

# **FINANCE COMMITTEE**

Thursday 9 September 2004

Session 2

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## **FINANCE COMMITTEE**

### **21<sup>st</sup> Meeting 2004, Session 2**

#### **CONVENER**

\*Des McNulty (Clydebank and Milngavie) (Lab)

#### **DEPUTY CONVENER**

\*Fergus Ewing (Inverness East, Nairn and Lochaber) (SNP)

#### **COMMITTEE MEMBERS**

\*Ms Wendy Alexander (Paisley North) (Lab)

\*Mr Ted Brocklebank (Mid Scotland and Fife) (Con)

\*Kate Maclean (Dundee West) (Lab)

\*Jim Mather (Highlands and Islands) (SNP)

\*Dr Elaine Murray (Dumfries) (Lab)

\*Jeremy Purvis (Tweeddale, Ettrick and Lauderdale) (LD)

\*John Swinburne (Central Scotland) (SSCUP)

#### **COMMITTEE SUBSTITUTES**

Mr Adam Ingram (South of Scotland) (SNP)

Gordon Jackson (Glasgow Govan) (Lab)

David Mundell (South of Scotland) (Con)

Iain Smith (North East Fife) (LD)

\*attended

#### **THE FOLLOWING ALSO ATTENDED:**

Professor Arthur Midwinter (Adviser)

#### **THE FOLLOWING GAVE EVIDENCE:**

Eileen Baird (Strathclyde Fire Brigade)

Dr Jon Hargreaves (Scottish Water)

Stephen Hunter (Tayside Fire Brigade)

Ian McMillan (Scottish Water)

Douglas Millican (Scottish Water)

Dr John Simpson (Office of the Water Industry Commissioner)

Councillor Julie Sturrock (Dundee Council)

Alan Sutherland (Water Industry Commissioner)

Councillor Pat Watters (Convention of Scottish Local Authorities)

#### **CLERK TO THE COMMITTEE**

Susan Duffy

#### **SENIOR ASSISTANT CLERK**

Terry Shevlin

#### **ASSISTANT CLERK**

Emma Berry

#### **LOCATION**

Committee Room 2



## Scottish Parliament

### Finance Committee

*Thursday 9 September 2004*

[THE CONVENER *opened the meeting at 10:03*]

**The Convener (Des McNulty):** Good morning. I welcome members of the Finance Committee, the press and the public to probably the most magnificent of the committee rooms in the new Holyrood buildings.

I start with the familiar message to members to switch off their pagers and mobile phones. I think that guidance on the new audio system has been issued to members, but I remind you to put your cards into the console. The microphones will come on automatically; you will not need to press the request-to-speak button. I also remind members that there will be no electronic voting in committee.

I have received apologies from John Swinburne, who will be about half an hour late.

## Public Sector Jobs Relocation Debate

10:04

**The Convener:** As members know, on Wednesday 15 September there will be a debate in the chamber on the committee's report into the relocation of public sector jobs. I put the item on the agenda because the Executive has not yet sent a response to the committee's report. Paragraph 17 of the protocol between the Executive and committee clerks says:

"The Executive will determine the form of its responses to Committee Reports according to the nature and content of the Reports. The Executive will normally provide a response within 2 months of publication of the Report. Where a response will take longer than 2 months to prepare, the Executive will write to the Committee Convener or Clerk explaining the reasons and indicating the likely timetable."

The clerks asked the Executive for such a letter when it became apparent that we would not receive a response within two months of the publication of our report, but they received no reply. I therefore faxed the letter to the Deputy Minister for Finance and Public Services yesterday, asking for his urgent response. I have received a letter, which has been circulated to members this morning, in which the minister says that he intends to respond to the committee in advance of the debate on Wednesday. There is no clear indication of when we are likely to receive that response.

Members will have seen the proposed motion, which I sent round in the normal format. We should lodge the motion in order to facilitate the debate, but it is unsatisfactory that we have been left in a situation in which we have no response from the Executive. Members of the committee will obviously be concerned about that.

**Fergus Ewing (Inverness East, Nairn and Lochaber) (SNP):** It is good to be here.

Members who were in the chamber yesterday might recollect that I raised the matter as a point of order. The protocol that the convener quoted is absolutely clear in stating that when a committee of the Parliament produces a report—in this case, a substantial report that represents a major piece of work—the Executive should normally provide a response within two months. The Executive has not done so. The protocol also clearly states that if the Executive considers that it cannot meet that deadline, it should explain why it needs more than two months and provide a timetable. The Executive agreed the protocol and agreed to abide by those rules. However, the Executive has broken the rules—apparently, rules are for other people. Given that the Executive is in breach of

the rules, it is particularly unfortunate and rather more than unsatisfactory that Tavish Scott, the Deputy Minister for Finance and Public Services, has failed to say when we will receive the Executive's report.

The matter is not just about form or a technical breach. The point of having rules is to ensure that we have the Executive's response to the work of the Parliament before we debate the issues; the debate should be informed by the Executive's response. If we do not know what that response is, we do not have a proper debate or proper accountability, openness and transparency, which are the principles on which the Parliament is founded. It is a matter of sadness to me that we must begin our first meeting in the new building with the Executive being in breach of the rules. As for the letter from Tavish Scott, I would advise Mr Scott that, if one is making a plea in mitigation, it is best to start with a clear apology.

The minister should today state when we will get the response. In my view, the Executive should today provide the Parliament either with that response or with a complete explanation for the delay and the failure to comply with the rules to which it agreed.

**The Convener:** I should make it clear that the rules to which Fergus Ewing refers are guidance, rather than standing orders of the Parliament. However, I do not think that that takes anything away from the burden of what he suggests.

**Dr Elaine Murray (Dumfries) (Lab):** I concur with your suggestion, convener, that we go ahead and lodge the motion even though we have not had the response from the Executive.

I add my concern about the Executive's somewhat cavalier attitude. Obviously, people have been moving over this period, so there has been a certain amount of dislocation. That may be the reason why we have not received a response within the time suggested by the guidance. However, the fact that we have not suggests a somewhat cavalier attitude. I hope that it is not typical of the Executive's attitude towards its relocation policy, but I would certainly welcome a more substantive response.

I can understand why Tavish Scott felt that he had to get a response back to the committee quickly after the convener had faxed him a letter, but Fergus Ewing is right: it is not satisfactory just to be told that we will be getting a response before Wednesday. If it became apparent to the Executive that it was not going to be able—for whatever reasons—to adhere to the guidance, we should have had a letter at that point and that letter should have been a bit more apologetic. Even if the letter had just said, "Because of the move, we have been unable to get this piece of

work done," I think that we would have accepted that, but the fact that the issue was ignored is not satisfactory.

**Mr Ted Brocklebank (Mid Scotland and Fife)**

**(Con):** I agree. I have to say that the minister's response is cursory. He states "I regret", but there is nothing to suggest that he really regrets anything. The letter reminds me of the minister's response when we were discussing the whole relocation business in connection with Scottish Natural Heritage's move to Inverness; he said that, ultimately, ministers decide those matters. There appears to be an in-built arrogance in the responses from certain ministers. That is regrettable.

I believe that we should lodge the motion and press ahead, but I do not see why we should not also say to the Executive that, if it cannot come up with a response today, the debate should be postponed, because those of us who wish to speak in the debate next week would not have an adequate opportunity to take into account the Executive's response. If the Executive cannot come back to us today, the debate should be postponed to give us an adequate opportunity to get our arguments together in response to the Executive's arguments, so that we can do justice to the fairly hefty piece of work in which the committee is involved.

**Jim Mather (Highlands and Islands) (SNP):**

The postponement suggestion makes enormous sense. To a large extent, the committee is event driven and we are often given little notice to debate matters and take them forward. However, a lot of work has been done on the issue and it would be good for us to have the chance to get our heads round a substantive response from the Executive and to see it in context with the work that we have produced and the inputs that we have had from various enterprise agencies.

**Ms Wendy Alexander (Paisley North) (Lab):**

As has been alluded to, the guidance exists to ensure that the Parliament can fulfil its scrutiny role; when the guidance is not adhered to, we cannot fulfil our scrutiny role. The point of compelling, or seeking, a response within eight weeks is to allow the committee collectively to consider the Executive's views and, if need be, to respond in advance of the debate.

I concur with the suggestion that we should seek the advice of the Presiding Officer, because it seems to me that, when there is a debate on a committee report and the Executive has not adhered to the guidance, a point of principle is raised. The appropriate way forward on the debate—because clearly the business managers have agreed to the business—is to ask the Presiding Officer whether he is willing to take a view, in this and other cases, about whether the

guidance has to be adhered to before committee debates are held. Otherwise, we are into the dangerous territory that the Executive could presumably choose not to adhere to the guidance and not to publish a response until after a debate. That is an issue for the Presiding Officer, given that the business managers have already timetabled the business for the next couple of weeks. Perhaps the clerks could forthwith raise with the Presiding Officer the issue of principle that is at stake.

10:15

**The Convener:** I will draw together the strands of the discussion. It is generally agreed that we do not want to be in breach of practice by not lodging our motion. I think that we should lodge our motion. It is unfortunate that we have not had the response from the Executive, which might have informed what we say in our motion, but we will leave that to one side for the minute.

A view is coming from members of the committee that we should write to Tavish Scott to indicate that we are dissatisfied with the tone and content of his letter, in that it does not deal with the issue of the timetable or give us a clear indication of when we are likely to receive the Executive's response. A letter to the minister from the committee is required in response to his very brief letter.

I am not sure about the practicalities of postponing the debate. As far as I understand the matter, the debate on relocation is the next business in the chamber and I am not sure of the mechanisms for changing that. We should draw to the Presiding Officer's attention the position that the committee has found itself in as a result of the Executive's failure to respond in the appropriate way to our report. This is entirely the Executive's fault; it is not the committee's fault that we are in this situation. Do members agree that we take those three steps?

**Fergus Ewing:** Time is short. The debate is next Wednesday and, as members have said, a serious point of principle is at stake. Wendy Alexander's points seemed to me to be extremely well made, as were Ted Brocklebank's. We really need an answer now—this morning. The letter from Tavish Scott is, frankly, an insult. He must know when the response will be published; he must know whether it will be published today, tomorrow, Monday or Tuesday. If he does not know, the Executive is surely completely failing to comply with the parliamentary process and is treating Parliament with contempt.

I suggest that Mr Scott's office be called and that a response from the officials in his office be obtained before the end of the meeting to clarify

information that they obviously have and are withholding from Parliament. If we do not get a response by the end of the meeting, which obviously we should do, we must seek guidance urgently from the Presiding Officer, as Wendy Alexander suggested, about whether in the circumstances it is correct for Parliament to go ahead and debate a vital piece of work when the Executive has not complied with the rules. I hope that those two suggestions, which I have put forward in a constructive fashion, can be acceded to.

**The Convener:** We can certainly attempt to put forward a communication to Tavish Scott's office during the meeting, but I am not sure whether we can secure a response. Irrespective of that, we should seek guidance from the Presiding Officer along the lines that Wendy Alexander suggested.

**Fergus Ewing:** By the end of the meeting.

**The Convener:** I do not know whether we can get the information by the end of the meeting; that is not an issue. However, do we agree to the proposition that we lodge the motion, that we try to get information from Tavish Scott's office and that we seek guidance from the Presiding Officer? I agree with Fergus Ewing that we should try to get the information within the shortest possible timescale. I think that those are the steps that we can take.

**Ms Alexander:** I am genuinely sympathetic to what Fergus Ewing is trying to achieve, but it is possible that Tavish Scott is on a plane to Shetland. The critical issue that we need to resolve is the status of the guidelines. If they are breached and no timetable is placed on the Executive in which to produce a response prior to a parliamentary debate, we will be complicit in setting a precedent that none of us would wish to set.

I therefore think that the Presiding Officer is the person to whom we should take the dilemma. We should let the Presiding Officer clarify the parliamentary practice that he will observe when the Executive has not met its own guideline of eight weeks. The Presiding Officer may choose to give the Executive a further 24 hours, or he may say, "I am sorry, but if you have not met the eight-week guideline, I will not allow the parliamentary debate to go ahead until the committee has had the chance collectively to consider your response, whatever it might be."

