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# Review of Guernsey Water



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I have prepared this report under an agreement with the Public Accounts Committee of the States of Guernsey, facilitated by Section 96C of the Government of Wales Act 1998. The Wales Audit Office study team that assisted me in preparing this report comprised Gill Lewis, Chris Bolton, Louise Fleet, David Metcalfe and John Herniman.

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**Guernsey Water is providing value for money within the context of its operation as an island water-supply company. While there are some opportunities for achieving additional value for money from Guernsey Water, there appear to be greater opportunities which could be realised through changes in the relationships between Guernsey Water, the Public Services Department and also the States of Guernsey.**



	<b>Summary</b>	<b>6</b>
	Recommendations	7
	<b>Detailed Report</b>	<b>8</b>
	The value for money provided by Guernsey Water depends upon Guernsey Water as well as the activities of the Public Services Directorate and the States of Guernsey	8
1	<b>Guernsey Water is providing value for money for the States of Guernsey within the context of its particular business and the island setting</b>	<b>9</b>
2	<b>Developing the current governance arrangements for Guernsey Water would enhance strategic risk management and support greater value for money</b>	<b>15</b>
	Enhancing the performance management of Guernsey Water by the Public Services Directorate would help to focus on value for money	16
	Centralisation of Guernsey Water support services into the Public Services Directorate needs to clearly demonstrate the value-for-money gains achievable	16
3	<b>The States of Guernsey needs to clearly articulate its long-term aspirations for water in Guernsey</b>	<b>18</b>
	Potential value-for-money gains from a Guernsey Water merger with waste-water operations need to be balanced against a clear understanding of the potential risks and benefits	18
	Commercialisation of Guernsey Water (in line with existing Guernsey models) is unlikely to provide any additional value for money that cannot be delivered via improvements to the existing structural arrangements	19

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Appendices	20
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Appendix 1 - Guernsey Water - Unit cost comparisons	20
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Appendix 2 - Methodology	29
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## Summary

- 1** The States of Guernsey (the States) Public Accounts Committee (PAC) was established in 2004 to ensure the proper scrutiny of the financial affairs of the States. This involves the PAC examining whether public funds have been applied for the purposes intended by the States, and that extravagance and waste are eradicated. The PAC carries out investigations into States' departments, either directly or via third parties, in this case the Wales Audit Office.
- 2** Guernsey Water (GW) is the sole water utility on Guernsey which collects raw water, stores and treats it to a potable standard, and distributes approximately 5,000 megalitres of wholesome drinking water to approximately 60,000 people and 24,000 premises on the island. Waste-water collection, treatment and disposal are not part of GW's operations. These activities are the responsibility of other business units, which are part of the Public Services Department (PSD).
- 3** Guernsey Water is financially 'self sufficient' in that it raises its income directly from customers via water charges which are based on a 'rateable value' or the volume of water consumed. By comparison with mainland United Kingdom (UK) water companies, it is a relatively small operation (income: £7 million per annum) which makes direct comparisons difficult. The most comparable organisations with GW operations are the Isle of Man (income: £9 million per annum) and Jersey (income: £12.5 million per annum).
- 4** The Machinery of Government (MoG) review in 2004 resulted in significant changes in the management and governance of GW. It moved from the 'stand-alone' States Water Board which was self-governing, with its own dedicated Board, into the much larger (£40 million per annum) PSD which comprises several large business units including, airports, harbours and States Works.
- 5** Guernsey Water is currently in the process of a major capital programme to upgrade its infrastructure of water-treatment works, distribution mains, pumping stations and storage facilities, to meet the objectives detailed in the 2003-2013 Business Plan.
- 6** Other Guernsey utilities – post, electricity and telecommunications – were subject to commercialisation in 2002. At the time, the water business was not considered to be appropriate for commercialisation.
- 7** This report summarises the work of the Wales Audit Office on behalf of the PAC to establish, 'is GW providing value for money for the States?' Overall, we have concluded that GW is providing value for money within the context of its operation as an island water-supply company.
- 8** While there could be some opportunities for achieving additional value for money from GW, there appear to be greater opportunities which could be realised through changes in the relationships between the PSD and also at States level.





- 9 Developing the current GW governance arrangements would enhance strategic risk management and would also help identify opportunities for further value for money. There is a need to provide an appropriate level of challenge to GW by the PSD Board.
- 10 Enhancing performance management of GW by the PSD would help it to focus upon value for money at a strategic level. PSD level performance management needs to focus on the big issues rather than less significant areas as part of securing the greatest value for money.
- 11 Value for money that could be achieved by the centralisation of GW support services into the PSD, needs to be reviewed and clearly demonstrated. The GW review should link with any wider review of support services within the PSD.
- 12 To secure greater value for money over the medium to long term, the strategic direction for water in Guernsey needs to be clearly articulated by the States, to ensure the PSD's and GW's plan to reach the aspirations of the States in the most effective manner is achieved.
- 13 A merger of the GW activities with waste-water activities could bring value-for-money gains and much wider benefits to the States. However, this needs to be carefully reviewed to ensure the financial arrangements (funding/billing/cost recovery) for waste water are clarified, and risks and benefits are fully understood before any potential merger is considered.
- 14 The commercialisation of GW (in line with existing Guernsey models) is unlikely to provide any additional value for money that cannot be delivered via improvements to the existing structural and procedural arrangements.

## Recommendations

- 15 In the light of our examination, we make the following recommendations:
  - a The challenge to GW provided by the PSD Board needs to be strengthened to appropriately reflect the mitigation of the risks identified.
  - b The States and the PSD need to clarify arrangements for the future regulation of GW. If PSD or another body is to undertake this role, it needs to strike an appropriate balance between governance and regulation.
  - c The performance management of GW by the PSD needs to focus on key issues of strategic importance and value. Jointly developing and agreeing a set of balanced (financial, operational, customer focused and corporate health) indicators alongside a reporting and monitoring framework, will help to focus on key issues.
  - d The centralisation of GW support services should be supported by clearly communicated business cases which demonstrate the benefits of the proposals.
  - e The States needs to clearly articulate its long-term aspirations for water in Guernsey to ensure the PSD and GW are able to develop coherent business plans and strategies.
  - f The financial and organisational arrangements for waste-water activities need to be clearly understood to establish if any additional value for money could be delivered.

## Detailed Report

### The value for money provided by Guernsey Water depends upon Guernsey Water as well as the activities of the Public Services Directorate and the States of Guernsey

- 16 The value for money provided by GW is dependent upon the activities of key stakeholders and its relationships with them. The principal internal stakeholders for GW are the PSD and the States.
- 17 While the activities within the control of GW have a significant impact upon its ability to deliver value for money, activities within the control of the PSD and the States also impact on value for money. The activities of stakeholders cannot be controlled by GW; it can only seek to influence these stakeholders through its relationship with them.
- 18 We have structured our report into three parts to reflect these levels of influence upon the value for money provided by GW. This is illustrated in [Exhibit 1](#). Part 1 of the report considers GW itself, Part 2 the PSD, and Part 3 the issues which are relevant at a wider States level.

