

WHAT'S HAPPENING TO WATER AND SEWERAGE SERVICES IN SCOTLAND

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INTRODUCTION

The future of water and sewerage services in Scotland is highly controversial. It has been suggested that this issue may 'rival the poll tax as one of the most contentious political issues of the decade' (Scott 1992).

These services have been provided by Scotland's regional and islands councils since May 1975, the occasion of the most recent re-organisation of local government. As this article explains, it is the current review by the Government of the structure and role of councils which has occasioned the proposals giving rise to recent controversy. However, there are two major underlying factors. The first relates to standards and new requirements, and in particular the capital-investment implications of these. The second, it is argued, following experience in England and Wales, is that Scottish water and sewerage services have been regarded by the Government as a privatisation opportunity. This includes the possible introduction of private capital and management of facilities as well as sale of assets.

The article therefore considers the interplay between these three forces: council re-organisation, investment needs, and privatisation. Meanwhile, it is suggested that the nub of the controversy can now be characterised as whether - and more subtly, to what extent - these services should remain in the public sector, not merely in local government.

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BACKGROUND: PROPOSALS FOR CHANGE

Although privatisation - here, asset sale - of water and sewerage services was announced in England and Wales in 1988, the Scottish Minister for the Environment, Lord James Douglas-Hamilton, stated on 7 December that the Government had 'no plans to privatise water and sewerage services in Scotland. The present arrangements operated by the regional and islands councils are satisfactory'.

Because of its relevance to Scotland, it is important briefly to trace experience in England and Wales. At the time of local government re-organisation there in 1974, and in contrast to the arrangements which would be made the following year in Scotland, water and sewerage services were transferred to ten regional water authorities. These were within the public sector, and each was controlled by a board. The boards originally contained a majority of local government representatives and a minority of central government appointees, but in 1983 local government representation was abolished, while Consumer Consultative Committees and Regional Recreation and Conservation Committees were introduced.

In a second stage re-organisation, the Water Act, 1989, permitted the creation of privatised supply companies. Ten water supply and sewerage companies were established in December 1989. A further 29 companies provide water services only. A National Rivers Authority (NRA) was also established. In a further important development, the Office for Water Services (OFWAT) was created. With the services outwith local democratic control, there are three regulators - the Secretary of State, the NRA and OFWAT.

Scotland did not follow suit, but this appeared to many - proponents and opponents alike - anomalous in relation to the Government's vigorous pursuit throughout the public sector of privatisation opportunities. Accordingly, well before the Government finally announced its proposals for water and sewerage in Scotland in July 1993, the suspicion that it favoured privatisation for these services had already provoked considerable comment and contention.

In June 1991, the Government published its earliest proposals for the re-organisation of Scottish local government (Scottish Office 1991). This consultative paper first contained the suggestion that water and sewerage services should be delivered separately from the new unitary authorities also proposed. Meanwhile, the committee which was reviewing local government re-organisation within the Scottish Conservative party had received a paper

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from a stockbroker analyst which suggested that privatisation was the only means by which the necessary investment could be found to raise facilities to the standards required by the European Community (**Scotland on Sunday** 18 August 1991).

These standards include EC directives on water and sewerage. High levels of investment are needed to meet these requirements, estimated by the Scottish Office at £2.5bn. over the next 15 years, while a further £2.5bn. is required for maintenance of the existing service infrastructure and for new requirements in relation to housing and industry (Scottish Office 1992a).

To great expectation, and apprehension, the Government published its Green Paper on water and sewerage services in November 1992 (Scottish Office 1992a). The paper set out eight options for change, ranging from passing responsibility for these to the new unitary local authorities it had separately proposed (Scottish Office 1992b) to outright privatisation in the form of one or more public limited companies. The first option appeared to be undermined immediately since one reason given by the Government for removal of water and sewerage from individual councils was that under the arrangements it had proposed for Scottish local government as a whole, the new authorities would be too small to manage these services. The issue of organisational scale is discussed later.

Despite the availability of eight options, by reason of the background described above, the debate was polarised from the outset between 'privatisation' and public ownership. Popular opinion overwhelmingly opposed privatisation. Insofar as 'public ownership' was defined, it appeared to be identified with the status quo (as was confirmed in a survey in autumn 1993 commissioned by the Convention of Scottish Local Authorities). This was certainly the pattern of responses to the Green Paper reported by the Scottish Office. A total of 4,834 responses (16% from organisations) were received, 94% of the total favouring continuing public control and 1% privatisation. Moreover, excluded from this analysis - and grudgingly acknowledged in the final paragraph - were 60,000 pre-printed postcards and petitions with 90,000 signatures all opposing privatisation (Scottish Office 1993a).