The risk is that we set a principle in relation to what is properly a matter of parliamentary practice. We should ask the Presiding Officer urgently to consider the issue and to state his view. Therefore, instead of agreeing not to have the debate unless Tavish Scott responds by 4 o'clock today, it seems to me more important that the

Presiding Officer should clarify the procedure for this and all other circumstances in which a similar situation might arise.

**The Convener:** I see several heads nodding in agreement with Wendy Alexander's suggestion.

**Mr Brocklebank:** Is it possible to establish that during this part of today's meeting, rather than to carry on for two hours and then gently find that the Presiding Officer does not have time? Is it possible to establish urgently whether the Presiding Officer will take a view on the matter?

**The Convener:** The clerks will endeavour to take the matter forward urgently now, but Wendy Alexander is right that the speed with which the Presiding Officer can respond is not the issue. Our role is not to put pressure on the Presiding Officer but to refer the issue of principle to him so that he has the opportunity to respond in the correct way. Ultimately, it is for the Presiding Officer to adjudicate on all matters of scheduling and parliamentary business.

**Fergus Ewing:** Can we revisit the issue at the end of today's meeting, after the clerks have had an opportunity to seek responses from the office of the Deputy Minister for Finance and Public Services and from the office of the Presiding Officer?

**The Convener:** We should revisit the issue if there is further information to impart, but it will not be necessary to revisit it if there is nothing further to report. We are clear about our position and about what we want to happen.

**Mr Brocklebank:** There is an issue of principle, but what makes the issue much more acute on this occasion is that our committee's debate will be the very next item of business in the chamber. Whether or not there is an issue of principle, we urgently need to know whether we will get a response from the Executive to our report and whether there will be a debate next week. I would have thought that we needed to know that today.

**The Convener:** In our communication both with the Deputy Minister for Finance and Public Services and with the Presiding Officer, we can certainly highlight what we feel to be the urgency of the matter, but Wendy Alexander has correctly pointed out that the Presiding Officer would need to come to a decision on the issue of principle not just for this narrow instance but across the board. He needs to do that in the way that he sees as being best.

**Fergus Ewing:** Wendy Alexander is correct that the Presiding Officer must clarify the position. However, if I may say so, he went a long way towards doing so yesterday in his response to my point of order. As the protocol is a matter between the Executive and the Parliament rather than part

of standing orders, there is no basis for him to instruct the Executive to comply with the rules by which it agreed to abide. I doubt that, under standing orders, the Presiding Officer can do anything about the matter. We are in the position that the Parliament is powerless to compel the Executive to do its job and to comply with the guidelines to which it agreed.

As Ted Brocklebank pointed out, for the next piece of parliamentary business, the Executive will have flagrantly breached the rules and guidelines to which it agreed, but the Presiding Officer can do nothing about it. To proceed with the debate when Tavish Scott is cocking a snook at the Scottish Parliament seems to me to be a wholly reprehensible principle to establish on this, the first day of committee meetings in the new building. If Tavish Scott is around today—and if he has some gumption—he should come before the committee and explain himself. If he is not around today, before the end of today's meeting we should find out from his office what is going on. We should also confirm the position with the Presiding Officer before the end of the meeting. To do otherwise would be to allow the Parliament to be subverted by the Executive.

**Ms Alexander:** Fergus Ewing's suggestion gets close to the heart of the issue. As the Presiding Officer made clear, the matter is not covered by standing orders; it is an issue of parliamentary convention rather than of parliamentary rules. Sadly—or perhaps fortuitously—there is no Erskine May in the Scottish Parliament, so it is important that we ask that the Presiding Officer establish a convention that upholds the scrutiny function of the Parliament forthwith. That would be the single most important result that the committee, by using its collective powers, could achieve from this unfortunate set of circumstances.

We should not rush the Presiding Officer to a decision. I have every faith in George Reid. If he finds himself in the unfortunate position of being unable to change next Wednesday's business, I have little doubt that he will tell the Parliamentary Bureau on Tuesday that he wishes to establish a convention that will operate forthwith whereby scheduled business for which the eight-week guideline has not been observed will not be accepted. As I said, I have no doubt about George Reid's independence, but we need to give him the opportunity to think about the convention that he wishes to adopt in such circumstances. I have no doubt that, in considering the best way forward, he will uphold the place of the Parliament by turning what has hitherto been a guideline into something that he will invest with the authority of a parliamentary convention for business on the floor of the chamber.



**Dr Murray:** It is important that we have the Presiding Officer's response, but we must also bear in mind the fact that the timetable for business in the Parliament is established not by the Presiding Officer but elsewhere. How much influence can we have on rescheduling the debate at this late stage, given that the decision has been taken? I am not sure that any of us can answer that question. Another debate would need to be brought forward at very short notice in place of that debate and that would be very difficult.

**The Convener:** Ultimately, the committee cannot dictate what happens in the chamber. However, we can set out our position clearly in letters to the Deputy Minister for Finance and Public Services and to the Presiding Officer, from whom we have agreed to seek guidance. I will undertake to report back to the committee by the end of today's meeting what progress, if any, has been made on that. However, we will not have a further substantive debate today because our position as a committee is clear.

## **Fire (Scotland) Bill: Financial Memorandum**

10:27

**The Convener:** Agenda item 2 is consideration of the financial memorandum to the Fire (Scotland) Bill, which was introduced on 28 June 2004 by Cathy Jamieson. To help us consider the bill, we will take evidence from witnesses: Councillor Pat Watters, who is president of the Convention of Scottish Local Authorities; Councillor Julie Sturrock, who is from Dundee City Council; Stephen Hunter, who is fire-master for Tayside fire brigade; and Eileen Baird, who is from Strathclyde fire brigade.

We have also received written submissions from COSLA, Central Scotland fire brigade, Dumfries and Galloway fire brigade, Lothian and Borders fire board, the Scottish Ambulance Service, Strathclyde fire board and Tayside fire brigade. I have been asked to point out that the reference to tables in the "Control Room Arrangement" section of Central Scotland fire brigade's submission is to the tables on pages 62 and 68 of the Mott MacDonald report "The Future of Fire Service Control Rooms in Scotland". We have also received submissions from the Association of Chief Police Officers in Scotland and from Grampian fire board, which were circulated to members on Tuesday.

We will begin with a brief opening statement from COSLA. After that, members can ask questions.

**Councillor Pat Watters (Convention of Scottish Local Authorities):** My short opening statement will not go into the detail that is in our written submission. I thank the committee for this positive opportunity to ensure that the financial provision for the bill allows for a fire service that will serve the needs of the people of Scotland effectively.

It is important that the financial memorandum considers the possible impact that the bill will have on the fire service and how that will be dealt with. I must point out that there is no robust evidence for the belief that we can make the necessary changes without any financial consequences for the fire service. We believe that there will be financial consequences for the fire service and that we should build into the bill the ability to take care of them. We acknowledge the statement in the memorandum that the bill will give ministers new powers that they will exercise in particular ways, and the acknowledgement that those measures will give rise to additional costs, but that is not expanded on; it is just left there. I would like to see an acknowledgement that the overall policy

thrust of the bill and the changes to the fire-safety regime will have financial implications. What was meant has not been explained fully or properly in the memorandum.

This is an opportunity for us to get the measures right. I would like to see us proceed in a spirit of partnership so that we can ensure that we get things right. In the recent agreement that we reached with the trade unions in the industry, there was an acknowledgement that the modernisation process is not a cost-neutral exercise. The Executive acknowledged that by providing fire authorities with transitional funding over the period when there will be additional costs from the modernisation process. We have reached an agreement with the Executive about what that funding should be. We have a wee bit of a dispute about when it will be phased out, but I am sure that we will be able to work that out.

10:30

**The Convener:** What level of consultation took place with local authorities and COSLA about not just the policy issues but the important financial implications? We have experience of consultation having focused purely on the policy issues and of the financial issues not having been consulted on. Do you feel that there has been adequate consultation on the financial memorandum?

**Councillor Watters:** There are gaps in the memorandum; it does not explain fully the consequences of financial regulations. The bill proposes various changes that would have a financial impact. One that springs to mind is about charging for services and issuing fire certificates. There will be a loss of revenue from that change of about £200,000 throughout Scotland. The memorandum does not acknowledge that there could be increased demand as a result of the changes that are to be made. Although there is no cost for that, the servicing of the change could cost more than we provide for at present, at the same time as reducing income from charges. We have consulted authorities, which have concerns—I put it no stronger than that at present. They would like the Executive to agree that, if the legislative changes require additional finances, those finances should not come from the core service and additional money will come in to fund the changes. If we made progress with that, everyone would be happy.

We are happy with the consultation on the policy. We know why the changes are going to be made—we have to make changes to allow modernisation—but we do not think that enough work has been done to make clear the financial implications for the services that we are trying to provide.

**Mr Brocklebank:** In your submission, under “Core Duties”, you say:

“It is completely unacceptable that new burdens were not funded, we do not accept that they simply a formalisation of the role which the Service currently undertakes”.

Will you spell out to us a little more clearly where you think the Executive has not taken into account the extra costs, and do you have any idea of a figure for the extra sums for which you are looking?

**Councillor Watters:** I will bring in my colleague, Stephen Hunter.

**Stephen Hunter (Tayside Fire Brigade):** The bill sets out the core duties that we have been carrying out for many years, such as duties around road traffic accidents. There is an assumption that we have adequate funding to provide those services. One of the main areas in which there will be an increase in core duties is the statutory duty to deliver community fire safety. At present, brigades are not structured and do not have sufficient resources to be able to deliver that statutory duty. For many years, brigades have been involved with the community in trying to prevent fires and reduce the number of fire deaths and injuries. That has not been a statutory duty and has been funded from existing budgets. As a result of its becoming a statutory duty, brigades will have a much greater responsibility to have sufficient resources to deliver a much more effective community safety campaign.

**Mr Brocklebank:** Can you quantify that financially? How much more money do you think would be required?

**Stephen Hunter:** It is difficult to say how much more money would be required throughout Scotland. The modernisation agenda implies that through time—it is acknowledged that this would happen through time—resources will be able to be taken away from the emergency-response side and put into community fire safety, but that cannot happen until it is demonstrated that community fire-safety measures work. An injection of finance might be required to pump-prime the additional community fire-safety responsibilities and duties. Through time, that money might be able to taper off, because of the other results of modernisation of the service. However, at the moment it is difficult to quantify what each brigade in Scotland would require to deliver effectively the new statutory duty around community fire safety.

**Councillor Watters:** There is a lack of detail in the bill about what will be required in relation to fire safety that would allow us to evaluate properly the impact. We strongly support the drive to deliver fire safety, because we believe that the best way to tackle a fire is to prevent it. If we get the education process and working with the

community right, through time we will see a reduction in the number of fires. That work has to be done continually, because it is vital to maintain awareness in communities. However, there is not enough detail in the bill to allow us to say, "That will cost X"

**Mr Brocklebank:** You might be able to help the committee and me with a point in the submission from Dumfries and Galloway fire brigade. On appliance fuel, it says:

"The Service currently pays fuel tax at a standard rate. The opportunity should be taken to exempt the Fire Service from this in respect of special appliances."

That concession is already given in respect of hydraulic platforms. Will you explain that? At the moment, are you paying tax at standard rate on fuel for fire engines?

**Stephen Hunter:** Yes, we are paying fuel tax at standard rate.

**Mr Brocklebank:** So that is the element that you would like to be removed. You are happy to carry on paying the standard rate for fuel for your normal little vehicles that you go about in, but you believe, perhaps understandably, that fuel for the appliances that go and fight fire should not be taxed at that rate.

