

Agenda – Public Accounts Committee

Meeting Venue:	For further information contact:
Committee Room 3 – Senedd	Fay Bowen
Meeting date: Monday, 22 May 2017	Committee Clerk
Meeting time: 13.45	0300 200 6565
	SeneddPAC@assembly.wales

(Private pre-meeting 13.45 – 14.00)

1 Introductions, apologies, substitutions and declarations of interest

(14.00)

2 Paper(s) to note

(14.05)

(Pages 1 – 3)

Reforming local government: Resilient and renewed – Letter from the Cabinet Secretary for Finance and Local Government (10 May 2017)

(Pages 4 – 5)

3 Natural Resources Wales: Annual Report and Accounts 2015–16: Evidence Session 2

(14.05 – 14.50)

(Pages 6 – 128)

Research Briefing

PAC(5)–15–17 Paper 1 – Natural Resources Wales Annual Accounts 2015–16

PAC(5)–15–17 Paper 2 – Auditor General for Wales’ Memorandum

David Sulman – Executive Director, UK Forest Products Association

4 Motion under Standing Order 17.42 to resolve to exclude the public from the meeting for the following business:

(14.50)



Cynulliad
Cenedlaethol
Cymru

National
Assembly for
Wales

Items 5 & 7

**5 Natural Resources Wales: Annual Report and Accounts 2015–16 –
Consideration of evidence received**

(14.50 – 15.05)

(Break 15.05 – 15.15)

(Public)

6 Natural Resources Wales: Evidence Session 3

(15.15 – 16.45)

(Pages 129 – 248)

Research Briefing

PAC(5)–15–17 Paper 3 – Auditor General for Wales’ Report: The Development of
Natural Resources Wales

PAC(5)–15–17 Paper 4 – Additional information from Natural Resources Wales (10
April 2017)

PAC(5)–15–17 Paper 5 – Natural Resources Wales – Internal Audit Report: Long
Term Timber Sales Contracts (May 2017)

Dr Emyr Roberts, Chief Executive

Kevin Ingram, Executive Director of Finance and Corporate Services

(Private)

7 Natural Resources Wales: Consideration of evidence received

(16.45 – 17.00)

Concise Minutes – Public Accounts Committee

Meeting Venue:

Committee Room 3 – Senedd

Meeting date: Monday, 15 May 2017

Meeting time: 14.00 – 15.38

This meeting can be viewed

on [Senedd TV](#) at:

<http://senedd.tv/en/4108>

Attendance

Category	Names
Assembly Members:	Nick Ramsay AM (Chair) Mohammad Asghar (Oscar) AM Neil Hamilton AM Mike Hedges AM Neil McEvoy AM Rhianon Passmore AM Lee Waters AM
Witnesses:	Steve Davies, Welsh Government Owen Evans, Welsh Government
Wales Audit Office:	Huw Vaughan Thomas – Auditor General for Wales Gareth Jones Matthew Mortlock
Committee Staff:	Meriel Singleton (Second Clerk) Claire Griffiths (Deputy Clerk) Katie Wyatt (Legal Adviser)



Transcript

[View the meeting transcript \(PDF 999KB\)](#) [View as HTML \(999KB\)](#)

1 Introductions, apologies, substitutions and declarations of interest

- 1.1 The Chair welcome the Members to the Committee.
- 1.2 There were no apologies.
- 1.3 Mike Hedges AM declared an interest as being a Governor of two primary schools and Neil McEvoy AM declared an interest as being a former teacher.

2 Paper(s) to note

- 2.1 The papers were noted.

3 Regional Education Consortia: Evidence Session 3

3.1 Members scrutinised Owen Evans, Deputy Permanent Secretary, Education & Public Services Group, and Steve Davies, Director of Education, Welsh Government as part of the inquiry into Regional Education Consortia.

3.2 Owen Evans agreed to provide the following information:

- Data from regions which indicates the extent to which school-to-school working is happening
- Data showing the percentage of improvement in the key GCSE subjects following the School Challenge Cymru programme
- Send a note regarding the use of Moodle
- Send headlines from the recent visit undertaken to Finland.

4 Motion under Standing Order 17.42 to resolve to exclude the public from the meeting for the following business:

- 4.1 The motion was agreed.

5 Regional Education Consortia: Consideration of evidence received

5.1 Members considered the evidence received.

5.2 The Chair agreed to write to the Welsh Government with areas of questioning the Members wish to explore further.

5.3 Members agreed that on consideration of the response from the Welsh Government, Committee's concerns should be sent to the Chair of the Children, Young People and Education Committee.

Agenda Item 2.1

Mark Drakeford AM/AC

Ysgrifennydd y Cabinet dros Gyllid a Llywodraeth Leol
Cabinet Secretary for Finance and Local Government



Llywodraeth Cymru
Welsh Government

Ein cyf/Our ref: MA-L-MD-0329-17

Nick Ramsay AM
Chair, Public Accounts Committee
National Assembly for Wales
Cardiff Bay
Cardiff
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SeneddPAC@assembly.wales

10 May 2017

Dear Nick

Thank you for your letter of 10 April, in which you set out the Public Accounts Committee's comments on the recent White Paper 'Reforming Local Government: Resilient and Renewed'.

I am grateful for the useful observations made by the Committee and will reflect on them alongside the wide range of other responses received to the consultation. I intend to publish a summary of the responses and to make a statement on the way forward in due course.

I note the Committee broadly welcomes the introduction of a 'General Power of Competence' for principal local authorities and the opportunity this will provide for innovative approaches to meeting the needs and aspirations of their communities.

I note the Committee welcomes the review of community and town councils, which I am establishing. I agree that the financial and governance issues which have been identified by the Auditor General for Wales should be part of the review's considerations. The Auditor General's reports will be an important part of the evidence base available to the review.

I appreciate why the Committee considers the General Power of Competence should not be available to community and town councils until the review has been undertaken and its recommendations implemented. However, under our proposals, the power will only be available to those councils which satisfy certain conditions, including being able to demonstrate that the two most recent Auditor General for Wales' opinions on the council's accounts have been unqualified.

Bae Caerdydd • Cardiff Bay
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Rydym yn croesawu derbyn gohebiaeth yn Gymraeg. Byddwn yn ateb gohebiaeth a dderbynnir yn Gymraeg yn Gymraeg ac ni fydd gohebu yn Gymraeg yn arwain at oedi.

We welcome receiving correspondence in Welsh. Any correspondence received in Welsh will be answered in Welsh and corresponding in Welsh will not lead to a delay in responding.

The preferred approach for regional working set out in the White Paper is for certain functions, for example, transport planning and strategic land-use planning to be undertaken on an economic development footprint. For other functions, such as public protection, local authorities would have flexibility to determine the collaborative footprints within a statutory framework prescribed in legislation, with the intention of removing overlap and promoting simplicity as far as possible. This will enable authorities to come together to put in place arrangements that best suit local circumstances. Where appropriate, they will be able to build on existing arrangements, such as the regional educational consortia to which you refer.

I agree the importance of having a clear and consistent approach to the governance, accountability and funding of regional arrangements. Again, I intend to provide a statutory framework for this within the proposed Bill. As indicated in the White Paper, my officials will be working closely with the Welsh Local Government Association and the Society of Local Authority Chief Executives to develop an appropriate governance framework, drawing on their knowledge and experience of existing arrangements.

Our proposals represent an evolution of existing arrangements, but one which puts them on a clear, consistent basis. I will be considering carefully what all stakeholders have to say about the proposals.

Our wider reform proposals recognise the importance of local councillors as leaders and advocates for their communities. They will have an important role in holding to account those responsible for decisions and the delivery of services and in supporting constituents when things go wrong. As I have said previously, the 22 existing local authorities will remain the means through which citizens access services and the democratic bodies to which they will continue to direct any concerns.

Like you, I am copying this letter to John Griffiths AM, Chair of the Equality, Local Government and Communities Committee.

Yours sincerely



Mark Drakeford AM/AC

Ysgrifennydd y Cabinet dros Gyllid a Llywodraeth Leol
Cabinet Secretary for Finance and Local Government

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Agenda Item 3

By virtue of paragraph(s) vi of Standing Order 17.42

Document is Restricted



**Cyfoeth
Naturiol**
Cymru
**Natural
Resources**
Wales

Annual Report & Accounts 2015/16



Noddir gan
Lywodraeth Cymru
Sponsored by
Welsh Government

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Welcome

It gives me great pleasure to introduce Natural Resources Wales' Annual Report for 2015/16. This is the first Annual Report since I was appointed in December 2015. I am delighted to have the opportunity to Chair the Board of this unique, dynamic organisation. We are proud to lead the way to a better future for Wales by managing the environment and natural resources sustainably and to reaffirm this, our vision. The progress made by NRW, as a young organisation, gives me and the Board great confidence in our ambitious environmental agenda for the future.

Many of the things we rely on to prosper as people and as a nation are borne from our environment and the natural resources around us: the water we drink, the air we breathe, the natural surroundings where we live and work. A healthy and resilient environment helps sustain people and our economy, helping build a solid foundation on which our society can thrive. This report sets out how our work in 2015/16 has contributed to achieving a more successful, prosperous Wales, based on healthy natural resources.

We are committed to building on this work for a stronger more resilient future, even with all its uncertainties. The Environment (Wales) Act and the Well-being of Future Generations (Wales) Act together provide the framework for all of us to collectively use our resources for the best possible outcomes. Using this new legislation to work together with partners from the public, private, community and voluntary sectors gives us an exciting opportunity to make sure that the people of Wales benefit now, and in the future, from a more resilient, sustainable and prosperous environment.

Formally and sincerely I want to thank all those people who have worked so tirelessly over the past year to deliver the significant achievements in this report. My predecessor Professor Peter Matthews CBE, with his unstinting energy and commitment to the establishment of our organisation, made an amazing contribution to Wales of which he should be proud. In addition the original Board members whose term of office came to an end during the year: Professor Lynda Warren, Harry Legge-Bourke and Rev Hywel Davies. Our Chief Executive Dr Emyr Roberts deserves special thanks for charting a clear way through the many challenges the organisation has faced during the year. And, of course each and every one of our dedicated staff who are indeed our greatest resource and who bring their professional expertise and determination to play in their vital role in championing the environment. This report gives an indication of the huge amount of progress made over the past year, demonstrating the strength, innovation and passion of all the people who have worked so hard to get us this far along our journey.

In the coming year, along with my Board colleagues, I look forward to working with the Chief Executive, his Executive Team and all of our staff, leading the way to a better future for Wales by managing the environment and natural resources sustainably – effectively and enthusiastically delivering our vision.

Diane McCrea MBE
Chair



Performance Report

Overview

Last year, I described our position as challenging yet successful, and this has also been the position for 2015/16. Against a backdrop of reduced funding and staff numbers, we continued our journey to integrate the work of the three legacy organisations, and to manage Wales' natural resources sustainably. We have delivered a credible performance, which has helped to establish NRW as an organisation that delivers for the environment, economy and people of Wales. Such achievement over the last 12 months gives us confidence that we can deliver our ambitions for the future.

Challenges have come in the form of preparing for our new duties under the Well-being of Future Generations (Wales) Act and for our new purpose under the Environment (Wales) Act; as well as serious financial pressures which have required us to be clear about priorities and the way we use our money. In terms of environmental outcomes, overall water quality has not reached the good ecological status we would have liked to have seen by this point, while biodiversity remains fragile in many areas.

Our successes include the excellent work to secure a significant amount of carbon is locked in Welsh peatland, cleaner bathing waters and our efforts to reduce the spread of *P. Ramorum* across our forests. We have learned a great deal about the needs of local communities from our 'area trials', our customer service as measured by timeliness in response to planning applications continues to improve, we responded well to the winter weather, and we met our targets for marketing of timber. We are publishing more of our data online, such as information on river levels, which is helping our stakeholders to make decisions. I was also pleased to receive formal Ministerial Approval that we had completed our probationary period as a new Welsh Government Sponsored Body.

As ever, there is much more to do and areas to improve. We are keen to learn and listen to the feedback from our staff and customers. Hopefully this Annual Report will give you a flavour of the journey we are on.

Dr Emyr Roberts
Chief Executive and Accounting Officer



Introduction

We are a Welsh Government Sponsored Body, responsible for making sure that the *environment and natural resources of Wales are sustainably maintained, sustainably enhanced and sustainably used, now and in the future*. Wales is the first country in the world to create one organisation that brings together many of the tools needed to help manage our natural resources coherently. We can achieve much more by joining up our knowledge and services so they are working together to deliver sustainable outcomes. Our success depends on how we work together, living our values to create a better Wales.

Whilst our environment is worth £8 billion to the Welsh economy, we believe there is the potential to unlock much more for the people, communities and environment in Wales. We have the ability to adapt to the changing needs of society quickly – providing better services, making more informed decisions, and forming strong partnerships.

Our themes are integrated, demonstrating the multiple benefits our work has on the Welsh environment, economy and communities. They also support the following outcomes we share with the Welsh Government.

- Enhancing our environment
- Protecting people
- Supporting enterprise and jobs
- Improving the nation's health
- Viable and vibrant places
- Delivering social justice
- Supporting skills and knowledge

We have a wide range of roles and responsibilities:

- Adviser: principal adviser to Welsh Government, and adviser to industry and the wider public and voluntary sector, and communicator about issues relating to the environment and its natural resources
- Regulator: protecting people and the environment including marine, forest and waste industries, and prosecuting those who breach the regulations that we are responsible for
- Designator: for Sites of Special Scientific Interest – areas of particular value for their wildlife or geology, Areas of Outstanding Natural Beauty, and National Parks, as well as declaring National Nature Reserves
- Responder: to some 9,000 reported environmental incidents a year as a Category 1 emergency responder
- Statutory consultee: to some 9,000 planning applications a year
- Manager/Operator: managing seven per cent of Wales' land area including woodlands, National Nature Reserves, water and flood defences, and operating our visitor centres, recreation facilities and a laboratory
- Partner, Educator and Enabler: key collaborator with the public, private and voluntary sectors, providing grant aid, and helping a wide range of people use the environment as a learning resource; acting as a catalyst for others' work
- Evidence gatherer: monitoring our environment, commissioning and undertaking research, developing our knowledge, and being a public records body
- Employer: of over 1,900 staff, as well as supporting other employment through contract work and volunteering opportunities.

Our values:

- Passionate and ambitious about our work and the positive impact we will have
- Disciplined and focussed in our prioritisation and delivery
- Trusted and professional in our relationships with stakeholders, staff, and their representatives
- Taking a common sense approach to our work and being responsible and accountable for our actions.

Performance summary

We are still a young organisation but with a clear purpose and a determination to succeed. Moving into our third year, and the second year of our current Corporate Plan, our ambition was clear, but in common with other public sector organisations, we faced ongoing financial challenges and the need to prioritise our resources and find new and innovative ways of delivering services as efficiently as possible.

Our focus in our first two years has been to build the foundations of our standalone capability and preparing our organisation to fully deliver the sustainable management of our natural resources in Wales – over the last year we started to move into our transformation phase to ‘unlock our potential’ and become a high performing organisation.

We have continued to review our services to secure the environmental outcomes we want to achieve, and have worked to ensure that efficiency and improved customer care are delivered together. Our focus has been to develop natural resource management, improve our range of services to customers and partners, and support Welsh Government in developing new legislation and policy to progress green growth, tackle poverty, use resources efficiently and enhance resilience and diversity.

Looking ahead, the next year will be a year of enormous change and challenge for us, as it will be for our environment and for other public bodies in Wales – and we are ready to rise to that challenge. Both the legislative and the financial context we are working in mean that we will need to be transformational – prioritising effort where we can make the greatest contribution, forging new relationships with partners and communities, and addressing the fundamental issues that will increase the resilience of our natural systems and so enhance the services they provide to society.

We are, and will be, seeing significant changes in the environment of Wales – in terms of climate change, population and the economy, as well as public finances and new legislation. All of these factors will have a major impact on our organisation and there will need to be a huge shift in the way we work in future. We want to be bold and ambitious – both about how we in Wales achieve the sustainable management of our natural resources, and about how we change as an organisation to make sure this can happen.

Some examples of our changing context will see us working to implement the requirements of new legislation, particularly the Well-being of Future Generations (Wales) Act 2015, Environment (Wales) Act 2016, Planning (Wales) Act 2015 and the Historic Environment (Wales) Act 2016; addressing environmental challenges such as water quality, biodiversity, invasive species, air quality and climate change as well as managing our own operations to ensure we work within our means and work with our stakeholders – Welsh Government, other public service organisations, business and industry, citizens and communities to develop alternative public service delivery models.

Performance Analysis

As a Welsh Government Sponsored Body our primary role is to fulfil our statutory responsibilities and to meet the aims established for us by the Welsh Ministers. Our objectives are set both through a long-term outcome approach and an annual Remit Letter to establish areas of our work that require a particular focus. To meet these objectives we prepare a longer term corporate plan, supported by an annual business plan and performance framework. All of this information is available on our website at <http://naturalresources.wales/about-us/strategies-and-plans>

This is our second report against our Corporate Plan 2014 – 2017 and we use its five themes: Good Knowledge; Good Environment; Good for People; Good for Business and Good Organisation to structure our Business Plan 2015/16, Performance Framework and this Performance Report. As part of our Performance Framework, our dashboard tracks longer term trends through *indicators* that our work contributes to, as well as annual operational *measures* that we control delivery of. This year, of 41 indicators and measures, 28 met the target set, nine were within 10% of the target set, and four were not where we had planned to be. Our progress is monitored by our Board and Welsh Government and published on our website three times each year. The final performance dashboard for 2015/16 is available on our website at <http://naturalresources.wales/about-us/strategies-and-plans/how-well-are-we-doing>. The following sections of this report outline examples of outcomes achieved in line with our objectives as well as some of our key performance information.

Good Knowledge: gaining wisdom and understanding of our natural resources and how we affect them – using evidence and applying learning from experience, so that we make good decisions

Our role involves gathering evidence and offering advice on environmental matters in order to inform the decisions of others as well as our own.

Key Information

- All 102 Welsh Bathing Waters pass tough new EU Standards in 2015
- 96 data sets available online
- 11 funded partnership projects to deliver natural resource management in development

Clean bathing waters are important to the economy in our coastal communities and for wildlife in our seas. In 2015, all identified bathing waters in Wales met new stricter European classifications for water quality, a key measure that helps to ensure a seaside holiday or day out at the beach remains one of the most popular activities for many families. The results of our monitoring programme show that 82 of the 102 bathing waters in Wales achieved the higher classification of excellent, with 16 achieving good and four sufficient. No Welsh bathing water was classed as poor during the first year of these tough new standards. The challenge now is to maintain this standard, working with others to protect and enhance our natural resources so our coast and natural environment will continue to provide huge benefits to the people of Wales and our visitors.

In line with our commitment to be a trusted and professional organisation, we want our customers to access our data quickly, easily and, where possible, re-use it for personal, research or commercial purposes. With this in mind, we have fully transitioned to using the

Welsh Government Information Hub (Lle), a single data publishing service that allows us to publish our data in one place. We now have 96 open datasets available for external re-use, up from 78 in 2013, including the Ancient Woodland Inventory, Flood Maps and National Biodiversity Network Species Data. Our new open data policy will see this increase in the future.

Our new guide, '[Introducing Sustainable Natural Resource Management](#)' was published this year to outline the challenges and opportunities this new approach brings to managing our resources in Wales as well as the principles we, and others, should apply in order to address them. Demonstrating what this means in practice, we used case studies from our three area trails in the Dyfi, Tawe and Rhondda catchments. Highlights include working with the local wildlife trust to set up Rhondda's first nature reserve in 20 years, and work with multiple partners on tackling wildfires. In Swansea we have sought to improve access on the eastside of the city using our different roles and responsibilities to join up forest, nature reserve and river opportunities.

Work has also continued to produce Wales' first State of Natural Resources Report, due in September 2016. Working with academia to source relevant information and Welsh Government and partners to plan future evidence needs is helping to ensure this vital piece of work will inform the Welsh Government's National Natural Resources Policy every five years.

Good Environment: ecosystems are resilient and secured for the future, wildlife and landscapes are enhanced, and the use of our natural resources is carefully managed

Our roles as an operator, regulator and designator contribute to sustainably managing the land and water we're responsible for, protecting and improving the environment in Wales, halting biodiversity loss and making Wales more resilient to climate change.

Key Information

- 1,000 hectares of diseased larch tree cleared
- 82% of actions completed to improve the condition of designated sites
- 39% of water bodies across Wales met good overall status

Our environment is currently facing many challenges and demands on its resources. We are still below the 2015 target of 50% of water bodies meeting good ecological status (39%), while the quality of our seas, land and rivers remains unfavourable against the 95% target in the Wales Environment Strategy. We know that our work alone will not achieve the required improvements. As part of the Welsh Nature Recovery Plan we have achieved our planned target for getting actions underway and complete in bringing protected sites back into favourable condition and have made a number of improvements to help bring about the changes needed to the Welsh environment.

In recent months we have seen slight delays in our reviewing of evidence to support our first State of Natural Resources Report. This important report will highlight pressures and potential impacts on natural resources, give an indication of resilience, and include an assessment of the extent to which sustainable management of natural resources is being achieved. Benefits provided to the environment, people and economy of Wales will be

central to the report. We have put in place actions to ensure that we can still meet the September deadline for publication.

Examples of our work in improving the environment include:

- A new Site of Special Scientific Interest designation at a fossil forest in Brymbo, near Wrexham, is helping to safeguard this superb scientific and educational resource for future generations. The site contains a fantastic variety of 300 million year old fossilised plants and trees, making it a world class site for plant fossils. This site has an extraordinary story to tell and plans are now underway, led by Brymbo Heritage Group, to establish an excavation and visitor centre on the site that will ensure the right conditions to study and display these fragile fossils. This has the potential to be a popular tourist attraction, also contributing to the local economy of this area.
- More than 1,000 native white-clawed crayfish have been released into a tributary of the River Irfon, near Builth Wells as part of continued efforts to save the species from extinction. Reared at our Cynrig Fish Culture Unit, the crayfish have been released into the wild in a bid to offset the damage caused by the non-native American signal crayfish, climate change and the impact of pollution on habitat and water quality to the native crayfish population. In its third year, early signs suggest the project has been a success with crayfish found at release sites 15 months after the initial introduction. Establishing a healthy population of native white-clawed crayfish would be a good sign that water quality and habitats are being restored to a condition suitable for the crayfish to flourish.
- Two new species of marine sponges at the protected marine site around Skomer Island have been identified demonstrating that our conservation work contributes to a healthy environment for the species living there. Protecting our natural resources provides an important home to the rich, diverse and valuable wildlife we have in Wales, which in turn provides a fantastic habitat not only for lesser known wildlife like sponges but also for species like grey seals and sea birds which are a huge draw for tourists to the area. The number of sponge species recorded at Skomer has been steadily increasing over the last 30 years and currently stands at around 122 species.
- Work to restore Welsh peatlands is showing signs of success – but there's a lot more to do. Due to damage from drying out over many years, Welsh peat is a source of greenhouse gas emissions, releasing around 550,000 tonnes of carbon into the atmosphere every year. Now, over fifty per cent of Wales's semi-natural peatland habitats are being managed in a sustainable way, helping to lock in carbon that could otherwise be released into the atmosphere contributing to climate change. Over the last few years, at least 750 km of ditches have been blocked across Welsh peatlands to restore and re-wet them. Key areas include the uplands of Migneint, Hiraethog, Elennydd and Berwyn and lowland sites on Anglesey and the Llyn Peninsula, among others. Peatlands don't just store carbon, they harbour a wealth of rare plants and wildlife; help store water which can reduce the risk of flooding in lower lying areas and help purify our water supplies. Cors Erddreiniog National Nature Reserve, Anglesey, was one of the major sites included in our Anglesey and Llyn Fens LIFE project. It is now locking in carbon that would otherwise be released into the atmosphere. We will continue to work on restoring priority peatland sites, using management agreements with landowners and partnership projects to continue to restore peatlands.

- Salmon and sewin are an important part of the health of our rivers and worth millions to Welsh economy, now thanks to an update to the fish pass on the River Tawe in Panteg the iconic species can access prime spawning grounds in the upper Swansea valley. A historic weir had an existing fish pass that had become virtually unusable due to erosion of the river bed downstream. Our focus is to make sure that our rivers are in the best possible condition so they can support healthy fish populations.

Good for People: people are safe, and enjoy and benefit from our natural resources and understand their relevance in our day to day lives

Our roles as an operator, regulator, responder and educator are keeping people safe and encouraging people to visit the Welsh environment.

Key Information

- 148,150 residential properties and 60,350 non-residential properties, approximately 11% of all properties in Wales, are at risk of flooding from rivers and the sea
- 98% of high risk flood assets maintained
- Our incident reporting line received over 10,000 calls and we attended 1,883 environmental incidents

We maintain 319 miles of flood defences, manage over 4,000 flood defence assets, support flood plans, and offer flood warning and flood forecasting services to help reduce the risk and increase preparedness in the event of a flood in Wales. Work to build new flood defences has reduced the risk of flooding to 511 houses and 145 businesses benefitting communities in Dolgellau, Ffordd Isa and the Caldicot levels, surpassing our target to benefit 500 properties this year.

To help people in Wales know what to do in the event of a flood, face to face flood awareness engagement work in 20 at risk communities across Wales has resulted in 193 new flood plans being created, and 671 new registrations on our Flood Warnings Direct service. These plans cover a range of businesses, medical premises, caravan parks, schools and homes. There are currently 280 flood plan leads or wardens supporting community plans across Wales in a voluntary capacity. In addition to this new work, 61 previously completed community flood plans were maintained, to ensure that they were still active and fit for purpose for the 19,241 people protected by them.

Our maintenance programme to high risk flood assets was hampered due to winter floods resulting in our maintenance level falling slightly to 98% against our target of 99%. Our teams re-prioritised their resources to carry out urgent asset repairs and blockage removal works; this had a knock-on effect on our ability to address the failing assets already identified. We are working to turn this around and develop new systems to ensure funding goes to the highest risk locations.

In partnership with Ford Motor Company, the Llynfi Woodland Project is working to transform a former colliery site near Bridgend into a sustainable woodland designed with people in mind. 60,000 trees have been planted so far creating a new 30 hectare woodland. This will not only provide a home for wildlife, help to reduce flooding and absorb carbon but in working with the local community to develop the plans to create the

woodland as a place for people to relax, exercise and socialise, it will also encourage people to spend more time outside and increase their activity levels. Over the next ten years, employees and local communities will play their part planting trees and developing green exercise facilities providing a space for health and wellbeing activities for the community.

Using our sustainable natural resource management approach, 10 biodiversity projects were funded as part of our plans to build and maintain flood defences. Building in steps to help local nature when delivering our schemes ensures we consider the impact our activities have on each other. Eight projects were completed this year creating 237.5ha of Biodiversity Action Plan habitat.

To help our customers get easy access to information they need to stay safe or to enjoy the natural environment, we launched our [River Levels Online](#) service in November 2015. This displays live river level data from sites around Wales on our website. The river level data that we collect has many applications within NRW and now our customers can also use it to decide how to respond to a flood event, or to see if levels are suitable for fishing or kayaking. Until now this information has been made available through the Environment Agency's website but our staff have designed, built and tested this updated service to make it easy to find and view river level information from our sites across Wales. The information can be accessed using an interactive map or by searching a list of the monitoring stations.

Providing opportunities for people and visitors to Wales to go outside and enjoy our natural environment is an important element of our work. This year, two of our most popular visitor attractions, Bwlch Nant yr Arian, near Aberystwyth and Coed y Brenin Forest Park near Dolgellau in the Snowdonia National Park have celebrated Gold Awards from Visit Wales after achieving excellence for their facilities and customer services. Providing valuable educational resources and a leading mountain biking centre along with popular catering facilities both sites have succeeded in what is a dynamic and exciting industry where the need to offer a memorable visitor experience is essential.

Good for Business: a 'location of choice' for business and enterprise, and a place where best practice environmental management is adopted and encouraged

Our roles as a manager, advisor, regulator and statutory consultee are supporting businesses working with the natural environment and benefiting the Welsh economy.

Key Information

- 91% of planning applications responded to within agreed timescales
- 91% of permits, licences and consents issued within agreed timescales
- We supplied over 800,000m³ of timber to the market

Our Energy Delivery Programme continues to meet the aspirations of Welsh Government's Low Carbon Economy agenda, contributing significantly to reducing the use of carbon and addresses the impact of climate change while protecting the environment. By supporting the Wind Energy Programme, Small Scale Hydro Programme and Third Party Accesses related to energy projects on the NRW Managed Estate, we are seeing direct financial

benefit for Welsh Government and NRW with these projects providing important opportunities for the supply chain and jobs in Wales.

We worked with developers to enable nine small scale hydropower schemes on the NRW Managed Estate. Due to reductions in Feed in Tariffs during the year, developers withdrew from a further 22 proposed schemes. We also identified 165,000 tonnes of wood material from the larch replacement programme and roadside vegetation management that was available for sale in late 2015 and received a single offer to clear the young larch and re-establish a crop for zero value.

Our enforcement action continues to help protect the environment while working to create a level playing field for legitimate businesses. A South East Wales recycling company failing to comply with their environmental permit, saw their Director receive a suspended custodial sentence and become disqualified from being named as a Director of a company for the next five years as well as losing a waste contract with a local authority as a result. Actions to treat and store increasing volumes of waste began to cause odour, drainage pollution and fly problems and the company failed to comply with enforcement notices to improve the situation. In taking action to ensure the environment and health of local people is protected, almost £200,000 of public waste contracts will be let to businesses who legally meet their environmental responsibilities.

This year, 110 prosecutions for waste, water quality and fisheries offences saw the Courts impose fines totalling £119,305.00 and award costs of £115,049.95 to NRW. Monies actually received in relation Proceeds of Crime Act Confiscation Orders relating to our prosecutions totalled £145,383.48.

We continue to be the largest supplier of certified timber in Wales, this year putting to market 800,000m³ overbark standing of timber. This sustainable woodland management supports further employment in the forestry sector across Wales.

Good Organisation: We want to be well led and well managed, with suitably skilled and experienced staff and effective underpinning systems and processes; transparent in our decision-making and continuously improving our service to customers and partners, benchmarking ourselves against the very best.

Our work as a manager and employer is helping our transformation to become an exemplar public service organisation.

Key information

- 5% reduction in our greenhouse gas emissions
- Retained our UK Woodland Assurance Standard
- Formally completed our probation period as a new Welsh Government Sponsored Body

The results of our recent People Survey show that we need to focus on those things that will build better engagement and communication across our organisation and encourage belief in our purpose to pursue the sustainable management of natural resources in everything that we do. A high response rate of 82% clearly shows that our staff are passionate about making NRW a better place to work. It also gives us a clear indication

that we must find ways to encourage a culture of trust and engage everyone far more in how we plan and run NRW to get the best from people and the collective skills we all have.

We had 10 lost time incidents reporting accidents involving staff from falls, burns, musculoskeletal injury, scalding and head impact. Our initial reviews indicate that there is no pattern connecting these incidents; we are reviewing each of them and lessons learned will be shared with the wider workforce to help prevent similar situations happening.

Work has continued this year to progress our stand alone capability and we have been able to reduce the amount we pay to legacy bodies for ICT services by £5.2m each year. Eighteen new ICT applications contributed to the reduction in our Information and Communications Technology (ICT) infrastructure from a total of 1,405 applications from all three legacy bodies down to 775 at the end of this year. Staff have worked hard on data migration and testing reporting processes as well as developing training packages including videos, courses and user guides to complement our new way of working. We are pleased to have established an agreed data sharing agreement with the Environment Agency (EA) and are now looking to deliver the remaining ICT deliverables that will allow us to finally close all the transition services with the EA and Forestry Commission GB by 31 March 2017.

Realising better value for money, we are expecting to generate benefits of £158 million over our first 10 years through the greater efficiencies gained by bringing three organisations into one. Currently we have successfully identified cash and non-cash realisable benefits of £147 million (93%). Although we are on target, we need to maintain a strong focus on making efficiencies, controlling costs and making sure plans to deliver the benefits are implemented. Work will continue to exit transitional EA and Forestry Commission GB services worth approximately a further £2.5 million in 2016/17.

Following our transition to a standalone organisation, we launched a major programme of Business Area Reviews to consider what we do, how we do it, and how we are structured to deliver our purpose effectively and efficiently. This will allow us to meet our new purpose, adapt to the changing legislative context in Wales, and to deliver our ambitions within a financially challenging environment. An overarching review of our senior management was included with the aim of delivering an operating model that meets the needs of our customers and partners, embeds sustainable management of natural resources in all we do, and delivers an affordable structure by the year 2020. It aims to ensure NRW is a great place to work and grow, so that people and teams can excel and deliver improved business performance on a sustained basis.

Following the [Wales Audit Office's Development of NRW Study](#) report, we were pleased to receive formal Ministerial Approval that we had completed our probationary period as a new Welsh Government Sponsored Body. This is an excellent result and an important milestone in the establishment of our organisation. The final report highlighted substantial challenges that have been overcome, while maintaining business continuity. The Welsh Audit Office recognised our *'adoption of a sound and well-structured approach'* so that we now have *'a solid platform for continuing to realise the intended benefits of creation and for tackling the future challenges'* we will face.

Our Carbon Positive project is progressing to establish our net carbon status, accounting for both greenhouse gas emissions emitted through our work and the carbon captured by

ecosystems across the whole of the NRW estate. The project is leading our approach to become an exemplar in carbon management. It will inform our wider work to tackle climate change by investigating and delivering measures to reduce our carbon impact, and planning future implementation of appropriate measures. Through sharing our approach and experiences, the Carbon Positive project will help to encourage best practice in carbon management across the Welsh public sector.

We have risen 78 places in the Stonewall Workplace Equality Index since last year and we are now placed 160 out of 415 top employers for lesbian, gay, bisexual and transgender workers in the UK and 14th place in Wales. We are pleased our swift progress over the past two years to provide an inclusive and diverse workplace has been recognised.

