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Sir Jon Cunliffe
Chair
Independent Water Commission

Emailed to: cfe.water@defra.gov.uk

Dear Sir Jon

Scottish Water Response to the Independent Water Commission's Call for Evidence

Scottish Water was established as a public corporation by the Water Industry (Scotland) Act 2002. The Act made provision for the transfer of functions from three regional water authorities to a single publicly owned, independently regulated and commercially operated water company for Scotland. Each of these three pillars of the model are critical to the success of Scottish Water, which has gone from being the poorest performing company in the UK in 2002, to one of the top performers today.

We are the fifth largest water company in the UK in terms of customer numbers, serving 2.64 million households and supplying over 150,000 businesses; and the largest water company by land area, spanning around a third of the UK.

Notably, given the Commission's focus, Scottish Water has led the water sector in 4 consecutive waves of the UK Customer Satisfaction Index; is ranked first in relation to trust and reputation; and performs strongly amongst other utilities and businesses. In this, and in other dimensions of performance, significant progress has been made over the 23 years since Scottish Water was formed.

In responding to the Commission's Call for Evidence, we recognise that the ownership model of the water sector in England and Wales is not under consideration. We believe that, beyond the choice of ownership model, there are aspects of Scotland's approach to regulation and policy, Scottish Water's operating model, and the principles of Ethical Business Practice and Regulation (EBP&R) that frame how the sector in Scotland operates, that could be useful to reflect on as the Commission seeks to discharge its remit.

We recognise that many of the underlying long-term challenges the sector faces are common across the globe. We also work productively with colleagues across the UK on common risks and opportunities; and have an interest in being part of a wider UK water sector that is well-regarded, resilient and able to respond successfully to the challenges ahead.

Beyond these covering comments, we have sought to respond to the most relevant of the Commission's questions, following the word limits provided.

Yours faithfully

Wendy Kimpton
Director of Strategy and Regulation
Scottish Water

Scottish Water Consultation Response
April 2025

Independent Water Commission – Call for Evidence

	Strategic Direction for the Water Industry
20.	**What role do you believe the government can play in providing strategic direction for the water industry?** **By 'strategic direction' we mean, for example: the Strategic Policy Statement / the Strategic Priorities and Objectives Statement; Government targets (e.g. in the Environment Act 2021 and the Plan for Water in England only); the Price Review Forum (Wales only). This is not an exhaustive list. Please answer below:**

We consider that there is an important role for Government in overseeing strategic direction for the water sector.

In Scotland, this role is devolved at national level to Scottish Ministers who are accountable to the Scottish Parliament. The structure of Scotland's water sector is primarily provided for by the Water Industry (Scotland) Act 2002.

The main policy levers routinely exercised by the Scottish Government are the provisions in legislation for Ministers to set out Directions for Scottish Water and Principles of Charging in advance of each 6-year regulatory period.

These policy statements do not take detailed decisions or resolve trade-offs in specific cases, but they do provide a clear, simple and stable framework that is understood by Scottish Water, its regulators and wider sector stakeholders. They also set out areas where greater weight should be placed, which helps both the regulators and Scottish Water as trade-offs are made in the price review process.

The Ministerial Directions made in December 2020 included the new requirement for Scottish Water to lead work with partners, and engagement with customers and communities, to support the realisation of a Water Sector Vision for Scotland.

This Vision was co-created with regulators, customer representatives and government. It was adopted as an agreed, simple statement of the whole sector's shared ambition. Scottish Water has a leadership role, but the Vision extends well beyond the remit of the water company. It provides a simple frame of reference that supports innovation and collaboration to achieve common goals: written with a view to remaining relevant for decades rather than a single parliamentary term or price control period.

We believe the Vision plays an important role as a "North Star" that guides the work of the main sector stakeholders. It helps to retain the sense of there being a shared destination, even if there are inevitably differing views as to the best route to take.

Example: Collaboration to enable co-digestion at Nigg WWTW in Aberdeen
A successful trial was delivered in 2021/22, in partnership with the Scottish Environment Protection Agency, to allow residues from regional distillers and

brewers in the north-east of Scotland to be co-digested with sewage sludge at Aberdeen's Nigg Waste Water Treatment Works. This increased biogas production via the site's thermal hydrolysis plant, lifting the WWTW's ability to meet its own energy needs above 90% and saving the equivalent of 250 tonnes of carbon emissions per year. There were also significant benefits for brewers and distillers involved, via provision of a local destination for these residues, with reduced need for long-distance haulage. The trial, which has since been incorporated to the site's normal operation, was enabled by SEPA's willingness to support licence variation at a site which has had some historic challenges and potentially sensitive local stakeholders.