**Stephen Hunter:** Yes.

**Mr Brocklebank:** In financial terms, how much would that save and how much would it help you?

**Eileen Baird (Strathclyde Fire Brigade):** The reduced rate of tax is 65 per cent lower than the standard rate. At the moment, brigades throughout Scotland spend something like £1.5 million on their fuel budget. We could save up to 65 per cent on a fairly high proportion of that budget. That could be a good few hundred thousand pounds. I do not have the exact figures, so I do not know how much of that £1.5 million is spent on fuel for the emergency-response vehicles, but I imagine that it would be a high proportion, so there could be a significant saving for us.

**The Convener:** I draw us back to the bill.

**Dr Murray:** I want to follow up on the fuel issue. It is not within the Parliament's remit to change the duty on fuel or the exemption. Are you suggesting that the Executive should consider subsidising the cost of fuel, which is all that could be done from here?

**Stephen Hunter:** Because it is concerned with the financial implications of the bill, our submission asked the Scottish Executive to consider an issue that would reduce the financial burden on fire authorities.

**Dr Murray:** That is action that would be taken in Westminster and not in the Scottish Parliament. It

is not in the power of the Scottish Parliament to affect that, but it is obviously something about which representations could be made.

My main concern is about the control-room arrangements and the costs associated with them. The Executive is suggesting that if the fire service moves to one control room, rather than the existing eight, a saving of £3.3 million could be made. I suppose that, in a sense, I am sidestepping from the financial aspects of the bill to some of the more contentious issues around centralisation. My own fire brigade in Dumfries and Galloway has said in its submission that

"a large number of functions carried out by our Fire Control staff will not be transferred to any of the proposed recommendations if they are implemented. This will therefore require alternative arrangements to be made for the carrying out of such functions and the resultant requirement in maintaining staff costs for this to be carried out."

Can you put a figure on the additional costs on brigades of transferring some of the functions that will not go to a central control room?

**Councillor Watters:** It is difficult for us to comment on that. The Executive's proposals are still out for consultation. We have the issue on the agenda for discussion at our next leaders' meeting. I will ask Stephen Hunter to comment on the details, but I would certainly say that, although it would be physically possible to run the fire service from one control room, I do not believe that that would be a safe way of operating. We would at least need a back-up system in case of emergencies, such as a terrorist attack on the control room, so I do not believe that it would be right to have only one control room.

However, the proposal is still out for consultation and no decision is being taken at present. If we operate with fewer control rooms than we have at present, there must be a financial impact, but we do not have details about that, because we received the report from the Executive only a short time ago. We have put that report out to authorities for consultation and responses are now coming back in, and brigades have their own views as well. I believe that Stephen Hunter may be able to help you with the details.

**Stephen Hunter:** The report was a technical review, and although I believe that it is accepted that it is technically possible to reduce the number of controls, there is a whole host of issues on which COSLA, the fire authorities and other organisations are responding in the present consultation.

Although the report identifies savings from a technical perspective, there are other areas that must be taken into account. For instance, there are important people issues in relation to the control centres, and a reduction from eight

controls to any of the numbers proposed by the report—one, two or three—does not automatically mean that there would be a saving. Having three controls would not automatically mean a saving on the five controls that had been done away with, because if there was a reduction, the current controls would not have the capacity to take over the work of the other brigades' controls, so there would have to be capital investment in infrastructure. People issues such as redundancy payments and redeployment of personnel into other areas were not fully explored in the report, so the financial savings included in the responses that the Executive will receive may not be as large as those quoted in the report.

**Dr Murray:** The report from the Dumfries and Galloway fire brigade appeared to suggest that there are some things that are currently done in the fire control room in Dumfries and Galloway that would remain in Dumfries and Galloway and would not be handled under the new arrangements. Therefore, there would be a cost to the brigade in taking over those functions.

I am a little bit concerned that, because the bill is still out for consultation, it is difficult for us to assess the financial implications. Because we do not know the shape and structure of what is being proposed, we do not know whether the savings that it is claimed could be made will in fact be made, or whether there will be additional costs on brigades that have not yet been quantified.

**The Convener:** That is a general issue that we might need to raise next week in our consideration of the issues that arose out of our away day.

10:45

**Jim Mather:** I want to follow up on the answers that Stephen Hunter gave a moment ago and I want to ask about the potential hidden costs of centralisation of control rooms in regard to the loss of local knowledge. There could be situations in which the similarity of place names in some parts of Scotland could lead to slow responses and worse damage. In the long term, that would result in higher insurance costs, to say nothing of the costs of damage to council tax payers and business rate payers. Beyond that, there is the possibility of negligence claims coming home to roost. There is also the possibility that there could be more hoax calls, with a centralised control room less able to differentiate between the real and the hoax. Have the witnesses anything to say about that?

**The Convener:** I think that we are drifting towards policy rather than concentrating on financial issues.

**Jim Mather:** I think that those issues could have bigger financial implications than making the change would have.

**Stephen Hunter:** In answer to Mr Mather's question, I would say that, as well as the financial costs of the centralisation of fire controls, we must consider the cost to society of any potential changes. There is not just a potential financial saving to the fire service; as Mr Mather outlined, there might be additional burdens on other areas of society as a result of the changes. That is why, at the end of the consultation, we will have to see the outcome of the Executive's consideration of what those issues might be.

**Jim Mather:** At the end of the day, what we need is an absolutely clear statement of the financial situation. We might even require some external skills to put the issue properly in context and to assess the net effect on Scotland of such a change.

**Jeremy Purvis (Tweeddale, Ettrick and Lauderdale) (LD):** My question is still on control rooms, I am afraid, but it comes from a slightly different angle, which was highlighted when I spent quite a few hours at the force communications centre of Lothian and Borders police in Bilston. I know that different forces are involved, but the work that COSLA will be doing with the authorities could include considering not only the efficiency savings and the assumptions about costs, but where the control rooms are located and what co-ordination there could be with the other emergency services, so that there could be sharing of technology platforms. Will you be considering those aspects as part of the consultation process? Rather than just the bare costs of the number of control rooms, perhaps we should consider the type of control rooms and their relationship with other services.

**Councillor Watters:** You are absolutely right; there is a governance issue there. At present, each individual brigade is responsible for its control room. With a smaller number of control rooms, there will be a governance issue with regard to who is responsible for the control rooms and who they are answerable to, and that has not been considered or worked out either. As you would expect, I am firmly of the belief that fire protection is a vital local service that is provided by local government. As such, the reshaping of any part of the organisation must be firmly within local government, so that we have control over the services that we are providing and for which we are responsible. You would expect me to say that, so I am not disappointing members of the committee by saying it.

**Stephen Hunter:** The consultants' report considered a number of options: keeping the status quo, with eight fire controls; having some fire controls merge with other fire controls; and having fire controls merge with other emergency service controls. The outcome of the consultants'

investigation was that the preferred option would be amalgamation of fire controls with other fire controls. The consultants' report rules out the amalgamation of fire controls with other emergency service controls, and it gives reasons for ruling out that option.

**Jeremy Purvis:** I was struck by the technology that the police have, with global positioning systems to identify every fire hydrant in the force area—or at least they have that in my constituency. That is not information that Lothian and Borders fire brigade has. On issues such as that, constituents are looking not only for efficiencies but for practicalities, but I appreciate that developing those practicalities is part of an on-going process.

**Stephen Hunter:** Another project mentioned in the bill is the firelink airwave project, which is a complete change to the radio system used by the fire service, following the changes made to the police service radio systems. Some of the issues concerning the electronic information that is available to fire personnel on the ground and at controls will be addressed as a result of the transition to the new airwave system.

**Jeremy Purvis:** Can any of our witnesses comment on the written evidence that we received from the Central Scotland fire brigade? Speaking about the proposed common fire services agency, it said:

"No costs are identified for this although, if implemented, this may represent an additional layer of management for the service".

What might the costs of that extra layer of management be?

**Councillor Watters:** It is difficult for us to answer that. The brigades submitted their responses directly to the Executive. We have not had sight of their responses to the consultation exercise.

**Jeremy Purvis:** Convener, could we ask Central Scotland fire brigade for more information on that point?

**The Convener:** We certainly could.

**Councillor Watters:** Councillor Sturrock would like to say something about the point that was being made earlier on.

**Councillor Julie Sturrock (Dundee Council):** The consultants might have said that they would regard more collaboration among police, fire and other agencies on a local basis to be less preferable than collaboration on a national basis among various fire brigades, but that is not necessarily COSLA's point of view. From our community planning perspective, local collaboration is the most obvious approach, and it

is perhaps the most directly accountable process. We are already co-operating locally on purchasing. Many of the suggestions for best-value projects, such as joint procurement for items other than fire equipment, are already taking place—office supplies, paper and so on are already being procured on a co-operative local best-value basis. The fact that the consultants have not voiced that as their preference does not mean that COSLA does not prefer that option. We have yet to reach a decision in that regard.

On the cost-effectiveness of the extra layer of management that you mentioned, COSLA's point of view has always been that we want to deliver obvious accountability. We want a local service that can be held to account by local agencies. There is another element beyond the financial aspect. I suggest that, if the financial aspect can be seen as being negative, other aspects could also be seen to be negative.

**Jeremy Purvis:** Beyond the financial aspect, there are a lot of policy issues. Given what I have seen of the force communications centre in my constituency and the need for local knowledge, which Jim Mather touched on, I hope that you are actively considering the issues that have been raised. As Pat Watters said, local accountability is vital.

Earlier, Ted Brocklebank asked Councillor Watters about COSLA's written evidence, which says:

"It is completely unacceptable that new burdens were not funded."

One of the examples of that related to fire-safety functions. I know that the officers in the Galashiels office in my constituency view fire-safety functions as being an automatic part of their work in the local community. I would be interested to know whether huge costs will be associated with doing what the bill will require to be done under statute—not any additional work that might not be rewarded but the work that officers currently do as members of the local community in responding to ad hoc requests and providing information, publicity and encouragement in respect of the steps to be taken to prevent death or injury by fire.

Basically, I am challenging whether there will be a significant level of additional cost. The words that I quoted from your submission are fairly strong, but I recall that you gave only the example of fire-safety functions. Are there other new burdens that will not be funded?

**Councillor Watters:** We are clear that the responsibility for legislation lies with the Scottish Parliament and the Executive. When legislation is introduced, its impact has to be considered. As local politicians, we have priorities that we have been elected to deal with and we do not think that

we should be expected to shelve some of our priorities, which the electorate expects us to deliver, to deliver priorities that have been set elsewhere, even if those priorities are shared ones. Community safety is a shared priority, of course, and I absolutely agree that the natural place for that to be dealt with is in the fire service—those people are the natural people to do the job. However, there is a difference between having community safety as a responsibility that we take on and it being a statutory responsibility that we have to deliver. If it is a statutory responsibility, we must ensure that the resources are there to allow us to carry it out. When something becomes a responsibility under statute, the expectation becomes higher.

Firefighters throughout Scotland are carrying out community fire-safety work at the present time, but it is not their main responsibility. Under statute, the delivery of community fire-safety measures will become one of their main responsibilities.

Stephen Hunter is better versed in these matters, as he deals with them every day.

**Stephen Hunter:** Legislative fire safety has been a statutory duty for fire authorities for more than 30 years and much progress has been made on safety since the passing of the Fire Precautions Act 1971. Community fire safety is about making people far more safe in their homes. Although, as has been said, all fire brigades in Scotland have been involved in that process, the statutory duty will mean that community fire safety will have to be delivered in a far more structured and auditable manner in order to measure the benefits that are accruing to the community as a result of the work that is taking place.

**Jeremy Purvis:** As I said, the submission uses strong language when it says:

“It is completely unacceptable that new burdens were not funded.”

However, all that you have mentioned so far is the fire safety element, which takes up officers’ time as they have to attend events—such as the recent “Safe T in the Park” event in Kelso and community council meetings—and have to produce leaflets. That does not warrant the strong language that is used in the submission. We are talking about £150,000 out of a Scottish budget of £23 billion.

**The Convener:** The view that is expressed in the submission in this instance might well be an illustration of the general view of COSLA across the board. Would it be fair to say that, Councillor Watters?

