ABSTRACT
This report sets out a proposed response to the Scottish Government consultation on the future development of Scottish Water as prepared by a member/officer group convened to consider the consultation document.

1 RECOMMENDATIONS

1.1 It is recommended that the committee agrees the proposed response to the consultation as attached to this report and instructs that this response be sent to the Scottish Government in accordance with the directions and timetable set out in the consultation document.

2 BACKGROUND

2.1 The committee will recall that at its meeting of 18 January 2011, it was agreed that a short life member/officer group should be convened to prepare a draft response to the Scottish Government’s consultation on the future development of Scottish Water. (Report No 47/11 refers). The consultation is sub-titled “Building a Hydro Nation – a Consultation” and requires a response no later than 9 March 2011.

2.2 The member/officer working group has now considered the consultation and has prepared a draft response for the consideration of the committee.

3 DETAIL

3.1 The consultation proposes some general principles for the future development of the business of Scottish Water and poses a series of questions (25 No) around the development and financing of that business. Much of the consultation is of specific interest to local authorities including in particular the delivery of the core services of Scottish Water and their role in drainage infrastructure and flood risk management as well as the provision of potable water and the appropriate treatment and disposal of sewage. A copy of the consultation document is provided with this report as Appendix 1.

3.2 Since the meeting of this committee on 18 January 2011 the member/officer group has been convened, considered the consultation in detail and has now prepared a draft response to the consultation including specific responses to each of the individual questions which have been posed. The committee is invited to consider the draft response as detailed in Appendix 2 to this report and it is recommended that the proposed response be agreed and forwarded to the Scottish Government in accordance with the timetable set out in the consultation document i.e. by 9 March 2011.

3.3 The committee may wish to note the following in particular:

The Scottish Government’s stated position is that:
- Scotland’s public water supply should never be privatised;
- Scottish Water should be enabled to evolve into a dynamic organisation able to exploit its expertise, assets and Scotland’s water resources to the fullest extent for the continuing benefit of water customers, the environment and the wider Scottish economy.
3.4 In preparing the draft response for the consideration of this committee the member/officer group has set down the following general views:

- while agreeing the objective which the government has set (stated in 3.3 above) the council is clear that Scottish Water should not be distracted from the efficient and effective delivery of their essential core services;

- there is significant scope for Scottish Water to make better use of their various assets and expertise and that there are potential commercial developments available in that regard;

- there is a significant issue in respect of the adoption of legacy sustainable drainage infrastructure which is causing an obstacle to economic development locally. This urgently needs addressed;

- Scottish Water should have a more active and integrated role in the management of flood risk and the development of flood management works, be it through partnership working with other agencies or otherwise;

- the proposal that Scottish Water raise funding to provide financial support to flood defence work, as set out in the consultation is strongly commended.

4 FINANCIAL IMPLICATIONS

4.1 There are no financial implications, either to the revenue or to the capital budget as a direct result of this report. Should any implications arise following the outcomes of the consultation these will be advised to the committee in due course.

5 HUMAN RIGHTS IMPLICATIONS

5.1 There are no human rights implications arising from this report.

6 EQUALITIES IMPLICATIONS

6.1 The issues contained in this report fall within an approved category that has been confirmed as exempt from an equalities perspective.

7 SINGLE OUTCOME AGREEMENT

7.1 This report contributes to the following local outcomes contained within the Single Outcome Agreement for Angus.

Our public services are high quality, continually improving, efficient and responsive to local people’s needs.

8 CONSULTATION

8.1 The Chief Executive, Director of Corporate Services, Head of Finance and the Head of Law and Administration were consulted in the preparation of this report.

9 CONCLUSION

9.1 The Scottish Government has issued a major consultation on the future development of Scottish Water. It is proposed that the draft response to the consultation as prepared by a short-life member/officer working group and provided in Appendix 2 to this report be approved by the committee and submitted to the Scottish Government by the deadline of 9 March 2011.

ERIC S LOWSON
NOTE

The background papers, as defined by Section 50D of the Local Government (Scotland) Act 1973 (other than any containing confidential or exempt information) which were relied on to any material extent in preparing the above report are:

- Report 47/11 – Scottish Government Consultation – “Building a Hydro Nation A Consultation” - Infrastructure Services Committee 18 January 2011
Q1 (Principles): Are the principles set out above the most appropriate to guide the development of Scottish Water into a wider role?