This outcome supports the Waster Sector Vision's commitment to innovate to support net zero (also flagged in the Ministerial Objectives), appropriate use of the planet's resources and economic prosperity.

21.	**What changes, if any, should be made to how the government provides strategic direction for the water industry?**

This is of course a matter primarily for colleagues in England and Wales. However, as we detail in our response to Question 20, the strategic direction the Scottish Ministers provide to the sector in Scotland (through the Ministerial Objectives and Commissioning Letter), along with the Water Sector Vision, are all important parts of the framework Scottish Water operates within. We believe this has worked well for Scotland.

23.	**What changes, if any, would help water companies to use planning frameworks more effectively to fulfil their duties and deliver their functions?** **Please answer and explain below.**

Scottish Water has benefited from clear policy direction from successive Governments over the 23 years since it was formed, with a high degree of stability, but also an ability to respond dynamically and in an agile way to emerging issues. We also benefit significantly from scrutiny and challenge from the Scottish Parliament, which also hears from regulators and a wide range of stakeholders.

We recognise that there can be challenges anticipating and responding promptly to growth needs in different regions, where there are significant uncertainties that are beyond water companies' (or others') control. Ministerial directions defining 'growth criteria' for domestic development have helped to enable a consistent approach to the timing of investment delivery in Scotland, while enabling planning of investment to take place earlier, in response to local authority-led development plans and strategy. The fact that Scotland does not have an "automatic right to connect" to the sewer system has also helped to support sustainable growth and supported more blue-green infrastructure solutions.

Where coordinated decision-making about public infrastructure investment can be achieved, for example at a city-region or regional level, it offers significant potential benefits for infrastructure providers and for growth.

A consistent governance framework to support this kind of collaboration could offer wider benefits – although the scope should extend beyond the water sector and consider how the funding needs of different infrastructure providers can be met in a more coordinated way to enable sustainable growth.

The same principle applies to support for the needs of new or growing industry, where coordinated spatial planning of energy and water infrastructure (at the UK level, and at national and regional level, building on the NESO model) could offer significant benefits – for example in enabling greater provision of renewable heat from waste water; sustainable use of final effluent for hydrogen production; or the production of sustainable aviation fuel from biosolids.

Example: Glasgow's Smart Canal
Via the wider framework provided by the Metropolitan Glasgow Strategic Drainage Partnership, the opportunity was identified to relieve drainage incapacity and enable growth in a significant area of North Glasgow using the capacity of the 18th century Forth & Clyde Canal system.

Close collaboration between Glasgow City Council, Scottish Water and Scottish Canals enabled funding to be assembled and preparatory work completed over a period of around 5 years, ahead of delivery between 2018 and 2020.

The scheme makes use of a specific regional opportunity to resolve a longstanding challenge in a different way, combining new technology with historic infrastructure. The water level in historic canal infrastructure is lowered ahead of forecast high rainfall, creating capacity for surface water from development sites to be stored. As a result, development of around 3,000 new homes has been enabled.

We believe this level of collaboration within the water sector and beyond could achieve similar success, with the right leadership and governance. Trusting relationships and willingness to work openly across established organisational boundaries are key.

	The Regulators
26.	**What changes, if any, do you consider are needed to the framework of water regulators to improve the regulation of the water industry?** **Please consider both potential benefits and costs of any proposed changes.** **Please answer and explain below, providing supporting examples or evidence, where possible.**

Although Scottish Water has a different ownership and operating model, there are clear similarities in the regulatory framework – with an economic regulator, a drinking water quality regulator, an environmental regulator and an organisation that represents broader consumer interests.

Generally, we consider that this structure works well, supported by the Water Sector Vision and the constructively challenging mindsets that exist across the regulatory

landscape. The level of engagement between Scottish Water and its regulators is far greater than we understand to be the case in England and Wales.

Ethical Business Regulation (EBR - C Hodges, 2016) has been central to the effective working of the regulatory model in Scotland. This draws upon research reflecting that better outcomes can be achieved by regulation which actively promotes a culture of openness and collaboration, based upon shared values, rather than being adversarial by default and liable to disincentivise transparency.

We consider that the proposed changes to water companies' articles of association, so that all companies are required to operate as Purposeful Companies, could provide a foundation for development of EBR in England and Wales.