Exhibit 1: Guernsey Water value for money influences







## Guernsey Water is providing value for money for the States of Guernsey within the context of its particular business and the island setting

- 19** There is no single indicator which provides a comprehensive measure of the value for money provided by a water-supply company. To evaluate the value for money provided by GW, we took a broad view across a range of measures and indicators, including a number which are used and reported by the UK water regulator – the Office of Water Services (Ofwat).
- 20** Sound and effective business processes are essential for any organisation in providing value for money. Alongside key quantitative measures, we also considered the effectiveness of the key business processes within GW: financial management, performance management and corporate governance.
- 21** Guernsey Water is significantly smaller than the majority of UK water companies, which makes direct comparisons difficult. In addition, factors such as the benefits available to UK companies from economies of scale, proximity to the marketplace for specialist equipment and supplies, and the availability of a larger pool of people with water-industry skills and expertise, all have an influence upon the value for money provided by GW.
- 22** Within this context, GW is providing value for money for the States, particularly when compared to its closest comparators, other island water suppliers. Although not specifically a focus of this review, measures of water quality and customer satisfaction also indicate that GW is providing a quality product and service to its customers. The following comparisons on costs have been made on the basis that water quality and customer service have not been significantly compromised.

### **Guernsey Water compares favourably with other water companies, including small island companies and larger UK-based organisations**

- 23** Some of the key indicators of value for money we considered are the same as those used by Ofwat. These provide information on relative operating efficiency using unit-cost comparisons from two customer-based perspectives: unit costs per cubic metre of water delivered and unit costs per property billed.
- 24** Costs to the 'customers' for each of these unit-cost perspectives considered by Ofwat can be broken down into three discrete components: costs of 'operations', of 'capital maintenance' and of 'return on capital'.
- 25** We have not used an 'average household water bill' comparison as it does not prove to be a useful comparator or reliable indicator of value for money. This is due to a number of factors which include the differing capital funding arrangements between water companies, socio-economic influences, such as population density, the company's profit margins and requirements for shareholder dividends.
- 26** The performance of GW relative to the UK average, the best and the worst-performing water companies in the UK, and the water businesses in the Isle of Man and Jersey, is summarised below using 2004/2005 information. More detailed information is provided in Appendix 2.

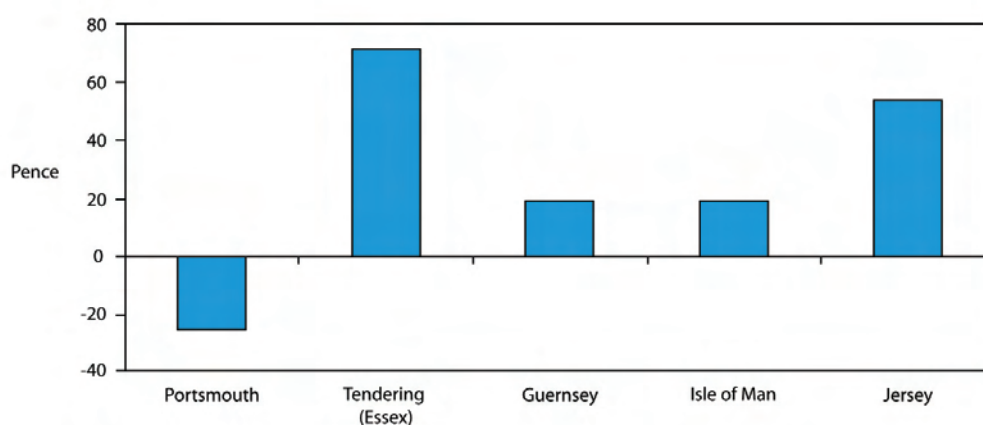
## Costs to 'customers' are lower than other island comparators

- 27** In broad terms, the lower the unit cost of the water provided to 'customers', the potentially better value for money that business is providing, as long as water quality does not deteriorate. The best-performing water companies in the UK tend to have the lowest costs to 'customers'.
- 28** **Exhibit 2** illustrates the cost to 'customers' per cubic metre of water supplied, relative to the UK average of 76 pence per cubic metre. While GW's costs are above the UK average, its costs are significantly lower than those for Jersey and the highest-cost water companies in the UK.
- 29** If the costs to 'customers' are considered from the perspective of unit cost per property billed, a similar indication of value for money is presented. Guernsey Water, at £202 costs per property billed, is above the UK average of £153. This compares to £102 for the water company with the lowest costs and £200 for the company with the highest. When compared with its other island comparators, which have unit costs to 'customers' of between £267 and £286 per property billed, GW is significantly lower.

## Costs of 'operations' are lower than other island comparators

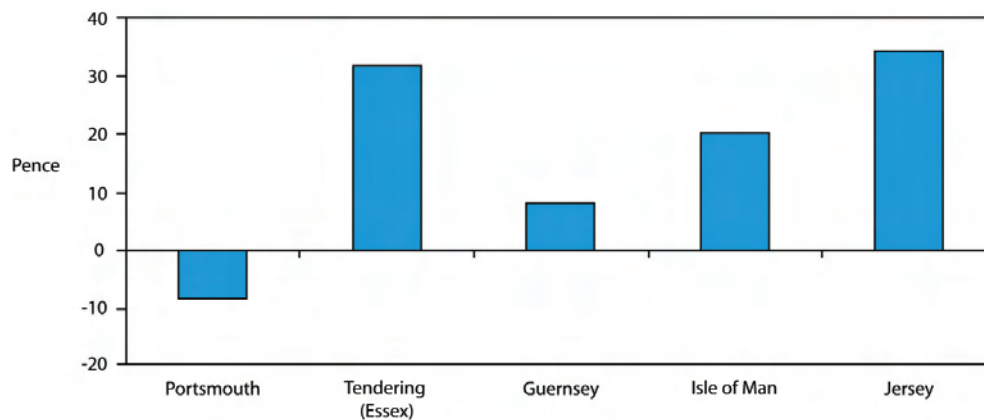
- 30** Costs of 'operations' are a reflection of what it costs to actually run and operate the organisation of the water business to deliver water to its customers. These include costs of staff, energy, materials and contractor costs but exclude costs relating to assets and capital spending. The best performing water companies will tend to have the lowest costs of operation.
- 31** **Exhibit 3** illustrates the costs of 'operations' per cubic metre of water supplied relative to the UK average. While GW's costs are above the UK average, its costs are significantly lower than those for the Isle of Man, Jersey and the highest-cost water companies in the UK.
- 32** If the costs of 'operations' are considered from the perspective of unit cost per property billed, a similar indication of value for money is presented. Guernsey Water, at £88 cost per property billed, is above the UK average of £65. This compares to £52 for the water company with the lowest costs and £98 for the company with the highest. When compared with its other island comparators, which have unit costs of

**Exhibit 2: Costs to 'customers' per cubic metre of water relative to the UK average of 76p**





**Exhibit 3: Costs of 'operations' per cubic metre of water relative to the UK average of 33p**



'operations' of between £138 and £175 per property billed, GW has a significantly lower cost.

#### **Costs of 'capital maintenance' are close to the UK average**

- 33** Costs of capital maintenance are a measure of a water company's expenditure on the maintenance and replacement of its above and below-ground infrastructure necessary to continue the operation of its business. As a value-for-money indicator, the lowest costs are not automatically a feature of best-performing companies.
- 34** Low cost can be a reflection of an under-funded capital programme, while high capital costs can be a feature of an extensive 'catch-up' programme of upgrading poor-quality assets. High or low costs can also be considered a feature of a poorly planned or delivered capital maintenance programme.
- 35** In determining value for money, we have considered a level of capital maintenance expenditure that is close to the UK average as being the most appropriate indicator of value for money.