Dr Emyr Roberts
Chief Executive and Accounting Officer

Date: 2 March 2017

Accountability Report

Corporate Governance Report

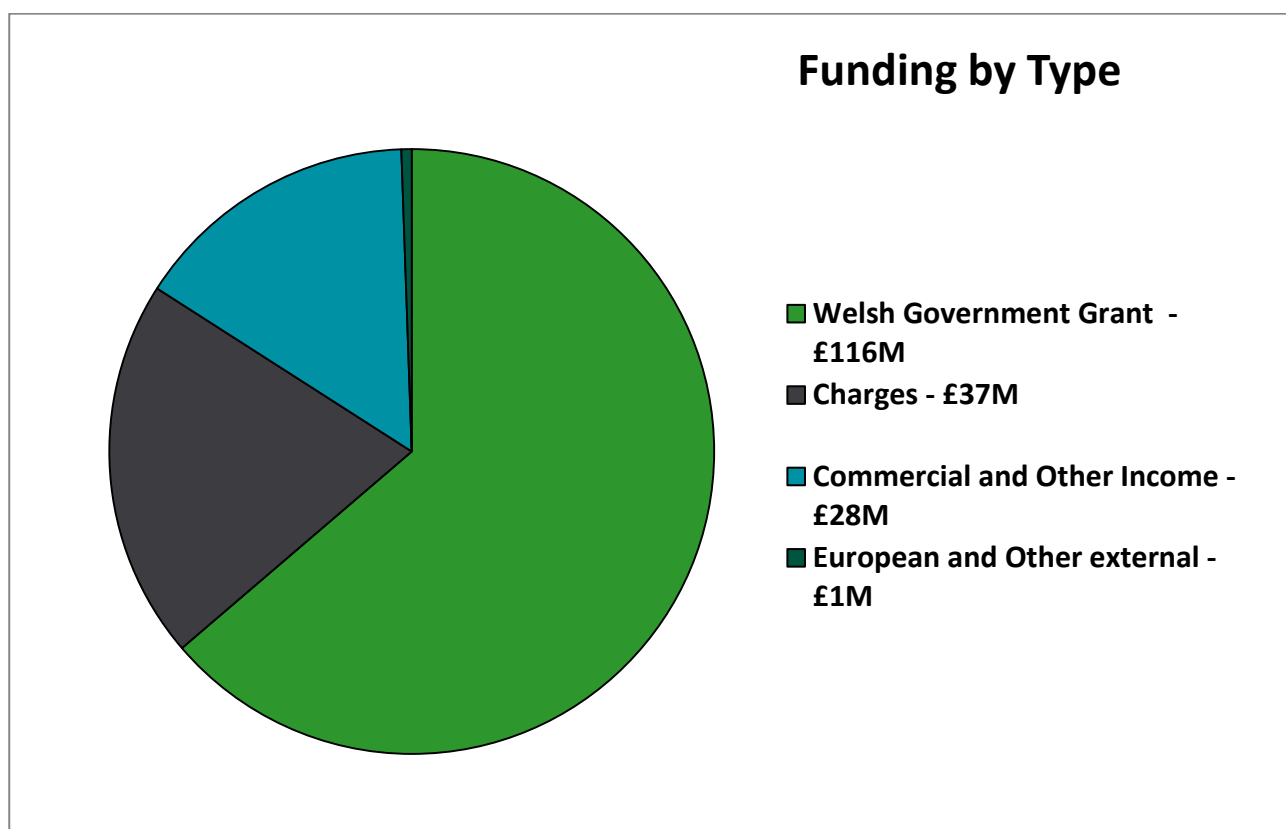
Director's Report

Managing our Money

Despite a £3.2 million reduction in our revenue Grant in Aid compared with 2014/15, we have successfully managed our expenditure in line with plans. As part of this, we instigated an efficiency campaign called 'Success with Less' which realised near £2.5 million of savings. We also exceeded our commercial income targets. This has been achieved whilst operating in a very challenging financial context in the current financial year and planning for future financial years. Our future financial viability, and achieving a financially sustainable organisation, is our major focus at the moment, and we have started to develop our Corporate Plan for 2017-2022.

Funding

Our total income for the year was £66 million. In addition, Welsh Government provided £116 million Grant in Aid towards a range of outcomes. £39 million was allocated to Flood Coastal Risk Management and £77 million to Non-Flood Coastal Risk Management. In the Accounts, Grant in Aid is treated as a contribution from a controlling authority and not a source of income. The chart below illustrates the distribution of our total funding:

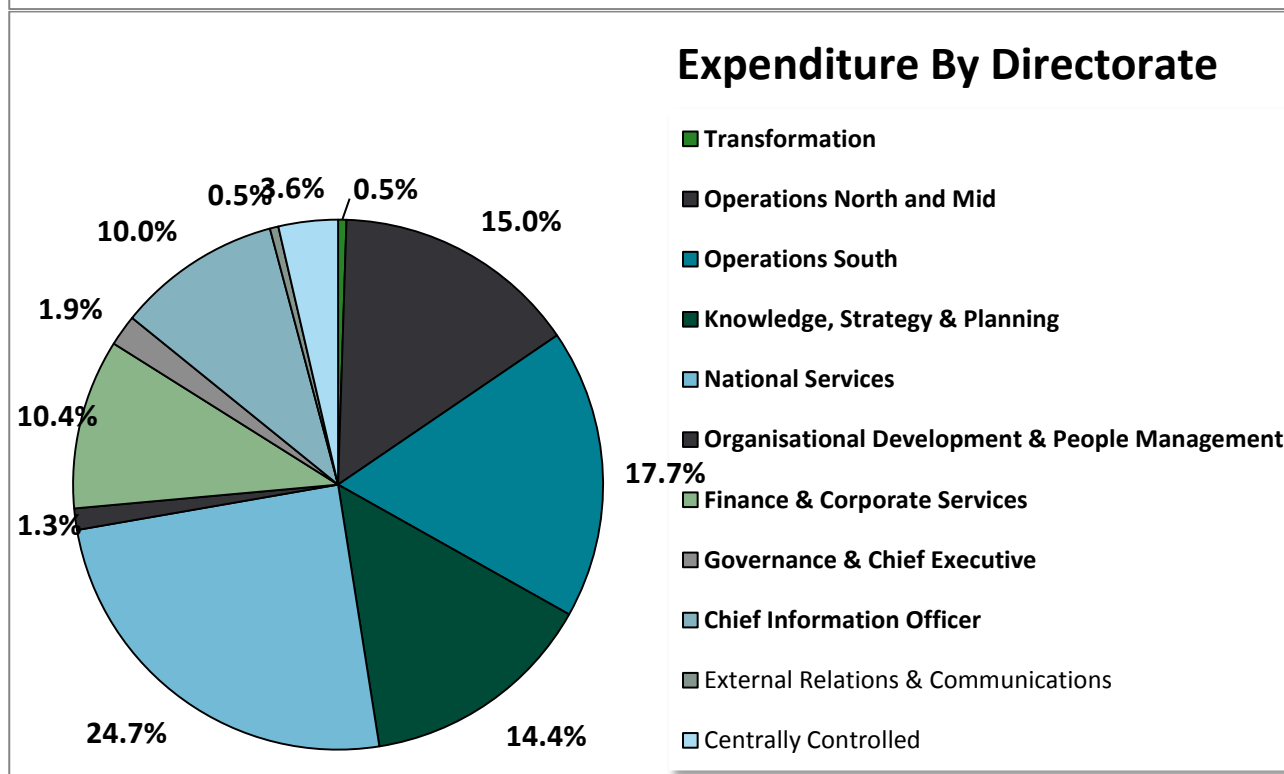
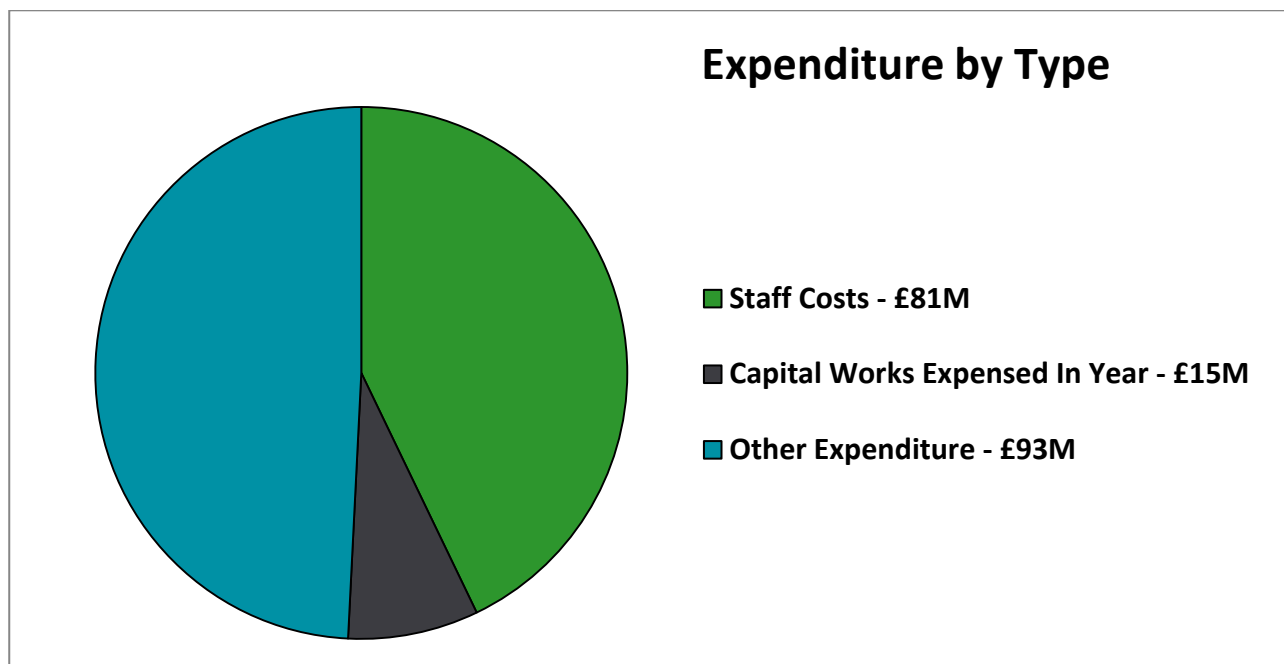


We have a number of funding sources which we keep discrete when planning and spending our resources. The main funding source of Grant in Aid is split between Flood and Coastal Risk Management and Non Flood and Coastal Risk Management – for both revenue and capital. We also have a number of Charge Schemes (see Note 6 of the

Financial Statements) which are based on the principle of 'cost recovery'. In addition, we apply and receive additional funding from a number of sources (such as European funding) which are spent on specific projects.

How we spent our money

Our total expenditure was £189 million. The detailed breakdown by category of spend can be found in Notes 5 to the Accounts and is also illustrated below:



Centrally controlled - Income and expenditure controlled centrally and not allocated to directorates. It includes depreciation, book value of fellings and year end accruals for provisions.

Note 2, 3, 4 and 5 of the Financial Statements details where the money was spent.

Success with Less Efficiency Campaign

Our 'Success with Less' campaign realised nearly £2.5 million of savings across a range of initiatives including changing the way we travel and use technology to communicate and letting better value contracts. Our campaign won the Wales National Procurement Award for Outstanding Contribution for demonstrating our unique and significant contribution in terms of implementing strategic public procurement initiatives and in driving change and leadership in order to help modernise Wales.

Future Developments

Funding for 2016/17 is particularly challenging due to further reductions in our revenue Grant in Aid funding from Welsh Government, and the costs of completing our transformation of Information and Communications Technology infrastructure which will allow to exit more services which are currently provided by the Environment Agency and Forestry Commission Great Britain.

We have implemented a range of measures to set an affordable budget for 2016/17, with several areas being reduced by over 10%, and we have continued with our tight workforce controls.

As part of our Roadmap we are in the process of implementing a significant programme of change and transformation that will allow us to meet our new purpose, adapt to the changing legislative context in Wales, and to deliver our ambitions within a financially challenging environment. This will help build our affordable Corporate Plan for 2017-2022.

Non-Current Assets

The value of our non-current assets was £874 million at 31 March 2016, a 12% (£97 million) increase compared to last financial year. The most significant component is the value of the forest estate and biological assets which accounts for £714 million of the value. We have undertaken an independent quinquennial revaluation of land and buildings and forest estate including biological assets and that has been incorporated into this result.

Quinquennial Revaluation

Every five years organisations undertake a thorough independent revaluation of most land, building and public use structures. This is the first time for NRW to undertake this exercise. As a result, the value of our non-current assets have increased by £95 million (compared to overall increase of £97 million). We are satisfied with the results of the valuation and it highlights the excellent commercial value that our asset base has. The main reasons for the increase of £95m is the improvement in the valuation of assets on our forest estate (£83 million), inclusion of assets that had not been previously identified as non-current assets such as Third Party access for energy projects, recreation, hydropower and mineral leases, car parks and trails (£9 million), increase in value of bike trails (£7 million) but offset by other movements including downward valuations of some of our assets (£4 million).

Payment of Trade and other Payables

Welsh Government has a commitment to pay 95% of suppliers within 30 days and we aim to meet this target wherever possible. By the end of the financial year our performance had

increased to 98%. Performance for the whole year was 91%. This helps to ease businesses' cash flow in the current challenging economic climate.

Going Concern

The Statement of Financial Position at 31 March 2016 shows positive taxpayers equity of £806 million. The future financing of our liabilities is to be met by Welsh Government Grant in Aid and the application of future income. We have already received approval for funding for 2016/17. Therefore, it is appropriate to adopt a going concern basis to prepare the Annual Accounts.

Estate Management

We manage Wales's public forest estate on behalf of the Welsh Ministers in accordance with our acquisitions and disposal policy and our Enterprise strategy. We also have Forest Plans for all the forests, which sets how each forest will be managed to deliver strategy objectives over the next 25 years.

We are also currently working to develop Natural Resource Plans that will provide a series of local plans/strategies which will guide the management of the estate and assets across Wales.

National Nature Reserves, which are owned or leased by us, are managed in accordance with an approved management plan, which include conservation objectives for all recognised features of interest and identifies necessary projects and work programmes. The plans are reviewed periodically and checked by our Conservation Management Team, through a rolling programme of reviews/environmental audits.

Pensions

The pensions liability are disclosed in the Annual Report and Accounts on the basis of IAS19. The liability has decreased for the LGPS pension scheme in the year due to an increase in the net discount rate over this period, the positive impact of which has outweighed the likely lower than expected asset returns.

This is different from the basis used for funding calculations. The last formal revaluation of the fund was undertaken at 31 March 2013 and showed an overall funding position of 86%.

Auditors

Our accounts are audited by the Auditor General for Wales. The audit fee for 2015/16 was £142,989.

Personal Data

There were no data losses reported this year.

Corporate Reporting

The following annual reports are also available on our website:

- [Equalities Report 2015/16](#)
- Wellbeing, Health and Safety Report 2015/16

Environmental Reporting

Over the coming years, we want to set the example in Wales in areas including our management and use of carbon, waste, water and land, as outlined in our Corporate and Business plans. Corporate reporting on our organisation's own environmental impact is included in Annex 1.

This year we have:

- retained ISO14001 and UK Woodland Assurance Standard (UKWAS) certification following independent external audits and verification, demonstrating our own commitment to achieving the highest possible environmental standards as an organisation
- increased our carbon footprint by 10% due to the increase in primary aggregate use in construction schemes
- met our target to reduce our carbon footprint by 5% in relation to occupied buildings energy use and business travel
- trained staff on key areas of our organisation's Environmental Management System

During the coming years, we will continue to improve our corporate environmental reporting in working towards Integrated Reporting.

Dr Emyr Roberts
Chief Executive and Accounting Officer

Date: 2 March 2017

Statement of Accounting Officer's Responsibilities

Paragraph 23 (1) of the Schedule to the Natural Resources Body for Wales (Establishment) Order 2012 required Natural Resources Wales to produce for each financial year a Statement of Accounts in the form and on the basis set out in the Accounts Direction.

The accounts are prepared on an accruals basis and must give a true and fair view of the state of affairs of Natural Resources Wales and of the income and expenditure, changes in taxpayers' equity and cash flows for the financial year.

In preparing the accounts, the Accounting Officer is required to comply with the requirements of the Government Financial Reporting Manual (FReM) and in particular to:

- observe the Accounts Direction issued by HM Treasury including the relevant accounting and disclosure requirements and apply suitable accounting policies on a consistent basis
- make judgements and estimates on a reasonable basis
- state whether applicable accounting standards as set out in the FReM have been followed, and disclose and explain any material departures in the financial statements
- prepare the financial statements on a going concern basis.

The Additional Accounting Officer for Welsh Government has designated the Chief Executive of Natural Resources Wales as its Accounting Officer. The Chief Executive's responsibilities as Accounting Officer are the propriety and regularity of the public finances for which he is answerable; the keeping of proper accounts; prudent and economical administration; avoidance of waste and extravagance; and the efficient and effective use of all the resources as set out in the Memorandum for the Accounting Officer for Natural Resources Wales.

Governance Statement

As the designated Accounting Officer for NRW, I am responsible for maintaining a sound system of internal control that supports the achievement of our aims and objectives. My role is also to safeguard public funds and organisational assets by putting in place proper arrangements for the governance of our affairs and effective exercise of our functions. As a result I am personally responsible for this governance statement. The full scope of my responsibility is described in the Memorandum for Accounting Officer of Natural Resources Wales, issued by the Welsh Government and additional content is described in Managing Welsh Public Money.

I have outlined the following in order to demonstrate how I have fulfilled this role.

- Governance structure
- Review of effectiveness
 - Board performance
 - System of internal control
 - ARAC Annual Report
- Risk management framework
- Internal Audit opinion

Our Governance Structure

Our Board members are appointed by Welsh Ministers in accordance with the Code of Practice for Ministerial Appointments in Public Bodies, and as such our Chair is accountable to the Minister for Natural Resources. We currently have eleven Board members, including myself as an Executive member of the Board. We are led by our Chair, Diane McCrea MBE. The remainder of the Board is made up of ten non-executive members. During the year, the Welsh Government led a public appointments process and the Minister for Natural Resources appointed Diane McCrea MBE from 1 December 2015 as the second Chair of NRW, as well as five new Board members (Karen Balmer, Chris Blake, Howard Davies, Elizabeth Haywood and Zoe Henderson). Dr Madeleine Havard was appointed as Deputy Chair from 1 December 2015 and remaining members Dr Ruth Hall CB, Andy Middleton, Nigel Reader CBE and Sir Paul Williams OBE agreed new two year terms.

In advance, and in support, of the Welsh Government public appointment process to appoint our new Chair and new Board members, we organised a series of 'Come on Board' promotion events across Wales. The primary purpose was to promote Board membership to the full cross section of Welsh society by explaining more about the work of NRW, as well as the specific requirements of Board members. More than 120 people attended one of the three events in Merthyr, Aberystwyth and Llandudno, including several of the newly appointed Board members.

I would like to acknowledge the leadership and dedication of our first Chair, Professor Peter Matthews CBE, whose term of office finished on 30 November 2015. Three of our founding Board members left the Board on 31 October 2015 (Prof Lynda Warren, Rev Hywel Davies and Harry Legge-Bourke).

To support the Board as a whole, and in order to ensure business continuity, all new Board members have participated in an induction programme to appraise them of key policies, procedures, and the current position and scope of our work. I am grateful to the continuing

experienced Board members for supporting this work, as well as my Executive Team. This induction will be continued through our full Board development programme during 2016/17.

The role and responsibility of the Board is to:

- provide strategic direction and leadership, driving performance and hold us to account against our strategic and corporate plans
- ensure propriety, regularity, economy, efficiency and effectiveness in the operation of the body and adherence to the seven Principles of Public Life (the Nolan principles)
- ensure that we fulfil our statutory and regulatory duties, in the light of such guidance and direction Ministers may give it
- be a champion for the organisation and its aims and objectives, as well as a role model for staff and stakeholders
- work co-operatively to build relationships with all stakeholders, including the Welsh Government, businesses, communities and staff and their representatives
- demonstrate high standards of corporate governance at all times, including by using the Audit and Risk Assurance Committee to help address key financial and other risks.

We operate to the principles set out in the Code of Good Practice for Corporate Governance issued by HM Treasury. This year our focus has been on supporting the development and implementation of the Welsh Government's legislative programme, as well as moving the organisation from a transition phase to a transformation phase. During the year, the Board has been actively involved in reviewing the implications of the Well-being of Future Generations (Wales) Act, as well as considering proposals for how we should take forward our new statutory purpose and responsibilities under the Environment (Wales) Act. In addition, the Board has agreed NRW's Business Plan 2016/17 during the year and taken some preparatory steps for the development of our next Corporate Plan 2017-22. The Board has also overseen the development of NRW's 'Fit for the Future' programme, which aims to transform the organisation to be able to deliver integrated natural resource management, whilst achieving financial sustainability. As well as through the work of the full Board, I am grateful to individual Board members for supporting this work through direct engagement with staff groups, as well as membership of Business Area Review programme boards.

We have held four meetings in public across Wales during the year, as well as a number of other Development Board meetings. Standing items on our agenda include: in year finance and performance reporting, strategic and operational updates from the Chair, Chief Executive, Committees, and Board Groups. To support our commitment that our governance is transparent, open and accessible to all, we publish a wide range of information regarding our work on our website, including papers to be considered by the Board in advance of those meetings held in public. All future meeting dates and previous agendas, papers and minutes are available on our website naturalresources.wales/about-us/our-chair-board-and-executive-team

Board Member Attendance

	No. of possible meetings	No. of meetings attended
Professor Peter Matthews CBE (Chair)*	3	3
Rev Hywel Davies**	3	2
Dr Ruth Hall CB	6	6
Dr Madeleine Havard (Deputy Chair)***	6	6
Harry Legge-Bourke**	3	3
Andy Middleton	6	6
Nigel Reader CBE	6	5
Dr Emyr Roberts	6	6
Professor Lynda Warren**	3	3
Sir Paul Williams OBE	6	5
Diane McCrea MBE (Chair)***	3	3
Karen Balmer****	3	3
Chris Blake****	3	3
Howard Davies****	3	3
Zoe Henderson****	3	2
Elizabeth Haywood****	3	2

*End of term as Chair in November 2015

**End of term as Board member in October 2015

***Appointed as new Chair and Deputy Chair from December 2015

****Appointed as new Board member from December 2015.

Our Board has three **sub committees**, each chaired by a Board Member, and include at least two other Board members. We do not have a Nomination Committee as our members are appointed by Welsh Ministers. Membership of each committee was reviewed in January 2016 following the appointment of new Board members. Attendance records below reflect these changes. Where necessary, the full Board has reviewed and agreed the terms of responsibility for each of the following:

- Audit and Risk Assurance Committee
- Remuneration Committee
- Protected Areas Committee

Audit and Risk Assurance Committee

The Audit and Risk Assurance Committee's (ARAC) principal role is to advise the Board and support the Accounting Officer in monitoring, scrutinising and challenging the arrangements in place for audit, governance, internal controls and risk management. As Accounting Officer I attend every meeting, along with our Executive Director of Finance and Corporate Services and Director of Governance.

This year ARAC addressed a range of issues including:

- Annual Report and Accounts 2014/15 and plans for this report, 2015/16
- External and internal audit plans and reports
- Corporate Risk Register including a number of 'deep dives' into specific risks

- Risk Management internal audit
- Audit arrangements for the Well-being of Future Generations (Wales) Act
- New Anti-Bribery and Corruption Policy
- Review of Complaints Policy
- Review of Conflicts of Interest Policy.

Board Member ARAC Attendance

	No. of possible meetings	No. of meetings attended
Nigel Reader CBE (Chair)	5	5
Dr Ruth Hall CB	5	5
Dr Madeleine Havard*	4	4
Andy Middleton*	4	4
Karen Balmer**	1	1
Chris Blake**	1	1

*Stood down from ARAC in December 2015

**Appointed to ARAC in March 2016

Remuneration Committee

The Remuneration Committee (REMCOM) considers matters relating to the pay and conditions of employment of our most senior staff and the overall pay strategy for all staff employed by NRW. The Committee also operates as the Transformation Advisory Group to monitor and review all transformation issues, including the delivery of the benefits identified in the business case for the creation of NRW.

As Accounting Officer I attend every meeting, along with our Executive Director of Organisational Development and People Management, and Director Transformation Portfolio.

The committee addressed a range of issues during the year including:

- Job Evaluation Scheme
- Voluntary Early Severance Scheme
- Changes to Pension Schemes
- Director appointments and remuneration
- Transformation programme.

Board Member REMCOM Attendance

	No. of possible meetings	No. of meetings attended
Sir Paul Williams OBE (Chair)	4	4
Nigel Reader CBE	4	4
Dr Ruth Hall CB*	3	3
Rev Hywel Davies*	2	2
Karen Balmer**	1	1
Zoë Henderson**	1	1

*Stood down from REMCOM in September 2015

**Appointed to REMCOM in March 2016

Protected Area Committee

The Board has delegated its statutory responsibilities in relation to objections to the notification and de-notification of Sites of Special Scientific Interest to the Protected Areas Committee (PAC). PAC members also support the Executive and full Board by providing advice on wider protected area issues and strategic casework.

During the year the committee considered objections and confirmed the designation of one new Site of Special Scientific Interest (SSSI).

Board Member PAC Attendance

	No. of possible meetings	No. of meetings attended
Andy Middleton (Chair)	1	1
Professor Peter Matthews CBE	1	1
Dr Ruth Hall CB	1	1
Dr Madeleine Havard	1	1
Sir Paul Williams OBE	1	1

Flood Risk Management Wales

This committee, although not a standing committee of the main Board, fulfils a number of statutory flood risk management functions of NRW in accordance with Section 106 of the Water Resources Act 1991. During the year, the Welsh Government reviewed the governance arrangements for flood risk management within Wales and through the Environment (Wales) Act will be implementing arrangements for a new Advisory Committee which will be accountable to Ministers from 2016/17. As a result of these changes, when the independently appointed Chair, Mr Deep Sagar's term ended in June 2015, the Minister for Natural Resources appointed NRW Board member Dr Madeleine Havard, as interim Chair to oversee the transition to the new governance arrangements. The remaining Committee members are Local Authority representatives and independent members, appointed either by Welsh Ministers or by NRW.

Board Groups

Outside of our formal meetings, Board members have played an active role in supporting the Executive in strategy development. The standing Board Groups until December 2015 were:

- Environment
- Communities
- Economy
- NRW Enterprise
- Knowledge.

These groups have provided an opportunity for Board members to contribute to the development of work at an early stage and allow the Executive to keep Board members informed of developments in specific areas of the business. Board members have also supported on 'task and finish' groups to provide advice on specific tasks e.g. performance reporting. The new Chair reviewed these arrangements on her appointment and, from January 2016, Board members were allocated to the following Board groups, which are all available to support the Executive when required:

- Knowledge
- Environment
- People (inc communities)
- Business (inc NRW Enterprise).

Board Effectiveness

Our Board held a session in July 2015 to review results of their previous Board effectiveness survey. The overall results showed continued progress in the maturity of the Board and key actions agreed included improving arrangements for engaging with stakeholders around Board meetings, better opportunity to input to strategy as a full Board via Development Board meetings, and improved arrangements for briefings on key operational activities by the Executive. New arrangements are in place in all these areas and improvements became evident during the second half of the year.

Due to changes to our Board membership close to the end of the financial year, and the prioritisation of the ongoing induction programme, we have decided to undertake a Board effectiveness review later in 2016. We are planning to use the indicators of High Performing Organisations developed by Academi Wales, to formally review Board Effectiveness.

Our new Chair, Diane McCrea MBE, has reviewed the membership of committees, as well as put in place new arrangements for informal support to my Executive Team as we develop proposals for the Board to consider. The new membership and arrangements has helped to blend the new Board members with the experienced Board members, building in continuity and resilience for the future.

In addition, Professor Peter Matthews CBE before the end of his term, conducted year-end performance appraisals for each Board Member. Our new Chair will be agreeing objectives and individual development plans for each Board Member for 2016/17.

The Audit and Risk Assurance Committee (ARAC) also conducted an annual review of its effectiveness via the completion of a questionnaire based on a checklist produced by the National Audit Office, the criteria for which are largely derived from HM Treasury's Audit Committee Handbook. Overall, the ARAC was considered to be very effective, with the majority of key arrangements and processes in place. However, the exercise highlighted that there are a small number of additional issues that the Committee could consider as part of its assurance role. As a result, an induction plan has been put together to support new ARAC members, as well as a plan to hold annual closed sessions with the Chief Executive and both Internal and External auditors to give an opportunity for greater independence and transparency if required.

Our Executive

Day to day management of our organisation is delivered through our Executive Team. As Chief Executive, I chair the meetings with six Executive Directors, three Directors, and our Chief Information Officer in attendance. We formally meet on a three weekly cycle. Our Business meetings deal with current and emerging issues, and monitor the performance of the organisation; Strategy and Policy meetings develop strategy for the organisation and recommend new policy positions to the Board; and we meet as a Change Programme Board to receive and consider updates on progress with the Change Programme.

Each Directorate has a Directorate Delivery Plan, which are linked to corporate targets and outcomes within the annual Business Plan. These are reviewed on monthly basis with their Leadership Team members and feed into the Corporate Performance Dashboard, which is reported to the Board and the Welsh Government three times a year.

Our Risk Management Framework

The Board has approved our Risk Management policy and is responsible for overseeing the implementation of the policy and process. Based on HM Treasury guidance for managing risks, the key objective is to ensure that we have a consistent approach to identifying, measuring, controlling, monitoring and reporting risks.

We face a broad range of risks across our responsibilities therefore it is not appropriate to make a single overarching statement of our attitude to risk. Instead, a range of risk appetite statements arising from different areas of our work have been agreed. The Board will be reviewing its risk appetite for our different activities in early 2016/17. This is in response to considering recommendations from our Business Area Reviews as part of our transformation to deliver integrated natural resource management.

Our day-to-day risks are identified, evaluated and managed at a number of different levels. Our Board is responsible for managing corporate risks in line with achieving strategic objectives. The Board retains ownership of the key corporate risks, but uses ARAC to exercise scrutiny over our risk management processes, as well as to drill-down into specific risks and issues. Executive Team members manage Directorate Risk Registers in line with achieving their targets and outcomes in their Directorate Delivery Plan. These are reviewed regularly and I discuss them during their performance reviews. Risk Registers are also in place for major projects and programmes and are reviewed at project and programme meetings.

Key risks that were identified and managed during the year included:

- responding to the short-term reduction in our grant in aid and planning for continued financial challenges
- ensuring that we are fully prepared for the new challenges arising from the Well-being of Future Generations and Environment (Wales) Acts
- responding to the spread of the *Phytophthora ramorum* tree disease.

Information Assurance

We are committed to ensuring data and information is well governed and managed and have continued to work to achieve the right balance between transparency and openness, and necessary information security. Our Director of Governance acts as the Senior Information Risk Owner (SIRO); we have concentrated our efforts during the year on consolidating the implementation of relevant Information Governance Policy and Procedures, as well as developing our information security incident handling arrangements.

In addition, we have progressed 22 Privacy Impact Assessments to cover a wide range of our activities where personal information is handled, as well as completed the training by the National Archives of the full cohort of Information Asset Owners.

Effectiveness of Internal Control

Members of my Executive Team have each signed a Certificate of Assurance and completed an Internal Control Checklist which required them to make an evidence based assessment of the effectiveness of the control framework in place for their Directorate;

Overall results this year show increased confidence in the control framework which is pleasing as this is evidence of systems and processes being embedded within the organisation after our first three years. However, information handling and security remain a concern as more information has migrated from legacy systems and staff are still developing their knowledge of our ICT system. This will be addressed with an Executive Team action plan through 2016/17.

We have an established whistleblowing policy and reporting procedure in place to raise serious concerns about malpractice or impropriety; this year there were no reported whistleblowing cases. This policy is due to be reviewed in 2016/17.

Our Internal Audit team have completed their annual audit plan, with regular progress and feedback to the Audit and Risk Assurance Committee. In year, it was noted that the number of outstanding actions was increasing. I have highlighted this to my Executive Team and, although the position is improving, it is something we will seek to address during 2016/17.

The opinion of the Internal Audit Manager (in a Head of Audit and Risk Assurance capacity), as set out in their annual assurance report is:

In my opinion, Natural Resources Wales can have Moderate assurance in the overall adequacy and effectiveness of its internal control environment, including its arrangements for governance and risk management.

During the year an audit of Risk Management identified weaknesses in control at a level such that only limited assurance was given. The management have given commitment to implement the recommendations made, addressing identified risks. However, the remedial work has taken longer than originally anticipated and further improvements are still required. Given that this is a key building block of good governance, this continued weakness has influenced the annual Audit Opinion.

External Audit

During the year, the Wales Audit Office's Development of NRW Study was undertaken to complete the Probationary Review of NRW on behalf of Welsh Government, and to prepare a Value for Money Report on behalf of National Assembly's Public Accounts Committee.

Following significant field work, I was pleased to receive formal Ministerial Approval that we had completed our probationary period as a new Welsh Government Sponsored Body. This is an excellent result and can be viewed as the final milestone in the setup of the new organisation. The final report highlighted substantial challenges that have been overcome, while maintaining business continuity. WAO recognised our 'adoption of a sound and well-structured approach' so that we now have 'a solid platform for continuing to realise the intended benefits of creation and for tackling the future challenges' we will face. An Action Plan has been developed in response to the final recommendations which I will now

oversee and report progress to our ARAC every six months in order to deliver the required improvements.

In early 2015, the Better Regulation Delivery Office undertook a review of our activities in line with the Principles of Good Regulation. I was pleased that their final report highlighted our broad understanding of the principles and that we have started to demonstrate these in our ways of working. Our follow up action plan in response to recommendations seeks to build on this and we will continue to engage with those we regulate or who are impacted by regulation to share their views as we develop our future approach.

Submission of Financial Statements

During the course of the annual financial audit the Auditor General for Wales became aware of an issue relating to the regularity of several long term timber sales contracts that had been let in 2014. The issue identified was complex and has required extensive evidence to be gathered and considered by the Auditor General for Wales. This review has identified some lessons to be learned for Natural Resources Wales and an action plan is being put in place that the Audit and Risk Committee will oversee.

The financial statements were originally submitted to the Auditor General for Wales on 23 August 2016. The delay caused by this additional review has resulted in the financial statements being resubmitted on 2 March 2017.

Dr Emyr Roberts
Chief Executive and Accounting Officer

Date: 2 March 2017

Remuneration and Staff Report (audited)

Remuneration policy

The Board has established a Remuneration Committee to consider matters relating to the pay and conditions of employment of the most senior staff and overall pay strategy for all staff employed by NRW. The Remuneration Committee is comprised of four non-executive Board members. The Board Chair is an ex officio member of the Committee.

The Chair and Board members' remuneration is set by Welsh Ministers. The terms of contract for senior employees (Executive Team members) is based on NRW terms and conditions. The remuneration policy for the most senior staff is not subject to collective bargaining and the remuneration package is set by reference to a set of benchmark roles in the Welsh public service and to comparable organisations based in the UK. Progression to the benchmark (rate for the job) is subject to satisfactory performance. Only on the basis of exceptional performance are the top two pay points used.

There is a social partnership agreement in place and the setting of terms and conditions for all other staff is through collective agreement with the social partners. The Welsh Government approves any changes to pay, terms and conditions and gives a pay remit to NRW within which it must deliver. A pay deal covering the period 1 July 2015 to 30 June 2016 was successfully negotiated in November 2015. Former Internal Drainage Board staff had a pay award from 1 April 2015 to 30 June 2016 to bring an alignment of pay award dates.

Service contracts

All appointments to the Board are made on behalf of the Minister for Natural Resources. Appointments are normally made for either two or three years.

The Chief Executive and Executive Team members are expected to be employed under permanent contracts. Appointments are made in accordance with our recruitment policy, which requires appointment to be made on merit and on the basis of fair and open competition.

Unless otherwise stated below, the Executive Team members covered by this report hold appointments which are open-ended. These officers and Board members are required to provide three months' notice of their intention to leave.

Salary and pension entitlements

The following sections provide details of the remuneration of members of the Board and the remuneration and pension interests of members of the Executive Team. Board members are not entitled to join the Civil Service Pension Scheme or receive other benefits. Early termination, other than for misconduct, would result in the Executive Team members receiving compensation in line with the Civil Service Compensation Scheme. Board members are not entitled to compensation.

