

THE DAVID HUME INSTITUTE



Improving productivity in Scotland's public services

A Research Project

Jo Armstrong

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Preface

The idea of research on this topic evolved from a seminar delivered for the David Hume Institute by Sir Ian Byatt, Chairman of the Water Industry Commission for Scotland and the subsequent paper by Sir Ian that we published. It was evident that there were lessons to be learned across the Scottish public sector from the experience with water – and obvious that productivity in public services would be increasingly important as demands upon these services increased while public sector resources became scarce.

I am extremely grateful to Gordon Downie of Shepherd and Wedderburn for getting a few people together to take forward the concept, and then to the Water Commission, Audit Scotland and the Office of Fair Trading for readily agreeing to fund the research. Support was also provided in practical form by Shepherd and Wedderburn and DTZ Consulting and Research.

At an early stage we identified Jo Armstrong as the ideal candidate to undertake the research. That judgement has been proved extremely sound by the quality of her work and of this report. We then agreed upon a strong steering committee, chaired by Professor David Simpson, formerly a Trustee of the Institute and Deputy Chairman of the Water Commission. Other members of the committee included Kyla Brand of the OFT, Barbara Hurst of Audit Scotland, Gordon Downie and Fiona Parker of Shepherd and Wedderburn, Professor Brian Main the Academic Director of the Institute, Martyn Evans of the Scottish Consumer Council, Tom Harvie Clark of the Scottish Government and Fabian Zuleeg, initially of DTZ Consulting and Research, now with the European Policy Centre. David Simpson, Jo Armstrong and I are extremely grateful for all their input.

As you will see, this report includes three case studies. For each of these we organised – thanks to Catriona Laing of the Institute - a ‘Hume discussion dinner’. These were exceptionally well attended and exceptionally valuable in talking through with a diverse range of informed parties the key issues, sector by sector. Our thanks go to all of those who participated and to those others who provided advice and information to Jo in the course of her work.

This paper does not mark the end of this research project. A seminar is being held at the RSE on 22nd November, kindly sponsored by Shepherd and Wedderburn and to be chaired by Bob Black, the Auditor General. After that seminar Jo Armstrong will produce a final report, which we shall also publish, bringing together the final conclusions from her research and the key recommendations for central and local government and other interested parties.

Finally I must add the usual caveat. While the David Hume Institute has been delighted to promote and support this research, and believes that the findings merit serious attention, as a charity the Institute can have no collective views on the issues or the policy matters raised,

Jeremy Peat
Director

Foreword

With rising living standards has come a general expectation of a continuous improvement in the delivery of public services, both in their quantity and in their quality. There is no foreseeable limit to this demand, perhaps not surprisingly when the services are supplied at a low or zero cost to the user. On the other hand, the growth of resources available to satisfy the increasing demand is limited by the growth of tax revenues. After a period of unprecedented growth in expenditure on public services, we are about to experience in the UK and in Scotland the tightest settlement in many years. The supply of funds available to finance public services will grow at only 1.8% annually over the coming three years. In these circumstances the only way to avoid disappointing expectations is to increase the effectiveness of public expenditure. In other words, to get ‘more bang for the buck’.

Governments’ efforts in the past to achieve such an improvement have been hampered by what has been perceived as the ineffectiveness of the public sector bodies delivering the services. The culture of the public sector is noted for its unnecessary bureaucracy, and for its lack of focus on new and better ways of doing things or on improving customer service. Despairing of any improvement, governments have often resorted to privatisation, or to arrangements such as PFI and PPP.

However, the recent experience of the water industry in Scotland, a public sector monopoly, has demonstrated that improvements in the delivery of public services can be achieved without privatisation. In this industry, innovation and customer service have improved and costs have been reduced. Bills are coming down. Are there lessons from this experience that might be applicable to the benefit of other public services in Scotland? Many commentators have pointed out that water is an industry with its own peculiar characteristics, one being that it is a natural monopoly, so that no easy comparisons with other public services are possible.

Nevertheless, in the case studies that Jo Armstrong has undertaken of three quite disparate public services, social housing, personal care and waste management, she has found that lessons can indeed be learned from the water industry. In a second volume that will be published shortly, she will discuss the common themes she has discovered in all three case studies that point the way to improving the delivery of public services generally. Meanwhile, in the present volume she describes the issues facing each of the three services individually, and gives her specific recommendations for measures for improvement that could be taken in each particular case.

David Simpson
The David Hume Institute

Acknowledgements

This research was undertaken during the summer of 2007 with the support of many sector specialists, colleagues and friends. When I agreed to undertake this exploration it was on the basis we were aiming to open a debate and that input from sector specialists was key to enhancing any simple data analysis. I am grateful to the many who offered additional evidence and suggestions. Jim Baird, Ken Gibb, Kelly Harris, John Lincoln, Mary Marshall, Rab Murray, Henry Simmons, John Simpson, Karen Watt and Sharon Wearing offered specific contributions for which I am indebted.

I have also greatly benefited from the support of the project Steering Group, specifically, David Simpson has offered me invaluable encouragement and guidance and Jeremy Peat's enthusiasm gave the project direction and momentum. I also wish to thank Keith Ingham for his insights and encouragement throughout.

Finally, I would like to recognise the tireless efforts of Johnny Elliot and Lesley Sutton who supported me in my seemingly unending quest for data and Catriona Laing of The David Hume Institute for effortlessly managing the organisation of the three associated dinners. Whilst I have attempted to reflect the various comments and ideas offered, the analysis and views expressed in this paper remain my responsibility.

Jo Armstrong

The Context

Introduction

1. The Scottish Parliament has entered its third session with a new minority Government¹ aiming to deliver policies and programmes via negotiation and consensus. Adding to this challenge is the size of the recent financial settlement from HM Treasury. Although the budget is still growing, it is now growing at a far slower rate than was enjoyed in either of the first two Scottish parliamentary sessions. Rather than viewing this as a major problem, now could be the time to embrace new ways of delivering Scotland's public services, increase productivity and so ensure increased value for money for the public purse. In its wish to contribute to the current delivery debate, the David Hume Institute has commissioned research to assess how improved productivity might be possible by changing the way targets are set and performance is rewarded. In particular, it is aiming to assess how delivery might be influenced and improved by increasing the role of contestability and competition and adopting relevant lessons from the recent successes of Scottish Water.
2. This paper provides the context for the study. It outlines why change is both desirable and, in some instances, inevitable, and what role a greater focus on outputs and outcomes along with increasing the level of competition within a sector might play. In particular, it draws on the recent experiences of Scottish Water operating as a publicly-owned monopoly provider of Scotland's water and sewerage services, and highlights where structural change and a restatement of objectives and targets has led to significant improvements in both the quantity as well as the quality of the services it now delivers.

Drivers for change

3. Expenditure on Scotland's public services has grown substantially in recent years, benefiting from the record levels of funding from Whitehall. In just 5 years the Scottish Government's spending² has risen from £21.5 billion to £31.3 billion (cash terms) by 2007-08³. In real terms the increase is almost 30%, up from £23.8 billion to £30.5 billion (06-07 prices). An analysis of the public sector's share of both spending and employment illustrates further the key and growing role it plays in Scotland. In 2004, the public sector accounted for 23%⁴ of total gross value added (GVA) compared to only 19% for the UK as a whole. Both are marginally higher than the 2001 levels of 22% and 18% respectively.

¹ This paper adopts the title Scottish Government throughout but it is taken to be synonymous with the Scottish Executive.

² As measured by Total Managed Expenditure (TME) the sum of departmental spending (DEL) and annually managed spending (AME)

³ The Scottish Government (2006c), Draft Budget 2007-08

⁴ Office for National Statistics (2006), Regional, sub-regional and local gross value added. www.statistics.gov.uk/pdfdir/gva1206.pdf

Of the 2.5 million employees in Scotland in 2005, 0.58 million⁵ worked in the public sector, over 23% of Scotland's employees in employment, an increase of over 9% in 5 years. At the UK level, the public sector accounted for 20%⁶ of all employees in employment in 2005, up 10.5% in the same 5-year period. These data illustrate how important the public sector is to Scotland both in absolute terms as well as relative to the UK as a whole. For these reasons, increasing public sector productivity is of greater importance as growth in public funding begins to slow.

4. The 2007 comprehensive spending review outlines what additional funding will be available to the Scottish Government for the three years 2008-09 to 2010-11. The overall increase is 1.8% per annum⁷ in real terms. It is worth putting this financial settlement into context. Public spending in Scotland grew around 5.5% per annum in real terms in the last 5 years. So, without major productivity improvements, a 1.8% per annum real increase combined with continued rising demand might actually feel like a cut.
5. In his statement, the Chancellor also signalled an extension to Whitehall's efficiency programme, setting a further reduction of 3% per annum overall and a 3.5% per annum real reduction in administration costs. Over the last 3 years Scotland has been delivering its own efficiency programme of around £1.5 billion by the end of 2007-08 (around 5% of the total 2004-05 budget). However, Audit Scotland's⁸ recent review suggests it cannot confirm services have not been put at risk. The new Scottish Government has signalled it will continue with a programme of efficiency savings of 1.5% annually by 2010-11.⁹ Given the recent experience with such a programme, the public sector's ability to deliver yet more efficiencies without damaging services will be a significant challenge.
6. On the demand side, pressures for public services are likely to continue to grow as Scotland's population ages. By 2024 it is estimated there will be 990,000¹⁰ households headed by people aged 60+, a rise of over 30% in 20 years, and over 115,000 headed by someone 85+, a doubling in the same timescale. The forecast for the total number of households in Scotland by 2024 is 2.5 million, a rise of 13% in the same period. This will clearly have implications for, among other things, the demand for free personal care as well as access to general health services.

⁵ The Scottish Government (2007c), Public Sector Employment in Scotland.

⁶ Office for National Statistics (2005), Labour Force Survey, Public Sector Employment trends.

⁷ The Scottish Government contends this figure arguing the 2007-08 increase is only 1.4% pa in real terms.

⁸ Audit Scotland (2006), The Efficient Government Initiative: A progress report

⁹ Based on the SNP Manifesto statement in April 2007.

¹⁰ General Register Office for Scotland (2006) Annual 2005 Review.

What change needs to deliver

7. These financial constraints heighten the need to maximise the productivity of Scotland's public sector funds. In this context, productivity improvements mean delivering the same quantity of service at a lower cost or securing more for the same cost¹¹. Under either outcome, it is assumed non-cash factors such as quality must be maintained, otherwise cash may be saved but productivity will not have been increased.
8. Consumers' expectations will further influence what service change needs to deliver. A wish for greater levels of choice combined with services more tailored to personal circumstances will probably require different modes of delivery, both factors lying behind the public service reform agenda of the last Administration:

The overriding aim of this complex [public sector reform]is not just to help us sustain the volume and quality of our public services; it is to radically improve on bothwhilst we generate the maximum benefit from every public pound spent...The prize... will be....providing simpler access to a universally high quality of service; new services delivered in new ways;greater choice for individuals in how they use public services and what services they can obtain....

The Scottish Government, Transforming Public Services, June 2006

9. The new Scottish Government has yet to indicate whether this approach remains the focus of its efficiency programme. Whilst the rhetoric may vary, financial constraints will make it hard for substantial deviations in practice.

How improvement might be delivered

10. There is already a wide array of levers available to effect productivity improvements in the delivery of public services. It would be possible to build on existing performance management or service level agreements to effect greater levels of output for the same or fewer levels of input. Alternatively, contractual arrangements with joint venture partners could be tightened or greater value for money from private sector providers might be possible through improved terms of trade. Indeed, with the best value framework for local government operating alongside the current shared services agenda¹² in public service delivery and the need to operate within EU procurement rules, it could be argued that the extensive set of existing incentives already delivers considerable productivity gains. However, pressures on services are expected to continue and the easiest efficiencies have probably already either been delivered or are in train to be delivered. With an increasing desire for more personalised public services it seems likely that it will be necessary to investigate yet more radical delivery approaches if this demand is to be adequately fulfilled.

¹¹ Productivity is the ratio of outputs to inputs. Outputs are a function of both quantity and quality. It is conceivable therefore, to have a productivity improvement with a reduction in quality so long as the reduction in inputs is greater than the reduction in quality.

¹² The shared services agenda aims to develop a shared infrastructure to support Scotland's public service delivery to free up resources for reinvestment in frontline services.

11. The aim of this research project is to investigate the potential for additional productivity increases by adapting current incentive structures underpinning the delivery of services. In particular, it aims to assess how, by increasing the transparency and monitoring of objectives, outputs and outcomes this might lead to better services for Scotland's consumers and so lead to better value for money. This may involve the re-setting of existing incentives and the introduction of greater levels of competition within a sector or, where competition is not possible or desirable, the introduction of rigorous economic regulation.
12. As economic theory teaches us, competition in product and service delivery would appear to be a necessary condition for the efficient allocation of scarce resources:

Competition is a process of rivalry between firms, each seeking to win customers' business,.... some firms competing on price, some still on developing the quality of existing products or services, while others use entrepreneurial or research skills to develop new products or services.....The consequences of this are that prices will typically be bid down to an efficient level of costs, a diversity of product offerings will come on to the market that matches the heterogeneity of consumer needs and tastes, and the rate of innovation will be high.

Professor Paul A Geroski, Chairman, Competition Commission, September, 2004

13. Although this may seem self evident when buying consumer goods (such as cars or books), many do not see the same necessity for competition when it comes to the delivery of what might be typically classed as public services (such as schooling and health care). The issue of competition in the delivery of public services in Scotland seems to get lost in the debate about whether something should be delivered either wholly or in part, by the private or the public sector. Competition (or even the threat of competition) leads to increased efficiency, be it applied in the public or the private sector. Critically, it offers the opportunity to benefit financially from discovering new, innovative and cost-effective ways of delivering goods and services. It is not necessary to have private ownership to ensure service provision is efficient and what consumers want.
14. Competition may not always be possible but, as Sir Ian Byatt suggests, any regulated alternative should be viewed as a second best solution¹³:

When competition is possible we should facilitate or promote it; Where natural monopoly is inevitable, it is necessary to turn to some form of regulation of outcomes and prices..... Regulation should focus on outcomes and incentives, not inputs and micro-management.

Sir Ian Byatt, Chair, Scottish Water Industry Commission for Scotland, Hume Occasional Paper No 67, April 2006

¹³ Economic regulation is viewed as a second-best option to competition because it requires intervention and price setting by a regulator who needs to rely on accessing suitable benchmarking information and who has adequate knowledge about what an efficient operation looks like. It also has to do so without costing the sector and customers more than any benefits delivered through its actions.

There may be valid reasons why competition is either absent or limited. Markets can fail to produce an adequate number of providers able or willing to provide a suitable service. Indeed, the lowest cost provision of a service may be by a natural monopoly supplier. Alternatively, there may be insufficient information to allow consumers of Scotland's public services to make effective purchasing decisions or, a government may decide that public provision is the only means of ensuring equitable distribution of key services. By its very nature, public service provision is more likely to have arisen as a consequence of such factors. Whilst these factors may historically have justified the direct public provision of services, this does not mean such a delivery approach should necessarily last in perpetuity nor that they should not be subject to competitive pressures from other providers, either in the public or private sector.

