
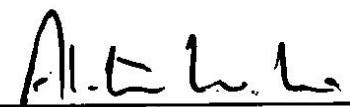


## FINANCIAL MEMORANDUM FOR BRITISH WATERWAYS IN SCOTLAND

Signed: 

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Chief Executive  
British Waterways

Date: 4 September 2009

Signed: 

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Date: 4 September 2009



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## OVERVIEW

### 1 Aims And Purpose

- 1.1 Scotland's inland waterways are an important national asset for future generations to enjoy. The Scottish Government (SG) is keen to see them maintained and developed in a sustainable manner so that they fulfil their full economic, social and environmental potential. British Waterways (BW) has responsibility for 220 km of canals in Scotland including statutory navigation and safety functions.
- 1.2 BW is a cross-border public authority under the Scotland Act 1998. BW is also classified as a Public Corporation and a public controlled market body since a majority of its revenues comes from its trading activities. BW is sponsored jointly by the Department of Environment, Food and Rural Affairs, and the SG. In law the BW Board is fully responsible for all of BW's activities.
- 1.3 The Accountability Framework for British Waterways in Scotland is a set of arrangements providing for the effective governance of BW in Scotland within the context of its statutory constitution. In particular the Accountability Framework establishes the respective responsibilities of the SG as the sponsor of BW in Scotland, the BW Board as the principal governing body and the Director Scotland together with the Scottish management as the delivery team. It has been drawn up by the SG, BW and the British Waterways Scotland business unit (BWS) in consultation with each other.
- 1.4 Documents within the Accountability Framework are:
  - SG policy documents setting the framework for public services in Scotland;
  - SG Policy document – Scotland's Canals: an asset for the future - published October 2002 (and any successor document). The Policy document is available at <http://www.scotland.gov.uk/Publications/2002/10/15571/11777>;
  - Financial Memorandum for BW in Scotland;
  - BW Corporate Governance Principles: Scotland; (see Annex B)
  - Financial Reporting Council – The Combined Code on Corporate Governance which is available at <http://www.frc.org.uk/CORPORATE/COMBINEDCODE.CFM>;
  - The "Greener deal" was outlined in the letter from Robin Evans, Chief Executive of BW, dated 3 September 2004. Details of a package to implement the outstanding BW commitment to increase commercial capital were agreed with SG and Defra by letters dated 17 March 2008, 15 April 2008 and 22 April 2008 (attached as Annexes J, K and L respectively); and
  - BW Business Plans for Scotland and Annual Reports and Accounts.
- 1.5 The SG has published a number of policy documents which set the overall context for public services in Scotland. These include the Government Economic Strategy – its purpose is to focus the SG and public services on creating a more successful country, with opportunities for all of Scotland to flourish, through increasing sustainable economic growth. A set of National Outcomes has been published, and there are Single Outcome Agreements between the SG and each local authority. In its Scottish operations, BW is required to work within the policy framework set overall by the SG and contribute to the outcomes sought.
- 1.6 The document Scotland's Canals: an asset for the future, published in 2002, describes in detail the SG's policy relating specifically to the canals. Briefly, in addition to their statutory functions relating to Scotland, the SG looks to BW to:
  - encourage much greater use of canals and associated facilities by the Scottish public;
  - promote and accommodate conservation and regeneration in Scotland;
  - maintain and enhance leisure, recreation, tourism and educational opportunities for the general public;

- facilitate water transport (including freight).

1.7 Working in partnership with local authorities and other Scottish public sector organisations, including enterprise and tourism bodies, the water industry and other private sector bodies, and the voluntary sector (including local groups) BW should seek to:

- maximise the quality of the waterways and surrounding amenities;
- secure additional investment;
- advance the management and operation of the waterways;
- explore ways to enable maximum public enjoyment of its facilities;
- increase income without damaging the environment and heritage of the assets;
- raise the profile of the waterways in general and the organisation in particular;
- enhance its national status, and improve its relationships with existing and future customers and potential partners.

## **2 The Role Of Scottish Ministers**

2.1 Scottish Ministers are ultimately accountable to the Scottish Parliament for the activities and performance of BW's activities relating to Scotland. Their responsibilities include:

- approving the policy and performance framework within which BW will operate, including agreeing objectives;
- providing information to the Scottish Parliament about BW's activities relating to Scotland as required;
- determining the amount of Grant-in-Aid payable to BW by Scottish Ministers within the context of the Scottish budgeting process;
- carrying out responsibilities specified in applicable legislation.

## **3 The Portfolio Accountable Officer**

3.1 The Director-General for Economy is designated by the Principal Accountable Officer for the SG as the Portfolio Accountable Officer for parts of the SG including the sponsor Directorate for BW (Transport Directorate). The Portfolio Accountable Officer must be satisfied that the financial and other management controls applied by the SG are appropriate and sufficient to safeguard Scottish public funds and the corresponding systems applied by BW for their activities relating to Scotland conform with the requirements of regularity, propriety and of good financial management. The responsibilities of a Portfolio Accountable Officer are set out in detail in the Memorandum to Accountable Officers from the Principal Accountable Officer - see Annex 1 of the section on Accountability in the Scottish Public Finance Manual (SPFM).

## **4 The Sponsoring Team In The Sponsor Directorate**

4.1 Within the Transport Directorate, the Freight and Inland Waterways Branch is the sponsoring team for BW. The Branch, in consultation as necessary with the Portfolio Accountable Officer, is the primary source of advice to Scottish Ministers on the discharge of their responsibilities in respect of BW, and the primary point of contact for BW in dealing with the Scottish Government. The Branch shall carry out its duties under a senior officer who shall have primary responsibility for overseeing the activities of BW.

4.2 The sponsoring team shall advise Scottish Ministers on:

- an appropriate framework of objectives and targets for BW in the light of Scottish Ministers' wider strategic aim[s];

- an appropriate budget for BW in the light of Scottish Ministers' overall public expenditure priorities;
- how well BW is achieving its strategic objectives and whether it is delivering value for money.

4.3 In support of the Portfolio Accountable Officer the sponsoring team shall:

**on performance and risk management**

- monitor BW's activities on a continuing basis through an adequate and timely flow of information from BW on performance, budgeting, control and risk management;
- address in a timely manner any significant problems arising in BW, whether financial or otherwise, making such interventions in the affairs of BW as is judged necessary;
- ensure that the activities of BW and the risks associated with them are properly and appropriately taken into account in the SG's risk assessment and management systems;
- ensure that appointments to the Board are made timeously and in accordance with the Commissioner for Public Appointments (OCPA) Code of Conduct. The OCPA code is followed rather than the Office of the Commissioner for Public Appointments in Scotland (OCPAS) code, as Defra is the lead sponsor.

**on communication with BW**

- inform BW of relevant SG policy in a timely manner; advise on the interpretation of that policy; and issue specific guidance to BW as necessary;
- the normal communication channel is between the Head of the sponsor branch and the BW, Director Scotland however the sponsor branch may bring concerns about the activities of BW in Scotland to the attention of the BW Board, and require explanations and assurances from the BW Board that appropriate action has been taken.

## **FINANCIAL MEMORANDUM for BW in SCOTLAND**

### **5 Purpose of Financial Memorandum**

- 5.1 This Financial Memorandum (FM) is one part of the Accountability Framework for BW in Scotland. The FM addresses financial governance issues such as safeguarding public monies; proper management of corporate financial resources; systems of control including the monitoring and management of financial and business risk; shareholder authorisation of substantial expenditure; financial propriety and compliance with applicable standards and protocols. The FM applies to those functions carried out by BW which are devolved to Scottish Ministers.
- 5.2 A separate FM exists in respect of BW's activities in England & Wales.
- 5.3 Copies of the FM and any subsequent substantive amendments will be placed in the Scottish Parliament Information Centre. It will also be made available on the SG and BWS websites at: <http://www.scotland.gov.uk> and <http://www.britishwaterways.co.uk/scotland>

### **6 Purpose of BW**

- 6.1 BW was established by the Transport Act 1962 to manage and maintain the inland waterways, and certain of the docks, originally nationalised under the Transport Act 1948. For national accounts purposes BW as a whole is classified as a Public Corporation. Furthermore, because its overall income from trading activities exceeds 50% of its overall revenues, it has a different and appropriate control framework to that of an Executive Non Departmental Public Body (NDPB). This classification is determined from the scale of its trading activities in England & Wales rather than those in Scotland.

### **7 Role of SG**

- 7.1 The SG is the sponsor for BW's activities as regards Scotland. Although BW is established by statute and is without share capital, the governance relationship between Defra and BW is described and treated under their Accountability Framework as that of "Shareholder" and "Company". In Scotland, the SG prefers the term "Sponsor", but uses the Shareholder term for consistency when accountability documents are common to both Scotland and England & Wales.

### **8 Review of FM**

- 8.1 This FM shall be reviewed every three years unless jointly agreed otherwise and may be subject to change within that time at the direction of the SG. The next review is due to start in 2012. Legislative changes will take precedence over any part of the FM. The SG shall resolve any question regarding the interpretation of the FM after consultation with BW's Director Scotland. Reviews may be initiated at the discretion of the SG or at BW's request.

## **9 Review of BW**

- 9.1 As part of the policy process, SG will also periodically review or confirm BW's purpose within the context of its statutory constitution and the Public Policy Objectives set, normally at least every 5 years. This may involve joint review activity with Defra and timing of the review would be subject to agreement with Defra.

## **Legal Context**

### **10 BW Statutory Powers**

- 10.1 Under powers contained in the 1962 and 1968 Transport Acts BW has responsibility, including statutory navigation and safety functions for over 3,200 km of canals and rivers, of which 220 km are in Scotland. With due regard to efficiency, economy and safety, it has the duty to provide services and facilities on the inland waterways and port facilities owned or managed by them (Transport Act 1962, S10). BW also has the duty to exploit commercial opportunities to raise income in support of its navigation and safety function and the duty to act as if it "were a company engaged in a commercial enterprise in its non navigation commercial activities." (Transport Act 1968, S134).

### **11 Devolved Powers for BW in Scotland**

- 11.1 As a consequence of the Scotland Act 1998, legislative competence regarding inland waterways in Scotland is devolved to the Scottish Parliament - BW was designated as a cross-border public authority under the Scotland Act 1998 (Cross-Border Public Authorities) (Specification) Order 1999. The Scotland Act 1998 (Cross-Border Public Authorities) (Adoption of Functions etc.) (No. 2) Order 2000 made under section 89 of the Scotland Act 1998 transferred responsibilities to the then Scottish Executive on 13 December 2000. Prior to this, the sponsorship of BW lay fully with the then Department of the Environment, Transport and the Regions (DETR).

## **Management Of Risk**

### **12 Risk Management Framework**

- 12.1 BW shall maintain a robust framework to manage risk that fully incorporates effective risk management. These processes should be embedded as far as possible into the everyday management of BW. The risk framework will comprise the following key elements:
- a culture which supports well thought out risk taking and promotes learning from experience of managing risk;
  - a corporate risk policy that sets out the overall approach to risk management;
  - effective processes for identifying, assessing, addressing, reviewing and reporting risks;
  - clear allocation of ownership of risks and delegation of authority for taking risks.

Ensuring that the risk framework is fit for purpose shall be a key responsibility of the BW Board, supported by the work of its Audit Committee.