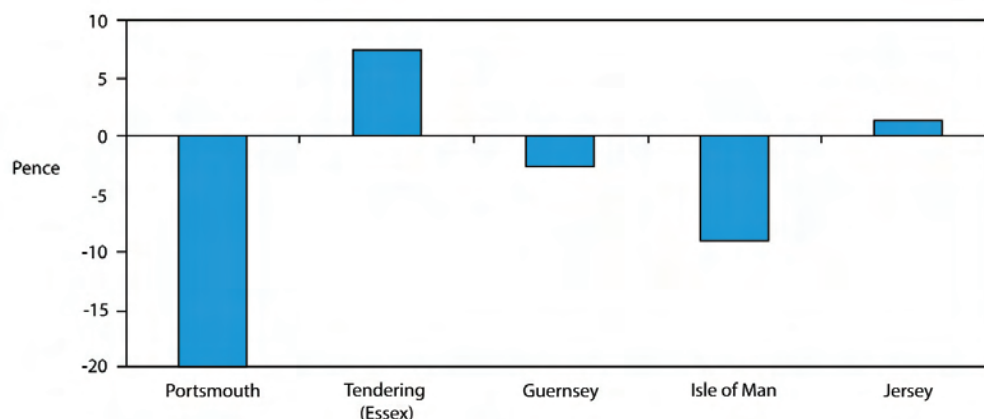
**36** Exhibit 4 illustrates the costs of 'capital maintenance' per cubic metre of water supplied relative to the UK average. Guernsey Water's costs are just below the UK average, higher than those for the Isle of Man and lower than those of Jersey.

- 37** If the costs of 'capital maintenance' are considered from the perspective of unit cost per property billed, a similar indication of value for money is presented. Guernsey Water, at £44 cost per property billed, is below the UK average of £47. This compares to £21 for the water company with the lowest costs and £62 for the company with the highest. When compared with its other island comparators, Jersey has unit costs of 'capital maintenance' of £49 while the Isle of Man has costs of £35.

#### **Costs of 'return on capital' are similar to other island comparators**

- 38** Return on capital is a reflection of the remuneration to the providers of capital and the funding requirements for investment. It is a complex measure which is influenced by many factors such as borrowing arrangements and capital investment requirements.

**Exhibit 4: Costs of ‘capital maintenance’ per cubic metre of water relative to the UK average of 23p**



**39** Indicators for costs of ‘return on capital’ present a similar picture to costs to ‘customers’, costs of ‘operations’ and costs of ‘capital maintenance’. While costs are above the average UK mainland water companies, they are either comparable to, or lower than, those of its island comparators.

**40** Costs of ‘return on capital’ should not be considered in isolation, but, in the context of the other comparators, examined as part of establishing a broad picture of the value for money provided by GW.

#### **Management and administrative costs require ongoing monitoring and evaluation**

**41** As part of developing a comprehensive picture of the value for money provided by GW, it is necessary to consider its management and administrative costs as part of a wide range of indicators. In general, lower management and administration costs can be seen as a broad indicator of value for money.

**42** When comparing the GW costs of management and administration per property billed with the best-performing water

companies in the UK, the GW costs appear to be relatively high. In comparison with Jersey, the costs are very similar while being slightly higher than those of the Isle of Man, as illustrated in [Exhibit 5](#).

**43** In contrast, the other comparisons, which are illustrated in [Exhibit 5](#), present a different picture of management and administration costs, when they are considered as a percentage of the water company’s total expenditure. Based on this indicator, GW appears to perform very favourably spending 31 per cent of total expenditure on ‘management’ compared to 35 per cent for Cambridge Water and 32 per cent for Portsmouth Water, both of which are considered to be amongst the best performing UK water companies.

**44** The complexity of the indicators on management and administration costs makes direct comparisons difficult. The impact of factors such as economies of scale and proximity to suppliers does need careful consideration when making comparisons and drawing conclusions.



## Exhibit 5: Management and administration cost comparisons

Company	Total income £ million	Total expenditure £ million	Management expenditure £ million	Management as a percentage of total	Unit cost (£) per property
Guernsey	7.6	5.2	1.6	31%	77
Cambridge	15.9	11.2	3.9	35%	34
Portsmouth	31.3	20.9	6.6	32%	10
Jersey	12.5	not known	not known	not known	76
Isle of Man	9.9	not known	not known	not known	54

- 45** Both of the value-for-money indicators we considered are potentially important in understanding the value for money provided by GW, however, they do suggest very different views of performance. As part of ongoing monitoring, GW and the PSD need to establish which of these, or other indicators, would be the most appropriate for them to use.
- 46** When the costs of management and administration are considered over a period of time for GW, Jersey and the Isle of Man, it is evident that they have all risen since 2001. For GW, figures show an increase of over 25 per cent in management and administration costs between 2001 and 2005. This indicates that these costs are an area that needs ongoing monitoring to ensure there is continued value for money.
- 47** Given the difficulties associated with the identification and use of indicators in this area, the development and use of an agreed set of indicators is necessary to deliver more effective monitoring of GW and allow comparisons with others.

### Internal key business processes are well-developed and staff are committed to the business

- 48** Sound and effective financial management, performance management and corporate governance arrangements are key business processes, which are essential for any organisation in providing value for money. We found that GW had well-developed arrangements in all of these areas. This forms a key component in understanding the broad picture of value for money and helped confirm our conclusion that GW is providing value for money within its own context.
- 49** Performance management arrangements are supported by a well-established business planning process, based on the 2003-2013 Business Plan. The Plan is used to set the direction within GW and monitor progress within an established monitoring and evaluation framework. Key GW staff are very aware of the objectives of the Plan and the role they play in its delivery.

- 50** Governance arrangements within GW are well-developed with an established scheme of delegation with individual responsibilities detailed. In areas such as risk management, GW is making good progress, allowing it to effectively manage the risks it faces both at the day-to-day technical and managerial level.
- 51** Effective financial management arrangements were demonstrated during our review.  
The major capital investment programme is being well managed with overall effective processes and controls for project prioritisation, scheme design, cost and delivery management. There are examples of schemes being delivered under budget and ahead of time as part of an overall programme which is delivering the required infrastructure improvements.
- 52** A key factor in delivering value for money, in addition to effective business processes, is the commitment, enthusiasm and the ability of the people charged with delivering the business. The GW people we met were experienced in the water business, committed to delivering a good service and enthusiastic about their roles.





## Developing the current governance arrangements for Guernsey Water would enhance strategic risk management and support greater value for money

- 53** The regulatory arrangements for GW differ from those of UK water companies where Ofwat, the Drinking Water Inspectorate (DWI) and the Environment Agency provide the regulation deemed necessary to meet the requirements of legislation. This model of regulation reflects the need to protect the health and wellbeing of water users, the wider environment through the impact of water abstraction and discharges, and the impact of financial costs imposed on water users.
- 54** There is no comparable regulatory activity undertaken for GW. The legislative controls that exist for GW are set out in the 1927 Water Law, with many of its current activities to meet water quality and other standards being carried out on a voluntary basis. As part of the PSD Board's governance responsibilities for GW, it can also be considered as having a 'quasi-regulatory' role in the absence of any other body undertaking this role.
- 55** As part of current arrangements, there appears to be limited challenge to GW from the PSD Board. When GW issues are considered by the PSD Board, it can appear to be superficial and has limited time dedicated to it. The PSD Board agenda includes a large number of issues which span the whole business of the PSD. In addition, many of the agenda items are operational rather than strategic in their focus.
- 56** There is potential for high-risk strategic issues concerning GW to be overlooked in favour of the PSD Board considering specific operational issues in both GW and other areas. For example, relatively minor areas of capital expenditure could receive attention ahead of new legislation requiring measures to protect public health in relation to drinking-water quality.
- 57** There is concern that through lack of time and focus, the PSD Board could become over-reliant upon GW staff to provide professional advice and technical expertise, and not provide the appropriate level of challenge that would be expected of a body which is responsible for the governance role as 'quasi-regulator'.
- 58** If a serious water-quality incident occurred which impacted upon health or the environment, it could have significant implications for the whole of Guernsey. The PSD Board needs to develop a risk-based approach which would assist it in focusing upon and mitigating the key strategic risks posed by GW.
- 59** The PSD Board also has a function in relation to its role as 'Financial Regulator' which has a direct impact upon the value for money provided by GW. The PSD Board needs to consider how robustly it challenges the GW strategic-level capital investment decisions and their impact upon the levels of water charges. An example might include questioning the benefits and costs of membrane filtration versus traditional

rapid-gravity sand filters for water treatment, and the long-term impact of these decisions on the charges to the customer.