15. The existence of EU procurement rules means public service contracts are subjected to competitive pressures via open tendering processes. Nonetheless, exemptions are permitted where the supply of services is not for a pecuniary interest¹⁴. This permits local authorities and other public bodies to exclude competitive tendering for services that are self-supplied, i.e., paid for from council taxes or from Scottish Government grant-in-aid.
16. This research aims to identify how and where incentives need to be adjusted or where competitive pressures could be more usefully applied in the delivery of Scotland's public services. Where such a competitive solution is not possible, it aims to assess how proper benchmarking and performance monitoring undertaken by an independent economic regulator could still mean many of the benefits of a freely competitive and properly function market can be captured.
17. The Crerar review¹⁵ on Scotland's regulation, inspection and audit¹⁶ functions suggests Scotland should be aiming for less, not more, levels of regulation. The review accepts increased external scrutiny has occurred in recent years partly due to a lack of "robust performance management" and may be needed to ensure public services are "well managed, safe, fit-for purpose and that public money is being used properly". This increase has, not surprisingly, resulted in a commensurate rise in the cost of scrutiny, and to halt this rise Crerar argues external regulation should be reduced by increasing the role of self-assessment amongst service providers and by reducing the number of scrutiny bodies.
18. Any proposed development of existing regulatory arrangements is aimed at developing economic regulation. Under such arrangements, incentives are set to encourage the delivery of agreed outputs and outcomes without prejudicing quality or safety.

¹⁴ As a general rule, EC public procurement rules apply where (a) the value of the contract exceeds the Directive's thresholds, (b) the contract is awarded by a contracting authority and, (c) the contract is of a pecuniary interest concluded in writing between the contracting authority and the third party.

¹⁵ The Crerar Review (2007), The Report of the Independent Review of Regulation, Audit, Inspection and Complaints Handling of Public Services in Scotland.

¹⁶ Regulation focuses on providing a licence to operate, enforcement of legislation and regulations, and monitoring the quality of services provided. External audit is the periodic external scrutiny of corporate governance and management; financial statements and underlying financial systems; and performance management and reporting of public bodies. Inspection is periodic, targeted scrutiny of specific services, to check whether they are meeting national and local performance standards, legislative and professional requirements, and the needs of service users.

Management is monitored and performance externally assessed to determine whether bonuses should be paid for excellence or penalties imposed for inadequate or inappropriate performance. Whilst this may appear to add to Scotland's regulatory burden, the aim would be to identify where such arrangements could be undertaken cost-effectively by building existing regulatory structures.

Scottish Water's experience

19. As a means of highlighting what productivity improvements may be possible by changing the incentive structures and opening a sector up to greater competitive pressures, Scottish Water's recent experience is worthy of closer inspection. Scottish Water is a publicly-owned monopoly business providing water and sewerage services to around 2.2 million households and 140,000 businesses across Scotland. It was established through the merger of the 3 separate Water Authorities of the West of Scotland, the East of Scotland and the North of Scotland in April 2002.
20. A key motivation for the merger was the need to bring control to water and sewerage prices whilst at the same time embarking on the unprecedented levels of investment required to meet the increased water quality standards imposed by EU directives. The merging of three separate authorities was expected to deliver efficiency savings so ensuring a slower rate of price increase overall, whilst the north would also benefit from an effective cross-subsidy from customers in the south. In 2000 the Regulator, the Water Commissioner, sought approval to raise prices in the west and the east by 20% and 15% for 2001-02 and 2002-03 respectively and 35% and 27% for the north of Scotland. These increases were thought unaffordable even though the associated investment in Scotland's water and sewerage infrastructure was necessary. Accordingly, the Minister capped prices at 15% and 12% in the west and the east and 35% and 12% in the north¹⁷. Without the merger of the three water authorities, price increases were expected to be even higher, especially in the north.
21. This would suggest Scottish Water does not face competitive pressure as a monopoly provider. Whilst it was expected to benefit from economies of scale it was also established to operate within a regulatory framework which aimed to emulate a competitive market by benchmarking against equivalent businesses in England and Wales. The economic regulator, the Water Industry Commission for Scotland (WICS)¹⁸, has been pivotal in the delivery of efficiencies. The WICS operates independently of Ministers, identifies the lowest reasonable overall cost at which Scottish Water is expected to deliver Ministers' objectives and then sets limits for water and sewerage charges. Scottish Water is able to challenge these charges via a formal review by the Competition Commission.
22. Since its establishment, Scottish Water has cut its annual running costs by a cumulative £453 million¹⁹ (outturn prices) whilst improving drinking water quality, wastewater treatment and cleanup of the environment. In 2005-06 alone, the annual saving was over £160 million.

¹⁷ The Scottish Government (2000), Press release

¹⁸ The WICS was established in 2005 and replaced the Water Industry Commissioner for Scotland.

¹⁹ Water Industry Commission for Scotland (2006), Cost and Performance Report 2003-06.

As a result, the average water bill for Scotland’s households is forecast to be lower than the average charge for customers in the privatised industry in England and Wales by the end of 2009-10²⁰. Critical to achieving these savings is the change in how Scottish Water has been managed. In addition to Scottish Ministers and the Scottish Parliament setting and monitoring Scottish Water’s overall objectives, there are a series of independent regulators that monitor its various activities against pre-defined targets (see Table 2).

Table 2: The various regulators of Scottish Water’s business

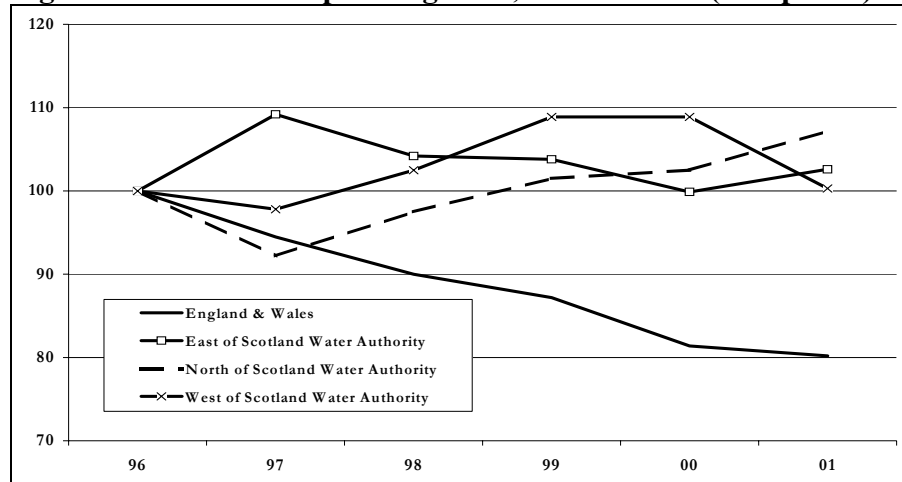
Drinking Water Quality Regulator	Responsible for protecting public health by ensuring compliance with drinking water quality regulations
Scottish Environment Protection Agency (SEPA)	Responsible for environment protection and improvement
Waterwatch Scotland	Responsible for representing the interests of customers (reporting via the WICS)
Water Industry Commission for Scotland (WICS)	Economic regulator which sets charges and reports on costs and performance

23. Ministers set Scottish Water’s objectives or outcomes whilst the WICS sets its prices. This leaves Scottish Water to implement as it sees fit. All stakeholders²¹ know what it is expected by way of outputs and outcomes, with penalties for non-performance and rewards for out-performance driving implementation strategies. Tensions do arise but this is the norm in any regulated industry. Management want to be set targets that are relatively easy to deliver, *ceteris paribus*, whilst regulators want to make sure customers do not over pay for the services delivered and so set stretching targets. This tension should be constructively managed via the use of objectively collected and suitably benchmarked cost data.
24. The WICS uses benchmark data taken from the water and sewerage industry in England and Wales. This allows it to set targets that are both meaningful and achievable as they are being delivered by similar organisations in an equivalently structured market. As Fig 1 highlights, in the period running up to Scottish Water’s establishment in 2002, the water and sewerage companies south of the border were far outstripping Scottish Water in generating operating cost efficiencies. Using England and Wales as a benchmark would ensure Scotland’s water consumers did not continue to be further disadvantaged.

²⁰ The average household price, £287 for 2006-07, does not take account of the continued differential in service quality between England and Wales and Scotland. Consequently, on a quality-adjusted basis it is likely that Scottish Water’s prices would still be higher than the equivalent price in England and Wales.

²¹ Ministers and the Regulator act in the interest of the retail consumer who cannot signal dissatisfaction with the supplier by purchasing from a competitor.

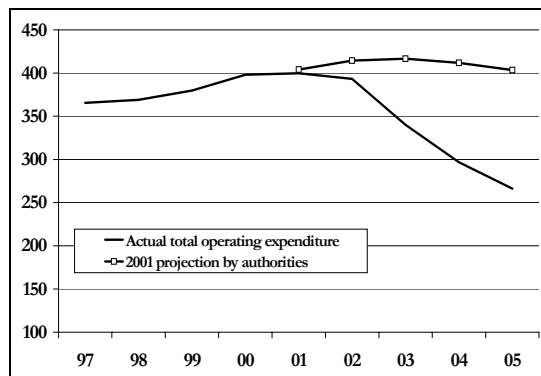
Fig 1: Trends in base operating costs, 1996-97=100 (real prices)



Source: WICS, 2005

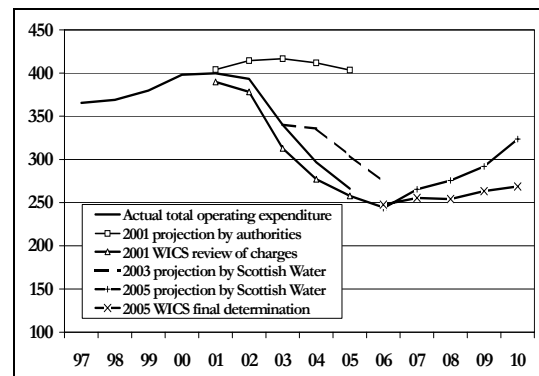
25. To illustrate further the importance of independent regulation setting challenging targets, we need only look at the industry's own cost inflation assumptions (see Figs 2 & 3. Note: Fig 2 is a sub-set of Fig 3).

Fig 2: Actual versus target operating costs (£m,03-04 prices)



Source: WICS, 2005

Fig 3: Actual versus target operating costs (£m,03-04 prices)



26. Fig 2 shows the actual operating cost delivered by Scotland's three water authorities and Scottish Water between 1996 and 2005 alongside what they had forecast for the period 2001 and 2005. Both assumed operating costs would continue their upward path but the reality has been a substantial reduction. By 2005 they had declined 33% in real terms in only 4 years and were less than 75% of their 1997 level²².

27. Fig 3 further adds to the evidence in support of having an independent regulator. The Regulator has consistently set cost targets below those sought by either the water authorities or Scottish Water whilst the outturn position has been operating costs lower than industry expectations, albeit higher than the WICS's levels.

²² It is not possible to establish how much of the savings are actually due to the efficiencies generated from economies of scale and which were due to the effects of setting tough but challenging regulatory targets.

This achievement has had a significant bearing on why Scottish Water's household prices are now forecast to be lower than those in England and Wales.

28. Setting achievable, objectively set and independently monitored output targets has had a significant impact in the productivity of the provision of water and sewerage services in the UK. In England and Wales²³ the motivation for increasing productivity has been influenced by the potential for increased dividend payments for private shareholders, a pressure not applicable in Scotland. As a consequence, the WICS has also had to derive a set of quasi-market related incentives specific to Scottish Water. Scottish Water is still in catch-up mode given its relatively poor, though improving performance on quality. Whilst the debate around Scottish Water's long term ownership structure may continue to rumble on, there is general satisfaction over the role of the economic regulator in setting its prices and so further increasing its operating efficiency.

Lessons for other sectors

29. This report is not aiming to show that what happened to Scottish Water is in any way a model that could be unthinkingly applied across other sectors. The objective is, nonetheless, to show that by interpreting these lessons correctly, and then applying them to other sectors, Scotland's consumers may be able to enjoy public services at a lower cost or receive more at the same cost. This view is supported by the findings of the recent Howat review:

The evidence suggests that independent economic regulation which makes use of external benchmarking with the private sector to set the charges and borrowing for Scottish Water will deliver Scottish Executive Ministers' objectives at the lowest reasonable cost. We would encourage the Scottish Executive to look at the wider relevance of the model beyond Scottish Water, especially in other areas of the public sector where there is significant commercial or business activity in delivering service.

The Scottish Government, Choices for a Purpose [The Howat Report], May 2007

30. There are 4 key lessons that are worthy of investigating in other sectors.

(a) Clarity of objectives

31. Critical to Scottish Water's successful delivery of operating savings and efficiencies has been the explicit statement of organisational objectives set by its shareholder, Scottish Ministers. The extent to which other sectors deliver greater efficiencies depends on whether clear statements on objectives are possible. This will require an understanding of who is the relevant stakeholder(s), e.g., is it Scottish Ministers, local authorities or the end users themselves, and are they able to articulate what is wanted, in what timescale with a given level of financial input? Can these then be fulfilled on a day-to-day basis free from inappropriate political interference?

²³ Whilst the sector has experienced both increased profitability and substantial dividend distributions since privatisation, a number of the water and sewerage companies have undergone substantial restructuring or have been acquired. These experiences highlight the effect of competitive pressures in driving efficiency.

(b) Level of competitive pressure

32. Although Scottish Water is not directly competing with an alternative water and sewerage supplier, it is being assessed against similar providers in England and Wales. These providers also operate in a regulated, non-competitive environment. Regulatory benchmarking aspires to create as far as is possible the benefits of competition by setting targets that relate to the outputs and outcomes achieved by the better (if not best) providers in the sector. Setting such targets and openly monitoring performance against them creates competitive pressure where management does not want to fail to deliver.
33. The review of each sector will aim to highlight where possible impediments to the extension of competition might exist. For example, is there evidence of producer interest and can it be overcome? It will also highlight where economic regulation may be preferable to ensure, for example, universality in supply or to prevent a race to the bottom in quality. Where the sector fulfills the definition of a natural monopoly this will simply reinforce the need for a strong economic regulator to ensure efficiency in service provision.
34. If it is thought necessary to introduce an economic regulator, it will be necessary to understand what is required in terms of administration, 'policing' and enforcement to make the structure work cost effectively and possibly building on existing regulatory arrangements rather than developing additional structures.

(c) Availability of suitable benchmarks

35. The identification of relevant efficiencies must be based on the availability of suitable benchmarking data. In Scottish Water's case the WICS benefited from having access to extensive cost and performance data compiled over a number of years by OFWAT, the Regulator for England and Wales. This may not be the case for other sectors and it will be important to know the extent to which such data deficiencies might be addressed if meaningful benchmarking is to work. These data requirements are essential to help stakeholders understand how efficient and effective their service provision is and what might be expected if competition and regulation were to be introduced or extended.

