City Council and Inverclyde Council to identify the appropriate long term solution to these and other drainage issues for delivery in future investment periods.

47 properties were removed from our internal sewer flooding in the last year and at 31 March 2016 the number of properties on our internal sewer flooding register was 334 (305 if the Greenock shopping centre was treated as one property). This is better than our expected range of 340 - 370 properties.

2.5 Capital Programme Delivery

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

In preparing for the 2015-21 investment programme, to implement the learning from investment delivery in SR10 and to deliver the stretching efficiencies that we committed to in our Delivery Plan, we put in place new investment planning and delivery arrangements. These arrangements included strengthened in-house investment planning capability and appointing three new delivery alliances.

Implementing this revised business model and tailored supply chain took longer to develop than originally anticipated and this impacted on our rate of investment delivery in the first half of the year. At the Output Monitoring Group during the year it was broadly accepted that the baselines for milestone delivery set in our 2015 Delivery Plan should be reviewed and reset. In agreement with the Output Monitoring Group and the Scottish Government, we have re-baselined our delivery profiles for the 2015-21 period. The assessment below is against these re-baselined profiles.

Investment

In the latter part of the year we have generated momentum in our investment delivery with investment increasing from £189 million in the first half of 2015/16 to a total of £482.6 million by the year end (£470 million in 2014/15). This comprised £382.7 million on Q&S4 projects and £99.9 million on completion (Q&S3b) projects.

The Overall Measure of Delivery (OMD) provides a high-level measure of progress in implementing the Q&S4 enhancement investment programme financed in the 2015-21 period and completing those Q&S3 projects planned to complete in the 2015-21 period. At the end of March 2016, our OMD score was 73 points².

Delivery of outputs in 2015/16 against the revised delivery profiles is show in the following three tables.

Objective	Quarterly monitored programme areas	2015/16 Year end Baseline	2015/16 Year end Actual	Total number of outputs over the regulatory period
Drinking water quality and reliability	Number of WTWs improved	No outputs planned to be delivered in 2015/16		28
	Number of zones made compliant with iron & manganese standards	No outputs planned to be delivered in 2015/16		88
	Number of improvements to reliability of supply (catchments and treatment)	0	2	47
	Number of improvements to reliability of supply (networks and storage)	0	1	82
	Distribution mains cleaned (km)	No outputs planned to be delivered in 2015/16		5,928
	Number of water quality etc studies to inform future periods	0	10	341
	2010-15 outputs planned to complete in the 2015-21 period	2	2	23
Drinking water security of supply	Water supply resilience strategy and improvements made	1	4	18
	Number of zones with improved security of supply (SOSI)	1	1	11
	Number of security measures and improvements to the infrastructure of critical reservoirs	0	3	689

Table 2.5.1: Drinking Water outputs

² When assessed against the original delivery profile, Scottish Water's OMD score would be 75 for March 2016, inside the original target range of 71 to 75.

Objective	Quarterly monitored programme areas	2015/16 Year end Baseline	2015/16 Year end Actual	Total number of outputs over the regulatory period
Protecting and enhancing the environment	Number of WWTWs improved to meet UWWTD	5	6	22
	Number of waste water networks improved to meet UWWTD	3	4	62
	Number of improvements required to meet UWWTD - Glasgow completion	21	24	94
	Number of improvements required to meet the Water Framework Directive	1	1	21
	Number of revised Bathing Waters Directive studies	No outputs planned to be delivered in 2015/16		7
	Number of environmental studies to inform future periods	No outputs planned to be delivered in 2015/16		131
	Number of improvements required by the Compliance Assessment Scheme; odour reduction and sludge management	6	10	38
	2010-15 outputs planned to complete in the 2015-21 period	1	7	16
Flood risk management	Reservoirs Act: improvements to dams	No outputs planned to be delivered in 2015/16		45
	Flood Risk Management Act: models and integrated catchment studies	No outputs planned to be delivered in 2015/16		218