- 60 Strategic level value-for-money opportunities for GW need to be routinely considered by the PSD Board. This type of activity would be in line with the approach undertaken by other utility regulators. If the PSD seeks to develop this 'quasi-regulatory' role, it may be necessary to provide some external specialist regulatory support. This approach could advise the PSD Board in specific areas of technical expertise while it develops its capacity in this area.

## **Enhancing the performance management of Guernsey Water by the Public Services Directorate would help to focus on value for money**

- 61 The arrangements for the performance management of GW by the PSD are continuing to develop following the MoG changes in 2004. We have confirmed that GW has well-developed internal performance management, financial management, and governance and risk arrangements. In this context, it would be appropriate for the PSD to focus on strategic-level issues as part of its performance management of GW.
- 62 To facilitate this process, it is necessary for the PSD and GW to jointly develop and use a set of appropriate performance measures. Measures need to be at the appropriate strategic level and reflect a balanced range of indicators which could include financial, operational, customer focus and aspects of corporate health. The indicators chosen need to have clear links to the PSD business priorities and objectives, and the priorities for the States.

- 63 Essential to the success of the performance management indicators, is their use as part of an agreed reporting and monitoring framework. The performance management framework needs to define timescales, reporting, monitoring and accountability arrangements which need to be developed and agreed alongside the indicators.

## **Centralisation of Guernsey Water support services into the Public Services Directorate needs to clearly demonstrate the value-for-money gains achievable**

- 64 Economies of scale can deliver cost savings and greater value for money from the centralised delivery of support services within organisations. Typically, payroll services in many organisations can be delivered at lower cost by a central unit rather than by the duplication of the payroll service within many different departments.
- 65 As part of initiatives to reduce costs across the States, some GW support services have been centralised into the PSD. Evidence from GW indicates that it has received limited benefits in service delivery or value for money following centralisation of support services.
- 66 The potential impacts from further centralisation need to be considered carefully, particularly in relation to recruitment and retention. It is common for changes to pose risks to retaining high-quality staff, and clear direction and communication are necessary to ensure that any potential negative impact is minimised.



- 67** To improve the situation, business cases for the centralisation of GW posts or services need to be provided by the PSD and clearly communicated to GW. The business case needs to clearly state the costs and benefits of the proposal, both financial and in terms of human capital. Based on a clear understanding of these factors, the value-for-money gains can then be more accurately evaluated.
- 68** If the business case clearly demonstrates that the benefits of centralisation exceed negative impacts and cost, the areas which are being centralised also need to respond positively to the changes.
- 69** There may be wider opportunities to secure value-for-money gains through centralisation of services beyond GW and across the whole of the PSD's functions, including the PSD core function itself. These opportunities should be approached in a similar manner, by evaluating the costs and benefits and communicating the findings clearly.

## The States of Guernsey needs to clearly articulate its long-term aspirations for water in Guernsey

- 70** Clear expectations and plans for water in Guernsey are necessary to support effective strategic planning and monitoring by GW and the PSD. At the time of our review, there was limited information available at the States level to provide a comprehensive long-term plan for water in Guernsey.
- 71** The principal vision for water and long-term plans comes from within GW itself, and is summarised within the GW 2003-2013 Business Plan. The Plan was developed by the States Water Board which no longer exists.
- 72** There is some uncertainty over the status of the GW Business Plan and how it connects with plans and policies for water and the water business held at the States level. The 2003-2013 Business Plan was submitted to the States where it was acknowledged, but was not formally approved. This has led to some uncertainty between GW and the PSD over areas such as additional income generation by GW and proposals to develop the St Andrews site as a GW headquarters.
- 73** A clear statement from the States of its overarching expectations for water in Guernsey would help the PSD and GW in having a clear strategic direction, and subsequently plan to achieve this in the most cost-effective and efficient manner. It would also allow monitoring of progress against a defined framework for the outcomes.

### Potential value-for-money gains from a Guernsey Water merger with waste-water operations need to be balanced against a clear understanding of the potential risks and benefits

- 74** Unlike many of the larger UK water companies, GW does not carry out waste-water collection, treatment and disposal activities. Potentially, there are a number of synergies between the two areas of activity which could deliver better value for money. Some of these opportunities are already being exploited, for example, customer bill production for cesspit emptying is being carried out by GW staff.
- 75** This approach through joint-working or as a discrete merger could be extended to other areas, for example, engineering and design, capital project management, support services and overall management as part of securing additional value for money.
- 76** As part of any considerations, there are a number of questions around the organisation of waste-water management that would need to be reviewed and understood to avoid any negative impact upon GW. A clear understanding of the costs, benefits and risks of joint-working or merged activities, with appropriate mitigation measures, is required to ensure value for money for the States.



## **Commercialisation of Guernsey Water (in line with existing Guernsey models) is unlikely to provide any additional value for money that cannot be delivered via improvements to the existing structural arrangements**

- 77** The commercialisation of post, electricity and telecoms in 2002 overcame a number of perceived barriers to improvement and delivered benefits to the users of these services and the States (reference: National Audit Office Commercialisation Report).
- 78** The commercialisation of an organisation can result in improved value for money and also deliver improvements which broadly relate to: improved regulation, tackling restrictive staff working conditions, more flexible financial management (borrowing to spend compared against saving to spend) and the introduction of a 'private-sector culture'.
- 79** Enhancing the existing PSD Board arrangements for challenge through the governance and regulation of GW would be possible within the current structural arrangements. This may require some specialist regulatory input to advise the PSD Board while they build their regulatory capacity.
- 80** Restrictive staff working practices, which impact upon value for money, were not highlighted as an area of significant concern within GW. We understand that if changes to staff working practices were required, they could be achieved through modifications to the current arrangements. There is evidence that other PSD business unit sections have already achieved this.
- 81** Potential benefits for GW arising from changes to financial management arrangements, particularly borrowing, need to be considered in relation to the overall policies of the States. Until recently, the GW capital programme reflected the fact that it was funded via water charges to customers using a 'save-to-spend' approach. Permission is, however, being sought to borrow the funds from the States Treasurer for the development of the Longue Hougue water-treatment works.
- 82** Changing the financial arrangements of GW to allow borrowing to spend may produce benefits to customers such as accelerating the overall capital programme. Potential benefits do, however, need to be balanced against the costs of the borrowing, and other impacts. For example, the capacity of GW to manage a capital programme with a shorter timescale and other knock-on effects, such as potentially increased highways disruption, needs to be carefully considered. Should GW be faced with a major capital expenditure issue, for example, replacing the dam wall at St Saviour's Reservoir, then reconsideration of the approach may be necessary.
- 83** Guernsey Water is currently performing well when compared to many of the UK water companies, all of which are private-sector organisations. It has a 'business-like culture' with staff focused on delivering a high-quality product in a customer-focused environment. It is difficult to see how pursuing commercialisation to introduce a 'private-sector culture' would add anything of greater value.