In July, the Government announced in a White Paper its long-awaited plans for the re-organisation of Scottish local government (Scottish Office 1993b). For water and sewerage, this involved the creation of three Public Water Authorities (PWAs), for North, South-East and South-West Scotland. This

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arrangement, corresponding to Option D in the Green Paper, places the services outwith local government while still in the public sector.

ANALYSIS OF ISSUES ARISING

In this section, three main issues arising from the Government's proposals are considered briefly (organisational scale; political effects; 'moral' issues), while three which are of wider significance (accountability; investment; effects on users) necessitate closer examination. Space precludes discussion of other issues: for example issues which have proved important in England and Wales since 1989 - such as the introduction of water metering, 'affordable bills', supply terminations (presently prohibited in Scotland), and the remuneration of top managers and shareholders. Similarly, more local issues, for example boundaries of the new PWAs, and the employment prospects facing 6,500 council staff across Scotland, are not discussed.

Scale of Organisational Delivery

The Scottish Association of Directors of Water and Sewerage Services had been concerned that in a re-organisation of water and sewerage, the bodies (or body) which would assume responsibility for these services should be large enough to deliver these effectively (**Scotland On Sunday** 18 August 1991). This view is consistent with the Kilbrandon concept of a 'strategic' service (Kilbrandon 1973). The Government's proposed PWAs appear to meet this requirement. This suggests that for these services 'local' will be re-defined to refer to areas approximating in territory more to those served by the privatised electricity companies than those served by local authorities.

Political Effects

A notable feature of the 'water debate' has been the divisions created within the ranks of Scottish Conservatives by privatisation. Analysis of all (19) submissions on the Green Paper from Conservative associations, council groups and committees found only one in favour of privatisation (**Municipal Journal** 2 April 1993). That so few submissions were received from such sources appears symptomatic of the stress caused by this issue. The decision to retain water and sewerage within the public sector can therefore be expected to create political relief for, and within, the party.

For the opposition parties, the position is less clear. It is arguable that the 'threat of privatisation' has had the effect of diverting their attention, like that

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of the general public, from other issues. Since this threat is perceived as 'averted', there is less clarity as to their position on - and indeed appreciation of - other problems such as accountability and costs for consumers (see below) in the proposed PWAs. Initial responses to the White Paper from opposition parties have chiefly been limited to criticism of 'option D' as simply a step towards eventual privatisation as originally intended by the Government.

'Moral' Issues

A unusual feature of the debate - focusing specifically on water supply - has been the extent to which this has been conducted in terms of moral principle. Briefly, this has rested on a view that water is a staple of life and should not be a source of profit. One aspect of this faces in an 'economic' direction: water falls free from the sky and should be delivered at no, or next-to-no, cost. However this view also has a 'moral' aspect: it is seen by some as 'God's water' (eg Macwhirter 1993) for all to enjoy, and its supply should not be a source of profit.

Interestingly, these views are shared elsewhere in the UK. In its research on user views for OFWAT, MORI noted 'some customers regard water services as a very special case, some even believe it should be provided free of charge; others have strong feelings about privatisation' (MORI 1992). The rejection of asset sale privatisation in the White Paper alleviates these 'moral' concerns, but the involvement of private interests inherent in 'option D' suggests they may not disappear and that any future privatisation proposal will revive them.

Accountability: Democratic Or Consumer - Or Both?

The debate has been preoccupied with 'profits out of water', but the White Paper proposals give rise to more complex issues. One is accountability. The Chairman of the Association of Conservative Councillors had expressed particular concern over accountability to the public were private supply companies established (**The Scotsman** 31 August 1992). The proposal to create PWAs does not necessarily remove this, since the management of these boards - which will have responsibility for the same services as presently managed by local authority staff - will not be accountable to elected members. Even joint boards, option B, although unpopular, would have offered some democratic accountability.

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In a single word, the Green Paper suggests managers would be subject to the control of board members who would be 'appointed' (Scottish Office 1992a Para. 5.4). Clearly this would be by the Scottish Secretary. Thus, local political accountability would be diminished, while simultaneously there would be unacknowledged centralisation of power. The type of political accountability offered by Public Water Authorities is problematic. While they would be accountable to the Scottish Secretary, this model is necessarily 'attenuated' and limited in relation to ministers and Parliament (Johnson 1982). Most strikingly however, PWAs offer less political accountability to the public.