- 12.2 In accordance with its duty to act as if it “were a company engaged in a commercial enterprise” in its non-navigation commercial activities, BW shall work to secure an adequate rate of return in the context of an acceptable level of risk and with due regard to the economic, social and environmental impacts for the benefit of Scotland. Its Investments Strategy, agreed by the BW Board and the Sponsor, establishes the overall risk/return balance of its activities portfolio, and is therefore a key element in articulating the level of exposure which is considered tolerable and justifiable and how much is actively put at risk for the benefits of the opportunity.

### **13 Sponsor assurance and communication**

- 13.1 There will be regular and open discussion of risk issues with the SG. BW shall provide such reasonable assurance as the SG requires of the effectiveness of its risk management through monitoring and reporting arrangements, by audit processes (internal and external) and by engagement with the BW Board. Through BWS, BW will communicate its key risks to the SG as part of the quarterly exchange of information within the reporting framework, on request, and when seeking approval for projects from the SG.
- 13.2 The BW Board will also report to Scottish Ministers on BW’s corporate level processes for risk identification and management in the Annual Report laid before the Scottish Parliament.

## **Management And Control Systems**

### **14 Board and Chief Executive of BW**

- 14.1 The Board of BW is responsible for all aspects of BW’s organisation and performance. The Chair has a particular responsibility for the proper discharge by the BW Board of its collective role, and compliance with this FM. The Chair of BW is personally responsible to Scottish Ministers for ensuring that BW’s policies relating to Scotland are compatible with those of the SG and ensuring probity in the conduct of BW’s affairs relating to Scotland.
- 14.2 The Chief Executive is appointed by the BW Board, following open competition. The BW Board delegates to him responsibility for day-to-day management. He must ensure that BW meets the requirements of BW’s FM in respect of Scotland and that BW takes full account of any guidance issued to it by the SG, and any recommendations of the Scottish Parliament or Parliamentary Committees which have been accepted by the SG.
- 14.3 BW has appointed a Director Scotland, who is responsible on a day to day basis for all aspects of BW activities relating to Scotland. This executive director will maintain regular contact with officials in the SG Transport Directorate and act as a key point of contact. This will involve attendance at quarterly progress review meetings.
- 14.4 The senior official of BW carries responsibilities which effectively put him in the position of BW’s Accountable Officer even though he is not formally designated as such. In this capacity the Chief Executive shall exercise the following specific responsibilities:

#### **on advising the Board**

- advise the Board on the discharge of its responsibilities as set out in this document and in any other relevant instructions and guidance issued by the Scottish Ministers / sponsor Directorate;

- advise the Board on BW's performance compared with its aim[s] and objectives;
- take action if the Board, or its Chairman, is contemplating a course of action involving a transaction which the Chief Executive considers would infringe the requirements of propriety or regularity

#### **on Staff Management**

- ensure for their activities relating to Scotland that BW has appropriate staff management policies in place for the recruitment, retention and motivation of its staff.

## **15 Standards and Maintenance**

- 15.1. Subject to its statutory obligations, BW is required by Scottish Ministers to operate and maintain its Scottish waterways to standards that reflect use and prospects of use and any land drainage requirements. As well as maintaining published customer service standards, BW carries out a rigorous, mandatory inspection programme of its structures such as bridges and embankments. BW repair and maintenance programme takes account of the level of risk identified by the inspection process.
- 15.2. BW seeks to co-operate and work in partnership with the relevant statutory bodies to ensure standards are appropriate to heritage, environment and public access rights and aspirations.
- 15.3. BW issues and maintains an Environmental Code of Practice and a Biodiversity Action Plan to ensure compliance with its statutory environmental obligations, and to give appropriate emphasis to environmental and heritage aspects in its management of Scotland's canals. BW seeks to co-operate and work in partnership with the relevant statutory bodies.
- 15.4. At all times BW will seek to ensure that its Scottish waterways are maintained in a safe condition so that they do not impose unreasonable risk on users or neighbours.

## **16 Control of Public Funds**

- 16.1. BW shall have appropriate management and control systems in place so that it can demonstrate proper stewardship of public funds provided to it and that it is able to manage and account for public funds properly and effectively. The management and control systems shall ensure that:
  - the BW Board and Chief Executive take effective responsibility for the proper use of public funds;
  - BW's activities conform with the requirements of propriety and regularity as set out in Managing Public Money;
  - high standards of internal control are maintained to ensure that internal procedures meet the applicable requirements of Managing Public Money; and
  - no funds are used for any expenditure of a novel, contentious or repercussive nature without approval from the SG.
- 16.2. In order to assist BW to meet its statutory obligations in Scotland, BW receives financial support from the SG. Funding from the SG bridges the gap between its agreed expenditure and the income it can generate from its Scottish operations. SG funding is allocated within its Spending Reviews and is provided separately for revenue and capital (currently in the ratio of 80:20). Chapter 11 of HM

Treasury's Consolidated Budgeting Guidance (updated periodically) provides guidance on the budgeting treatment of public corporations.

- 16.3. The Grant-in-Aid level will be determined by Scottish Ministers in order to achieve agreed standards of performance and operation of the waterways and, in particular, to maintain and conserve the integrity and safety of the assets. In common with all public bodies, it is necessary for priorities to be established and a balance struck between the canal policy and the wider interests of the Scottish economy and SG policy. Each year the sponsor Directorate will send to BW:
- a formal letter stating the annual budgetary provision allocated by Scottish Ministers in the light of competing priorities across the SG and of the associated Grant-in-Aid; and
  - a statement of any planned change in policies affecting BW.

The Grant-in-Aid notification may contain conditions. An example is achievement of required levels of efficiency savings, where BWS will report on delivery of these in their quarterly reports to the SG.

- 16.4. In pursuing its aims relating to Scotland, BW should:
- seek to achieve value for money in all its activities whilst having due regard to the economic, social and environmental impacts for the benefit of Scotland;
  - work to secure an adequate rate of return in the context of an acceptable level of risk;
  - seek opportunities for private sector partnerships, for example, through direct investment, joint ventures and sales of surplus assets;
  - make maximum use of funds from Europe, National Lottery or other funding mechanisms so as to keep BW's demands on SG funds to a minimum.
- 16.5. The SG shall make payments to BW on a monthly basis, subject to the agreed Grant-in-Aid allocation not being exceeded and Grant-in-Aid not being drawn down in advance of need. The SG shall make monthly payments based on the phased budget profile submitted to the SG by BWS in March for the forthcoming year. More frequent requests for payment may be submitted to meet any unforeseen cash shortfall.
- 16.6. Once BW Grant-in-Aid has been approved by the SG, BW shall have the authority to incur expenditure/consume resources without further reference to the SG, on the following conditions:
- BW shall comply with the specific delegations set out in Annex F.
  - BW shall comply with the conditions set out in this FM and with any relevant guidance issued by Scottish Ministers.
  - Inclusion of any planned and approved expenditure in BW's budget shall not remove the need to seek SG approval where any proposed expenditure is outside the delegated limits or is for new schemes not previously agreed.
- 16.7. BW shall provide the SG with such information about its operations, performance, individual projects or other expenditure as the SG may reasonably require. BW and its activities in relation to Scotland should keep within its allocated budget. If regular monitoring suggests that BW may overshoot the budgets then remedial action should be taken by BW to prevent this. BWS should inform the SG at the earliest opportunity of any circumstances which might compromise its ability to remain within these limits. The SG reserves the right to review allocations during the year and adjust them if the SG's financial position requires it. Any changes to the allocation will not take place without prior consultation with BWS.
- 16.8. BW must inform the sponsor team of any potential underspend, and must do so as soon as the underspend is identified. Depending on the size and nature of the underspend, and on the stage of the financial year at which it is identified, the sponsor team, in consultation with the Finance Directorate, will decide on the

appropriate action. It is particularly important for BW to identify any slippage on capital projects as early as possible.

- 16.9 BW shall seek to maximise income from other sources provided this is consistent with the SG's policy document, BW's core functions and its Scottish Business Plan as agreed with the SG. Whenever practical it should charge its customers directly for benefits received consistent with prevailing market rates and only resort to Grant-in-Aid to fund activities where, in agreement with the SG, there are wider social benefits or it is impractical or not cost effective to charge directly for services provided.
- 16.10 BW should ensure that the SG is informed of potential EU funding prior to acceptance so that there can be a full assessment of the implications of such funding for the SG.

## **17 Increasing commercial capital in Scotland**

- 17.1 The "Greener deal" was outlined in the letter from Robin Evans, Chief Executive of BW, dated 3 September 2004. Details of a package to implement the outstanding BW commitment to increase commercial capital were agreed with SG and Defra letters dated 17 March 2008, 15 April 2008 and 22 April 2008 (attached as Annexes J, K and L respectively) ("The 2008 Agreement")
- 17.2 The 2008 Agreement also addressed ring fence funding and accountability for BWS, established an appropriate process for approval of capital investment and disposal transactions and reviewed the internal service level agreement between BWS and BW for central services.
- 17.3 BW will maintain a separate commercial bank account for Scotland in which to deposit receipts from disposal of non operational estate and make payments to acquire investments to grow its non operational estate. BWS shall report commercial capital transactions in its quarterly report to the SG.
- 17.4 BW shall carefully control the level of central charges under the internal service level agreement between BW and BWS and this shall be subject to reduction as efficiency savings are achieved by BW.

## **18 Commercial Exploitation**

- 18.1 BW currently enjoys statutory rights in respect of existing water abstractions, but it should work with the regulatory authority to ensure that best practice and conservation is demonstrated in its use of water. In this way BW will ensure that, where it applies for approval to increase water abstractions in order to sustain navigation or undertake additional water sale opportunities, the proposals are practical and environmentally sound. BW maintain Water Management Plans for Scotland's canals to ensure the optimum long-term use is made of water resources.
- 18.2 BW should encourage adjoining landowners and authorities to participate in jointly enhancing value by the regeneration and provision of facilities that are to the benefit of the general public and that improve the tourism, recreational, amenity and community value of the waterways for boaters, anglers, walkers and cyclists. BW will seek funds from grant awarding bodies, such as Lottery distributive bodies, European, regional and local agencies, in order to facilitate the achievement of these objectives.

- 18.3 BW should continue to encourage the development of more commercial leisure activities and marina developments where opportunities exist.
- 18.4 BW should exploit its technical and management expertise in waterways in conjunction with other organisations who need this specialist capability. BW will pursue diverse and innovative schemes for the use, development, conservation and exploitation of the Scottish waterways to increase revenue earning capability and minimise running costs.

## **19 BWS Strategy**

- 19.1 The SG has published a number of policy documents which set the overall context for public services in Scotland. The SG's policy document, Scotland's Canals: an asset for the future, recognises that Scotland's canals are an asset that, if used wisely, can enhance the future quality of life in Scotland. BW's strategy and business model is determined to achieve the objectives as determined in the SG's policy document. The SG and BWS will agree this strategy, as well as periodically reviewing progress at the Quarterly meetings.