## Appendix 1 - Guernsey Water - Unit-cost comparisons

- 1** Variations in unit costs between water companies are due to many factors: differences in operating environments, asset condition and suitability for purpose, expenditure needed to upgrade assets and systems, as well as differences in the efficiency of their activities. High unit costs do not always indicate inefficiency (such a company may be operating in a highly unfavourable environment) and low costs do not necessarily indicate high efficiency. Likewise, rising costs over time do not necessarily indicate increased inefficiency as, for example, a company's costs may be increasing to meet higher water-quality standards. Unit costs should be interpreted with care in light of a broad understanding of particular business contexts.
- 2** Unit costs for GW, Jersey Water and the Isle of Man Water Authority have been derived by the Wales Audit Office from these three bodies' financial statements and performance statistics over a number of years, with source data being harmonised and standardised, as far as possible, to make them broadly comparable with each other and, where relevant, with data published by Ofwat for UK mainland water companies. They are not directly readable from published sources.
- 3** The source cost data for GW, Jersey Water and the Isle of Man Water Authority have not been subject to any regional price adjustment by the Wales Audit Office, either between the three islands or relative to the UK mainland. The overall effect of such an adjustment would be to improve slightly the relative position of the island bodies in relation to the UK mainland water companies.
- 4** Ofwat assesses UK mainland water companies' relative operating efficiency using unit cost comparisons from two customer-based perspectives: unit costs per cubic metre of water delivered and unit costs per property billed. For its water-service efficiency assessment, Ofwat uses four performance measures, overall unit costs, which it denotes as costs to 'customers', broken down into three discrete components: costs of 'operations', of 'capital maintenance' and of 'return on capital'.
- 5** As defined by Ofwat, unit costs of 'operations' include such costs as staff, energy, materials and contractor costs, but exclude costs relating to assets and capital spending. Unit costs of 'capital maintenance' are costs necessary to maintain the operating capability of above-ground and below-ground assets. Unit costs of 'return on capital' reflect remuneration to the providers of capital and funding requirements for investment. Unit costs to 'customers' are the aggregate of these three, on two bases: water delivered to customers and customers' property billed.
- 6** **Figure 1** summarises these unit costs, as derived by the Wales Audit Office, for GW, Jersey Water and the Isle of Man Water Authority. **Figure 1** also includes unit costs for Portsmouth Water and South Staffordshire Water, two of the best-performing UK mainland water companies, Tendering





Hundred Water, and Folkestone and Dover Water Services Limited, two of the worst performers, as assessed by Ofwat. Figures 2 and 4 include 'best' and 'worst' performance profiles for UK mainland water companies, which are composites from the best and worst performers in each separate cost category and not profiles of particular companies.

7. Figures 2 and 3 show unit costs of water delivered, and Figures 4 and 5 show unit costs per property billed – Ofwat's measures of operational efficiency. Figure 6 shows unit costs of water production and Figure 7 unit costs of water distribution – GW's key measures of its own performance. Figure 8 shows unit costs of management and administration, a measure created by the Wales Audit Office to complement the others and give a rounded overall picture.

**Figure 1: Unit costs of property billed and water delivered, 2004/2005**

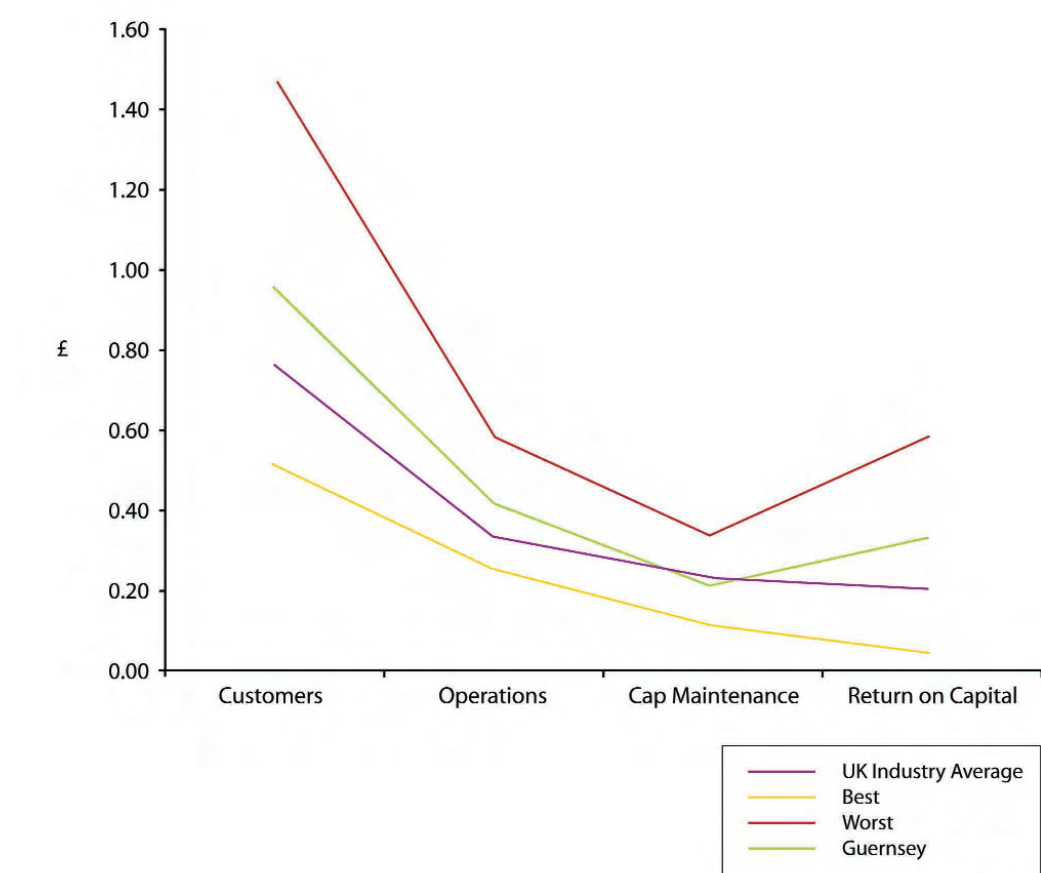
	Guernsey Water	Jersey Water	Isle of Man	UK mainland average	Portsmouth	South Staffordshire	Tendering Hundred	Folkestone and Dover
Unit cost	£	£	£	£	£	£	£	£
<b>Per property billed</b>								
Customers	202	267	286	153	102	113	197	200
Operations	88	138	175	65	52	59	78	98
Capital maintenance	44	49	35	47	25	30	41	39
Return on capital	70	80	76	40	26	24	78	63
<b>Per cubic metre of water delivered</b>								
Customers	0.95	1.30	0.96	0.76	0.51	0.59	1.47	0.98
Operations	0.41	0.67	0.53	0.33	0.26	0.31	0.58	0.48
Capital maintenance	0.21	0.24	0.14	0.23	0.12	0.16	0.31	0.19
Return on capital	0.33	0.39	0.29	0.20	0.13	0.13	0.58	0.31

*Main Sources:*

1. Wales Audit Office analysis of Guernsey Water (2004), Jersey Water (2004) and the Isle of Man Water Authority (2004/2005) – published financial statements and performance statistics, with adjustments
2. Water and sewerage service unit costs and relative efficiency 2004/2005 report, Ofwat, December 2005, for UK mainland water companies

Figure 2: Unit costs of water delivered – Guernsey and UK mainland water companies, 2004/2005

Figure 2 shows that GW’s unit-cost profile for water delivered compares favourably with that of UK mainland water companies. Guernsey Water is close to the average for the UK mainland water companies for unit costs to ‘customers’ overall. For individual unit-cost components, GW is close to the UK mainland company average for ‘operations’ and ‘return on capital’ and slightly better than average for ‘capital maintenance’.