Table 2.5.2: Environmental outputs

Objective	Quarterly monitored programme areas	2015/16 Year end Baseline	2015/16 Year end Actual	Total number of outputs over the regulatory period
Supporting economic development	Number of new connections to households and businesses	demand driven	15,098	56,500
	Delivery of new waste water capacity for 58,000 people	demand driven	1,351	58,000
	Number of first time non domestic meters installed	demand driven	4,069	18,000
	Number of wholesale meters	7,700	7,729	84,000
Climate change	Number of climate change vulnerability assessments	0	4	122
Long term cost of service	Improvements in renewable power and energy efficiency (GWh)	0.9	1.64	17.5

Table 2.5.3: Supporting Scotland's economy outputs

Scottish Water started the 2015-21 period with 37 projects from the previous programme which were due but not completed by March 2015. We have achieved regulatory sign-off for 22 of these projects against an original target of 28. A further 5 projects are now in supply and providing benefits to customers and 2 more are in commissioning trials. Scottish Water takes seriously the concerns raised by the Water Industry Commission and the quality regulators with the challenges that have occurred with the outstanding elements of our investment programme from the 2010-15 period. Where necessary we have put in place temporary mitigation measures pending the delivery of a permanent solution and will maintain a strong focus on delivering the remaining 15 projects to ensure that benefits to customers are delivered as soon as possible.

Community Engagement

Every day we carry out planned works in communities all across Scotland to maintain the levels of service to customers or to improve drinking water quality or the environment. Our work tends to involve street works or building which can have an impact not only on our customers lives, but the community overall.

In delivering our investment, we are implementing a new approach. ‘Communities at the Heart’ provides us with the opportunity to think through how our work could impact on the community, even before we start investigatory work, and to engage with the community well before we start any construction work to ensure that our plans accommodate their priorities and preferences.



Our approach includes community engagement materials that empathise with the community and their lives, such as the barrier signs we used at the sewer flooding work in Milnathort. We also focus on the way that we leave sites tidy and restored and, better still, if we can enhance the site or environment that we leave behind.



2.6 Wholesale Service

2015/16 has seen the Scottish competitive market continue to develop rapidly with licences granted to a further six Licensed Providers. This takes the total number of Licensed Providers operating in the retail market in Scotland to 23 and businesses have continued to switch Licensed Providers in significant numbers.

Scottish Water has participated in a number of cross-market initiatives:

Market data quality programme: The Central Market Authority (CMA) has run a project to match Supply Points to business premises recorded by the Scottish Assessors Association (SAA) in order to improve market data; this has identified a significant number of candidate gap sites. We continue to work with participating Licensed Providers to qualify these sites and, where appropriate, register them in the Central Systems. In addition to a project to process the candidates identified by the CMA, an on-going process has been established to pro-actively identify new gap sites (for example, arising from properties reconfigured by customers). The cost of the project and this on-going activity will be financed from the incremental revenue delivered by the initiative.

Following on from the CMA’s work, we initiated a further project with the objectives of improving market data quality, completing the matching of Supply Points to SAA data and facilitating changes in charging policy planned by the Scottish Government. The project is being implemented by Scottish Water under the governance of the CMA board.

Scottish Government Exemption Scheme: In August 2014 the Scottish Government announced a new Charitable Exemption Scheme to support Charities and Community Amateur Sports Clubs with the costs of water and sewerage charges from April 2015. The new scheme is simpler and fairer than the previous arrangements and opened for applications from January 2015. As at May 2016, 7,000 applications have been processed with over 3,000 charities and sports clubs now receiving exemption under the new scheme.

Public Sector switch: The contract for the public sector was awarded to Anglian Water Business (AWBS) and on 1 March 2016 24,000 supply points transferred successfully to AWBS.

Shared Supplies: During 2015/16 we have established a policy and process for working with Licensed Providers and customers to identify potential solutions to separate shared supplies so that, where feasible, customers are individually billed based on their metered consumption. Having completed a pilot, we have now initiated a project to review 1,800 potentially affected premises over the course of 2016/17. The potential costs of making physical changes to the supply arrangements are still being assessed as the number of properties completed is currently too low to confidently extrapolate from.