Comments:
The premise of the consultation and this question is that Scottish Water need to develop a wider role to enable it to play a ‘key role in the development of the hydro nation and evolve into a dynamic organisation, able to exploit its expertise, assets and Scotland’s water resources to the fullest extent for the continuing benefit of water customers, the environment and the wider Scottish economy’.

It is not considered that Scottish Water is performing all of its core functions comprehensively at present, for example in relation to cross-contamination from foul sewers, responses to planning authorities and in the appropriate development of SUDS. It is further considered that Scottish Water should have a stronger impact on sustainable economic growth than at present, which should be stated in Principle 1. In addition, the ‘essential services’ detailed in Principle 1 do not include Scottish Water’s duty, under the Sewerage (Scotland) Act 1968 to provide such public sewers as may be necessary for effectually draining its area of surface water i.e. as statutory drainage authority.
We believe that the primary priority should be in fulfilling the established core functions before diversifying as proposed. It is not evident that within existing resources these can be achieved satisfactorily.
In terms of Principle 2, commercial activities should support government purpose of “Sustainable Economic Growth”. Legacy of changing standards in SUDS is currently constraining “Sustainable Economic Growth” through delayed adoption which in turn impacts on road adoption which together impact on private sector commercial activity. We would like to ensure that focus on the core services is not lost or diluted.

In terms of Principles 3 and 4, it is generally considered that further consideration of the detailed proposals will be required albeit that the generality of these principles is valid and appropriate.

Whilst there are areas where Scottish Water may be able to exploit its expertise and assets to this end, particularly in terms of commercial activities, these would need to be suitably aligned to its expertise. Priority should be on sorting out the legacy of uncertainty that endures following Scottish Water’s succession from the three regional water authorities.

It is difficult to see how adding statutory functions to Scottish Water will lead to the development of a more dynamic enterprise. Whilst some changes to legislation may allow Scottish Water to diversify into other areas, the stated merits of ‘leaving
it to the Board and management of Scottish Water to identify the most appropriate opportunities and activities’ may be more aligned to the development of Scottish Water as a non-governmental, commercial entity. As a major player in provision of infrastructure which enable development SW needs to accept its responsibilities and to ensure that its role is clearly defined to remove uncertainties which constrain investment. Certainly SW should remain accountable to Scottish Ministers.

It is considered that, whilst Scottish Water have a major role to play in terms of the water environment, other organisations such as SEPA and Local Authorities also contribute to the wider issues.

In terms of Flood Risk Management, a major area identified in the consultation, it is questionable the degree to which Scottish Water have demonstrable expertise and resources to deliver comprehensively across this area. Sewer flooding is aligned to pluvial, fluvial, coastal and groundwater flooding, and many of these mechanisms interact to cause flooding incidents. However, they do require different skills and expertise to manage. Since the Scottish regional water authorities were formed, which subsequently amalgamated into Scottish Water, much of the broader drainage expertise in terms of flood risk has been dispersed between SEPA, Scottish Water, local authorities and private consultants. Given that one of Scottish Water’s core function, as defined in Section 25 of the Water Industry (Scotland) 2002 Act, is ‘to collect and treat wastewater’, Scottish Water in themselves are to an extent reliant on private sector consultants to deliver schemes, even relating directly to sewerage and their other core function ‘to deliver high quality drinking water’. There are significant differences with regard to flood risk management and the relevance of the sewerage networks between predominantly urban and predominantly rural catchments.

That said, expertise in all these areas of flood risk is not held exclusively within any single organisation, although councils retain significant local knowledge in regards to flood risk. To deliver Flood Risk Management functions, a combination of parties and sharing of expertise and skills through formal contractual arrangements, and both formal and informal partnerships, would be welcomed.