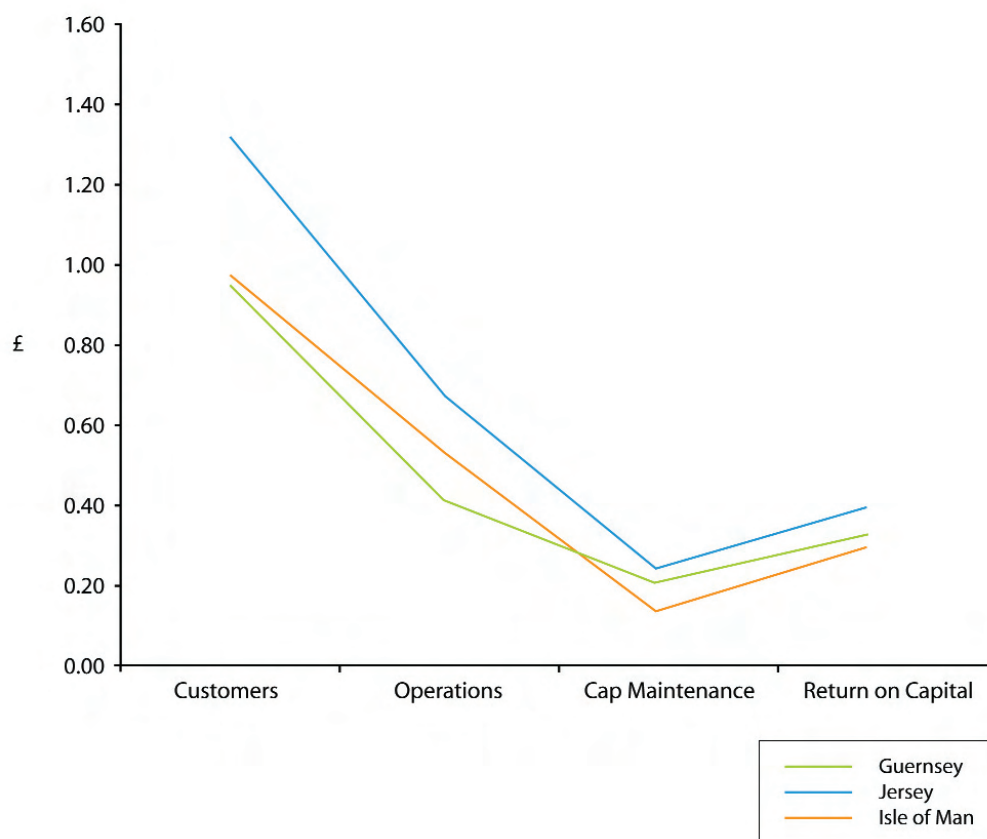


**Note**  
This graph has been developed to illustrate the profile of GW for a number of indicators in comparison with the profile for other water companies. A close fit to the best performing water companies indicates lower cost and potentially better value for money.



**Figure 3: Unit costs of water delivered – Guernsey Water, Jersey Water and the Isle of Man Water Authority, 2004/2005**

Figure 3 shows that GW's unit-cost profile for water delivered compares favourably with that of other island water companies (Jersey Water and the Isle of Man Water Authority). Guernsey Water is virtually the same as the Isle of Man Water Authority and better than Jersey Water for unit costs to 'customers' overall. For individual unit-cost components, GW is better than the Isle of Man Water Authority and Jersey Water for 'operations', and all three are broadly similar for 'capital maintenance' and 'return on capital'.

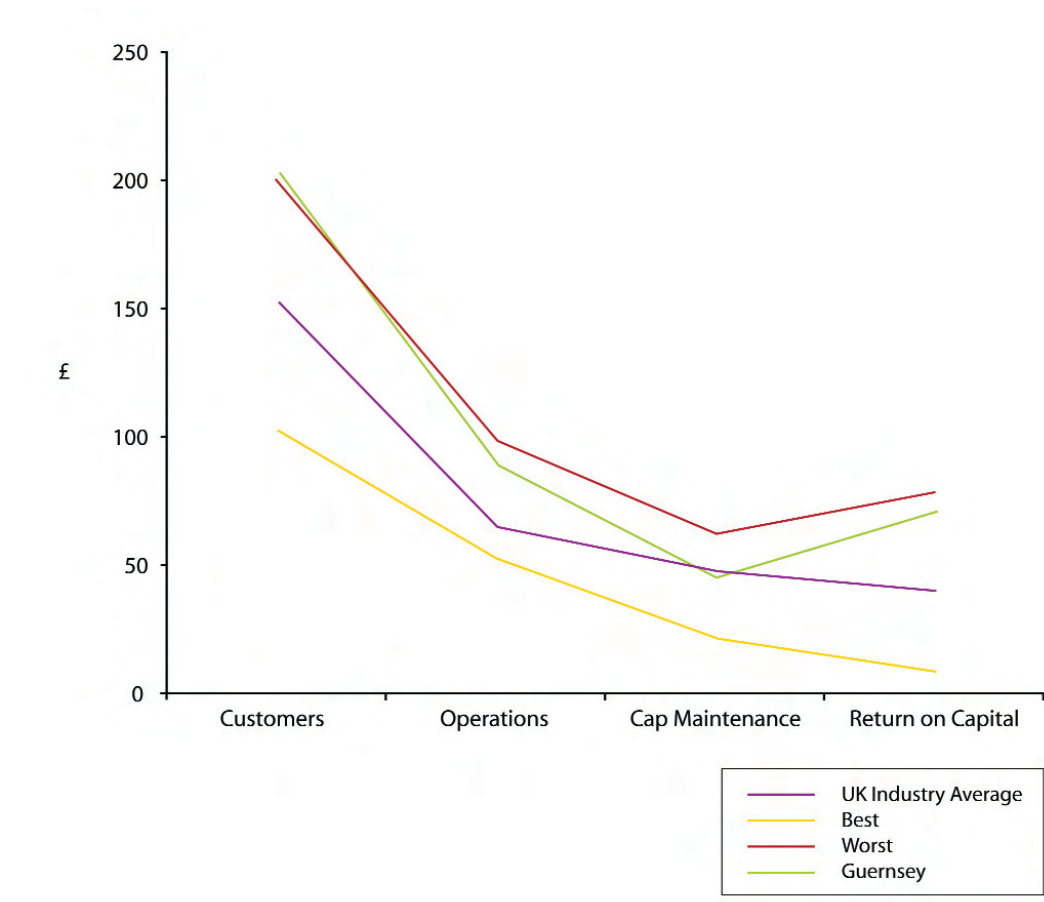


**Note**

This graph has been developed to illustrate the profile of GW for a number of indicators in comparison with the profile for other island water companies. A close fit to the water companies with lower costs indicates potentially better value for money.

Figure 4: Unit costs per property billed – Guernsey and UK mainland water companies, 2004/2005

Figure 4 shows that GW’s unit-cost profile per property billed compares less favourably with that of UK mainland water companies, but not unreasonably, given its island setting. Guernsey Water is similar to the worst UK mainland company for unit costs to ‘customers’ overall. For individual unit-cost components, GW is between the UK mainland company average and worst performance for ‘operations’ and ‘return on capital’, and is around average for ‘capital maintenance’.