The approach allows trade-offs between different regulatory interests to be discussed openly and understood. The specific challenges of Scotland (and of regions such as the Highlands and Islands) can be recognised and tailored solutions agreed. The dynamic and agile nature of EBR allows the system to adapt swiftly to changing circumstances – including crises such as the Covid-19 pandemic; and significant leadership changes across the main sector stakeholders. This, along with the willingness of all parties to respond to feedback, improves outcomes for customers and the environment.

For example, the 2021-27 price control process introduced significantly greater flexibility to investment planning to allow more responsive, collaborative decision-making throughout.

Current discussions about the next regulatory period anticipate an adjustment to provide a higher level of detail in long-term plans so that progress with delivery can be clearly understood, while retaining the benefits of appropriate flexibility.

Example: Improving Urban Waters
The Commission notes that environmental outcomes for Scottish Water appear to lag behind; however, there is a different context, with a generally improving water environment and 87% of water bodies assessed as having 'good' or better water quality by SEPA.

With respect to monitoring of combined sewer overflows, an earlier decision was taken in Scotland to invest in improved understanding via hydraulic modelling. This enabled interventions to improve discharges with the highest environmental risks, supporting the highest environmental benefits from a necessarily constrained budget.

EBR's dynamic approach has enabled us to respond to increased demand for monitoring, and evidence of the benefits this offers, with an additional £500 million investment programme via our Improving Urban Waters Routemap.

This was agreed in late 2021 after the SR21 process had concluded. As a result, monitoring of overflows in Scotland is expanding rapidly, while still targeting locations where there is significant environmental benefit (rather than aiming to monitor all overflows). This acknowledges the trade-off with other important investment needs and the affordability of water charges.

29.	**How do you think the Price Review process should balance the need to keep customer bills low with the need for infrastructure resilience? (Infrastructure resilience is the ability of an organisation's infrastructure, and the skills to run that infrastructure, to avoid, cope with, and recover from disruption in its performance).** **Please answer and explain below, providing supporting examples or evidence, where possible.**

As we set out above, the Price Review process in Scotland has sought to balance a focus on customer bills with infrastructure resilience, whilst being cognisant of the impacts on resilience from climate change, the need to replace ageing assets, respond to population change, and enable capital maintenance. The issue of intergenerational equity has also been to the fore. We think these are important elements for all economic regulators to consider.

30.	**What, if any, changes could be made to the Price Review process to better enable the water industry to deliver positive outcomes?** **Please answer and explain below, providing supporting examples or evidence, where possible.**

The contribution of customers to the process in Scotland has been supported by the establishment of an Independent Customer Group (ICG). We consider the ICG's work is important in protecting customers' interests and supporting trust, ensuring a customer voice in relatively complex, and sometimes technical, discussions - during the Price Review process, but also the work that takes place both before and after.

Previously a 'Customer Forum' was convened by the Water Industry Commission for Scotland to provide challenge on behalf of customers during the 6-yearly cycle of business planning.

From 2021, the ICG was established in a permanent form, hosted and supported by Scottish Water while remaining operationally independent. Its role is to ensure customers and communities are at the heart of Scottish Water's strategy and service delivery; investment priorities reflect customers' expectations of the sector; and charges represent value for money and are affordable.

The permanence of the ICG has allowed it to take a leadership role in a forum which co-designs the significant programme of customer research undertaken by Scottish Water or others. This research helps all stakeholders understand wider customer views and provides a strong evidence base for current and future decision-making about a wide range of issues and topics. The ICG is also able to provide scrutiny, challenge and insight about emerging issues and more routine business decision-making.

The requirement for water companies to establish and support Independent Customer Groups or Customer Panels with appropriate independence and remit could play a long-term role in restoring trust; as well as bringing a strong customer

perspective into the Price Review process with understanding of regional issues, opportunities and priorities.

Example: Sustainable Investment Decision-Making
Scottish Water has undertaken a comprehensive process redesign, to ensure all investment decisions are made on a long-term basis; and are evaluated through its Benefits Framework to make sure wider public benefits are considered. The ICG's involvement has been key throughout this redesign process, ensuring that technical expertise is balanced with customer and community expectations and priorities.

The Group has challenged the implementation of Scottish Water's new Asset Investment Planning and Management Tool, Copperleaf, to make sure customer priorities are not overshadowed by the best cost solution. The Group is also continuing to push us to identify Capital Investment projects in the pipeline where early engagement with communities about possible options could give them a stronger voice and opportunity to contribute to wider outcomes. This is expected to be particularly important in the wider deployment of nature-based solutions in public spaces, gardens or privately-owned land; as well as other initiatives that rely on customer participation.