**Q2 (Developing Non-core):** *Does the proposed revision to Section 25 of the 2002 Act deliver the Government’s aim of making it certain that Scottish Water is able to utilise its assets and expertise in any way its sees fit for commercial and/or social benefit?*

**Comments:**

As stated in response to Question 1, whilst Scottish Water may be able to exploit its expertise and assets, the draft provision for clarifying Scottish Water’s existing powers, i.e. the ‘power to do anything that Scottish Water considers will assist in the development or exploitation of Scotland’s water resources or any of Scottish Water’s assets’, and as stated in the question as ‘any way it sees fit’ is considered to be too broad and needs to be clarified. This is particularly the case as the consultation does not propose that new duties for commercial activities are the subject of legislation.
Moreover, it is considered that the proposed revision fails in its aim to give clarity to Scottish Water as to its remit. It is generally considered that the drafting of the supplementary section 25 clause should be more explicit about what it is intended to facilitate. Exploitation of their resources is already permitted under the existing wording provided it “is not inconsistent with the economic, efficient and effective exercise of its core functions…” Instead, it is felt that attention should be directed towards clarification of the core duties where there appears to be some confusion within Scottish Water as alluded to elsewhere in our responses (Q8 and 10 refer).

What Scotland needs is a world class infrastructure provider where there are no constraints to development and all assets are working well. Care must be taken that it does not compromise the key purpose of Scottish Water. Scottish Water demonstrably has many strengths but it is considered that their basic remit should be met fully before extending into other sectors.

**Q3 (Developing Non-Core): Should Scottish Water be under an obligation to seek to develop commercially attractive opportunities?**

**Comments:**

Whilst Scottish Water should be enabled to pursue commercially attractive opportunities where such opportunities are not at risk of compromising its core functions and may reduce its dependence on public funding, there is a risk that making it an obligation could divert resource towards commercial return to the detriment of core functions.

It is therefore considered that the ‘broad objective’ that Scottish Water seek to add value year on year is more aligned to the development of an efficient business than to the objectives of developing a Hydro Nation. This objective should therefore describe the obligation for Scottish Water to seek to develop commercially attractive opportunities with a holistic view, including environmental and sustainability considerations, which can then be managed by the Board of Scottish Water.

**Q4 (New Functions):**

(a) Do you support the proposal that Scottish Water should work with the Scottish Government to identify areas where they may contribute to water-related international development activities?

(b) Should Scottish Water be asked to use part of their own resources to support the proposed water-related international development activities?

(c) If yes, should Scottish Water be given a statutory obligation to do so or should they take responsibility for deciding how best they can contribute resource and expertise?

**Comments:**

(a) Yes, Angus Council does support the proposal. The general principle of supporting humanitarian aid is laudable as is the principle of using profit from
commercial activity. Throughout history, Scotland has had a role in this and given the importance of water to all this should be endorsed.

(b) Yes. However, it is considered that sufficient resources should be available to ensure that the territorial requirements of Scottish Water are fully met before expanding outward. Angus Council supports the Government’s belief that such resources should come from the financial surpluses generated by Scottish Water’s commercial subsidiaries, and further believes that such resources must be sourced from commercial trading only.

(c) It is not considered that this should be made obligatory at this stage of Scottish Water’s development, but such an obligation may in time become a statutory duty. Scottish Water should not be distracted from delivering satisfactory performance of its core functions. There will be occasions where “charity begins at home” so it should be Scottish Water’s responsibility to decide how best they can contribute resource and expertise. This is about taking opportunities as they arise and can be accommodated.

Q5 (New Functions):

(a). Which areas of water science and innovation in Scotland could contribute to assist in the initiative, and how could this input best be achieved and organised?

(b). What role should Scottish Water play in any such Centre?

Comments:

(a) Scottish Centre of Expertise. With Angus being well located geographically between three of the major Scottish Water research establishments (Macaulay and both Dundee and Abertay Universities) and the area being well advanced with the collaborative South Esk Catchment Management Plan, the area could be regarded as having competitive advantage as a base for the Scottish Centre of Expertise.

As the current extreme weather conditions demonstrate, water management, in its widest sense, is likely to be of increasing importance in achieving “Sustainable Economic Growth” in coming generations. The impacts of weather conditions on water need to be understood, improvements made on predictive models e.g. (linking games technology with GIS advances) and documentation and application of best practice. For example frozen ground conditions linked to rapid thaw will result in flooding but conversely water locked in ice can lead to drought conditions for plants and animals. The expansion of water in its frozen state leads to untold damage to infrastructure with frozen pipes, cracked and deteriorating roads, damaged electrical cables etc. Although Scotland is well blessed with water resource, increasing climate extremes may increase the likelihood of droughts. It is considered that more could be done at catchment level to manage extremes more effectively, reducing potential impacts of both flood and drought. A practical approach to understanding such impacts and identifying and implementing design solutions is required.