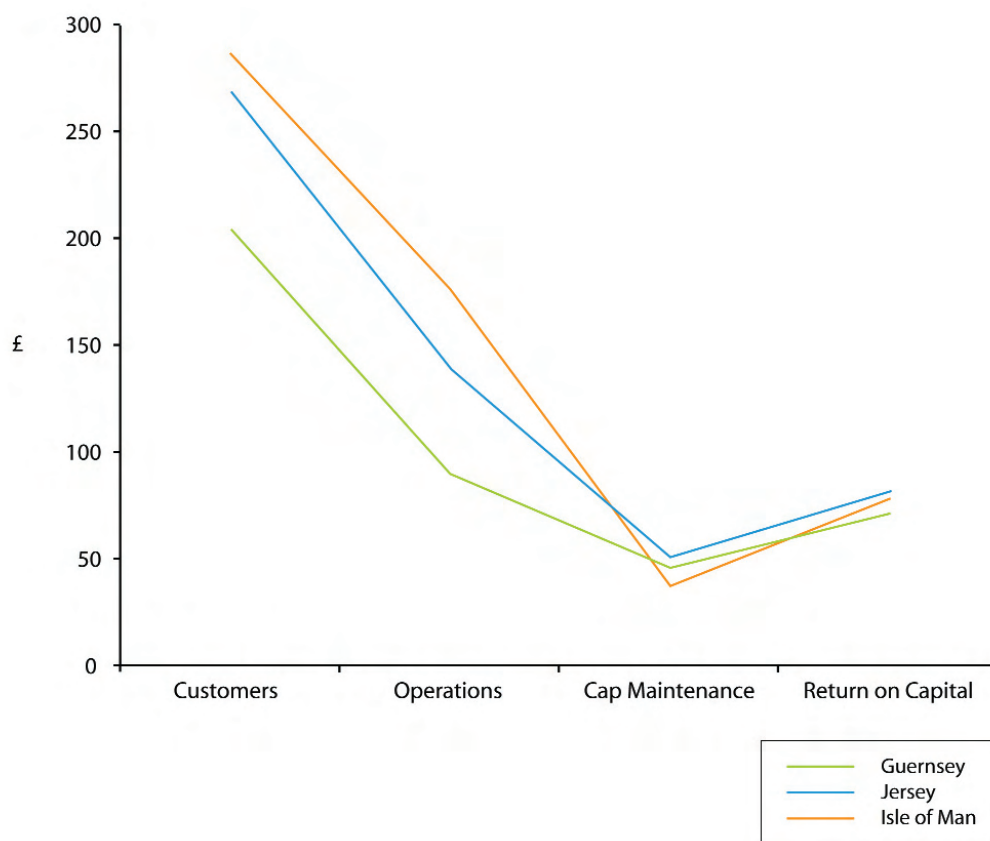


**Note**  
This graph has been developed to illustrate the profile of GW for a number of indicators in comparison with the profile for other water companies. A close fit to the best performing water companies indicates lower cost and potentially better value for money.



**Figure 5: Unit costs per property billed – Guernsey Water, Jersey Water and the Isle of Man Water Authority, 2004/2005**

Figure 5 shows that GW's unit-cost profile per property billed compares favourably with that of other island water companies. Guernsey Water is better than Jersey Water and the Isle of Man Water Authority for unit costs to 'customers' overall. For individual unit-cost components, GW is better than Jersey Water and the Isle of Man Water Authority for 'operations', but all three are broadly similar for 'capital maintenance' and 'return on capital'.

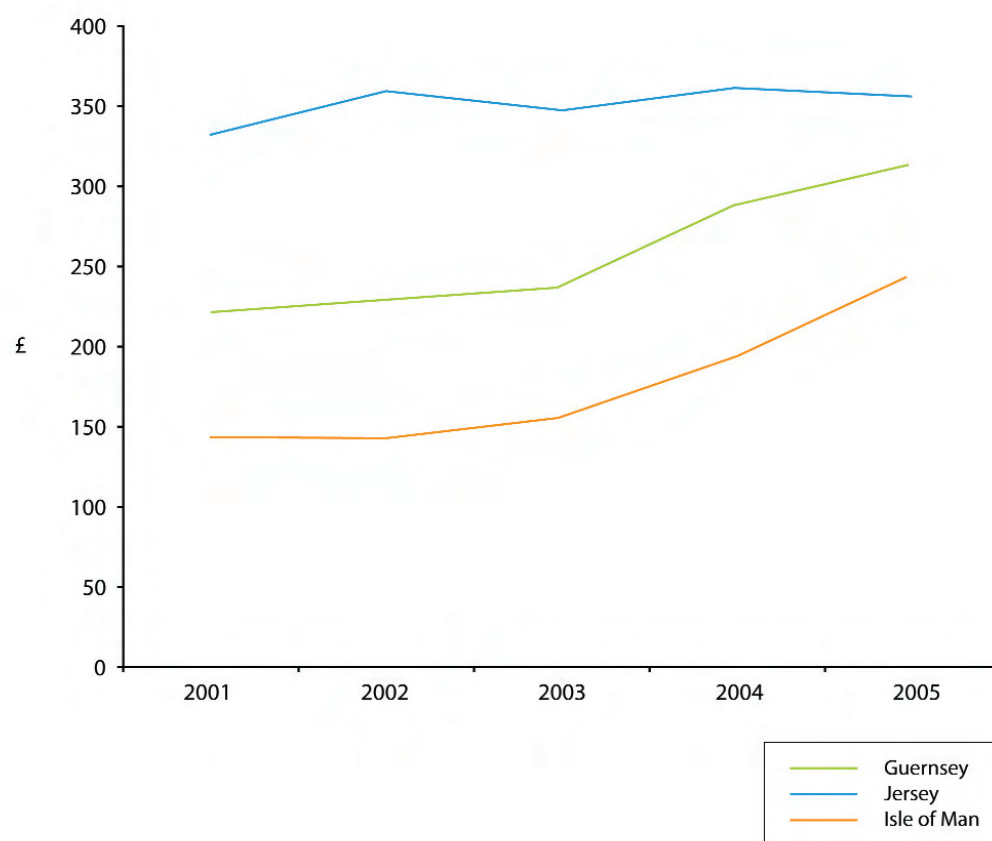


**Note**

This graph has been developed to illustrate the profile of GW for a number of indicators in comparison with the profile for other island water companies. A close fit to the water companies with lower costs indicates potentially better value for money.

**Figure 6: Unit costs of water production – Guernsey Water, Jersey Water and the Isle of Man Water Authority, 2001-2005**

Figure 6 shows that GW's unit costs for water production over time are between those of Jersey Water and the Isle of Man Water Authority. It also shows that both GW and the Isle of Man Water Authority have experienced rises in unit costs whereas Jersey Water has remained relatively stable.