(d) Suitability of incentives

36. Scottish Water's stakeholders agreed to the development of an incentive structure that aimed to deliver what Ministers and consumers want; an affordable, sustainable water and sewerage service. If there are no incentives to encourage changes to working practices, it is hard to see how necessary changes may be implemented in a timely manner. The potential for delivering productivity improvements will depend on the flexibility of the existing incentives. More specifically, incentives need to leave management and workforce feeling adequately rewarded for exceeding pre-determined targets whilst also facing suitable penalties to limit inadequate or inappropriate performance.

Sector selection

37. The project has chosen three sectors in which to assess the applicability of these lessons; social housing, waste management services and social care services. This selection was based on two key factors; a sector had to be facing severe challenges to its long-term viability, thus making the introduction of structural change potentially attractive, and it had to be one in which the proposed structural changes could be implemented in a meaningful timescale. The analysis of these three sectors is intended to be an overview, offering initial suggestions where more detailed analysis may be worthwhile.

Conclusions

38. Scotland's public services face real challenges as demand rises whilst growth in funding slows considerably. Scottish Water's experience shows that by extending competitive pressures and introducing effective economic regulation and management incentives, Scotland's public service users would greatly benefit. Scottish Water, a publicly-owned company has achieved significant cost savings and quality improvements in the delivery of water and sewerage services. If the Scottish Government achieved equivalent savings across its total discretionary budget i.e., a real saving of over 8% per annum, then almost £1.9 billion would be released in 2007-08 alone²⁴. This is equivalent to securing an additional 1,000 teachers²⁵ in the classroom, 1,000 police on the beat along with a 40% reduction in the average Band D council tax charge as well as in Scotland's total non - domestic rates bill, at no extra cost to consumers or taxpayers.

²⁴ This assumes the Scottish Government's total discretionary spending (i.e., DEL resource) amounted to £23.4 billion in 2007-08.

²⁵ Based on salary data taken from (a) The Scottish Government (2006d), Class Sizes, Staffing & Resources Working Group, (b) Police pay rates (2006) and, (c) Scottish Local Government Financial Statistics (2006), 2005-06.

Case Study 1

Social Housing

Introduction

1. In this financial year, 2007-08, the Scottish Government is set to spend around £450 million²⁶ on new affordable houses throughout Scotland. This is on top of the £2 billion (2006-07 prices) of public funding that has already been invested since 2002-03. Affordable housing includes both social housing (owned in the main by local authorities and housing associations) and low-cost housing built for owner-occupation. Notwithstanding this significant injection of public money, the new Scottish Government has stated that to meet current estimates of demand for affordable housing - ranging between 4,700 and 11,300 extra homes per annum²⁷ - an additional £750 million²⁸ over current spending forecasts will be required. So, large though they may have been, current spending levels still appear insufficient. Nonetheless, with a very tight spending settlement the likelihood of being able maintain current spending levels must be under threat.
2. Overall, the share of Scotland's total housing stock accounted for by rented housing continues to decline, with Scotland's housing sector (as in the rest of the UK), being dominated by owner occupation (see Table 1). In 1993, the total housing stock stood at just under 2.2 million with owner occupation accounting for 55%. By 2005, this had risen to 2.4 million, with 67% in owner occupation. Over the same period rented accommodation has fallen from 976,000 to 793,000, a fall of almost 20%.

Table 1: Share of rented housing by tenure type

	Dec 93	Dec 96	Dec 99	Dec 03	Dec 05
Total rented stock (000)	976	921	869	814	793
- Local Authority	77%	73%	67%	48%	46%
- Registered Social Landlords (RSLs)	7%	11%	15%	31%	32%
- Private rented	16%	17%	18%	22%	22%

Source: Scottish Government, Statistical Bulletin, Housing Series, May 2007

3. Notwithstanding the trend towards owner occupation, for some it is not and never will be a viable or preferred option and social housing is the most popular alternative. Local authorities are still the largest provider of all rented social housing, even following the transfer of over 100,000 houses to housing associations in Glasgow, the Scottish Borders and Dumfries & Galloway. By the end of 2005, local authorities held 46% of the total rented stock compared to 32% for housing associations and 22% for private landlords.

²⁶ The Scottish Government (2006c)

²⁷ As estimated in the 2006 forecast by Communities Scotland, Local housing need and affordability model for Scotland – Update (2005 based), November 2006. The range arises because of the variation in values that can be attributed to key modelling assumptions such as the geographical boundaries of the various local housing areas, first time buyers' ability to fund mortgage deposits, the new household formation rate and migration levels etc.

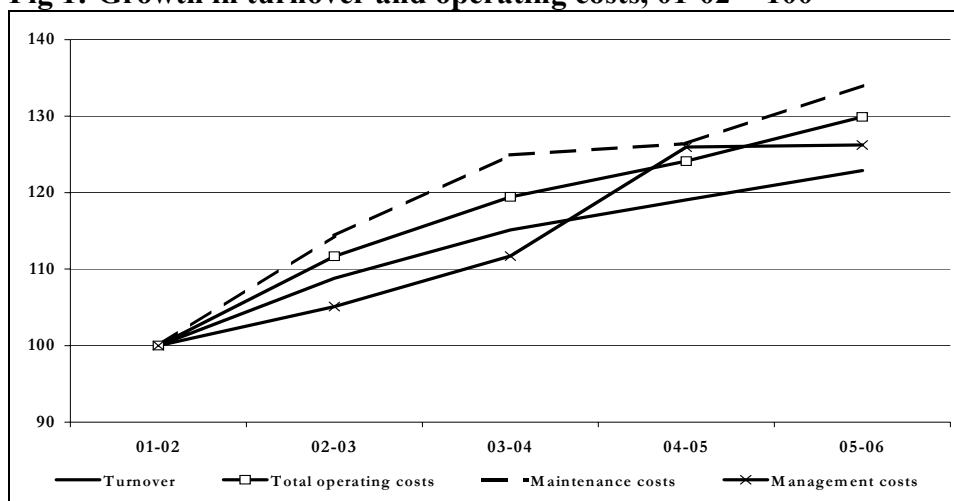
²⁸ The Scottish Government (2006e), Statement from Minister for Communities

Drivers for change

Registered Social Landlord provision

4. Between 2001-02 and 2005-06, the volume of stock owned and managed by registered social landlords (RSLs)²⁹ rose 90% from 138,700³⁰ to 264,300. This took the average number of units managed by a single RSL from 740 in 2001-02 to 1,500 in 2005-06. Although operating costs also increased in this period, they did so by only 30% in real terms (see Fig 1). This would seem to suggest that consolidation, limited though it has been, has delivered some benefits from the economies of scale.

Fig 1: Growth in turnover and operating costs, 01-02 = 100³¹



Note: the costs exclude those relating to the stock transferred by Glasgow, the Borders and Dumfries & Galloway councils

Source: Communities Scotland, FOI request, 2007

5. After adjusting for inflation, maintenance costs rose 34% in this 5-year period and management costs were up 26%. Turnover rose only 23%. Maintenance costs are likely to have increased in this period as RSLs seek to meet the Scottish Housing Quality Standard³² (SHQS). However, unlike maintenance costs, management costs are largely under the control of each RSL. Above inflation increases and, indeed, increases that exceed the uplift in turnover are unacceptable unless associated with productivity improvements.
6. With the differential in growth rates between operating costs and turnover, total operating surpluses fell over 80% since 2000-01, reaching only £120 (2006-07 prices) per house by 2005-06 (see Table 2).

²⁹ These are landlords (mostly housing associations) registered with Communities Scotland to provide social housing. RSLs run as businesses on a non-profit distributing basis.

³⁰ Communities Scotland (various years), RSL Statistics; excludes Abbeyfield Associations

³¹ The cost and turnover data for registered local landlords (RSLs) has been taken from Communities Scotland's in-house databases. Data relating to the transfer of local authority housing in Glasgow, the Borders and Dumfries & Galloway have been excluded to eliminate any potential distortions to underlying trends. The time period covers only 5 years and any trend analysis is intended to trigger a debate about, rather than offer definitive statements on, the efficiency of effectiveness of the sector in its current form.

³² In 2004, the Minister for Communities announced a cross-tenure Scottish Housing Quality Standard to introduce a decent homes standard. The target date of 2015 was set for local authorities and registered social landlords to achieve the standard.

7. Rents account for more than three-quarters of the sector's turnover. In the last 5 years, sector turnover has been rising 5% above the rate of inflation. If operating costs continue to rise at their historic rates, rents will also need to rise above the rate of inflation³³ to maintain annual operating surpluses. If rents cannot maintain their ever-upward path annual operating surpluses will be eliminated leaving the financially weaker RSLs facing unsustainable financial losses.

Table 2: RSL turnover and annual operating surpluses, 01-02 to 05-06 (2006-07 prices)

	00-01	01-02	02-03	03-04	04-05	05-06
Turnover per house	3,152	3,221	3,395	3,189	3,311	3,436
- pa increase (%)		2.2	5.4%	-6.1%	3.9%	3.8%
Op surplus per house	656	647	611	645	239	121
- pa increase (%)		-1.3	-5.5%	5.5%	-63%	-49.3%

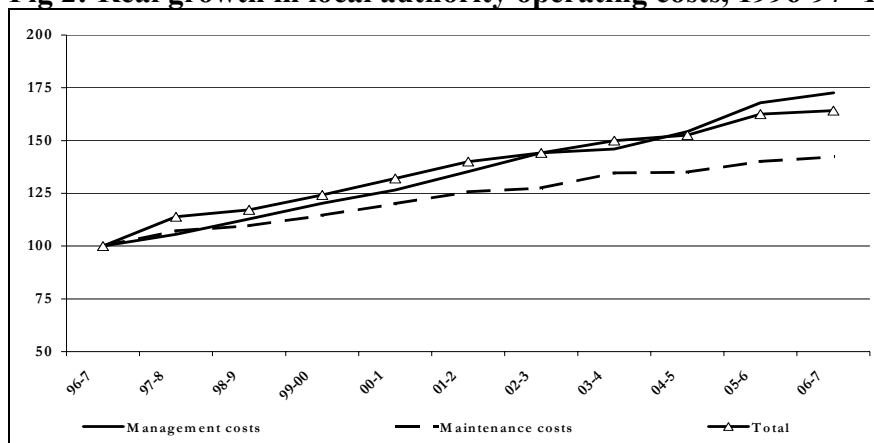
Source: Scottish Government, Statistical Bulletin, Housing Series, May 2006 & January 2007

8. Whilst rent capping has not arisen as a means of controlling rent increases, pressures to keep them down must be growing. In 2005/06 over 50%³⁴ of RSLs' rental income came from housing benefit. The outcome of the Chancellor's tight public sector funding settlement for 2008-09 to 2010-11 left the Department for Work and Pensions (DWP) with a cash cut of 5.6% per annum³⁵, a real reduction of £1.24 billion (2007-08 prices) by 2010-11. Although limiting the level of housing benefit has been politically unacceptable, such a budget reduction could force DWP to look again at what can be afforded, especially if they feel rental increases are effectively funding increased management costs and not delivering productivity improvements. In such circumstances, RSLs dependent on tenants receiving such housing benefits and whose rent is above the capped rate will be under severe financial pressure.

Local authority provision

9. The financial position in the local authority sector is no stronger (see Fig 2) with operating costs also on a rising trend.

Fig 2: Real growth in local authority operating costs, 1996-97=100



Source: The Scottish Government

³³ Most RSLs who received local authority or Scottish Homes transferred stock will be operating some level of rent guarantees. As a consequence, should rents need to rise above these guarantee rates to maintain surpluses, the impact falls disproportionately on those tenants without a guarantee.

³⁴ Communities Scotland (2007), Scottish Registered Social Landlord Statistics, 2005/06

³⁵ HM Treasury (2007), Pre-Budget Report and Comprehensive Spending Review.

10. In the 10 years to 2006-07, they rose over 60% in real terms with management costs rising even faster, at over 70% in real terms. Incomes have inevitably had to increase to accommodate such levels of expenditure. With the same financial pressures facing local authorities as all Government departments, it is difficult to see how such cost levels are affordable in the longer-term. The prudential borrowing regime³⁶ may allow some to add debt to restructure their finances but care would be needed to ensure future housing maintenance is not sacrificed simply to pay debt charges. Local authorities face additional cost pressures as they seek to comply with the homelessness legislation³⁷ as well as the need to ensure all their stock meets the Scottish housing quality standard.

The role for structural changes

11. The current delivery approach appears to be leaving those owning and managing Scotland's social housing with serious financial challenges. Adapting the current operating framework to improve productivity may now be essential (Gibb and Maclennan, 2006³⁸, Maclennan, 2006³⁹, and Dwelly and Cowans⁴⁰, 2006). The remainder of this section reviews the sector with respect to the 4 areas identified as key to improving performance.

(a) Clarity of objectives

12. Scottish Water's success can in large part be attributed to the fact that it has been given a clear set of objectives to deliver within a specified period of time. It is not certain whether all those operating within the social housing sector in Scotland have such clarity. In some instances, ensuring the stock under ownership is warm and dry and rents are affordable is all that is demanded. Whilst delivering these outcomes for tenants may be a significant challenge for some, the challenge for others may be even greater. For example, they may also be involved in the cost-effective development of new, affordable housing, the delivery of wider regeneration activities or securing suitable employment opportunities for local tenants.
13. There is no one model of delivery of both housing and wider regeneration services. RSLs and local authority landlords come in varying sizes and levels of competence. Pressures to extend the remit of landlords may exist as local and national politicians seek to secure sustainable and socially included local communities. However, if landlords are asked to deliver a very broad range of outputs, it is essential the full cost of their delivery is clear and tenants know if their management is performing adequately.

³⁶ The prudential borrowing regime for housing finance was introduced in April 2004. Local authorities can now decide what is an affordable and prudent level of borrowing for them to carry thus potentially allowing them access to increased levels of finance for housing.

³⁷ In 2005/06 the number of applications to councils under the homelessness legislation was around 60,000, see The Scottish Government, Operation of the Homeless Persons Legislation in Scotland, March 2007, www.scotland.gov.uk/Publications/2007/03/12095510/8. By 2012 every unintentionally homeless person will be entitled to permanent accommodation.

³⁸ Gibb K, and Maclennan D (2006), Changing Social Housing: Economic System Issues, Public Finance Management, Vol 6, No 1.

³⁹ Maclennan D (2006), UK Housing Policy Reform – A Global Perspective, in Rethinking Social Housing, The Smith Institute.

⁴⁰ Dwelly T, and Cowans J (2006), Conclusions – Headline Ideas For Reform, in “Rethinking social housing”, The Smith Institute.

The Scottish Water experience shows that by fully specifying what needs to be delivered the inherent conflicts between the various stakeholders will be reduced. In social housing the stakeholders would need to include tenants (existing as well as new), politicians (both local and national), private funders as well as housing owners, managers and staff.

14. There are 4 main categories of activity that each landlord may wish or be expected to deliver: (i) management of existing stock of houses; (ii) development of new houses; (iii) delivery of wider community and regeneration activities; and, (iv) ownership and financing of housing.
15. By providing such a split, tenants would have better information to help them assess how well their management is performing and seek assurances that management have the competence and financial capacity to provide more than one service cost-effectively. For example, a stock-managing landlord would need to provide evidence of its ability to develop new stock, as the necessary skills to do so would not necessarily be gained from housing management activities. That would not mean wholly competent housing managers should not continue to do so, but it may mean they should not be encouraged to grow by developing new assets, funded with scarce public resources. Whilst this could raise the issue of how to keep and attract competent management in an RSL designated as management-only, dealing with it explicitly is likely to produce the outcome more appropriate for tenants.