**Councillor Watters:** Yes, as a general point. I would say that £150,000 out of the national budget is fine, as long as that money is going to be spent

on only one area. However, if £150,000 is to be spent on everything, that will have an impact.

Another point that we make in our submission is that, under the additional investment for the tackling of major disasters, around £8 million was invested in new equipment and a further £3 million is to be invested in the fire service. However, as well as that £11 million investment for new equipment that will allow the fire service to tackle the sort of things that happen these days, there will also need to be investment to cover the on-going revenue costs to support that equipment on a day-to-day basis. Having the capital investment to purchase equipment is one thing; having the staff and resources to ensure that the equipment can be used is an entirely different matter.

I think that “burdens” is not the word that we are supposed to use and that “opportunities” is perhaps better. The opportunity to deliver a better service can be taken advantage of only if the resources to enable people to do so are also present.

11:00

**Councillor Sturrock:** The point is that under the proposed legislation the minister has sweeping powers to make many financial decisions that will have a knock-on effect on the fire service. For instance, although the bill contains requirements on the purchase of equipment and what have you that will have on-going effects on revenue, it does not contain any obligation to make available appropriate finances to meet those requirements and on-going expenses.

**The Convener:** I will try and draw this item to a close with questions from Ted Brocklebank and myself.

**Mr Brocklebank:** I want to clarify the point that Jeremy Purvis was trying to elicit. On fire safety, Dumfries and Galloway fire brigade’s submission says:

“It is anticipated that we will be required to provide funding for local advertising campaigns and PR activities.”

The brigade then makes a certain link when it goes on to say:

“The Bill proposes the removal of the need for fire certification. In consequence, we anticipate a reduction in income as a result of this.”

Will you tell us the amount of money that you receive for fire certification and, therefore, the sums that you will have to raise to pay for the advertising and public relations that you say will be required?

**Councillor Watters:** I have two points in response to that question. In an exercise that we carried out with one fire brigade, we came up with

a figure on which we based an estimate for the rest of the brigades. We believe that about £200,000 in income would not be available at that particular point.

However, we should remember that, under the proposed arrangements, there will be self-certification on advice and that the advertising that we will put out will generate more input into the fire service than we receive under the current system of certification. After all, we currently do not charge for advice.

**Stephen Hunter:** At the moment, brigades have a structure for inspecting premises that need a fire certificate. Because that process has been in place for 30 years, each brigade knows the resources that need to be applied to that activity. As Councillor Watters has pointed out, after the need for fire certification is removed, we will lose £200,000. We cannot predict the activity levels for the provision of advice; however, it is likely that after an advertising campaign occupiers and owners of commercial and industrial properties will want to take the fire service's advice which, up to now, has always been given free of charge.

**The Convener:** Fergus Ewing will ask a brief question.

**Fergus Ewing:** I apologise to witnesses for being unavoidably detained elsewhere earlier.

I want to ask about auxiliaries and volunteers who assist full-time and retained firefighters. They play a vital role in the Highlands, and in my constituency of Inverness East, Nairn and Lochaber, with regard to forest fires, muirburn and serious road traffic accidents. Although those people are part of the fabric of the community and have traditionally played an absolutely essential role, their ability to continue to operate is under threat because of the interpretation of the rules on breathing apparatus. Such apparatus has to be made available to volunteers who assist in fighting fires inside a building; however, housing that equipment is an expensive business and it has been suggested that each auxiliary service—which there are more than 100—will need a major building to do so. That is threatening the viability of more than 30 auxiliary services in the Highlands.

I note that the bill seeks to provide for a process of integrated risk assessment and to impose a duty on employers to provide for the safety of employees. However, as far as I can see, the financial memorandum contains no provision for the implications of the risk assessment process for the future of auxiliaries and volunteers. Do you feel that the memorandum might have any implications that the Executive has not provided for?

Finally, do you agree that it is essential that we continue to have the benefit of those who

volunteer and who play such a useful role in their communities in the Highlands of Scotland?

**The Convener:** I think that the last part of that question was really more about a policy issue than about the financial memorandum. However, I appreciate why Fergus Ewing wants to raise it.

I will add the question that I was going to ask to Fergus Ewing's question on volunteers. Given that he has just mentioned integrated risk management plans, do you have any general comments on the effect of such plans on the formula that is currently used for funding calculations for the fire services? After all, this is clearly an all-Scotland issue that affects urban and rural areas.

**Councillor Watters:** One of the main planks of fire service modernisation is the integrated risk management plan, under which one will assess needs on an on-going basis. Even the Executive acknowledges that we will have to see how the plan operates over a period of time before we can appreciate whether it will generate savings or additional costs.

The whole point about modernising the service is not necessarily to have a cheaper service, but to have an improved service that is fit for this century. After all, although the integrated risk management plan will undoubtedly generate savings for the people of Scotland, they might not be financial ones. For example, more lives might be saved. Moreover, the plan might have an effect on property and on the national health service, which might not have to deal with such serious burdens.

As I have said, implementing the plan might have many pluses and benefits but we will have to see it in operation before we can assess its impact or any implications that it might have. Indeed, the Bain report makes it clear that implementing the integrated risk management plan will have not just financial impacts for the whole community.

As for Fergus Ewing's point, I should point out that more than one brigade of volunteers and auxiliaries act as a link in providing the whole service in a community. However, his question is very specific to that particular area of the service and I am not sure whether Stephen Hunter or I can answer it.

**The Convener:** We will accept written answers to our questions.

**Stephen Hunter:** Elaborating slightly on the point that Fergus Ewing raised, I should say that Highlands and Islands has far more auxiliaries and volunteers than any other brigade in Scotland. We are greatly concerned about the remoteness of such areas from retained and whole-time fire stations.

The issue of breathing apparatus is linked to other legislative requirements to ensure firefighter safety that are contained in the Health and Safety at Work etc Act 1974 and so on. I know that the issues that the Highlands and Islands fire brigade is wrestling with are dear to Fergus Ewing's heart and that the fire-master in Moray and Highlands and Islands is actively seeking to resolve them to provide an effective service in remote areas.

**Eileen Baird:** On the future funding of the service, COSLA is represented on a working group that, as Councillor Watters has pointed out, will consider changes in the service following the implementation of the integrated risk management plan. That process will continue, but we have agreed that it will be some years yet—perhaps with the comprehensive spending review in 2008—before any impacts will manifest themselves in service funding.

**The Convener:** On behalf of the committee, I thank the witnesses very much for attending the meeting. I should apologise for not mentioning Barbara Lindsay when I introduced the witnesses at the start.

I suspend the meeting for a couple of minutes to allow the witnesses to be switched around.

11:09

*Meeting suspended.*

11:11

*On resuming—*

## **Water Services etc (Scotland) Bill: Financial Memorandum**

**The Convener:** The third item on our agenda is consideration of the financial memorandum of the Water Services etc (Scotland) Bill. The bill was introduced on 11 June 2004 by Ross Finnie. We have with us the water industry commissioner, Alan Sutherland, and with him is Dr John Simpson, the director of cost and performance. We also have with us from Scottish Water Dr Jon Hargreaves, who is the chief executive, Douglas Millican, who is the finance director, and Ian McMillan, who is a non-executive board director. I welcome you all.

Committee members have a copy of a submission from Scottish Water, and also a submission from Water UK, Scottish Enterprise and the water customer consultation panels. I remind members that—as we agreed at our away day—the Minister for Environment and Rural Development will be coming before the committee on 28 September. He will talk about broader water issues, so today and next week we will concentrate on the financial memorandum. I will be reasonably strict about that, because we must focus.

I will ask the two groups of witnesses whether they would like to make a brief opening statement; I begin by asking the two Scottish Water witnesses.

**Ian McMillan (Scottish Water):** Good morning. Thank you for your invitation, which went to our chairman. Unfortunately, Alan Alexander is unavailable today and sends his apologies. He has asked me to come here on behalf of the board of Scottish Water.

I will give a brief personal introduction. My utility credentials come from a career in the electricity industry, not in the water industry: I spent my career with Scottish and Southern Energy and its predecessor, Scottish Hydro-Electric. Having experienced full economic regulation and, indeed, the introduction of competition, members can probably guess why I have a particular interest in the proposals in the bill.

Today we are primarily concerned with the financial aspects of the bill, but it is important to summarise Scottish Water's view of the policy proposals in their entirety. Members will gather from our submission that we are pleased that the Executive is proposing the introduction of more certain and transparent economic regulation, in response to this committee's earlier report. We



welcome, too, the Executive's proposals to regulate the scope of competition in the water market in Scotland. The formal approach to setting out the limits on competition will, we believe, limit the current risk that Scottish Water is exposed to in terms of any challenge under the Competition Act 1998. We feel that those matters are important.

If the proposed bill is approved, I know that my board colleagues will be seeking satisfaction that certain areas have been addressed. Firstly, the wholesale business that is left in Scottish Water must be properly funded for the conduct of all its activities. No new cross-subsidies should be created between customer groups. Secondly, although Scottish Water is unlikely to take on the role of a general utilities retailer—in the modern way in which that is conceived—we would seek assurances that a stand-alone subsidiary company in Scotland, selling only water services, would have to be viable at the outset. Thirdly, there is the need to ensure that the market that is set up operates in such a way that customers throughout Scotland do not suffer any disadvantage as a result of the changes.

In my experience, new markets are always very unpredictable; and, because this is a small market, it could well be more unpredictable than most. Non-household users of public water services in Scotland will need an assurance either that a sustainable market will develop throughout Scotland or that Scottish Water's retail subsidiary will be capable of delivering retail services throughout the country until such time as a sustainable market presents itself.

11:15

**The Convener:** I will also take an opening statement from the water industry commissioner before I proceed to ask members whether they want to put any questions to our witnesses.

**Alan Sutherland (Water Industry Commissioner):** Good morning, and thank you for the opportunity to give evidence this morning.

From a customer perspective, this is a very important bill and it will benefit customers in a couple of ways. The first way is one that Scottish Water has already touched on: as the bill is precautionary it will bring a degree of certainty to the Scottish water industry that is currently lacking. It is important to understand that the Competition Act 1998 is a fact of life and that the challenge of that act could have potentially detrimental impacts, both on customers directly and on the Parliament's aspirations for the water industry in Scotland.

I will give members some examples of the sorts of thing that could happen were Scottish Water to be successfully challenged under the act: fines of

up to 10 per cent of turnover for each year of an offence are possible, which, in Scottish Water's case, would be just short of £100 million per year per offence; charging policies—such as the harmonisation of charges across Scotland, or the offer of support to more vulnerable customers—could be unwound if cross-subsidies were found to be anti-competitive; and there could be a requirement to have the Executive fund Scottish Water on a more commercial funding basis and not give it access to public debt, which would clearly have a material impact, with an increase in costs that Scottish Water, and therefore its customers, would face.

The second important aspect of the proposals that will benefit customers is that the separation of retail activities from wholesale activities—and the transparency that that will bring—will identify and release costs that may not otherwise as quickly be released. That is certainly a characteristic of other utility markets where such a separation has happened. It is also quite possible that new entrants who benefit from the proposals on competitiveness will seek to lower prices to customers. The benefits from greater efficiency, and the strengthened regulation regime that is included in the bill, will also ensure that vulnerable customers, and domestic customers in general, do not suffer.

**The Convener:** I now invite questions from members. I remind them that they do not need to touch anything on their consoles. All that they need is an indication from me that they may speak.

**Dr Murray:** I am grateful to Mr Sutherland in particular for explaining to us what the alternatives would be if we did not introduce the licensing regime and what the costs to Scottish Water would be if that did not happen. Initially I was a bit alarmed by the costs of establishing the licensing regime and wondered whether it was going to be worth it. However, the question remains whether the financial memorandum is accurate.

Scottish Water's current estimates, which are based on independent research, suggest that establishing the competitive regime will be a lot more expensive than is suggested in the financial memorandum. Do you want to comment on the independent research and the possible costs to Scottish Water, as well as on the statement in the financial memorandum that some of those costs could be offset by a benefit from the division of the retail function? The submission from Scottish Water shows that instead of the costs being £2.5 million plus half a million a year, they tend to be something like £10 million to £18.4 million. I have concerns if the financial memorandum has the potential to be that inaccurate.