(b) Scottish Water definitely has a role to play here along with Local Authorities, SNH, SEPA etc. It may well be appropriate that SW takes the lead in such a centre of excellence given in particular its geographical spread across the whole of Scotland.
Q6 (New Functions):
(a). What opportunities are there for creating additional public benefit from Scotland’s water infrastructure, both inland and maritime?
(b). What role could Scottish Water play?

Comments:
(a) This section of the consultation appears to relate only to canals when this question has much wider application. In reality Scottish Water retains many inland water reservoirs that could have considerable untapped potential for recreation. Understandably the primary concern for Scottish Water relates to maintaining water quality and human activity on and around these bodies of water could threaten this if improperly managed. If wider social/economic and environmental benefit is to be gained from such facilities then additional resource needs to be directed towards management best practice. Commercial return from recreational activity might be required to fund this.

(b) Scottish Water and other bodies have a role to play in developing proposals related to these opportunities for further consideration. As a land holding company etc it’s a question of establishing partnerships with other providers where joint benefit could be derived whilst ensuring that the water resource is not compromised. Nevertheless it is considered that there is significant potential for Scottish Water to make more of its extensive physical assets.

Q7 (New Functions): Should Scottish Water and Local Authorities be given powers to establish Partnership Boards to address the issues of surface water flooding and implement solutions?

Comments:
Partnerships of various statutory and other parties and sharing of expertise and skills in general are required to deliver Flood Risk Management functions particularly in areas where Scottish Water sewerage systems interact with surface water, coastal water, groundwater and roads drainage. It remains a concern to us the amount of sources of cross contamination of water bodies that remain including for example the abundance of uncontrolled storm water overflows. We would like to see these dealt with promptly. As summarised in the consultation document, ‘Scottish Water is responsible for the drainage of rainwater runoff from roofs and any paved ground surface within the property boundary. Local Authorities are responsible for the drainage of local roads and public highways.’ However, local authorities hold the general power to manage flood risk under the Flood Risk Management (Scotland) Act 2009 (FRMA2009). Formal powers and mechanisms to establish such Partnership Boards are therefore considered to be a positive step in terms of governance and also in terms of sharing expertise and skills. However, such powers would need to identify regulations and guidance to clearly identify the responsibilities and accountabilities of the parties, and also to provide some consistency in terms of flood risk. For example, at present there is no consistency between the levels of flood protection provided by a sewerage system (e.g. no surface water flooding for a 1in30 year event) and those applied to a flood prevention scheme (e.g. 1in200 year event). It is also considered that the power to establish such partnerships must not lead to confusion as to which
organisation holds the relevant statutory duties, e.g. Scottish water is the water supply and sewerage authority, and local authorities are the roads authority and flood prevention authority.

The example of the voluntary partnership of the Metropolitan Glasgow Surface Drainage Partnership is generally held up as an exemplar of good practice and is referenced in the consultation. This partnership model may be promoted as one to deliver integrated urban drainage, however, it is still not clear how accountable such partnerships are, what physical evidence and practical outputs there are from the MGSD to support such an approach, and how effective they will be in delivering projects in general and elsewhere in Scotland. In addition, in predominantly rural areas, the benefits of such partnerships may be less evident. It is therefore considered that a stronger statutory basis to deliver appropriate drainage plans and shared projects, specifically in urban areas, would be worthy of more detailed consideration. In particular, the interactions of pluvial, fluvial and coastal flooding merit further detailed consideration.

Q8 (New Functions): Could Scottish Water fulfil a proactive role in promoting the use of more sustainable urban drainage techniques for flood management?

Comments:
All organisations and agencies should have a proactive role in promoting sustainable use of water resources. The principle of good surface water management involving increased use of Sustainable Drainage Systems (SUDS) and surface water flow routes has been widely accepted. Notwithstanding this we would commend the realisation that such are not necessarily a universal panacea nor an immediate resolution of established problems or restrictions. Despite explicit provision in the Water Environment and Water Services (Scotland) Act 2003 for the vesting of sustainable urban drainage systems and publication of documents such as CIRIA’s SUDS Manual, Sewers for Scotland 2, and SUDS for Roads, the vesting of SUDS to Scottish Water, particularly involving “legacy” SUDS, and the processing of Section 7 agreements between Scottish Water and roads authorities remain problematic. Such recent and ongoing examples of where there appears to be disconnect between Scottish Water’s published support of SUDS and the practical challenges of having these vested. On this basis, it appears questionable if Scottish Water on their own could fulfil a proactive role in promoting the use of more sustainable urban drainage techniques for flood management. In the short term, it is considered by Angus Council that legacy SUDS and the broader implementation of Section 7 agreements is required. Once this is done and there is a body of evidence to show that Scottish Water are fulfilling their current core function, , it may be that by making such a role an explicit objective then Scottish Water would be in a clearer position to take on and successfully deliver such a broader role.

