

SCOTTISH WATER'S COMPLIANCE OFFICER'S REPORT

ANNUAL COMPLIANCE OFFICER'S REPORT FOR 2024/25

COMPLIANCE OFFICER'S ACTIVITIES

ANNUAL REPORT ON BUSINESS SEPARATION 2024/25

1 Introduction

This report fulfils the reporting requirements of the Water Services (Intra-Group Regulation) Directions 2006, as amended (the "Intra-Group Directions") in relation to 2024/25. It covers the duties of the Compliance Officer and implementation of practices, procedures and systems to ensure compliance with the Market Directions. The specific responsibilities of the Compliance Officer are:

- to provide advice to Scottish Water on compliance with the Market Directions;
- to ensure the ring-fencing of Business Stream so that its management and operations are independent from Scottish Water; and
- to ensure that each Licensed Provider is treated no more or less favourably than any other.

The associated Compliance Statement sets out the detailed arrangements by which Scottish Water will comply with its responsibilities in 2025/26.

2 Compliance with the Market Directions

2.1 *Advice to Scottish Water*

The Compliance team resolves enquiries from the organisation in relation to compliance with the Market Directions. In 2024/25 there were 37 enquiries including on specific issues such as provision of non-market related collateral to Business Stream, the limits on the visibility of financial information for group accounting purposes, the treatment of certain customer enquiries for gap sites without Licensed Providers and the approach to reporting potential conflicts of interest.

In relation to the first item mentioned above, Business Stream had asked if Scottish Water would be willing to share a copy of the Scottish Water expenses policy as it was planning to revise its own policy to ensure it fulfilled controls on Scottish public sector bodies more widely. This policy is not related to market activities and so it was considered reasonable in the circumstances to share it with a subsidiary of Scottish Water for information. It is, in any case, a matter for Business Stream and their board to determine its expenses policy, and how this is monitored.

Compliance training was provided to all new starts within the key market-facing teams and new senior staff.

2.2 *Compliance with the Intra-Group Directions*

Scottish Water is required to manage its systems and processes so that no Licensed Provider is able to access Scottish Water's confidential information, or that of any other Licensed Provider. In 2024/25, no Licensed Provider had access to any of Scottish Water's premises, equipment or facilities. Scottish Water's systems were only accessible to people working for or on behalf of Scottish Water, and subject to password and profile-controlled access. As set out in the Compliance Statement, in 2024/25 there were four portals accessible to Licensed Providers with the following functionality (i) to allow the submission of requests for operational activities; (ii) to see information about the wholesale services in general; (iii) to view general information about ongoing operational activity; and (iv) to view information about the trade effluent service, but only in relation to customers that registered to them, and only for the period of registration. Over 2025/26, further "self-service" functionality may become available, for example in relation to business smart metering, should that be rolled out in the period.

Intra-group contracts

At the end of 2024/25, there were four intra-group contracts between Scottish Water and Business Stream, each of which has been approved in advance by the Commission:

- Business Stream's use of the Scottish Water marque was covered by a licensing agreement;
- Business Stream provided a meter reading service to Scottish Water in relation to non-market domestic properties managed by a third party to whom Scottish Water was a sub-contractor; and
- Scottish Water provided two services to Business Stream: Internal Audit services; and Insurance and Taxation Advice.

In order to allow Scottish Water Internal Audit employees to carry out audits on Business Stream activities, two individuals have time-limited password-controlled access to a secure portal for the sharing of sensitive documents.

There were no contracts between Scottish Water and any other Licensed Provider. There are currently two Licensed Providers which have affiliates that own or operate Wastewater Treatment Works under PFI contracts with Scottish Water. In accordance with the annual process, Scottish Water wrote to each relevant Licensed Provider in 2024/25 asking them to ensure the confidentiality of the market information held by the affiliated PFI contractor.