(b) Level of competitive pressure

16. It could be argued that the development of social housing by local authorities or housing associations arose because of a market failure to deliver an adequate quantity and quality of affordable housing in all the required locations. With over 170 housing associations now in existence and 32 local authorities providing or able to provide⁴¹ social housing, it is perhaps worth asking whether a more competitive environment might now work.
17. In theory, competition for tenants exists between housing associations, local authorities, and the private rented sector as well as from developers providing low-cost housing for owner occupation. Effective competition is, however, more limited where demand exceeds actual supply or where affordability is questionable. In 2005/06 only 7% of the total RSL stock was classified as being in low demand⁴², taking an average of 53 days to re-let. Of the remaining stock, fewer than 20,000 units (less than 8% of total RSL stock) were available for re-letting, taking an average time of only 24 days to do so. It appears that, on average, RSL tenancies do not change much and, those that do are readily re-let. This could reflect a customer base content with the service offered but also reflects demand in excess of supply⁴³. This latter point becomes more significant should rents continue to rise above inflation. Tenants can signal their unwillingness to pay higher rents through their management boards or via council housing management.

⁴¹ The prudential borrowing regime now offers local authorities the opportunity to build new housing stock, even in council areas where stock was transferred to housing associations.

⁴² Based on 34,200 properties out of a total stock of 252,000

⁴³ This analysis uses RSL sector aggregates but Communities Scotland data show there are significant variations within the sector.

However, should they choose not to be an active tenant, or should management ignore their wishes, they have limited ability to seek an alternative supplier in or around the same area.

18. In the main, social housing in Scotland appears to be provided by monopolistic suppliers operating within their own mutually exclusive geographical areas. There is no obvious evidence to suggest they are natural monopolies so greater levels of competition could benefit tenants without undermining the delivery of affordable, quality housing for rent. Given the potential imbalance of power between tenant and landlord, tenants may require reassurances that a competitive arrangement would be beneficial. Regulation may be needed to give this reassurance by, perhaps, requiring all that might seek to compete to be approved as fit and proper organisations⁴⁴.
19. Consolidation of the sector would produce economies of scale and so deliver productivity gains, as would innovation stimulated by new entrants. Whilst consolidation is already taking place, typically it occurs when assets and undertakings are transferred⁴⁵ because, for example, management is looking to retire and continuing with new management is not possible or, where an RSL gets into financial difficulty and the Regulator is seeking to secure tenants' housing services. It is not clear this approach offers tenants the full benefits of competition. Mergers or takeovers of housing associations where all interested RSLs are encouraged to tender for the assets would make the value of any such transfer more transparent to both sets of tenants. It would also allow more effective consolidation and permit new entrants the ability to offer services in areas hitherto closed to their services.
20. The potential for increasing the level of competition within the sector differs across the 4 areas of delivery.

(i) Management of existing stock of houses

On the supply side, the current Regulator(s) could state a preference for open competition for the ownership and management of stock. Competent bodies could be encouraged to bid to take on the management of neighbouring stock or stock of similar characteristics where current management is deemed to be failing. To win the support of tenants, prospective landlords would have to make it clear how they will deliver a superior service. Tenants may not perceive a need to change their current management arrangements if surpluses are being generated and rents are affordable. Nonetheless, if the Regulator were to signal rent caps were appropriate, this would provide a strong incentive to keep cost growth down. On the demand side, support for the extension of competition for tenants from choice-based lettings (CBL)⁴⁶ offers tenants a level of control over where they may live.

⁴⁴ Fit persons could include private profit distributing bodies as well as the established RSLs and local authorities.

⁴⁵ A transfer of undertakings does not require a cash value to be paid by the acquiring landlord, which makes it difficult to ensure best value for both sets of tenants is actually assured.

⁴⁶ Choice-based lettings (CBL) allow eligible tenants to bid for a preferred tenancy although the likelihood of a successful bid depends on there being an adequate number of suitable properties on offer and the tenant having sufficient priority to merit allocation.

Although useful, the lack of an effective surplus of housing means such a system offers opportunities to those on a waiting list but not those simply dissatisfied with the performance of their existing management.

(ii) Development of new houses

Communities Scotland's latest guidance for Strategic Housing Investment Plans⁴⁷ signals the need to ensure any public subsidy required to deliver new affordable housing is targeted where it is needed most with smarter procurement delivering efficiency savings. It has also commissioned research that concludes procurement efficiencies are most likely to be delivered by greater collaboration and a reduction in the number of RSLs actively undertaking new build activities⁴⁸. Such recommendations do not necessarily mean greater levels of competition will occur. Whilst collaborative procurement may secure efficiency savings, this may need to be weighed against the potential loss from discouraging new entrants into an area in the future⁴⁹.

In 2005/06 the Regulator for England, the Housing Corporation, opened up their new-build grants to commercial developers. It anticipates this will allow them to deliver a 33% increase⁵⁰ in the number of houses being built with only a 15% increase in funding being made available. It would seem reasonable to assume that a similar approach in Scotland would deliver equivalent and much needed efficiencies.

(iii) Delivery of wider community and regeneration activities

Competence at delivering wider community and regeneration activities does not necessarily reside with effective managers of local social houses. Whilst RSLs may play some role in their delivery locally, any funding allocated for such services should be open to competitive tender by all bodies deemed competent e.g., suitably qualified RSLs, local authorities, urban regeneration companies or other sector specialists.

(iv) Owning and financing the stock

As with procurement, efficiencies can be delivered from creating economies of scale in financing, either by consolidating ownership or by pooling assets into one security package⁵¹. This could mean lower margins being levied as debt is secured over a larger asset base. Perhaps a more important benefit from such an arrangement is that debt free⁵² assets could be included in any security package so securing additional private funding for new build.

⁴⁷ Communities Scotland (2007b), Guidance on Preparing Strategic Housing Investment Plans.

⁴⁸ CWC conclude Communities Scotland's current approach to new build procurement is too fragmented with 170 RSL receiving £450 million development funding but the top 20 spending only 37% of this total. See CWC, Recommendations for a national procurement strategy for social housing in Scotland, 2007.

⁴⁹ As highlighted by evaluation of the Devanha Initiative in Grampian in 2003/04. See Communities Scotland (2006b), Precis No 89.

⁵⁰ The Housing Corporation (2007), Annual Report and Accounts 2005-06.

⁵¹ It could be argued that the funding structure underpinning the Glasgow housing stock transfer is one example where asset pooling has given access to cheaper funding overall.

⁵² The gross value of the RSL asset base as at March 2006 was just under £7 billion with long-term loans outstanding of £1.5 billion. See Communities Scotland (2007a), The Digest, 2005/06.

Tenants would need to be reassured that they would not face any inappropriate increase in rents simply as a consequence of additional debt being raised to fund new houses⁵³. It will also mean only those owners that have the skills and track record in operating sophisticated financial structures should be encouraged to compete for the delivery of such a service.

21. Should increasing the level of competition not prove possible, bolstering the current regulatory arrangements could produce necessary productivity improvements. The recent Cave Review⁵⁴ of social housing regulation in England discusses the advantages and disadvantages of the main regulatory instruments that might be applied⁵⁵. The review advocates reducing the current regulatory barriers to entry to increase the level of competition in the sector. It also recommends the adoption of a more effective regulatory system to operate across all social housing providers which would reduce regulatory costs, ensure an adequate supply of quality, affordable social housing and strengthen the voice and role of tenants.
22. Cave highlights two additional reasons for the retention of regulation in the sector, both equally applicable in Scotland. First, tenants who voted to transfer from a local authority landlord to a housing association did so in the knowledge that a regulatory safety net would be retained. Secondly, private funders have been willing lenders at extremely keen prices because they recognise the benefit of a regulator who intervenes to facilitate the replacement of inadequate management, so reducing the risks of debt default.
23. The providers of social housing in Scotland are subject to review and regulation by a number of bodies including Communities Scotland, OSCR, the Care Commission, Audit Scotland, as well as private sector providers of finance. The Cave Review⁵⁶ recommends the creation of an independent regulator, established by statute with specific duties and powers relating to the ownership and management of the social housing sector throughout England. Scotland's sector faces many of the same regulatory conflicts and overlap as in England. Communities Scotland faces a similar conflict of interest to that of its English counterpart. It is the Regulator but it also has an objective to develop Scotland's social housing provision wherever it is needed. This could mean it has to assist an RSL through grant funding, as the only suitable one in a pressurised areas whilst, at the same time, this RSL is facing a critical inspection. Perhaps the current review of Communities Scotland's activities provides an opportunity to consider building on its Regulation and Inspection expertise and powers to create an independent regulatory body established by statute and responsible to the Scottish Parliament and not to Ministers. Key duties for such a body would be to promote greater levels of competition whilst also seeking to empower tenants.

⁵³ Rents on existing houses may need to increase if the additional debt is being raised to fund major repairs and maintenance activities on these assets.

⁵⁴ The Cave Review (2007).

⁵⁵ The mechanisms outlined by Cave covered Command & Control, Self-regulation, Contract Regulation, Licensing, Constitutional Regulation, Co-regulation / Enforced Self-regulation, Information and Competition.

⁵⁶ The Cave Review (2007).

(c) Availability of suitable benchmarks

24. If greater competitive pressures were to be introduced, then the level of benchmark data required would be significantly less than for a regulatory arrangement to work effectively. However, in any transitional period the Regulator needs better performance information covering all the key operational activities to reduce the likelihood of management disputes⁵⁷. At present, Communities Scotland, Audit Scotland and the Scottish Government each gathers various performance information. This is costly exercise for all and their suitability for any benchmarking exercise is questionable. Standardisation of what is to be collected would reduce duplication of effort and give greater clarity on how well the sector as a whole and individuals within it are performing. Unless tenants see the relevance of the management information and management feels the need to strive to be efficient, tenants are funding an irrelevant cost as management time is directed at unproductive activities. No doubt well managed RSLs and local authority housing management teams use performance information to seek continuous improvement and some may be incentivised to exceed sector averages. With an ever growing operating cost base and little or no competition in service delivery, the current performance data are not adequately helping to generate the much needed productivity improvements.

(d) Suitability of incentives

25. For productivity improvements to be secured through regulation, suitable incentives for all stakeholders need to be put in place which seek to replicate the pressures of a competitive market. For many RSLs, management salaries are set with reference to EVH's (Employers in Voluntary Housing)⁵⁸ job evaluation rates, which benchmarks individual salaries to other equivalent job classes in the sector. With no or little performance-related pay there is limited incentive to meet or exceed pre-determined performance targets, be they set for the individual post holder or for the RSL as a whole. However, introducing a bonus-related system without significant changes to the current governance structure is more likely simply to inflate salaries and have limited effect on overall productivity.
26. Access to development funding for new build could be one way of suitably incentivising management that may have spillover effects on the management of existing stock. Scarce development funding could be allocated to social housing providers that meet pre-defined performance levels. This would reward efficient performers and galvanise those performing inadequately. It could also encourage new entrants into the sector and allow existing providers to operate in areas of Scotland historically not open to them.
27. For local authority housing, suitable incentive structures could be based on any new approach proposed for the RSL sector, with the Scottish Government explicitly rewarding good performance.
For example, if local authorities adopted the structure applied to RSLs, their performance would be independently measured by the Regulator and savings

⁵⁷ Whilst the WICS has adopted seemingly relevant OFWAT benchmarks to regulate Scottish Water, this has not stopped Scottish Water challenging their overall suitability.

⁵⁸ see www.evh.org.uk/content/default.asp?page=s1_12

could be retained by the local authorities for use in wider housing and regeneration activities.

Alternatively, local authorities could be encouraged to transfer housing ownership and management to an ALMO⁵⁹ (arm's-length management organisation) where their performance could be monitored and rewarded on the same basis as for RSLs⁶⁰.

Conclusions

28. Scotland's social housing sub-sector has benefited from substantial injections of both public as well as private sector funding and has delivered local affordable housing solutions around Scotland. Although sheltered by a degree of protectionism, the ownership structure has become more mixed. A fragmented regulatory regime and limited effective competition across the sector does nonetheless allow inefficient management to survive and this analysis identifies a number of key recommendations to challenge such inefficiencies.

Develop appropriate benchmarks

29. There is a need to identify appropriate benchmark data to allow tenants to understand what constitutes good and excellent practice. The collection of such data would seek to reflect what consumers need and so act as a substitute for more transparent market signals that a fully competitive sector would deliver. Such data would then allow the tenants and more probably the Regulator to challenge RSL and local authority management to improve performance. A more focussed data set would also help to reduce the quantum of data currently collected and so reduce RSL operating costs.

Streamline regulation

30. There is a need to introduce a single regulator for the regulation of the whole sector in Scotland, including local authority housing. This should be established under statute, answerable to the Scottish Parliament and not Ministers as is currently the case with Communities Scotland. Such an approach to regulation would be in keeping with the findings of the Crerar review.⁶¹ To ensure this works effectively, the Regulator must have the legislative competence as well as the in-house skills to ensure it identifies appropriate benchmarks, sets achievable targets for each RSL and has adequate sanctions in the event it finds inappropriate or inadequate performance. Building on Communities Scotland's Regulation and Inspection activities could be a cost-effective way of developing the necessary capacity and skill for such a sector-wide regulatory body.

⁵⁹ In England, 20% of social housing is provided by ALMOs.

⁶⁰ The long-term viability of an ALMO could be at risk if the transferred housing carries a high level of historic housing debt. To date, the Scottish Government's and HM Treasury's policy on debt write-off has required housing assets to be taken off the public sector balance sheet which then ensures any new debt raised for upgrading and developing the stock does not count as public sector borrowing. For ALMOs to work the policy on both debt write-off and new ALMO debt may need to be adapted.

⁶¹ The Crerar Review (2007)

Change the nature of the competition

31. The sector would benefit from changing the nature of the competitive environment. This could take a number of forms.

- First, competent bodies should be allowed to bid for the ownership and / or management of social housing assets. Whilst it is unlikely that such an approach could be introduced retrospectively, where there is a need or wish for a change in either asset ownership or management in the future, any such transfer should be subjected to full competition. In this way tenants on both sides of the agreement can be sure it is both best value and meets their needs.
- Secondly, where ownership is not facing competitive pressures, the regulatory framework needs to be adapted to help mirror its benefits. For example, management should be set targets for delivering operating efficiencies with a failure to deliver leading to the tendering of the RSL's management services.
- Thirdly, the Scottish Government's new-build grant funding should be opened up to a wider target group than locally based RSLs and their builder(s). In particular, the Scottish Government should seek to include direct bidding by private sector builders so maximising the efficiency of this increasingly scarce resource, as is already underway in England. Who owns and manages the assets once built would also need to be addressed at the same time as grant funding was being issued.