Board Members' Remuneration

Board Member	Employment Contract	Salary 2015/16 (£5,000 range)	Salary 2014/15 (£5,000 range)
Karen Balmer ⁶	9-11-15 to 8-11-17	0-5	0
Chris Blake ⁶	9-11-15 to 8-11-17	0-5	0
Dr Michael Brooker	01-11-12 to 31-10-14	0	10-15
Howard Davies ⁶	9-11-15 to 8-11-17	0-5	0
Rev Hywel Davies ⁷	01-11-12 to 31-10-15	10-15	20-25
Dr Ruth Hall CB ¹	01-11-12 to 31-10-17	15-20	20-25
Dr Madeleine Havard (Deputy Chair) ^{1,5}	01-11-12 to 31-10-17	20-25	20-25
Elizabeth Haywood ⁶	9-11-15 to 8-11-17	0-5	0
Zoë Henderson ⁶	9-11-15 to 8-11-17	0-5	0
Harry Legge-Bourke ⁷	01-11-12 to 31-10-15	10-15	20-25
Diane McCrea (Chair) MBE ⁹	1-12-15 to 30-11-18	5-10	0
Prof Peter Matthews CBE (Chair) ⁸	01-08-12 to 31-11-15	30-35	50-55
Andy Middleton ^{1,4}	01-11-12 to 31-10-17	15-20	20-25
Nigel Reader ^{1,2} CBE	01-11-12 to 31-10-17	20-25	25-30
Prof Lynda Warren ⁷	01-11-12 to 31-10-15	10-15	20-25
Sir Paul Williams ^{1,3} OBE	01-11-12 to 31-10-17	20-25	25-30

¹ These members have been reappointed for another 2 years from November 2015 until 31 October 2017.

² Nigel Reader is Chair of the Audit and Risk Assurance Committee.

³ Paul Williams is Chair of the Remuneration Committee and the Transformation Advisory Group.

⁴ Andy Middleton is Chair of the Protected Areas Committee.

⁵ Madeleine Havard was appointed as Deputy Chair from December 2015 to October 2017 and was appointed as the Chair of Flood Risk Management Wales in June 2015.

⁶ The full year equivalent salary is £12,600.

⁷ The full year equivalent salary is £21,000.

⁸ The full year equivalent salary is £50,000.

⁹ The full year equivalent salary is £28,000.

Executive Team's Remuneration

Executive Team Member	Salary		Benefits in kind ⁶		Pension benefits ⁷		Total	
	(£5000 range)		(nearest £100)		(nearest £1,000)		(£5,000 range)	
	2015/16	2014/15	2015/16	2014/15	2015/16	2014/15	2015/16	2014/15
Dr Emyr Roberts (Chief Executive)	145-150	145-150	0	0	45,000	61,000	190-195	205-210
Martin Britton ¹	0	125-130	0	0	0	0	0	125-130
Martin Britton ²	65-70	15-20	0	0	26,000	6,000	95-100	20-25
Ceri Davies	95-100	95-100	2,400	2,000	47,000	24,000	145-150	120-125
Elizabeth Davis ¹⁰	0	35-40	0	0	0	59,000	0	90-95
Ashleigh Dunn ⁸	90-95	30-35	0	0	35,000	12,000	125-130	45-50
Graham Hillier ³	5-10	90-95	0	3,600	11,000	21,000	15-20	115-120
Kevin Ingram	90-95	90-95	4,000	2,600	35,000	53,000	130-135	145-150
Tim Jones	90-95	85-90	2,700	2,400	40,000	30,000	130-135	120-125
Gareth O'Shea ⁴	85-90	0	2,800	0	179,000	0	265-270	0
Trefor Owen ⁵	90-95	90-95	0	0	34,000	17,000	125-130	105-110
Niall Reynolds	75-80	75-80	0	0	(7,000)	19,000	70-75	90-95
Catherine Smith ⁹	75-80	70-75	0	0	29,000	23,000	100-105	90-95
Clive Thomas	75-80	70-75	0	2,300 ¹¹	48,000	22,000	120-125	95-100

¹ Martin Britton fulfilled the role of Chief Information Officer on the Executive Team under contract with his employment agency until January 2015. This action had been approved and supported by the Remuneration Committee, based on the exceptional circumstances involved with setting up our ICT services. For 2014/15 the figure reported as his salary above represents the agency costs incurred by NRW (excluding expenses) from 1st April 2014 until January 2015.

² Following a review by the Chief Executive and confirmation by the Remuneration Committee it was decided to appoint a permanent Chief Information Officer. The successful candidate was Martin Britton and he was a full time employee from 1st February 2015 to 31st December 2015. The relevant salary costs for February 2015 to March 2015 and April 2015 to December 2015 are reported above. The full year equivalent salary for 2014/15 and 2015/16 is £90-95,000.

³ Until 26th April 2015. The full year equivalent salary is £90-95,000.

⁴ Gareth O'Shea was appointed as Director of Operations South on 27th April 2015. The figures quoted are for the period 27/04/15 to 31/3/16. The full year equivalent salary is £90-95,000.

⁵ Trefor Owen finished on the 31st March 2016.

⁶ Relates to the provision of an allocated car.

⁷ The value of pension benefits accrued during the year is calculated as (the real increase in pension multiplied by 20) plus (the real increase in any lump sum) less (contributions made by the individual). The real increases exclude increases due to inflation or any increases or decreases due to a transfer of pension rights.

⁸ Ashleigh Dunn was appointed as Director of Organisational Development and People Management on 17th November 2014. The figures quoted for 2014/15 are for the period 17/11/14 to 31/3/15. The full year equivalent salary is £90-95,000.

⁹ Catherine Smith was appointed as Director of External Relations and Communications on the 22nd April 2014. The figures quoted for 2014/15 are for the period 22/4/14 to 31/3/15. The full year equivalent salary is £75-80,000.

¹⁰ Elizabeth Davis was working as part of the Welsh Government's Living Wales Programme and on formal secondment from WG from 1 April until 31 July 2014. The full year equivalent salary is £105-110,000.

¹¹ Until 5th November 2014.

Salary

Salary covers both pensionable and non-pensionable amounts and includes gross salary, overtime and any allowances or payments that are subject to UK taxation. It does not include amounts which are a reimbursement of expenses directly incurred in the performance of an individual's duties.

Performance related pay

For the Executive Team, movement between the pay points is subject to performance assessment by the Chief Executive and moderation by the Remuneration Committee. Any movement beyond the benchmark point will only be for consistent outstanding performance as assessed by the Chief Executive and confirmed by the Remuneration Committee.

Benefits in kind

The monetary value of benefits in kind covers any benefits provided by the employer and treated by the HM Revenue and Customs as a taxable emolument. The ones shown above relate to the provision of lease cars.

None of the Board members or senior staff received any remuneration other than shown above.

Pension Benefits

Executive Team member	Accrued Pension at pension age as at 31/3/16 £000	Accrued Lump Sum at pension age as at 31/3/16 £000	Real Increase in pension at pension age £000	Real Increase in Accrued Lump Sum at pension age £000	CETV at 31/03/16 ⁴ £000	CETV at 31/03/15 ⁴ £000	Real Increase in CETV £000
Dr Emyr Roberts (Chief Executive)	60-65	185-190	0-2.5	5-7.5	1388	1251	43
Martin Britton ¹	0-5	0	0-2.5	0	14	3	6
Ceri Davies	30-35	60-65	2.5-5	0-2.5	597	533	26
Ashleigh Dunn	0-5	0	0-2.5	0	40	10	22
Graham Hillier ²	50-55	15-20	0-2.5	0-2.5	722	714	7
Kevin Ingram	25-30	35-40	0-2.5	0-2.5	343	303	14
Tim Jones	35-40	105-110	0-2.5	5-7.5	703	611	33
Gareth O'Shea ³	35-40	75-80	7.5-10	15-17.5	574	422	119
Trefor Owen	40-45	0	0-2.5	0	720	634	26
Niall Reynolds	30-35	65-70	0-2.5	(2.5-5)	599	582	(15) ⁵
Catherine Smith	0-5	0	0-2.5	0	31	13	10
Clive Thomas	20-25	60-65	2.5-5	0-2.5	390	327	29

¹ until 31/12/15

² until 26/4/15

³ from 27/4/15

⁴ the factors used to calculate the CETV were reviewed by the scheme actuary in 2015, so the tables of factors used to calculate the CETV in 2015 are not the same as those used to calculate the CETV in 2016.

⁵ taking account of inflation, the CETV funded by the employer has decreased in real terms.

Cash Equivalent Transfer Values

A Cash Equivalent Transfer Value (CETV) is the actuarially assessed capitalised value of the pension scheme benefits accrued by a member at a particular point in time. The benefits valued are the member's accrued benefits and any contingent spouse's pension payable from the scheme. A CETV is a payment made by a pension scheme or arrangement to secure pension benefits in another pension scheme or arrangement when the member leaves a scheme and chooses to transfer the benefits accrued in their former scheme. The pension figures shown relate to the benefits that the individual has accrued as a consequence of their total membership of the pension scheme, not just their service in a senior capacity to which disclosure applies.

The figures include the value of any pension benefit in another scheme or arrangement which the member has transferred to the Civil Service pension arrangements. They also include any additional pension benefit accrued to the member as a result of their buying additional pension benefits at their own cost. CETVs are worked out in accordance with The Occupational Pension Schemes (Transfer Values) (Amendment) Regulations 2008 and do not take account of any actual or potential reduction to benefits resulting from Lifetime Allowance Tax which may be due when pension benefits are taken.

Real increase in CETV

This reflects the increase in CETV that is funded by the employer. It does not include the increase in accrued pension due to inflation, contributions paid by the employee (including the value of any benefits transferred from another pension scheme or arrangement) and uses common market valuation factors for the start and end of the period.

Fair pay disclosure

NRW and similar bodies are required to disclose the relationship between the remuneration of the highest paid director in their organisation and the median remuneration of the organisation's workforce. Total remuneration includes salary and benefits in kind. It does not include severance payments, employer pension contributions and the cash equivalent transfer value of pensions.

In 2015/16, no employees (2014/15: none) received remuneration in excess of the highest-paid director. The banded remuneration of the highest paid Director in the financial year 2015/16 was £145,000-£150,000 (2014/15 £145,000-£150,000). This was 5.2 times (2014/15, 5.0 times) the median remuneration of the workforce which was £28,215 (2014/15 £29,535). The change in median pay is due to harmonised pay scales and more staff employed at lower rates of pay. Staff pay scales range from £12,250 to £64,624. Directors' remuneration is shown in the table above.

Staff report

Number of staff by headcount and full time equivalent (FTE) at 31st March 2016.

	Male		Female		Total	
	Headcount	FTE	Headcount	FTE	Headcount	FTE
All employees	1222	1197.8	886	802.5	2108	2000.3
of which:						
Leadership team	21	21.0	8	7.1	29	28.1
Executive team	6	6.0	3	3.0	9	9.0

Average number of full-time equivalent persons employed during the year was:

	2015/16			2014/15
	Permanent Staff	Others	Total	Total
Directly employed	1,855	57	1,912	1,905
Agency and contract staff	0	89	89	47
Total	1,855	146	2,001	1,952

The average full time equivalent number of staff employed on capital projects was 75.8 (50 in 2014/15)

Staff costs

	2015/16			2014/15
	Permanent Staff	Other Staff	Total	Total
	£'000	£'000	£'000	£'000
Wages and salaries	57,822	7,747	65,569	62,372
Social security costs	4,724	100	4,824	4,739
Other pension costs	13,452	13	13,465	12,177
Total net salary costs	75,998	7,860	83,858	79,288
Other expenditure for staff				
Exit package costs			132	2,790
IAS 19 (Pensions) additional service charge			8,325	7,323
Less early retirement pension costs			(144)	(97)
Less in-year LGPS pension contributions			(7,936)	(7,216)
Transfer to Provision for Annual Compensation Payments			(2)	5
Other staff costs			341	0
Movement in Accrued Holiday Pay			(159)	81
Total other expenditure for staff			557	2,886
Less amounts charged to capital projects			(3,176)	(2,019)
Total staff costs			<u>81,239</u>	<u>80,155</u>

Details of NRW's pension arrangements can be found in note 13.

Details of the remuneration of Board members and directors are in the remuneration report.

Bought in services in Note 5 (Other expenditure) includes £6.58m of expenditure on consultants.

Pension schemes

NRW is a member of two pension schemes. The Principal Civil Service Pension Scheme is an open scheme and is the scheme for the former Countryside Council for Wales and Forestry Commission Wales staff and new members of staff. NRW is a closed member of the Environment Agency's pension fund (a Local Government pension fund) under a community admission agreement. Further details of these pension schemes shown below.

Principal Civil Service Pension Scheme contributions

The Principal Civil Service Pension Scheme (PCSPS) and the Civil Servant and Other Pension Scheme (CSOPS) - known as "alpha" are unfunded multi-employer defined benefit scheme but NRW is unable to identify its share of the underlying assets and liabilities. The scheme actuary valued the scheme as at 31 March 2012. You can find details in the resource accounts of the Cabinet Office: Civil Superannuation at: www.civilservicepensionscheme.org.uk/about-us/resource-accounts/

For 2015/16, employers' contributions of £5,663k were payable to the PCSPS (2014/15 £4,931k) at one of four rates in the range 20.0% to 24.5% of pensionable earnings, based on salary bands. The Scheme Actuary reviews employer contributions usually every four years following a full scheme valuation. The contribution rates are set to meet the cost of the benefits accruing during 2015/16 to be paid when the member retires and not the benefits paid during this period to existing pensioners.

Stakeholder partnership pensions

Employees can opt to open a partnership pension account, a stakeholder pension with an employer contribution. Employers' contributions of £44k were paid to one or more of the panel of three appointed stakeholder pension providers. Employer contributions are age-related and range from 3% to 12.5% of pensionable earnings up to 30 September 2015 and from 8% to 14.75% of pensionable earning from 1 October 2015. Employers also match employee contributions up to 3% of pensionable earnings. In addition, employer contributions of £2k, 0.5% of pensionable pay, were payable to the PCSPS to cover the cost of the future provision of lump sum benefits on death in service or ill health retirement of these employees.

No contributions due to the partnership pension providers at the balance sheet date, and no contributions were prepaid.

Local Government Pension Scheme contributions

NRW makes payments to the Environment Agency Pension Fund (EAPF), as the administering authority for the Local Government Pension Scheme (LGPS) via Capita, the pension fund administrators.

The LGPS is a funded, statutory, defined contribution public service pension scheme. Hymans Robertson, the actuary for the EAPF, carries out a triennial valuation of the fund's assets and liabilities in order to ensure that LGPS benefits are properly funded. The assets of the fund are for meeting future pension liabilities. The main purpose of the actuarial valuation is to review the financial position of the fund and to set the level of future contributions for employers in the fund. The latest valuation was carried out as at 31 March 2013 for the three year period from 1 April 2014 to 31 March 2017.

NRW has a community admission agreement with the EAPF in order to participate in the LGPS, which was approved by the Secretary of State for Communities and Local Government in respect of former Environment Agency Wales staff who transferred to NRW on 1 April 2013. The liabilities for former members employed by the Environment Agency in respect of Welsh functions (pensions in payment and deferred members) also transferred. Welsh Government has entered into a guarantee with the EAPF to indemnify them for any liabilities that arise from the participation of NRW in the EAPF.

For 2015/16 the employer's contribution rate was 21.2%. (Contribution rate in 2014/15 was 20.2%). In 2015/16 employer's contributions of £7,936k were paid to the LGPS. (Contributions in 2014/15 were £7,216k)

Exit packages

The number of staff receiving redundancy payment by cost band:	2015/16	2014/15
Under £10,000	4	0
£10,001 - £25,000	3	10
£25,001 - £50,000	0	18
£50,001 - £100,000	0	29
£100,001 - £150,000	0	1
Over £150,000	0	0
Total	7	58

Total resource cost for 2015/16 was £63k. (Total cost of £2,884k in 2014/15)

There were no compulsory redundancies in 2015/16 or in 2014/15.

The voluntary exit costs have been paid in accordance with provisions of the Civil Service Compensation Scheme, a statutory scheme made under the Superannuation Act 1972. Exit costs are accounted for in full in the year they are agreed.

Where the legacy bodies agreed early retirements, the costs were accounted for in full in the year when they were agreed and a provision made for future commitments. The annual compensation payments in respect of these are shown in Note 12 (Provisions).

Ill-health retirement costs are met by the pension schemes and are not included in the table.

Sickness Absence (Unaudited)

Our sickness absence rates as at 31 March 2016 showed an average of 5.2 days lost per employee and equates to 2.37%. This was against a target of an average of up to 7 days lost, which equates to 3.1% of available working days.

Off payroll engagements (Unaudited)

In 2012 the Treasury announced a review of the tax arrangements of public sector appointees in order to determine the extent of arrangements which could allow public sector appointees to minimise their tax payments. The review concluded that:

- the most senior staff must be on the payroll, unless there were exceptional temporary circumstances which would require Accounting Officer sign-off and could not last longer than six months
- departments (and their arm's length bodies) must be able to seek formal assurance from contractors with off payroll arrangements lasting more than six months and costing over £220 per day that income tax and national insurance obligations are being met. If that assurance is not provided, contracts should be terminated
- Departments (and their arm's length bodies) are required to report to Parliament as part of their Annual Report and Accounts on the outcome of applying the above principles.

The following tables show our position in relation to these conclusions.

For all off-payroll engagements as of 31 March 2016, for more than £220 per day and that last for longer than six months	Number of contractors
The total number of existing engagements as of 31 March 2016	27
of which:	
The number that have existed for less than one year at time of reporting	6
The number that have existed for between one and two years at time of reporting	18
The number that have existed for between two and three years at time of reporting	3
The number that have existed for between three and four years at time of reporting	0
The number that have existed for four or more years at time of reporting	0

For all new off-payroll engagements, or those that reached six months in duration, between 1 April 2015 and 31 March 2016, for more than £220 per day and that last for longer than six months	Number of contractors
The number of new engagements, or those that reached six months in duration, during the time period.	12
The number of these engagements which include contractual clauses giving the department the right to request assurance in relation to income tax and National Insurance obligations.	12
The number for whom assurance has been requested	5
of which	
• The number for whom assurance has been requested and received.	5
• The number for whom assurance has been requested but not received	0
The number that have been terminated as a result of assurance not being received	0

Parliamentary and Audit Report (audited)

Losses and special payments

Welsh Government's Managing Public Money rules require disclosure of losses and special payments by category, type and value where they exceed £300k in total and for any individual items above £300k.

Individual losses of more than £300k

There were no losses or special payments over £300k throughout 2015/16.

A provision for of £1,201k was created for the Communities and Nature project in 2014/15 which was used during 2015/16. It is therefore not included in Note 5 in these accounts.

Losses and special payments by category

The table below provides the number of requests for write offs and special payments approved in the year.

Category or type of loss	2015/16 Number	2015/16 £'000	2014/15 Number	2014/15 £'000
Write-off of irrecoverable debts	56	280	38	187
Write-off of Communities and Nature Project	1	57	1	455
Assets written off	135	456	145	626
Loss of assets	0	0	3	320
Other losses (cash losses, fruitless payments, unenforceable claims, special payments or gifts)	15	57	20	178
Total	207	850	207	1,766

Dr Emyr Roberts
Chief Executive and Accounting Officer

Date: 2 March 2017

The Certificate and Report of the Auditor General for Wales to the National Assembly for Wales

I certify that I have audited the financial statements of Natural Resources Wales for the year ended 31 March 2016 under paragraph 23 of the Schedule to the Natural Resources Body for Wales (Establishment) Order 2012. These comprise the Statement of Comprehensive Net Expenditure, Statement of Financial Position, Statement of Cash flows, Statement of Changes in Taxpayers Equity and related notes. These financial statements have been prepared under the accounting policies set out within them. I have also audited the information in the Remuneration Report that is described in that report as having been audited.

Respective responsibilities of the Accounting Officer and auditor

As explained more fully in the Statement of Accounting Officer's Responsibilities, the Accounting Officer is responsible for preparing the financial statements, in accordance with Paragraph 23 of the Schedule to the Natural Resources Body for Wales (Establishment) Order 2012 and Welsh Ministers' directions made there under and for ensuring the regularity of financial transactions.

My responsibility is to audit, certify and report on the financial statements in accordance with applicable law and with International Standards on Auditing (UK and Ireland). These standards require me to comply with the Financial Reporting Council's Ethical Standards for Auditors. I consider that the audit evidence I have obtained is sufficient and appropriate to provide a basis for the qualified regularity audit opinion.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to Natural Resources Wales' circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by Natural Resources Wales; and the overall presentation of the financial statements.

In addition, I obtain evidence sufficient to give reasonable assurance that the expenditure and income have been applied to the purposes intended by the National Assembly for Wales and the financial transactions conform to the authorities which govern them.

In addition I read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my certificate and report.

Opinion on Financial Statements

In my opinion the financial statements:

- give a true and fair view of the state of Natural Resources Wales' affairs as at 31 March 2016 and of its net operating costs for the year then ended; and
- have been properly prepared in accordance with Welsh Ministers' directions issued under Paragraph 23 of the Schedule to the Natural Resources Body for Wales (Establishment) Order 2012.

Basis for qualified regularity opinion

Note 6 to the accounts records timber income of £16.5 million in 2015/16.

Under Natural Resources Wales' framework of authority it is required to refer any activities which appear novel, contentious or repercussive to its sponsor department within the Welsh Government. Natural Resources Wales did not refer its decision to enter into a series of interrelated timber sales contracts, which I consider to be contentious and repercussive, to its sponsor department. I therefore consider the transactions relating to these contracts to be irregular. As these transactions are material to the financial statements, I have qualified my regularity opinion accordingly.

Furthermore, there was an insufficiency of evidence to form a conclusion in respect of these same transactions on both the lawfulness of decision-making and compliance with State aid rules. I was therefore unable to satisfy myself as to the lawfulness of the transactions and I have therefore also qualified my regularity opinion accordingly.

Further details on these matters are set out in my accompanying Report on pages 43 to 47.

Qualified opinion on regularity

In my opinion, except for the effects of the failure to comply with its framework of authority and the possible effects of insufficient evidence to conclude on compliance with public law principles in decision making and compliance with state aid rules, as described in the above 'basis for qualified regularity opinion' paragraphs, in all material respects the expenditure and income in the financial statements have been applied to the purposes intended by the National Assembly for Wales and the financial transactions recorded in the financial statements conform to the authorities which govern them.

Opinion on other matters

In my opinion:

- the part of the Remuneration Report to be audited has been properly prepared in accordance with Welsh Ministers' directions made under Paragraph 23 of the Schedule to the Natural Resources Body for Wales (Establishment) Order 2012; and
- the information in the Annual Report is consistent with the financial statements.

Matters on which I report by exception

I have nothing to report in respect of the following matters which I report to you if, in my opinion:

- the Governance Statement does not reflect compliance with Welsh Ministers' guidance;
- adequate accounting records have not been kept;
- the financial statements and the part of the Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- information specified by Welsh Ministers regarding the remuneration and other transactions is not disclosed.

Other than in respect of the transactions referenced in the above 'basis for qualified regularity opinion' paragraphs, I have received all of the information and explanations I require for my audit.

Huw Vaughan Thomas
Auditor General for Wales
2 March 2017

Wales Audit Office
24 Cathedral Road
Cardiff
CF11 9LJ

Report of the Auditor General for Wales Timber Sales Contracts

1. Natural Resources Wales (NRW) is a Welsh Government sponsored body created for the purpose of ensuring that the environment and natural resources of Wales are:
 - sustainably maintained;
 - sustainably enhanced; and
 - sustainably used.¹
2. NRW became operational from 1 April 2013, taking over responsibility for delivering the functions of the former Countryside Council for Wales, Environment Agency Wales, and the Forestry Commission Wales. NRW managed the first two years of its development as a 'transition' stage, aiming to manage continuity whilst bringing together functions from its legacy bodies. In February 2016, I published a Value for Money report on the development of NRW concluding that: 'NRW adopted a sound and well-structured approach to meeting the significant challenges presented by its creation; ensuring continuity in delivering its wide range of functions and with a clear focus on achieving the intended benefits'.² Notwithstanding the matters raised in this report, I remain satisfied that NRW's approach to managing the transition stage was sound and well-structured.
3. Under paragraph 23 of Schedule 1 to the Natural Resources Body for Wales (Establishment) Order 2012 (the 'Establishment Order'), I am required to examine, certify and report on the statement of accounts of NRW. My audit certificate on pages 41 and 42 contains my opinion that the financial statements give a 'true and fair view'.
4. My certificate also includes my 'regularity' opinion, i.e. my opinion on whether the expenditure and income shown in the accounts have been applied to the purposes intended by the National Assembly for Wales and whether the financial transactions conform to the authorities that govern them. This year I have qualified my regularity opinion on the basis that the agreement of eight inter-related timber sales contracts did not comply with the framework of authority under which NRW was operating and, furthermore, on the basis of the information provided by NRW in relation to its decision-making procedure, I have not been able to satisfy myself that the decision to agree those contracts was lawful and did not involve the provision of State aid.
5. It was necessary to undertake extensive unplanned audit enquiries to enable me to give my 'true and fair' audit opinion and my regularity opinion. The issues encountered are legally complex and have necessitated NRW gathering a significant quantity of documentation. It was also necessary for auditors, acting on my behalf, to review that documentation and obtain external legal advice on the issues.
6. The Establishment Order sets a deadline for laying the certified statement of accounts and my audit report before the National Assembly for Wales of within four months of NRW submitting the financial statement to me for audit. NRW submitted its statement on 23 August 2016, so the deadline for laying was 23 December 2016. That timetable, however, is not the only statutory requirement applying to the audit. I am also under a statutory duty to comply with the Code of Audit Practice (the 'Code') pursuant to section 10 of the Public Audit (Wales) Act 2013 (the '2013 Act'). The Code includes several requirements, reflecting the

¹ The Environment Wales Act 2016 amended the general purpose of the Natural Resources Body for Wales to: "The Body must pursue sustainable management of natural resources in relation to Wales, and apply the principles of sustainable management of natural resources, in the exercise of its functions, so far as consistent with their proper exercise."

² The Development of Natural Resources Wales, February 2016

http://audit.wales/system/files/publications/Development_of_Natural_Resources_Wales_English_2016.pdf

need to undertake audit functions properly, including offering audited bodies and relevant third parties the opportunity to comment on findings.

7. In the circumstances, it has not been possible to meet both the requirements of the 2013 Act and the timetable set by the Establishment Order. I am advised by my legal adviser that given the conflicting statutory duties, it was appropriate to give more prominence to the requirements of the 2013 Act and the Code, and I have therefore completed my audit accordingly. It was important to complete the investigatory process properly, including seeking comments from the audited body and relevant third parties to satisfy the requirements of the Code and also to ensure that the audit conclusions are sufficiently rigorous.
8. One of the key operational challenges which had been facing the Forestry Commission in Wales prior to the merger was how to manage and control the spread of *Phytophthora Ramorum* (*P Ramorum*) in larch forests and woodlands. *P Ramorum* is a fungus-like pathogen which causes extensive damage to, and kills a wide range of trees and other plants. *P Ramorum* was detected in Japanese larch in Wales in 2010. Efforts were made to manage the spread of the disease through targeted felling, but the disease spread rapidly. Following its establishment, NRW inherited this challenge and was faced with having to take urgent action to manage and control the disease. During the summer months of 2013, NRW identified that there was a rapid increase in the spread of *P Ramorum* and had to find a long-term solution to combating the disease. I have been told by NRW that its intention in meeting this challenge was primarily and overwhelmingly to increase capacity for dealing with diseased larch and avoid disruption to existing trade in other types of timber.
9. In May 2014, NRW entered into a Memorandum of Agreement with a sawmill operator ('the sawmill operator'). The Memorandum of Agreement related to eight connected timber sales contracts. Under the contractual terms, NRW agreed to sell both standing trees and pre-felled timber to the sawmill operator. The sawmill operator also agreed, as a condition of the contract, that it would construct and operate a new saw line at its Welsh premises by 31 March 2016.
10. In my estimation, the purchase price the sawmill operator agreed with NRW amounts to approximately £72 million over the ten year duration of the contracts. However, the sawmill operator is entitled to deduct from the purchase price agreed costs for felling, extraction, haulage and management fees. In consequence, NRW estimates that the contract value to NRW will be approximately £39 million over the ten year contractual period.
11. NRW has estimated that the annual volume of timber sold to the sawmill operator under the terms of the contract to be between 20% and 25% of the annual total timber released by NRW per annum.
12. During the course of my audit of NRW's 2015/16 accounts, I received correspondence from an interested party raising concerns regarding the way in which NRW awarded contracts to the sawmill operator in May 2014. These concerns included:
 - (a) NRW awarded the contracts for the sale of spruce without seeking competition from the market;
 - (b) lack of transparency within NRW's decision-making processes;
 - (c) the required contracted investment in the operator's Welsh premises had not been made;
 - (d) the impact on the wider supplier market of awarding high volume long-term contracts to one supplier; and
 - (e) whether the decision to award the contracts to the sawmill operator represented good value for money.
13. These concerns appeared to me to raise questions about the regularity of transactions relating to the contracts signed in May 2014, and I have examined the award of the timber sales contracts accordingly.

14. I have not sought to examine whether the contracts entered into by NRW represented value for money. This is because such value for money examinations do not form part of my financial audit of the financial statements, which is performed in accordance with legislation and United Kingdom auditing standards prescribed by the Financial Reporting Council.
15. My main conclusions are as follows:

Compliance with framework of authority

16. The decision to award a number of very significant contracts to the sawmill operator was, in my view, contentious and repercussive. This was due to a combination of factors, in particular:
 - The size of the contracts.
 - The contracts for larch and spruce were awarded following a competitive tender for larch contracts (in which the sawmill operator was not the winning bidder. However, NRW decided to offer contracts for larch to all three bidders) and therefore no other potential purchasers were given the opportunity to purchase the volume of larch and spruce timber which was ultimately awarded to the sawmill operator. NRW contends that there was no market for diseased larch based on (a) the lack of interest shown in the sale of 21 individual parcels of trees offered to the market and (b) that only three bids were received in response to a tender issued in April 2013 for two long-term contracts (LTCs) for clearance and marketing of infected Larch stands over a five year period. In my view, the size of those parcels and the tender offer are not comparable to the offer of eight LTCs for both diseased larch and spruce, particularly as the sawmill operator itself made clear that four LTCs for larch would be insufficient for it to invest in the new saw line. The contract volume awarded to the sawmill operator was designed to enable it to make major investment in its sawmill. This investment enabled the sawmill operator to significantly increase its processing capacity. NRW contends that it was highly unlikely that any other operators would have been interested in such significant volumes of diseased larch and in the timescales in which NRW had to act. NRW has told me that it was aware of the risk of challenge on this point but that their 'professional view was that there was no alternative'. However, there is little within the contemporaneous documentation to evidence that NRW officials gave careful consideration to whether higher volumes might draw interest from a wider range of timber companies (ie, companies that did not bid in the 2013 competition) nor whether those volumes might have sufficed to encourage other competitors to invest in additional capacity. In my view, the commitment of NRW to sell the sawmill operator a high volume of timber over a ten year period would appear to be an opportunity which other operators may have been interested in.
 - The decision to award the contracts was not informed by relevant market testing.
 - NRW acknowledged in its internal documents that the award of the contracts in this way gave rise to risks including the risk of challenge by another operator.

17. Under the terms of the Framework Agreement provided to NRW by the Welsh Government³, and the then extant Welsh Government publication: 'Managing Welsh Public Money'⁴, NRW was required to refer to the Welsh Government activities which appeared novel, contentious or repercussive.
18. NRW officials did inform the Board and the Welsh Government that it was seeking to negotiate with the sawmill operator and to warn the Welsh Government that the sawmill operator might seek to lobby Welsh Ministers because the sawmill operator was unhappy with a contract offer NRW had made to it in August 2013. However, NRW did not refer its proposal to contract with the sawmill operator in May 2014 to the Welsh Government as a contentious or repercussive proposal. NRW has told me that at the time it did not regard the award of the contracts as contentious or repercussive. In my view, NRW should have referred the matter and therefore did not operate within the framework of authority to which it was subject. In consequence, the contractual transactions with the sawmill operator were in my view irregular.

Compliance with public law principles in decision-making

19. The decision-making process which led to the award of contracts to the sawmill operator in May 2014 was in my view neither robust nor transparent. NRW has not been able to provide me with sufficient contemporaneous documentation to adequately demonstrate the considerations it took into account in deciding to enter into these contracts with the sawmill operator. NRW considers the decision to enter contracts with the sawmill operator was taken lawfully, however, in the absence of sufficient evidence, I have been unable to satisfy myself that NRW's decision to enter into these contracts with the sawmill operator was taken in accordance with public law principles. I note that NRW disputes this conclusion.
20. Whilst I have significant concerns regarding the decision-making process, the evidence is not sufficient for me to reach a conclusion that the decision to enter into the contracts was in breach of public law principles. My uncertainty does not mean that the contracts should now be regarded as unlawful, nor does it mean they represent poor value for money. The decisions to award the contracts remain valid in the absence of any challenge and quashing by a Court. My conclusions arise in the context of my audit functions and do not bear on the validity or enforceability of the decisions taken by NRW (and I note NRW's point that none of the industry representatives sought to bring a challenge to the award of the contracts). My regularity opinion, however, takes the form of positive assurance, which means that I state whether transactions are in accordance with the authorities that govern them. Given the significant uncertainty, I am unable to give an unqualified regularity opinion on the financial statements.

Compliance with State aid rules

21. Under Article 107 of the EU Treaty on the Functioning of the European Union, State aid is aid granted from State resources in any form which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods, in so far as it affects trade between Member States. The provision of State aid is unlawful unless authorised in advance, whether by an existing 'block exemption' or by individual authorisation granted by the European Commission in response to a notification from the relevant State. I have sought legal advice on whether or not the award of the contracts constituted a grant of State aid to

³ The NRW Framework Document was drawn up by the Welsh Government in consultation with NRW. It sets out the broad framework of accountabilities within which NRW operates and details the terms and conditions under which the Welsh Ministers provide grant-in-aid to NRW.

⁴ Managing Welsh Public Money sets out the framework and principles which must be applied by the Welsh Government, its sponsored bodies, the NHS in Wales, its commissioners, the Education Workforce Council, Estyn and the Welsh Government's subsidiary bodies.

the sawmill operator. I am advised that this turns on whether or not those contracts constituted the provision of an 'economic advantage' and the value of that advantage was potentially material to inter-State trade (a benchmark for materiality in this context is the European Commission's State aid *de minimis* threshold of €200,000). There would be no such advantage if the contracts were concluded on market terms. NRW considers that the contracts were on market terms but it is apparent from the contemporaneous documents that the terms of the contracts were not determined either by the outcome of a competition for meeting NRW's relevant requirements, or by other relevant market testing focused upon those requirements.