### **BWS Business Plan – The link between resources and outputs**

- 19.2 BW has an important role to play in achieving the strategic objectives set by the SG for the Scottish public sector, especially in aspects such as sustainable development, sustainable transport, regeneration, heritage, leisure, tourism, climate change and environment in Scotland. Further details of controls on BW's resources and the spending flexibilities available to the BW Board are set out in this part of the FM.
- 19.3 To complement the SG's policy document and BW's strategy, BW management will prepare a detailed 3 year rolling Business Plan for Scotland ('the Plan') to deliver the Strategy. A draft of the Plan will be submitted and agreed with the BW Board and the SG in accordance with an agreed timetable as set out in Annex C and revised on an annual basis. Progress against the Plan will be regularly assessed as part of the performance monitoring/interaction process (see para 39-42 of this document). The quarterly performance reports will also incorporate the Key Performance Indicators to monitor progress. Progress against Key Performance Indicators will be covered in the Annual Report and Accounts. BW will publish a summary of the Plan annually (excluding any commercially sensitive information) and hold at least one public meeting in Scotland each year. The summary plan will be made accessible on the SG and BWS websites.
- 19.4 In order to monitor BW's performance in achieving agreed objectives and targets and to inform future spending plans, BWS is to provide the SG with information as defined and timetabled in Annex C. The appropriate SG officials will meet with representatives of the BW Board from time to time to discuss BW's performance relating to Scotland, its current and future activities and any policy developments relevant to those activities. These meetings will occur both at day to day contact level via the Quarterly meetings and at senior official level via High Level meetings, including the SG Director of Transport, the Chair of BW and the Chief Executive of BW.
- 19.5 In drawing up the Plan, BW shall have regard to guidance issued by Scottish Ministers such as the policy framework as described in Scotland's Canals: an asset for the future (or successor) and to any other guidance on Corporate Planning issued from time to time. Unless otherwise notified, BW will submit a draft Plan in accordance with the timetable as set out in Annex C.

- 19.6 The SG expects BW to present the Scottish Business Plan in a form that readily assists them to reach conclusions about the effectiveness of BW, its strategy, the level of performance to be expected of it and the resources it requires. BW shall maintain a system of planning covering all Scottish functions for which it is responsible, all its income and expenditure and its profit and loss. The Plan will span 4 financial years – the previous year and three future years. During a Scottish Spending Review (SSR) period there may be the requirement to report 5 financial years, the current year and 4 future years.
- 19.7 The forward looking Plan will, in relation to BW's Scottish activities:
- set out BW's aims and objectives and its performance indicators and targets, which are subject to agreement with the SG;
  - provide a forecast showing BW's Scottish income (having regard to likely levels of Grant-in-Aid) and gross expenditure over the following three financial years, together with planned outputs;
  - include BW's planned expenditure on fixed assets and proposals for disposal and investment targets for non-operational land;
  - present key details of administrative expenditure including a strategy to produce continuous improvement in efficiency and cost effectiveness;
  - report on areas of the Scottish network for which grants from third parties have been sought, their purpose, expected amount and anticipated timing of receipt; and
  - require to demonstrate delivery of any outstanding commitments such as the "Greener deal".

## **20 Performance Targets**

- 20.1 The Plan should contain formal targets for BW in Scotland as agreed between the SG and BWS.
- 20.2 The SG will discuss the Plan with BW's Director Scotland and will confirm agreement of targets for standards of performance and operation of the Scottish waterways and, in particular, maintenance and conservation of the integrity and safety of assets.

## **21 BW Commercial Activities and its Property Estate**

- 21.1 BW is responsible for the management of its Scottish estate in accordance with its objectives to achieve agreed policy aims and plan targets.
- 21.2 BW shall define as operational such land and property that is essential to the maintenance of the Scottish waterways and held for running its business, recreational, amenity and freight activities. It shall take account of potential developments in defining assets as operational.
- 21.3 BW shall report to the SG on its Scottish land and property activity annually, with an independent valuation of its Scottish land and property provided every three years.
- 21.4 In determining how to best make use of its Scottish non-operational properties, the BW Board shall be free to act within the guidance and consents set out in Annex E, subject to the delegation limits at Annex F, and project appraisal and approval procedures set out in Annex H.
- 21.5 Defra Ministerial consent is required for the abstraction and sale of water by BW in Scotland.

## **22 Joint Ventures**

- 22.1 Before negotiating a joint venture and seeking the SG's approval BWS should ensure that they fulfil all requirements of the SG including:
- the choice of participant is subject to open competition in accordance with EU procurement rules ( in Joint Ventures involving owners of neighbouring property with marriage value, no choice may be available);
  - in respect of any BW assets provided to the venture, the option of outright disposal is kept open to be considered alongside partnership bid;
  - the nature and purposes of the venture are consistent with BW's powers and objectives;
  - all reasonable alternative options have been considered, including doing nothing, and full financial analysis has been undertaken;
  - a robust sensitivity and risk analysis has been undertaken and adequate safeguards for BW are available, such as BW's ability to sell or assign its interest; and
  - SG Finance is satisfied that the venture entity will not be classified by the Office for National Statistics (ONS) as a public body.

Further considerations are shown at Annex E.

## **23 Disposal proceeds**

- 23.1 In managing its non-operational estate for Scotland, in accordance with the guidance at Annex E, BW will work to secure adequate rate of return in the context of an acceptable level of risk and with due regard to the economic, social and environmental impacts for the benefit of Scotland. BW's estimated disposals proceeds will be taken into account, and fixed asset investment levels set, in the annual planning process.
- 23.2 It is recognised that in seeking to maximise income from its estates portfolio, BW may not be able to match the timings of disposal proceeds with re-investments. Combined with restrictions on borrowing, this will generally mean that BW holds disposal proceeds awaiting re-investment particularly when additional receipts (in excess of approved plan levels) are received in the current year; or planned receipts are received too late to be re-invested within the current year; or unexpected problems occur with the re-investment opportunities which make it impossible or inadvisable to re-invest within the current year.

## **24 Project appraisal and approval**

- 24.1 BW, through BWS, shall obtain the prior approval of the SG before incurring any expenditure with novel or contentious features. It shall secure the prior approval of the SG before entering into any financial commitment which exceeds the delegations summarised at Annex F. Project approval guidelines are at Annex H. Submissions for approval should be made by a person notified to the SG as authorised to do so on behalf of the BW Board and should contain the information stipulated at Annex H.
- 24.2 BW is to maintain, operate and document appraisal and authorisation procedures for all projects (whether capital, maintenance, estates, market research, or administration). BW staff undertaking appraisals should be trained to carry out the documented procedures. All proposed projects must be appraised in line with agreed good practice. Guidance on project appraisal is at Annex H.

- 24.3 In January and July each year BW shall submit to the SG a list of all development projects (land acquisition and/or improvement) involving expenditure above £500,000 (inclusive of fees) authorised within the previous six months. This enables the SG to monitor BW's compliance with the procedures and their commitment to conduct post-project evaluations.

## **25 Income**

- 25.1 BW should maximise, as far as practicable, revenue from its operational activities by charging a market rate for its services. Receipts from operational activities are internal resources. Proposals for new sources of income or methods of fundraising should be cleared with the SG. Any receipts which are additional to those estimated in the Plan may be used to increase expenditure in the year they arise.
- 25.2 Interest earned by BW on cash balances may be used to provide additional spending power subject to it being included in the approved budget.

## **26 Claims, losses, write offs**

- 26.1 BW shall keep a record of all losses, write-offs, and compensation payments, available for inspection if required. BWS shall report to the SG any losses, write-offs and compensation payments in the format at Annex C and in the Annual Report and Accounts. A loss may be material for either financial or reputational reasons or both.
- 26.2 The prior approval of the SG shall be required for any agreement by BW to make any compensation or loss payments which exceed £5,000 or (if less) are "novel, contentious or repercussive". Any non voluntary payments of such nature (e.g. pursuant to an order of a court) shall forthwith be reported to the SG.

## **27 Gifts, awards and prizes**

- 27.1 The making of gifts, awards and prizes shall be directly related to the achievement of BW's objectives in Scotland. In the context of BW's commercial activities, prizes may be offered to retail customers of BW (other than employees of BW or their close associates) in connection with normal marketing practices.
- 27.2 In other circumstances, BW's Director Scotland may authorise the giving of gifts of a value of no more than £300 to any persons (other than employees of BW or their close associates) where in the interests of BW and not for any improper use.
- 27.3 BW's Chief Executive and Director Scotland may authorise the giving of gifts or awards to employees of BW in connection with generally acceptable employment practices (including but not limited to, recognition of long service, incentivisation, promotion of good practice, and improvement of skills and knowledge).
- 27.4 BWS shall keep a record of all gifts, awards and prizes. It should include a brief description of the item, the cost, the name of the recipient and the reason for making the gift, award or prize. The record should be submitted to the SG annually and also made available to the SG at other times on request.
- 27.5 Gifts do not include the issue of free or complimentary copies of publications, leaflets, calendars or other such promotional material produced and distributed in large numbers. If BWS is in any doubt about whether a particular item of expenditure counts as publicity or as a gift, the SG should be consulted.

## **28 Insurance**

- 28.1 BW may act in accordance with good insurance practice for commercial bodies and may insure to the level that is appropriate to the business.
- 28.2 Such insurance arrangements may include self insurance through a captive insurance subsidiary (subject to all necessary authorisation) that operates in accordance with EU Insurance Directive requirements.
- 28.3 BW shall review the management of its insurance from time to time to ensure that the risks it faces are dealt with in an appropriate manner and shall make a return to the SG by 31 May 2009 and every 3 years from that date setting out details of its current insurance policies and highlighting any changes as appropriate.

## **29 Procurement**

- 29.1 BW's procurement policies shall reflect the guidance from the Office of Government Commerce. BW shall also ensure that it complies with any relevant EU or other international procuring rules. All contracts let by BW, whether for works (capital or maintenance), consultancies, stores or services should be designed to secure value for money and periodically benchmarked against best practice elsewhere. They should be let on a competitive basis. BW shall prepare and maintain internal instructions which ensure that the number of tenders sought for each contract is consistent with the best public sector practices. Procurement by BW of works, equipment, goods and services shall be based on value for money, ie quality (in terms of fitness for purpose) and delivery against price. Where appropriate, a full option appraisal shall be carried out before procurement decisions are taken.

## **30 Timeliness in paying bills**

- 30.1 BW shall comply with the Late Payment of Commercial Debts (Interest) Act 1998 as amended. (NOTE; the 1998 Act allows creditors to claim statutory interest and compensation on late payment of commercial debts).
- 30.2 BW shall take full account of any direction from the SG to the Scottish public sector about prompt payment of bills in force from time to time.

## **31 Partnerships with either Public or Private Bodies**

- 31.1 The policy document Scotland's Canals: an asset for the future identified that public bodies in Scotland whose activities are relevant to the canals need to work together in order to maximise the public benefits available from Scotland's canals.
- 31.2 The Scottish Canals Development Group, a partnership chaired by the SG, meets annually or as appropriate with the agreement of SG to pro-actively engage and work together at chief executive level to progress the development of

the canal corridors to ensure that they fulfil their wider economic, social and environmental development potential for the benefit of Scotland.

- 31.3 The British Waterways Scotland Group (BWSG) was formed to build BW status, relationships and profile in keeping with its enhanced role as an active, responsible member of the Scottish community in Scotland's devolved political environment. It is a non-statutory group with a counselling, consultative and influencing function externally and internally, working to support the BW Board and its executive directors.
- 31.4 Where appropriate, BW should consider the scope for developing Partnerships with either Public or Private bodies for developing and improving existing services, the development of new services and to obtain the benefit of new capital investment. In considering the scope for improving and developing such projects BW should have regard to SG policy documents and existing SG guidance.