Q9 (New Functions): Is there a role for Scottish Water to be required to undertake urban surface water flooding studies that examine above and below ground drainage?

Comments:
Yes. As stated in response to earlier questions, partnerships of a combination of parties and sharing of expertise and skills are required to deliver Flood Risk Management functions in areas where Scottish Water sewerage systems interact with surface water, coastal water, groundwater and roads drainage, where the Local Authority is the statutory body. It is therefore considered that there is a role for Scottish Water to be required to undertake urban surface water flooding studies that examine above and below ground drainage, in partnership with Local Authorities. Scottish Water’s expertise in commissioning sewer modelling and urban drainage studies is often most beneficial to multi-agency interventions in urban environments. However, incompatibilities between the levels of flood protection provided by a sewerage system (e.g. no surface water flooding for a 1in30 year event) and those applied to a flood prevention scheme (e.g. 1in200 year event) would need to be formally resolved. In addition, the occurrence of cross-contamination from foul sewers to surface water systems and water bodies, and its impact on flooding events needs to be resolved.

**Q10 (New Functions): Are there further steps Scottish Water can take with respect to SUDS that provide flood management benefits?**

**Comments:**
Sustainable Urban drainage systems (SUDS) are promoted by Scottish Water and its predecessors but such systems mix responsibilities by combining roof and private ground run-off (Scottish Water’s responsibility) with roads drainage (Local Authority responsibility). Such drainage schemes implemented in the transitional periods between transfer of responsibilities between the old water authorities and Scottish Water remain contentious in terms of clearly defined responsibilities. Orchardbank Business Park in Forfar is an example of such a scheme. As a result of an ongoing dispute, not only has neither authority at this time accepted responsibility for the surface drainage but this in turn has delayed formal adoption of the roads system. While the joint developers, Angus Council and Hermiston Security continue to maintain both the surface water and the roads systems this is not only an unplanned drain on their resources but it is also having a detrimental impact on commercial business located on the park bringing adverse publicity and therefore potentially impacting on the ability to attract new private sector investment to the park. The legal wrangles regarding adoption of such schemes urgently need to be resolved otherwise it will act as a constraint to achieving “Sustainable Economic Growth”. The prospect remains of a proliferation of “orphaned” drainage schemes remains a real one. The opportunity should be taken to address this through this review.

Angus Council considers that the ability of Scottish Water to apply proportionate and appropriate decisions to the implementation of SUDS without significant input from others is restricted by a lack of specific local knowledge within Scottish Water.

**Q11 (New Functions): Would a greater role for Scottish Water in surface water flooding detract from the important role that planning authorities play in this area?**

**Comments:**
Where Scottish Water sewerage systems are the cause or contribute to surface water flood risk that affects development planning then these are adequately identified through the preparation of the strategic development plan and local development plan, which guides development decisions made by planning authorities, to which Scottish Water are a consultee. Consideration should though also be given to the important role that SEPA, the national agency, plays in this area.

Scottish Water also has a responsibility and opportunity to comment on planning applications as a statutory consultee in the planning process where a development is likely to require a material addition to or a material change in the services that it provides. Scottish Water therefore has a duty to provide advice to the planning authority where they are aware of surface water flooding that would impact on a development proposal. A clearer and more coordinated approach, which is perhaps being advocated, could only help and ensure that appropriate consideration is given to flooding issues. However, the reality for planning authorities is that such comments and advice is severely limited by a lack of local knowledge within Scottish Water.

Any studies undertaken by Scottish Water in relation to urban surface water flooding could be used to inform the development process. However, resolving the inconsistencies between the levels of flood protection provided by a sewerage system (e.g. no surface water flooding for a 1in30 year event) and those applied to a flood prevention scheme (e.g. 1in200 year event) would make the advice given and conditions applied to planning applications much clearer and understandable to applicants and the public.