Investigations

The Compliance team identified and/or investigated four compliance concerns in 2024/25. These related to:

1. The potential for a Licensed Provider to raise concerns about the level-playing field in the market: This was identified internally as a part of a risk review process. The potential concerns that might be raised were considered together with probability and impact. Controls and mitigating factors were considered. It was concluded that all areas of potential concern were well-monitored and managed, and that no further action was necessary.
2. Reviews of two elements of market transactions:
 - The first area related to arrangements for measuring compliance with operational KPIs when activities are paused while waiting for Licensed Providers or customers to take action; and
 - The second area related to the use of data correction mechanisms where data updates cannot be carried out through transactions on the Central Systems.

In each case, the Compliance Team was asked by internal stakeholders to provide assurance on the operational processes. A sample audit of cases was carried out to determine the nature and effectiveness of existing controls. Where required, these controls were clarified with the relevant subject matter experts, and guidance was refreshed.

3. The categorisation of certain service requests relating to gap sites: As part of the annual review of Operational Code processes, the Compliance Team raised a question about the attribution of steps in the Gap Site process as there seemed to be a lack of alignment between the process steps in Dynamics and transactions to the Central Market Agency ("CMA") systems. However, on investigation, it became clear that the apparent mis-alignment was due to re-attribution of process steps to the relevant Licensed Provider once a gap site owner or occupier appointed a Licensed Provider. No further action was necessary.

There were no formal complaints from Licensed Providers or the Commission in 2024/25.

2.3 Compliance with the Governance Code Directions

Scottish Water is required to ensure that Business Stream has an independent management structure and independent operations. Throughout 2024/25, this was delivered in line with the requirements of the Governance Code through Scottish Water Horizons Holdings Limited (SWHH), and Scottish Water Business Stream Holdings Limited (SWBSH), which exercise Scottish Water's ownership responsibilities in relation to Business Stream.

SWBSH comprises the Chief Executive of Business Stream, the Non-Executive Directors of Scottish Water, including the Chair, and Scottish Water's Chief Financial Officer. As the Chief Executive Officer of Scottish Water is the Accountable Officer for all Scottish Water group companies, excluding Business Stream, he attended SWBSH Board meetings as an observer, but it has been agreed with the Commission that he will no longer attend SWBSH Board meetings, nor receive meeting papers, with effect from 25th March 2025.

As required by its Standard Licence Condition A9 ("SLC A9"), Business Stream provided Scottish Water with the appropriate assurances that, during the period from 1 January to 31 December 2024, it (i) only received financial support on commercial, arm's length terms; (ii) had an appropriate financial structure; and (iii) ensured that its Scottish customers were not disadvantaged by its operations in England and Wales.

2.4 Compliance with the Codes and Services Directions

Scottish Water complied with the Codes and Services Directions in 2024/25. Operational Code performance is reported to the Board and out-performed the corporate target. Market Code metrics also out-performed the corporate target. These obligations were subject to external audit by the CMA with no significant negative findings. Both metrics compared favourably with the equivalent standards in the English and Welsh market.

The Compliance team monitored operational performance to ensure that each Licensed Provider was treated no more or less favourably in relation to compliance with the operational standards, and in terms of recovery in the rare instances of KPI failure. There was no evidence of preferential treatment to any LP, either in terms of pass/fail KPI performance or the time taken to resolve KPIs (outperformance of KPI).

2.5 Other market requirements

There are a number of other requirements within the Market Directions. The following activities were carried out to fulfil these obligations:

- The Compliance team kept records of all meetings between Scottish Water and Business Stream. These records were cross-referenced against the equivalent records held by Business Stream to ensure consistency.
- Each Licensed Provider was offered a senior-level meeting with an appropriate staff within Scottish Water. The Business Stream and Scottish Water Chief Executives met 6 times in 2024/25 – the Compliance Manager attended each of these meetings.
- Scottish Water continued to develop its policy on Section 29E departures through the "Partner Ecosystem" approach. This will be reviewed in the light of the Long-Term Strategy.

3 Conclusion

In the 2024/25 financial year, Scottish Water continued to operate robust separation and market-facing structures. Systems and processes are in place to monitor the level of Scottish Water's performance and there continues to be effective identification and remediation of potential and actual issues. Scottish Water is committed to ensuring that its separation and market obligations are achieved.

Emma Campbell
Compliance Officer