## **32 Shareholding and Interests in Corporate/Unincorporated Bodies**

- 32.1 Except in the circumstances set out in the Acquisition of Securities section of Annex E, BW requires the SG's consent before subscribing for or acquiring securities in corporate bodies. BW should seek the SG's prior approval before acquiring any interest in an unincorporated body.

## **33 Contingent Liabilities**

- 33.1 BW with regard to its activities in Scotland shall not lend money, charge any asset or security, give any guarantee or indemnities or letters of comfort, or incur any other contingent liability except with the approval of the SG. It shall report to the SG on any contingent liabilities incurred otherwise than in the course of its normal trading activities.

## **34 Gifts, bequests and donations**

- 34.1 BW is free to retain any gifts, bequests or similar donations. These shall be treated as receipts that, where appropriate, can be used to increase spending power. BW shall keep a written record of any such gifts, bequests and donations and of their estimated value and whether they are disposed of or retained.

## **Regularity and Propriety**

### **35 BW Management of Risk**

- 35.1 BW has a duty to ensure that the resources provided from the Scottish Consolidated Fund, and for which it is accountable to the Scottish Parliament are managed in a way which meets the requirements of SG guidance in terms of regularity, propriety and value for money, and satisfies the requirements of the SG's Accountable Officer. BW will comply with Managing Public Money procedures where specific reporting requirements are necessary.

## **36 Fraud and theft**

- 36.1 Any novel or material (financial or reputational) fraud or suspected fraud, whether involving a member of BW or a third party, must be reported immediately to the SG in the format at Annex C. An annual report on fraud and theft shall be made to the SG by BWS.

## **37 Relations with Users and Appeals Procedures**

- 37.1 BW maintains a statement of customer services standards incorporating people, safety and performance standards which it publishes on its web-site.
- 37.2 So far as is practicable, BW consults with individual waterway users, user organisations and others affected by its activities on matters such as standards, leisure, amenities and charges, in advance of decisions of significant interest to them. The SG expects that BW will engage in a high level of dialogue with the Scottish public to gain advice and feedback on its activities and provision of services. This will involve means such as formal liaison groups, informal relationships with local communities and partnership working with other organisations.
- 37.3 The Inland Waterways Advisory Council (IWAC) was established under the Transport Act 1968. IWAC's statutory remit was amended by the Natural Environment and Rural Communities Act 2006 (NERC Act). Scottish Ministers appoint 2 members of the Council. The Act gives IWAC wider terms of reference covering all waterways in England and Wales. In Scotland, its remit is limited to waterways owned or managed by BW, or in respect of which BW is providing technical advice and assistance. It is part funded by the SG and provides advice to Scottish Ministers and to BW on matters relevant to canals.

## **38 Complaints and appeals to Waterways Ombudsman**

- 38.1 Customers who consider themselves to have been unfairly treated by BW are entitled to invoke the BW two stage complaints procedure.
- 38.2 Where maladministration is alleged, customers have a right of appeal to an independent Waterways Ombudsman. BW has agreed to be bound by the Ombudsman's decisions on matters relating to maladministration.

## **Monitoring Arrangements**

### **39 Reporting to the SG**

- 39.1 BW has a general duty to supply such Scottish-related financial information and output data as the SG may require to monitor BW's expenditure, income and performance against agreed targets, and account, for Grant-in-Aid paid to BW by the SG. In general this information will be supplied through BWS. A timetable for submission of key financial information and output data is at Annex C.
- 39.2 The SG is required by legislation in the Transport Act 1962, paragraph 8(2A) of schedule 1, to lay details before the Scottish Parliament of appointments to the BW Board and changes in their remuneration, as soon as possible. BW is therefore required to provide the SG with accurate details (including dates) of changes to BW Board committee membership as soon as these changes have

been agreed. This is necessary as Board committee membership attracts additional fees.

## **40 Annual Report and Accounts**

- 40.1 At the end of each financial year, BW is required to publish a GB annual report of its activities together with its audited annual accounts (see Annex C). A pre-publication copy of the report shall be submitted to the SG in accordance with an agreed timetable. The report and accounts shall be laid before the Scottish Parliament by the SG.
- 40.2 The SG should receive copies of any management letters sent to the BW Board by the auditors together with the BW Board's response when the latter issues; this should be in accordance with any timetable set for the purpose.
- 40.3 The quinquennial policy review of BW undertaken in 2004 identified a need for transparency of reporting on BW's activities relating to Scotland. BW address this in their Annual Statement of Accounts by showing separate accounting information as far as possible for Scotland together with a separate report from Director Scotland. In addition, the BW Board will provide the SG with such returns, accounts and other information with respect to its property and activities in Scotland, as the SG may from time to time require.

## **41 External Audit**

- 41.1 The BW Board and Audit Committee will select external auditors to recommend for appointment by the Secretary of State (required by Transport Act 1962, Section 24(2)) after consultation with Scottish Ministers. BW bear the audit expenses. Subject to satisfactory performance the auditor can be reappointed annually. The frequency of re-tendering is by reference to current UK Finance guidance.
- 41.2 External auditors are responsible for reporting on:
- the preparation of BW's accounts in accordance with the Accounts Direction issued by Defra with the approval of Scottish Ministers (such report to be addressed to the BW Board who are required to send it to the Scottish Ministers);
  - Regulatory Compliance with the relevant principles of Managing Public Money (insofar as they relate to Public Corporations) and other requirements as detailed in their appointment letter (such report to be addressed to Scottish Ministers); and
  - the scope, nature and effectiveness of the BW Board's Internal Audit processes in meeting Government Internal Audit Standards (GIAS) (such reports to be addressed to the BW Board and copied to Scottish Ministers).

## **42 Internal Audit**

- 42.1 It is the responsibility of the Chief Executive to maintain an effective internal audit service in accordance with the standards, objectives and practices set out in an appropriate professional standard. The internal audit service shall provide an independent appraisal and evaluation of BW's internal control systems, i.e. the whole network of systems and controls established by BW to deliver its objectives with regularity, propriety and value for money.
- 42.2 The BW Board shall operate an Audit Committee and shall incorporate within its annual report to the Secretary of State a statement to confirm that BW's internal

audit arrangements accord with the objectives, standards and practices set out in GIAS.

- 42.3 The SG's Internal Audit Service shall have a right of access to all documents prepared by BW's internal auditor, including where the service is contracted out.

## Annex A – Glossary

Glossary of main terms and abbreviations used in this memorandum

1962 Act	Transport Act 1962
1968 Act	Transport Act 1968
The Board	The Board managing BW, appointed by the Secretary of State and in the case of 2 members, Scottish Ministers.
BW	British Waterways, the cross border public authority
BWS	British Waterways Scotland, the business unit of BW based in Scotland
BWSG	The British Waterways Scotland Group
Chair	The chairman/woman of the BW Board (appointed by the Secretary of State after consulting Scottish Ministers)
Chief Executive	The senior executive director of BW (appointed by the BW Board)
CIG	Commercial Investment Group
Defra	Department for Environment, Food and Rural Affairs
DEL	Departmental Expenditure Limit
Devolution	The Scotland Act 1998 which devolves legislative responsibility for inland waterways in Scotland to Scottish Ministers and associated Statutory Instruments (SIs)
Director Scotland	The official appointed by the BW Board to head up the operational business unit for Scotland
FM	Financial Memorandum
GIAS	Government Internal Audit Standards
Government	Scottish Government / Scottish Government and Defra
Grant-in-Aid	The financial support provided by the SG to BW to support their core activities relating to Scotland. It is split 80:20 resource to capital.
Greener deal (implementation of)	In 2004, BW committed, in return for increased grant levels from SG in the budget period 2004-07, to invest an additional £12m to £15m commercial capital in Scottish projects in order to generate additional income for BWS of at least £1m per annum in future years.
IFRS	International Finance Reporting Standards
IWAC	The Inland Waterways Advisory Council
OCPA	The Office of the Commissioner for Public Appointments (in England and Wales) – this code is used for all BW appointments including appointments by Scottish Ministers
OCPAS	The Office of the Commissioner for Public Appointments in Scotland
ONS	Office for National Statistics
Secretary of State	The Secretary of State responsible for inland waterways policy in England and Wales and those acting on his/her authority
Scottish Government	The devolved Government for Scotland (incorporates Treasury function for Scotland)
Scottish Ministers	Responsible for devolved inland waterways policy in Scotland and those acting on their authority.
SG	Scottish Government
Shareholder/Sponsor	The Scottish Government
SPFM	Scottish Public Finance Manual
Sponsor Team	The Scottish Government Transport Directorate

## Annex B - Corporate Governance Principles

### BRITISH WATERWAYS CORPORATE GOVERNANCE PRINCIPLES: SCOTLAND, as signed off 21 December 2006

#### Background

- 1 BW is a statutory cross-border public corporation established by the Transport Act 1962, as amended and supplemented by the Transport Act 1968, an Order to the Scotland Act 1998 and other legislation. The governance framework provided by those statutes is the equivalent of the Memorandum and Articles of Association for a limited company (though with less detail and precision). Hence in this document the Scottish Ministers are described as “the Shareholder” and British Waterways as “the Company”.
- 2 This document is intended to explain how the relationship between the Company and the Shareholder should work so as to maximise the success of the business consistent with BW’s underlying statutory provisions.
- 3 Considerable discretion is delegated to the Board under BW’s governing statutes that broadly follow the Companies Act model. A key provision concerning the Shareholder’s powers (Transport Act 1962, Section 27, entitled ‘Powers of Ministers in relation to Boards’) provides that powers of general direction are limited to “directions of a general character as to the exercise by the Board of their functions.....in relation to matters which appeared to him to affect the national interest.” The Public Corporation model (as compared to an Executive Agency) requires an arms length relationship with the Shareholder who exercises no direct executive control over the business. The governance regime will acknowledge these powers of the Board together with the legitimate rights of the Shareholder to exercise effective scrutiny as owner of the Company.
- 4 Specific powers of direction are reserved for a few particular acts or events, but the statutory governance framework clearly gives the Board significant discretion to devise the strategy necessary to meet the public policy objectives determined by the Shareholder. Nevertheless the absence of financial market disciplines on the Board means that its powers as described are predicated on the presence of effective shareholder scrutiny.
- 5 The best practice governance arrangements for government owned businesses being put in place for other public corporations will apply equally to BW. However, as guardian of a unique national asset with particular heritage, amenity and environmental value, BW has a wider breadth of responsibility than the duty of a typical limited company to its shareholder. This is dealt with in the Public Policy Objectives proposed in the 2004-2005 Policy Review of BW. Thus the Board has additional considerations not usually encompassed in a standard shareholder and company relationship. These additional responsibilities are taken into account by the Shareholder in decisions on Board composition and in terms of the broader range of matters the Board itself is required to take into account in its governance of its business.
- 6 As a public body, BW is required to meet standards of openness and accountability (e.g. Freedom of Information) applicable to other public bodies. In addition, as a body with significant commercial activities it will also meet standards of accepted best practice under the relevant provisions of Combined Code on Corporate Governance.