**Note**

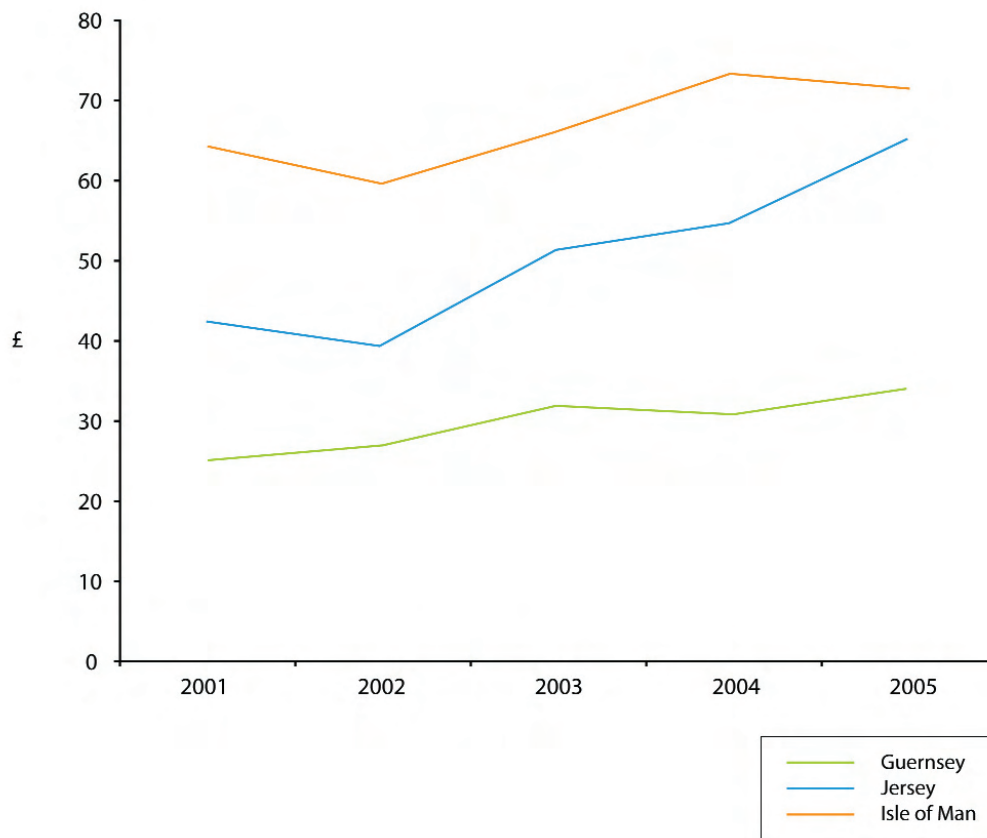
This graph has been developed to illustrate the profile of GW for a number of indicators in comparison with the profile for other island water companies. A close fit to the water companies with lower costs indicates potentially better value for money.





**Figure 7: Unit costs of water distribution – Guernsey Water, Jersey Water and the Isle of Man Water Authority, 2001-2005**

Figure 7 shows that GW's unit costs for water distribution over time have been consistently better than Jersey Water and the Isle of Man Water Authority.

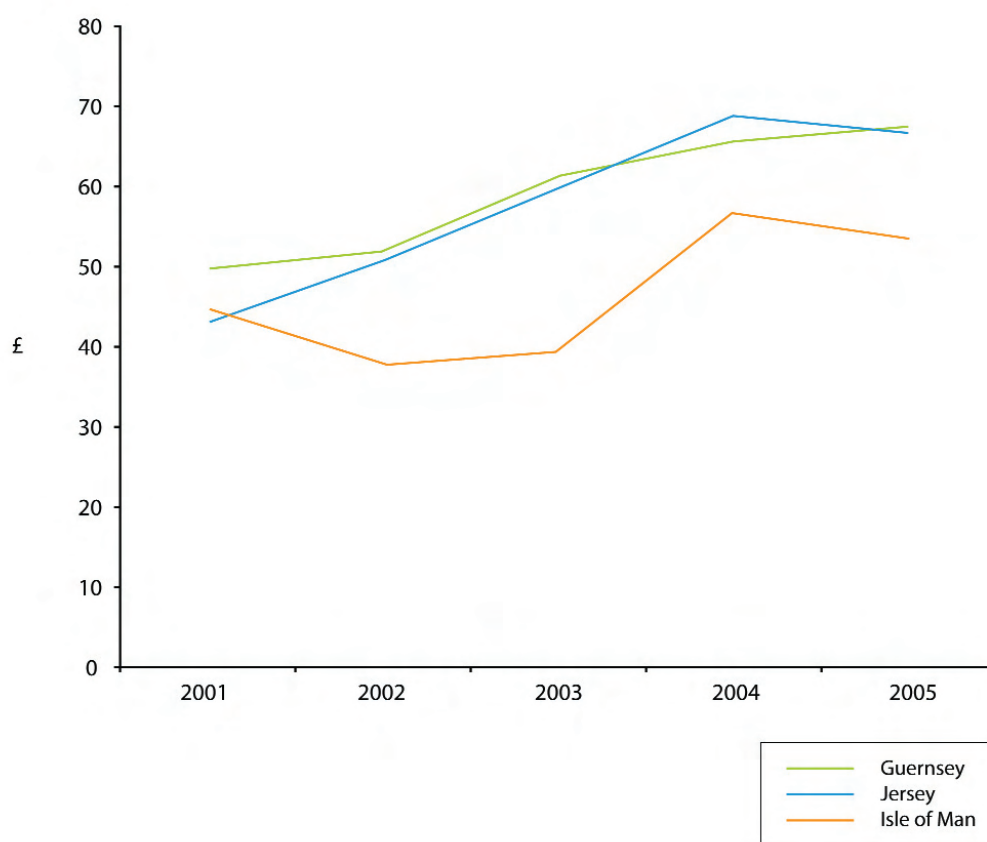


**Note**

This graph has been developed to illustrate the profile of GW for a number of indicators in comparison with the profile for other island water companies. A close fit to the water companies with lower costs indicates potentially better value for money.

### Figure 8: Unit costs of management and administration – Guernsey Water, Jersey Water and the Isle of Man Water Authority, 2001-2005

Figure 8 shows that GW's unit costs of management and administration over time are similar to those of Jersey Water, while the Isle of Man Water Authority is better than the other two.



#### Note

This graph has been developed to illustrate the profile of GW for a number of indicators in comparison with the profile for other island water companies. A close fit to the water companies with lower costs indicates potentially better value for money.



## Appendix 2 - Methodology

- 1 The development of the methodology was outlined in our tender submission for the work. The detailed arrangements were developed and refined in close liaison with the PAC. As part of this we agreed that the main question to be answered by the work was to be: **Is GW providing value for money for the States?**
- 2 In order to provide a sound, rigorous basis for the answer to this main question, we agreed a number of sub-questions which needed to be addressed. These were: are there 'sound and effective' systems in place for financial management, performance management and corporate governance?
- 3 The development of these questions took place with members of the PAC following a series of scoping meetings with key individuals during April 2006. Following this, a methodology to answer the questions was developed and delivered through:
  - **Documentary reviews** – desk-based research which included analysis of financial information, performance information, business plans, meeting minutes, strategies, benchmarking information and other documents relevant to GW, and the scope of the study.
  - **Semi-structured interviews** during June and July with:
    - The States deputies (PSD Minister and PSD Board members);
    - GW staff;
    - PSD staff (including States Works and Environment);
    - The States Civil Service staff;
    - Guernsey Post and Guernsey Electricity staff; and
    - The Office of Utility Regulation.
  - **Focus groups** concentrating on performance management arrangements with two groups of 'front-line' and managerial GW staff.
- 4 **Initial findings** were presented to the PAC at the end of July as part of a 'drawing conclusions' session.
- 5 A **draft report** was presented at the September PAC meeting, and clearance of the report took place during September and October to ensure accuracy. The key stakeholders involved were GW, the PSD and the States via the Chief Executive.
- 6 A **final draft report** for approval was provided to the PAC in October with submission of the final report in November.



**WALES AUDIT OFFICE**  

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