For example, they could be offered for sale to existing RSLs or, alternatively, management of these new housing assets could be leased or franchised to suitably regulated organisations.

Establish suitable incentives

32. The sector also needs to establish a more appropriate set of incentives to encourage innovation and productivity. First, management salaries and bonuses need to be more closely linked to actual performance where accepting and managing risk is suitably rewarded. Such an incentive arrangement is especially required where management are not exposed to market pressures, rents are still affordable and rent increases can still be absorbed by tenants. The Regulator may need to provide the tenants with the knowledge that such an arrangement is not the only option open to them and/or intervene to set suitable targets or rent caps to effect a change in management behaviours.

33. Secondly, RSLs should be encouraged to utilise financial surpluses or under-leveraged asset bases to allow the development of new social housing. Much of these surpluses have effectively been funded by the public purse, either through direct grants or housing benefit payments. The Scottish Government's budget settlement for 2008-09 to 2010-11 is very tight and funding for new social housing is unlikely to be as generous as in the recent past. Setting incentives to encourage the sector to use its surpluses to build the much-needed additional supply of social houses would be equitable for those on waiting lists and in need of affordable housing

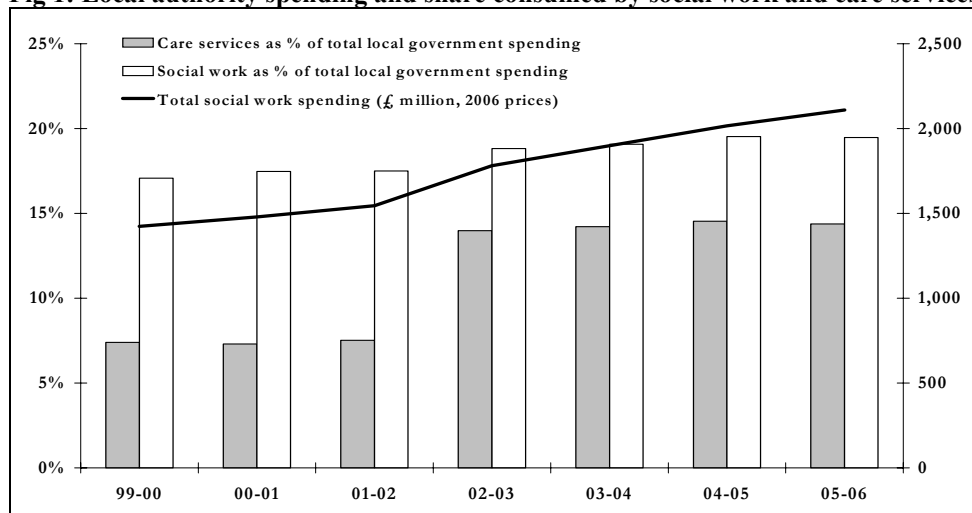
Case Study 2

Care Services

Introduction

1. Since devolution, spending by Scotland's local authorities has increased by 50%, reaching £10.6 billion⁶² by 2005-06 (30% on an inflation adjusted basis). By 2005-06, social work services⁶³ consumed over £2 billion (in 2006 prices) and accounted for 20% of total local authority annual spending. This rise in social work spending reflects the substantial increase in demand for care services that has faced local authorities since devolution. Other factors driving expenditure have been the introduction of free personal and nursing care (FP&NC) for older people in 2002, increasing costs of regulation and growing wages costs which account for a high percentage of any care service budget.
2. For the purposes of this analysis Scotland's adult care services⁶⁴ include (a) support for older people in their own home as well as in residential care, (b) care for adults with learning and physical disabilities, (c) support for adults with mental health needs and, (d) support for adults with addiction and substance misuse needs.
3. As Fig 1 illustrates, spending on social work⁶⁵ services has risen as a proportion of total local authority spending, up from 17% at devolution to 20% by 2005-06. However, for care services the rise has been substantially greater. In 1999-00 these consumed less than 7.5% of local government's total spending. By 2005-06 this had risen to just around 14.5%, a near doubling of the budget for such services in 6 years.

Fig 1: Local authority spending and share consumed by social work and care services



Source: Scottish Government, SE/2007/1, Scottish Local Government Financial Statistics, 2005-06

⁶² Source: Scottish Government, SE/2007/1, Scottish Local Government Financial Statistics, 2005-06, in www.scotland.gov.uk/Resource/Doc/162320/0044124.pdf

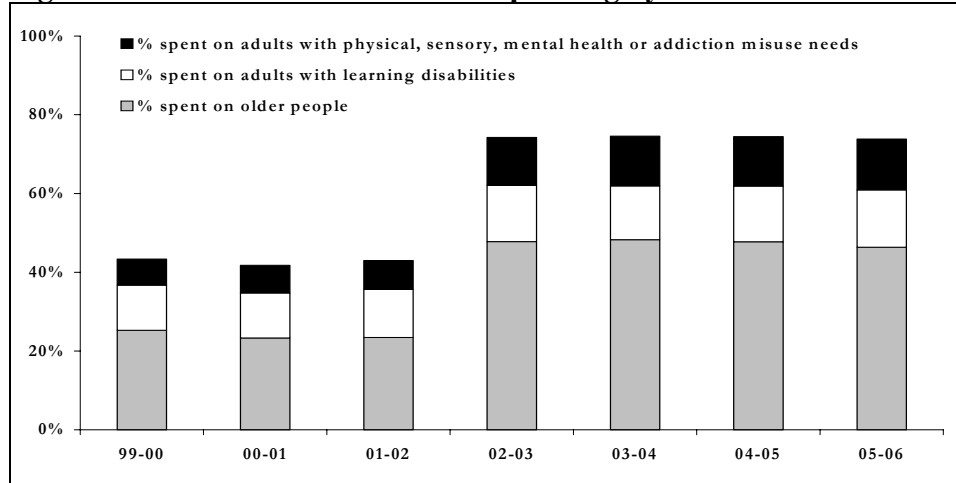
⁶³ Local authority spending on social work services covers 27 different spending categories of which the 4 identified 2 above are a subset.

⁶⁴ This analysis assumes the care and intervention provided is actively requested by users or carers and not that which is required by a court or legal order.

⁶⁵ In addition to the general GAE allocations, local authorities also receive specific ring-fenced grants for Mental Health and Social Work training amounting to 10% of the total estimated expenditure of local authorities in 2007-08.

4. Whilst older people traditionally consumed the largest share of social work spending, not surprisingly the introduction of FP&NC for older people in 2002 means the share has risen substantially, up from 25% of the total social work budget in 1999-00 to 46% by 2005-06 (See Fig 2). So, in the seven years to 2005-06 spending to meet this long-term care obligation has risen almost 3 times, from £359 million to £979 million (2006 prices). Spending on care services now accounts for almost three quarters of the total social work budget in Scotland.

Fig 2: Share of social work services spending by service user



Source: Scottish Government, SE/2007/1, Scottish Local Government Financial Statistics

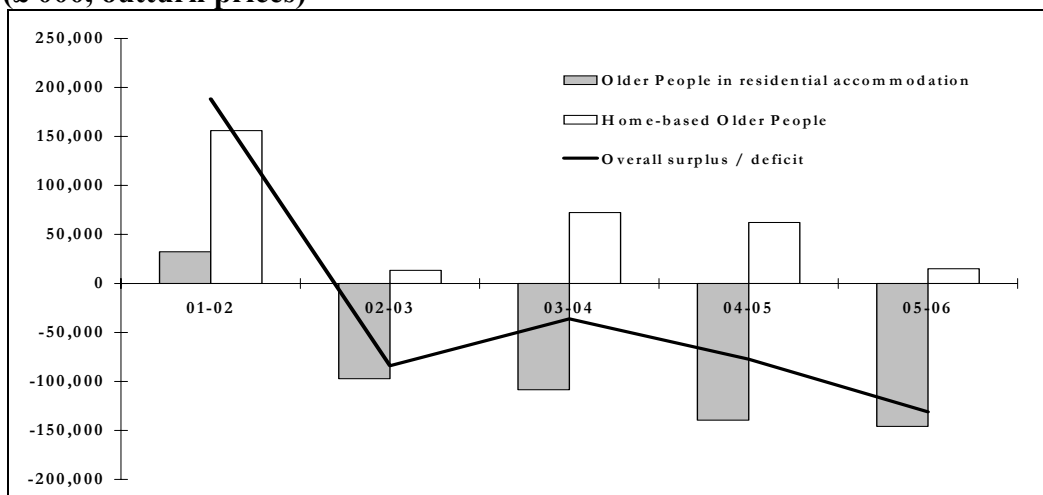
5. Spending for adults with learning disabilities has also risen, up from £164 million (2006 prices) in 1999-00 to £307 million (2006 prices) by 2005-06. This is an annual average real increase of 11% compared to 18% for older people and 19% for adults with physical, sensory, mental health or addiction misuses needs.

Drivers for change

6. Local authorities in Scotland receive grant aided expenditure (GAE) funding from the Scottish Government to help fund local spending obligations. This GAE allocation is awarded on a formula basis to all authorities and so does not necessarily reflect the actual cost of each local authority's financial commitments on such services. As Fig 3 highlights, there has been a growing divergence between what local authorities receive in GAE allocations and what is recorded as the actual local authority spending on care services for older people.
7. Although the aggregate local authority GAE allocation in 2001-02 appears well in excess of what was required to meet their care service obligations, by 2005-06 the data show they are now running a deficit. Since 2002-03, funding for older people staying at home has been in surplus although, by 2005-06 this had fallen to only £15 million out of a total of £467 million in GAE. A far more difficult challenge facing local authorities is represented by the apparent under funding position of older people in residential accommodation. Since the launch of FP&NC in 2002, the GAE allocation for this cohort has been less than the expenditures incurred by Scotland's local authorities, with the deficit position for 2005-06 reaching over £145 million (nominal prices).

Taking the funding of the two care groups together, local authorities faced a total deficit funding position of just over £130 million (nominal prices) in 2005-06. Demand for services for older people is clearly putting pressure on local authority finances. Although local authorities can and do allocate their GAE funding to suit their local needs and preferences, continuation of the current approach must challenge their ability to maintain both the quantity and quality of services in the future.

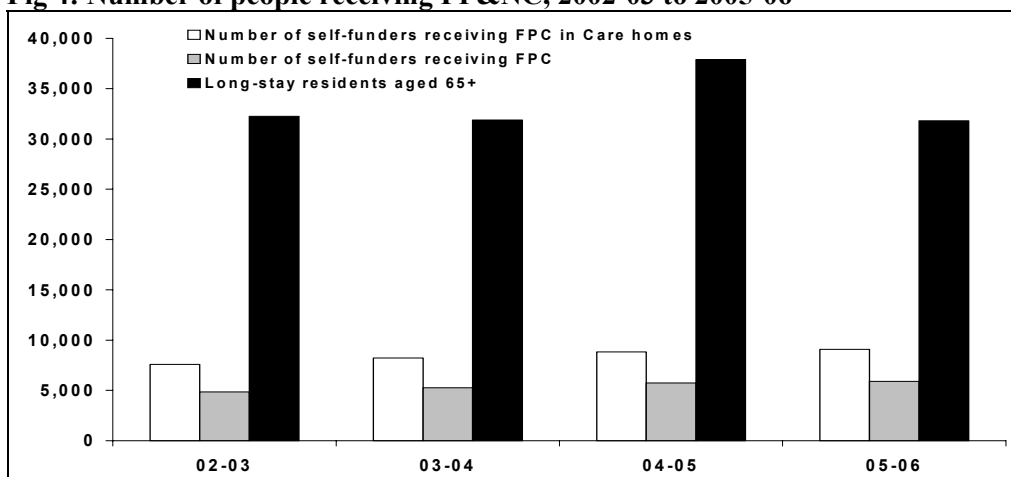
Fig 3: Surplus / deficit in local authority GAE allocations: services for older people (£ 000, outturn prices)



Source: Scottish Government, June 2007, Statistical Release, Free Personal & Nursing Care Scotland 2002-03 to 2005-06; Grant Aided Expenditure; www.scotland.gov.uk/Topics/Statistics/18209/12073

- The number of people receiving FP&NC either in a care home or at home has risen 20% since its introduction, up from 12,430 in 2002-03 to 14,970 in 2005-06 (see Fig 4). Not surprisingly, it has allowed greater numbers of older people to remain longer in their own homes; long-term care home provision for older people (aged 65+) has fallen 1.4% since 2002-03, down from 32,250 to 31,810.

Fig 4: Number of people receiving FP&NC, 2002-03 to 2005-06



Source: The Scottish Government, Statistical Release, Free Personal and Nursing Care Scotland, 2002-03 to 2005-06

9. Although the number of older people staying in residential accommodation has fallen, the total bill for local authorities continues to rise in real terms (see Table 1). In 2001-02 spending on care homes for older people stood at £287 million but by 2005-06 this had risen to over £490 million (both in 2006 prices). This represents a real increase of over 70% or an average real increase of almost 14.5% per annum. The GAE allocation from the Scottish Government to cover such financial commitments has, however, risen only 9% in real terms over the same period, up from £324 million (2006 prices) in 2001-02 to £352 million (2006 prices) by 2005-06.

Table 1: GAE and local authority spending on care homes and home care for older people, (£ million, 2006 prices)

	01-02	02-03	03-04	04-05	05-06
<u>Older people in residential accommodation</u>					
GAE allocation	324	323	327	343	352
Net expenditure on care homes	287	411	437	481	492
<u>Home-based older people</u>					
GAE allocation	336	344	445	466	480
Net expenditure on home care	158	227	237	253	292

Source: LFR3 - Local Financial Return; www.scotland.gov.uk/Topics/Statistics/16945/6901

10. As was indicated earlier, although the GAE is not intended to reflect a budget allocation from the Scottish Government, the widening divergence between what local authorities are spending on care for older people and what they actually receive increases the pressure on the other parts of the local authorities' budgets. Anything that does not have a statutory obligation must increasingly come under threat as will the quality and potentially the quantity of services being made available to council tax payers.
11. The forthcoming local authority funding settlement for the three years 2008-09 to 2010-11 is unlikely to be anything other than tight. Indeed, the new Scottish Government has signalled that it expects to continue the efficiency savings programme set for local government by the last administration. This is in addition to the reduction in funding local authorities will be able to collect following any potential freeze in council taxes. The challenge facing providers of care services in Scotland is heightened further by the anticipated rise in demand for services as Scotland's population ages; by 2020, 21% of Scotland's population will be over 65 and 10% over 75, and by 2024 these will be 23% and 11% respectively.
12. Less cash could lead to fewer services being provided or the quality diminished. The challenge then is to ensure both the quantity and quality of services are maintained whilst accommodating growing demand and without resorting to the introduction or extension of waiting lists.

The role for structural changes

13. The current delivery approach would seem to be on an unsustainable path, requiring the delivery of increased levels of productivity. In this instance, increased levels of productivity may not result in significant levels of cash savings.

However, improved value for money does mean getting more outputs for the same level of inputs or increasing the quality or quantity of services with the same level of inputs. The remainder of this section reviews the sector with respect to the 4 areas identified as key to improving performance.