**The Convener:** It is a big gap.

**Douglas Millican (Scottish Water):** Scottish Water has no experience yet of operating in the competitive retail market. We have been keen to take sound advice from those who have experience of setting up new markets as to what might be involved and what the costs might be. Our primary concern is to ensure that, when the market is set up, it is set up in such a way that it operates in an orderly fashion to minimise the risk of confusion for customers who want to stay with Scottish Water, for customers who want to switch, and for new retailers within the market. We believe, therefore, that the market should be structured in an orderly fashion. It is important that the appropriate thinking and design in investment are done up front to facilitate the orderly introduction of the market.

With that in mind, we sought advice from IBM Consulting—the former PricewaterhouseCoopers Consulting—which has done similar work in a number of countries throughout the world, on what it would take to set up the market in an orderly fashion. The consultants do not suggest that there is a precise estimate; they have given a cost range of £10 million to £18 million. The cost might be lower or higher, but time will tell. Our main plea is to ensure that, when it happens, the market is set up in an orderly fashion.

**Alan Sutherland:** I have not had the advantage of seeing any consultants' report from Scottish Water, but I have seen the numbers in its submission to the committee. The most significant difference is in the costs of managing the customer information and the market mechanism.

Among the critical issues is to hear what the regulated company says its costs will be, to challenge those costs, and to understand what scope for efficiency the company believes will arise that would offset the costs in some way. Until we have gone through that process, which is an important part of economic regulation, it would not be appropriate for me to comment in detail on those numbers.

**Dr Murray:** I flag up a concern that we will also pursue with the Executive—the fact that your consultants consider that it could cost five to seven times as much to set up the competitive regime and that the on-going costs could be six to 10 times as much as are stated in the financial memorandum.

Would it be possible for us to have further detail of the research that was commissioned by Scottish Water in advance of following up the matter with the Executive, so that we can probe it further?

**Douglas Millican:** We are happy to check with IBM whether it is willing to divulge those details to you.

**The Convener:** That would be helpful.

My question concerns charges determination. The financial memorandum states that it is not possible to predict what the costs might be of complying with the ministerial direction. The costs would depend on the nature of the direction that is given. Have you done any scenario planning on the anticipated costs of certain kinds of ministerial direction? That question is first for Scottish Water and subsequently for the water industry commissioner.

**Douglas Millican:** The principal circumstance that we envisage in that respect is the direction that ministers will provide at the start of each strategic review charge setting process in relation to the standards and objectives that they want Scottish Water to follow in a given period. The Executive is consulting at the moment on the quality and standards III process in the upcoming period from 2006 to 2010.

We expect to receive guidance from the Executive in January that it expects us to cost in a business plan to be submitted in April. The consultation document on quality and standards III sets out the Executive's thinking on what the range of costs might be for those investment obligations.

**Alan Sutherland:** From a regulations standpoint, we have an additional budget this year of £1 million to conduct the strategic review. That is in addition to approximately £1.5 million, which is our annual budget.

We are about a quarter of the way through conducting the strategic review. The budget is tight, but it is manageable. I hope that the experience of going through the determination process to the current level of detail, and the set-up costs that are inevitably being incurred as this is the first time that we have done it this way, will mean that the process will cost about £1 million every four years in the future.

**The Convener:** I have a question about the costs that will be associated with setting up the body corporate, which is covered in the bill. Will there be only marginal, additional administrative costs associated with the process and are the quantifications in the financial memorandum accurate?

**Alan Sutherland:** When I saw the figure of £150,000, John Simpson and I sat down and counted up the salaries, the number of days and the likely on-costs that go with having a commission. We came to £149,000. Even on a bottoms-up costing basis, which everyone who tries to maximise their budget uses, the £150,000 seemed about right.

**The Convener:** Does Scottish Water have any views on the matter?

**Dr Jon Hargreaves (Scottish Water):** We would like to keep costs as small as possible, because customers end up paying for them.

**Fergus Ewing:** I admit to having serious concern about the massive cost to introduce the legislation. I will ask Mr McMillan and Mr Sutherland questions that arise from their opening statements. Each gentleman said that the bill is necessary because if we do not have it, we might be exposed to risks. I think that Mr McMillan said that, and Mr Sutherland referred to some of the sanctions that are contained in the Competition Act 1998—10 per cent of turnover and so on. Each described those as potential problems.

I appreciate that the question whether there is a potential risk, a real risk, an actual risk or a notional risk, might depend on an interpretation of the Competition Act 1998 and its application to the particular circumstances in Scotland where we have a monopoly supplier. However, given that we are to embark on the bill, which has costs of establishing a licensing regime of £10 million plus £2 million each year, should not we be absolutely clear in this Parliament whether there is a real risk or a non-risk? Will Mr McMillan and Mr Sutherland comment and indicate whether they have had legal advice on the matter and, if so, whether we can be in receipt of it?

**Ian McMillan:** Yes, indeed. The legal advice that we have at the moment is that we are exposed. The problem with being exposed to, say, the Competition Act 1998, is that the exposure is unquantified, so one tends to use the top limit, which we believe is of the order of £100 million.

Whether that sanction would ever be invoked is debatable and, as you well know, there is only one place in which it could be tested. There is a clear exposure at the moment under the Competition Act 1998, and the bill is a way of circumventing it. Within Scottish Water's risk management, because of the quantum of that exposure, the directors would need to ensure that it was high on their agenda.

11:30

**The Convener:** I would like a response to the converse of that question. I presume that a company could challenge whether the new arrangements satisfy the requirements of the Competition Act 1998. Have you received advice that a successful challenge is unlikely, based on the proposed arrangements?

**Dr Hargreaves:** One can never be certain in an area such as competition, but we are as satisfied as we can be, given the advice that we have

received and the way in which we have examined the bill, that it addresses the fundamental issue of the current exposure. One never knows in a market—somebody may find a different angle or make a challenge based on something that happens in the future, therefore it is probably correct to say that such challenges can never be legislated out of existence. However, the bill will achieve its primary aim of protecting domestic customers, which is part of the Scottish Parliament's desire, and it looks as though it will do that very well.

The bill will open up the market in a way that reduces the possibility of introducing an unquantifiable—and perhaps minute—risk to public health. That exists in England and Wales with common carriage, although they have decided that common carriage is not a risk. Until somebody has run that market for a period of time and lived through several incidents—which inevitably will happen in the industry—it is difficult to say what will happen. The aim is to avoid introducing a risk to public health, the protection of which is fundamental to the water industry. In both senses the bill achieves the objective.

**The Convener:** We take that on board. However, Mr Ewing's point was that we would like to see the advice that you have received that substantiates your points. If you cannot give us the original legal advice, a summary of it would be helpful.

**Dr Hargreaves:** We do not have a document sitting in Scottish Water that says, "Here is the advice on the bill." The advice has been built up over time—it is not a single piece of advice—but we can let you have what we have got.

**The Convener:** It would be useful to get the advice from both sides that states that the bill is necessary and will be effective. Mr Sutherland, what is your view on those questions?

**Alan Sutherland:** Likewise, we can share with you the legal opinions that have been provided to us.

It is not just new entrants who could challenge Scottish Water; a customer could challenge Scottish Water. It is important to have the framework, because any such challenge could have consequences. Yes, it is not possible to say when or if a challenge will come, but we are aware from customers of Scottish Water and potential new entrants who have contacted us that challenges are likely. They are considering challenges, and they are waiting to see what happens and whether the bill is passed before they decide whether to challenge.

**Fergus Ewing:** Who is contemplating a challenge?

**Alan Sutherland:** It would not be appropriate for me to divulge commercial confidences that have been shared with us.

**Fergus Ewing:** I do not agree with you, sir, because this committee is examining expenditure of £10 million for risks that I am not satisfied will ever occur. As a Parliament, we need to be clear when we authorise expenditure of £10 million that there is a real risk. I am grateful that Mr Sutherland has undertaken to provide us with the original legal advice. I think that that is correct, is it not?

**Alan Sutherland:** We will provide the advice that we have.

**Fergus Ewing:** However, I was not quite so enthused—

**Dr Hargreaves:** We will do the same. The assumption was that there was a single document, but because the bill has evolved we have taken advice at different stages. We will let you have that advice.

**Fergus Ewing:** I have a separate question. The figures for the cost of establishing a licensing regime seem to be vague, ball-park figures. Do Scottish Water and the WIC have confidence in those figures? Can we have more detail on how they were arrived at? Whenever we see a figure of £5 million, I immediately think, "Has someone worked out this huge figure on the back of an envelope?" and I would like to see how the figures are made up. From past experience, when we probe the detail behind a big number we find suddenly that no-one has worked it out or thought it through. Could the representatives of the two bodies give us some comfort on that general point?

**Ian McMillan:** Yes, we can. Douglas Millican will help with the detail, but I make the general point that the experience of every utility is that the cost of the regime and systems that underpin the industry is always greater than was originally estimated. There is an interesting record of that happening. Equally, until such time as the details of the regime are laid out and specified, it is difficult to cost it. You are right to say that we are dealing with estimates, but they are estimates based on similar types of systems that have to be implemented.

**Douglas Millican:** On the specific point of the £5 million to establish the licensing regime, the cost of which would fall on the water industry commission, the financial memorandum was based on advice given by the water industry commissioner, and we have no reason to believe that that advice did not reflect fairly the underlying costs.

**Alan Sutherland:** We have had advice on the legal component of £1.5 million and the

accounting projects of £0.5 million. On the other advisory work, the figures are in line with our observed experience of changing elements of the regulatory regime. There is a market research budget of £0.1 million, which is one major project. The £2.5 million is over five years—it is £500,000 a year—and covers all staffing, developing licences and consulting extensively on the introduction of those licences over five years.

**The Convener:** A written note of the breakdown would be helpful.

**Fergus Ewing:** I have one point specifically for Mr Sutherland. He can correct me if I am wrong, but the budget of the water industry commissioner was overspent by £140,000. That is a matter of considerable concern, given that the WIC is a financial regulator and there is a substantial overspend in relation to the total budget. Can you reassure us that that overspend was a one-off mistake and will not recur?

**Alan Sutherland:** It is certainly a one-off, and was a direct function of extra work that we were asked to undertake.

**Jim Mather:** Going back to the regulatory impact assessment, paragraphs 14 and 16 give different figures for the reduced bill for standard connections. One refers to £30, and the other states that there will be a minimum benefit of £25 per standard connection. Is that anticipated to be an annual saving?

**Alan Sutherland:** The difference between the two figures is that £30 is the pre-cost amount, and £25 is what you would expect the supplier to pass on.

**Jim Mather:** So that is the anticipated annual saving.

**Alan Sutherland:** Yes, for an average bill.

**Jim Mather:** The RIA goes on to say that the water industry commissioner estimates that there is an efficiency gap of 43 per cent between Scottish Water and most comparable companies in England and Wales. Is that figure agreed between both parties represented? If not, could we hear Scottish Water's standpoint on the matter?

**Douglas Millican:** It would be appropriate for the commissioner to explain where that figure came from before we comment.

**Alan Sutherland:** In our costs and performance report of last year, which covered until the end of the 2002-03 financial year, the gap to the leading company in England and Wales was assessed as 53 per cent. In its recent draft determination, the Office of Water Services—Ofwat—has said that the industry as a whole is likely to be moving forward at around 3 per cent per year. Conservatively, we could consider that as a couple of per cent per year for the frontier company.

John Simpson will take members through the detail, but it is important first to recognise a couple of things. Over the past two years, Scottish Water has made quite impressive progress in reducing its operating costs. We have been particularly encouraged by the progress that has been made over the past year and by the information that is beginning to come out on the trend line for the current financial year. There is good news, but there is still a considerable gap to the frontier company. The estimate that is contained in the financial memorandum is of the right order.