22. In my view, NRW's decision to award the contracts to the sawmill operator was not informed by relevant market testing, and was also not supported by persuasive reasoning to support a conclusion that seeking alternative providers would inevitably have proved fruitless. In my view, NRW failed to follow appropriate processes for ensuring that the outputs for which it contracted with the sawmill operator were obtained on market terms. This failure gives rise to doubt as to the compliance of the contracts with the State aid rules. In view of this uncertainty, I am unable to give an unqualified regularity opinion on the financial statements. I note that NRW disagrees with my analysis of the State aid position and relies on legal advice (which it sought during the course of my audit and shared with me) to the effect that among other things, the award complied with State aid rules.
23. The Chief Executive of Natural Resources Wales has told me that he considers that qualification of the regularity opinion is disproportionate to the shortcomings identified and that he disagrees with my conclusions and relies on legal advice which NRW sought during the course of my audit. However, I have sought my own legal advice from Counsel (including in relation to NRW's legal advice) and I agree with the advice I have received, which is to the effect that there is insufficient evidence to conclude that the decision-making process was in compliance with public law principles and State aid rules. The significant uncertainty which exists means that I consider the correct and proportionate action for me to take as the auditor of NRW is to qualify my regularity opinion.

FINANCIAL STATEMENTS and NOTES TO THE ACCOUNTS

for 2015/16

Statement of Comprehensive Net Expenditure

For the year ended 31 March 2016

	Note	2015/16 £'000	2014/15 £'000
Staff costs	3	81,239	80,155
Capital works expensed in year	4	14,834	15,518
Other expenditure	5	92,737	102,427
Total operating expenditure		<u>188,810</u>	<u>198,100</u>
Charge income	6	(36,969)	(38,027)
Commercial and other income	6	(27,735)	(28,726)
European and other external funding	6	(1,540)	(2,287)
Total operating income		<u>(66,244)</u>	<u>(69,040)</u>
Net operating expenditure		<u>122,566</u>	<u>129,060</u>
Financing on pension scheme assets and liabilities	13.3	2,439	2,116
Net expenditure for the year		<u>125,005</u>	<u>131,176</u>
Other comprehensive net expenditure			
Net gain from transfer of functions	1.6	(275)	0
Pension actuarial remeasurements	13.3	(33,179)	24,778
Revaluation			
Net loss / (gain) on revaluation		15,996	(19,996)
Total comprehensive net expenditure for the year		<u><u>107,547</u></u>	<u><u>135,958</u></u>

The notes on pages 53 to 81 form part of these accounts.

Statement of Financial Position

As at 31 March 2016

		31 March 2016	31 March 2015
	Note	£'000	£'000
Non-current assets			
Property plant and equipment	7.1	752,001	644,900
Heritage assets	7.1	6,432	6,432
Biological assets	7.1	102,450	117,881
Intangible assets	7.2	13,340	8,397
Financial assets		140	220
Total non-current assets		<u>874,363</u>	<u>777,830</u>
Current assets			
Assets held for sale		180	979
Inventories		759	835
Trade and other receivables	9	16,496	17,460
Cash and cash equivalents	10	22,735	26,798
Total current assets		<u>40,170</u>	<u>46,072</u>
Total assets		<u>914,533</u>	<u>823,902</u>
Current liabilities			
Trade and other payables	11	(19,568)	(25,911)
Provisions	12	(1,582)	(2,955)
Total current liabilities		<u>(21,150)</u>	<u>(28,866)</u>
Assets less current liabilities		<u>893,383</u>	<u>795,036</u>
Non-current liabilities			
Pension liabilities	13.3	(46,957)	(76,104)
Financial liabilities	8	(39,991)	(39,973)
Total non-current liabilities		<u>(86,948)</u>	<u>(116,077)</u>
Assets less liabilities		<u>806,435</u>	<u>678,959</u>
Taxpayers' equity and other reserves			
General fund	SoCTE	197,532	211,460
Revaluation reserve	SoCTE	655,860	543,603
Pensions reserve	SoCTE	(46,957)	(76,104)
Total taxpayers' equity		<u>806,435</u>	<u>678,959</u>

The notes on pages 53 to 81 form part of these accounts.

Dr Emyr Roberts
Chief Executive & Accounting Officer

Date: 2nd March 2017

Statement of Cash Flows

For the year ended 31 March 2016

	Note	2015/16 £'000	2014/15 £'000
Cash flows from operating activities			
Net operating expenditure	SoCNE	(122,566)	(129,060)
Adjustment for non-cash transactions		17,902	15,245
(Increase)/Decrease in trade and other receivables	9	802	1,865
Increase/(Decrease) in trade and other payables	11	(8,112)	8,199
Increase/(Decrease) in provisions	12	(1,356)	861
Net cash flow from operating activities		<u>(113,330)</u>	<u>(102,890)</u>
Cash flows from investing activities			
Purchase of property, plant and equipment	7.1	(2,606)	(7,457)
Purchase of intangible assets	7.2	(6,627)	(2,934)
Proceeds on disposal of property, plant and equipment		1,130	631
Net cash flow from investing activities		<u>(8,103)</u>	<u>(9,760)</u>
Cash flows from financing activities			
Cash receipt on transfer of functions	1.6	927	0
Grants from Welsh Government	SoCTE	116,443	124,337
Net Financing		<u>117,370</u>	<u>124,337</u>
Net increase in cash and cash equivalents in the period		(4,063)	11,687
Cash and cash equivalents at the beginning of the period		<u>26,798</u>	<u>15,111</u>
Cash and cash equivalents at the end of the period	10	<u><u>22,735</u></u>	<u><u>26,798</u></u>

The notes on pages 53 to 81 form part of these accounts.

Statement of Changes in Taxpayers' Equity

For the year ended 31 March 2016

	General Fund £'000	Revaluation Reserve £'000	Pension Reserve £'000	Total £'000
Opening balance	211,460	543,603	(76,104)	678,959
Comprehensive net expenditure for year	(107,547)	0	0	(107,547)
Transfer of function adjustment	(359)	0	(1,348)	(1,707)
In-year movement				
In year revaluation	0	120,287	0	120,287
Realised revaluation	8,030	(8,030)	0	0
Actuarial gain on pension scheme	(33,179)	0	33,179	0
Increase in pension liability	2,684	0	(2,684)	0
Total in-year movement	(22,465)	112,257	30,495	120,287
Funding				
Grants from Welsh Government	116,443	0	0	116,443
Balance at 31 March 2016	197,532	655,860	(46,957)	806,435

General fund - reflects the cumulative position of net expenditure and funding from Welsh Government.
 Revaluation reserve - reflects the cumulative balance of revaluation and indexation of non-current assets.
 Pension reserve - reflects the cumulative position of the net liabilities of the pension scheme.

The notes on pages 53 to 81 form part of these accounts.

Comparative figures for the year ended 31 March 2015

	General Fund £'000	Revaluation Reserve £'000	Pension Reserve £'000	Total £'000
Opening Balance	188,256	511,056	(49,200)	650,112
Comprehensive net expenditure for year	(135,958)	0	0	(135,958)
In Year Movement				
Opening balance correction	183	(183)	0	0
Assets from previous years	160	0	0	160
In year revaluation	0	40,308	0	40,308
Realised revaluation	7,578	(7,578)	0	0
Actuarial loss on pension scheme	24,778	0	(24,778)	0
Increase in pension liability	2,126	0	(2,126)	0
Total in-year movement	34,825	32,547	(26,904)	40,468
Funding				
Grants from Welsh Government	124,337	0	0	124,337
Balance at 31 March 2015	211,460	543,603	(76,104)	678,959

Note 1 Accounting policies

1.1 Requirement to prepare accounts

The financial statements have been prepared in accordance with the 2015/16 Government Financial Reporting Manual (FReM) issued by HM Treasury and with the accounts direction given by the Welsh Government in accordance with paragraph 23(1) of the Natural Resources Body for Wales (Establishment) Order 2012.

The accounting policies contained in the FReM apply International Financial Reporting Standards (IFRS) as adapted or interpreted for the public sector context. Where the FReM allows a choice of accounting policy, these accounts follow the policy which is most appropriate to give a true and fair view for Natural Resources Wales (NRW).

The policies adopted are described below and in the various notes to the accounts. They have been applied consistently in dealing with items considered material to the accounts.

The preparation of financial statements requires various estimates and assumptions to be made that affect the application of accounting policies and reported amounts. All such estimates and judgments are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future period affected. All estimates are based on knowledge of current facts and circumstances, assumptions concerning past events and forecasts of future events.

The most significant areas of estimation and critical judgements are shown against the relevant notes. Please note that the actual future results may differ from these estimates.

1.2 Accounting convention

These accounts have been prepared on an accruals basis, under the historical cost convention, modified to account for the revaluation of property, plant and equipment, intangible assets (apart from vehicles and assets under construction) to fair value as determined by the relevant accounting standard.

These financial statements are based on the going concern principle.

1.3 Income, expenditure and grants

The accruals basis of accounting means that income and expenditure disclosed in the accounts are accounted for in the year that it takes place, not when cash payments are made or received, apart from option fees income received from windfarm operators which is included in the year in which it is received. The full value of windfarm option fees is shown within renewable energy income in note 6, and the net payment to Welsh Government included in operational costs in note 5.

Income received in advance of the work being done is treated as deferred income.

Where income and expenditure have been recognised but cash has not been received or paid, a payable or receivable for the relevant amount is recorded in the Statement of Financial Position. Where debts may not be settled, the balance of receivables is written down and a charge made to the Statement of Comprehensive Net Expenditure for the income that might not be collected.

All grant contributions received have been recognised as income within the Statement of Comprehensive Net Expenditure.

1.4 Value added tax

NRW is classified as a body to which section 33 of the Value Added Tax (VAT) Act 1994 applies and accordingly recovers tax paid on both business and non-business activities. The recovery of VAT on exempt supplies is dependent on the threshold for exempt activities. In all instances, where output tax is charged, or input tax is recoverable, the amounts included in these accounts are stated net of VAT.

1.5 Grant in aid

Grant in aid and other grants received from Welsh Government are treated as financing received from a controlling party and are credited directly to the general fund.

1.6 Internal drainage districts and transfer of functions

On 1st April 2015 the functions, staff and assets of the Caldicot & Wentlooge, Lower Wye and Powysland internal drainage boards transferred to NRW. In accordance with the FReM, this transfer will be accounted for as a transfer by absorption and as such, there is no requirement to restate comparatives in primary statements nor adjust the carrying values of assets and liabilities to fair value. The net assets of £275k will be recorded through the Statement of Comprehensive Net Expenditure as a net gain from the transfer of functions. Adjustments of £84k required to achieve uniformity of accounting policies are shown against the general fund.

Analysis of gain on transfer of functions

	£'000
Non-current assets	777
Other assets	83
Cash	927
Pension liabilities	(1,221)
Other liabilities	(291)
Total	<u>275</u>

NRW now acts as the drainage board that runs these internal drainage districts, along with eleven other internal drainage districts located in North Wales. The work undertaken in each district is funded by a combination of drainage rates levied on occupiers of agricultural land and special levies paid by local authorities in respect of non-agricultural land.

NRW is required by section 40 of the Land Drainage Act 1991 to set drainage rates, and by regulation 7 of the Internal Drainage Boards (Finance) Regulations 1992 to issue special levies before the 15th February of the financial year preceding the year to which they relate.

The three internal drainage boards approved the work programmes and associated drainage rates and special levies for 2015/16 that NRW inherited. The drainage rates, special levies and precepts for 2015/16, in relation to the existing eleven internal drainage districts were set by NRW, acting as the drainage board. This income is included in Note 6.

1.7 Adoption of new and revised IFRS or FReM interpretations

FReM

Every year HM Treasury issues a new FReM which interprets IFRS for the public sector. The form and content of the annual report and accounts for 2015/16 has been changed in line with the amendments made to the FReM reflecting the outcomes of the Simplification and Streamlining Statutory Annual Report and Accounts project. The main changes include the introduction of three parts to the Annual Report and Accounts and the requirement to disclose policies and notes for material items only. Categories within statements and notes have been merged where appropriate, and figures for 2014/15 restated accordingly.

IFRS

In accordance with IAS 8, NRW has considered the impact of standards and interpretations which have been issued but are not yet effective and which have not been adopted early by NRW. With the exception of IFRS 16 Leases, it is anticipated that the adoption of these Standards and Interpretations in future periods will have no material impact on the financial statements of NRW. The impact of IFRS 16 Leases which has been issued by the IASB but not yet been adopted by the European Union and will apply from 2019-20, can not be estimated at this stage.

1.8 Financial provisions (Landfill sites)

For all landfill sites, financial provision arrangements need to be established before a permit is granted. The financial provision arrangements must be in place prior to the commencement of disposal operations, and such provisions need to be sufficient (in monetary terms), secure and available when required. Landfill sites include all waste sites that are subject to the landfill directive.

The following are the principal mechanisms that NRW will accept for demonstrating financial provision arrangements:

- Renewable bonds (shown in note 11)
- Cash deposits with NRW (shown in note 11)
- Escrow accounts
- Local authority deed agreements
- Parent company guarantees
- Umbrella agreements (covering a number of sites)

1.9 Notes to the accounts

Note 2 provides an analysis of income and expenditure to operating segments.

Notes 3 to 13 provide analysis of material figures reported in the statements of comprehensive net expenditure, financial position and cash flows.

Notes 14 to 20 relate to figures not disclosed elsewhere in these accounts.

2. Analysis of net operating expenditure by segment

For year to 31 March 2016

	Transformation	OD & People Management	Finance & Corporate Services	National Services	Operations North & Mid Wales	Operations South	Knowledge Strategy & Planning	Chief Executive, Governance & Planning	External Relations & Communications	Chief Information Officer	Centrally Controlled	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Reported by segments												
Expenditure	956	2,467	18,873	44,907	27,909	33,041	27,117	3,584	980	12,725	16,251	188,810
Income	0	0	(36,216)	(23,278)	(4,019)	(2,893)	(1,877)	0	0	(27)	2,066	(66,244)
Total	956	2,467	(17,343)	21,629	23,890	30,148	25,240	3,584	980	12,698	18,317	122,566
Capital expenditure	0	0	703	1,820	358	320	4	0	0	6,207	9	9,421

These segments are components for which financial information is managed and reported internally. Income and expenditure shown above were directly attributed to the segments

Description of segments

Transformation	Manages the transformational programmes for NRW to enable us to be self sufficient.
OD & People Management	Provides organisational development and staff resource management.
Finance & Corporate Services	Provides financial and procurement support. Manages Natural Resources Wales's buildings and fleet.
National Services	Delivers a range of services for whole of Wales. There include flood and coastal risk management, capital programme management, forestry harvesting and the customer contact centre.
Operations North & Mid Wales	Delivers statutory purposes and aspirations, at an operational level and via a network of local teams, within the seven counties of North Wales, Ceredigion and the Montgomery and Radnor areas of Powys.
Operations South	Delivers statutory purposes and aspirations, at an operational level and via a network of local teams, within the counties of South Wales and the Brecknockshire area of Powys.
Knowledge Strategy & Planning	Manages the strategic, environmental and spatial planning functions.
Chief Executive, Governance & Planning	The Chief Executive is also the Accounting Officer and is personally responsible for the proper stewardship of the public funds within his charge, for the day-to-day operations and management of the NRW. Governance provides and delivers legal services; planning, performance & reporting; audit & risk assurance and secretariat and information governance.
External Relations & Communications	External Relations and Communications provide an integrated communications and marketing service.
Chief information officer	Delivers ICT 'business as usual' services and transformation services.
Centrally Controlled	Income and expenditure controlled centrally and not allocated to directorates. It includes depreciation, book value of fellings, year end accruals for provisions.

In 2015/16 the ICT Service was transferred from Finance and Corporate Services to Chief Information Officer.

Analysis of net operating expenditure by segment (continued)

Comparatives for year to 31 March 2015

	Transition	OD & People Management	Finance & Corporate Services	National Services	Operations North & Mid Wales	Operations South	Knowledge Strategy & Planning	Chief Executive, Governance & Planning	External Relations & Communications	Centrally Controlled	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Reported by segments											
Expenditure	6,435	5,529	31,323	44,004	25,603	32,275	28,864	3,847	1,073	19,147	198,100
Income	0	0	(36,081)	(25,269)	(3,132)	(1,643)	(2,998)	(354)	0	437	(69,040)
Total	6,435	5,529	(4,758)	18,735	22,471	30,632	25,866	3,493	1,073	19,584	129,060
Capital Expenditure	6,874	0	1,501	1,673	217	409	0	0	0	0	10,674

3 Staff costs

Details of staff costs and numbers are now disclosed in the Accountability section on page 36.

4. Capital works expensed in year

	2015/16	2014/15	31 March 2016	31 March 2015
Categories	Actual £'000	Actual £'000	Committed £'000	Committed £'000
Operational Work	13,368	13,480	2,304	6,486
Capital grants	1,466	2,038	1,481	0
Total	14,834	15,518	3,785	6,486

Capital works expensed in year relates to expenditure which is capital in nature but where NRW does not retain the related risks and rewards of ownership or cannot reliably estimate the useful life of the asset. This includes items such as :

- Flood defence assets built on land which is not owned by NRW but where it has permissive powers to maintain the defence.
- Assets where it is not possible to check for impairment, for example beach replenishment, so it is more prudent to write the asset off in year.

Operational work includes:

- Work to ensure that the condition of the flood defences are retained in the appropriate condition and restored to that condition as necessary.
- Creation, improvement or heightening of embankments along watercourses to reduce the risk of the water escaping from the river channel.
- Production of multi-layered maps which provide information on flooding from groundwater, rivers and the sea for Wales, and including information on flood defences and the areas benefiting from those flood defences.
- Installation of piles along the river banks to strengthen them and secure the adjacent land and prevent landslips into the river causing obstructions. These works would largely be below ground.
- Repairing or replacing culverts under land, roads and properties and channel improvements that assist the flow of watercourses.
- Development of strategies to provide long term flood risk options to cover a large area. It is from the long term strategies that individual flood risk projects are developed.
- Preparation of Water Level Management Plans and Catchment Flood Management Plans, improvements to locks and other waterways, telemetry replacement and fish habitats improvement.

Capital grants

These are grants, mostly to Local Authorities, which fund work of a capital nature. It includes work on the Wales Coast Path, the Right of Way Improvement Programme, and also grants to assist with purchase of land.

5. Other expenditure

	2015/16 £'000	2014/15 £'000
Cash items		
Bought in services	20,324	18,919
Service levels agreements	9,535	14,607
Reservoir operating agreements	6,892	6,938
Grants	5,384	8,222
Materials and equipment	4,073	2,931
Forest roads network maintenance	3,955	3,365
Office running costs	3,871	5,010
Operational costs	3,609	3,686
ICT costs	3,086	6,222
Collaborative agreements	2,894	2,899
Fleet costs	2,794	3,613
Travel and subsistence	2,360	3,077
Staff related costs	2,026	1,639
Rents	2,007	1,938
Fees and court costs	852	1,103
Rates	795	780
Statutory audit fees	143	171
Write-offs and special payments	57	498
Finance lease interest	51	40
European grants	33	474
Donations	0	5
Sub-total	74,741	86,137
Non-cash expenditure		
Depreciation and amortisation	9,787	7,211
Value of felled trees	6,970	6,644
Prior year expenditure on assets	794	801
Write-offs	793	642
Asset review adjustments	85	626
Movement on provision for doubtful debt	57	(427)
Movement on other provisions	(17)	1,072
(Gain) / Loss on disposal	(473)	(279)
Sub-total	17,996	16,290
Total	92,737	102,427

Details of write-offs and special payments are now shown in the Accountability section on page 40.

6. Income analysis

	2015/16 £'000	2014/15 £'000
Abstraction charges	18,797	20,434
Environmental permitting regulations: water quality	6,272	6,523
Environmental permitting regulations: installations	3,033	3,028
Environmental permitting regulations: waste	2,183	2,432
Nuclear regulation	1,765	1,336
Fishing licences	1,380	1,468
Other environmental protection charges	1,218	917
Hazardous waste	1,013	981
Water resources rechargeable works	675	453
Marine licensing	322	184
Emissions trading and carbon reduction commitment	311	271
Charge Income	36,969	38,027
Timber income	16,475	16,336
Renewable energy income	4,927	7,522
Income from estates	2,917	2,512
Internal drainage district income	1,401	472
Provision of information and services	923	1,194
Legal costs recovered and Proceeds of Crime Act income	589	468
Income towards site clean up costs	500	0
Interest receivable	55	41
Miscellaneous income	(52)	181
Commercial and other income	27,735	28,726
European income ⁺	792	2,080
Grants and contributions	748	207
European and other external funding	1,540	2,287
Total income	66,244	69,040

+ Including income claimed via Welsh European Funding Office or the Welsh Government for european funded projects.

6.1 Analysis of fees and charges

Year ending 31 March 2016	Income billed £'000	Expenditure £'000	Surplus/ (Deficit) £'000
Abstraction charges	17,613	18,797	(1,184)
Environmental permitting regulations: water quality	6,506	6,272	234
Environmental permitting regulations: installations	3,380	3,033	347
Environmental permitting regulations: waste	2,111	2,183	(72)
Nuclear regulation	1,709	1,765	(56)
Fishing licences	1,380	1,380	0
Other environmental protection charges	1,002	1,218	(216)
Hazardous waste	959	1,013	(54)
Water resources rechargeable works	675	675	0
Marine licences	322	322	0
Emissions trading and carbon reduction commitment	298	311	(13)
Total	35,955	36,969	(1,014)

Comparative figures - year ending 31 March 2015	Income billed £'000	Expenditure £'000	Surplus/ (Deficit) £'000
Abstraction charges	20,225	20,434	(209)
Environmental permitting regulations: water quality	6,562	6,523	39
Environmental permitting regulations: installations	2,946	2,939	7
Environmental permitting regulations: waste	2,319	2,432	(113)
Nuclear regulation	1,600	1,336	264
Fishing licences	1,468	1,468	0
Other environmental protection charges	828	917	(89)
Hazardous waste	1,101	981	120
Water resources rechargeable works	453	453	0
Marine licences	184	499	(315)
Emissions trading and carbon reduction commitment	271	271	0
Total	37,957	38,253	(296)

Income from charges for the regulation of businesses in Wales to monitor and control their impact on the environment, whether air, water or land, is derived from a combination of fees and charges.

Accumulated surpluses and deficits are treated as deferred income or accrued income depending on whether the charging scheme is in surplus or deficit. These balances are only treated as deferred or accrued income where there is an expectation that the balances will be recoverable over a reasonable period of time. The balances are considered when setting future years' fees and charges, to enable a break even position to be achieved over a reasonable time period, which is currently considered to be three years.

The above table of fees and charges differs from income reported in note 6 due to the policy stated above. The cumulative surpluses and deficits are included in accrued and deferred income in notes 9 and 11 respectively.

Costs funded by grant-in-aid have been excluded from the table above. The above table does not include the effect of IAS 19 pension adjustments as these costs/benefits are not passed on to charge payers. The financial objective is full cost recovery including current cost deciation and a rate of return on relevant assets.

The key activities of each area are listed below:

- Abstraction charges – charging for businesses using water abstraction from rivers or groundwater. The income reported also includes other elements of water resources income.
- Water resources rechargeable works - income to recover NRW water resources effort on the ground, such as operational costs in the Upper Severn catchment (on the welsh side of the boundary), which falls under Environment Agency jurisdiction.
- Fishing licences – charging individuals for licences to fish.
- Environmental permitting regulations: water quality – charging for discharges from businesses into the environment.
- Environmental permitting regulations: installations - permitting to control and minimize pollution from industrial activities
- Environmental permitting regulations: waste – waste management licensing and exemptions.
- Hazardous waste – licensing for producing, transporting, or receiving hazardous waste.
- Emissions trading and carbon reduction commitment – regulation of businesses under EU schemes.
- Nuclear regulation – regulation of nuclear and non-nuclear sites, and nuclear new build sites.
- Marine licences – charging individuals for boat licences.
- Other environmental protection – licensing for registration of waste carriers and brokers, transfrontier shipments, producer responsibility licensing for waste electronic and electrical equipment , end of life vehicles, polychlorinated biphenyls and regulation of businesses under such schemes as control of major accident hazards.

7. Non-current assets

There are two categories of non-current assets - tangible assets shown in Note 7.1 and intangible assets shown in Note 7.2.

Recognition

All land is capitalised regardless of value. The threshold for capitalising other assets with a useful economic life of more than one year is £5,000. Individual items costing less than £5,000 can be grouped as one asset if the total cost exceeds £5,000 and these assets operate as part of a network. Subsequent expenditure on an asset is capitalised if the criteria for initial capitalisation are met, it is probable that additional economic benefits will flow to NRW and the cost of the expenditure can be reliably measured.

Measurement

All non-current assets apart from heritage assets and assets under construction are reported at either current value in existing use or fair value in the Statement of Financial Position.

Assets classified as heritage assets comprise land within designated conservation areas. This land is held in support of NRW's purpose. Because of the diverse nature of the land held and the lack of comparable market values, NRW considers that obtaining external valuations would involve disproportionate cost. Heritage assets are therefore held at cost. Preservation costs (expenditure required to preserve the heritage asset) are recognised in the Statement of Comprehensive Net Expenditure when they are incurred. Further information on heritage assets can be found in Note 7.1.2.

Assets capitalised as under construction are carried at cost and transferred to the appropriate non-current asset category when completed and ready for use.

Indexation and Revaluation

All assets apart from heritage assets, vehicles and those under construction are indexed annually using an appropriate index under the modified historical cost convention.

Land and buildings and public structures (reported within operational structures) are subject to professional revaluation every five years in accordance with the Royal Institution of Chartered Surveyors (RICS) valuation standards. These assets were professionally revalued at 31st March 2016 by chartered surveyors and signed off by a registered valuer. The chartered surveyors were John Clegg & Co, Cooke and Arkwright, Lambert Smith Hampton, Llewellyn Humphreys, Williams Rural & Commercial, Strutt & Parker, Bidwells and internal land agents.

All valuers who undertook the quinquennial revaluation, are members of the RICS and are Registered Valuers in accordance with the RICS Valuer Registration Scheme, apart from those valuers who have undertaken certain infrastructure valuations on heritage assets. Those valuations have been quality assured by the NRW Principal Surveyor. All valuers have sufficient current local and national knowledge of the particular market, and the skills and understanding to undertake the valuation competently.

All our freehold and leasehold offices commercial properties were valued on 31st March 2016 by external valuers, Elizabeth Hill and Alan Jones of Cooke & Arkwright Chartered Surveyors.

The valuations of other land, public structures and specialist assets were arranged by our in-house team of Chartered Surveyors, under the direction of the Principal Surveyor.

For those assets where we have future rental income on our land we used external professional surveyors. Cefn Croes Windfarm was valued by Bidwells and the telecommunications portfolio by Strutt & Parker.

For specialised assets where there are no market comparables, the estimate of 'fair value' has been estimated using a depreciated replacement cost approach.

Operational structures are used in NRW's service delivery and are specific in nature, location or function. It is not possible to revalue these assets effectively using market comparatives or professional valuations.

Adjustments arising from indexation and revaluations are taken to the revaluation reserve unless the reserve balance in respect of a particular asset has been fully utilised against downward revaluation, in which case the movement is recognised in the Statement of Comprehensive Net Expenditure. Any permanent reductions in value are transferred to the Statement of Comprehensive Net Expenditure.

Depreciation

Land is not depreciated, unless it forms an essential element of an operational structure. These assets are being depreciated over the life of the relevant operational structure. Assets under construction are not depreciated until they are capable of operating in the manner intended by management.

Vehicles shown in the plant and machinery category are depreciated on a reducing balance basis at a rate of 21%. All other assets are depreciated/amortised on a straight line basis over their expected useful economic life. Depreciation is charged in the month of disposal to the Statement of Comprehensive Expenditure, but not in the month of acquisition.

The estimated asset lives are reviewed, and adjusted if appropriate, at each reporting date. The principal economic lives used for depreciation purposes are:

Asset category	Principal economic life
Tangible assets	
Operational structures	5 - 100 years
Buildings and dwellings	10 - 60 years
Plant and machinery	4 - 25 years
Information technology	3 - 10 years
Intangible assets	
Software licences	5 - 25 years
Other licences	5 - 100 years
Software development	3 - 10 years

The range in the economic lives reflects the variety of assets within the asset categories.

Disposals

When an asset is disposed of, its carrying amount is written off to the Statement of Comprehensive Net Expenditure as part of the gain or loss on disposal. Receipts from disposals (if any) are also credited to the same line. Any revaluation gains accumulated for the asset in the Revaluation Reserve are transferred to the General Fund.

Revaluation Reserve

The revaluation reserve shows the gains made by NRW arising from increases in the value of non-current assets. The balance is reduced when assets with accumulated gains are:

- Revalued downwards or impaired and the gains are lost.
- Used in the provision of services and the gains are consumed through depreciation.
- Disposed of and the gains are realised.

An amount representing the difference between the depreciation charged on the revalued assets and that which would have been charged if the assets were shown at cost is transferred from the revaluation reserve to the general fund.

Impairment

Non-current assets are subject to annual impairment reviews. Impairments are recognised when the recoverable amount of non-current assets falls below their net book value, as a result of either a fall in value owing to market conditions or a loss in economic benefit. Downward revaluations resulting from changes in market value only result in an impairment where the asset is revalued below its historical cost carrying amount. The FReM requires that the effect of downward revaluation is firstly set against any accumulated balance in the revaluation reserve. Any amount in addition to this is recognised as impairment through the Statement of Comprehensive Net Expenditure. Any loss of economic benefit is recognised in full against expenditure. An amount to the value of the impairment is transferred from the revaluation reserve to the general fund for the individual assets concerned.

Non-current assets held for sale

Non-current assets are classified as held for sale if the carrying amount will be recovered principally through a sale transaction rather than through continuing use. Depreciation ceases immediately on the classification of the assets as being held for sale. They are stated at the lower of their carrying amount and fair value less costs to sell. They are recorded as current assets in the Statement of Financial Position.

Non-current assets are only deemed to be assets held for sale if management is committed to a plan to sell and if the asset is being actively marketed in its present condition at a price which is reasonable in relation to its current condition.

7.1 Tangible non-current assets

	Forest estate	Other land	Buildings	Plant and machinery	Information technology	Operational structures	Assets under construction	Total Property Plant & Equipment	Biological assets	Heritage assets	Total Tangible Assets
Cost or Valuation	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
At 1 April 2015	524,297	39,657	20,881	23,756	13,912	58,909	3,025	684,437	117,881	6,432	808,750
Additions from transfer of function	0	152	364	758	19	180	0	1,473	0	0	1,473
Additions	0	206	0	140	0	21	2,427	2,794	0	0	2,794
Assets commissioned in year	0	101	0	1,213	0	566	(1,880)	0	0	0	0
Asset review adjustments and write-offs	0	(95)	0	(238)	(1,195)	(540)	0	(2,068)	0	0	(2,068)
Prior year costs expensed	0	0	0	0	0	(436)	(387)	(823)	0	0	(823)
Disposals	(33)	(469)	(225)	(1,272)	(19)	0	0	(2,018)	0	0	(2,018)
Movement from/(to) held for sale	9	788	0	0	0	0	0	797	0	0	797
Fellings	(5,072)	0	0	0	0	0	0	(5,072)	(1,822)	0	(6,894)
Indexation and revaluation	92,602	12,556	(8,274)	16	177	9,283	0	106,360	(13,609)	0	92,751
Reclassification	0	1,022	36	0	0	(329)	0	729	0	0	729
At 31 March 2016	611,803	53,918	12,782	24,373	12,894	67,654	3,185	786,609	102,450	6,432	895,491
Depreciation											
At 1 April 2015	0	0	5,320	16,245	3,299	14,673	0	39,537	0	0	39,537
Additions from transfer of function	0	0	193	516	14	57	0	780	0	0	780
Charged in year	0	0	644	2,187	3,858	1,751	0	8,440	0	0	8,440
Asset review adjustments and write-offs	0	0	0	(208)	(1,172)	(156)	0	(1,536)	0	0	(1,536)
Prior year costs expensed	0	0	0	0	0	(48)	0	(48)	0	0	(48)
Disposals	0	0	(191)	(1,161)	(15)	0	0	(1,367)	0	0	(1,367)
Indexation and revaluation	0	0	(5,718)	7	79	(5,566)	0	(11,198)	0	0	(11,198)
Reclassification	0	0	67	0	0	(67)	0	0	0	0	0
At 31 March 2016	0	0	315	17,586	6,063	10,644	0	34,608	0	0	34,608
Carrying amount at 1 April 2015	524,297	39,657	15,561	7,511	10,613	44,236	3,025	644,900	117,881	6,432	769,213
Carrying amount at 31 March 2016	611,803	53,918	12,467	6,787	6,831	57,010	3,185	752,001	102,450	6,432	860,883
Asset Financing											
Owned	568,985	49,516	12,467	6,120	6,831	57,010	3,185	704,114	102,450	6,432	812,996
Leased	42,818	4,402	0	667	0	0	0	47,887	0	0	47,887
Carrying amount at 31 March 2016	611,803	53,918	12,467	6,787	6,831	57,010	3,185	752,001	102,450	6,432	860,883

Buildings include dwellings with a carrying amount of £350k. Our other buildings are offices and workbases.

Comparative figures for period to 31 March 2015

	Forest estate	Other land	Buildings	Plant and machinery	Information technology	Operational structures	Assets under construction	Total Property Plant & Equipment	Biological assets	Heritage assets	Total Tangible Assets
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Cost or Valuation											
At 1 April 2014	495,112	39,442	18,897	23,242	3,327	52,859	11,401	644,280	100,051	6,432	750,763
Adjustment to opening balance	0	(8)	0	(6)	0	0	(1)	(15)	0	0	(15)
Additions from verification	0	160	0	0	0	0	0	160	0	0	160
Additions	0	73	0	1,077	4,059	140	2,108	7,457	0	0	7,457
Assets commissioned in year	0	8	0	851	6,509	2,908	(10,276)	0	0	0	0
Asset review adjustments and write-offs	0	(39)	(142)	(1,099)	(112)	(405)	0	(1,797)	0	0	(1,797)
Prior year costs expensed	0	(129)	0	0	0	(75)	(189)	(393)	0	0	(393)
Disposals	(9)	(53)	0	(243)	0	(45)	(18)	(368)	(3)	0	(371)
Reclassified as held for sale	(9)	(969)	0	0	0	0	0	(978)	0	0	(978)
Fellings	(5,200)	0	0	0	0	0	0	(5,200)	(1,868)	0	(7,068)
Indexation	34,403	1,361	1,045	(75)	138	4,612	0	41,484	19,701	0	61,185
Reclassification	0	(189)	1,081	9	(9)	(1,085)	0	(193)	0	0	(193)
At 31 March 2015	524,297	39,657	20,881	23,756	13,912	58,909	3,025	684,437	117,881	6,432	808,750
Depreciation											
At 1 April 2014	0	0	4,157	14,820	2,257	12,507	0	33,741	0	0	33,741
Adjustment to opening balance	0	0	0	(6)	0	0	0	(6)	0	0	(6)
Charged in year	0	0	681	2,545	1,125	1,636	0	5,987	0	0	5,987
Asset review adjustments and write-offs	0	0	(142)	(869)	(108)	(89)	0	(1,208)	0	0	(1,208)
Disposals	0	0	0	(199)	0	(9)	0	(208)	0	0	(208)
Indexation	0	0	217	(46)	25	1,035	0	1,231	0	0	1,231
Reclassification	0	0	407	0	0	(407)	0	0	0	0	0
At 31 March 2015	0	0	5,320	16,245	3,299	14,673	0	39,537	0	0	39,537
Carrying amount at 1 April 2014	495,112	39,442	14,740	8,422	1,070	40,352	11,401	610,539	100,051	6,432	717,022
Carrying amount at 31 March 2015	524,297	39,657	15,561	7,511	10,613	44,236	3,025	644,900	117,881	6,432	769,213
Asset Financing											
Owned	508,915	36,429	15,561	6,519	10,613	44,236	3,025	625,298	117,881	6,432	749,611
Leased	15,382	3,228	0	992	0	0	0	19,602	0	0	19,602
Carrying amount at 31 March 2015	524,297	39,657	15,561	7,511	10,613	44,236	3,025	644,900	117,881	6,432	769,213

Buildings include dwellings with a carrying amount of £416k. Our other buildings are offices and workbases.