(a) Clarity of objectives

14. The recent extensive review of the role of social work in Scotland offers the following views of what users and their carers want from the provision of care services:

“Services should meet the needs of people. People shouldn't have to fit services.....”

“We expect to be respected as whole people and supported to achieve our aspirations....”

Users and Carers Panel,
Changing Lives: Report of the 21st Century Social Work Review⁶⁶

15. The evolving “personalisation” agenda advocated by the Scottish Government and Scotland’s 32 local authorities’ offers users the opportunity to choose the services they want rather than take what is on offer. This would seem to suggest clarity of objectives. However, a detailed description of what personalisation actually means for an individual user and, more importantly, what statutory obligation or financial incentive each local authority has for implementation is far from clear.
16. Service funders, most notably local authorities, need to be sure they can afford to offer a bespoke set of care packages. The current local authority approach to service provision offers them a high degree of cost control. They dictate the terms by bulk-buying services from providers or use their own in-house services and simply offer users this set of options. Not surprisingly, this means users have limited flexibility around the composition of their care packages should they wish to do something that is not standard (for example, something that is not routinely provided by a local authority) or where demand outstrips supply. The challenge for local authorities under a personalisation approach is to deliver what users want whilst not damaging their finances.
17. A key step in the delivery of bespoke services is for potential users to be independently assessed, so that local authorities can be assured what is being procured is actually required. Suitably qualified care assessors will need to work with users and, where necessary, their carers to identify what package of care is needed and how best this might be implemented⁶⁷.

⁶⁶ Scottish Government (2006b)

⁶⁷ The approach of separating assessment from management and involving user in the development of care packages was advocated by Sir Roy Griffiths in 1988, a key contribution to the 1990 White Paper on community care. See Griffiths (1988).

The Scottish Government’s review of Scotland’s social work recognised assessors will need to work differently in this new world otherwise the cost of assessment alone could quickly become prohibitive:

“Doing more of the same won't work. Increasing demand, greater complexity and rising expectations mean that the current situation is not sustainable”

Changing Lives: Report of the 21st Century Social Work Review⁶⁸

18. The objectives of personalisation are clear and commonly held by funders and care users alike. Service providers will need to change the way they provide services, not just to deliver efficiencies in procurement but because consumers will become more demanding in what they want as to-days’ middle-aged become the cohort seeking better, more bespoke services. It is not clear what trade off will be required between statutory enforcement, financial incentives and political imperatives to make it work for all stakeholders.

(b) Level of competitive pressure

19. A high percentage of services in this sector are already provided by organisations located outside the public sector (ref Table 2). Of the providers registered with the Care Commission, almost 80% are outside local authority ownership and control⁶⁹. However, private sector provision per se does not necessarily imply the market is operating competitively. Private and non-public providers may charge non-competitive market prices when they are near monopoly providers in a particular service or geography.

Table 2: Provision of care services in Scotland by provider type, March 2006 (%)

	Private	Voluntary	Total Non-public Sector	Local Authority	NHS Board	Total Public Sector
All services	57.0	22.9	79.9	20.0	0.1	20.1
Care home (older people)	67.8	13.1	80.9	19.1	0.0	19.1
Care at home	29.6	53.7	83.3	16.5	0.3	16.8
Adult day care	17.6	31.8	49.4	50.4	0.1	50.5
Housing support	17.3	62.2	79.5	20.2	0.3	20.5
Care home (other adults)	28.5	60.5	89.0	10.6	0.4	11.0

Source: The Scottish Care Commission (2007), *The Quality of Care Services in Scotland*

20. One way local authorities ensure value for money (VFM) for the public purse is by exercising their power as a bulk purchaser of services. Although only 20% of services are provided by Scotland’s local authorities, they occupy a dominant position⁷⁰ in the market place. This may be beneficial for council tax payers where economies of scale in procurement are achieved.

⁶⁸ Scottish Government (2006b)

⁶⁹ The voluntary sector providers comprise charities that are primarily private companies limited by guarantee.

⁷⁰ The power local authorities have is similar to that of a monopsonist - a single buyer facing many sellers - where they influence the market price of the services supplied by varying the quantity they seek to buy.

However such dominance and dictation of terms has the real potential for stifling innovation in delivery, a major benefit of competition and essential when the outputs and outcomes required are not uniform across all potential user types, as will increasingly be the case as personalised delivery increases. This stifling effect may be exacerbated by the growing dependence of the voluntary providers on funding from the public sector, either from local authorities or the Scottish Government. Such dependence forces a uniformity in service provision at the lowest per unit cost.

21. Finally, the public sector provides at least 20% of care services and for some (adult day care services) over 50%. This has the potential of having a negative influence on how new entrants view the sector. For example, if the first 20-50% of service provision automatically goes to local authority owned facilities, new entrants have to make a judgement on their ability to operate profitably⁷¹ with only 50-80% of the market and where the model of delivery is heavily influenced by the local authority owned facilities.
22. If the market fails to provide key services then there would be justification for direct public sector provision. Alternatively, if public provision is as efficient as the market then public intervention would again be defensible. Without the discipline of possible market failure and with in-house services being the first option and not the service of last resort, local authorities have a significant conflict of interest as both procurer and provider of care services. Simply seeking the lowest price for a defined set of care packages is not in itself a signal of a competitive market operating efficiently and effectively in the interest of users.
23. Whilst there are a number of regulatory bodies⁷² operating in the care services sector, none acts as an economic regulator. Primarily they ensure quality in service provision or ensure individual carers have the minimum necessary level of skills to safeguard the safety of care users. Although local authorities can exercise their power as the largest buyer of services locally by imposing price caps, this is not the same as all local authorities being incentivised to ensure that services are what clients want and the price being paid reflects the efficient cost of delivery.
24. If personalisation works, local authorities will no longer be the dominant buyer of services⁷³. It is not clear what form economic regulation would need to play in such circumstances as more buyers seek services from the wider array of suppliers. It is likely that in many cases care users will still require assistance in understanding what constitutes efficient and effective service provision, making some form of economic regulation necessary.

⁷¹ Organisations may also be not-for-profit entities for which the issue is whether or not the market is likely to be large enough for them to at least breakeven.

⁷² The would included, *inter alia*, the Care Commission, the Social Work Inspectorate Agency (SWIA), the Office of the Scottish Charity Regulator (OSCR), the Scottish Social Services Council (SSSC) and Audit Scotland.

⁷³ It may be possible and desirable to maintain the local authority as a procuring agent for the care services users. In this way issues of information asymmetry between user and supplier could be overcome as could the potential problems of financial mismanagement.

More importantly, should supply be constrained on a permanent basis - either because of the specialist nature of the services or because there are geographical constraints - then there may be a need to have a more formal price capping mechanism⁷⁴. This would be aimed at ensuring a Scottish-wide delivery of services at a price reflecting the cost of delivery and not the scarcity of supply.

25. Regulation has been developed to ensure quality of service provision and ensure users are not exposed to unacceptable levels of risk. In an environment where services are provided on a more individualised basis it is not clear the current regulatory arrangements would be able to cope.

For example:

- Could the current regulatory arrangements accommodate a substantial increase in the volume of care packages delivered at home and in the community or would it increase the burden on the Scottish Social Services Council and the Care Commission to a level that was unmanageable or unaffordable?
- How would the greater use of family members and carers friends in more flexible care packages be viewed by the current regulatory regime where all are formally vetted and monitored on a regular basis?
- How could financial abuse be minimised so that local authorities do not end up funding inappropriate or fraudulent claims?

26. If politicians are serious about implementing personalisation, getting the right level and form of regulation is critical and the additional responsibility of economic regulation just adds to the potential complexity and cost. Nonetheless, suitably restructured regulation remains essential if the market is to work more efficiently and effectively.

(c) Availability of suitable benchmarks

27. As with many areas of the public sector, databases abound providing statistics and evidence of all that is apparently being spent and delivered. Audit Scotland's best value reviews and SWIA's multi-agency inspections on local authority performance provide valuable data sets that allow comparisons across Scotland's 32 local authorities. However, it is not clear they always act as catalysts to deliver best practice across all services for the benefit of both users and Scotland's council tax payers.

28. Within a fully functioning competitive market, benchmarking would no longer be required as buyers openly compete to secure the contract of a new user. It is likely, however, that many individual buyers will continue to have insufficient information to make meaningful decisions about the type of services that would best suit their needs. In such circumstances suitable external benchmarking data are needed to help cover both the quality as well as the cost of various service types.

⁷⁴ If provision increased because the market prices signalled to potential new entrants that it would be financially feasible to enter the market, then formal long-term price capping would be inappropriate.

29. Finally, with inadequate benchmarking data local authorities might use this as a reason to continue their own in-house provision as a means of understanding both cost and quality issues. Alternative means of gathering suitable benchmarking data should be found to reduce the market distorting effect of local authority provision.

(d) Suitability of incentives

30. Local Authorities would argue they are inadequately funded to meet their current statutory obligations. Current financing arrangements effectively encourage them to favour in-house provision. To allow them to move away from in-house provision whilst maintaining their care obligations, some form of transitional funding may be required to fund increasingly unsustainable in-house services. The use of subsidies was more recently seen when the previous Scottish Administration encouraged the closure of local authority hostels for the homeless.

31. Whilst advocating personalisation as the way forward, Ministers may be advised that such an approach will be more expensive. As the population ages, more will seek care packages and procuring them individually rather than bulk buying through local authorities might seem more costly. Given the possibly of conflicting demands, it is essential that care users, care providers and funders are suitably incentivised to ensure packages are more flexible but no more expensive to the tax payer. For example, users could be offered care package options where they could choose between a package that is more flexible and personal to them but comprises fewer hours of care directly funded by the local authority compared to a more “standard” local authority package that might be less personal. Offering users what they want may actually lead to less waste overall as users no longer have to contract into unwanted elements of the more standardised packages.

Conclusions

32. Scotland’s care services are already delivered through a variety of public, private and third sector operators funded by a combination of public subsidy and private contributions. The sector is already open to competition and the regulators ensure service quality is maintained. Nonetheless, it is probable that ever increasing levels of demand will exceed likely available public funds. Changes to delivery will be a necessary, if not a sufficient, condition to minimise the re-introduction of significant levels of means testing. This research suggests a number of changes would help to increase productivity within the sector and so maximise the quantity and quality of outputs for the given level of inputs.

Benchmarking data

33. For the personalisation to work effectively, individual users need better benchmarking data to help them know the cost of service provision and feel confident that the price being charged is a fair reflection of the actual cost of provision. This is needed for three main reasons.

- First, an individual making a single purchase could face discriminatory pricing where a service provider charges above the cost of provision (i.e., above the price that would generate a normal profit⁷⁵). This may be possible where there are no other equivalent services on offer or where bulk purchasers such as local authorities use their market dominance to negotiate a more favourable price. Knowledge of the cost of such services would limit the potential for such price discrimination;
- Secondly, even where there is an effective market in operation, there may still be a need for price data to be published to prevent unfair cross-subsidies between the various types of service users;
- Finally, where service providers are competing with local authorities it is important for the non-local authority providers to feel sure there is no inappropriate subsidy for the local authority service and all are competing on a like-for-like basis.

Develop sector brokerage service

34. To facilitate a quicker and more effective implementation of personalisation there is a need to develop a sector brokerage facility. This will be aimed at helping users develop their own care packages whilst retaining many of the efficiencies in procurement that local authorities currently deliver. Brokers would need to be organisations independent of service providers and could be from either the private or voluntary sectors. Local authorities could act as the broker of last resort so long as there were no conflicts of interest i.e. there would need to be sufficient arms-length arrangements in place to distance it from any retained in-house service on offer.
35. In addition to offering procuring efficiencies a brokerage service could offer a number of other services. For example, it could (a) undertake the task of managing a user's budget, (b) ensure care packages make use of suitably qualified staff and, (c) provide resource management services for individual users, e.g., ensure there is adequate carer cover in the event of sickness or annual leave.

Increase effective competition

36. Although there is a wide array of service providers, the power of the local authorities distorts the competitive process. This should be reduced, with any provision by local authorities being on an arms-length basis to ensure third party provision is not disadvantaged and innovation is not stifled. Financial incentives should be offered to local authorities to help cover any transition phase failing which legislation may be required. Without such a clear arms-length arrangement, it is difficult to see how care service users can become more closely involved in the procurement process and have a direct say in who will supply the services they require.

⁷⁵ Even not-for-profit organisation might over charge where surpluses are used to cross-subsidise other non-programme or user-related activities.

37. Regulatory changes will also be needed if personalisation is to flourish. Competitive pressures cannot be at the expense of quality, making regulation essential.

However, the current regulatory arrangements have not been developed to offer input for individuals who seek to purchase a care package involving a variety of providers or providers operating from a user's own home.

Improve contract performance

38. A more personalised approach to developing and delivering care packages requires a change in how contracts should be monitored. Critically, output and outcome targets need to be identified requiring the input from users and their carers or the brokerage service acting as a proxy.

Although outcomes are difficult to define, the recently developed Scottish Government's Supporting People outcome matrix⁷⁶ may be a useful template. Budget information for the various care package elements is needed to complement this outcome data. It is only with a full understanding of what services cost and what is expected to be delivered that users and funders of such services can be assured they are getting value for money while ensuring quality is being maintained.

⁷⁶ The Scottish Government (2007g), Supporting People Outcome Framework, Final Report.

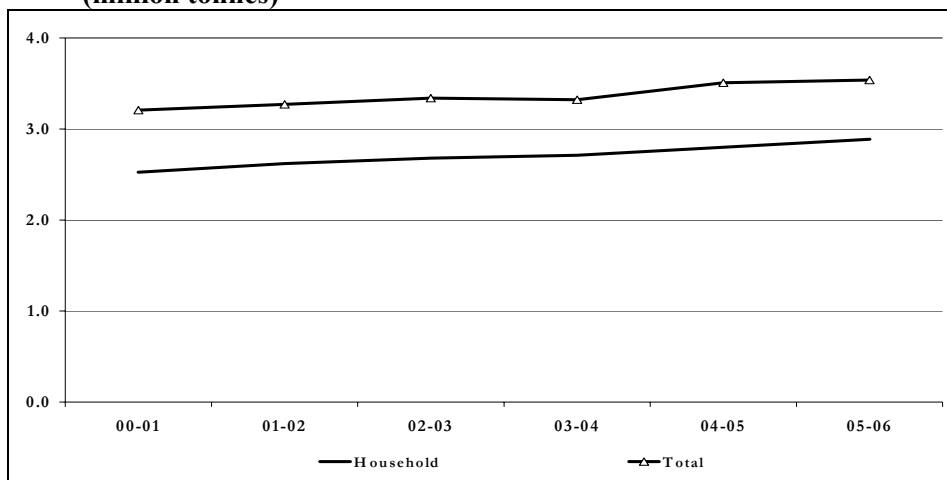
Case Study 3

Waste Management

Introduction

1. Twenty-two million tonnes of waste was generated in Scotland in 2005-06. Of this, about 10 million tonnes from demolition and construction is predominately inert. Of the rest, 9 million tonnes, or 75%, is from commerce and industry, with less than 3 million tonnes being generated by households. It is this latter form of waste which is of specific interest in this paper, as the management of household waste is the responsibility of local authorities. As Fig 1 highlights, the quantity of household waste continues to rise. By 2005-06, the total waste collected by local authorities from Scotland's households reached 2.89 million tonnes, an increase of 460,000 tonnes since 2000-01.