**Dr John Simpson (Office of the Water Industry Commissioner):** As Alan Sutherland said, the estimated gap in our 2002-03 report was 53 per cent. I would like to take members through some numbers. It is easier to deal in pounds and pence. On the basis of the gap that we published, it would cost Scottish Water £1.86 to deliver a service equivalent to that which the leading company can deliver for 87p. That comparison or benchmark uses tried and tested benchmarking models, which were developed by Ofwat. In fact, the models were developed by me when I worked at Ofwat. We have applied those models to Scotland and we have done a lot of work to ensure that the additional costs of operating in Scotland—which do exist—are properly taken into account.

The latest comparisons that we have are for 2002-03; Ofwat has not yet published any information for 2003-04. I would regard the efficiency gap, as stated in the impact assessment, as of the right order. It is interesting to note that both Scottish Water and Water UK have thrown doubt on that, but I would say that that doubt is premature.

Scottish Water has made substantial and welcome improvements over the past financial year, and that is continuing today. On the basis of the figures that Scottish Water has provided to us, my £1.86 figure becomes £1.67 thanks to the 10 per cent improvement of last year. Scottish Water says that it expects to improve by a further 10 per cent in this financial year; that takes us to £1.51. Another 10 per cent improvement in the following year would take us to £1.36. That last improvement would deliver the targets that we set in the strategic review of charges.

11:45

Remember that the leading company can deliver for a cost of 87p and falling. Companies continue to improve. If we ask where the leading company will be by 2008, we can only speculate but, if we assume that the leading company improves by 2 per cent per year, which is in line with what Ofwat is saying, then the figure of 87p becomes 77p, so the respective figures for that year would be £1.36 and 77p. By my calculation, that is a 43 per cent

gap. The gap is 59p—a 43 per cent gap when divided by £1.36.

If Scottish Water continues to improve, as I am sure it will, the gap will be smaller. If it improves by 15 per cent, the £1.36 becomes £1.16, and the gap is then 39p, or 34 per cent. My point is that there will still be a significant gap in 2008. I do not know whether the gap will be 42 per cent.

**Jim Mather:** Does your methodology factor in topography, geography, the sparsity of population and the relatively smaller market in Scotland?

**Dr Simpson:** Very much so. That is at the heart of the benchmarking and modelling process. It is absolutely about that kind of thing.

**Jim Mather:** A response from Scottish Water would be appropriate at this point.

**Douglas Millican:** The discussion shows that the relevant question is what the level of efficiency will be in 2008, when the market opens. I am not going to predict what that will be, because it all depends on how we and the companies down south reduce our operating costs.

In England and Wales, there is a wide range of performance. John Simpson has highlighted his assessments relative to the leading company. If you consider the efficiency performance for the companies in England and Wales, which has been quoted by Ofwat, you will see that there is a wide range between the most efficient company and the least efficient company. The relevant factor with respect to the benefit that would be available to customers in Scotland who choose to go with a retailer, rather than with Scottish Water, will be the operating cost base of that retailer compared with that of Scottish Water retail in 2008.

**Jim Mather:** We are talking about a minimum saving to a business of £25 per annum. We know that charges have been high for the business community here. Is it likely, in the opinion of the Scottish Water witnesses and, perhaps more important, in the opinion of the water industry commissioner, that the new regime will force an improvement in the ratio of capital expenditure funded from borrowing, and possibly even a rethink on some of the accounting protocols through which so much of the infrastructure has been written off in year one?

**Alan Sutherland:** As far as the price determination is concerned, we will shortly publish for consultation our proposals on how we will set prices for the regulatory period. We are in the fortunate position of having considerably more information about the industry in Scotland. In particular, we have a much higher quality of information on Scottish Water's assets compared with the information that was available when there were three water authorities, when the 2002-06 review was written.

We propose to use a method of setting prices that assesses a regulatory capital value, which will be in line with the process that is used in the water industry in England and Wales and in other utilities. That will facilitate comparison: it will make possible, immediately and directly, comparisons on the basis of funding or financial ratios, and without any adjustments being required. In essence, the regime will allow people to make representations in a transparent way.

The current proposals are that, if the bill is passed, we will publish a draft determination at the end of June next year. There will then be a period lasting until about the end of September next year, during which people may comment in detail, having seen the answers—but prior to a final answer being struck. If Scottish Water was not happy with that answer, or if it did not think it to be manageable, it would have the right of appeal to the Competition Commission, in line with that of other utilities. There is a very robust process in place to ensure that we have a proper and transparent regulatory regime for the calculation of prices. Many of the issues that we have discussed previously are therefore being addressed.

**The Convener:** Dr Simpson gave us a projection using pounds and pence. It would be useful if members of the committee could have that in writing. I am also conscious that the witnesses from Scottish Water have not had a chance to comment on the pounds and pence figures, so if they would like to they can do so now.

**Douglas Millican:** I tried to address that issue previously by saying that I would not want to make projections as to where the companies in England and Wales will be in 2008 when the market opens. Ofwat will make assumptions, just as it did at the last periodic review. It is interesting that some of the predictions that were made at the 1999 periodic review of the companies in England and Wales are not holding true. Operating costs in companies in England are tending towards being higher at the end of the current regulatory period than Ofwat predicted. There are always dangers with predictions.

We expect that the gap will be much narrower in 2008 than it is at the moment. However, the most relevant aspect is not what the gap might be against the leading company, because that leading company might have no interest in competing in the Scottish market. The relevant issue is the cost base of Scottish Water's retail activities compared to the cost base of new retail companies that want to come into the market. Those are the companies that might provide benefits to Scottish customers.

**The Convener:** Is that the cost base across the current activities of competitors? If we take

Thames Water as an example, are we talking about that company's current costs or what it would cost for it to enter the Scottish market and compete here?

**Douglas Millican:** Under the proposals that are set out in the bill, the cost of the retail activities is of primary relevance. The wholesale monopoly activities of providing water and treating sewage will continue to be provided by Scottish Water. The most relevant comparison is of the costs of the activities that fall into the new retail element and which will be licensed by the new commission. If new entrants to the market can operate their retail activities for a lower cost than Scottish Water can, that might offer a competitive advantage to customers. Clearly, that will also give Scottish Water retail an incentive to continue to bear down on its retail costs.

**Mr Brocklebank:** I was interested in Dr Simpson's figures, and I take the point that he compared the best, most efficient and most economic of the English and Welsh companies against Scottish Water. Can he produce an average figure that might provide a more direct comparison? Is it anything like 29 per cent by 2008?

**Dr Simpson:** The pounds and pence were carefully chosen so that the average company in 2002-03 would have delivered the equivalent service for £1. We have Scottish Water at £1.86, the average company at £1 and 87p for the leading company. Ofwat tells us that the companies are set to improve at a rate of 3 per cent per year. 2008 is five years away from 2003, so that would result in improvement of the order of 15 per cent on our £1, which will mean an amount of 85p by 2008. I return to my original point that the figures are £1.36 for Scottish Water, about 85p for the average company and 77p for the leading company. Douglas Millican is correct to say that the gap is narrower; nevertheless, there is a gap.

There is also a point to be made about retail costs. It was said—rightly—that what matters is the retail cost base. There are issues there with economies of scale and scope in that Scottish Water can allocate its billing costs only across non-domestic customers. The water and sewerage companies down south can allocate those costs right across their customer bases, which gives them better cost bases from which to compete.

**Mr Brocklebank:** Ultimately, what concerns us all is how much our water is going to cost us, whether as individual customers or businesses. I do not know whether you have seen Scottish Enterprise's submission, but I found it to be fairly damning in that it claims that Scotland is not competitive in terms of water charges because it is the fifth most expensive country, with

“countries such as Belgium, Italy and Spain having a comparative advantage in terms of pricing.”

I am an amateur, but given the rainfall in Spain and Italy and all the rain that we have seen here this summer, it seems to be utterly incredible that Scotland is among the most expensive countries in Europe. The Scottish Enterprise submission goes on to suggest that the situation makes us particularly uncompetitive in sectors such as paper processing, pharmaceuticals and so on. There are two paper mills in the constituency that I represent: can they look forward to any improvement in that competitive situation five years down the line as a result of the bill?

**Alan Sutherland:** In the previous review, we said that if Scottish Water were to deliver on its targets, and were the capital programme to run at or around the same level as it does in the current regulatory period, there would be no need for real price increases across the board. The division of who pays what is something on which we will get guidance from ministers in January after the principles of charging consultation closes. Once we get that, we will be in a position to look forward and say what that revenue line will mean for prices for individual customers.

**Dr Hargreaves:** I have a comment on the international comparisons. The data are sometimes difficult to collect, but let us assume for a minute that the data are correct. We are not talking just about Scotland but about Britain, and Alan Sutherland will agree with me that the English and Welsh water companies are now probably among the most efficient in the world after 15 years of pretty tough regulation. I am concerned about where we are going to end up with those data, mainly because of the way in which improvements in environmental conditions and other issues associated with the water industry are funded in the UK versus the funding in other countries in Europe. I am not saying that those countries do not implement European directives in the same way as we do; members are probably a lot closer to that than we are.

The only real example I can give is of a Scandinavian country where nitrogen removal from the water supplies was funded through a grant system rather than its being paid for directly by customers. Such things lead to an ongoing, but false, view that water prices in such countries are lower. Other countries use subsidies that are not used in Britain, in which I include Scotland.

Looking down the line, how we will end up is of concern. At the end of this period, Scottish Water will not be the least efficient of the big water and sewerage companies. We believe that that is an amazing—I mean that—feat given that we have had four years to achieve it when the other companies have had 15 years and some time

before that. It is important that Scotland should recognise that.

Nevertheless, the amount of money that needs to be spent on the infrastructure in order to maintain and improve the standard of service to customers, and the continuing flow of environmental legislation requiring huge sums of money are of concern in respect of the bill and as a general question about the competitiveness of the water industry. Although water falls out of the sky a lot in Scotland, that does not mean that it is cheap. Parts of Spain have much higher rainfall than Scotland. It is about the treatment that the water requires once it has been collected, whether it has to be pumped over hills, how far it has to be pumped and so on.

**Ms Alexander:** Like other members, I was struck by the figures that John Simpson offered the committee. I want to pursue them.

Obviously the committee's concern is about stewardship of the public purse and value for money for Scottish consumers and taxpayers. I seek a professional opinion. I am struck by the fact that having a near-monopoly provider and a sole regulator—with all the risk of regulatory capture that that carries—is not a structure that has commended itself historically to closing efficiency gaps, to reducing cost bases or to innovation. Most historical evidence suggests that a more competitive market will close an efficiency gap. Will you comment on whether, based on the evidence of which you are aware professionally, we have a structure that commends itself to closing the efficiency gap? I will ask a follow-up question.

12:00

**Dr Simpson:** There is no risk of regulatory capture.

**Ms Alexander:** I take that point.

**Dr Simpson:** The regime that Ofwat has operated in England and Wales has shown that an independent regulator can create a regime and incentives under which companies feel pressure to improve. It is fair to say that since the companies became fully regulated by Ofwat, they have made great strides in improving their efficiency—that is true of every company. If there had been no regulation, but there had been competition instead, would improvement have been greater? I do not know. All I know is that the regime under Ofwat seems to have worked and to continue to work.

The arrangements in the bill to establish powers of determination and so forth will give us a similar regime to Ofwat's. We have made a good start—Scottish Water has made a good start by

achieving considerable efficiencies. I hope that we can now build on that initial progress.

**Ms Alexander:** In your professional opinion, are savings such as have been made in England and Wales more difficult to achieve because, although we have an independent regulator, we have a sole provider in large parts of the market?

**Alan Sutherland:** We are in a fortunate position because we have access to all the information that comes from England and Wales. If we had no easy benchmarking opportunities—as was the case with the Royal Mail and the Postal Services Commission, Postcomm, which cannot make immediate and easy comparisons because of accounting differences and statutory and other legal differences in postal services—regulation would be much more difficult. However, when information about 10 large water and sewerage companies and another 13 water-only companies is being collected and audited consistently on both sides of the border, very detailed comparison work can be undertaken. John Simpson has talked about that important point.