Q12 (New Functions): Should Scottish water be given a stronger role in planning decisions that could affect surface water flooding?

Comments:
We believe that the performance of Scottish Water in terms of planning decisions and its engagement with the process could be improved within the regime that is already established. It is therefore considered that Scottish Water’s role in planning decisions that could affect surface water flooding should be strengthened by Scottish Water more consistently and regularly providing advice to the planning authority where they are aware of surface water flooding that would impact on a development proposal. As stated in response to Question 11 above, in practice this advice is severely limited by a lack of local knowledge within Scottish Water.

Q13 (New Functions): Should Scottish Water be given a formal role to support Local Authorities in relation to flood defence projects?

Comments:
It would be beneficial if Scottish Water were given a formal role to support Local Authorities in relation to flood alleviation projects where Scottish Water’s assets are affected by or are contributing to the flooding. This could be through the establishment of Partnership Boards as proposed elsewhere in the consultation. As stated earlier, the form of support would need to be clearly identified within the
partnership agreement to ensure accountability and governance by the organisation holding the relevant statutory duty, which in the case of flood defence projects would remain as the Local Authority. In addition, as stated in earlier responses, inconsistencies between the levels of flood protection provided by a sewerage system (e.g. no surface water flooding for a 1in30 year event) and those applied to a flood prevention scheme (e.g. 1in200 year event) would need to be formally resolved.

However, whilst Scottish Water may have extensive experience in procuring and managing large scale capital projects, it is not considered that this particular role necessarily be expanded in this area unless the Local Authority, which holds the relevant statutory duty, requires such assistance. This could be facilitated through the establishment of a formal partnership.

There remains an issue in the perceived application of the relevant statutory obligations and powers of both Scottish Water and the Local Authority’s in terms of the proper promotion of works where the effectiveness of a proposed scheme is dependent on works associated with Scottish Water apparatus. Although this may be achievable through the establishment of partnership working, this review presents the opportunity to reconsider the relevant legislation in this regard.

It is also essential that any further consideration of extending Scottish Water’s functions in relation to flood defence projects that the duties and powers on other bodies such as Local Authorities and SEPA are fully reviewed to ensure consistency and clarity (and prevent any conflict). In addition, clarity of intention and wording of guidance and legislation is required in terms of what are powers (may do) and what are duties (must do). This would remove any perception of an ‘opt-out’ in terms of Scottish Water’s support in flood defence projects. This may require further changes to a series of relatively recent major pieces of legislation.

Q14 (New Functions): Do you think Scottish Water should be given additional functions? Please give details.

Comments:
It is agreed that further consideration should be given to the extent to which it is appropriate for Scottish Water to contribute financially to the implementation of actions set out in flood risk management plans prepared by SEPA and local authorities. (see Q17) However, this would need to resolve the previously cited inconsistencies between the levels of flood protection required for sewerage systems and flood defence schemes as such actions may be beyond Scottish Water’s present responsibilities for surface water and standard of protection and sewer flooding.

It is considered that the benefits of Scottish Water being able to more readily support local authorities in relation to flood risk management plan actions and flood defence projects, and contribute to the funding of such projects through the Scottish Water charge review, requires further examination to draft appropriate provisions into the FRMA2009. It is agreed that the benefits of such a move would be to create greater certainty in the implementation of flood risk management plans and develop a greater integration on the ground between the activities of
Scottish Water and Local Authorities, recognising the need to manage the implications for local accountability and engagement.

**Q15 (New Functions):** What would be the most appropriate way to confer such functions on Scottish Water? For example it could be done on a statutory basis or through Ministers’ powers of directions. If it were done on a statutory basis, is it appropriate to extend Scottish Water’s core functions to include the additional functions or is it more appropriate to have separate legislative frameworks for the functions for water and sewerage (core functions) and any other functions?

**Comments:**
It is considered that separate legislative frameworks for the functions for water and sewerage (core functions) and any other functions that develop a greater integration on the ground between the activities of Scottish Water and Local Authorities be utilised for clarity of responsibilities, local accountability and engagement. Whilst these new functions are a development of a wider role for Scottish Water so that it is more able to exploit its expertise and assets, wider responsibilities for surface water and sewer flooding are separate from the core functions as defined in Section 25 of the Water Industry (Scotland) 2002 Act.