Fig 1: Total waste collected for or on behalf of Scotland's local authorities, (million tonnes)

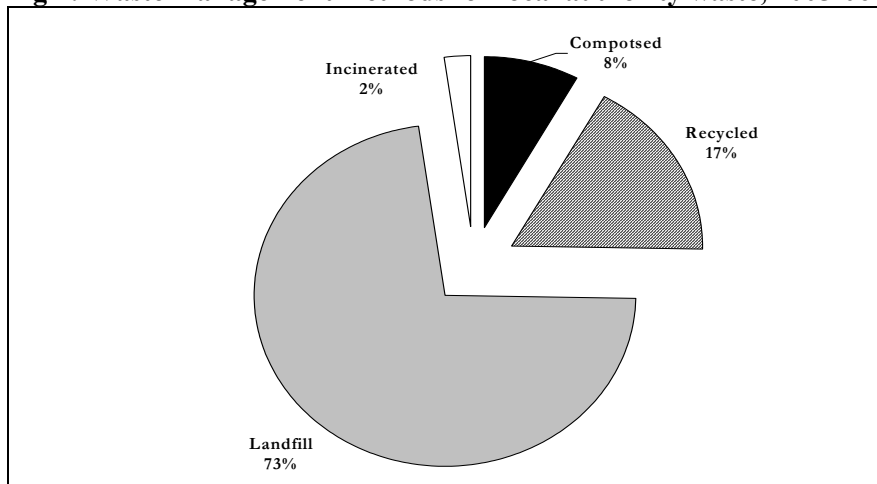


Note: Scotland's local authorities also collect small amount of waste from the commercial and industrial sector.

Source: SEPA, Waste Data Digest, various years

2. A key challenge facing local authorities is to reduce the amount of waste created, to recycle and reuse where possible and so to minimise the amount of biodegradable waste deposited in landfill sites across the country. As Fig 2 shows, 73% of local authority managed waste was still being tipped into landfill in 2005-06. Only 17% was recycled and less than 10% composted or burned in energy-from-waste (EfW) incineration plants.

Fig 2: Waste management methods for local authority waste, 2005-06



3. Whilst a logistical challenge, spending on waste collection and disposal in Scotland's local authorities amounts to only 3.5% of total local authority expenditure; £350 million compared to a spend on all local authority services of £10.54 billion in 2005-06. So, the driver for change is unlikely to be the achievement of substantial financial savings.

Drivers for change

Landfill taxes

4. Since 1996, all waste deposited in landfill sites has been subject to a landfill tax levied by HM Treasury. In 2006-07 this stood at £21 per tonne, and is set to rise to £24 per tonne for 2007-08 and to £32 per tonne by 2008-09⁷⁷. So, in three years the cost of landfill will rise by more than 50%, adding to the financial pressures facing local authorities.

Landfill allowance

5. In addition to reducing the volume of waste going to landfill, local authorities face the further challenge of reducing the proportion of its waste that is classified as biodegradable - biodegradable municipal waste (BMW). Overall Scotland must achieve the target set for the UK of no more than 35% of the level of BMW produced in 1995 to be deposited in landfill sites by 2020, i.e. 0.59 million tonnes compared to 1.68 million tonnes in 1995 (see Table 1).

Table 1: Assumed landfill directive targets for Scotland

	tonnes	% of 1995 BMW
1995 quantity of municipal waste	2.80 million	
1995 quantity of BMW	1.68 million	100%
Target for BMW to landfill by 2006	1.50 million	89%
Target for BMW to landfill by 2010	1.26 million	75%
Target for BMW to landfill by 2013	0.84 million	50%
Target for BMW to landfill by 2020	0.59 million	35%

Source: *The Scottish Government and SEPA, The National Waste Plan, 2003*

6. Interim targets have also been set for 2006, 2010 and 2013. Although the target is a Scottish-wide one, the Scottish Government set complementary targets for each of the 32 Scottish local authorities to ensure the 2020 target would be achieved (see Appendix 1 for the local authority targets).
7. In keeping with what is being implemented in the rest of the UK, the Scottish Government provides local authorities with grant funding to aid the development of Scotland's new waste infrastructure. Fines have also been introduced to penalise local authorities that exceed their landfill allowances. Such a combination of incentives aims to change the way local authorities manage Scotland's municipal waste but leaves them to decide their own delivery solution(s).

⁷⁷ HM Revenue and Customs (2007), Budget 2007, Budget Notes

8. Grants have been allocated on the basis of both the efficiency and the effectiveness⁷⁸ of the proposed solutions. To date, local authorities have not all received what they may have expected under the Scottish Government's standard approach to funding local government. This may have caused some problems where schemes were deemed too expensive which lead, in some instances, to a delay in development of some needed infrastructure.
9. The burden of the penalty arrangement for the more tardy authorities is expected to increase over time (see Table 2).

Table 2: Local Authority penalty for exceeding landfill allowance (£ per tonne)

2005-06	2006-07	2007-08	2008-09
10	25	50	150

Source: SEPA, Landfill Allowance Scheme (Scotland) Regulations 2005: SEPA Guidance on Operational Procedures

10. Whilst the penalty in 2005-06 is only £10 per tonne, by 2008-09 each tonne over the allowance will cost local authorities £150 in penalty payments, a 15 times increase over to-day's rates. In 2005-06, there were only three councils who breached their allowances, namely, Aberdeenshire, the Scottish Borders and Dumfries & Galloway. By 2008/09 local authorities will be able to trade allowances to allow those who face penalties to defray this cost by buying free allowance from those local authorities who have been able to divert more BMW than their target amount. This trading arrangement will allow those local authorities that are quick to find solutions to their BMW problems to benefit financially from those who have been slow putting the necessary infrastructure in place. For some local authorities delaying implementation may be a deliberate strategy. They may choose to wait to make use of solutions tested and implemented elsewhere since this may be cheaper and politically more acceptable.

Recycling targets

11. A final key driver of change is the desire for all local authorities to meet recycling targets again set by the National Waste Plan:
 - Achieve 25% recycling and composting of municipal waste by 2006
 - Achieve 55% recycling and composting of municipal waste by 2020
12. The latest data from SEPA⁷⁹ indicate the interim target of 25% recycling and composting by 2006 has been achieved. Nonetheless, as the recent Audit Scotland⁸⁰ report indicates, the 2020 target remains a significant challenge.
13. The national recycling targets have been cascaded down to all of Scotland's local authorities, adjusted to take into account specific implementation problems each face as a consequence of their specific geography or by the nature of the housing type they service.

⁷⁸ Efficiency is a measure of the ratio of inputs to outputs achieved. Effectiveness measures the extent to which any spending has fulfilled its intended purpose.

⁷⁹ See www.sepa.org.uk/nws/data/returns.htm

⁸⁰ Audit Scotland, (2007), Sustainable Waste Management

14. For example, local authorities with more sparsely populated areas to service or with a higher percentage of multi-occupancy households face a greater challenge introducing cost effective recycling solutions compared to those with predominately single household properties in more urban areas. Notwithstanding these differences, the targets will offer clear indications of the success of each local authority in their delivery.
15. As Appendix 2 highlights, the variability of recycling and composting across the 32 local authorities is significant. In 2005-06, 19 of the 32 exceeded the recycling and composting rate for Scotland as a whole, with Clackmannanshire achieving the highest rate at 40% compared to the Scottish average of 24.4%. Whilst Scotland's recycling rate for 2006/07 is 28.4%, and so exceeds the interim target of 25%, the variability between local authorities is still wide.

Strategic Waste Fund

16. For new infrastructure, the Scottish Government has allocated over £500 million in grant funding through its Strategic Waste Fund (SWF). By 2007-08 the annual allocation had reached over £130 million compared to only £3 million in 2002-03. The actual spend has, however, been less than that allocated as the lead-in time for implementation has delayed the drawdown. Given these delays the funding requirement to meet landfill targets remains substantial. The previous Administration's estimate for the cost of delivering the National Waste Plan targets between 2006-07 and 2019-20 amounted to around £2.4 billion,⁸¹ an average spend of over £170 million per annum.
17. Should the new administration seek to deliver higher recycling targets than in the current National Waste Plan, the necessary financial support will be substantially higher. The incremental costs of recycling increase as recycling rises. Above 40%, costs are estimated to be over £200 per tonne, compared to £150 per tonne for between 30% and 40%. The tough spending round facing the new Scottish Government may mean aspirations for higher recycling targets are not fundable in the short to medium term.

Changes needed to increase productivity

18. Give these underlying forces facing the sector, this next section considers structural changes that may help improve productivity within the sector and so maximise the return for the public purse.

(a) Clarity of objectives

19. The key participants in this sector have spent some considerable time seeking solutions to Scotland's waste problems. The National Waste Strategy⁸² and the National Waste Plan have helped clarify the various objectives for the public sector in Scotland. However, uncertainty remains on at least two levels.
20. First, the new Scottish Government is currently taking stock of what the targets should now be for recycling and composting.

⁸¹ Audit Scotland, (2007)

⁸² SEPA, (1999), The National Waste Strategy

Whilst such a stock-take may be sensible and defensible, the target dates for delivering major infrastructure solutions are extremely tight. Any prolonged delay will lead to increased uncertainty around the required mix of recycling and waste treatment infrastructure to meet the 2013 and 2020 target dates. Local authorities are less sure about the size of the recycling challenge they now face. More importantly, this lack of clarity sends mixed signals to potential suppliers of recycling and waste treatment infrastructure. They cannot readily interpret, for planning purposes, what the size and nature of the infrastructure requirements might be.

21. Secondly, if waste treatment plants are to be used to deal with residual waste, the need for planning approval and subsequent licensing arrangements could lead to severe delays or even cancellation. Should local residents fear the environmental efficacy or safety of potential new plants or if the licensing authority seeks to license facilities that the market deems to be too expensive or technically risky to fund, the suppliers of infrastructure may be unable or unwilling to install the necessary capacity to manage Scotland's residual waste.

22. Given the long lead times for the development of new and, in some instances, costly infrastructure, it is imperative that all those operating within the sector fully understand what it is the Scottish Government wants to achieve in managing Scotland's growing waste problem. It must send clear signals about what level of recycling and composting it is prepared to fund and over what timescale. That will then allow all those wishing to offer solutions a far greater degree of certainty around the quantum of waste that needs to be managed through recycling, composting, incineration and landfill, key to delivering cost effective solutions.

(b) Level of competitive pressure

Waste collection

23. As was outlined earlier, the Strategic Waste Fund (SWF) has allowed Scotland's local authorities to deliver recycling solutions fit for their own local needs. As Audit Scotland highlights this has led to "...67 recycling schemes in operation across Scotland using 41 types of receptacle, collecting differing combinations of 20 materials". The SWF has helped local authorities to develop new approaches to managing Scotland's waste. It is not clear if retaining all these approaches is now the most efficient way forward. Without competitive pressures focussing activity around the more effective solutions, how will local authorities consolidate around such options?

24. Appendix 3 illustrates the net cost of collection and disposal per household for all 32 local authorities. Factors such as the number, composition and location of households will inevitably influence these costs. Nonetheless, the data highlight a number of interesting differences that merit further investigation. For example, between 2001-02 and 2005-06, Argyll and Bute and Orkney both delivered cost reductions of 10% and 9% respectively. This compares to a total Scottish average rise of 20%. These two councils have achieved cost reductions whilst also achieving a recycling and composting rate roughly equivalent to the Scottish average of 24% in 2005-06.

Could increasing competitive pressures induce poorer performing local authorities to seek to benefit from best practice elsewhere and so deliver improvements in productivity?

New waste infrastructure

25. The development of Scotland's new waste and recycling infrastructure has been boosted significantly by the funds allocated to local authorities from the SWF. Notwithstanding the stock-take currently under way and the tight spending round facing the Scottish Government, funding will continue to be made available to develop the infrastructure Scotland's needs to meet its recycling targets. The amount, timing and distribution of such funding is less certain, as is the shape and size of Scotland's new waste infrastructure sector.
26. Whilst the infrastructure will evolve as funds become available the development of the sector will also be highly influenced by the inherent risks and uncertainty it must face. For example, the delivery of large scale energy-from-waste (EfW) plants to process residual waste may be viewed as being too risky to fund without public sector support:
- the planning process surrounding the granting of planning permission for any specific site may be protracted and the outcome highly uncertain;
 - the chosen EfW plant may require a minimum quantity of waste that comes from more than one source of supply making it difficult for any asset owner to invest should it have only one contract with a single local authority;
 - the EfW technology chosen may not be considered proven, leaving funders unsure as to whether it will work as required in whole or in part;
 - the private sector asset owner may not be sufficiently creditworthy to allow private funders to lend long term finance at attractive levels.
27. All risks and uncertainties cannot be totally eliminated in the implementation of large infrastructure projects. However, by reducing a number of them, private investors should be more willing to invest. Currently, local authorities (north and south of the border) are being encouraged to work together to develop PPPs as a means of managing a number of these risks and uncertainties. PPP structures aim to ensure sufficient waste supply is secured on a long-term basis to guarantee the asset owner an income stream, so reducing some of the related funding risks. Properly structured PPP arrangements aim to limit the risks that need to be carried by the public sector. By entering into PPP obligations local authorities will nonetheless be locked in on a long-term basis leaving them with limited flexibility in how to manage their waste obligations⁸³. It is not clear that PPPs are now the solution best suited to solve Scotland's waste management problems.

⁸³ PPPs involve the development of complex legal arrangements between, for example, the infrastructure owner(s), the local authorities seeking to make use of the waste facilities and any associated funders. The greater the number of parties involved in such a system, the greater the likelihood of legal breaches or of failing to meet key financial covenants.

28. With more clarity around what Ministers want in outputs and outcomes, suppliers of waste solutions could make judgements on what that means for the likely levels and location of residual waste that will need to be treated. Given the relatively high entry costs, there are unlikely to be a large number of new competing facilities. Indeed, it is highly likely that Scotland's new waste management infrastructure (or at least the larger, more complex technology solutions) will ultimately be composed of a series of regional monopolies not only dealing with public sector waste but taking most or all of the adjacent commercial and industrial biodegradable waste.
29. How might the market develop and offer local authorities a more flexible waste solution? To make infrastructure solutions fundable, grant funding or an injection of public sector equity⁸⁴ would improve the financial return to any private equity investment. By improving the returns on these assets, waste management solutions that meet local authority's requirements could be delivered without the necessity of local authorities having to take the added risk of effectively locking-in to any one delivery solution.
30. Investors delivering infrastructure that meet pre-determined output specifications could bid for any Scottish Government grant or equity with the lowest bidder securing the financial support required. The idea of a capital injection into infrastructure projects is not a new one as PPPs⁸⁵ can seek to include such funding where it is deemed appropriate. To ensure this approach is best value, any grant or equity required could be compared to the value of any public subsidy needed in, for example, any alternative PPP solution.
31. Risks need to be shared but the public sector should only be expected to pay for those risks over which it has control, with the providers of the infrastructure and their funders carrying the major technology and funding risks. Uncertainty over what infrastructure will be needed can be greatly reduced by Ministerial clarity on objectives. It would also be improved if the nascent market was able to assess the likelihood of planning consents being given and the number and nature of the operating licences that may be issued. The market could then assess the extent to which any one plant was likely to be the effective regional monopoly provider.