#### Key Principles

- The Shareholder sets Public Policy Objectives for the Company that meet the national interest and will include strategic financial performance targets. (All subsequent references to Public Policy Objectives should be taken to include relevant financial performance targets).
- The Board is the principal instrument of governance of the Company and, under the leadership of its Chairman, has collective responsibility for the performance of the duties placed upon it by the statutes in a manner that achieves the Public Policy Objectives of the Shareholder to whom it is accountable.
- The Board, working with the executive management, determines a Strategy to achieve those Public Policy Objectives.
- The Shareholder and the BW Board agree the Strategy and the measures by which the success of the Strategy in meeting the Public Policy Objectives is evaluated.

- The Board and the Shareholder periodically review progress of the Strategy in delivering the Public Policy Objectives.
- The Board approves a Corporate Plan for delivery of the Strategy that is prepared by the executive management. The Corporate Plan will include measures against which the Board will evaluate performance in delivery of the Strategy.
- The Board discusses the Corporate Plan with the Shareholder to enable effective measurement of progress in delivering the Strategy.

## The Board

- 7 The composition of the Board is a critical factor for the Shareholder and the Shareholder's power of appointment (and, in extremis, removal) is a key instrument of the Shareholder in the exercise of its influence. It will therefore be a key responsibility of the Shareholder to ensure, working with the Chairman of the Board, that the Board contains an appropriate combination of the necessary skills and experience for both the effective direction of a complex business and oversight of the public interest. To achieve this, the following will take place:
- 7.1 In accordance with the provisions of TA 1962 the Secretary of State will, in consultation with Scottish Ministers, appoint the Chairman. Scottish Ministers will, in consultation with the Secretary of State and the Chairman, will appoint 2 members of the BW Board. The Chairman will consult with Scottish Ministers periodically as to the most appropriate size and "shape" of the Board. During each year the Chairman will discuss with the Shareholder any impending changes to Board membership;
- 7.2 The appointments process will be in accordance with the code of practice for Ministerial Appointments to Public Bodies issued by OCPA although Scottish Ministers may adapt the process to meet the requirements of the equivalent Scottish Code as reflected in the guidance developed by the Scottish Executive. The process will also follow the recommendations of the Combined Code on Corporate Governance. To those ends the Chairman will use the Nominations Committee of the Board for providing advice to Ministers on Board appointments.
- 7.3 The Shareholder acknowledges its responsibility, when exercising its powers to determine the terms of appointment, of ensuring that Board members' remuneration is appropriate to incentivise applications from persons of calibre with the desired qualities, whilst adhering to the Scottish Executive's policy in relation to the remuneration of public body board members.
- 7.4 The Board will annually evaluate its own performance in accordance with the recommendations of the Combined Code on Corporate Governance. The outcome of the evaluation will be shared by the Chairman of the Board (and where appropriate the Board Nominations Committee) with the Shareholder.
- 7.5 The Board recognises that one of its key responsibilities is the setting of appropriate remuneration and incentives for the executive management team to ensure the Executive is properly incentivised to deliver the Corporate Plan. The Shareholder looks to the Board to develop an appropriate remuneration framework for the Company through the use of a Remuneration Committee which will set executive remuneration. The Board and its Remuneration Committee will follow best practice in accordance with the Combined Code on Corporate Governance.

## **Company Purpose & Public Policy Objectives**

- 8 The Shareholder recognises the need to clearly articulate its Public Policy Objectives for the Company. As part of that policy process it will also periodically (re) confirm the company's purpose within the context of the Public Policy Objectives the Shareholder may determine from time to time.
- 9 The primary purpose of the Company is to manage, maintain and develop its network of waterways and docks for the wider public benefit. The 2004/05 Policy Review of BW clarified these aims and will serve as the strategic objectives for the Company until they are revised.

## **Confirming Strategies & Agreeing the Corporate Plan**

- 10 The Shareholder recognises that it is the responsibility of the Board of the Company to approve an appropriate set of business strategies put forward by the Chief Executive ('the Strategy') that will deliver the Shareholder's Public Policy Objectives consistent with the Company's purpose as defined. The Strategy will be subject to in depth review and challenge by the non-executive Board prior to adoption.
- 11 A process will be defined under which the Strategy will be agreed with the Shareholder. All concerned will ensure that there is a common understanding of the agreed Strategy between the Shareholder, the Board and the Executive. As part of this, the Chairman and Chief Executive will explain to the Shareholder how the Strategy is aligned to delivering the Shareholder's Public Policy Objectives and any specific shareholding objectives it may have.
- 12 A rolling 3 Year Corporate Plan derived from the Strategy will be discussed annually with the Shareholder. The Corporate Plan will include appropriate milestones and metrics against which performance in delivering the Strategy can be measured. The longer term strategic plan will also be available to the Shareholder if required.

## **Performance Reporting**

- 13 The Shareholder will agree an appropriate process with the Board of the Company to review the progress of the Strategy in meeting the Public Policy Objectives of the Shareholder. The focus will be high level strategic milestones, reported to the Shareholder quarterly as agreed at the time of the Policy Review in 2004-05.

## **Funding Framework Monitoring**

- 14 To allow the Shareholder to focus on strategic issues, the measuring and monitoring of operational performance under the funding framework, which will be in the form of a policy priority letter, will be distinct and separate from consideration of the strategic milestones referred to above.
- 15 The funding framework will also provide for appropriate audit of operational performance that will enable officials to confirm the propriety of public funds disbursed.

## **Delegated Limits**

- 16 As an appendix to this document there shall be a schedule of general delegated limits. The Company and the Shareholder agree to keep the schedule under review and to ensure that it appropriately reflects the principles set out in this document.

## **Working Together**

- 17 The Company and the Shareholder agree that the interactions between them need to be underpinned by resolve on both sides to conduct business in a professional and efficient manner reflecting the following:
- open dialogue based on a shared commitment to meet the Public Policy Objectives that will provide the Company with the framework for success.
  - people with the relevant experience to be able to engage in informed dialogue relevant to creating value for the Company and its Shareholder with mutual commitments to deliver on time and to specification.
  - both parties ensuring a joined up approach amongst their constituent parts with single statements of requirements that avoid duplication and unnecessary analysis
- 18 The Company and the Shareholder agree that there will be different elements to the relationship between Shareholder and the Company and the primary contact points will vary as a result. This will reflect the three separate but related roles of the Scottish Executive:
- as Shareholder,
  - as purchaser of services under the Contract; and
  - as government sponsor of the Company.
- 20 The primary contact points will normally be as follows:
- Shareholder Meetings - Ministers and relevant advisers from the Scottish Executive and with the Company Chairman / Chief Executive and Scottish Director
  - Quarterly Operational Review Meetings - Scottish Executive officials with members of the Company Executive and their management teams
  - Sponsorship Matters (PQ's etc) - As appropriate to the matter in hand

## **Parliamentary & Other Accountabilities**

- 21 Notwithstanding the above governance principles and respective division of roles and responsibilities, the Shareholder and Company recognise the need to support and assist each other in their respective accountabilities; in particular to support:
- the need of Ministers to respond timely to Parliamentary and intra-governmental questions and requests for information;
  - the need for Ministers and / or officials to respond timely to other public enquiries;
  - the need for the Company to respond timely to issues arising under its accountability mechanisms, including the British Waterways Advisory Forum and the British Waterways Scotland Group; and
  - the need for Ministers to review, modify or change from time to time the Public Policy Objectives.

Signed: Robin Evans  
Chief Executive, British Waterways  
Date: 21 December 2006

## Annex C – Financial Information and Other Returns

### Timetable

The timetable below has been agreed for the sharing of information between BWS and the SG. The timetable and its content may be varied in the light of experience.

In general terms there are a number of issues which lend themselves to annual reporting, and feed into an annual cycle of discussions on planning (including further expenditure on assets) such as:

- Long term income profile, including changes in assumptions on venture income but also including other issues such as fees and charges
- Evolution of the network asset 'health' – to date and projected over the current Scottish Spending Review period, e.g. movement in the proportion of assets in each asset and condition category
- The deliverables by which the SG's requirements for the canal network are to be delivered
- Benchmarking reports (ad hoc or regular) on an agreed basis

End of January	Draft Business Plan for Scotland submitted to the SG for the year beginning 1 April. List of all projects over £500,000 (July – December) in accordance with Annex E
End of February	SG offer comments to BWS on draft Business Plan
First Week in March	Redraft Business Plan submitted to the SG and BW Board
Third week in March	BW Board sign off Business Plan including Scottish plan
End March	Final Scottish plan submitted to Scottish Ministers
During April	Final Version of the Scottish plan agreed
2nd Week of March	BWS submit phased budget (monthly profile of Grant-in-Aid drawdown) for the forthcoming year
31 May	Provisional final outturn figures for the preceding financial year, including Grant-in-Aid used for the current and capital expenditure. Annual return on de minimis disposals and those not subject to market conditions. Annual return on theft and fraud. Annual return on Scottish contingent liabilities. Annual return on compensation payments and losses. Annual return on gifts, awards and prizes. BW report to the SG on its Scottish land and property activity annually, with an independent valuation of its Scottish land and property provided every three years.
First week in June	Draft annual report and accounts submitted to the SG (including Scottish Accounts). SG to offer BW comments within 10 working days of receipt,
July	Final Annual Report and Accounts published.
July	List of all projects over £500,000 (January-June) in accordance with Annex E
September/October	Review of External management letter – meeting with external auditor
As and when	Changes to Board committee membership/Board pay to allow laying in the Scottish Parliament (see para 39.2).
3-yearly from 31 May 2009	Details of BW's current insurance policies and any changes (see para 28.3)

## Format for Losses and Fraud Reports

Compensation and losses payments made during the Financial Year summarised in the tables below

Amount	Vehicle		Personal Injuries		Other Property		Total	
	No.	£Value	No.	£Value	No.	£Value	No.	£Value
Under 10k								
£10k-20k								
Over £20k								
Total								

Notes should be provided as follows:

- Explanation of individual payments over £20,000
- Number of outstanding claims and their estimate total value
- Number and total value of uninsured commercial vehicles stolen and not recovered and any similar losses of equipment

## Fraud reports

The following information should be reported to the Sponsor Team as soon as fraud or any other irregularity is discovered or suspected:

- The amount, type and date
- How it occurred and how it was discovered
- Whether any amount can be recovered and what actions has been taken to do so
- Who was primarily responsible
- Whether prosecution is proposed and if not, why not; Whether the incident was caused by the neglect of a BW official and, if so, whether it is proposed to make the official bear part of the loss. Whether disciplinary action is proposed and, if not, the reasons why not
- The existing security or control arrangements and the steps necessary to prevent a recurrent of loss

Any additional matters which are relevant.

## Annex D – Schedule of Regular Meetings

Quarterly Progress Meetings	Incorporating formal documentation of <ul style="list-style-type: none"> <li>• Current Issues</li> <li>• Key risks</li> <li>• Financial update</li> <li>• Efficiency update</li> <li>• Outcomes and objectives update</li> <li>• One off initiatives e.g. Homecoming</li> <li>• Expectation of future approvals</li> </ul>
Bi -annually	High Level meetings between BW and SG Senior management
Annually	Annual meeting and Lowlands Customer Forum
Annually	Annual meeting and Highlands Customer Forum
Annually (or as appropriate with the agreement of SG)	Scottish Canals Development Group
Annually	Defra/SG/BW Property meeting

## **Annex E – Management of the non-operational estate for Scotland**

In managing its non-operational properties BW has the following broad options:

- retention of properties for investment purposes;
- outright sale to the private sector;
- development with private sector through profitable joint ventures or other collaborations;
- acquisition and improvement of land under BW's powers in the 1962 and 1968 Acts.