As stated in response to Question 13, it is also essential that in any further consideration of extending Scottish Water’s functions in relation to flood defence projects that the duties and powers are properly integrated with those of other bodies such as Local Authorities and SEPA and fully reviewed to ensure consistency and clarity (and to prevent any conflict). Clarity of intention and wording of guidance and legislation in terms of what are powers (may do) and what are duties (must do) is required. Angus Council would welcome clarity from the Government on the longer term plan for duties and powers of Local Authorities, SEPA, Scottish Water and SNH, and the proposed overlap of such duties and powers as proposed in this consultation.

**Q16 (Financing):** What is an appropriate balance for surpluses generated by Scottish Water and its subsidiaries between building up a financial buffer, developing Scottish Water’s commercial activities, financing social initiatives and being returned to Government to fund other priorities?

**Comments:**
As a general principle Scottish Water should be permitted to retain surpluses that it generates as an incentive to outperform, however the financial buffer should not be permitted to grow beyond that required to deal with reasonable risk (not easily defined).

It is considered that cash surpluses from within the Scottish Water business must be prioritised towards reducing development constraints to enable sustainable economic growth and used to fund other Government priorities, which might include initiatives that deliver social benefits. It is considered that some of these monies should be allocated to supporting local authorities in relation to flood risk management and funding contributions to flood defence projects and flood risk management plan actions (reference response to Question 13), as well as
offsetting the costs that Scottish Water will incur in taking on other responsibilities proposed in this consultation.

It is proposed that any surpluses gained from outperformance compared with the regulatory targets set for core water and sewerage business should be retained separately from surpluses generated from other subsidiary businesses. Any surpluses generated as a result of outperformance on water and sewerage should be applied to the following:

1. create and maintain a financial reserve at a proportion of net expenditure on core water and sewerage activities, which is commensurate with the expenditure and income risks to which Scottish Water is exposed; or
2. reduce borrowing either through utilising surpluses to reduce the net cost of capital projects or allow early repayment of debt to reduce overall borrowing.

In the event that Scottish Water are allocated responsibilities with regard to flood risk management then surpluses generated from main water and sewerage could be used to fund investment in flood risk management schemes. It is not Angus Council’s view that surpluses generated from main water and sewerage are used to fund investment in commercial activities, rather these should be reinvested in projects that deliver a social benefit to the residents of Scotland.

Q17 (Financing): Is it appropriate to ask water and sewerage customers to fund the costs arising from other activities such as flood defences?

Comments:
Angus Council agrees with the statement made in the consultation (section 6.3, paragraph 3), ‘Where customers receive a direct benefit, such as for flood defences, it might be appropriate to ask customers to pay for some of these additional functions.’ It is therefore considered that if Scottish Water’s functions are extended to include a role in Flood Risk Management then it is appropriate that a modest amount of customer charges should support borrowing of several hundreds of millions of pounds that could be spent on flood defence work, particularly where sewer flooding is the cause or a contributory factor in the need for such flood defence work. This would require to be applied on a national basis. Given the severe difficulties with regard to the raising of very significant capital sums by a local authority for such purposes within the current regime of Local Authority funding such a mechanism would allow vital infrastructure projects where these affect both Scottish Water infrastructure and Local Authority flood defence schemes to proceed timeously, which will save the misery and worry caused by flooding and support the wider economy. There would be an associated need to prioritise delivery of such schemes on a national basis but the FRMA facilitates such prioritisation in any case. We would strongly advocate that this possibility be fully explored.

In addition, the timeous delivery of effective flood prevention should reduce insurance premiums for customers and be of benefit to insurance companies through reduced claims. The formal endorsement of the insurance industry to support such a measure should be considered.
Q18 (Financing): Is it appropriate for customers to have part of their charges invested in commercial opportunities if they could receive the profits which flow from this investment in the form of lower bills in the future?

Comments:
It is considered that any investment in commercial opportunities should be funded from profits that Scottish Water makes through its commercial activities and not through the speculative investment of customer charges. Angus Council believe that there is an important distinction between private customers and industrial/commercial customers, which is not clear in the consultation proposals. It is Angus Council’s view that it would not be appropriate for domestic customers to incur an additional financial burden as a result of the failure of any of Scottish Water’s commercial activities. It is also considered that Scottish Water should not be distracted from delivering satisfactory performance of its core functions through such investments in commercial opportunities; and it is considered inappropriate for domestic customers to bear the risk of losses from commercial activities.