Most economists would probably argue that at least the potential for competition—if not competition itself, the idea that competition may occur, which might be market competition, outsourcing or competition for capital in financial terms—would help to stimulate further improvements.

**Ms Alexander:** I say with respect that John Simpson has not had the chance to answer my question; he may choose not to. The question is whether, in your professional opinion, having a sole provider in large parts of the market in Scotland in any way inhibits closure of the efficiency gap.

**Dr Simpson:** The answer is no, for the reasons that Alan Sutherland gave. We have the information and techniques that we think we need to establish the relative level of performance, which allows us—through committees such as this and through the Scottish Executive—to put appropriate pressure on Scottish Water.

**Ms Alexander:** I will ask just one follow-up question. If the sole-provider ownership structure, which was chosen several years ago, does not of itself represent a barrier to closing the efficiency gap, why have we made such slow progress on delivering the promise that was held out for the sole-provider model just a few years ago?

**Dr Simpson:** I am not sure whether I understand the question. We had three providers in 2001 and our judgment at that time, in the strategic review of charges, was that the best chance to close the efficiency gap would arise from having a sole provider, rather than three providers. That was our judgment then and I would not revise it now.

**Jim Mather:** In the past, we have had flawed and unhelpful comparisons with England and Wales, so I am keen to go through the methodology of your comparison of charging down south and up here in Scotland. Does your methodology adjust Scottish Water's accounts and those from England and Wales on to a similar basis for borrowing levels and the protocol of writing off infrastructure replacement in the year in which it occurs?

**Dr Simpson:** At the heart of the comparisons that we make are comparisons of cost—operating and capital cost.

**Jim Mather:** So that is a no.

**Dr Simpson:** We think that because the inefficiencies lie in those costs. The regime that we have established for the current strategic review, with a regulatory capital value, will allow us to make direct comparisons going forward, but we are not in a position to make exact like-for-like comparisons along the lines that you described.

**Jim Mather:** Would going along the lines that I suggested present a truer and fairer view?

**Dr Simpson:** It would do so for a comparison of the businesses as a whole, but it would make no difference in respect of efficiency.

**Jim Mather:** Has Scottish Water recalculated the figures to deal with an assumption that the water boards down south applied a similar ratio of capital expenditure from charges and therefore did not borrow as much, for example? Has it reworked the numbers to show its numbers in a proper and fairer light?

**The Convener:** I will let Scottish Water answer that question, but I am anxious to draw us back to the bill and the financial memorandum, which is what we are meant to discuss.

**Douglas Millican:** At the moment, we are concerned primarily with planning for the next regulatory period. We are due to submit our first draft business plan to the water industry commissioner at the end of October—obviously, part of that will depend on his draft methodology, which he will publish later this month for consultation. In submitting our business plan, our main aim will be to give the commissioner all the information we believe we have, which he needs to ensure that he can undertake proper like-for-like comparisons and that the draft determination that he will publish in June next year is comparable with that of Ofwat for the companies in England and Wales.

**John Swinburne (Central Scotland) (SSCUP):** As always, I have sat and listened to beautiful rhetoric and must try to separate the wheat from the chaff and, as usual, there is more chaff than wheat.



Alan Sutherland said that the budget is "tight, but it is manageable".

The budget of the people whom I represent is tight, but totally unmanageable, and pensioners found out that in the last tranche of increases, the increase was 5 per cent. Mr Ian McMillan made a lovely statement that boosted my confidence. He said that part of the remit was to ensure that customers do not suffer disadvantage. How can you reconcile that with the fact that every senior citizen in the country has been disadvantaged by a 5 per cent increase while their pensions have increased by only 2.5 per cent? You have disadvantaged every senior citizen with that little increase. I suppose that that will continue next year and in the future and the £1.87 increase—or whatever it is—will go up and up.

No one ever seems to think about the people at the bottom of the scale. The Executive, in conjunction with you, came up with a beautiful deal of 2 per cent for small businesses. What about senior citizens who are on a fixed income? You people have got to get real.

**The Convener:** I am not sure that we are getting to the bill.

**Fergus Ewing:** I wonder whether I missed something. Dr Simpson read out a series of statistics that justified his conclusion that there is a 43 per cent gap in efficiency between Scottish Water and the most efficient English or Welsh water company. Have we received an explanation of how those figures were arrived at?

**Dr Simpson:** Yes. We published—

**Fergus Ewing:** Has the committee received a submission from you?

**Dr Simpson:** Do you mean the figures on the financial memorandum or the pounds and pence that I described?

**The Convener:** I think that the problem is that the committee has not received a written submission from your organisation. I have asked for the figures to be provided to us, perhaps with an explanation. I am sure that that is what Mr Ewing is suggesting.

**Fergus Ewing:** Yes. The figures are obviously important and underlie many of the assumptions that make the bill necessary, in your view. The bill will involve £10 million of initial set-up costs—money that I, like Mr Swinburne, believe would be better used to cut water rates. It is unfortunate that we have not received a submission that shows how you calculated those figures.

I will move on and raise two matters that arise from the figures that you gave this morning. First, Scottish Water began life with accumulated debt of about £2 billion. Senior citizens face swingeing water charges, as John Swinburne rightly said,

partly because the customer has to pay back that debt through the interest element that must be met each year. The WIC compares Scottish Water with the 10 privatised companies south of the border, but is not the debt that the Scottish water-rates payer must pay back much greater than the debt of the English and Welsh water companies? I recall that those companies received a green dowry as part of the privatisation package, when their debts were written off. Are you not therefore comparing apples with pears?

**The Convener:** It might be more appropriate to put that question to Mr Finnie when he comes before the committee. I have been very specific; I said that we are concerned with the financial memorandum to the Water Services etc (Scotland) Bill. Members should direct their questions accordingly.

**Fergus Ewing:** With respect, convener, I understand from the Scottish Parliament information centre's briefing paper that the Executive's figures are based on information from the WIC. However, the WIC has not given us a computation of the figures that he brought to this meeting. It is highly relevant to request an answer to a simple question: is there a comparison of apples with pears, because Scottish Water began life with a massive debt of £2 billion, which was not the case south of the border? Any comparison must surely take account of that fact and make it explicit. Has that been done in relation to your figures?

**Dr Simpson:** I will make three points in response. First, there is an account of how the figure of £1.87 was derived. Secondly, the debt in England and Wales currently stands at about £20 billion—I do not have the exact figure to hand—so we in Scotland are not out of kilter in relation to the debt borrowing by water and sewerage businesses in England and Wales.

12:15

There are one or two myths about the green dowry. In our costs and performance report, we explained the amount of debt that was commuted when the industry was privatised in 1989, which was just short of £5 billion. The Treasury provided a cash injection—the green dowry—of about £1.6 billion. The total cost of the transaction was therefore about £6.5 billion, which is equivalent to £275 for each household in England and Wales. Privatisation raised £5.2 billion as proceeds, so the net cost to the Treasury was £1.3 billion. The net cost per household was approximately £55. Tax losses were also transferred by the Treasury.

In Scotland, £700 million of debt was commuted when the three water authorities were set up, leaving £1 billion debt on the books. The cost to the Treasury of that transaction was £700 million,

which equates to £330 per household in Scotland. The cost to the Treasury in Scotland was about six times greater than that which was incurred by the privatisation arrangements in England and Wales. As it happened, there were also transfers of tax losses as in England and Wales.

**The Convener:** Thank you for that explanation. If Fergus Ewing has another question, I would prefer it to relate specifically to the financial memorandum.

**Fergus Ewing:** I have a question that relates specifically to the memorandum. I have read before the figures that Dr Simpson cited, and I believe that they are being examined by experts to determine whether the conclusions that have just been expressed are challengeable.

I raise a specific concern that BP and Unison have expressed about the requirement that Scottish Water set up a subsidiary. BP and Unison are not the most traditional of partnerships, but they have argued that the requirement to set up a subsidiary, which obviously has huge cost implications, would detract from the main task of meeting efficiency targets. I agree with BP and Unison. Attention is drawn specifically to one concern which is, namely, that in Scotland the market will be open; any customers will be open to competition. However, in England only customers who use 50 million litres of water a year—which would probably exclude most householders—will be open to competition.

At the beginning of the meeting, we heard both Scottish Water and the WIC say that we need to spend the £10 million because we must have open competition and if we do not set up a subsidiary we may be sued and face swingeing charges. However, we do not have open competition. Again, apples are being compared with pears. I understand that, in England, only the biggest customers—those who consume 50 million litres a year—will be open to competition. In Scotland, everyone's water supply is open to competition. In England, there will be common carriage. In Scotland, common carriage—that is to say, use of the water pipes by more than one company—is prohibited. Do we not again have different situations in Scotland and England? Are we not comparing apples with pears? Why do we need to spend all this money?

**Alan Sutherland:** The bill will allow for competition for all non-domestic customers. It will not allow competition for household customers. We are talking about between 120,000 and 130,000 businesses in Scotland that could benefit from having a choice of supplier.

I understand from conversations with the Executive that the bill was designed as a precautionary bill. It will not introduce competition,

but will put in place a framework that will protect the Government's social, environmental and public health policies. As I said in my opening remarks, there is a real possibility that a challenge under the Competition Act 1998 will impact on things that are the prerogative of the Parliament, and that would have consequences for customers. Therefore the costs would seem worth the benefits.

**The Convener:** The concern was raised initially by Scottish Water, so it would be appropriate to give it an opportunity to comment.

**Dr Hargreaves:** On the setting up of the subsidiary, which was the first part of your question, there is a timing issue: when should we do that? Competition comes into being in 2008, so clearly it needs to be done before then. There is no doubt that creating a subsidiary—taking people who work in one part of the business and dividing up call centres and billing staff—will be disruptive to the business. Will that inhibit Scottish Water driving out more efficiencies? In the past two years, Scottish Water has delivered more efficiencies than any other water company in a two-year period. It will continue to drive out efficiencies, but will creating a subsidiary stop us continuing with that trend? The answer to that must be no. Ministers and the Parliament will expect Scottish Water to manage both activities at the same time.

**Fergus Ewing:** Sorry—I do not think either of the gentlemen has answered the question that I raised. Scottish Water has raised the specific concern that

“Scottish Water retail will not be treated equally with other retailers. This is due to the fact that the Scottish retail water market will be wholly open to other retailers, whereas the retail water market in other parts of the UK will not be wholly open because retailers will only be able to compete for non-domestic customers who use over 50 megalitres.”

Why has the bill been framed in such a way that your concern has not been taken up?

**Dr Hargreaves:** We did not say that in our evidence, but I am happy to comment on the point. England and Wales have chosen, quite simply, to take a different route to achieve the same objective. The Scottish Executive has chosen—it is not Scottish Water's choice, but ultimately your choice, as Parliament—to take a different route. As I said earlier, although one quality regulator south of the border believes that common carriage is not a risk, the view of the Scottish regulator is that there is a residual risk. If an operator in the water industry can avoid putting two or three lots of water from different ownerships down the same pipe and still achieve its objective—as Alan Sutherland said, the objective is to prevent challenge—that is by definition a good thing to do. I am not saying that it is impossible.

England and Wales have chosen to go down a different route. They are trying to mirror what happened with electricity and gas and create the market gradually, that is at 50 megalitres. It is highly likely that that figure will reduce in future, but of course customers will get the benefit of either retail competition or common carriage. I question the English system—why do they believe that retail per se is not a good thing for their commercial customers?

**Fergus Ewing:** I have one final question. We have heard the WIC argue that Scottish Water is massively less efficient than the most efficient water company in England. You will be exposed to competition from that company. If that company can supply water at 43 per cent of the cost—or anything remotely like that—it will be able to steal your customers. That will mean that the business customers will be the customers of the most efficient English company and you will be left with exactly the same costs. You will lose revenue massively to your more efficient competitors and the victims will be the remaining customers of Scottish Water who, instead of paying for part of the costs, will pay for all the costs.