In choosing between these options BW should seek to obtain the best possible overall return within a reasonable timescale whilst minimising risk.

The following guidance should be observed:

### **Investment properties**

BW should establish criteria for deciding whether or not to retain properties in Scotland for investment purposes. These criteria should include prospects for future development, minimum net return and operational links and be based on Scottish circumstances rather than any criteria set for England and Wales. They should be regularly reviewed. The SG should be notified of these criteria timeously.

### **Disposal**

Where land and buildings are to be disposed of, the aim should be to secure an adequate rate of return in the context of an acceptable level of risk and with due regard to the economic, social and environmental impacts for the benefit of Scotland. For the appraisal of schemes involving the disposal of historic buildings, the maximisation of receipts should not be regarded as the overriding objective. Where appropriate, disposal should be with the benefit of planning permission to establish maximum development value. Property should be offered for sale in a manner which ensures full exposure to the market, unless there are specific reasons why a more restrictive approach is likely to achieve a better price or a better outcome for Scotland. Consideration should also be given to the inclusion of clawback provisions.

Prior agreement from the SG should be sought where:

- disposal is not subject to open market competition and, except in the case of *de minimis* disposals, a certificate from an independent valuer that disposal is at market value has not been obtained; or
- there are novel and contentious features because the disposal does not or may not comply with the requirements of regularity and propriety and good financial management.

### **De minimis disposals**

In Scotland all *de minimis* non operational disposals must be approved by the Director Scotland, who must be satisfied that each disposal has been fully exposed to the market, unless the sale is to a special purchaser and the Director Scotland certifies that the price exceeds the open market value. BWS may dispose of certain low value properties in the absence of an independent valuer's certificate, without reference to the SG, i.e. where the value of the property determined using the arrangements set out below should not exceed £100,000.

BWS will report at the end of the financial year on the number of *de minimis* disposals which have taken place in Scotland, giving total value of such disposals and percentage of all disposals in Scotland by number and value this represents. This report will also contain confirmation that the property involved was non-operational.

## **Joint ventures**

Before negotiating a joint venture or seeking SG approval to do so, BW should ensure that:

- the choice of development partner is subject to competition with normally at least 4 parties invited to submit details of proposals;
- the option of outright disposal is kept open to be considered alongside partnership bids and that, in any agreement, options for BW to sell or assign its interests are preserved;
- the nature and purposes of the partnership are consistent with BW's powers and Scottish objectives;
- all reasonable options have been considered, including doing nothing, and a full financial analysis has been undertaken with maximum practicable use of NPVs and with future streams of costs and incomes discounted at a rate agreed with the SG;
- a robust sensitivity and risk analysis has been undertaken and adequate safeguards for BW are available;
- guarantees are given of a minimum level of profit/revenue for BW; and
- BW gives no open-ended or unreasonable guarantees nor accepts any contingent liabilities.

## **Land acquisition and improvement**

BW requires the SG's consent for the acquisition or improvement of Scottish land under its statutory powers, except where:

- the value of the land to be acquired or BW investment for development does not exceed £3,000,000; or
- the acquisition is for the purpose of enhancing the value of a planned wider development which is expected to proceed as expeditiously as possible (within 5 years) and satisfies current SG policies.

BW should consult the SG at the earliest stage in the case of major development proposals where:

- the value of any BW investment, including the value of land with planning consent for the proposal, exceeds £3,000,000; or
- open market competition is not intended; or
- there are novel or contentious features because the proposed development does not or may not comply with the requirements of regularity, propriety and good financial management.

At the beginning of January and July each year BW shall submit to the SG a list of all development projects (land acquisition and/or improvement) involving expenditure above £500,000 (inclusive of fees) authorised within the previous six months.

BW should consider seeking independent professional advice, on both estates and legal aspects, for major or complex property transactions of all kinds.

## **Acquisition of securities**

BW requires the approval of the SG for the subscription to, or acquisition of, any securities of a corporate body, except where:

- subscription or acquisition is in connection with a joint venture arrangement for the purposes of trading or estate management related to BW's business;
- the value of any securities to be subscribed for or acquired does not exceed £250,000 for each corporate body;
- BW's interest in each corporate body does not exceed 49%;
- the risks and liabilities arising from cost sharing agreements etc and the degree of BW's control over the corporate body's activities are in proportion to BW's interest in the corporate body; and
- BW acquires no contingent liabilities.

BW should consult the SG at the earliest stage in the case of proposals to subscribe for or acquire securities in a corporate body which exceed the financial limits set in Annex F or otherwise have novel or contentious features because they do not or may not comply with the requirements of regularity and propriety and good financial management. BW should similarly consult the SG about any proposal to acquire an interest in an unincorporated body which exceed the financial limits applicable

to corporate bodies or otherwise has novel or contentious features because the proposed acquisition does not or may not comply with the requirements of regularity and propriety and good financial management.

## Annex F – Summary of Delegation Levels

The following table summarises the thresholds below which different types of expenditure can be approved by BW for Scottish assets and above which approval is to be sought from the SG.

Category	SG sponsor team approval	SG Finance approval
Operational and non-operational projects	£3m	£5m
Single tender	£10k	
Disposal not subject to market competition	£100k	
Subscription to or acquisition of securities	£250k	
Compensation payments & write-offs	£5k	£5m
Gifts	£300	

### Notes

1. The delegation is for the acquisition or improvement of operational and non-operational property where the process is subject to open competition. Where there is no market competition the proposal must be referred to the SG for approval.
2. Where the project is subject to variation of more than 20% of the approved budget, or the total value of the project goes over one of the delegation limits, it should be reappraised and resubmitted if necessary.
3. BW shall require the prior approval of the SG in all cases where it is proposed to let any contract estimated to cost £10,000 or more by single tender action or otherwise to depart from normal tendering arrangements.
4. Below the threshold of £10,000, any proposal to let a contract by single tender action or otherwise to depart from normal tendering arrangements shall require the prior approval of the Chief Executive, the Finance Director or another person with delegated authority in this respect.
5. All cases where contracts were let by single tender action or otherwise depart from normal tendering arrangements shall be reported to the BW Board at least every six months. In accordance with the guidance in the Land Acquisition and Improvement section of Annex E, such cases shall also be highlighted in BWS' annual return on new commitments above £500,000.

## **Annex G – Operational Project Expenditure**

### **Scope**

1. This annex concerns substantial outlay (other than under the Transport Act 1962, section 11) that may not be carried out by BW unless it acts along lines settled with the SG in accordance with the Transport Act 1962, section 27(2). A project for the purposes of this Annex is a commitment to a discrete item of expenditure or to a set of expenditures related in such a way that the benefits of any one of them cannot be fully realised independently of the others. A project may not be artificially divided in order to circumvent the requirement to obtain SG approval.

### **Costs**

2. The cost of a project is the total expenditure to which it would commit BW. Consultancies or reports from consultants which are directly and solely required as part of a project shall be included in the project cost. The estimated project cost shall be taken to include the value of any land with planning consent for the scheme which BW proposes to make available.

### **Contracts**

3. Contracts shall normally be let by competitive tendering – see guidance at paragraph 29.1 and Annex F.

### **Project appraisal**

4. In appraising projects, the SG looks to the BW Board to observe its duties of efficiency, economy and effectiveness in ensuring that projects receive the appropriate level of scrutiny, bearing in mind associated risks and any potential safeguards and guarantees. The BW internal project assessment process is set out in Annex I.

### **Referral to the Scottish Government**

5. Before entering into any commitment, for projects estimated to cost more than £3m BW shall submit an appraisal of the project to the SG - guidance on the process is at Annex H. Proposed projects estimated to cost more than £5m will in addition require Scottish Government Finance approval.
6. Projects which are part financed by third party funding, (e.g. Lottery, Scottish Enterprise, Local Government or EU funds) will not need SG approval unless BW's input of resources exceeds £3m.
7. Projects should be kept under regular review and specifically reviewed prior to key decision points, such as binding contracts, purchases of land to implement schemes and closing off major options, including put options.
8. If a project appears about to exceed its estimated costs when originally approved by 20% or more, it shall be reappraised and resubmitted to the SG; and shall be reappraised and referred to the SG if the increase brings the costs above the thresholds in paragraph 5 above.

### **Research**

9. BW should consult the SG about any significant changes in the direction of the research programme (Transport Act 1968, section 46).

### **Compliance monitoring**

10. In January and July each year BW shall submit to the SG a list of all projects involving expenditure above £500,000 (inclusive of fees) let within the previous six months. The list should indicate which, if any, of the projects was let by single tender action or where the lowest tender was not accepted. The SG will look to the relevant BW Board Committees (property and audit) for assurance that appropriate procedures are followed.

### **Post project evaluation**

11. BW should take stock of all projects on completion to ensure that systematic weaknesses can be corrected and best practice techniques disseminated at all levels of BW. It should report to the SG on any project for which the SG saw a full appraisal. Post project analysis should be carried out on projects where outturn is 25% greater or less than estimated expenditure, or for which the final value in rental or capital terms is 25% less than estimated.

### **Approval levels**

12. Subject to the above rules and the delegation levels contained in Annex F, and assuming proposed expenditure is consistent with resources available or likely to be available to BW, BW shall be free to approve projects without reference to the SG.

## Annex H – Appraisal of BW Projects

As outlined above, the SG is responsible for approving BW projects that are either above the Levels of Authority (see Annex F) or are ‘novel, contentious or repercussive’.

The SG is responsible for approval of BW projects in Scotland and Defra is responsible for projects in England and Wales.

Government approval is the final stage in the process and Government would expect projects to have undergone rigorous internal scrutiny and received BW Board approval prior to formal submission, as set out in Annex I. In exceptional cases this may be subject to final approval of specific documentation.

Dependent on the scale and complexity of the project Government may require early warning that approval will be required in order to ensure the process is smooth.

### Principles

There will be a single process for operational and non-operational projects within the SG’s responsibility. This process will also apply to any projects of mutual interest to the SG and Defra, with Defra officials involved throughout.

1. In all cases both parties (BW and the SG) will seek to ensure transparency and timeliness in its dealings. However the onus is on BW (subject to market time constraints and disciplines) to give the SG sufficient early warning of the transaction so the SG has enough time to appraise it properly.
2. For projects of mutual interest to the SG and Defra, this will normally be provided once the Property Director Approval Stage (as set out in Annex I) has been reached. For Scottish projects, it will normally be the practice for awareness of the potential project to have been raised by BWS from project conception with the sponsor team via quarterly reports/meetings, and with a presentation about the generalities to the SG (sponsor team, Finance, accountancy and property advisers) when the Property Director Approval Stage is drawing near.
3. Government’s assessment of a project needs to ensure that:
  - There is a business case demonstrating strategic fit and financial justification, showing a positive return in line with the investment strategy agreed with Government;
  - The project represents value for money;
  - The project is consistent with Government aims for BW;
  - Risks have been identified and are sufficiently managed; and
  - All practicable options have been appraised.
4. BW will ensure that projects comply with any other necessary requirements (e.g. State Aid compliance, ONS clearance, the Green Book, ‘Red Book’ valuation etc). Copies of documents or written assurances need to be given before approval.
5. Government should have access to BW’s advisers when necessary;
6. The information that BW submits to Government should demonstrate that each of these areas has been met.