In the event that this route is pursued there would be a need for strict governance arrangements to be put in place to allow Scottish Water to demonstrate that any profits were being used to limit charge increases to domestic customers rather than simply being reinvested in commercial activities.

Q19 (Governance): In the light of the Government’s proposals to make best use of Scottish Water’s assets and expertise, would putting in place a more standard corporate structure, consisting of a holding entity controlling distinct and separate business units, enhance the governance of Scottish Water?

Comments:
The legal elements of the corporate structure of Scottish Water is considered to be beyond the scope of Angus Council’s response to the consultation, however, the governance issue is an area where Angus Council do wish to comment.

Scottish Water Solutions is an innovative joint venture partnership to support Scottish Water in the delivery of its Capital Investment Programme, and one of the biggest partnering agreements of its kind. Scottish Water Solutions work covers the whole of Scotland.
It is a limited liability company within a publicly owned organisation (Scottish Water is the majority owner with 51% of the shares). Much of the work carried out by in-house delivery partners and associate delivery partners. The amount of capital investment delivered or being delivered through this mechanism is approaching £2bn.
It is not clear to Angus Council how this procurement mechanism leads to the most efficient governance as Scottish Water Solutions are effectively selling services back to itself. Financial surpluses from almost half of Scottish Water’s Capital Investment Programme are therefore lost from the public purse. In addition, such a partnership leads to Chinese walls forming between the ‘client’ (Scottish Water) and the ‘supplier’ (Scottish Water Solutions) to avoid conflicts of interest in commercial terms and in decision making at an operational level. It is
therefore considered that improved governance may be achieved through the use of a more arms-length, not-for-profit organisation.

**Q20 (Governance):** In the light of the Government’s proposals to make best use of Scottish Water’s assets and expertise does the economic regulatory framework in the Scottish Water industry remain fit for purpose to or could it be strengthened?

**Comments:**

No comment.

**Q21 (Governance):** Are there lessons from the economic regulation of Scottish Water that could be applied successfully elsewhere in the public sector in Scotland?

**Comments:**

Scottish Water is regulated against an economic model that applies capital funding and objectives over a five year period. These objectives are set by Ministers through Directions (reference Section 2.2 of the consultation) and also require improvements in service standards in comparison with industry performance in England and Wales.

Local Authorities funding is dependent on the Comprehensive Spending Review cycle, which determines the Scottish block grant allocation and thereafter the Scottish Government’s determination of resources at an individual local authority level. The Scottish Government also sets specific efficiency targets for local authorities and achievement of these targets must be demonstrated annually in each Council’s annual efficiency statement. It is the Council’s view that these arrangements, along with Single Outcome Agreements set clear targets for efficiencies and service outcomes that guide the delivery of services. Given the current funding arrangements for local authorities it is difficult to see how the economic model applied to Scottish Water could be applied to other areas of the public sector, although the application of a longer funding cycle for capital investment in areas of Local Authorities responsibility is considered to merit further consideration to allow longer term planning and delivery of improved service standards.

**Q22 (Governance):** What barriers might there be to Scottish based firms competing in an English retail market and what steps can be taken to minimise these? In particular, should the aim be to have a single retail market covering the nondomestic sector in Scotland and England?

**Comments:**

The barriers to Scottish based firms competing in the English retail marker are purely physical or rather geographical. Angus Council agree that the aim should be to have a single retail market covering the nondomestic sector in Scotland and England.

**Q23 (Areas to Modernise):** Do respondents have any comments about the areas identified, or any others relating to the water environment, and the best way to modernise them?
Comments:
  No further comment.

Q24 (Building a Hydro Nation): How could Scotland best develop itself as a hydro nation and take a global lead on water governance?

Comments:
  Refer to response to Questions 4&5.

Q25 (Building a Hydro Nation): To what degree should the water centre for excellence, and our wider academic base, focus on providing educational services to the world and capacity building in the water sector?

Comments:
  Refer to response to Questions 4&5. In addition, Angus Council considers that the remit for the water centre of excellence should be concentrated on research and development into pragmatic solutions to water management issues in Scotland. In order to achieve this it will be necessary to learn from and to contribute to understanding of Best Practice throughout the world.