Meanwhile, in lieu of political accountability, the Government proposes to substitute a form of consumer protection in the form of un-named 'ample precedents for this' and the Citizen's Charter which, it is claimed, has 'seen a significant strengthening of the consumer's voice in analogous circumstances' (ibid.). This is discussed further below. In effect therefore, Scottish water and sewerage services are to be placed in a position analogous to that of the pre-1989 English and Wales regional water authorities, with electoral accountability swapped for consumer protection. The Green Paper does not acknowledge, far less explain, why these are seen as alternatives. Yet clearly they serve different purposes and offer quite different things to the public in its dual electoral and consumer capacities. Moreover these can co-exist already under council provision: Fife Regional Council, for example, has service standards similar to those within OFWAT's Guaranteed Standards Scheme (Fife RC, 1993).

Investment

At present, in common with other local authority services, capital investment in water and sewerage services is made not on the basis of a cash transfer from Government, but its consent - under S.94 of the Local Government (Scotland) Act, 1973 - to councils to borrow to meet the cost of investment in capital projects such as the sewerage network or water treatment plants. On this method, the Scottish share is apportioned as ten eighty-fifths of that for England. However, in the case of water and sewerage services, there has been no equivalent English expenditure programme since privatisation. Consequently, there is no direct link in relation to which the Scottish allocation can stay in line, with the effect that this allocation decision has become more discretionary within the Scottish Secretary's overall programme.

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In fact local authorities can claim that since before 1989 they have given greater emphasis to water and sewerage investment than the Scottish Secretary in that their investment has actually exceeded his consent. This has been accomplished by transferring consents from other council services and by sale of assets. Total consents for 1987/88 to 1991/92 were £598m. whereas the actual investment total in this period was £638m. (CoSLA 1993) - in effect, an additional investment averaging £8m. annually arising from local decisions.

Councils can borrow at rates which are favourable, from sources such as the European Investment Bank and the Public Works Loan Board. Nevertheless, interest payments on these capital debts as a proportion of the cost to the final user are onerous - 40-50% of community water charges in 1992/93 (**Scotland on Sunday** 23 August 1992). However the absolute cost to the user is likely to be higher under a system based on borrowing from private sources of capital because interest rates will be less favourable to the water agency. Moreover this does not take into account the dividend expectations of shareholders and remuneration expectations of top managers, a major consumer grievance in the South.

In England and Wales, the new companies enjoyed financial benefits at taxpayers' expense: 'when the water authorities were privatised, the Government wrote off debts of nearly £5bn. and gave the industry a cash gift of nearly £1.5bn.' (Scottish & Westminster 1992). Following privatisation, investment by the water companies increased considerably, but over 60% of this was 'financed from current cash flows; in other words it has been paid for by customers. This source of finance would have been available to the water industry whether it were privately or publicly owned' (ibid.).

Conservatives have pressed Labour as to how it would resolve the problem of the additional investment needed - for example by increasing taxation, or by reducing public expenditure in other areas (**Scotland On Sunday** 23 August 1992). Labour's shadow Minister for Scottish Affairs, Henry McLeish, has suggested that 'if Scotland receives the same treatment as England and Wales with a debt write-off, a green dowry and flexibility for local authorities to secure extra resources, then most of the challenges of the 1990s can be dealt with' (Scotsman 4 September 1992).

However, the 'investment question' is not solved by pointing to more advantageous public borrowing which could be released by more generous consents, or suggesting that write-offs can be used for public services too. There is a third aspect which reveals that Government creates a playing field

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which is far from level. The Institution of Water and Environmental Management, whose members work in both the public and the private sectors, identifies a 'strange contradiction - if the English water PLCs put up their charges ... that is private investment and acceptable, but if regional councils do the precisely the same, that is public expenditure which is controlled by the Government. If in fact water and sewerage expenditure is funded directly by those served, it does not impinge on any other aspect of general public expenditure and need not be classified as such' (IWEM 1993).

Cost And Quality Issues For Consumers

A National Consumer Council study found a high level of satisfaction in Scotland, with 91% of users 'very' or 'fairly' satisfied with the water and sewerage service they received, as compared with three-quarters in England and Wales. The dissatisfaction rate in Scotland (3% of users) was noticeably less than that for the England and Wales (one in eight) (NCC 1991).

One reason would appear to be the cost to users. The average household bill in Scotland for water and sewerage in 1992/93 was £102 (Scottish Office 1992a). The equivalent figure in England and Wales for the same period has been estimated by OFWAT as £170, where, since privatisation in 1989, 'domestic consumers have seen their annual water and sewerage bills increase on average by 5% more than the rate of inflation each year' (Scottish & Westminster 1992). It has generally been accepted that charges for users will have to increase because of the need to invest. While this appears to be true, the extent of this appears to depend on who is responsible for running the services. Fife Regional Council commissioned Coopers, Lybrand to examine the effect of services being run by the public and the private sectors who found that charges would rise over the next 15 years by 95% in the public sector, but 152% in the private sector (**The Scotsman** 25 June 1993).