## Process

BWS and the SG shall agree the process whereby BW projects shall be approved. Key to ensuring that the approval process is smooth and effective will be giving Government enough time to respond to BW proposals. It is important that the information given to Government is clear, covers the right issues and meets the criteria set out above. Government will then seek to ensure that the principles outlined above are observed while respecting the autonomy and commercial independence of BW management. Taking these factors into account and paragraph 2 in Principles above, the key steps in the approval process might include, for example:

1. BW gives Government early warning that a transaction is impending, giving an outline description of the project (size, rationale etc) and an indication of when approval will be required. This should be accompanied by a short paper outlining the proposal and attendant issues, bearing in mind the more detail given at this stage can help accelerate the overall process.
2. An initial meeting between BW and the Scottish and UK Governments (depending on the nature of the project) will discuss the issues and relate any views and concerns to BW. Following the meeting, Government will outline any preliminary concerns in writing to BW including the scale and scope of work required for the formal proposal.
3. BW continues to work up proposal to be submitted to Government. In concurrence, additional meetings between BW, their advisers and Government parties may be necessary – depending on the size, complexity and risks associated with the project.
4. No less than one month prior to the approval deadline, BW should submit its draft paper to Government demonstrating the robustness of the proposal (consistent with principles set out above) and also covering points raised by Government. This will need to bear in mind the 12 working days outlined below as the time required to approve any final submission. Where necessary Government can call for additional information.
5. The SG will review BW's paper. BW and Government meet to discuss final outstanding issues if necessary. BW will prepare the final proposal.
6. Final submission of project proposal. Government requires a minimum of 12 working days for consideration of applications and, where Ministerial consent is required, this could be longer although in all cases Government will expedite approval. Projects requiring approval should be submitted in hard copy in their final form. Electronic versions will exceptionally be accepted for less complicated projects where deadlines are very tight. Copies should be sent, where relevant, to the necessary individuals at the SG and the UK Government (Defra), the Department of Communities and Local Government, The Shareholder Executive and HM Treasury.  
  
**Note:** Depending on the nature and size of the project, steps 3-6 may be highly iterative and involve a number of discussions between Government and BW as well as development of BW's written proposal to Government. Alternatively, there may be no further meetings required after step 2.
7. Government will then come to a decision on whether or not to formally approve (with or without conditions) the proposals. The outcome of this will be communicated to BW.

## Annex I – Approval Process for Joint Ventures and Capital Investments

### British Waterways Approval Process for Joint Ventures and Capital Investments in excess of £100,000

#### 1. Introduction

This annex sets out the BW internal approval process for all joint ventures and capital investments in excess of £100,000.

Its objective is to ensure timely decision making, efficient use of resource, appropriate delegation and that decision makers are adequately informed on the issues appropriate to their legitimate concerns.

It is the responsibility of BW to ensure that there is an appropriate audit trail for its internal approval process.

#### 2. BW Authority Levels Limits

For Scotland all projects over £3m will be submitted to Scottish Government for approval in accordance with Annex H.

	<b>Capital investment projects</b>	<b>Joint ventures</b>
SG (including Finance)	projects above £3m	All new joint ventures/ companies.
BW Board	projects above £3m	All new joint ventures/ companies.
Chief Executive with concurrence from Finance Director	projects £1,500,001 to £3,000,000	
Property Director with concurrence from Head of Property and Finance Controller Property and Ventures	projects £100,001 to £1,500,000	Investment into joint ventures/ companies within approvals given by the BW Board

#### 3. Conformance with the BW investment Strategy

Conformance with the investment strategy is a key element of the capital investment approval process. The investment strategy is a BW policy document which directs the BW executive on the key attributes of its capital investment programme to meet BW's vision and portfolio development. It is updated annually and requires approval by BW Board as part of the business plan approval process. It will be provided to SG annually.

The main areas covered within the investment strategy are:

- Financial hurdle rates for the different categories of project type;
- Target levels of investment in the three/ four year plan between investment categories;
- Non financial benefits which are deemed most desirable;
- How to maximise BW's commercial advantage by linking to other BW activities, for example waterside expertise, public sector relationships, environment and heritage;
- Fit with the Business plan, for example with respect to BW's main areas of regeneration and marketing and leisure strategy;
- Risk;
- Sensitivities such as planning issues.

## 4. Approval Process

### a) Property Director

The Property Director will exercise his approval through a recommendation from the Commercial Investment Group (CIG).

Any project with a capital value in excess of £100,000 and all joint ventures are reviewed by this group for recommendation to the relevant delegated authority.

Any proposal submitted for CIG consideration should comply with this FM and will address:

- The nature of the project and background, usually including relevant maps, drawings and photos
- How the project meets the investment strategy
- The targeted outputs (financial and non-financial)
- The level of investment required, including any elements of risk in this
- Compliance with BW's relevant operating instructions
- In the case of joint ventures, the proposed debt financing plan, appropriate evidence of its achievability and terms
- Any key planning or external funding considerations
- Any key political, public relations, heritage, environment considerations
- Alternative options considered to structure the deal differently or to undertake an alternative project, including a do nothing option
- The likely timing for the various implementation milestones and targeted outputs
- Discounted cash flow projections to show the real IRR and net present value at the appropriate hurdle rate from the investment strategy. The commercial hurdle rates set out in the investment strategy (ranging from 6% to 12% real) and the sensitivity analysis serve to provide the appropriate financial rigour required by the Treasury Green Book. These measures seek to reflect the risk of a project and obviate the need for the use of Optimism Bias.
- Identification of the major assumptions in the financial appraisal
- Sensitivity analysis showing both upside and downside scenarios on the major assumptions
- Appropriate advice or external valuations to support the major assumptions. Typically investment property acquisitions will be supported by external valuations. Larger acquisitions (over £1.5m) are usually supported by a second valuation from BW's property valuers to ensure the purchase price can be supported on the balance sheet. Development property acquisitions will be supported by valuations where appropriate or development appraisals
- The major risks to achieving the projected financial and non-financial outcomes and to the BW portfolio
- If the project is a joint venture proposal then the project submission will also set out the proposed partner (how selected and their capabilities); advantages and disadvantages of venturing; and the proposed level of gearing.

Submissions to the CIG will be at least three working days prior to the CIG meeting. The contents of the project submission to CIG must meet the BW relevant elements of the Green Book.

CIG may call for any other supporting material that it deems appropriate

On the basis of the submission the CIG will either accept the proposal, reject the proposal or seek further amendments to be made.

For approved projects, any amendments to the submissions made to CIG, additional material considered, minutes of the key issues raised and considered, or any conditionality for the approval, will form part of the "CIG approval papers" available for any further consideration in any subsequent layers of the approval process, or any post-project appraisal, if required.

## **b) Chief Executive**

The Chief Executive will exercise his approval through a recommendation from the executive directors, including the concurrent approval of the Finance Director. The BW executive directors meet fortnightly. The papers submitted to the CEO will be either the "Property Director approval papers" or a summary of these, particularly if the project will require onward approval by the BW Board. In the latter case, the CEO can call for the "Property Director approval papers". The papers will be submitted to the CEO and executive directors at least three working days prior to their meeting.

In addition to providing another layer of approval, the CEO will consider any further input from the executive directors, for these larger projects that the rationale for acquisition is sufficiently supportive of BW's vision, and that there is strong business area integration.

On the basis of the submission the CEO will either accept the proposal, reject the proposal or seek further amendments to be made.

For approved projects, any amendments to the submissions made to CEO, additional material considered, minutes of the key issues raised and considered, or any conditionality for the approval, will form part of the "CEO approval papers" available for any further consideration in any subsequent layers of the approval process, or any post-project appraisal, if required.

## **c) BW Board**

The BW Board will exercise its approval at a BW Board meeting, at which, at least two members of the property committee must be present. The BW Board meets approximately every two months.

The submission to the Board will be a summary of the "CEO approval papers" focusing in particular on the most pertinent issues for the BW Board:

- Rationale for the investment
- Strategic fit with the business plan, investment plan and regeneration plans
- Identification and management of risks, drawing up of a risk strategy, assessment of the impact on portfolio risk, including affordability
- Financial inputs and outcomes including project risk and sensitivity range
- Public relations and political implications

Papers will be submitted to the BW Board five working days prior to the Board meeting. On the basis of the submission the Board will either accept the proposal, reject the proposal or seek further amendments to be made.

For approved projects, any amendments to the submissions made to the Board, additional material considered, minutes of the key issues raised and considered, or any conditionality for the approval, will form part of the "Board approval papers" available for any further consideration in any subsequent layers of the approval process, or any post-project appraisal, if required.

## **d) Scottish Government**

Projects for approval by the SG will be submitted by BWS to the SG. BWS will initially provide the "Board approval papers". The SG may call for the "CEO approval papers" and/or the "CIG approval papers".

For projects of mutual interest to the SG and Defra, the BW Property Director will be the lead BW executive for co-ordinating this process. He will ensure that the SG is advised of the likelihood of a project submission as soon as it has passed the Property Director approval stage. SG may call for the "CIG approval papers" in order to accelerate understanding, identify any particular issues at an early stage, and thus facilitate the process to ensure adherence to the overall timescales.

For projects not of mutual interest, BW Director Scotland will undertake the functions described above for the Property Director.

## 5. Conditional and/or “in principle” approvals

All layers of this process may offer, if asked, “conditional” or “in principle” approvals, i.e. approvals subject to certain specified conditions, or approvals to the principle of a project subject to consideration of further specified details. The objective in seeking and granting these types of approvals can greatly assist in the timely progression of any project, in particular where negotiations are needed with third parties, and assurances are needed at stages in such negotiations. When such “conditional” approvals are granted, they will be on the basis that lower layers in the approvals process confirm to the approval grantor that these conditions have been met. Where in principle approvals are granted, it will be on the basis that the grantor has a further opportunity to consider the specified details.

## 6. Post Project Appraisals

### PPA process and approval by project type

All projects require a Post Project Appraisal (PPA) to be completed.

All full PPAs (long form) will be signed off at the most senior BW executive level of approval, as well as by the project sponsor.