Price capping

32. If Scotland's new waste infrastructure is developed around a number of local or regional monopolies there is a need to ensure the asset owners are not able to exploit their monopoly powers. In particular, there would be a need to ensure the prices charged for use reflect the actual cost of dealing with the waste rather than a price reflecting the negotiating power of the owner. Price capping arrangements⁸⁶ would be essential for municipal waste disposal.

⁸⁴ It may also be possible to encourage the development of the infrastructure through the Scottish Government taking an equity stake in any new businesses set up.

⁸⁵ See Scottish Guidance Notes on Use of Capital Injections in PPP/PFI Projects, The Scottish Government (2006).

⁸⁶ Any such price capping arrangements would wish to draw on the experiences of similar systems operating in the UK's water sector and what worked historically in the UK's electricity and off-shore gas pipeline sectors.

33. This may also need to be extended to cover commercial waste in the event small businesses were forced to send to waste to landfill simply because the commercial price of the EfW plant was higher than the capped household price. Finally, whilst price capping would be essential to limit abuse of a dominant position, it must also be flexible enough to encourage efficiency and innovation in delivery.

Regular re-licensing arrangements

34. The likelihood of regional monopolies does not exclude the introduction of competitive pressures. Separating asset ownership from management and issuing licences to manage the assets would create a contestable or competitive environment, keeping pressure on costs and encouraging innovation in management and service delivery. Such an approach is used in the operation of the UK's rail franchises and would allow the Scottish Government to maintain more control over pricing and asset returns.

(c) Availability of suitable benchmarks

35. With 64 different recycling schemes operating across Scotland and with such a wide variation in delivery costs, the Accounts Commission performance indicators (PIs)⁸⁷ would seem well suited to being used for benchmarking. Whilst they could be used to set targets for councils, there would be a considerable amount of work required to ensure they were robust enough for effective benchmarking. The recent OFT⁸⁸ review on waste collection in England suggests there are few economies of scale in collection, and competition would help to deliver efficiency savings in local authority waste management. Scotland's local authorities have a duty to consider best value in the provision of all their services. Market testing would ensure it was delivered efficiently and effectively without the need for expensive and time consuming data collection and monitoring.

(d) Suitability of incentives

Landfill Allowance Scheme penalties

36. The Landfill Allowances Scheme (LAS) is aimed at assisting the development of a cost-effective delivery of the UK's BMW targets. To ensure such a scheme operates effectively⁸⁹, the value of allowances set for each local authority has to be deemed fair by all, and any penalties levied must be based on independent and transparent calculations. Local authorities must not be able to argue for the cancellation of any such penalty. Currently, SEPA notifies Ministers of the likelihood of any potential breaches and estimates the level of any associated penalty. To date, Scottish Ministers have chosen to operate the system in Scotland in parallel with that in England, although there will be full trading with English⁹⁰ authorities from 2008-09.

⁸⁷ Accounts Commission, Performance Indicators, various years

⁸⁸ See OFT (2006).

⁸⁹ For efficient operation of the UK landfill allowance trading scheme local authorities will also need to have suitably qualified traders working for them (directly or indirectly) within an appropriately monitored trading regime.

⁹⁰ Local authorities from Wales and Northern Ireland are also eligible to join the scheme.

In 2005-06, although Scottish councils as a whole met their targets for BMW, three authorities faced penalties for exceeding their individual targets – Aberdeenshire, the Scottish Borders and Dumfries & Galloway. In this lead-in period it is possible for local authorities to seek adjustments to their allowances and seek deferment or cancellation of any penalties.

37. As sponsor of Scotland's new waste infrastructure, the Minister could be facing a conflict of interest. Local authorities face penalties under this scheme should they fail to have the necessary infrastructure in place in time to allow them to divert waste effectively. Infrastructure delays could be directly due to delays in funding from the Scottish Government. Perhaps there is the need to seek separation between those whose role it is to sponsor the development of the sector from those who must ensure the effective operation of the trading scheme. This would minimise the likelihood of penalties being cancelled or the effective operation of the scheme being put at risk.

Commercial biodegradable waste

38. The landfill trading scheme operates only for municipal waste and there is no target for the amount of biodegradable material sent to landfill by commercial businesses. With such asymmetry in the treatment of biodegradable waste, local authorities may well feel aggrieved that their cost base for dealing with waste is higher than necessary. For example, the cost of new infrastructure to the public sector is most likely to be based on the level of waste available from households with little (or possibly nothing) being assumed to be forthcoming from businesses. Should the price for using such new disposal options be cheaper than the landfill tax, commercial users may nonetheless seek to make use of such facilities. Adapting the landfill trading system to include commercial waste would create a level playing field between the cost of disposal of both household as well as commercial waste, although adapting it needs careful planning. In particular, unless there is a UK-wide solution, Scottish businesses could face higher waste disposal costs potentially leaving them with a significant cost disadvantages relative to their UK and/or English competitors.

Household charges

39. Households are now facing the possibility of additional charges for dealing with their waste. Such charges are aimed at both paying for the service but also as a means of encouraging a change in household behaviours by reducing the amount of waste they seek to have collected. Some households already face an additional penalty where bins are uplifted less frequently than weekly. Whilst incentives for households may be necessary, they do not deal with the problem most households face, i.e., excessive and largely inescapable wrapping on most goods. Without dealing with manufacturers of such packaging, households will rightly feel aggrieved that they are being penalised for something they cannot easily avoid.

Conclusions

40. There are a number of key conclusions arising from this analysis.

Clarity of objectives

41. To meet the demanding municipal recycling targets by 2013 and 2020 greater clarity around the Ministerial targets for recycling and the level of public funding that will be forthcoming is now essential. This will reduce, though not eliminate, the inherent risks and uncertainty surrounding what infrastructure Scotland needs and, more importantly, is willing to pay for.

Landfill Allowances

42. The potential for failure of the Landfill Allowance Scheme needs to be addressed. First, it needs to include commercial waste otherwise there is the danger that local authorities can argue that they are effectively subsidising heavy, waste-producing commercial businesses. The Scottish Government should work with the UK Government to find a UK-wide solution to include commercial waste into any trading arrangement. In the shorter-term, it is important that Scotland's local authorities cannot circumvent the LAS penalty arrangement by seeking special treatment from the Scottish environment minister. Since the Minister is also the sector sponsor, any appeal system should not have the Minister as its final arbiter but should rest with a suitably qualified independent body (e.g., SEPA) who, in this instance at least, should be answerable to the Scottish Parliament.

Scottish Government Grants

43. The Scottish Government should open up its grant funding and potentially offer equity investments to all providers of waste recycling and treatment infrastructure. This would be aimed at developing the Scottish waste infrastructure market without the need for large, long-term and inevitably inflexible PPP arrangements. The Scottish Government funding could be set at the minimum grant necessary to encourage suitable investment to meet local authority output requirements. Funding should be awarded on the basis of achieving output specifications and not be based on any particular technology solution. If, however, there is a wish to see particular technologies being promoted, the Scottish Government should be willing to increase its initial subsidy to reduce any associated risks and uncertainties.

Regulatory structure

44. Where regional monopolies in Scotland's new waste infrastructure are likely to develop the Scottish Government should establish an appropriate regulatory framework for its on-going management. Price capping arrangements will be required to prevent abuse in pricing and any associated licensing arrangements should consider including frequent re-tendering of any rights to manage these key assets.

45. Any such price capping arrangement needs to ensure investors are adequately rewarded for the risks they carry. In particular, where lower levels of public subsidy have been secured to deliver any infrastructure, price-capping restrictions should be related only to the subsidised element of funding.

Appendix 1

The Allocation of Landfill Allowances (tonnes)

	05-06	09-10	% reduction
Aberdeen	73,076	53,004	-27.5%
Aberdeenshire	74,496	54,917	-26.3%
Angus	26,968	24,788	-8.1%
Argyll & Bute	37,009	27,560	-25.5%
Clackmannanshire	18,842	13,574	-28.0%
Dumfries & Galloway	50,251	35,741	-28.9%
Dundee	31,686	29,838	-5.8%
East Ayrshire	40,876	29,177	-28.6%
East Dunbartonshire	37,485	27,572	-26.4%
East Lothian	32,327	23,744	-26.6%
East Renfrewshire	29,395	22,023	-25.1%
Edinburgh	144,511	104,597	-27.6%
Falkirk	66,506	48,144	-27.6%
Fife	147,030	104,413	-29.0%
Glasgow	213,142	151,648	-28.9%
Highland	86,216	60,817	-29.5%
Inverclyde	26,940	19,131	-29.0%
Midlothian	30,770	21,915	-28.8%
Moray	33,881	25,437	-24.9%
North Ayrshire	45,619	33,823	-25.9%
North Lanarkshire	111,756	79,513	-28.9%
Orkney	1,487	1,400	-5.9%
Perth & Kinross	48,252	38,990	-19.2%
Renfrewshire	59,600	43,160	-27.6%
Scottish Borders	37,051	27,648	-25.4%
Shetland	2,694	2,537	-5.8%
South Ayrshire	44,356	32,308	-27.2%
South Lanarkshire	103,728	77,835	-25.0%
Stirling	41,305	30,384	-26.4%
West Dunbartonshire	32,772	23,832	-27.3%
West Lothian	55,664	40,405	-27.4%
Western Isles	14,310	10,125	-29.2%
Total	1,800,000	1,320,000	-26.7%

Source: Landfill Allowance Scheme (Scotland) Regulations 2005, Scottish Government Guidance: March 2007

Appendix 2

Recycling & composting rates for Scottish local authorities 2005-06

	Total waste	Recycled	Composted	Recycled & Composted
Aberdeen	133,675	12.5%	6.6%	19.1%
Aberdeenshire	155,123	11.9%	4.4%	16.3%
Angus	73,333	24.1%	8.6%	32.7%
Argyll & Bute	67,259	14.0%	11.1%	25.1%
Clackmannanshire	36,990	29.1%	11.1%	40.2%
Dumfries & Galloway	102,379	10.3%	0.1%	10.4%
Dundee	95,416	24.1%	6.8%	30.9%
East Ayrshire	71,776	21.3%	11.3%	32.6%
East Dunbartonshire	73,605	14.8%	11.0%	25.8%
East Lothian	64,331	18.0%	9.5%	27.5%
East Renfrewshire	58,117	18.1%	12.1%	30.2%
Edinburgh	261,493	14.3%	7.3%	21.6%
Eilean Siar	22,786	11.0%	0.0%	11.0%
Falkirk	115,168	21.2%	9.0%	30.2%
Fife	252,904	21.3%	7.7%	29.0%
Glasgow	397,880	6.5%	8.0%	14.5%
Highland	161,082	12.8%	7.1%	19.9%
Inverclyde	51,988	13.2%	5.4%	18.6%
Midlothian	52,567	10.8%	10.6%	21.4%
Moray	61,696	21.7%	9.1%	30.8%
North Ayrshire	87,205	15.0%	10.7%	25.7%
North Lanarkshire	231,898	18.2%	10.0%	28.2%
Orkney Islands	13,968	15.7%	7.1%	22.8%
Perth & Kinross	103,048	20.9%	12.4%	33.3%
Renfrewshire	102,615	18.3%	6.2%	24.5%
Scottish Borders	73,214	13.1%	2.9%	16.0%
Shetland Islands	13,086	9.6%	0.0%	9.6%
South Ayrshire	78,701	22.6%	11.7%	34.3%
South Lanarkshire	202,703	23.4%	9.9%	33.3%
Stirling	59,813	20.0%	13.9%	33.9%
West Dunbartonshire	61,220	13.5%	5.5%	19.0%
West Lothian	111,374	13.2%	13.8%	27.0%
SCOTLAND	3,448,413	16.1%	8.3%	24.4%

Source: SEPA Waste Data Digest 7, Table 15

Appendix 3

Net cost per household of local authority waste collection & disposal (£, nominal prices) for various years & Recycling / composting rate as at 2005-06

	COLLECTION & DISPOSAL					% Recycle & Composting
	01-02	02-03	03-04	04-05	05-06	05-06
<u>URBAN COUNCILS</u>						
Aberdeen	92.85	101.38	99.77	111.55	119.33	19
Dundee	115.99	128.58	130.81	114.01	124.69	31
East Dunbartonshire	93.47	97.09	108.64	115.57	111.83	26
Edinburgh	98.32	113.75	115.32	110.46	129.24	22
Falkirk	87.47	91.14	94.05	106.59	114.46	30
Glasgow	102.24	112.17	114.47	83.21	80.98	15
North Lanarkshire	90.17	104.59	89.51	78.17	93.99	28
Renfrewshire	90.59	96.11	104.42	89.28	100.14	25
West Dunbartonshire	82.31	92.69	93.21	97.72	91.44	19
Average	94.82	104.17	105.58	100.73	107.34	
<u>MIXED COUNCILS</u>						
Angus	95.04	105.22	106.02	72.90	98.81	33
Clackmannanshire	94.63	114.36	134.06	132.58	134.73	40
East Ayrshire	100.23	109.10	111.58	133.09	133.24	33
East Lothian	90.24	98.48	103.04	113.40	130.13	28
East Renfrewshire	88.17	94.07	121.77	106.19	127.06	30
Fife	88.78	91.35	106.34	81.35	93.75	29
Inverclyde	79.81	84.51	86.03	66.01	108.75	19
Midlothian	78.16	86.32	99.97	95.36	152.97	21
Moray	84.00	114.28	113.32	110.21	119.85	31
North Ayrshire	82.41	81.47	84.93	92.20	116.09	26
South Ayrshire	87.42	85.85	90.90	140.32	114.00	34
South Lanarkshire	77.47	79.84	104.03	120.24	116.80	33
Stirling	109.52	106.89	117.61	153.80	186.36	34
West Lothian	91.77	104.37	97.59	108.72	129.56	27
Average	89.12	96.87	105.51	109.03	125.86	
<u>RURAL COUNCILS</u>						
Aberdeenshire	99.19	110.19	121.28	97.78	112.99	16
Argyll & Bute	186.57	192.87	185.31	184.14	168.72	25
Dumfries & Galloway	95.92	109.07	107.42	132.34	145.37	10
Highland	129.72	121.66	145.75	153.49	185.94	20
Orkney	150.32	156.47	133.81	143.03	136.54	23
Perth & Kinross	140.22	150.70	146.68	137.84	150.53	33
Scottish Borders	87.46	98.42	96.64	63.74	64.16	16
Shetland	102.46	150.24	161.31	98.32	131.26	10
Western Isles	144.33	169.68	148.43	91.88	146.65	11
Average	118.88	130.62	130.61	122.84	140.33	
SCOTLAND AVERAGE	100.94	110.55	113.90	110.87	124.51	24

Source: Accounts Commission, Performance Indicators, local authority waste management, various years

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