Meanwhile, EC standards have risen since 1989, and new requirements will raise these still further. This has been regarded as an important reason for past increases in charges to users. OFWAT has explicitly welcomed a debate on quality, including the issue of whether standards are being set at an unnecessarily high level. However while average bills for Scottish water and sewerage services have risen 'almost 50% in the last 5 years' (Scottish Office, 1992b, Para. 21.3), this has been partly due to an important but extraneous factor - non-payment of the poll tax. In Strathclyde, for example, the estimated average household bill for water in 1992/93 was £56, but would otherwise have been £40 (Strathclyde RC 1993). Nevertheless, bills are

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expected to rise in future because of investment needs (Scottish Office 1992a Para. 1.18).

It might have been expected that there would have been a backlash from users against the cost implications, yet not only is there little sign of this, but there is evidence that these requirements are accepted. In its research for OFWAT, MORI found that within a range of 14 key user standards, the need for sewerage treatment to meet current EC standards was rated as 'essential' or 'very important' by 88% of respondents, and ranked fifth equal in importance overall (MORI, 1992).

As compensation for loss of democratic control, the Government regards standards of operational service as a key means of protecting the citizen's interest - an important matter since the advent of the Citizen's Charter initiative (Prime Minister 1991). Although the water companies in the South are in the private sector, they are within the ambit of the Charter. OFWAT has suggested that households should be entitled to improved compensation for poor service under the Guaranteed Standards Scheme (**Financial Times** 23 September 1992) and that existing sanctions in relation to these standards, which take the form of a cash penalty on suppliers, should be doubled - to £10.00.

CONCLUSIONS

Even before the White Paper was published, there was little doubt as to the cast of Scottish public opinion or that of the opposition parties. The Government's decisions not to extend to Scotland changes made in England and Wales in 1974, 1983 and 1989, and its preference for the Public Water Authority option in 1993, can each be seen as appeasement. In the 1970s and 1980s this was successful but possibly unrecognised; in the 1990s its effect may be temporary only.

As argued above, the debate has always been polarised around two options, and the response to the Green Paper indicates not simply that there is little support for movement to any other option (not just 'privatisation'), but that there is strong opposition to any change. The option of PWAs is preferred by almost no-one, favoured by 64 respondents or 0.04% of all respondents to the Green Paper (Hansard Written Answer Col 44 19 July 1993). CoSLA's publication in November 1993 of a poll indicating 95% support for the status quo simply re-confirms public opposition. It must be a matter of concern that the provision of a virtually universal public service is to be put on a basis

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which commands so little support when the same consultation indicates such overwhelming support for the status quo. In this latter respect, re-organisation of water and sewerage services is arguably more contentious than the poll tax.

The analysis above does not suggest that the inherent needs of the industry or users are such that removal of water and services from local government control is a pre-requisite for continuing upgrading. In relation to past investment and current standards, local authorities appear to have managed these services well - and are regarded by the public as having done so. Meanwhile experiences in England and Wales immediately before, and particularly since, privatisation reveal several detrimental outcomes for the public, both as consumers and local electors, in relation to bills and accountability, while the resulting service standards do not appear to be superior to those which currently obtain in Scotland. Fundamental questions therefore remain as to the need for re-organisation of these services.

The Government continues to look for private finance opportunities for these and other public services, as Ian Lang has confirmed (Hansard Written Answer Col 245 3 November 1993). Public Water Authorities may trigger new, private funds, but experience in England and Wales indicates that the major burden of this would in any case be passed to users. Meanwhile the Government's proposals in relation to accountability substitute unspecified consumer protection in the flimsy Charter mould for present political accountability to voters. (It might mischievously be suggested that the price of democracy lost in England and Wales - the penalty on suppliers for poor service - had been set originally at £5, but has subsequently been discovered to be worth twice this sum.)

Moreover the Government's proposals to create three PWAs fits comfortably into the now well-established pattern of centralisation as the dominant influence in central-local relations since 1979 (eg Stoker 1991; King 1993), but goes beyond these examples by removing water and sewerage services from local government altogether, as has been accomplished in two stages in England and Wales.

This suggests a possible scenario for the period following 1996, the date when the Government expects the PWAs to be vested. Fears that it remains intent on privatisation in the longer term are not likely to be assuaged by the recent announcement by the Scottish Office of amendments to public finance regulations (the Private Sector Initiative) which have the effect of permitting private sector companies to build, own and operate water and sewerage

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facilities (**Municipal Journal** 26 August 1993). At the time of writing, the publication of the Government's 'reorganisation' legislation - the Local Government etc (Scotland) Bill - is imminent. Stormy waters are forecast.

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