7.1.1 Forest estate

Legal ownership of the Welsh Government Woodland Estate is vested with the Welsh Ministers. It is included in Natural Resources Wales' Statement of Financial Position as it carries the financial risks and rewards associated with the estate and undertakes all estate management activities. The estate comprise land and growing timber. Legal ownership of timber, including uncut trees, is vested in Natural Resources Wales.

Woodlands and forests are primarily held and managed to meet the sustainable forest management objectives set out in Woodlands for Wales (The Welsh Government's strategy for woodlands and trees). Their purpose can be split between economic (contribution to a thriving and sustainable Welsh economy) and other (social, environmental, climate change). Under International Accounting Standard 41 (Agriculture), timber grown for economic purpose must be classified as biological assets. The rest of the timber, together with all underlying land, is classified as property, plant and equipment and referred to as the forest estate.

Assets in both categories are shown at fair value. External professional valuers undertake a valuation of the estate at five yearly intervals. John Clegg & Co were appointed as valuers for the last valuation as at 31 March 2016. In accordance with the Royal Institution of Chartered Surveyors (RICS)'s Appraisal and Valuation Standards (the Red Book), the estate is valued as appropriate for obtaining a fair value. In the intervening years, custom indices are used to restate values. Natural Resources Wales and its external professional valuers have developed processes, including key assumptions, which produce a reasonable estimate of a compliant valuation.

Adjustments arising from revaluation of the forest estate are taken to the revaluation reserve and released to General Fund when gains are realised in the felling of trees. Adjustments arising from revaluation of biological assets are recognised in the Statement of Comprehensive Net Expenditure in the year of revaluation.

Estimation techniques, assumptions and judgements

Elements of the valuation and therefore the accounting for these assets rely on estimation techniques.

It is not considered cost effective to carry out a quinquennial external professional valuation covering all areas of woodland. Following advice from qualified valuers, it is deemed that a reasonable valuation can be derived by carrying out on-site valuations of a random sample of sites representing between eight and ten per cent of the estate then extrapolating these for the whole, and using the factors of location, species, age and quality (yield class) of the trees.

It is also considered that the most appropriate market-based evidence of value is derived from the market for the sale of woodlands and forests over fifty hectares in area. It is recognised that even so there can still be a wide spread of values and these can be somewhat subjective judgements. Thus any valuation of woods will have a degree of reliance on professional opinion. The external valuers subsequently apportion values to land and timber. The value of leasehold land is estimated to be 15% less than freehold land.

The apportionment of trees between biological assets and property, plant and equipment was carried out by Natural Resources Wales staff using judgements and estimates. An assessment was made of the proportion primarily held for economic purposes and the resulting percentage was used to determine the value of trees classed as a biological asset. Should there be an acquisition or disposal of land that would create a total change in our forest estate land holding of ten per cent or more, an interim review of the assessment would take place. There was no such change during the period ending 31 March 2016. The percentage split is currently 26% for biological assets and 74% for Property, Plant and Equipment. As required under IAS 41, the fair value of biological assets is reduced by estimated costs to the point of sale. These costs are estimated at five per cent of timber values and reflect the costs of selling the woodland or forest.

Lake Vyrnwy joint afforestation scheme

Natural Resources Wales manages a forest in the Lake Vyrnwy area under a joint afforestation scheme with Severn Trent Water. Income is received and costs incurred by Natural Resources Wales and an annual payment of 50% of the operating surplus is paid to Severn Trent Water. Natural Resources Wales shows the value of 50% of the growing trees for this area of forest in the Statement of Financial Position, split between forest estate and biological assets. The value of the underlying land which remains Severn Trent Water's property is not included.

7.1.2 Heritage assets

Heritage assets are tangible assets with historical, artistic, scientific, technological, geophysical or environmental qualities that is held and maintained principally for their contribution to knowledge and culture. They are intended to be preserved in trust for future generations because of their cultural, environmental or historical associations.

Our National Nature Reserves meet the criteria for heritage assets. They comprise non-operational land within designated conservation areas which were set up to conserve and to allow people to study their wildlife, habitats or geological features of special interest. This land is held for conservation and for sustainable public use. Under the FReM interpretation of IAS 16 (Property, Plant and Equipment) these assets have been capitalised at cost.

As at 31 March 2016 Natural Resources Wales manages 58 of Wales's National Nature Reserves, either entirely, or in partnership and one Marine Nature Reserve (MNR). No material land purchases have been made during the last three financial years.

Further information on Natural Resources Wales's heritage assets and policies on the acquisition, preservation, management, disposal and access to heritage assets can be found on our website at:

<http://naturalresources.wales/conservation-biodiversity-and-wildlife/find-protected-areas-of-land-and-seas/?lang=en>

7.2 Intangible non-current assets

	Software Licences	Other Licences	Software Development Expenditure	Web Site	Assets under construction	Total
	£'000	£'000	£'000	£'000	£'000	£'000
Cost or valuation						
At 1 April 2015	5,130	2,607	4,554	165	862	13,318
Additions from transfer of function	8	0	0	0	0	8
Additions	377	0	0	0	6,250	6,627
Assets commissioned in year	632	0	0	0	(632)	0
Asset review adjustments and write-offs	(108)	0	(118)	0	0	(226)
Prior year adjustments	0	0	0	0	(19)	(19)
Disposals	(57)	0	0	0	0	(57)
Indexation and revaluation	(87)	541	(44)	(4)	0	406
Reclassification	0	(729)	0	0	0	(729)
At 31 March 2016	5,895	2,419	4,392	161	6,461	19,328
Amortisation						
At 1 April 2015	1,509	28	3,384	0	0	4,921
Additions from transfer of function	7	0	0	0	0	7
Charged in year	900	28	388	31	0	1,347
Asset review adjustments and write-offs	(98)	0	(118)	0	0	(216)
Disposals	(54)	0	0	0	0	(54)
Indexation and revaluation	(7)	0	(11)	1	0	(17)
At 31 March 2016	2,257	56	3,643	32	0	5,988
Carrying Amount at 1 April 2015	3,621	2,579	1,170	165	862	8,397
Carrying Amount at 31 March 2016	3,638	2,363	749	129	6,461	13,340
Asset Financing						
Owned	3,638	2,363	749	129	6,461	13,340
Carrying Amount at 31 March 2016	3,638	2,363	749	129	6,461	13,340

Comparative figures for period to 31 March 2015

	Software Licences	Other Licences	Software Development Expenditure	Web Site	Assets under construction	Total
	£'000	£'000	£'000	£'000	£'000	£'000
Cost or valuation						
At 1 April 2014	2,608	2,045	4,803	0	1,801	11,257
Additions	1,075	2	0	39	1,958	3,074
Assets commissioned in year	2,124	249	0	116	(2,489)	0
Asset review adjustments and write-offs	(937)	(23)	(487)	0	0	(1,447)
Prior year costs expensed	0	0	0	0	(408)	(408)
Indexation	260	141	238	10	0	649
Reclassification	0	193	0	0	0	193
At 31 March 2015	5,130	2,607	4,554	165	862	13,318
Amortisation						
At 1 April 2014	2,038	0	2,492	0	0	4,530
Charged in year	351	26	847	0	0	1,224
Asset review adjustments and write-offs	(937)	0	(155)	0	0	(1,092)
Indexation	57	2	200	0	0	259
At 31 March 2015	1,509	28	3,384	0	0	4,921
Carrying Amount at 1 April 2014	570	2,045	2,311	0	1,801	6,727
Carrying Amount at 31 March 2015	3,621	2,579	1,170	165	862	8,397
Asset Financing						
Owned	3,621	2,579	1,170	165	862	8,397
Carrying Amount at 31 March 2015	3,621	2,579	1,170	165	862	8,397

8. Financial liabilities and instruments

8.1 Financial liability

The financial liability of £39,991k reported in the Statement of Financial Position includes £39,844k of liability from reservoir operating agreements.

In 1989, to enable privatisation to occur, HM Government negotiated reservoir operating agreements with the water companies. These agreements included fixed payments (indexed annually on the Retail Price Index) payable in perpetuity to the water companies. Natural Resources Wales is now responsible for the payments to Dŵr Cymru Welsh Water.

As the total liability has been calculated as perpetuity on an amortised cost basis it will not change from year to year except in the unlikely event of an agreement ceasing. Natural Resources Wales is able to recover the full cost of reservoir operating agreements including the annual indexation through its charges for water abstraction.

£5,226k was paid to Dŵr Cymru Welsh Water during 2015/16 (£5,189k in 2014/15) for the indexed fixed payments. These are included with other payments under the reservoir operating agreements in Note 5.

8.2 Financial instruments

As the cash requirement of Natural Resources Wales is mainly met through grant in aid, financial instruments play a more limited role in creating and managing risk than would apply to a non-public sector body. The majority of financial instruments relate to contracts to buy non-financial items in line with Natural Resources Wales's expected purchase and usage requirements and Natural Resources Wales is therefore exposed to little credit, liquidity or market risk.

9. Trade and other receivables

	31 March 2016 £'000	31 March 2015 £'000
Trade receivables	6,520	5,951
Provision for doubtful debt	(413)	(355)
Accrued income	3,869	3,158
VAT receivable	3,129	3,102
Prepayments	2,009	1,740
Accrued European income	1,201	3,138
Other receivables	158	515
Deposit	23	211
Total	16,496	17,460

10. Cash and cash equivalents

	31 March 2016 £'000	31 March 2015 £'000
Opening balance	26,798	15,111
Net change in cash and cash equivalent balances	(4,063)	11,687
Total	22,735	26,798

The following balances were held at 31 March

Government Banking Service	17,695	32,075
Other bank accounts	5,039	(5,278)
Cash in hand	1	1
Total	22,735	26,798

11. Trade and other payables

	31 March 2016 £'000	31 March 2015 £'000
Trade payables accrual	7,273	13,956
Deferred income	6,705	6,007
Holiday pay	1,606	1,765
Trade payables	1,464	1,237
Finance leases	718	1,219
Customer deposits and receipts in advance	271	268
Other payables	106	55
Bonds and deposits	1,425	1,404
Total	19,568	25,911

12. Provisions

	Early departure costs £'000	Other £'000	Total £'000
Balance at 1 April 2015	415	2,540	2,955
Provided in the year	0	1,287	1,287
Released in year	(5)	(1,303)	(1,308)
Used in the year	(154)	(1,201)	(1,355)
Unwinding of discount	3	0	3
Balance at 31 March 2016	259	1,323	1,582
Estimated timing of discounted cash flows			
Due within one year	131	1,323	1,454
Due between one and five years	128	0	128
Total	259	1,323	1,582

In line with the requirement of IAS 37 (Provisions, Contingent Liabilities and Contingent Assets), where material, Natural Resources Wales provides for obligations arising from past events where there is a present obligation at the reporting date, it is probable that we will be required to settle the obligation and a reliable financial estimate can be made.

Where material, the future costs of provisions are discounted using the rates directed by HM Treasury.

Provision for early departure costs consist of annual compensation payments to former staff who left under legacy bodies' early retirement programmes. These payments are indexed by the consumer price index and continue until each individual reaches pensionable age. The provision represents the cost to Natural Resources Wales, using an indexation rate of 0% (2014/15 1.2%), and discounted by the HM Treasury discount rate of 1.2% (2014/15 1.2%)

Other provisions include £1,197k of grant offers to fund work to be undertaken up to 31 March 2016 but which will not to be claimed until June 2016 and £126k for other claims. It is expected that all of these will be paid within the next twelve months.

The cost of additional provision and changes in discount for the early departure costs provision are included in note 3. The costs of the additional other provisions are shown in note 5. The total provisions reported above are in the Statement of Financial Position under liabilities. The additional provision for doubtful debt, also shown in note 5, is included in total provision for doubtful debt in note 9 and included in the Statement of Financial Position under receivables.

13. Pension obligations

Natural Resources Wales (NRW) is a member of two pension schemes, the Civil Service Pension Scheme (CSPS) and the Local Government Pension Scheme (LGPS).

Civil Service Pension Scheme

CSPS is open to new employees.

Pension benefits are provided through the Civil Service pension arrangements. From 1 April 2015 a new pension scheme for civil servants was introduced – the Civil Servants and Others Pension Scheme or alpha, which provides benefits on a career average basis with a normal pension age equal to the member's State Pension Age (or 65 if higher). From that date all newly appointed civil servants and the majority of those already in service joined alpha. Prior to that date, civil servants participated in the Principal Civil Service Pension Scheme (PCSPS). The PCSPS has four sections: 3 providing benefits on a final salary basis (classic, premium or classic plus) with a normal pension age of 60; and one providing benefits on a whole career basis (nuvos) with a normal pension age of 65.

These statutory arrangements are unfunded with the cost of benefits met by monies voted by Parliament each year. Pensions payable under classic, premium, classic plus, nuvos and alpha are increased annually in line with Pensions Increase legislation. Existing members of the PCSPS who were within 10 years of their normal pension age on 1 April 2012 remained in the PCSPS after 1 April 2015. Those who were between 10 years and 13 years and 5 months from their normal pension age on 1 April 2012 will switch into alpha sometime between 1 June 2015 and 1 February 2022. All members who switch to alpha have their PCSPS benefits 'banked', with those with earlier benefits in one of the final salary sections of the PCSPS having those benefits based on their final salary when they leave alpha. (The pension figures quoted for officials show pension earned in PCSPS or alpha – as appropriate. Where the official has benefits in both the PCSPS and alpha the figure quoted is the combined value of their benefits in the two schemes.) Members joining from October 2002 may opt for either the appropriate defined benefit arrangement or a 'money purchase' stakeholder pension with an employer contribution (partnership pension account).

Employee contributions are salary-related and range between 3% and 8.05% of pensionable earnings for members of classic (and members of alpha who were members of classic immediately before joining alpha) and between 4.6% and 8.05% for members of premium, classic plus, nuvos and all other members of alpha. Benefits in classic accrue at the rate of 1/80th of final pensionable earnings for each year of service. In addition, a lump sum equivalent to three years initial pension is payable on retirement. For premium, benefits accrue at the rate of 1/60th of final pensionable earnings for each year of service. Unlike classic, there is no automatic lump sum. classic plus is essentially a hybrid with benefits for service before 1 October 2002 calculated broadly as per classic and benefits for service from October 2002 worked out as in premium. In nuvos a member builds up a pension based on his pensionable earnings during their period of scheme membership. At the end of the scheme year (31 March) the member's earned pension account is credited with 2.3% of their pensionable earnings in that scheme year and the accrued pension is uprated in line with Pensions Increase legislation. Benefits in alpha build up in a similar way to nuvos, except that the accrual rate is 2.32%. In all cases members may opt to give up (commute) pension for a lump sum up to the limits set by the Finance Act 2004.

The partnership pension account is a stakeholder pension arrangement. The employer makes a basic contribution of between 3% and 12.5% up to 30 September 2015 and 8% and 14.75% from 1 October 2015 (depending on the age of the member) into a stakeholder pension product chosen by the employee from a panel of providers. The employee does not have to contribute, but where they do make contributions, the employer will match these up to a limit of 3% of pensionable salary (in addition to the employer's basic contribution). Employers also contribute a further 0.8% of pensionable salary up to 30 September 2015 and 0.5% of pensionable salary from 1 October 2015 to cover the cost of centrally-provided risk benefit cover (death in service and ill health retirement).

The accrued pension quoted is the pension the member is entitled to receive when they reach pension age, or immediately on ceasing to be an active member of the scheme if they are already at or over pension age. Pension age is 60 for members of classic, premium and classic plus, 65 for members of nuvos, and the higher of 65 or State Pension Age for members of alpha. (The pension figures quoted for officials show pension earned in PCSPS or alpha – as appropriate. Where the official has benefits in both the PCSPS and alpha the figure quoted is the combined value of their benefits in the two schemes, but note that part of that pension may be payable from different ages.)

Further details about the Civil Service pension arrangements can be found at the website www.civilservicepensionscheme.org.uk

Local Government Pension Scheme (LGPS)

On 1st April 2013, the pension activities of Environment Agency Wales (EAW) were transferred to Natural Resources Wales pursuant to the Natural Resources Body for Wales Transfer Scheme 2013 under the Public Bodies Act 2011. The employees of NRW that were employees of EAW remain members of the Environment Agency Pension Fund (EAPF) as an admitted body.

EAPF operates a statutory, defined benefit pension scheme, administered in accordance with the Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007, the Local Government Pension Scheme (Administration) Regulations 2008 and the Local Government Pension Scheme (Transitional Provisions) Regulations 2008. It is contracted out of the State Second Pension. Further details on the pension fund including its annual report and accounts, are on the EAPF website, www.eapf.org.uk.

The total pension charge for NRW was £8.325 million. The pension charge relating to the scheme was assessed in accordance with the advice of an independent qualified actuary using the projected unit method of valuation to calculate the service costs.

The latest triennial actuarial valuation of the EAPF was at 31 March 2013. The assets taken at market value (£2.1 billion) were sufficient to cover 90% of the value of liabilities in respect of past service benefits which had accrued to members. NRW has accepted the independent actuary's recommendation in respect of future employer contributions. The next triennial actuarial valuation will be as at 31st March 2016 and will be used to set employer contribution rates for the three year period starting 1st April 2017.

The annual report and financial statements for the EAPF report that it had sufficient assets to meet 85% of its expected future liabilities at 31 March 2016 on an ongoing funding basis. NRW's share of the EAPF's liabilities as reported in these financial statements is calculated using different actuarial assumptions, required by IAS19, to those used in the EAPF's annual report. This leads to a different funding level to that reported by the EAPF.

The main difference in assumption is the discount rate used to value pension liabilities. The EAPF discount rate is based on long term UK government bond yields and assumes a level of future asset outperformance by the bonds owned by the EAPF. The discount rate used in these financial statements, as required by IAS19 is based on high quality corporate bond yields, with no additional asset performance assumption. The sensitivity analysis in note 13.4 indicates the sensitivity of the fund liabilities to a difference in discount rate.

A number of assumptions are made as part of the actuarial valuation process. The prudent actuarial assumptions used do not represent a view on what future pay movements may be. It has been assumed that present and future pensions in payment will increase at the rate of 1.9% per annum. The estimated contribution payable by NRW, excluding any discretionary lump sum payments, for the year to 31 March 2017 will be approximately £6.480 million.

The notes below set out the disclosure requirements of IAS 19 for the current year in relation to NRW's participation in the EAPF. All calculations have been made by a qualified independent actuary and were based on the most recent actuarial valuation of the fund at 31 March 2013 updated to 31 March 2016. The assumptions underlying the calculation of a net liability at 31 March 2016 are only used for accounting purposes as required under IAS 19. There is no requirement for the reported net liability to be met as a lump sum. Cash contributions paid by NRW to the pension fund will continue to be set by reference to assumptions agreed at each triennial actuarial valuation of the scheme.

13.1 Financial and longevity assumptions

Period Ended	31 Mar 2016	31 Mar 2015
	% p.a.	% p.a.
Pension Increase Rate	1.90%	2.10%
Salary Increase Rate	3.40%	3.50%
Discount Rate	3.50%	3.20%

Average future life expectancy at 65	Males	Females
Current Pensioners	22.6 years	24.5 years
Future Pensioners (People aged 65 in 20 years)	24.7 years	27.0 years

13.2 Fair Value of Assets for the year ended 31 March 2016

Asset Category	31 March 2016 (£'000)				
	Quoted	Unquoted	Undetermined	Total	%
Equity Securities:					
Common Stock	80,441	291	0	80,732	30%
Preferred Stock	0	0	0	0	0%
Rights/Warrants	0	0	0	0	0%
Other Equity Assets	817	0	0	817	0%
Debt Securities:					
UK Government Bonds	0	26,123	0	26,123	10%
Corporate Bonds	0	22,548	0	22,548	8%
Other	0	1,507	0	1,507	1%
Pooled Investment Vehicles:					
Equities	0	0	42,082	42,082	16%
Bonds	620	0	41,349	41,969	16%
Funds - Common Stock	1,146	0	8,869	10,015	4%
Funds - Real Estate	392	1,564	11,837	13,793	5%
Funds - Venture Capital	0	0	0	0	0%
Venture Capital and Partnerships:					
Partnerships & Real Estate	0	21,316	0	21,316	8%
Other Investment:					
Stapled Securities	488	0	0	488	0%
Derivative Contracts:					
Equity Derivatives - Futures	4	0	0	4	0%
Forward FX Contracts	0	0	98	98	0%
Cash and Cash equivalents					
All	5,179	(25)	744	5,898	2%
Totals	89,087	73,324	104,979	267,390	100%

13.3 Change in fair value of plan assets, defined benefit obligation and net liability

Period ended 31 March 2016	Assets	Obligations	Net (liability)/ asset
	£'000	£'000	£'000
Fair value of employer assets	258,249	0	258,249
Present value of liabilities	0	334,353	(334,353)
Present value of unfunded liabilities	0	0	0
Opening Position as at 31 March 2015	258,249	334,353	(76,104)
Service cost			
- Current service cost*	0	8,227	(8,227)
- Past service cost (including curtailments)	0	98	(98)
- Effect of settlements	0	0	0
Total service cost	0	8,325	(8,325)
Net interest			
- Interest income on plan assets	8,315	0	8,315
- Interest cost on defined benefit obligation	0	10,754	(10,754)
- Impact of asset ceiling on net interest	0	0	0
Total net interest	8,315	10,754	(2,439)
Total defined benefit cost recognised in Profit or (Loss)	8,315	19,079	(10,764)
Cashflows			
- Plan participants' contributions	2,111	2,111	0
- Employer contributions	8,080	0	8,080
- Contributions in respect of unfunded benefits	0	0	0
- Benefits paid	(6,993)	(6,993)	0
- Unfunded benefits paid	0	0	0
Effect of business combinations and disposals	2,432	3,780	(1,348)
Expected closing position	272,194	352,330	(80,136)
Remeasurements			
- Change in demographic assumptions	0	0	0
- Change in financial assumptions	0	(35,130)	35,130
- Other experience	0	(2,853)	2,853
- Return on assets excluding amounts included in net interest	(4,804)	0	(4,804)
- Changes in asset ceiling	0	0	0
Total remeasurements recognised in Other Comprehensive Income (OCI)	(4,804)	(37,983)	33,179
Exchange differences	0	0	0
Fair value of employer assets	267,390	0	267,390
Present value of funded liabilities	0	314,347	(314,347)
Present value of unfunded liabilities	0	0	0
Closing position as at 31 March 2016	267,390	314,347	(46,957)

* The current service cost includes an allowance for administration expenses of 0.4% of payroll.

13.4 Sensitivity analysis

Change in assumptions at 31 March 2016:	Approximate % increase to employer liability	Approximate monetary amount (£000)
0.5% decrease in Real Discount Rate	12%	38,207
1 year increase in member life expectancy	3%	9,430
0.5% increase in the Salary Increase Rate	5%	15,205
0.5% increase in the Pension Increase Rate	7%	22,262

14. Capital commitments

	31 March 2016 £'000	31 March 2015 £'000
Property plant and equipment		
Plant and machinery	24	34
Transport equipment	759	138
IT equipment	48	154
Operational structures	222	544
Total	1,053	870
Intangible assets		
Information technology - software licences	0	56
Information technology - software development	590	805
Total	590	861

15. Commitments under leases

The determination of whether an arrangement is, or contains, a lease is based upon the substance of that arrangement. An arrangement which is dependent on the use of a specific asset and which conveys the right to use the asset, is regarded as a lease.

A finance lease is one which transfers substantially the risks and rewards of ownership of an asset to the lessee. An operating lease is a lease other than a finance lease. Leases are assessed using the criteria laid down in IAS 17 (Leases). Land held under a finance lease is not depreciated.

Costs relating to operating leases are charged to the Statement of Comprehensive Net Expenditure on a straight line basis over the lease term and are shown in Note 5.

Finance leases are capitalised at commencement at the lower of fair value of the leased asset or the present value of the minimum lease payments. A corresponding debt due to the lessor is recorded. Finance charges are charged to the Statement of Comprehensive Net Expenditure. Vehicles held under finance lease are depreciated over the term of the lease.

15.1 Operating leases

Total future minimum lease payments under operating leases are given in the table below for each of the following periods.

	31 March 2016			
	Land	Buildings	Vehicles	Total
	£'000	£'000	£'000	£'000
Obligations under operating leases are:				
Not later than one year	92	1,763	424	2,279
Later than one year and not later than five years	295	4,548	496	5,339
Later than five years	1,562	1,696	0	3,258
Total value of obligations	1,949	8,007	920	10,876
	31 March 2015			
	Land	Buildings	Vehicles	Total
	£'000	£'000	£'000	£'000
Obligations under operating leases are:				
Not later than one year	115	1,700	1,204	3,019
Later than one year and not later than five years	386	5,221	918	6,525
Later than five years	1,756	1,829	0	3,585
Total value of obligations	2,257	8,750	2,122	13,129

15.2 Finance leases

	31 March 2016		
	Land	Vehicles	Total
	£'000	£'000	£'000
Obligations under finance leases are:			
Not later than one year	13	260	273
Later than one year and not later than five years	38	198	236
Later than five years	209	0	209
Total value of obligations	260	458	718

	31 March 2015		
	Land	Vehicles	Total
	£'000	£'000	£'000
Obligations under finance leases are:			
Not later than one year	13	243	256
Later than one year and not later than five years	38	716	754
Later than five years	209	0	209
Total value of obligations	260	959	1,219

16. Other financial commitments

Natural Resources Wales has entered into non-cancellable contracts not reported elsewhere. The total payments to which Natural Resources Wales is committed at 31 March 2016 are :

	31 March 2016	31 March 2015
	£'000	£'000
Not later than one year	18,241	34,878
Later than one year and not later than five years	18,971	19,081
Later than five years	3,895	708
Total	41,107	54,667

17. Lease receivables

Assets leased to external parties under an operating lease are capitalised under the appropriate accounting policy as outlined in Note 7. Operating lease income is accounted for on a straight line basis and the future minimum lease payments receivable under non-cancellable operating leases are as follows:

	31 March 2016
	£'000
Not later than one year	697
Later than one year and not later than five years	2,474
Later than five years	6,540
Total	9,711

No comparatives are available for 2014/15 as this is the first year of disclosure for NRW.

18. Contingent liabilities

Natural resources Wales has the following contingent liabilities:

	31 March 2016	31 March 2015
	£'000	£'000
Public and employee liability	605	30
Contractors' claims	0	250
Total	<u>605</u>	<u>280</u>

Natural Resources Wales discloses contingent liabilities in accordance with IAS 37.

The above table does not include values for the following contingent liabilities:-

Forestry Commission Wales was part of the Forestry Commission until 31 March 2013, and shared their VAT registration. An HMRC audit of the Forestry Commission's treatment of VAT and Income Tax is underway for the period 2012/13. An unquantifiable contingent liability is disclosed to recognise the present obligation of non-compliance liabilities arising from the audit. A reliable estimate of the amount of the obligation is not available.

There is a job evaluation process underway with the aim of creating a single, unified structure of jobs and grades that works for all in Natural Resources Wales. We are undertaking a pay modelling exercise to assess the impact and cost of the single unified structure. This exercise, whose results will not be known until the latter part of 2016/17, could identify back pay owed to staff whose role is judged to be of a higher grade than what they are being paid. The date from which back pay could be calculated is 1st April 2013.

19. Events after the end of the reporting period

We have considered the results of the United Kingdom's European Union referendum for its impact on the financial statements. We have concluded that it is not possible to quantify the risk at this time given the current uncertainty of impact and timing of potential changes. The elements of the financial statements that could be the most impacted in the future is the value of the pension reserve and the forest estate.

20. Related parties

Natural Resources Wales is a Sponsored Body of the Welsh Government, which is regarded as a related party. During the year NRW has had significant material transactions with the Welsh Government in the normal course of business (the grant-in-aid and grants received from WG during the year is reported in the Statement of Taxpayers Equity) and with other entities for which the Welsh Government is regarded as the parent department namely Welsh Local Authorities and National Parks.

In addition, NRW has had various material transactions with other government departments and other central government bodies. Most of these transactions have been with Department for Environment, Food and Rural Affairs (DEFRA), Environment Agency, Forestry Commission, HMRC and Natural England.

During the year NRW, in the normal course of its business, entered into the following transactions with the following organisations in which board and executive members or other related parties had an interest. The board and executive members have no direct involvement in the transactions with these related parties.

We have shown transactions for the full year including where members have joined or left during the year.

Organisation	Member	Nature of relationship	Total payments	Total income	Amount owed by NRW at 31 March 2016	Amount owed to NRW at 31 March 2016
			£'000	£'000	£'000	£'000
Aberystwyth University	Emyr Roberts	Council member	25	4	0	0
All Wales Partnership of the Canal and River Trust in Wales	Ruth Hall	Member	21	27	0	0
Cardiff University (Public Policy Institute for Wales)	Ruth Hall	Governor/Vice Chair	65	9	0	0
Dee Valley Water	Diane McCrea	Chair of Customer Challenge Panel	1	778	0	0
DEFRA including Joint Nature Conservation Committee and Support Company	Lynda Warren Peter Matthews Diane McCrea Madeleine Havard	Member of JNCC & Science Advisory Council Board Member of JNCC Board Member of JNCC Board Member of JNCC & NED of JNCC Support Co	30	0	6	0
Dwr Cymru Welsh Water	Diane McCrea	Chair of Customer Challenge Group	6,886	14,296	104	0
Glanusk Estate	Harry Legge-Bourke	Owner/Partner/ Trustee	3	0	0	0
Groundwork North Wales	Karen Balmer	Chief Executive	18	0	0	0
Leonard Cheshire Disability	Elizabeth Haywood	Board member and trustee	0	1	0	0
National Association of Areas of Outstanding Natural Beauty	Howard Davies	Chief Executive	48	0	0	0
National Trust	Ruth Hall	Council member	202	12	0	0
Natural England	Nigel Reader	Non-Executive Board Member and Audit Committee Chair	153	0	11	0
North East Wales Wildlife Ltd	Karen Balmer	Trustee	14	0	0	0
North Wales Wildlife Trust	Howard Davies	Trustee and Honorary Vice President	172	0	0	0
SP Energy Network Holdings Ltd	Elizabeth Haywood	Non-Executive Director	0	48	0	5
TGV Hydro Ltd	Chris Blake	Director	0	3	0	0

Annex 1 Corporate Environmental Report

Introduction

We have made the commitment that sustainable development will be at the heart of all our business decisions. Over the coming years, we want to develop ourselves as an exemplar organisation with regards to sustainability and environmental management in Wales, especially in our management and use of carbon, waste, water and land.

Our focus during this year has been to:

- reduce our carbon footprint
- embed our Environmental Management System (EMS) into the culture of our organisation
- integrate environmental, social and economic factors into our procurement activity and be an engaging and transparent organisation for our EMS stakeholders; and
- conform with the new ISO14001:2015 standard; and to establish a baseline for waste monitoring, reporting and reduction targets.

This report relates primarily to environmental sustainability, as distinct from wider sustainability actions or outcomes. Wider sustainability-related reporting can be found throughout our Annual Report and Accounts.

Summary of Performance

We have retained ISO14001 certification for our EMS, following independent external surveillance audits and verification. Our EMS⁵ now also includes all our forestry operations. Having an externally verified EMS allows us to demonstrate our own commitment to achieving the highest possible environmental standards as an organisation.

We have also retained woodland certification (the UK Woodland Assurance Standard) for the Welsh Government Woodland Estate we manage, following independent external audits and verification via Société Générale de Surveillance (SGS). This enables us to produce FSC/PEFC⁶ certified timber from the Welsh Government Woodland Estate we manage.

⁵ Our EMS is currently applicable to: “Activities and services associated with the sustainable management of the environment and the natural resources of Wales”

⁶ Forest Stewardship Council (FSC). Programme for the Endorsement of Forest Certification (PEFC). As supported by our [UK Woodland Assurance Standard](#) (UKWAS) accreditation

Table 1: Corporate Environmental report summary table

Area	Units	2013/14	2014/15	2015/16	Change
Greenhouse gas emissions ⁷	Consumption (tCO ₂ e)	7,301	7,164	7,894	Increased
	Expenditure (£k)	3,323	3,345	2,961	Decreased
Estate energy	Consumption (million kWh)	7.0	6.3	6.9	Increased
	Expenditure (£k)	570	587	632	Increased
Estate waste	Consumption (tonnes)	400	419	752	Increased
	Expenditure (£k)	147	110	127	Increased
Estate water	Consumption (m ³)	86,486	29,455	78,304	Increased
	Expenditure (£k)	35	27	59	Increased

Table 1 reflects relative change for key areas in the last year. More detail around each can be found within the related sections of this report. In summary there has been:

- a 10% increase in greenhouse gas emissions primarily due to the increase in primary aggregate use in construction schemes
- a 10% increase in energy use due in large part to unmanned site electricity use
- a 68% increase in the reported amount of waste we handle, following the inclusion of additional waste streams in our reporting for the first time this year (primarily for offices and depots)
- a 160% increase in the reported amount of water we use largely related to a meter being repaired at Cynrig Fish Hatchery, which also resulted in under-reporting in previous years

We have targets in place relating to each of these areas in 2016/17 (as described in the next section).

Summary of Future Strategy

Over the next two years we intend to focus on:

- Achieving certification to the revised ISO14001:2015 environmental standard
- Aiming to maintain our UKWAS accreditation
- Cutting our carbon emissions from occupied buildings, business travel and water use by 5% from 2015/16 levels, year on year
- Fulfilling our commitments under the Sustainable Development Charter, taking forward the provisions of the Well-being of Future Generations (Wales) Act and work towards becoming an acknowledged exemplar of sustainability
- Ensuring our procurement practices are open and transparent, supporting the delivery of economic, social and environmental priorities and that our contracts are appropriately accessible for SMEs, social businesses and larger scale enterprises helping to support the Welsh Government's Tackling Poverty Action Plan
- Investigating scope for distributed energy / small scale renewable developments on land we manage, taking a positive, risk-based approach
- Developing our approach to Integrated Reporting including the delivery of our Business Case.

⁷ (Scopes 1, 2 and 3 including air/rail travel and excluding outside of scopes emissions)

Next year we want to

- Reduce our carbon footprint – and have set a target to reduce our carbon dioxide emissions from occupied buildings, travel and water use by 5% based on 2015/16 data
- Deliver our Carbon Positive Project - Progressing us towards becoming an exemplar in carbon management and sharing best practice for use across the Welsh public sector
- Meet the requirements of the new ISO14001:2015 standard
- Meet the requirements of our Incident Management Enabling Plan – Achieving UK Spill accreditation
- Continue to embed our EMS into the culture of the organisation – Raising staff awareness of the contribution they can make as individuals to environmental performance and how their work can contribute to the Sustainable Management of Natural Resources

Greenhouse Gas Emissions

Our greenhouse gas emissions are outlined below/right.