Service Levels: We completed 91% of Licensed Provider requested tasks within the required Operational Code or Disconnection Document KPIs in 2015/16, excluding tasks which had been delayed at customer or Licensed Providers' request. Performance remained high across many service areas but fell below the target level of 95%, predominantly due to our connections service and the focus on resolving process and system issues combined with the clearance of backlog activity. Recognising that the current KPIs focus solely on timeliness, a non-household Customer Experience Measure is also being developed to be monitored internally during 2016/17 prior to full launch in April 2017.

Developments to the Wholesale Service

In 2015/16 we developed our Licensed Provider Payment Security Policy to ensure a consistent approach with Licensed Providers across the market. This policy is now implemented.

Along with other market participants, we continue to engage in the Open Water programme and now MoSL, who are implementing the competitive market framework in England in 2017. We have participated in a series of Open Water, MoSL and OFWAT workshops and met with a number of English wholesalers over the last year to share our experience of water retail competition.

3. Expenditure, Performance and Efficiency

International Financial Reporting Standard (IFRS) financial results

Table 3.1 compares the results for Scottish Water's regulated activities to 31 March 2016 on an IFRS basis consistent with the presentation within Table M4 of the Regulatory Accounts for 2015/16.

£million	2015/16	2014/15	Change
Turnover	1,120.4	1,096.9	23.5
Operating costs	367.6	353.1	-14.5
PPP operating costs	112.9	112.1	-0.8
Infrastructure maintenance costs	118.6	136.2	17.6
Depreciation / amortisation	242.1	236.3	-5.8
PPP depreciation	18.9	18.1	-0.8
Gain on sale of assets	-14.7	-10.7	4.0
Total costs	845.4	845.1	-0.3
Operating surplus before interest	275.0	251.8	23.2
Finance costs - net	149.6	158.0	8.4
PPP interest charges	22.6	23.6	1.0
Regulated surplus before tax	102.8	70.2	32.6
Taxation credit/(charge)	21.3	-10.0	31.3
Surplus after tax	124.1	60.2	63.9

Table 3.1: IFRS financial results

The regulated surplus before tax in the year for Scottish Water was £102.8 million, £32.6 million higher than in 2014/15 (£70.2 million).

Revenue

Regulated revenue for the year totalled £1,120.4 million (2015: £1,096.9 million) and is analysed by category in Table 3.2 below:

£million	2015/16	2014/15	Change
Household	820.7	800.8	19.9
Wholesale	291.5	289.2	2.3
Other	8.2	6.9	1.3
Total regulated revenue	1,120.4	1,096.9	23.5

Table 3.2: Regulated revenue for 2015/16

Revenue from services supplied to household customers increased by £19.9 million or 2.5% to £820.7 million reflecting the 1.6% tariff increase effective from 1 April 2015 and the increase in properties connected to the network.

Revenue from wholesale services supplied to Licensed Providers increased by £2.3 million or 0.8% to £291.5 million reflecting the project to identify and bring into charge unregistered premises and an average tariff increase of 0.5%, partly offset by a reduction in consumption.

Revenue from other sales increased by £1.3 million to £8.2 million.

Total costs

Total costs increased by £0.3 million to £845.4 million (2015: £845.1 million).

Regulated operating costs at £367.6 million were 4.1% or £14.5 million higher than in 2014/15. The increase was primarily due to: a £15.1 million increase in local authority rates charges, reflecting the one-off refund received in 2014/15 (associated with the successful revaluation appeal) and the unwinding of an accrual in 2014/15 that was no longer required (associated with potential retrospective landfill tax charges) of £5.5 million. These variances were partially offset by a reduction of £7.0 million in the bad debt charge for 2015/16. After adjusting for these items, the increase in energy prices, carbon reduction charges and new operating costs associated with capital investment, like-for-like costs, decreased in real terms by 2.4% or £7.1 million. Table 3.3 below summarises this movement:

£million	2015/16	2014/15	(inc)/dec	%
Regulated operating costs	367.6	353.1	-14.5	-4.1%
Local Authority rates charges	-61.6	-46.5	15.1	
Landfill tax	-	5.5	5.5	
Carbon Reduction Charge & energy price	-5.7	-4.2	1.5	
Weather related costs	-0.8	-	0.8	
Bad debt charge	-12.8	-19.8	-7.0	
New operating costs	-2.6	-	2.6	
Like-for-like costs	284.1	288.1	4.0	1.4%
Average RPI inflation at 1.08%		3.1	3.1	
Like-for-like real controllable costs	284.1	291.2	7.1	2.4%

Table 3.3: Movement in regulated operating costs 2015/16

The increase in PPP costs of £0.8 million to £112.9 million was attributable to the annual indexation of service costs of £1.4 million and the higher volumes of waste being treated by the PFI schemes, partly offset by a £3.4 million non-compliance deduction applied to the operator of the Nigg PFI plant.

Infrastructure maintenance costs were £17.6 million lower than last year at £118.6 million reflecting the profile of maintenance expenditure in the 2010-15 regulatory period.

Depreciation, including PPP depreciation, increased by £6.6 million to £261.0 million due to the profile of the capital investment in the year. The gain on sale from asset disposals was £4.0 million higher than in 2014/15 at £14.7 million.

Finance costs

As at 31 March 2016, the weighted average interest cost of the outstanding long-term debt was 4.73%, (2015: 4.86%). Net interest payable during the year was £149.6 million, £8.4 million lower than in 2014/15. The finance costs total is net of the foreign exchange gain of £1.2 million (2015: £1.4 million loss) in respect of the forward Euro currency contracts.

PPP finance costs were £1.0 million lower at £22.6 million.

During the year, net debt decreased by £23.2 million to £3,055.7 million (being loans of £3,424.3 million less cash balances of £368.6 million). The decrease was driven by a £23.2 million increase in cash balances, with no net new borrowings from the Scottish Government.

Taxation

Scottish Water's tax credit was £21.3 million (2015: £10.0 million charge). Changes to the UK corporation tax system were announced in the Summer 2015 budget statement and substantively enacted prior to 31 March 2016. The main rate of corporation tax will reduce from 20% to 19% from 1 April 2017 and to 18% from 1 April 2020. Therefore, the re-measurement of deferred tax due to the reduction in the UK rate of corporation tax from 20% to 18% generated the majority of the tax credit in 2015/16.

Reconciliation of cash from Final Determination to Actual Results 2016

The closing cash balances forecast in the Final Determination for 31 March 2015 and 2016 were £265.0 million and £216.3 million respectively. Actual cash balances for the years were £345.4 million and £368.6 million respectively.

The £152.3 million increase in cash to 31 March 2016 compared to the Final Determination is summarised below in Table 3.4.

Closing Cash (£million)	2014/15	2015/16
Final Determination	265.0	216.3
Actual results	345.4	368.6
Difference	80.4	152.3
Generated during 2014/15		80.4
Generated during 2015/16		71.9
Timing differences	50.5	15.8
Available to support investment	29.9	56.1
	80.4	71.9

Table 3.4: Comparison of cash in 2015/16 to the Final Determination

£66.3 million of the increase in the cash position at 31 March 2016 relative to the Final Determination relates to timing differences that can be expected to reverse out over the remainder of the regulatory period. The increase in cash balances, excluding timing differences, of £86.0 million will be used to support investment delivery, including the Ayrshire Resilience Scheme, Strategic Mains diversions and the emerging risks for Daldowie and Dalarnock Waste Water Treatment Works, as set out in our 2016 Delivery Plan update and agreed by the Scottish Government.

Cash forecasts to 2021 continue to be in line with those presented in our 2016 Delivery Plan update.

4. Supporting Information

4.1 Research and Innovation

We recognise that innovation is key to sustaining high performance and delivering ever higher service standards. We continue to develop our strategic approach to research and development, accelerating the adoption of new technologies and developing a corporate culture that supports innovation in all areas of the business. We are also pursuing single topic issues such as leakage, sewer flooding and carbon reduction through the UKWIR programme.