	Investment
47.	**How does the public and political portrayal of water companies in the media and elsewhere affect the attractiveness of the water sector to investors?**

- Other

If you selected other, please specify below

Scottish Water is not best placed to comment on the attractiveness of the sector to investors, but the public and political portrayal of the sector is critically important: to companies' ability to attract and retain people with the right skills and commitment; and to work collaboratively with customers and stakeholders beyond the water sector. Like water companies in England and Wales, we need strong supply chain relationships, able to attract talented people; and partnerships with academic institutions and technology developers. All these dependencies would benefit from the collaborative development of a stable, long-term vision for the sector as a whole. Public trust in the way charges are set and collected is vital to the financial sustainability of the sector; the long-term investment that is needed; and the willingness of customers to contribute to the best outcomes. There is no complacency about the work needed to retain and build trust, but Scottish Water and the model we work within have performed well in research on this theme – monthly YouGov research within Scotland recording trust between 61% and 71% over the past year. The January 2025 UK Customer Satisfaction Index ranked Scottish Water as the most trusted water company and among the top performing utilities in the UK.

We welcome the Secretary of State's announcements on companies changing their Articles of Association (or licence) to reflect the wider social and environmental purpose of water companies, and believe this may help, alongside wider reforms to rebuild public trust in England and Wales.

	Innovation and Technology
65.	**To what extent does the overall water regulatory framework currently support or hinder innovation?**

- Somewhat supports innovation

66.	**Which of the following changes in the sector, if any, would enable innovation outcomes? (Please select all that apply)**

- Changes to the way companies and regulators approach risk (for example, introducing a regulatory 'sandboxing' tool)
- More outcome-based regulation to allow flexibility on delivery approaches
- Changes to the Price Review process to support innovation (for example, treating research and development spending separately in the Price Review)
- Other

If you selected other, please specify below:

Flexibility in delivery of business plans to allow space for the implementation phase of innovation.

Scottish Water participates in the Ofwat Innovation Fund and considers that it creates the impetus and funding needed to drive the exploratory stage of innovation projects. However, the "fixed" delivery approach of company business plans often doesn't incentivise or provide flexibility for the implementation stage. Unless an outcome of an innovation project results in business savings within the immediate regulatory period, companies may not benefit from investing in implementation. This stifles long-term progression, especially where the innovation project leads to new capability that enhances compliance or customer service objectives. Outcome-based regulation could address this, but the fixed 5-year regulatory period risks prioritising relatively short-term performance improvement.

Regulatory flexibility can have a wider role in enabling innovation that has potential to benefit customers and the environment. For example, we understand that Ofwat has a 3-hour interruption to supply measure that effectively excludes 'cure in place' lining technology in England and Wales. This technology could be used in Scotland under current arrangements, and has potential to bring benefits via faster and less disruptive water network repairs, but Scotland alone is too small a market to enable the market to invest in this capability.

There is a broader risk that initiatives like the Ofwat Innovation Fund support innovation, while other inflexible standards and policies stifle it (in the absence of a process to support their implementation).

67.	**What opportunities, if any, do new technologies present for companies and the regulators?** **Please answer and explain below, providing evidence and examples, where possible.**

The right technology at the right time presents huge opportunity. However, technology for technology's sake creates cost and inefficiency. Technology advancement either needs to respond to an unmet need or highlight a gap in capability.

A prominent example is combined sewer overflows, which have been designed into the sewer network for over 100 years. For a number of reasons, there has been a significant increase in public interest and concern about overflows, presenting the industry with an unmet need to be able to respond and bring about improvement. The right technology to manage sewer flows within the network to minimise discharge and, where necessary, treat overflows at a fraction of the cost of the currently available solution would present a huge opportunity.

Artificial Intelligence is a good example of a gap in capability. As generative language models such as Chat GPT and Co-Pilot develop there is the opportunity to drive productivity gains in administrative tasks. Advanced AI in decision support could potentially reduce the number of sensors required to control a treatment works or provide greater consistency in decision-making by learning from incidents and suggesting interventions to prevent them.

There is a widely recognised issue with Regulation 31 of The Water Supply (Water Quality) Regulations 2016, linked to a current lack of testing laboratory capacity in the UK. This slows the adoption process for new products and materials; and discourages new entrants due to the time and cost to reach the market. In this instance, the issue is less with the regulation than with the strategic infrastructure needed to enable it to be applied without unintended adverse consequences.