We set out a target to achieve a 5% reduction in CO₂e emissions from our business travel and buildings this year, and have achieved this, with a 10% reduction in CO₂e emissions overall from these areas. However, overall emissions have increased by 8% due to the increase in primary aggregate use in construction schemes.

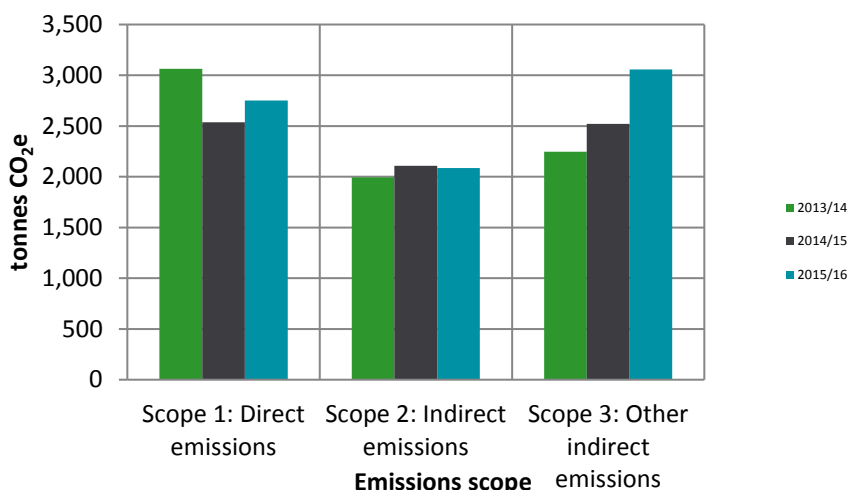


Table 2: Greenhouse gas emissions

Greenhouse gas emissions	2013/14	2014/15	2015/16	Change
Scope 1: Direct GHG emissions (tCO ₂ e)	3,064	2,537	2,752	Increased
Scope 2: Energy indirect emissions (tCO ₂ e)	1,993	2,107	2,086	Decreased
Scope 3: Other indirect GHG emissions (tCO ₂ e)	2,245	2,520	3,057	Decreased
Total gross GHG emissions (tCO₂e)	7,301	7,164	7,894	Increased
<i>Outside of scopes (i.e. biomass)</i>	180	176	248	Increased
<i>Carbon intensity (tCO₂e per £m expenditure)</i>	41.3	39.8	44.9	Increased

Waste Minimisation and Management

We have improved the number of waste streams we can report in line with our target to measure and report on all NRW waste streams consistently in 2015/16. This has particularly improved for our offices and depots. Our largest single source of waste is cess pit waste at our Pye Corner depot. Mixed municipal waste from our Coed y Brenin visitor centre is the second largest source of waste. We will be looking into ways to reduce these, and other, large areas of waste in 2016/17

Table 3: Waste Generated

Waste generated	Units	2013/14	2014/15	2015/16	Change
Landfilled	Consumption (tonnes)	80	64	216	Increased
	Consumption (tCO ₂ e)	23	18	80	Increased
	Expenditure (£k)	90	47	25	Decreased
Recycled / reused	Consumption (tonnes)	253	229	359	Increased
	Consumption (tCO ₂ e)	5	5	8	Increased
	Expenditure (£k)	57	Not available	101	Increased
Fly tipped	Consumption (tonnes)	37	95	45	Decreased
	Consumption (tCO ₂ e)	9	22	19	Decreased
	Expenditure (£k)	Not available	Not available	Not available	Not available
Incinerated	Consumption (tonnes)	30	31	132	Increased
	Consumption (tCO ₂ e)	1	1	3	Increased
	Expenditure (£k)	Not currently available[1]	Not available	Not available	Not available
Total waste	Consumption (tonnes)	400	419	752	Increased
	Consumption (tCO ₂ e)	38	46	110	Increased
	Expenditure (£k)	147	110	127	Increased

Use of Finite Resources

We have reported on our estate water and energy use below. The stones/aggregate used in construction projects is also one of our significant areas of resource consumption, and is reported in the Sustainable Construction section of this report.

Water: Our water use reporting was improved last year to ensure office water use figures purely reflect office water use (i.e. not including any combined use sites, depots, visitor centres, hatcheries, etc.). Our water use intensity is below average for water use⁸, and we have set a 5% reduction target for 2016/17.

Table 4: Water Consumption

Resource use – Estate water	Units	2013/14	2014/15	2015/16	Change
Water supplied: Office use	Consumption (m ³)	8,161	7,208	6,859	Decreased
Water supplied: Non-office use:					
- Mains supply	Consumption (m ³)	4,863	6,630	5,529	Decreased
- Abstraction	Consumption (m ³)	73,428	15,581	65,886	Increased
- Rainwater	Consumption (m ³)	34	35	30	Decreased
Water use intensity (for Office use)	m ³ per FTE	4.1	3.7	3.4	Decreased
Water supplied: Total	Consumption (m ³)	86,486	29,455	78,304	Increased
	Expenditure (£k)	35	27	59	Increased
	Consumption (tCO ₂ e)	30	10	27	Increased

Abstraction of water used to operate our fish hatchery site was the most significant water use this year, at over 60,000 m³. Much of the apparent increase in abstracted water use

⁸ Average = 4m³ per FTE (Source: Water Key Performance Indicators and benchmarks for offices and hotels. C657 CIRIA www.ciria.org)

relates to the repair of a non-functioning meter during the year, which meant 2014/15 water use is not reflective of usual site usage. Maintaining the wetland habitats at Newport Wetlands National Nature Reserve (designated SSSI and part of the Severn Estuary SPA, RAMSAR and SAC) was the second largest use⁹ this year, and largest in use 2014/15. We also abstract water at remote sites where mains water is not available.

Energy: Our energy use has increased this year, with the large part of the increase related to our unoccupied sites (electricity use in particular). In the last year we have also generated 1.5% of our own energy use from our buildings with onsite renewables (wind and solar power). Our largest renewable installation (photovoltaic panels at the Maes Y Ffynnon office in Bangor) generated 24,864 kWh during the year. We aim to increase the number of onsite renewables on our own buildings as and when funding becomes available and is economically feasible.

Table 5: Energy Consumption

Resource use – Estate energy	Units	2013/14	2014/15	2015/16	Change
Energy used: Occupied sites	Consumption (kwh)	6,026,274	5,361,986	5,502,994	Increased
	Consumption (tCO ₂ e)	2,151	2,081	1,990	Decreased
Energy used: Unoccupied sites	Consumption (kwh)	930,846	993,431	1,434,275	Increased
	Consumption (tCO ₂ e)	415	491	663	Increased
Renewable energy: Self-generated	Generation (kwh)	77,730	80,870	81,713	Increased
	Consumption (% of energy used)	1.3%	1.5%	1.4%	Decreased
Energy used: Total	Consumption (kwh)	6,957,120	6,355,417	6,937,269	Increased
	Consumption (tCO ₂ e)	2,566	2,572	2,653	Increased
	Expenditure (£k)	570	587	632	Increased
Renewable energy installations ¹⁰	Consumption (MW)	59	59 ¹¹	60	Increased

There is also large scale renewable energy generation on the wider estate we manage (the Welsh Government Woodland Estate) through the Cefn Croes wind farm, which has an installed capacity of 59MW. On a smaller scale, ~1,268kW of renewable energy has become operational in the last two years from small scale hydro generation we have enabled. We have an Energy Delivery Plan to develop further onshore energy projects (covering wind, hydro, solar, biomass, coal, oil and gas), through or over the managed estate. Over the next three years we are anticipating the amount of energy generated on

⁹ Abstracted water is used in dry hot weather to maintain the correct water and salinity levels in the Newport Wetlands Saline Lagoons, vital for the many species of water bird that rely on them. In the autumn, the abstraction is also used to ensure the reserve's lowland wet grassland is kept in the right condition to support overwintering birds.

¹⁰ Schemes on the estate we manage which involve developers leasing land we manage on which to site installations of renewables (e.g. wind farms). This figure also includes schemes that are only partially on the estate we manage (e.g. small scale hydropower schemes). Figures given reflect installed capacity of operational installations, as opposed to the actual energy generation

¹¹ Full figure is 60.3MW, when including the ~1,268kW of small scale hydro generation we have enabled

the estate we manage will increase significantly (in excess of 600MW additional capacity provided via renewables, enough to power ~350,000 houses).

Sustainable Procurement

Sustainable procurement takes into account the economic, environmental and social impacts in our buying decisions. It allows our organisation to meet its need for goods and services in a way that achieves value for money on a whole-life basis, whilst also providing opportunities for Welsh SMEs. These key principles are reflected in our Sustainable Procurement Strategy 2015-2017, and our progress is reported throughout the year in our Business Plan Dashboard.

We have developed a Market Approach Plan which allows requisitioners to question the need to buy, and to consider in practical terms the impact of their purchase and all available options before entering into a contract. The plan also contains the Sustainability Impact Assessment, which examines the impact of the purchase on a whole life cost basis, and identifies mitigation controls.

In the forthcoming year, we will be building on this approach to consider the environmental and socio economic impact of procurement by further aligning to, and integrating, the provisions of the Well-being of Future Generations and Environment (Wales) Acts, whilst also taking into account risk, scope and influence. This will enable us to work with suppliers ensuring their commitment to sustainability, and will help target areas where the best results can be realised. We will also continue to deliver community benefits introduced through key contract awards, and report on the outcomes delivered.

Travel

Our travel needs include: working to manage sites, responding to serious environmental incidents, taking samples, dealing with flooding, site meetings, etc. This year we have travelled ~9 million miles in undertaking our work an 18% reduction from our 2013/14 baseline year. We have a target of a further 5% reduction in travel emissions for 2016/17, which will be achieved by using lower carbon vehicles as well as reducing mileage.

Table 6: Travel detail

Travel by vehicle	Units	2013/14	2014/15	2015/16	Change
Owned vehicles	Miles travelled	6,562,934	5,416,119	5,833,839	Increased
	Expenditure (£k)	1,101	1,033	800	Decreased
Lease vehicles	Miles travelled	2,154,755	2,531,396	1,649,345	Decreased
	Expenditure (£k)	223	329	162	Decreased
Grey vehicles ¹²	Miles travelled	673,345	618,795	552,343	Decreased
	Expenditure (£k)	74	81	244	Increased
Hire	Miles travelled	326,810	357,526	256,654	Decreased
	Expenditure (£k)	14	N/A	N/A	No change
Train	Miles travelled	1,405,603	1,367,762	865,693	Decreased
	Expenditure (£k)	342	377	291	Decreased
Air	Miles travelled	27,997	30,221	18,898	Decreased
	Expenditure (£k)	8	11	6	Decreased
Bicycle	Miles travelled	4,812	804	1,944	Increased
	Expenditure (£k)	0	0	0	No change
Motorbike	Miles travelled	N/A	N/A	4,475	N/A
	Expenditure (£k)	N/A	N/A	1	N/A

¹² Grey vehicles are staff's own private vehicles

Travel by vehicle	Units	2013/14	2014/15	2015/16	Change
Total vehicle travel	Miles travelled	11,156,256	10,322,623	9,183,191	Decreased
	Expenditure (£k)	1,762	1,831	1,502	Decreased

As part of work to reduce our costs and environmental impact related to travel, we have a travel policy in place. Supporting the policy, we have created a travel decision tree which lays out the best to worst options for travel. We also operate a 'no fly policy' within Wales and England, requiring all air travel requests to be fully justified and cleared at Executive Team level. Our use of video/audio conferencing has increased significantly through the year, with increases in the number of users, meetings held and minutes recorded.

Environmental incidents

There have been 18 environmental incidents as a result of our work (or that of our contractors) and three near misses. This a 47% reduction compared with the 38 incidents reported in the previous year 2014/15. None of these incidents were classified as serious according to the environmental incident classification scheme that we apply to environmental incidents. Where incidents occur as a result of our work (or that of our contractors), we review what has happened, and act to address the root cause of the incident.

Sustainable Construction

Much of our construction activity is contracted out, and some of this activity is not covered by the figures below.

Aggregate/stone: This year, 22% of aggregate use has been from a secondary source. The construction of Sea Defence Improvements at Tabbs Gout involved most use of aggregate. Our use of aggregate has dropped significantly this this year for such schemes. Our use of primary aggregate on the Public Forest Estate is typically for infrastructure construction, maintenance and reinstatement, and amounted to 178,000 tonnes in in 2015, most of which was produced from minerals on the estate.

Table 7: Stones/aggregate use

Resource use – Stone/aggregate	Units	2013/14	2014/15	2015/16	Change
Stone/aggregate – primary source	Consumption (tonnes)	63,923	115,786	182,999	Increased
	Expenditure (£k)	526	538	555	Increased
	Consumption (tCO2e)	703	1,274	2,013	Increased
Stone/aggregate – secondary source	Consumption (tonnes)	190,623 ¹³	13,102	51,945	Increased
	Expenditure (£k)	10	12	86	Increased
	Consumption (tCO2e)	381	26	104	Increased
Secondary source use	Expenditure (£k)	536	795	641	Decreased
	(% by total weight)	75	10	22	Increased

Timber: We aim to ensure all the timber we use is from sustainable sources, and we also produce FSC/PEFC¹⁴ certified timber from the Welsh Government Woodland Estate we manage. This year, all timber used in construction¹³ has been from a sustainable source.

¹³ A large amount of aggregate was used in 2014/15 increasing river capacity in the Lower Swansea Vale

¹⁴ Forest Stewardship Council (FSC). Programme for the Endorsement of Forest Certification (PEFC). As supported by our [UK Woodland Assurance Standard](#) (UKWAS) accreditation

Table 8: Timber use

Resource use – Timber	Units	2013/14	2014/15	2015/16	Change
Timber	Consumption (tonnes)	115	32	56	Increased
– sustainable source	Expenditure (£k)	22	9	5	Decreased
Timber	Consumption (tonnes)	0	0	0	No change
– unknown source	Expenditure (£k)	0	0	0	No change
Sustainable source use	(% by total weight)	100%	100%	100%	No change

Site consolidations

When our organisation was formed, we inherited a large amount of accommodation (e.g. depots, offices), some of which fulfilled a similar function at similar sites. We are continuing to sell off spare sites, reducing our accommodation costs, and their related carbon footprint. We will continue to consolidate our sites over the coming years.

Behaviour change

As part of our work to embed our Environmental Management System (EMS) into the culture of our organisation, we have delivered a number of training courses (to ~1,800 staff). Training areas have included awareness raising around our key environmental procedures, waste management, timber procurement and incident response.

Governance and Reporting

We report on our carbon footprint as part of our performance framework, which is reported by the Executive Team to the Board (in open public session) three times each year.

We collect the data used within this sustainability report through a combination of meter readings (e.g. gas, electricity), invoices (e.g. fuel card purchases) and suppliers data (e.g. train miles), using the most accurate source/s we have available. We have improved our biomass and waste data reporting and baselines in this report. We also look to minimise use of any estimated data in our reporting, and we are working to improve in this area.



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WALES AUDIT OFFICE
SWYDDFA ARCHWILIO CYMRU

Archwilydd Cyffredinol Cymru
Auditor General for Wales

Supplementary Memorandum of the Auditor General for Wales to the Public Accounts Committee – Timber Sales Contracts

Date issued: March 2017

Document reference: 253A2017

I have prepared this memorandum for the Public Accounts Committee of the National Assembly for Wales to support its consideration of my report under the Natural Resources Body for Wales (Establishment) Order 2012 on the financial statements of Natural Resources Wales for the year ended 31 March 2016.

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Supplementary Memorandum

Context

- 1 NRW is a Welsh Government sponsored body created for the purpose of ensuring that the environment and natural resources of Wales are:
 - sustainably maintained;
 - sustainably enhanced; and
 - sustainably used.¹
- 2 NRW became operational from 1 April 2013, taking over responsibility for delivering the functions of the former Countryside Council for Wales, Environment Agency Wales, and the Forestry Commission Wales. NRW managed the first two years of its development as a 'transition' stage, aiming to manage continuity whilst bringing together functions from its legacy bodies. In February 2016, I published a Value for Money report on the development of NRW that focused on:
 - the creation of NRW and its operation within its initial two-year transition period, including its progress in achieving the benefits intended from its creation; and
 - the arrangements NRW was putting in place to support its transformation phase.
- 3 I found that: 'NRW [had] adopted a sound and well-structured approach to meeting the significant challenges presented by its creation; ensuring continuity in delivering its wide range of functions and with a clear focus on achieving the intended benefits and that NRW [had] learned from progress made and challenges faced and [was] proceeding with a more ambitious and comprehensive change programme, necessary to transform itself for the future and deal with legislative changes and resource pressures'.² Whilst my report on NRW's 2015/16 accounts sets out some specific concerns regarding the regularity of timber sales contracts awarded by NRW to a sawmill operator in May 2014, I remain satisfied that NRW's approach to managing the transition stage was sound and well-structured.

¹ The Environment Wales Act 2016 amended the general purpose of the Natural Resources Body for Wales to: 'The Body must pursue sustainable management of natural resources in relation to Wales, and apply the principles of sustainable management of natural resources, in the exercise of its functions, so far as consistent with their proper exercise.'

² [The Development of Natural Resources Wales](#), February 2016

- 4 One of the key operational challenges which had been facing the Forestry Commission in Wales prior to the merger was how to manage and control the spread of Phytophthora Ramorum (P Ramorum) in larch forests and woodlands. P Ramorum is a fungus-like pathogen which causes extensive damage to, and kills a wide range of trees and other plants. P Ramorum was detected in Japanese larch in Wales in 2010. Efforts were made to manage the spread of the disease through targeted felling, but the disease spread rapidly. Following its establishment NRW inherited this challenge and was faced with having to take urgent action to manage and control the disease. During the summer months of 2013, NRW identified that there was a rapid increase in the spread of P Ramorum and NRW had to find a long-term solution to combating the disease. I have been told by NRW that its intention in meeting this challenge was primarily and overwhelmingly to increase capacity for dealing with diseased larch and avoid disruption to existing trade in other types of timber.

Chronology

Tender exercise for larch long-term sales contracts

- 5 In early 2013, the Forestry Commission in Wales, faced with a significant number of Statutory Plant Health Notices³ over an extensive geographical area, decided that large-scale felling of larch was necessary if P Ramorum was to be effectively controlled. An invitation to tender (ITT) was developed, whereby interested parties would be invited to tender to purchase larch timber from the Forestry Commission in Wales. NRW inherited the tender process from Forestry Commission in Wales on 1 April 2013 as a consequence of the merger.
- 6 In April 2013, NRW issued an ITT for two long-term contracts (LTCs) 'for clearance and marketing of infected Larch stands. Each contract being 330,000m³obs [approximately 266,000 tonnes] over a five year period'⁴. The ITT noted that the award of the contract 'will be made on the combined basis of the price offered and clear demonstrable linkages to how the timber will be harvested and processed with minimal displacement to the current harvesting or processing resource in Wales'. Therefore, it is clear that NRW's decision on contract award was to take into account both the price and wider market considerations in terms of how the timber will be harvested and processed, with the objective of minimising disruption to harvesting and processing resources in Wales. The ITT made clear that there

³ Statutory Plant Health Notices require the landowner to fell, destroy and/or contain infected trees within a defined time period. In Wales, the notices were issued by the Forestry Commission until 31 March 2013 and by Natural Resources Wales thereafter as part of its regulatory functions

⁴ m³ obs = cubic metres overbark standing, i.e., volume of wood in standing trees, including bark

was the possibility of further discussions with bidders before the contract was awarded.

- 7 NRW received three tenders, one of which was submitted by the sawmill operator. In its response to the ITT, the sawmill operator set out plans for infrastructure investment at its Welsh premises. The submission noted: 'The greater the volumes of long-term contract commitments in both larch and spruce that can be acquired, will add significant weight and security to that investment decision. It is unlikely that securing just one of the parcels tendered would provide sufficient critical mass in order to secure funding for the investment and, as such, we propose two gate prices which return greater value to NRW for increased volume by awarding both contracts.' It is clear from the sawmill operator's submission that the sawmill operator was looking to be awarded both larch contracts, and for NRW to provide long-term contractual commitments in relation to both larch and spruce, in order to secure the investment at the sawmill operator's Welsh premises.
- 8 The tenders were evaluated on 19 June 2013 based on a combination of price and each bidders' overall approach to the delivery of the contract. Following the evaluation, NRW held discussions with each of the bidders, in accordance with the ITT.
- 9 In July 2013, NRW produced a report on the tender. The Report stated that since the ITT had been issued, the disease has been found to have spread significantly north and eastward and that there would be a need to fell at least 350,000m³ (c 282,000 tonnes) of larch each year for several years to come. In consequence, the conditions and objectives of the tender had 'significantly changed'.
- 10 The report of July 2013 indicated that although the overall volume of larch to be felled to 2025/26 remained the same, NRW's revised larch removal plan of June 2013 required a greater volume of larch to be felled in the years to 2019/2020 and a reduced volume thereafter (ie 'front loading' the felling). I am satisfied that the report provided justification for NRW to deviate from the course set out in the ITT.
- 11 The report referred to the key risks if NRW did not award sufficient contracts that reflected the increased larch programme. The report also notes that the proposed sawmill operator small log line and Bidder 3's pelleting plant, were both much needed new and effective capacity for marketing the increasing larch harvest. I consider these were all relevant considerations for NRW to take into account in determining how best to proceed.
- 12 The report set out NRW's assessment of each of the three responses to the tender and looks at the respective financial returns. Each bid was awarded an overall percentage score as follows:
 - Bidder 1 – 92.78%
 - Bidder 2 – [the sawmill operator] – 79.31%
 - Bidder 3 – 75.42%

- 13 The report set out the advantages and disadvantages of different options for award, for example awarding the offer volume in accordance with the scoring of the ITT to Bidder 1. The report ultimately recommends offering the original volume to Bidder 1 and/or Bidder 3 and 'offering [the sawmill operator] further standing volume to address the massive increase in the LLD programme, together with a log and bar element'. One of the stated reasons for favouring this option was that it would encourage the investment in the sawmill operator's Welsh saw line and in Bidder 3's energy pelleting plant.
- 14 The report recognised that this recommended way forward required: 'stepping outside the terms of the original tender in terms of volume and location in response to current larch replacement plan demand'. The report also recognised that there was a risk of challenge from other timber processors but that, in NRW's view, there was unlikely to be any new bidders if the tender exercise were re-run. The report set out that the risk of challenge as a consequence of deviating from the ITT, was balanced against a greater risk to NRW of not doing enough given the growing levels of infection and the marketing/harvesting requirement and the risk of losing the sawmill operator's Welsh saw line, if NRW did not take action. An internal email from NRW's Head of Forest Operations on 8 July 2013 stated: 'we could run a further exercise, however, we are sure [we] will not receive new bids other than from the existing bidders in the current exercise – failure to do this will mean further delay in putting in place contracts to deal with the disease'.

Post tender competitive dialogue process

- 15 At the end of July 2013, NRW wrote to the bidders to inform them of the outcome of the tender process. The sawmill operator was informed that it had been unsuccessful in the tender process but that NRW was willing to make the sawmill operator an offer of a standing parcel of larch in Llandovery Forest of 65,000m³obs (c 52,400 tonnes) per annum for five years. This volume was equivalent to one of the two original tendered lots. The correspondence also set out that there was an option to extend this and a possibility of further supply of larch from direct production as part of an offer which NRW wished to discuss with the sawmill operator 'in order to secure the proposals that were put forward'.
- 16 It is apparent from contemporaneous emails that the sawmill operator was unhappy with the offer and were in dialogue with NRW about it.

- 17 On 2 August 2013, the sawmill operator wrote to NRW stating: 'as explained when we spoke earlier today, I am shocked and completely dismayed that NRW have treated the sawmill operator in such an off-hand and short-sighted way Clearly NRW value a harvesting contracting business and an English sawmill with greater enthusiasm than the sawmill operator, and if that remains the situation, we will invest our time and money elsewhere outside Wales. The 'offer' from [the Head of Forest Management] is totally inadequate and unacceptable. We need a far more robust and expansive commitment if we are to re-engage with NRW. We will contact you with specific details, however, time is of the essence, while we review our future strategic plan in Wales and inform Ministers of our decisions.'
- 18 NRW and the sawmill operator met on 12 August 2013 to discuss larch and spruce contracts. In an email of 22 August 2013, the Head of Forest Operations indicated to the sawmill operator that NRW was actively considering the sawmill operator's proposal in relation to spruce and larch contracts and that, in principle, NRW had no objection to offering an extension of LTCs for a period of between five and ten years.
- 19 In August 2013, NRW's Head of Timber Marketing prepared a paper: **Developing Options for the sawmill operator Larch Investment and wider guidance on replacement of existing Spruce LTCs**, for consideration by NRW's Executive Team. Whilst the paper was prepared for consideration by NRW's Executive Team, there is insufficient contemporaneous evidence that it was provided to or considered by the Executive Team.
- 20 The paper set out a revised larch clearance plan dated July 2013 which required an even greater amount to be felled in the earlier years – 350,000m³obs (c 282,000 tonnes) per annum for the years 2014/15 to 2019/20. It noted that the larch that had been offered to the market by NRW had been absorbed by substitution, but that there was a need to increase overall processing capacity for larch.
- 21 The paper stated that two standing contracts of 65,000m³obs (c 52,400 tonnes) each per annum for five years were offered to Bidder 1 and one to Bidder 3, all in the Coed y Cymoedd Forest District area and a further standing contract for 65,000m³obs (c 52,400 tonnes) was offered to the sawmill operator in Llandoverly Forest District, ie a contract the same size as either of the two contracts advertised in the ITT, but in a different location. The paper noted that the sawmill operator was 'not content with the offer that was made to them'. The paper went on to explain that NRW was aware that the sawmill operator needed a further guaranteed supply of larch volume before committing to increase the capacity at its Welsh premises, and that it had indicated that investment at those premises would not go ahead unless they could be offered some surety on continuing supply of the spruce element of the mill. This reflected the sawmill operator's statements in its response to the ITT.

- 22 The paper set out several options but concluded that it was essential that the proposed development at the operator's Welsh premises was secured 'as it will provide a marketing solution to the sawlog element that will be coming forward from the potential seven million cubic metres of standing larch [from both public and private woodland] that will need to be felled in Wales and the Marches over the next 10 to 12 years'. The document also showed that NRW's larch clearance plan estimated that NRW would have to clear 2.8 million cubic metres of standing larch by 2025/26 and standing infected stands at the time already amounted to nearly one million cubic metres on the Welsh Estate with further infection likely.
- 23 The paper also notes that it is unlikely that NRW would see an equally good proposal if it went out to market, (although there is no evidence set out in the paper to support that contention), and that time was of the essence in respect of the planned investment at the sawmill operator's Welsh premises.
- 24 The paper recommended offering the sawmill operator contracts for both larch and spruce. However, as noted above, there is insufficient contemporaneous evidence that the paper was presented to the Executive Team or NRW's Board for decision. I therefore understand that the decision to proceed on this basis was therefore taken by NRW officers exercising delegated powers. The paper indicated that the recommended option could be viewed as contentious: 'we recognise that there is a danger of seeming to favour the sawmill operator if only volume that was destined to their facility was granted a long-term contract extension, having the effect of reducing opportunity for others in future sales'.
- 25 A paper presented to the Board dated 15 October 2013 titled: 'Phytophthora ramorum Update' noted that 'the overall level of non-compliance with Statutory Plant Health Notices increased sharply at the end of August, as this was the deadline for compliance, and that 2000Ha of new infections were identified on the Welsh Government Woodland Estate in that year'. The update referred to the competitive bidding process and the contracts offered and noted that the final amount offered may be higher depending on the outcome of negotiations relating to investment decisions by processors. However, there is insufficient evidence that the details of the negotiations were brought to the attention of the Executive Team or the Board at the time.
- 26 In November 2013, the Head of Forest Operations sought further information from the sawmill operator in order for NRW to make a final decision. The sawmill operator responded on 11 November 2013.
- 27 On 14 November 2013, the Head of Forest Operations emailed the sawmill operator to confirm that, in principle, NRW was satisfied with the pricing mechanism and was entering into the ten year contract. NRW has not been able to provide internal emails or documentation in this period regarding its decision making, and so I have been unable to confirm the internal reasons for the decision. In his email of 14 November 2013, the Head of Forest Operations stated that there would be detail to agree with the sawmill operator and this would progress over the coming weeks.

28 NRW has recently provided me with some further contemporaneous evidence of the contract negotiations that took place between November 2013 and May 2014, although I note that there remain some gaps in the documentation.

Contract Award

29 In May 2014, NRW's former Executive Director National Services signed eight timber sales contracts between NRW and the sawmill operator and an overarching Memorandum of Agreement. The contractual start date is specified as 1 April 2014. The contracts remain in force.

30 The eight linked timber sales contracts are set out in [Table 1](#).

Table 1: timber sales contracts awarded by NRW to the sawmill operator in May 2014

Contract	Type of contract	Contract period (years)	Species type	Contract Volume (tonnes)	Annual Volume (tonnes)
A	Sale of pre-felled timber	10	Spruce	100,000	10,000
B	Sale of pre-felled timber	10	Spruce	350,000	35,000
C	Sale of pre-felled timber	10	Larch	70,000	7,000
D	Sale of pre-felled timber	10	Larch	150,000	15,000
E	Sale of standing trees	10	Larch	525,000	52,500
F	Sale of standing trees	10	Spruce	162,000	16,200
G	Sale of standing trees	10	Spruce	242,000	24,200
H	Sale of standing trees	5	Larch	262,500	52,500
				1,861,500	212,400

New saw line investment

31 In August 2015, NRW's former Head of Forest Operations wrote to the sawmill operator regarding NRW's concern that the sawmill operator would not meet its contractual duty to construct and commence operating a new saw line at its Welsh premises by 31 March 2016. The sawmill operator responded setting out reasons why the project had been delayed and requesting an extension to the contractual deadline. In March 2016, NRW and the sawmill operator entered into a contract variation whereby the deadline for the operator to construct and commence operation of the new saw line was extended until 31 March 2017.

Compliance with framework of authority

Internal delegation arrangements

- 32 The functions of NRW are set out in the Natural Resources Body for Wales (Establishment) Order 2012 (the 2012 Order). These functions include undertaking any devolved function of the Forestry Commissioners. NRW is therefore empowered to manage the publicly-owned forest estate and to make decisions necessary to effectively carry out that function. The 2012 Order sets out that NRW may delegate the exercise of its functions to a committee, sub-committee, member or employee of NRW. This includes entering into contracts with external suppliers and purchasers.
- 33 The Board approved a 'Financial Scheme of Delegation' that ensured that all financial activities of NRW were delegated to an agreed level of authority or specific post holder. It allowed the Board and Executive Team to delegate decision-making responsibility for financial matters. The Financial Scheme of Delegation in place in 2014 delegated authority to the Head of Enterprise to sign harvesting timber contracts with a value above £1 million.
- 34 The contracts with the sawmill operator were signed off by NRW's Executive Director for National Services, who was a member of NRW's Executive Team with executive responsibilities for forestry operations (and the line manager of the Head of Enterprise). I am of the view that the Executive Director for National Services had the necessary delegated authority to enter into timber sales of any value.
- 35 NRW's Financial Scheme of Delegation stated that: 'all staff must alert their line manager if they are involved in any financial decisions which they believe the Chief Executive and/or the Board would want to be consulted with, particularly if it involves novel, unusual or financially contentious action'. I consider that the decision to contract with the sawmill operator was contentious and repercussive for the reasons set out in [paragraph 44](#).
- 36 Although NRW considers that the Financial Scheme of Delegation did not require the matter to be referred to NRW's Board or Executive Team, it has provided evidence that the CEO and Board were, at least, aware of the negotiations with the sawmill operator. NRW has provided me with a letter dated 16 October 2016 from NRW's former Executive Director for National Services in which he states that he kept NRW's Chief Executive apprised of the ongoing negotiations with the sawmill operator. In addition, NRW has provided a Board paper dated 15 October 2013 that referred to the competitive bidding process and that there were further negotiations relating to investment decisions by processors (but, as noted above, the paper did not provide further detail). A non-executive Board member attended a meeting with the sawmill operator in August 2013 and NRW has provided board minutes showing that this was discussed at a Board meeting on 3 September 2013.

37 The Chief Executive of NRW has confirmed to me that both he and the Board were aware of the negotiations with the sawmill operator and that the requirements of the Financial Scheme of Delegation were complied with. Nevertheless, I am concerned that the Board and/or Executive Team do not appear to have scrutinised and discussed the proposal given its financial size and contentious and repercussive nature.

Requirement to refer novel, repercussive or contentious activities and proposals to the Welsh Government for scrutiny and/or approval

- 38 Whilst NRW complied with its internal delegation arrangements, the principal document that provides authority for NRW transactions is the NRW Framework Document. The Framework Document sets out that payment of grant-in-aid to NRW is conditional upon the satisfactory performance by NRW of all its obligations as set out in the Framework Document, which includes compliance with Welsh Government publication, 'Managing Welsh Public Money'. The requirement to comply with Managing Welsh Public Money relates to section 70 (2) of the Government of Wales Act 2006 (2) which states that: 'the Welsh Ministers may attach conditions to the giving of financial assistance by them; and the conditions which may be attached include, in particular, conditions requiring the repayment of the whole or any part of a grant, or the making of any other payments, in any circumstances'.
- 39 Under the title 'Expenditure', paragraph 3.9.1 of the NRW Framework Document says that: 'NRW shall comply with the delegations set out in Annex 5'. Annex 5 sets out that approval of the sponsor team is required for any novel, contentious or repercussive proposals.
- 40 Paragraph 3.9.8 of the Framework Document provides that NRW's income-generating activity must be undertaken in accordance with the terms of Managing Welsh Public Money and the Framework Document. In addition, paragraph 1.2.9 of the Framework Document states that the Chief Executive of NRW, as Accounting Officer, is personally responsible for ensuring compliance with the requirements of Managing Welsh Public Money.