Project Type	PPA text box on SAP (short form)	Full PPA (Long form)	Executive Director & Financial Controller	CEO & Finance Director
Major Works (including restoration & regeneration projects) Non Routine expenditure (GWP and small scale regeneration projects in excess of £20K, one off marketing projects regeneration etc). Operational craft, plant and equipment.	This is a minimum requirement for all projects with a planned cost of less than £100k	Required for all projects with a planned cost <b>more than £100k</b> . Additionally required for a project for <b>less than £100k</b> where the project over spent or did not achieve the anticipated output. (e.g. less output was achieved for the money spent)	Over £250k	Over £500k
Property disposals	This is a minimum requirement for all projects with planned sale proceeds of less than £250k or exempted from long form PPA	Required for all projects with planned proceeds of <b>more than £250k</b> . However only a short form PPA will be required for projects where achieved proceeds were <b>within 5% of planned value</b> and disposal costs were <b>within 10% of planned expenditure</b>	Over £500k	Over £1m
Commercial expenditure (Property & Income generating projects)	This is a minimum requirement for all projects with an initial budget of less than £100k or exempted from long form PPA	Required for all projects with an initial budget <b>more than £100k</b> However only a short form PPA will be required for projects if project/acquisition completed <b>within 5% of planned costs and planned IRR achieved</b>	Over £250k	Over £500k
Joint Ventures	Not applicable	All joint ventures	All joint ventures	All joint ventures

## **Annex J - Letter between SG and Defra (17 March 2008)**

Sarah Nason  
Department for Environment, Food & Rural Affairs  
EAW Division  
Zone 2D  
Ergon House  
Horseferry Road  
LONDON  
SW1P 2AL

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17 March 2008

Dear Sarah

### **BRITISH WATERWAYS: PROPOSALS TO INCREASE COMMERCIAL CAPITAL INVESTMENT IN SCOTLAND AND FOR A REVISED SCOTTISH SHARE OF BW CENTRAL COSTS**

We met on 21 February with colleagues from BW, BW Scotland (BWS) and Shareholder Executive to discuss a package of proposed measures to:-

- implement an outstanding BW commitment to invest an additional £12-15m of commercial capital in Scottish projects, in order to generate for BWS additional income of at least £1m per annum;
- in the context of transparent, ring-fenced funding and financial accountability for BWS, establish an appropriate process for approval of capital investment and disposal transactions; and
- review the Service Level Agreement levels paid by BWS to BW for central services.

The background to these proposals was set out in my letter to you of 15 February and Philip Ridal's paper of 20 February. These formed the basis of our helpful discussion on 21 February.

#### **Capital Employed in BWS**

BW have proposed to implement their capital investment commitment to us as follows.

First, the draft BWS business plan for 2008-11 identifies opportunities to invest in property and property development joint ventures (JVs) in Scotland. These investments, which require additional capital of between £2m and £5m over the business plan period, would be funded by a combination of cash from planned property disposals and draw-down from a new capital fund for BWS. The income from the £2-5m of capital to be invested directly in Scottish properties/JVs would be derived directly from those investments and would be accounted for separately within BWS. A separate BWS commercial capital bank account would be opened for the purpose of collecting Scottish receipts. These funds would be available for direct reinvestment in Scottish projects.

Secondly, BW have proposed that all other existing and planned BW JVs (ie excluding those identified in the draft BWS business plan for 2008-11) would form a national (i.e. GB) common good "pot" of investments. On the assumption that £2m-£5m of capital would be utilised by BWS to invest in property and property development JVs in Scotland, there would remain an outstanding amount of £10m due to BWS under the BW commitment: BW propose that a share of the "common good" pot of JVs could be purchased by BWS to provide an income yield.

These two measures would generate the required additional income to implement the commitment.

BW have proposed that the BWS investment in the GB JV pot should be regarded as a notional stake of £10m, rather than an "equity" share, and that a fixed "bond-like" return is earned on the stake. This notional investment would not be tied to any specific JVs or investments and BWS would receive the fixed yield regardless of the actual yield from the pot in a given year. To reflect the lower risk inherent in a fixed non-performance related return, BW have proposed that the investment yield should be set at a relatively low rate. The fixed rate discussed when we met was between 6% and 8%. Our Ministers take the view that a rate of 8% would be required, alongside the Scottish capital investment fund, to deliver the BW commitment. Subject to that, our Ministers are content to see delivery of the BW commitment on this basis.

BW have proposed the following process for Government approval of capital investments:-

- a. Investment in Scottish property and Scottish JVs operating wholly in Scotland from within the BWS-identified capital funds would be matters for the Scottish Government to approve, without the need for Defra concurrence.
- b. Where JVs in the national (i.e. GB) "pot" proposed to carry out projects in Scotland, the approval of the Scottish Government, with UK Government concurrence, would be required.
- c. Other JVs in the national (i.e. GB) "pot" would require the approval of Defra, without the need for Scottish Government concurrence.

These proposed approval arrangements appear to us to be consistent with the relevant legislation. Subject to that, and bearing in mind the approval role of the BW Board, our Ministers are content for the approval process to be developed on this basis.

When we met, it was also proposed that the JV arrangements should be reviewed after 3 years. I can confirm that our Ministers are content to proceed on that basis, although we would expect the outcome of the review to permit further capital investment in Scotland in the following period, bearing in mind the longer timescale covered by the original BW commitment.

### **Central Costs Allocation**

We also discussed the Service Level Agreement (SLA) charge to be paid by BWS to BW for central services for the period covered by the 2008-11 business plan.

This charge was established at the time of Devolution to represent the value to BWS of services received from BW central functions. The intention was to establish a single annual charge, given the services being provided to BWS: it was fixed in 2001 at £0.3m per annum and has remained at that level since, with scrutiny during the 2005 quinquennial review.

As explained in Philip's paper, BW has identified two elements: central services costs - comprising IT, shared financial and administrative services, HR, legal services, and marketing and customer services - and HQ costs. No charge has been levied from BWS for HQ costs to date on the basis that HQ resources carry out a stewardship role on behalf of BW and the costs are therefore rightly borne by BW. This understanding was reflected in the fact that Defra's predecessor – as sponsor department for BW including BWS prior to devolution - retained the PES cover for all BW HQ costs. I was grateful for your recognition at our meeting on 21 February that Defra should therefore continue to bear BW HQ costs in their entirety.

As regards central services costs, Philip's paper concluded that the original charge set did not fully reflect current assessed costs of approximately £1.49m. However, the wayleave income from the Easynet fibre optic cable laid under the Scottish canal network, currently £0.9m, has hitherto been remitted directly to the centre rather than being attributed to BWS. Going forward, we agreed that the Easynet income will be attributed to BWS. This means that we are effectively agreeing to increase payment from BWS to BW by £0.29m from 2008-09. To ensure transparency the SLA and the Easynet income due to Scotland should be identified separately in the accounts.

I can confirm that our Ministers are prepared to agree to this increase, on the basis (a) that the proposed net increase of £0.29m would be an absolute maximum: it would be subject to reduction as efficiency savings are achieved by BW in the business plan period; (b) that BW central service costs are carefully controlled; and (c) that the increased contribution to BW is met by BWS from its existing Scottish Government grant.

I very much hope that we can now agree to the implementation of this package of measures, which – taken together – our Ministers see as being the minimum required to deliver BW's commitment.

I am copying this to Philip Ridal and Robin Evans at BW, Steve Dunlop at BWS and Peter Shortt at Shareholder Executive, and to colleagues here.

Yours sincerely

ALASTAIR WILSON  
Deputy Director - Aviation, Ports & Mobility

## **Annex K – Letter between SG and Defra (15 April 2008)**

Alastair Wilson  
Deputy Director  
Aviation, Ports & Mobility Division  
Transport Directorate  
The Scottish Government  
Victoria Quay  
Edinburgh  
EH6 6QQ

15 April 2008

### **BRITISH WATERWAYS – PROPOSAL TO INCREASE COMMERCIAL CAPITAL IN SCOTLAND**

Thank you for your letter of 17 March about the proposed package of measures that include how to implement BW's commitment to invest an additional £12-15 million of commercial capital in Scottish projects in order to generate for BWS additional income of at least £1m per annum (the "Greener commitment" as outlined in Robin Evan's letter of 3 September 2004).

You will appreciate, I hope, that Defra does not seem to have been party to this agreement and commitments to particular BW resource investments in Scotland clearly have implications for England and Wales. This is of particular concern at times of uncertainty and high risk for BW's commercial business, such as we are experiencing at present.

In the spirit of co-operation and in recognition that BW is a British organisation, we can accept all the proposals subject to the three year review and to one point which I detail below. We would also like to agree that we can revisit the arrangements should we reach any further conclusions on overall accountability (which we are currently trying to bottom out) that would suggest the agreement is flawed.

We can agree the proposal that you have a fixed notional stake of £10 million with a fixed return which seems necessary for the Greener commitment to be delivered. I appreciate the 8% figure proposed is designed to meet that commitment, but we have real difficulties with this figure in the current climate and any agreement must be realistic and reasonable today.

We think that the yield should be based on an assessment of a reasonable risk premium over the current risk free rate offered to the market. The current yield on Treasury 10 year gilts is 4.42% setting the effective risk free rate. Anything over this should reflect risk premium and, given the BW investment is not entirely risk free, some premium is justified. Most private sector firms with strong credit ratings offering low risk debt to market would offer bonds at 2-3% above this point. By way of comparison with commercial money market lending rates, the current LIBOR is c.5.5% which reflects the current lending difficulties between the main UK banks. Finally, we bear in mind that the public sector cost of capital is 3.5% unadjusted for risk. Looking at these points altogether, we feel that anything over 6.5% would be excessive.

Nevertheless, in the interests of reaching agreement, I am prepared to go to 7% to get this arrangement settled so BW can get on with finalising their Corporate Plan. I hope you will appreciate our reasoning and acknowledge Defra's position in this has been more than reasonable, bearing in mind the Greener commitment was not agreed by us and our decision to accept that you should not contribute to HQ costs was based on the PES transfer arrangements of some time ago which seem not to have been as explicit as we would have wished.

I hope we can now agree on this basis.  
I am copying to recipients of your letter.

Yours as ever,

Sarah Nason  
Head of Environment Agency and Waterways

## **Annex K – Letter between SG and Defra (22 April 2008)**

Sarah Nason  
Department for Environment, Food & Rural Affairs  
Head of Environment Agency and Waterways Division  
Zone 2D  
Ergon House  
Horseferry Road  
LONDON  
SW1P 2AL

—  
22 April 2008

Dear Sarah

### **BRITISH WATERWAYS: PROPOSALS TO INCREASE COMMERCIAL CAPITAL INVESTMENT IN SCOTLAND AND FOR A REVISED SCOTTISH SHARE OF BW CENTRAL COSTS**

Thank you for your letter of 15 April in response to mine of 17 March (attached for ease of reference) setting out a package of proposed measures to:-

- implement an outstanding BW commitment to invest an additional £12-15m of commercial capital in Scottish projects, in order to generate for BW Scotland (BWS) additional income of at least £1m per annum;
- in the context of transparent, ring-fenced funding and financial accountability for BWS, establish an appropriate process for approval of capital investment and disposal transactions; and
- review the Service Level Agreement levels paid by BWS to BW for central services.

You have very helpfully indicated that you can accept all of these proposals (as set out in my letter of 17 March), subject to the 3-year review and to the fixed income yield on the BWS investment in the GB joint venture pot being set at 7%, rather than 8%.

I can confirm that we are content with the 3-year review and to agree a fixed return of 7%.

We are most grateful to you and to BW for the constructive and co-operative way in which you have approached this package of measures. We can now proceed to the implementation of the whole package on this basis and I hope that this will allow BW to finalise their Corporate Plan.

I am copying this letter, as before, to Philip Ridal and Robin Evans at BW, Steve Dunlop at BWS and Peter Shortt at Shareholder Executive, and to colleagues here.

Yours sincerely

ALASTAIR WILSON  
Deputy Director - Aviation, Ports, Freight and Canals