Research engagement

A number of pilot plants have been developed and commissioned to translate academic findings and to explore new treatment technologies; such as evaluation of alternative polymeric and ceramic membranes and ion exchange processes for advanced organics removal. We are seeking to identify whether there could be significant performance and efficiency opportunities identified through these trials.

European research programme

We are taking part in collaborative bids for European Union (EU) funding through Horizon 2020 and INTERREG calls, whilst we continue to seek European partnerships through the EU Framework Programme that support our strategic aspirations. We are also finalising partnership agreements for an EU funded project where we will pilot test natural waste water treatment utilising worms. This will be deployed in Scotland at a trial site to understand the performance particularly in the extremes of a Scottish winter.

Innovation in action

We are already starting to see benefits from some key innovations we introduced in previous years. For example:

- conducting trials of Nereda to determine its applicability in waste water applications for Water Framework Directive compliance. This is now being considered in designs for works in the current investment period.
- delivering a new treatment works on Mull utilising an innovative modular packaged treatment system. This standardised approach is being developed further for application across Scotland.
- PoDDS (Prediction of Discolouration in Distribution Systems) models water quality in distribution systems allowing us to predict the optimum time and flows for flushing, minimising water quality disruption to customers and reducing the cost of our flushing programmes.
- commissioning our water innovation testing site at Gorthleck WTW and waste water testing site at Bo'Ness WWTW.

Scottish Water supported the successful 25th World Water Congress in May 2015, promoting Scottish Water across an international arena, in conjunction with the Scottish Government who hosted the event.

4.2 Board Changes

As at March 2016, the Scottish Water Board consisted of:

Chair

Lady Susan Rice CBE

Executive Directors

Douglas Millican - CEO

Alan P Scott – Finance Director

Peter Farrer – Chief Operating Officer

Geoff Aitkenhead – Executive Director of Capital Investment

Non-executive Directors

Alan Bryce

Lynne Peacock

James Spowart

Donald Emslie (until 31 March 2016)

Matt Smith OBE JP

Andrew Wyllie CBE

4.3 Executive Leadership Team

Geoff Aitkenhead, Executive Director Capital Investment, will be retiring from Scottish Water in July having served as an Executive Board member since the formation of Scottish Water. Mark Dickson, who is currently Director of Technology, Information and Business Change, will assume responsibility for capital investment leadership, and he will be succeeded by Rob Mustard.

4.4 Recognition

In 2015, Scottish Water was named as Scotland's Best Large Employer at the prestigious Business Insider awards.

Our commitment to achieving the highest levels of health and safety were recognised again when we were named as winner of the prestigious UK Water Industry Sector Award for Health and Safety 2016.

Our excellence in customer service saw us receive ServiceMark accreditation from the Institute of Customer Service during the year.

Our procurement procedures were described as world-class by the Chartered Institute of Procurement and Supply, who awarded us with platinum accreditation status.

In a report published in 2015, Investors in People Scotland praised our 'exceptionally strong commitment to employ and develop young people'. We are a Living Wage accredited employer and were one of the first public sector organisations to have been formally accredited as an Investor in Young People.

5. Looking forward

Our Delivery Plan for 2015-21 is ambitious and sets out to build on our success to date. Over the remainder of the regulatory period our focus remains on providing our customers a leading service while at the same time reducing their charges in real terms. We will seek to continue to drive up customer service, improve the quality of our drinking water we supply, minimise the impact of our discharges on the environment and outperform the challenging financial limits set out in the Final Determination 2014.

We were pleased to work with the Water Industry Commission for Scotland on developments to the approach for setting prices for 2015 to 2021. We look forward to working with the Water Industry Commission for Scotland and other stakeholders in determining the most effective way that customers remain at the heart of decision making in the water industry.

Appendix A: BOARD ASSURANCE STATEMENT

Annual Return 2015/16 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)

Date

1/4/16

CHIEF EXECUTIVE OFFICER