- 41 I have considered the version of the Welsh Government's Managing Welsh Public Money which was in force at the relevant time. This document states in paragraph 3.8.3: 'The framework document agreed between a public body and its sponsor always envisages the sponsor department exercising meaningful oversight of the public body's strategy and performance, pay arrangements and/or major financial transactions, eg by monthly returns, standard delegations, exception reporting or other techniques. Public bodies should refer to their sponsor departments any activities which appear novel, contentious or repercussive; in turn the sponsor department may need to seek WAG's Corporate Governance Unit consent.' Managing Welsh Public Money does not confine the requirement to refer novel, contentious or repercussive activities to expenditure.
- 42 I am therefore satisfied, that Managing Welsh Public Money required NRW to refer any activities to its Welsh Government sponsor departments which appeared novel, contentious or repercussive.
- 43 Neither the Framework Document nor Managing Welsh Public Money define 'novel, contentious or repercussive' proposals, though the latter gives some examples. Determining whether a proposal or activity is novel, contentious or repercussive, is therefore a matter of fact and judgement.
- 44 The Oxford English Dictionary defines 'contentious' as 'causing or likely to cause an argument; controversial' and defines the noun 'repercussion' as 'an unintended consequence of an event or action, especially an unwelcome one' (the adjective 'repercussive' is not in the dictionary). NRW's Chief Executive has told me that he does not consider the decision to contract with the sawmill operator in May 2014 to be contentious or repercussive. I disagree and consider that it was contentious and repercussive for the following reasons:
- The contracts awarded to the sawmill operator were very substantial in size, NRW has estimated that the volume of timber sold under these contracts represented approximately 20 to 25% of the total timber made available to the market by NRW over a ten year period and the award of such a large contract to one purchaser had wider market repercussions. NRW's Executive Team Paper of August 2013 acknowledges that in consequence of the proposed contract with the sawmill operator 'there will be very little spruce to offer standing sales merchants over the next five years'.
 - The contracts for larch and spruce were awarded following a competitive tender for larch contracts (in which the sawmill operator was not the winning bidder, however, NRW decided to offer contracts for larch to all three bidders) and therefore no other potential purchasers were given the opportunity to purchase the volume of larch and spruce timber which was ultimately awarded to the sawmill operator. NRW's view is that there was no market for diseased larch based on (a) the lack of interest in 21 individual parcels of trees that NRW sought to sell between November 2012 and September 2013 referred to in [paragraph 71](#); and (b) that only three bids were received in response to the 2013 tender referred to in [paragraphs 5 to](#)

14. In my view, the size of those parcels and tender offer are not comparable to the offer of eight Long Term Contracts (LTCs) for both diseased larch and spruce, particularly as the sawmill operator itself made clear that four LTCs for larch would be insufficient for it to invest in the new saw line. The contract volume awarded to the sawmill operator was designed to enable it to make major investment in its sawmill. This investment enabled the sawmill operator to significantly increase its processing capacity. NRW considers that it was highly unlikely that any other operators would have been interested in such significant volumes of diseased larch and in the timescales in which NRW had to act and that it was aware of the risk of challenge on this point but that their 'professional view was that there was no alternative'. However, there is little within the contemporaneous documentation to evidence that NRW officials gave careful consideration to whether the higher volumes might draw interest from a wider range of timber companies (ie, companies that did not bid in the 2013 competition) nor whether those volumes might have sufficed to encourage other competitors to invest in additional capacity. In my view, the commitment of NRW to sell the sawmill operator a high volume of timber over a ten year period would appear to be an opportunity which other operators may have been interested in.

- The decision to award the contracts was not informed by relevant market testing.
- Internal papers prepared by NRW acknowledged the risks associated with awarding these contracts given that the sawmill operator had been unsuccessful in the tender exercise conducted in 2013. The papers also acknowledged that the decision to award the contracts to the sawmill operator in this way might be subject to challenge.

45 I therefore consider that the proposal should have been referred to NRW's sponsor division within the Welsh Government in accordance with the requirements of the Framework Document and Managing Welsh Public Money.

46 NRW has told me that at the time it did not regard the award of the contracts as contentious or repercussive. NRW has also told me that the Board and Welsh Government were aware of the process and NRW has provided me with a copy of an email sent to NRW's Sponsor division within the Welsh Government on 4 August 2013 (nine months before the contracts were entered into). The email was sent to the Welsh Government following receipt of the correspondence from the sawmill operator referred to in [paragraph 17](#). The email to the Welsh Government set out NRW's concern that the sawmill operator might seek to lobby Ministers following its unsuccessful tender and its unwillingness to accept an offer it viewed as 'totally inadequate and unacceptable'.

- 47 The email does not specify the details of the offer made to the sawmill operator and states that: 'we will continue to speak with [the sawmill operator] and develop lines to take in pursuit of a good outcome for all parties'. I do not consider the email represents a referral to the Welsh Government. I am of the view that the purpose was to alert the Welsh Government of potential lobbying and not to make the Welsh Government aware of a matter that was contentious and repercussive. Furthermore, as at 4 August 2013, the volume of timber offered to the sawmill operator was only 14% of the total eventually sold to the sawmill operator under the contracts entered into in May 2014, and the offer was solely for larch.
- 48 The Welsh Government has told me that whilst its forestry officials were aware that negotiations were taking place between NRW and the sawmill operator, they were not involved in the detail. Furthermore, the Welsh Government's forestry officials briefed the relevant Minister prior to a ministerial visit to the sawmill operator's premises that: 'Welsh Government has an interest in ensuring a competitive timber market, both for the good of the sector and for its own revenues via NRW's timber sales. Opportunities for [the sawmill operator] to expand should be balanced by fair open and transparent marketing of timber from the [Welsh Government] woodland estate.'
- 49 I therefore consider that NRW did not meet the requirements of the Framework Document and Managing Welsh Public Money to refer a contentious and repercussive proposal to the Welsh Government. I consider that the transactions related to these contracts which are included within NRW's financial statements for 2015/2016 were outside the framework of authority governing them and are therefore irregular. In consequence, I have qualified my regularity opinion on NRW's 2015/2016 financial statements.

Compliance with public law principles in decision-making

Impact of legality concerns on the regularity opinion

- 50 Where there is significant uncertainty that transactions are lawful, I am unable to provide a clear opinion. This is because positive assurance cannot reasonably be given where there is significant uncertainty.
- 51 As part of my deliberations leading to giving my regularity opinion on NRW's financial statements for 2015/16, I accordingly considered concerns relating to the legality of transactions associated with contracts NRW entered into with the sawmill operator in May 2014. These concerns were whether NRW's decision to award the contracts to the sawmill operator was lawful in terms of public law and State aid rules.

- 52 I note that my consideration of the transactions arises in the context of my audit functions and does not bear on the validity or enforceability of the decisions taken by NRW (and I note NRW's point that none of the industry representatives sought to bring a challenge to the award of the contracts). The decision to award the contracts remain valid in the absence of any challenge and quashing by a Court. My regularity opinion, however, takes the form of positive assurance, which means that I state whether transactions are in accordance with the authorities that govern them.
- 53 My considerations of these matters are set out below.
- 54 For a decision of a public body to be lawful it must be made in accordance with applicable legislation and with public law principles (for example, the decision must not be irrational). A decision should be taken in accordance with the public body's policies, unless there is a good reason to depart from them.

Powers

- 55 I have considered whether NRW had the legal powers to enter into contracts for the sale of timber with the sawmill operator in May 2014. At the relevant time, the Forestry Act 1967 (the 'Act') applied to NRW. Under the Act, NRW has a general duty of promoting the interests of forestry, the development of afforestation and the production and supply of timber and other forest products. NRW has the power to sell or dispose of any timber belonging to it and to generally promote the supply, sale, utilisation and conversion of timber.
- 56 In addition, the 2012 Order provided at the relevant time that the purpose of NRW was to ensure that the environment and natural resources of Wales were: (a) sustainably maintained, (b) sustainably enhanced and (c) sustainably used. Under the 2012 Order, the NRW has the power to charge 'for work that it carries out and for goods, services and facilities that it provides'. It also has incidental powers under the 2012 Order to 'do anything that appears to it to be conducive or incidental to the discharge of its functions', and in particular (amongst other things) to enter into agreements, and acquire or dispose of property.
- 57 NRW was also subject to statutory notices under the Plant Health (Forestry) Order 2005 in relation to the diseased larch trees in specified areas which required the felling, destruction and/or containment of infected trees within a specified timescale. NRW was therefore under a legal duty in relation to the diseased larch trees and sought to comply with that duty by exercising its power to enter into contracts for the sale of standing and pre-felled timber.
- 58 I am therefore satisfied that NRW had the powers required to enter into timber sales contracts in May 2014.

Policies

- 59 As noted above, public bodies must: (a) take into account and (b) follow relevant policies, unless they have a good reason to depart from them, or at the very least have stated clear reasons for the departures. A failure to do so can render a decision, and in turn an item of account, contrary to law. Public law also requires that any reasons given are substantiated.
- 60 I have seen some evidence that NRW took its policies into account and considered whether there were good reasons to depart from them. For example, the tender evaluation report produced in July and the Executive Team paper dated August 2013 contained consideration of different options, including going back to the market.
- 61 However, there is an evidential gap (in terms of NRW's internal decision making) between the Executive Team Paper dated August 2013 and the contracts entered into by NRW in May 2014. If the policies were not taken into account but the decision nevertheless clearly followed the policy, this would be unlikely to render the contracts and associated transactions unlawful. I have therefore considered whether there are incidences of NRW's policies being departed from with no good reasons set out for doing so.
- 62 NRW's timber sales policy, at the relevant time was contained in the FCW Timber Marketing Strategy 2011 – 2016. This document covered both standing and roadside sales. It also provided that NRW's marketing objectives in selling timber were that it would:
- 'Secure best value from the sale of timber by offering it for sale in a fair, open and transparent way;
 - offer timber to the market in ways that allow the greatest practicable number of customers to compete for it and in ways that recognise the business needs of NRW's customers and enable them to add the greatest possible value to it;
 - offer timber in ways that supports investment in the whole supply chain, from harvesting through to processing and which focuses on areas where that supply chain is weaker; and
 - offer timber in ways that encourage its use to best effect to help Wales to reduce its carbon footprint.'
- 63 In this case the spruce and larch timber was not offered for sale to the market, potentially contrary to (a) and (b) above. However, the document also includes a section: 'Dealing with unforeseen events' and, in particular, a statement that: 'In exceptional circumstances only we may decide to negotiate the sale of timber to customers who are able to respond quickly to events'.

- 64 NRW argues, and has provided contemporaneous evidence in support, that the circumstances it faced in 2013, ie the rapid increase in the spread of P Ramorum during the summer months represented 'exceptional circumstances' that warranted departing from its stated timber marketing objectives. This was considered necessary as NRW needed to act quickly to find a long-term solution to combating the disease.
- 65 I am accordingly satisfied that NRW has demonstrated that there was a good reason to depart from its usual policy and that there were exceptional circumstances such that it might decide to negotiate the sale of timber to those customers who could respond quickly.

Process

- 66 In paragraphs 5 to 31 I have set out my understanding of the decision-making process followed by NRW leading to contracts being awarded to the sawmill operator in May 2014.
- 67 Considering the decision-making process as a whole, it is evident that NRW took steps at various stages to assess the advantages and disadvantages of the options available to it. However, crucially, NRW has been able to provide me with very little documentation in respect of its decision to enter into the larch and spruce contracts and the Memorandum of Agreement. In particular, there is little documentation relating to the decision to enter into the contracts (which appears to have been taken in November 2013). NRW has recently provided me with documentation relating to the negotiations that took place between August 2013 and May 2014. NRW position is that the negotiations to 14 November were in line with the decision making arising from the Executive Team paper and that the contracts which were concluded were largely on Forestry Commission/NRW standard terms and in line with the strategy in the Executive Team paper. In my view, on the basis of the records provided by NRW, there is insufficient documentation in relation to the decision to enter into the contracts and it is not possible to be certain what factors were considered by the decision maker when entering into the contracts and consequently whether the decisions taken were lawful.
- 68 The failure of NRW to maintain sufficient contemporaneous documentation setting out its decisions during this period and the reasons for those decisions has meant that I have been unable to satisfy myself on some key issues. NRW has told me that having only just concluded an open market exercise for diseased larch, it took the view that the time pressures, driven by the rapid spread of the disease, were such that repeating the exercise would significantly delay its response by several additional months and such an exercise was deemed by its experienced timber marketing team as highly unlikely to attract any new interested parties.

- 69 I am however not persuaded that the urgent need for NRW to contract to address the rapid spread of P Ramorum was the reason, or the only reason NRW entered into the contracts with the sawmill operator. I am concerned that one of NRW's considerations may have been to secure the investment at the sawmill operator's premises. That is unlikely to be a legitimate consideration in and of itself. NRW has provided some evidence to support the award of contracts on the basis of urgency and has stated that its purpose was to increase capacity for processing diseased larch and that there were no other options in the market, but in its internal documents it also refers to the objective of wanting to support the sawmill operator's investment.
- 70 NRW maintains, and I accept, that it may have been the case that NRW's underlying consideration was to increase capacity as a way of dealing with the increasing amount of infected larch to be processed in the years to come. Whilst this was a potentially valid motive, I have received representations from industry representatives that in 2013 there was significant unused capacity in other Welsh sawmills which would have taken, subject to price, as much timber as could be supplied. If that is correct, it is clearly a relevant consideration which NRW should have been aware of and taken into account. If it was aware of it, it would call into question NRW's motive in entering into these contracts with the sawmill operator. NRW strongly disputes the assertion that there was unused sawmill capacity.
- 71 NRW holds the view that there was no market for infected larch because during November 2012 to September 2013 Forestry Commission/NRW attempted to sell 21 individual parcels of infected larch and, of these, seven received no bids, eight received only a single bid and there were no parcels which received more than three bids. NRW has informed me that the average price was a negative price of -£20.71 per tonne. NRW also considers that the three bids received in response to the 2013 tender show that there was neither demand for, nor capacity for, switching to diseased larch. As stated above, in my view, the size of those parcels and tender offer are not comparable to the contracts which NRW entered into with the sawmill operator. The contract volume awarded to the sawmill operator was designed to enable it to make major investment in its sawmill. This investment enabled the sawmill operator to significantly increase its processing capacity. The commitment of NRW to sell the sawmill operator a high volume of timber over a ten year period would appear to be an opportunity which other operators may have been interested in.
- 72 I am also concerned that NRW may have been influenced by the sawmill operator's statement that unless NRW changed its position it would seek to invest its time and money outside of Wales ([paragraph 17](#) refers). I note that NRW informed the Welsh Government by email on 4 August 2016 that the sawmill operator was using such statements to apply pressure. I also note that NRW said that it was used to this type of behaviour and would not be influenced by it. I remain, however, concerned the sawmill operator's pressure may have influenced NRW because NRW's documentation as a whole does not set out a clear record of the decision-making process.

- 73 I am of the view that serious questions remain as to why, given that the sawmill operator was unsuccessful in the competitive tender, it was ultimately awarded such a high volume of timber on the basis that NRW felt that increased capacity was needed. This is within the context that NRW did not go out to market to see whether other operators could increase capacity in a way which would secure better value for money.
- 74 Whilst I have concerns regarding the decision-making process, the evidence is not sufficient for me to reach a conclusion that the decision to enter into the contracts was in breach of public law principles. My uncertainty does not mean that the contracts should now be regarded as unlawful as set out in [paragraph 52](#), however, means that I am unable to give an unqualified regularity opinion on the financial statements.
- 75 The Chief Executive of Natural Resources Wales has told me that he considers that qualification of the regularity opinion is disproportionate to the shortcomings identified and that he disagrees with my conclusions and relies on legal advice which NRW sought during the course of my audit investigation and shared with me. However, I have sought my own legal advice from Counsel (including in relation to NRW's advice) and I agree with the advice I have received, which is to the effect that there is insufficient evidence to conclude that the decision-making process was in compliance with public law principles and State aid rules. The significant uncertainty which exists means that I consider that the correct and proportionate action for me to take as the auditor of NRW is to qualify my regularity opinion.

Compliance with State aid rules

- 76 The decision of NRW to enter into timber sales contracts with the sawmill operator without opening the opportunity to the wider market led me to consider whether NRW has provided the sawmill operator with unlawful State aid.
- 77 State aid is any aid granted by an EU Member State or through State resources in any form whatsoever, which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods, in so far as it affects trade between Member States (Article 107 of the Treaty on the Functioning of the European Union). The provision of State aid is unlawful unless authorised in advance, whether by an existing 'block exemption' or by individual authorisation granted by the European Commission in response to a notification from the relevant State.

- 78 I have sought legal advice on whether or not the award of the contracts to the sawmill operator constituted a grant of State aid to the sawmill operator. I am advised that this turns on whether or not those contracts constituted the provision of an 'economic advantage' to the sawmill operator. If they did, and the value of that advantage was potentially material to inter-State trade (a benchmark for materiality in this context is the European Commission's State aid *de minimis* threshold of €200,000), then the other conditions for State aid will also be satisfied because such an economic advantage:
- a. would plainly be granted from State resources, since the assets of NRW (including trees that it has the right to sell) are State resources, and decisions of NRW are imputable to the United Kingdom as an EU Member State;
 - b. would plainly be 'selective', since the advantage would have been given specifically to the sawmill operator and not to other sawmill operators; and
 - c. would also be liable to distort competition and affect inter-State trade, since (i) the advantage would strengthen the overall economic position of the corporate group of which the sawmill operator is part, and (ii) the markets (such as for timber and timber products) in which that corporate group competes are markets in which there is clearly a significant amount of cross-border trade within the EU.
- 79 The kinds of measures which can constitute an 'economic advantage' provided by the State, include direct financial measures (eg capital investments or interest free loans), indirect financial measures (eg waiver of debts or exemptions from taxes) and the provision of assets, services or dedicated infrastructure free of charge or at an undervalue. The award of a contract will constitute an advantage where its terms are unduly generous (as compared with 'market terms') to the undertaking, whether because those terms provide for the supply of goods or services to the undertaking at an undervalue, or because they provide for the undertaking to receive remuneration for the goods or services that it supplies which exceeds the market price.
- 80 The burden of proof in relation to showing that a measure constitutes an economic advantage is on the person (usually the European Commission) alleging that it does so. The European Commission has, in its decisions and published guidelines, adopted the position that it is incumbent on a State body that is awarding a contract, or selling land or other valuable assets, to either (a) carry out a competitive process or, (b) where it is not practicable to hold a competition, at least use 'market testing' or some other mechanism for verifying that the terms to which it ultimately agrees are in accordance with market terms and therefore do not confer any economic advantage. Where the State body has not done so, the position as a matter of law is still that the burden of proof of advantage is on the person alleging the advantage. Nevertheless, the European Commission will typically take the position that it is entitled to draw from the circumstances an inference (or 'rebuttable presumption') that the terms of the contract were generous

to the undertaking as compared with the terms that would have been produced by a competitive process.

- 81 No economic advantage arises where the State is doing something (such as selling a piece of land that it owns) which can also be done by non-State entities, and does so on terms that a non-State entity in a comparable situation might well have been willing to accept *for commercial reasons*. This principle is known as the 'market economy operator principle'. To apply that principle, it is necessary to compare the behaviour of NRW with what a market operator would have done in comparable circumstances. This may give rise to evidential difficulties because evidence of what a market operator would have done may not be available and because there may be room for argument as to whether certain objectives or interests should, or should not, be amongst those imputed to the hypothetical market operator. I am not persuaded that NRW acted as a market operator would have done as one of NRW's reasons for seeking to increase capacity for processing diseased larch was to ensure increased capacity, both for the public sector and the private sector estates, which is not a consideration which a market operator would have taken into account.
- 82 NRW's position is that the sawmill operator did not have significant numbers of overseas customers and therefore that the contracts did not have the requisite effect on inter-State trade. However, I am advised that a selective advantage to a particular operator is effectively assumed to affect inter-State trade where the undertaking receiving that advantage is active in markets characterised by significant volumes of inter-State trade. That is so regardless of whether the undertaking itself supplies customers in, or has a presence in, any other EU State. There is very substantial inter-State trade in markets for timber and timber products and the sawmill operator is involved in cross-border trade.
- 83 It is apparent from the contemporaneous documents that the terms of the contracts were not determined either by the outcome of a competition for meeting NRW's relevant requirements, or by other relevant market testing focussed upon those requirements. Although NRW's officials were informed by their experience of the bids received in 2013, the difference between the volumes covered by that competition, as compared with the volumes being awarded to the sawmill operator alone, was very substantial. There is little within the contemporaneous documentation to provide evidence that NRW officials gave careful consideration to whether the higher volumes might draw interest from a wider range of timber companies (ie companies that did not bid in the 2013 competition, potentially including companies without an existing presence in Wales). Nor do they appear to have considered whether those volumes might have sufficed to encourage the sawmill operator's competitors with sawmills in Wales to invest in additional capacity so as to be able to handle those volumes. I am not aware of any convincing evidence which would allow a conclusion that these possibilities could be dismissed out of hand as being wholly unrealistic.

- 84 If the terms of the contracts reflected market prices then there would be no State aid arising from the contracts, and I accept that the contracts may be on market terms. However, NRW's decision to award the contracts to the sawmill operator was not informed by relevant market testing, and was also not supported by persuasive reasoning to support a conclusion that seeking alternative providers would inevitably have proved fruitless. In my view, NRW failed to follow appropriate processes for ensuring that the outputs for which it contracted with the sawmill operator were obtained on market terms. This failure gives rise to doubt as to the compliance of the contracts with the State aid rules. In view of this uncertainty, I am again unable to give an unqualified regularity opinion on the financial statements.
- 85 As noted at [paragraph 75](#) above, the Chief Executive of Natural Resources Wales has told me that he considers that qualification of the regularity opinion is disproportionate to the shortcomings identified and that he disagrees with my conclusions and relies on legal advice which NRW sought during the course of my audit investigation and shared with me. However, I have sought my own legal advice (including in relation to NRW's advice), with which I agree and which is to the effect that there is insufficient evidence to conclude that the decision-making process was in compliance with public law principles and State aid rules. The significant uncertainty which exists means that I consider that the correct and proportionate action for me to take as the auditor of NRW is to qualify my regularity opinion.

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Auditor General for Wales

The development of Natural Resources Wales



WALES AUDIT OFFICE
SWYDDFA ARCHWILIO CYMRU



I have prepared and published this report in accordance with the Government of Wales Acts 1998 and 2006.

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All photos courtesy of Natural Resource Wales

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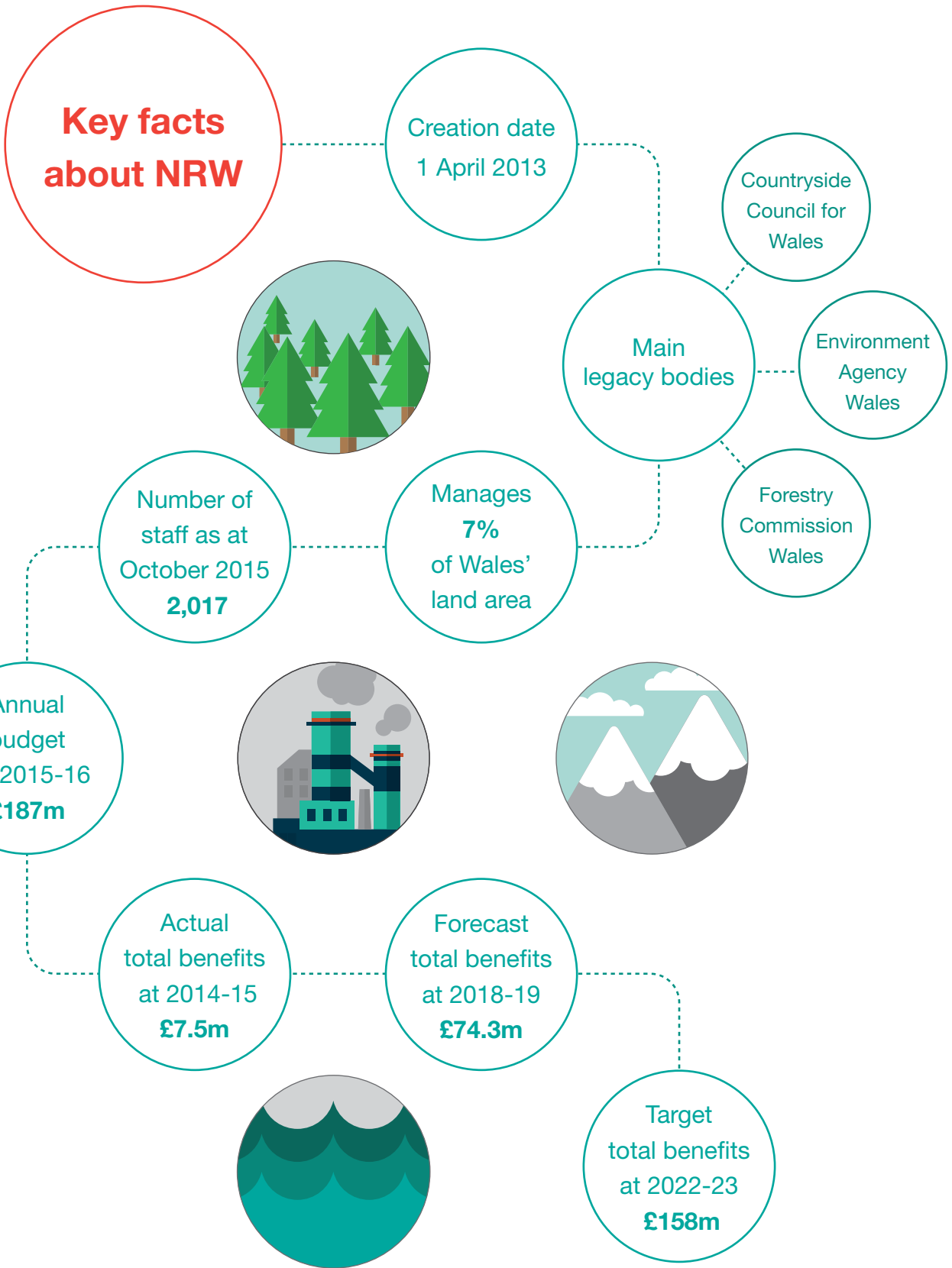
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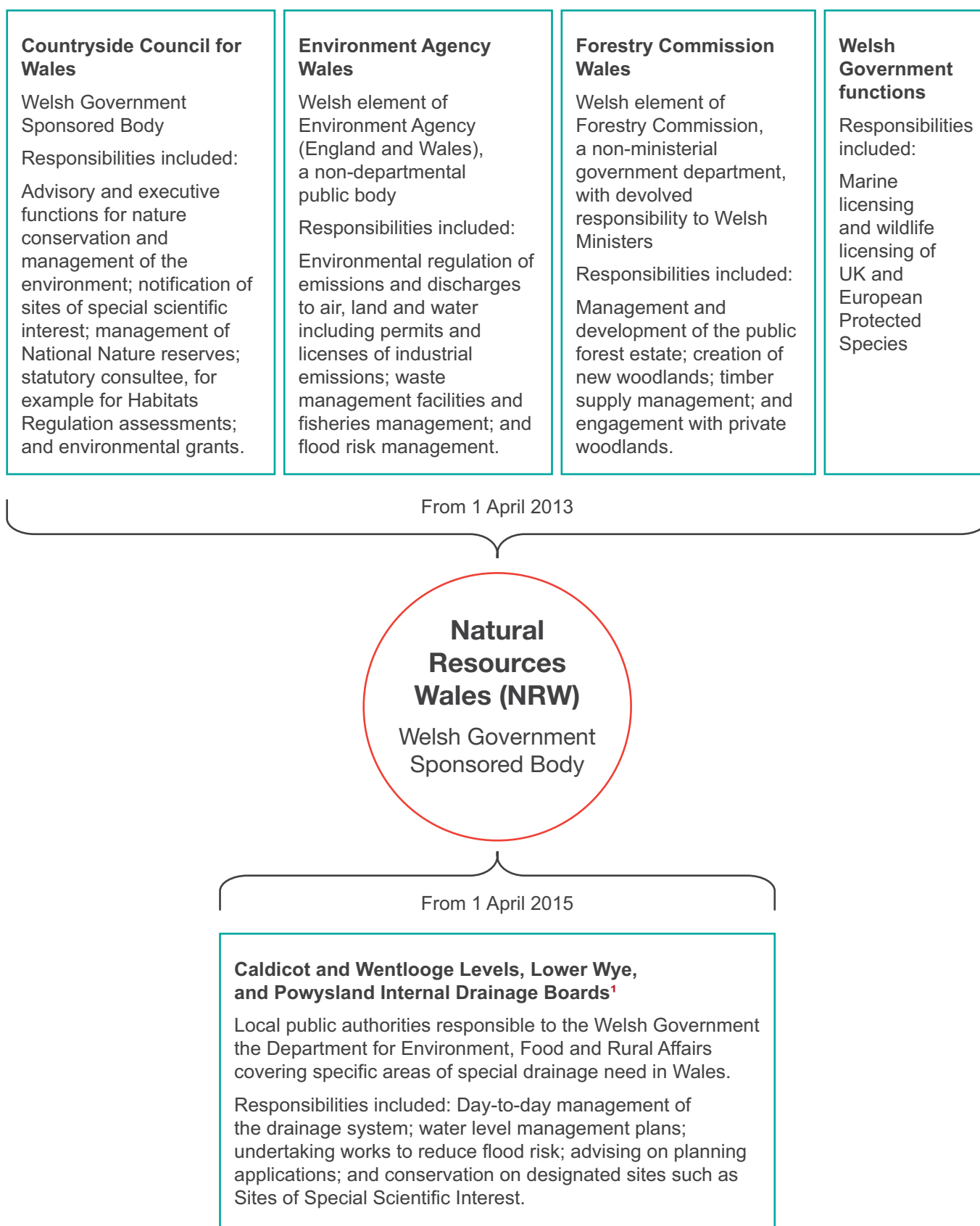
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Summary report



Figure 1 – Legacy organisations and their responsibilities



Note:

¹ Caldicot and Wentlooge Levels Internal Drainage Board operated wholly in Wales. Lower Wye and Powysland Internal Drainage Boards were split along the English and Welsh border, with the functions relating to areas in Wales transferred to NRW.

Source: Wales Audit Office, using information from [Natural Resources Wales](#)

- 1 Natural Resources Wales (NRW) is by far the largest Welsh Government sponsored body¹. It has an annual budget of £187 million for 2015-16 and as at October 2015 employed 1,941 permanent staff, 71 temporary staff and five apprentices throughout Wales. The Welsh Government created NRW on 1 April 2013, replacing three legacy bodies – the Countryside Council for Wales, Environment Agency Wales, and Forestry Commission Wales – as well as incorporating certain Welsh Government functions (Figure 1). On 1 April 2015, the Welsh Government transferred the functions of the three Internal Drainage Boards operating wholly or partly in Wales into NRW.
- 2 NRW has a wide and complex range of roles and responsibilities, which contribute to delivering Welsh Government policy objectives relating to the environment, economy and quality of life (Figure 2). The Welsh Government sets out the key priorities for NRW in annual remit letters.

Figure 2 – NRW's roles and responsibilities

Adviser	Principal adviser to Welsh Government, and adviser to industry and the wider public and voluntary sector, and communicator about issues relating to the environment and its natural resources.
Regulator	Protecting people and the environment including marine, forest and waste industries, and prosecuting those who breach the regulations that NRW is responsible for.
Designator	For Sites of Special Scientific Interest – areas of particular value for their wildlife or geology, Areas of Outstanding Natural Beauty, and National Parks, as well as declaring National Nature Reserves.
Responder	To some 9,000 reported environmental incidents a year as a Category 1 emergency responder.
Statutory consultee	To some 9,000 planning applications a year.
Manager/Operator	Managing seven per cent of Wales' land area including woodlands, National Nature Reserves, water and flood defences, and operating visitor centres, recreation facilities and a laboratory.
Partner, Educator and Enabler	Key collaborator with the public, private and voluntary sectors, providing grant aid, and helping a wide range of people use the environment as a learning resource; acting as a catalyst for others' work.
Evidence gatherer	Monitoring the environment, commissioning and undertaking research, developing knowledge, and being a public records body.
Employer	Of over 1,900 [permanent] staff, as well as supporting other employment through contract work and volunteering opportunities.

Source: Natural Resources Wales 2014-15 Annual Report

¹ Welsh Government sponsored bodies are public bodies funded by the Welsh Government that have a role in the processes of Government but are not part of Government departments. Each sponsored body has a framework agreement with the Welsh Government setting out roles and responsibilities. Sponsored bodies operate at arms-length from Welsh Government Ministers, but the Board of the sponsored body is accountable to Ministers through their sponsor department within the Welsh Government. Other sponsored bodies include, for example, the National Museum of Wales, the Care Council for Wales and Sport Wales.

- 3 The business case for setting up NRW identified a range of benefits that the Welsh Government expected to be realised through the creation of NRW, centred around better outcomes, better delivery for Wales and better value for money. The business case identified quantifiable benefits that the Welsh Government expected NRW to make, totalling £158 million over the 10 years to the end of 2022-23². The Welsh Government and NRW revised the business case in July 2013, varying the profile of forecast benefits per year but keeping the overall total 10-year forecast of £158 million the same³. The total expected costs of NRW's creation were £66 million in the revised business case, giving a forecast net saving of £92 million to 2022-23.
- 4 NRW's creation involved a range of potential risks and challenges and was subject to considerable scrutiny. Some organisations, particularly in the forestry sector, contested the original decision to replace the three organisations, raising concerns over continuity and a dilution of focus on their particular areas of interest. The original business case for the creation of NRW, prepared by the Welsh Government, identified several strategic risks including:
 - a negative stakeholder response;
 - b a lack of common purpose;
 - c adverse impact on staff and organisational performance;
 - d loss of organisational skills; and
 - e disruption to cross border working arrangements.
- 5 The National Assembly for Wales' Environment and Sustainability Committee considered some of these issues in its 2012 inquiry to assess whether the business case that informed the Welsh Government's decision to create a new body would deliver the natural environment outcomes the Government wishes to secure⁴. The Committee identified that it could not yet be confident that mechanisms would be in place to mitigate risks and concerns raised with the Committee; and recommended that the Welsh Government ensure there would be no weakening in performance during the transition period, and that commercial expertise from the legacy bodies would be mainstreamed into the work of NRW. The Committee's interest has continued since NRW was created, including a further inquiry relating to the public forestry estate in Wales and public consultation as part of the Committee's annual scrutiny of NRW.

² These benefits include both cash and other quantifiable savings of being a single, streamlined body, reducing duplication, simplifying processes, and achieving productivity gains.

³ The original November 2011 business case forecast total benefits of £158.4 million. The revised July 2013 business case forecast total benefits of £158.0 million.

⁴ **Report – The business case for a single environmental body**, National Assembly for Wales Environment and Sustainability Committee, May 2012.

- 6 Given the inherent risks in NRW's creation and the level of organisational change involved, and because NRW is a new organisation that utilises significant public resources in the course of discharging important functions, the Auditor General included an examination of the development of NRW in his programme of value-for-money examinations. Our study focused on whether NRW has in place, or is developing, effective governance arrangements that support delivery of its key priorities and outcomes. Further details of the scope of our work and audit methods are included in [Appendix 1](#). Although we did not examine the operational delivery of NRW's functions as part of our study, Wales Audit Office staff are currently preparing a report on managing the risks of coastal flooding and erosion that will include some consideration of NRW's role in this area. In addition, in the future, we expect to undertake audit work to follow up on our current studies; perform new audit work at NRW related to the Well-being of Future Generations (Wales) Act 2015 duties; and continue to include work in our value-for-money study programme that is relevant to NRW's functions.
- 7 NRW managed the first two years of its development as a 'transition' stage, aiming to manage continuity whilst bringing together functions from its legacy bodies. NRW has now reached a key development point as it moves from 'transition' into the 'transformation' stage of building the new organisation further. As part of this next stage, NRW faces the challenge of increasing statutory responsibilities under new legislation including the Well-being of Future Generations (Wales) Act 2015 and the Environment (Wales) Bill, due to be enacted by spring 2016 ([Appendix 2](#)).
- 8 **Overall, we have concluded that NRW adopted a sound and well-structured approach to quickly establishing the key systems and controls that enabled its smooth creation. These arrangements supported continuity in its operations in order to deliver its key priorities and outcomes. We consider that NRW has a solid platform for continuing to realise the benefits envisaged in the business case for its creation and for tackling the challenges of transforming NRW for the future, in light of anticipated funding constraints, new statutory responsibilities and stakeholders' expectations.**
- 9 We reached this conclusion because NRW's transition arrangements have supported business continuity in a period of ongoing organisational change during which NRW also had to deal with significant incidents of flooding and tree disease. We consider that NRW has made good progress towards achieving financial savings and delivering other benefits intended from its creation. NRW is now proceeding with a more ambitious transformation programme, using learning gained from its own experience, along with good practice from elsewhere. NRW has recognised the constraints and limitations of its initial change programme and has prioritised a focus on people management and communication within its transformation programme.

