Benchmarking and Scottish Water

1. Benchmarking has been used over a number of years to assess Scottish Water’s performance with respect to our English and Welsh peers. The main areas where benchmarking has been used are as follows:
   - Service levels using the Overall Performance Assessment (OPA)
   - Operating expenditure using an econometric modelling approach
   - Capital maintenance using an econometric modelling approach,
   - Capital enhancement using a cost base approach

2. The approaches adopted are all relatively complex and have evolved through time since first used by Ofwat in the early 1990s.

Scottish Water Experience

3. Our experience of benchmarking revolves around it being used to assess both existing financial and service performance and in the setting of future targets.

4. Benchmarking of Scottish Water started back in 2000 with the previous three Water Authorities and each Authority developed its own set of information that was different from that which was generally used to assess their own performance.

5. With any approach that requires comparison, the data being used must be based on the same definitions across all the organisations that are being compared. Any benchmarking system that does not do this will struggle to be credible since any decisions made using it can be easily contested on the grounds of not comparing ‘like-with-like’.

6. On the creation of Scottish Water, considerable time and resource was committed to developing data that was consistent with our English and Welsh peers in order to allow valid comparisons to take place. Although it is not possible to quantify this time and resource precisely it should be noted that relative to the service and efficiency improvements this has assisted in identifying, this cost has been modest. Moreover, the process has assisted us in developing our knowledge and understanding of our business.

7. In the Water Sector, benchmarking techniques vary considerably from straightforward unit cost comparison to much more mathematically complex methodologies. The benchmarking tools used have been developed over a significant period of time with academic economists, as well as respected international economic and engineering consultancies.

8. The data used in the benchmarking exercises is audited by a set of independent auditors to ensure that it has been put together accurately and corresponds to the definitions adopted. The benchmarking tools are continually reviewed and some aspects are retired as they become less relevant and are replaced with new tools that are developed through a consultative/joint working approach.
9. In the water sector the benchmarking tools adopted allow us to be clearly ranked against our peer companies. The tools can also identify specific service gaps and cost efficiencies with respect to an individual company or group of companies, which can be expressed as simple numeric targets to achieve within a given time period. Performance against these targets can be monitored. Although the messages are clear and easy to understand across interested stakeholders, the process underneath this is technically complex and can be information intensive.

10. Scottish Water initially resisted the adoption a benchmarking approach and its place within a rigorous price control process adopted by the Water Industry Commission. It took time before we culturally accepted the role and value of benchmarking for Scottish Water.

11. Scottish Water did initially question the benchmarking approaches, identifying technical issues with the methodology that caused the results to be biased or developing arguments about why it was not appropriate to use the methodological approach as it does not account for the specific geographic conditions in Scotland. The level of intensity associated with this questioning rose as the benchmarking was used to identify significant cost efficiency targets.

12. The benchmarking tools used by the Water Industry Commission and Ofwat allow for ‘Special Factors’. These relate to the legitimate differences outside of management control that can be suitably justified and quantified to the satisfaction of the Economic Regulator and independent auditors. Over time Scottish Water became more familiar with the benchmarking tools and the nature of ‘Special Factors’.

13. Broadly speaking it is not possible for any methodological approach to be absolutely accurate or take account of all availing circumstances. Our experience suggests that in order for benchmarking to be accepted it is generally necessary for those it will affect to have some involvement in developing it and for experts in the benchmarking field to have input into the methodology. It also helps if it is understood by those it impacts upon and that they are capable of replicating it. There also needs to be a commitment to continually reviewing the approach to ensure it is fit-for-purpose and developing any proposed changes in a collaborative manner.

14. The benchmarking approach adopted has external validation as it has been developed by the Water Industry Commission and Ofwat. Within Scotland, the Water Industry Commission has to formally verify whether we have met the performance targets set and undertakes audits to check the validity of our data and claims. Within Scottish Water the data underpinning the critical elements of the benchmarking system are collected and audited yearly in most cases in order to ensure that performance against any targets set can be monitored effectively.

15. After 10 years of benchmarking with an accepted set of benchmarking models and techniques the industry is now entering a period where techniques and models are being reviewed to ensure that service and productivity improvement can continue.
16. It is also worth noting that the results of benchmarking approaches in the Water Sector have been made publicly visible and understandable which in itself drives productivity improvement and changes behaviours. The approach adopted across the UK water industry allows simple 'league tables' to be developed that rank companies performance on a service and cost basis. These tables are understandable to the public and can provide strong incentives to improve performance. It is, however, important to ensure that improving the 'league table' position in publicly available measures of performance does not become an end in itself.

Scottish Water

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