I am trying to put this as clearly as possible. Does not the bill really represent a gigantic threat to the ordinary domestic water-rates payers in Scotland? If I am wrong, can you explain why I am wrong?

**Douglas Millican:** Central to the successful operation of the bill will be the clear setting of the price that Scottish Water will, in future, charge businesses for the wholesale supply of water. It is critical that the wholesale price that Scottish Water will charge retailers is properly set so that it fully covers—but no more than that—all Scottish Water's future costs of providing treatment and distribution activities. If those wholesale charges are set properly, there will be neither a benefit nor a disbenefit to household customers arising from the bill.

**Fergus Ewing:** What is the point of the bill, then? If the price is going to be set artificially at a level that enables Scottish Water to supply the water, what is the point of the bill?

**Douglas Millican:** The water side of our business runs everything from raw water resource abstraction through treatment and distribution to the selling and delivery of services to customers. The bill proposes that companies will be able to obtain licences from the commission to undertake those aspects of activities that are not prohibited under the bill. Therefore, Scottish Water's future wholesale price will not be for the same service that it provides today; it will be for those elements of the service that remain with Scottish Water and that are not provided by newly licensed entrants.

**The Convener:** I think that we are reaching the end of this process.

**Mr Brocklebank:** Can I just clarify something?

**The Convener:** Fergus Ewing's points were on policy, not the financial memorandum. It is important that we confine—

**Mr Brocklebank:** My point is related to Water UK's apparent criticism of what is proposed in the bill.

**The Convener:** Okay.

**Mr Brocklebank:** In its conclusions, Water UK basically says what Fergus Ewing has pointed out. If these issues are not addressed through legislation and regulation, competition in Scotland could encourage cherry picking and leave domestic customers alone to pay for the environmental and social objectives that are given to Scottish Water. Is that not a real danger? Water UK points that out in its submission.

**Douglas Millican:** Absolutely. That is why it is critical that the wholesale price is set correctly.

**The Convener:** I thank our witnesses for coming along. We will have Executive officials at our next meeting, and you have given us food for thought and ammunition for questions to those witnesses. Thank you very much for coming along today.

## Budget Process 2005-06

12:30

**The Convener:** The fourth item on our agenda is consideration of a paper from our adviser on trend series data that we received from the Executive. Members have a copy of the data together with an analysis produced by “Professor Arthur” and by SPICe. We cannot see the rest of your name, Arthur, so you have just become Professor Arthur. We also have copies of correspondence between me and the minister and a brief note from Arthur Midwinter offering advice on the minister’s letter. I will give our adviser an opportunity to speak briefly to his paper and will then invite contributions from members.

**Professor Arthur Midwinter (Adviser):** I will be brief. Members have had most of the papers for some time; they were sent out to give the committee information during the summer. All I would say about the data that we have received is that the results of the analysis that we carried out are broadly consistent with the trends that we identified—even with the problematic data in the post-devolution period. I am pleased to say that Jim Mather has provided me with his own calculations, which are consistent with our findings. He has health and education as the big winners and local government and environment and rural affairs as the big losers.

The main reason for bringing this agenda item before the committee today is to get a decision from committee members on how they would like to have the information published. There is no dispute that Andy Kerr, the Minister for Finance and Public Services, is happy to publish the information for us. In our correspondence, the Executive’s preference—which I would agree with—was to publish the five-year run, which it now has, using the current resource accounting and budgeting system, in the draft budget.

The Executive’s preference was also to publish separately the 10-year trend data, which is on a different price basis, excludes significant one-off increases and takes account of shifts in responsibility. However, the minister is prepared to publish that information in the draft budget if members think that that is where it should be. My view is that, as the draft budget is the beginning of the document for parliamentary control of expenditure, it is more appropriate to have the 10-year data published separately, because otherwise the data will not be consistent and might cause confusion among members and among the public. I am therefore suggesting that we agree with the minister’s initial recommendation on where to publish.

**The Convener:** I will give Wendy Alexander the first opportunity to ask questions on this, because she has been the most relentless pursuer of trend series data.

**Ms Alexander:** The paper is helpful and I agree with the recommendations that Arthur Midwinter has made—that five-year data, in resource terms, and 10-year data should be published under separate covers. The conclusion is relatively successful, although it leaves unresolved an issue that I have raised offline, perhaps for discussion over the next year—the need for a distinction between what is important for control purposes, which is appropriate for budget documentation, and what other additional information may be appropriate for policy purposes. However, let us agree this paper today and leave that issue on the table for discussion over the coming year.

**Mr Brocklebank:** I agree with Wendy Alexander that this is a useful paper. As those of us who represent rural areas have long argued, we are, as ever, the big losers. I am delighted that Professor Midwinter has highlighted that point.

**Professor Midwinter:** But you are not delighted that you are losing.

**Mr Brocklebank:** No—I am delighted that you have highlighted the fact.

**Ms Alexander:** Of course, that is diametrically opposed to Peter Wood’s assessment of the rural-urban split. These joys await us this year.

**The Convener:** I am sure that we will have plenty of discussions on these issues, but I think that we have a consensus that we should agree with Arthur Midwinter’s advice. We will pursue that.

**Members indicated agreement.**

## Item in Private

12:34

**The Convener:** Agenda item 5 is consideration of whether to discuss the appointment of a budget adviser in private at our next meeting. We have to get the process in place, so we will be discussing names.

**Fergus Ewing:** Just before we go into private session, can we not—

**The Convener:** We are not going into private session; we are agreeing to go into private session at our next meeting. Do members agree that we should do so?

**Members** *indicated agreement.*

## Public Sector Jobs Relocation Debate

12:35

**The Convener:** I indicated earlier that I would get some information on the relocation debate from various sources. On the issue that was raised, I have received a letter from Patricia Ferguson, which I propose simply to read out. She says:

“In light of the Executive’s failure to respond within the agreed timescale to your Committee’s Report on the Relocation Policy of the Scottish Executive, I am writing to advise you that new monitoring procedures are being put in place to prevent a reoccurrence of this nature.

The Scottish Executive endeavours at all times to comply with the protocols it has with the Parliament and it is a matter of concern to Ministers that this has not been the case in this instance. Please be assured that we take this matter seriously and convey to your Committee my apologies for this failure on our part.

I am copying this letter to the Presiding Officer.”

In a sense, we have received a positive response on the question of procedure. However, I have also received an indication that the specific response to our relocation report will not be available until Monday, which is obviously less than satisfactory.

As far as the possibility of changing business is concerned, the Presiding Officer is currently in a meeting, but the informal advice that I have received from clerks is that any move towards trying to pull or change the substance of the debate would seriously disrupt parliamentary business. In any case, it is not within our powers to do so, as any such move would depend on a vote of the Parliament. Instead, I propose to respond to Patricia Ferguson’s letter, welcoming the procedural mechanisms that she has indicated will be put in place and registering our continuing disappointment that we will not receive a response before Monday. I am happy to take on board any other points that members wish to highlight.

**Ms Alexander:** We should respond to Patricia Ferguson, saying that we appreciate the generous nature of her apology, from which I do not want to detract in any way. We should also indicate that, in the circumstances, we are happy to receive the response to our report on Monday.

We should also say to the Presiding Officer that we are anxious to find out the convention that he will adopt if such circumstances recur. After all, Patricia Ferguson is only reaffirming that the Executive should have met the deadline—as I have said, she has done that generously and we should accept her apology. However, her letter does not deal with the convention with regard to

parliamentary scrutiny in such matters, which remains an issue for the Presiding Officer. The clerks should convey to him that we and other committees would find it helpful to know the convention that he will adopt towards parliamentary business if the eight-week deadline is not met and a debate is looming.

As a result, I propose that we reply to Patricia Ferguson by appreciating the generous nature of her apology and indicating that we are looking forward to receiving the response on Monday. Moreover, we should indicate to the Presiding Officer that we hope that in due course he will reach a view on the scheduling of parliamentary business when such a deadline has been breached. Obviously, I do not want to disrupt Wednesday's business.

**Fergus Ewing:** It is gratifying that the Minister for Parliamentary Business has apologised and admitted that the Executive is in the wrong. However, as well as entirely endorsing Wendy Alexander's proposals, I want to make two other suggestions.

First, in accordance with paragraph 17 of the protocol, an explanation is required to be provided when the two-month deadline is not complied with. Even now, we have received no explanation from the minister, Tavish Scott, of why it was not possible to comply with the usual deadline. The protocol requires us to have an explanation and the fact that we have not received one means that there is a continuing breach, which should be remedied. There might well be some acceptable explanation such as staff absence, illness or change of personnel; nevertheless, we should know what it is and I hope that the minister can be asked to explain why we are in this position.

Secondly, and more important for the future, I suspect that the Presiding Officer will simply say that, because of standing orders, the matter is not within his powers. However, I agree entirely that we should try to establish some convention.

Given that the Parliamentary Bureau has responsibility for setting debates, I suggest that the matter should be raised with it in a letter setting out our concerns and referring members of the bureau to today's debate. I suggest that we invite them to express a view on whether it is appropriate to schedule debates where the Executive has not responded in time and asking them to offer Parliament some comment on whether there should be a minimum period of notice, such as seven days, which would allow Parliament to have the benefit of the Executive response a set period before the debate takes place. It is not only MSPs who are interested in the relocation of public sector jobs; it is plainly a matter of great interest to members of the public. They may wish to see the Executive response and

invite MSPs to make representations in the debate, but they will not have much of an opportunity to do so on this occasion.

I hope that, as a matter of practice, members of the bureau will at least consider that suggestion and revert to us after they have done so with the specific recommendation that there should normally be a minimum period between the publication of the Executive response to a committee report and the holding of the debate. That recommendation should be incorporated in the reply. That seems to me to be an appropriate way ahead, but perhaps the bureau could examine the whole issue and come back to us with a considered view.

**Mr Brocklebank:** I would not disagree with a thing that either Wendy Alexander or Fergus Ewing has said. My only addition to their comments is that, as I mentioned earlier, the tone of Tavish Scott's letter, in which he claims that he regrets that

"there has not been better communication between the Executive and the Committee",

implies in some way that that was partly the committee's fault. He seems to be saying, "It's not my fault. It was a problem of communication between us." It should be stressed that any lack of communication was not on the part of the committee, but on the part of the Executive.

Perhaps it would also be useful to know at what time on Monday the Executive plans to give its response. If it is to be at close of business on Monday, that leaves us only one day to put together our contributions to the debate on Wednesday.

**The Convener:** On Ted Brocklebank's first point, I am quite clear about the fact that no blame attaches to our staff. We have followed the procedures entirely properly. We published our report and we reminded the Executive at the due date—strenuous attempts have been made to secure a response from the Executive.

**John Swinburne:** I will make a brief suggestion in the spirit of reconciliation that is currently prevailing in Parliament. We have just moved into a new building and there are many reasons why the Executive may not have complied with the rules. However, as a member of the newly formed alliance of independents, I am sure that we could take over that debating time on Wednesday and let the committee have another run at the issue at a future date.

**The Convener:** That is a kind offer, John, but I am not sure that it is likely to be taken up.

The suggestions that have been made are generally helpful. I think that, as has been suggested, we should reply to Patricia Ferguson,

welcoming the fact that an apology has been made and that new procedures are to be put in place. We should seek further information about when the report is likely to be received and we should stress the fact that, from the point of view of the committee and of members in general, the earlier the report is available, the better.

We should perhaps write to the Presiding Officer highlighting our concerns about the matter and the issues of principle involved. Perhaps we should also take up Fergus Ewing's recommendation and suggest to the Presiding Officer that the matter should be discussed by the Parliamentary Bureau as a procedural issue. It needs to be discussed properly and its ramifications and implications must be thought out.

**John Swinburne:** Will Wednesday's debate now take place?

**The Convener:** Yes, it will proceed.

We ought to write to the bureau and suggest that the matter be looked at in principle. I think that that is the burden of members' thoughts on the issue. Is that agreed?

**Members** *indicated agreement.*

**The Convener:** If members are content, a motion will be lodged today. I thank members for attending the meeting.

*Meeting closed at 12:45.*





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