10 We note there are significant internal and external challenges for NRW to address to transform itself for the future. NRW has taken a pro-active approach to dealing with legislative changes and new statutory responsibilities. However, there is uncertainty regarding any additional funding for this work. In December 2015, the Welsh Government confirmed to NRW a cash-terms reduction of eight per cent on a like-for-like basis in the revenue grant-in-aid funding for 2016-17 related to non-flood risk management, and a five per cent reduction in flood risk management grant-in-aid⁵. The Welsh Government has maintained capital grant-in-aid at current levels. NRW has modelled a range of budget scenarios to plan for potential funding reductions year on year; however, the level of funding beyond 2016-17 is unknown at present⁶. Funding pressures combined with the need to realise existing savings commitments whilst delivering new or enhanced responsibilities creates significant challenges for NRW in medium-term financial and service delivery planning. Responding to these multiple pressures will require NRW to have an integrated approach to all aspects of its activities.

5 The reduction in flood risk management grant-in-aid in 2016-17 may be mitigated in-part by funding that NRW intends to carry forward from 2015-16; and, following flooding incidents in December 2015 and January 2016, additional Welsh Government funding sourced partly from its own budgets and partly from an uplift in its block grant from the UK Government following an announcement of additional support for England.

6 The Welsh Government published its 2016-17 draft budget in December 2015, which provides high-level details for one financial year. The Welsh Government subsequently confirmed to NRW its specific budget allocation. More detail on future years' budgets will not be available until the publication of the new Programme for Government, following the May 2016 National Assembly elections.

Recommendations

- 11 In making our recommendations we recognise that NRW has already been subject to a range of additional internal and external reviews, which resulted in a number of recommendations. These include a Better Regulation Delivery Office review; Environment and Sustainability Committee inquiries; a procurement self-assessment, with an expected formal Welsh Government assessment in 2016; and internal audit reviews such as on risk management. NRW is implementing action plans to address these recommendations and therefore, we have not repeated existing recommendations in these areas. Similarly, NRW has already taken action in response to a number of other issues we raised during the course of our study fieldwork.

Recommendations

To provide clarity on future funding arrangements and agree on key priorities given resource pressures

- R1 NRW is likely to face significant and continuing financial pressures in future years, given cuts to grant-in-aid funding for 2015-16 and 2016-17. NRW also has increased statutory responsibilities, which may or may not attract additional funding. The public and stakeholders may not fully understand the exact nature of NRW's role and the size of contribution that NRW can be reasonably expected to make towards environmental targets, particularly in light of budget pressures ([paragraphs 2.30 to 2.33](#) and [paragraphs 2.38 to 2.41](#)).
- a **To enable NRW to undertake more robust medium-term planning, the Welsh Government should provide NRW with more certainty over future funding arrangements, particularly for the next three years, including whether additional funding will be available for the increased statutory responsibilities; and**
 - b **NRW should engage in dialogue with the Welsh Government and stakeholders to agree on the key delivery priorities for NRW over the next five years, and to manage expectations of its role and its contribution to environmental outcomes, given reduced funding.**

To agree the future approach to benefits realisation and management

- R2 While we consider that NRW has a sound platform for continuing to realise the benefits envisaged in the business case for its creation, it is becoming increasingly difficult and resource intensive to separate benefits arising specifically from NRW's creation from the impact of actions required to address further budgetary pressures ([paragraph 1.51](#)). **NRW and the Welsh Government should agree an appropriate approach to monitoring and reporting benefits realisation in the context of the wider action that NRW is taking in response to budgetary pressures.**

Recommendations

To develop the functions that support delivery of the accommodation strategy

R3 NRW is delivering an accommodation strategy, part of which involves appraising options for rationalising accommodation sites ([paragraphs 1.39 to 1.44](#)). Although NRW has made good progress, NRW could improve its ability to deliver the strategy by:

- a **considering NRW's long-term accommodation needs; and**
- b **making more effective use of data in order to track sites' usage, expenditure, and performance; and to assess effectiveness of the rationalisation programme.**

To ensure that job evaluation is effective in meeting the future needs of NRW

R4 NRW is currently undertaking an extensive job evaluation exercise. The current timeframe of completion by February 2016 is very challenging. At present, the extent to which role descriptions and job design are aligned with new service delivery arrangements, organisation development, and staff training and development is not fully clear ([paragraph 2.9](#)). **NRW should ensure that the approach to job evaluation is flexible enough to meet NRW's future business needs.**

To review the effectiveness of its staff and stakeholder engagement

R5 Since its creation, NRW has undertaken a range of internal and external communications activities, including publishing a three-year communications strategy in October 2014. However, NRW recognises the need for improvement and is implementing activities to improve staff and stakeholder engagement ([paragraphs 2.12 to 2.17](#)). **NRW should review its staff and stakeholder engagement activities to demonstrate value, effectiveness and alignment to organisational purpose, priorities, and the transformation programme activities and outcomes.**

To improve the use and reporting of workforce-related data

R6 NRW has experienced issues with the accuracy of some workforce data but has recently developed data in areas such as vacancies and is now building an approach to electronic data collection ([paragraph 2.11](#)). **NRW should monitor its use of workforce-related data to ensure it is meaningful and accurate and reported appropriately through to the executive team and Board, and to other Committees where relevant.**

Recommendations

To maintain the effectiveness of the NRW Board

- R7 The original NRW Board in place from its creation was well run, with evidence of robust challenge and decision-making and annual assessments of board effectiveness. From November 2015, alongside some changes in the membership of the Board, the Welsh Government is reducing the number of days' time per Board member and the new appointments have a shorter tenure of two years ([paragraphs 2.46 to 2.48](#)). **The Welsh Government and NRW should ensure that they set out clear guidelines on the expected role of Board members given the reduction in time, and keep under review whether the reduction in time has any impact on the effectiveness of the Board.**

Part 1

NRW adopted a sound and well-structured approach to meeting the significant challenges presented by its creation; ensuring continuity in delivering its wide range of functions, and with a clear focus on achieving the intended benefits



- 1.1 This section focuses on the creation of NRW and its operation within its initial two-year transition period, including its progress in achieving the benefits intended from its creation. Section two looks at the arrangements NRW is putting in place to support its transformation phase, including in relation to areas emerging during the transition stage that NRW is now giving more focus to, such as staff and stakeholder engagement.

NRW's successful creation involved significant challenges

- 1.2 There were some substantial challenges to overcome in NRW's creation, particularly because the three legacy organisations had different governance arrangements, operating systems and organisational cultures, and there was a short handover period:
- a The three legacy organisations carried out a range of diverse activities, such as constructing and managing flood defences; managing the Welsh Government-owned forestry estate; and advising the Welsh Government on nature conservation and enhancement (Figure 1). The scale of their responsibilities took in the whole of Wales, and Forestry Commission Wales alone was responsible for managing around seven per cent of land in Wales. The functions encompassed key statutory responsibilities set out in Welsh, UK and European legislation.
 - b Two of the three legacy organisations operated within complex governance arrangements, because they were part of wider geographical bodies:
 - Forestry Commission Wales was part of the overall Forestry Commission that covered England, Wales and Scotland, but with devolved responsibility to Welsh ministers. From its head office in Edinburgh, Forestry Commission GB delivered all financial and human resources activities for Forestry Commission Wales.
 - The Environment Agency Wales was part of the Environment Agency, a non-departmental public body covering England and Wales. The Environment Agency provided all the ICT support and much of the strategic technical guidance to Environment Agency Wales.

These arrangements presented challenges in terms of separating certain functions from their larger parent organisations because the Welsh bodies lacked their own local capacity and capability in some areas. Achieving the benefits identified in the business case for NRW's creation, totalling £158 million over the 10 years to the end of 2022-23, depended in part on quick separation of duties to end reliance on services provided by the legacy bodies.

- c The culture and ways of working at each legacy organisation were different, compounded by the varying professions and skills of staff.
 - d In November 2011, the then Environment Minister announced the replacement of the three legacy organisations with a new body to be operational from 1 April 2013. The Welsh Government legally established NRW on 18 July 2012. Subsequently in August 2012 and October 2012, the Minister announced the Chair and the Board members of NRW, resulting in a short, five-month shadow period for the new members. Further time pressures were created as 1 April 2013 represented a 'hard launch' date, with the legacy bodies undertaking operations up to this date, and NRW taking over operations from that date. Had NRW failed to deliver the day-to-day operations of the legacy bodies on handover, the impact would be high, particularly in terms of the future reputation of NRW.
- 1.3 Nevertheless, the three organisations did share a number of features that contributed to a smooth creation. For example, all had some accountability to Welsh ministers and played an advisory role to the Welsh Government; delivered a regulatory function to help protect and enhance the natural environment; and worked to support public use of the areas that they managed.
- 1.4 The Welsh Government provided £3 million in Invest-to-Save funding⁷ to facilitate setting up NRW, largely for ICT costs. NRW repaid £1.5 million of this sum in 2014-15 and is repaying the remaining £1.5 million in 2015-16.

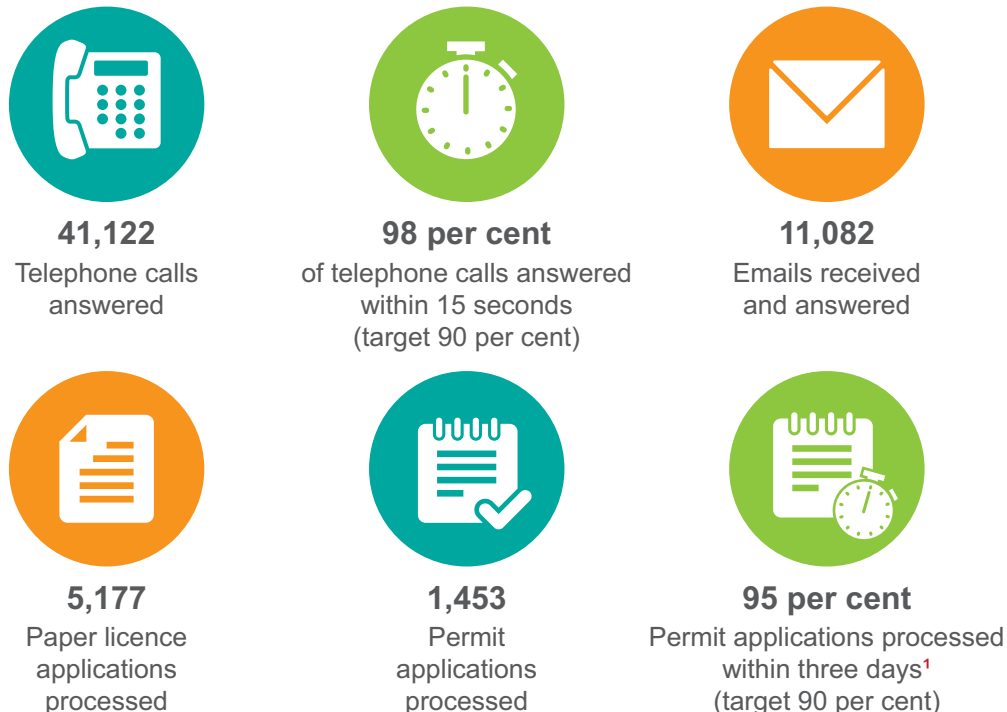
⁷ The Welsh Government also provided NRW with an additional £6 million of Invest-to-Save funding for the costs of two voluntary exit schemes.

Since its creation, NRW has maintained business continuity and has also dealt effectively with some significant incidents

Supported by a clear corporate plan and performance framework, NRW has continued the services of the legacy bodies, although it is difficult to assess trends in performance

1.5 NRW has continued the day-to-day services provided by the legacy bodies, by bringing services in-house and by taking over or renegotiating service level agreements. NRW also took over the provision of some services previously provided by Welsh Government, including marine licensing and wildlife licensing of UK and European Protected Species⁸. To help maintain a smooth service for customers, NRW established a customer care centre, in operation from vesting day, which reduced the number of contact telephone numbers from 10 to one. The centre processes permit and licence applications, and responds to calls and emails, dealing with issues relating to any aspect of NRW's functions. The centre deals with approximately 90 per cent of queries, with 10 per cent referred on to other departments. Figure 3 shows some data on the performance of the centre in 2014-15.

Figure 3 – Performance data of NRW's Customer Care Centre, 2014-15



Note:

1 This relates to the Customer Care Centre's process of checking applications and processing relevant payments before moving the application to the wider permitting teams.

Source: Natural Resources Wales

⁸ Marine licences are required under the Marine and Coastal Access Act 2009 for activities such as river dredging or harbour construction. Protected species licences are required for a range of activities that may affect certain species classified as protected under UK and European law. Activities include undertaking building work that could disturb a protected species; and use of protected species for scientific or educational purposes.

1.6 In its first year of operation, NRW produced a three-year Corporate Plan for 2014 to 2017. This plan focused on indicators and outcomes based around five ‘Good’ themes (Box 1) on which NRW currently apportions its activity and reporting. NRW developed the corporate plan through consultation with stakeholders, staff, the Welsh Government and the wider public. The plan demonstrates that NRW has established a clear vision and purpose. The corporate plan references the areas of potential benefits and savings set out in the business case; and aligns with NRW’s one-year business plans which focus on measures and outputs. NRW has recognised that its strategies and plans below the corporate plan and business plan level have developed in a range of formats, and is currently undertaking further work to link planning more clearly at all levels of the organisation. NRW is creating a standard template to express all future strategies as an ‘Enabling Plan’ consisting of a strategic statement linking to the corporate plan; a results-based accountability plan linking to the performance framework; and an action plan linking to the business plan, and directorate, team and individual delivery plans.

Box 1 – NRW ‘Good’ themes

- **Good Knowledge** – good information helps us to make good decisions.
- **Good for the Environment** – to ensure that our ecosystems are resilient, that our wildlife and landscape are enhanced and that our natural resources are carefully managed.
- **Good for People** – to ensure that people are safe, that they are able to benefit from and enjoy our natural resources and they understand the relevance of these resources to our day-to-day lives.
- **Good for Business** – Natural Resources Wales aims to make Wales a ‘location of choice’ for business and enterprise and a place where best practice environmental management is adopted and encouraged.
- **Good Organisation** – to make Natural Resources Wales the best organisation it can possibly be.

Source: Natural Resources Wales

1.7 NRW’s performance measurement framework tracks progress against the three-year Corporate Plan and annual Business Plan, and business case targets relating to benefits and intended savings. Indicators also link to ministerial priorities and corporate risk areas. NRW reports progress to the Board every four months, with Board papers available on the NRW website. Some of the indicators reflect aspects of NRW’s day-to-day operations, and as such contribute to stakeholders’ understanding that NRW is continuing to deliver its core functions. For example, there are indicators that cover managing the Welsh Government Woodland Estate to meet industry standards; timescales for issuing permits, licences and consents; and the publishing of information on flood risk management.

1.8 The business plan performance dashboard for 2014-15 showed 28 green 'on target' indicators out of 41 (Figure 4). One of the red indicators related to long-term issues of the condition of Natura 2000 sites⁹, and the other red indicator related to actions to halt biodiversity loss, both of which are not solely reliant on NRW input. NRW did not give two indicators a rating due to a lack of baseline. NRW's internal audit team gave substantial assurance¹⁰ on the accuracy of reported performance in the 2014-15 dashboard in May 2015.

Figure 4 – 2014-15 Business Plan Dashboard performance indicator summary



Source: Natural Resources Wales 2014-15 Annual Report

1.9 It is difficult to assess trends in performance because 2014-15 performance indicators were not directly comparable to 2013-14 indicators or to historic measures used by the legacy bodies. However, in some cases, there are mixed views to indicate whether NRW has maintained the level of service previously provided by the legacy bodies (Case Study 1).

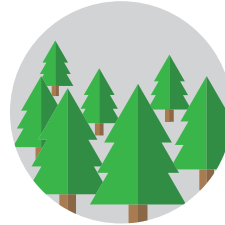
⁹ Natura 2000 sites are an ecological network of protected areas across the European Union set up to ensure the survival of Europe's most valuable species and habitats.

¹⁰ A Substantial level of assurance is the highest level of assurance out of four possible ratings, and is defined as 'the framework of governance, risk management and control is adequate and effective'.

Case Study 1 – Examples relating to NRW's continuity of day-to-day operations

Forestry estate

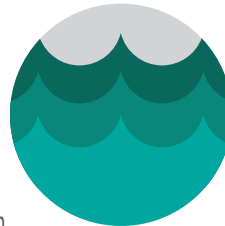
NRW has increased the supply of timber to the market. In 2012-13, Forestry Commission Wales supplied 801,000m³ of timber to the market. In 2013-14 and 2014-15, NRW supplied 887,000m³ and 869,000m³ of timber to the market respectively.



However, evidence to the National Assembly's Environment and Sustainability Committee's 2014 inquiry on the public forestry estate detailed that some external bodies felt there had been deterioration in the commercial focus and management of the public forestry estate since NRW's creation. The Committee noted that processes were embedding and communication had improved between NRW and other bodies. NRW accepted the Committee's findings and NRW, the Welsh Government, the Wales Forest Business Partnership and Confor (a membership organisation promoting sustainable forestry and low-carbon businesses) agreed in December 2014 a joint action plan to address them, which they are working to implement. NRW provides updates on progress at six-monthly forestry business sector meetings, which show that NRW has completed several agreed actions and is continuing action on outstanding areas.

Hydropower permitting

NRW took over the function of hydropower licence applications from Environment Agency Wales. The number of licences issued rose from nine in 2010 to 99 in 2014. NRW changed the approach to assessing the impact of hydropower schemes from April 2014 including issuing new guidance co-produced with a Hydropower Stakeholder Group. This reduced the proportion of invalid applications from 52 per cent between August 2013 to June 2014, to 20 per cent between July 2014 and March 2015. The average time to process an application internally reduced from 91 days to 53 days in the same period, providing an improved service to customers.



Source: Forestry Commission Wales 2012-13 Annual Report; Natural Resources Wales; National Assembly's Environment and Sustainability Committee **Inquiry into the public forestry estate in Wales**

- 1.10 For 2015-16, NRW has used the 2014-15 indicators as the basis for the indicators in its updated business plan performance dashboard in order to assess progress more easily. Thirty-two indicators have remained largely the same but with updated targets, and nine have been replaced with new indicators, or in some cases multiple indicators.
- 1.11 Data for 1 April to 30 November 2015 show the number of green and amber ratings has remained largely the same as for 2014-15 (Figure 5). However, where indicators relate to annual targets, during the year NRW typically rates these as amber, even if progress is consistent with achieving them at the year-end. Therefore, NRW expects some indicators that are currently amber to progress to green by the year-end.

Figure 5 – Business Plan Dashboard performance indicator summary, 1 April to 30 November 2015

Rating	Indicators carried forward from 2014-15		New indicators
	2014-15 year-end rating	1 April to 30 November 2015	1 April to 30 November 2015
Green	22	20	6
Amber	6	7	3
Red	2	5	0
No rating	2	0	0

Source: Natural Resources Wales

- 1.12 Of the two red indicators at the 2014-15 year-end (paragraph 1.8), the indicator relating to halting biodiversity loss has progressed to green, while the indicator relating to the condition of Natura 2000 sites has remained red. The four new red indicators relate to:
- Compliance with the ‘good status’ under the Water Framework Directive¹¹ (not rated in 2014-15).
 - Staff engagement, which NRW will assess in its February 2016 People Survey (not rated in 2014-15).
 - Delivery against NRW’s Recreation and Enabling Access Plan, where the target of four exemplar Recreation and Access plans by March 2016 will not be met in order to achieve fewer, higher-quality plans (rated green in 2014-15 when the target was to complete the overarching Plan).

¹¹ Following its March 2015 report on the Glastir agri-environment scheme, the National Assembly’s Public Accounts Committee sought evidence from the Welsh Government about the specific proportion of Water Framework Directive failures that could be attributed to land managed by NRW. In response, the Welsh Government emphasised that there is a mixed tapestry of land ownership in the catchments affecting the failing water bodies. As a consequence, both private and public land owners have their part to play in resolving the issues. The Welsh Government has outlined in its evidence to the Public Accounts Committee work that NRW has undertaken to both understand and propose remediation of the causes of these failures.

- An increase in the number of incidents involving NRW staff that have resulted in time off (rated green in 2014-15). To reduce the number of incidents NRW is currently reviewing them in order to identify preventative measures and share lessons learned.

1.13 The Welsh Government assesses the performance of NRW against its annual remit letter to NRW. The letter sets out the key deliverables for NRW; and targets in the letter reflect NRW's long-term strategic vision. NRW incorporates the remit letter priorities into its annual business plan. Performance reports to the NRW Board are subject to formal scrutiny by the Welsh Government in four-monthly sponsorship meetings¹². From the sponsorship meetings, business plan and corporate plan, the Welsh Government is clear what NRW is intending to deliver to meet the remit letter priorities. Sponsorship arrangements appear resilient and sustainable and both the Welsh Government and NRW view their relationship as constructive and positive.

1.14 In January 2014, the Welsh Government's internal audit services reported on the sponsorship arrangements for NRW and noted that significant progress had been made in establishing sponsorship arrangements with an overall finding of substantial assurance. The report made five main recommendations to strengthen sponsorship controls, largely relating to improving monitoring arrangements. The Welsh Government addressed all five recommendations by October 2014.

NRW has dealt effectively with significant incidents such as the coastal floods of December 2013 and January 2014 and tree disease

1.15 Since April 2013, there have been two very large coastal flooding incidents: on the north Wales coast in December 2013 and in south and west Wales in January 2014. During December 2013 and January 2014, NRW issued eight Severe Flood Warnings and over 100 Flood Warnings¹³. NRW reported that the severity and number of warnings was unprecedented in recent years, with evacuation procedures initiated in a number of locations. Following the coastal floods, the Minister for Natural Resources and Food commissioned NRW to undertake a review of the flooding. The review concluded that the operational response by NRW, and other relevant authorities¹⁴ was 'coordinated, effective and proportionate'. The review made 47 recommendations in six priority areas to help to deliver a more resilient coastal flood risk and erosion management service. A forthcoming Auditor General for Wales report will examine how the Welsh Government is working with NRW and other relevant stakeholders to manage the risks of coastal flooding and erosion.

¹² These meetings are between the NRW Chief Executive and executive team; and Welsh Government directors and deputy directors of relevant policy areas.

¹³ Severe Flood Warning is the highest alert and means 'Severe Flooding. Danger to Life'. Flood Warning means that 'Flooding is expected. Immediate action is required'.

¹⁴ There were 31 flood Risk Management Authorities in Wales, including NRW; the 22 local authorities; utility companies, for example, Dŵr Cymru Welsh Water; and the three Internal Drainage Boards operating wholly or partly in Wales, which are now part of NRW.

- 1.16 Since NRW's creation, there has been a significant increase in the spread of the tree disease *Phytophthora ramorum*, which primarily causes infection and fatality in larch. The disease was first found in Wales in May 2010 and has since become the most serious disease to affect forestry in Wales, infecting over six million trees predominantly on the Welsh Government's woodland estate¹⁵. NRW identified the spread of the disease in its first month of operation, and has implemented a number of approaches to date to try to tackle the disease. Some witnesses to the National Assembly's Environment and Sustainability Committee 2014 inquiry on the public forestry estate in Wales were critical of NRW's response to the outbreak, stating the initial response was too slow¹⁶. However, the Committee noted that the timing was unfortunate and would have caused significant problems for any organisation. In January 2014, a University of Cambridge study found that where resources are limited, the most effective method of disease prevention is through the felling of outlying infections, mirroring the approach taken by NRW and the Welsh Government.
- 1.17 Between April 2013 and March 2015, NRW replanted over 1.75 million trees to restock areas affected by disease, replacing larch with a mixture of species to enhance tree diversity and build greater resilience to any future disease outbreaks. This restocking is in addition to around 5.5 million trees replanted in the same period to regenerate forests after felling for timber production.

¹⁵ **Forestry in Wales**, National Assembly for Wales Research Service, November 2013, ***Phytophthora ramorum***, National Assembly for Wales Research Service, September 2015

¹⁶ **Inquiry into the public forestry estate in Wales letter**, National Assembly for Wales Environment and Sustainability Committee, October 2014.

NRW has taken a sound, well-structured and pragmatic approach to making the transition from the pre-existing arrangements to becoming a single body

NRW established a sound transition programme for its first two years, learning lessons from elsewhere and revising its plans to ensure focus on priority areas

- 1.18 From its creation in April 2013, NRW undertook a wide-ranging transition programme to progress the organisation. The programme focussed on achieving transition to establish NRW as an independent body and realise some early benefits of integration. The target completion date for this first phase was March 2015. In December 2013, NRW appointed external reviewers to undertake a formal 'gateway' review of the programme. The review found that NRW was unlikely to complete phase one in full by March 2015, and NRW reviewed its phase one plans to focus on key deliverables within the original timeframe. This resulted in changes to the schedule for the rolling out of NRW's ICT systems and exits from legacy systems.
- 1.19 The transition phase programme has been extensive with good linkages between activities across it. The change programme portfolio comprised 25 sub-programmes with over 120 projects, each comprising further sub-projects. The final transition programme progress update in April 2015 showed almost all sub-programmes were complete or on target for the transition stage, following the revisions made in relation to the gateway review (Figure 6). NRW classified one programme, Sampling and Analysis, as amber due to delays in implementing a 'lab information management system' although this is currently in progress and on-track to be delivered by the end of March 2016.

Figure 6 – Transition programme progress at April 2015



Source: Natural Resources Wales

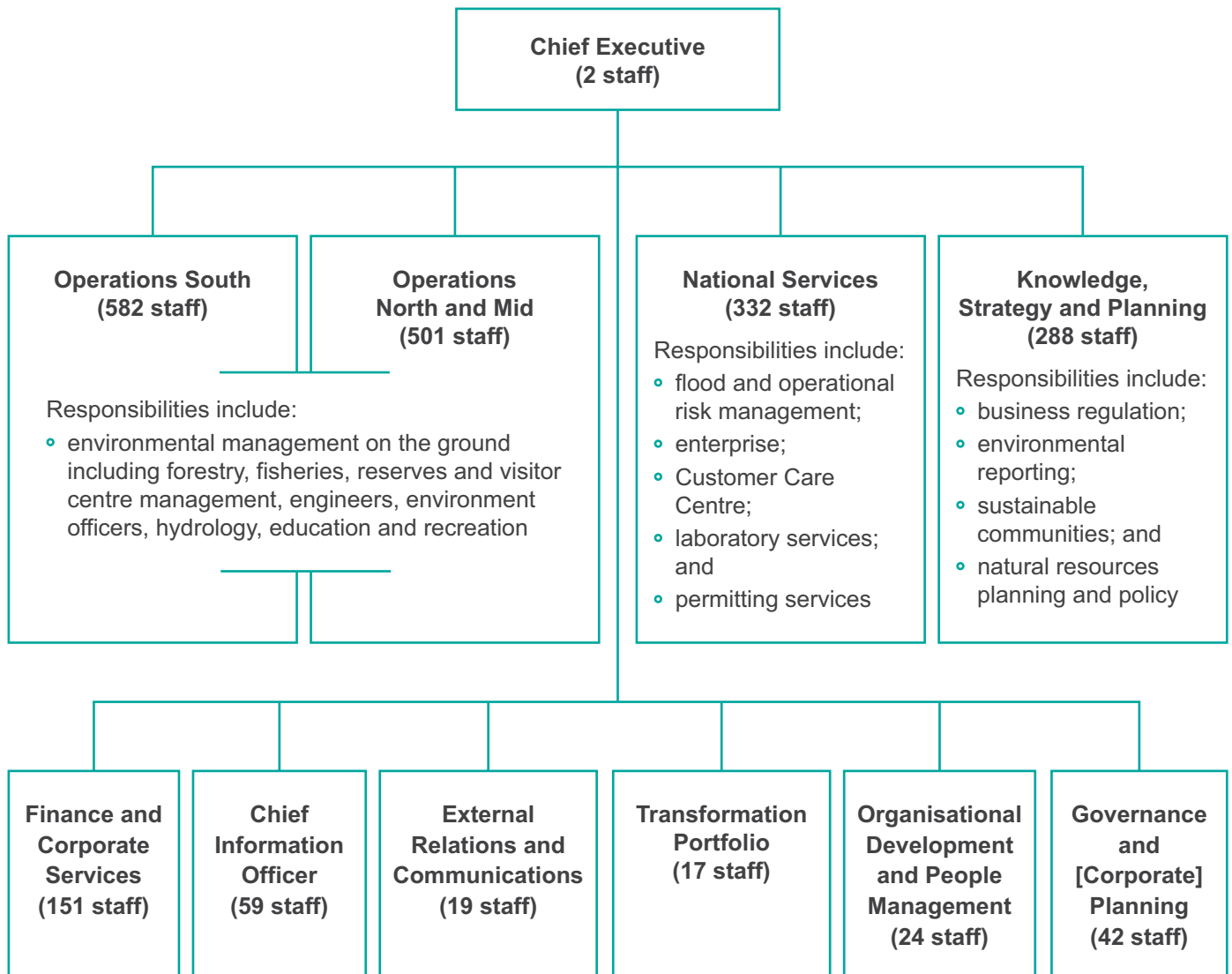
1.20 There is evidence of a very structured and systematic approach to the management of performance around the change programme, including its co-ordination by a transition team and wider reporting through to the NRW Board. NRW has identified good practice from Ofcom, Natural England and the Royal Mint in relation to designing, managing, monitoring and communicating its change management programme. NRW has adapted and adopted this good practice within its transition programme.

From April 2013, NRW established an organisational structure focussed on combining legacy departments on a geographic basis, and NRW has further evolved the structure to increase efficiencies and take into account new legislation and ways of working

1.21 Prior to NRW's creation, the shadow arrangements mapped out the overarching directorates and teams within NRW's organisational structure. The structure created operational directorates based on geography and function, and brought together staff undertaking similar corporate roles or delivering similar activities in the same area. NRW implemented this structure from the day of creation on 1 April 2013.

1.22 **Figure 7** shows NRW's current organisational structure at a directorate level. The directorate structure has remained largely the same since vesting day. However, within directorates, NRW has revised structures through the transition programme to create better alignment and integration; and recognise the effects of exit from legacy body arrangements in functions like finance and ICT. NRW has undertaken two voluntary exit schemes to support these changes (**paragraph 2.42**). NRW has also evolved structures to consider future legislative responsibilities and new ways of working based around natural resource management. NRW has indicated to us that it will be undertaking further structural changes based on what is needed to deliver the organisation's purpose.

Figure 7 – NRW’s organisation structure at directorate level, October 2015¹



Note:

1 Between April 2013 and October 2015, the External Relations and Communications, and Governance and Planning directorates have replaced a Governance and Communications directorate; and the Transformation Portfolio directorate has replaced the Transition directorate.

Source: Natural Resources Wales

NRW's arrangements for governance and financial management are generally sound, although there have been issues with internal audit capacity and staff perceptions of leadership

- 1.23 From vesting day, the Welsh Government had established a governance framework agreement for NRW in consultation with NRW's shadow arrangements. The framework sets out the responsibilities that the Welsh Government has delegated to NRW and the standards expected. NRW and the Welsh Government undertook a formal review of the framework in the summer of 2014 and agreed the framework was working well.
- 1.24 NRW publishes details of its governance arrangements in its Governance Statement within the NRW Annual Report. The 2014-15 statement includes details on the governance framework in place; the roles and responsibilities of the Board, sub committees, and executive team; mechanisms to review internal control and risk management. Our financial audit of NRW reviewed the governance statement and found it to be consistent with our knowledge of the arrangements in place.
- 1.25 NRW has a well-run Board in place, with three formal sub-committees comprising an Audit and Risk Assurance Committee, Remuneration Committee and Protected Areas Committee, which have additional sub-groups. Both the Board, and Audit and Risk Assurance Committee conduct annual effectiveness reviews with workshops and action plans developed in response. Observation of a board meeting showed robust decision-making processes, and appropriate challenge and scrutiny. Relationships amongst Board members and the senior leadership team are generally constructive and effective. Some staff highlighted past issues with a lack of clarity of responsibilities between the Board and the senior leadership team, but which they felt had been resolved.
- 1.26 NRW demonstrated to us open and inclusive leadership and the senior leadership team appear united in wanting to present a clear message. However, evidence from NRW's first staff survey in February 2015 identified concerns about leadership and change management; only 14 per cent of respondents answered positively that change is managed well; and 20 per cent answered positively that the organisation as a whole is managed well. NRW has committed to improving staff engagement and has an action plan to respond to the issues raised by comments in the staff survey.
- 1.27 NRW has made good progress on harmonising corporate policies and processes. **Box 2** gives examples of areas in which NRW has developed common policies. NRW manages compliance with a range of legislation largely through individual officers in relevant parts of the business, for example, an Equalities Advisor, Head of Well-being, Health and Safety, Senior Access to Information Advisor, and Governance Partner.

Box 2 – Examples of NRW’s corporate policies

Since creation, NRW has harmonised corporate policies to create single common policies on a range of areas including:

- human resource issues such as expenses, performance management and sickness absence;
- equalities;
- well-being, health and safety;
- whistleblowing;
- complaints;
- fraud prevention and detection;
- environment management; and
- managing conflicts of interest.

Source: Natural Resources Wales

- 1.28 From April 2013, NRW introduced financial and non-financial schemes of delegation. These provide common policies across the organisation for financial activities and decision-making. During 2014-15, NRW implemented a new single integrated HR and finance system, 'MyNRW', into which NRW has built-in its financial schemes of delegation. In 2015, NRW conducted a review of the financial scheme of delegation, involving consultation across directorates. The review found that the current scheme did not always provide the most effective approval route and could be confusing to staff. NRW has redeveloped the scheme, renamed as Managing Our Money. NRW benchmarked the new scheme of delegation against Managing Welsh Public Money, the governance framework, and internal policies, and conducted consultation with Internal Audit, to ensure the scheme complied with regulatory criteria and met NRW's vision and priorities.
- 1.29 Budget holders in each directorate manage NRW's budget on a day-to-day basis. The finance team produce monthly budget monitoring reports for directorates and budget holders, and provide financial support and guidance. The reports include monthly update papers for the Executive Team and further papers for each Board meeting tracking actual year-to-date progress against the budget and the forecast full-year outturn. NRW undertakes formal budget reviews with each directorate during the year to revise the budget and identify any significant issues that require escalation. For example, during 2013-14 NRW requested and obtained additional funding from the Welsh Government to contribute to a deficit on expenditure related to tree disease.

1.30 NRW aim to break even each year, with income equal to expenditure. However, NRW is able to carry forward from one financial year to the next up to five per cent of its Welsh Government grant-in-aid funding. It can also carry forward up to 20 per cent of non-grant-in-aid income, such as income from timber sales and other commercial income (excluding charge schemes). This provides some leeway in its financial budgeting and management, and can aid long-term planning. NRW carried forward the following income:

- a In 2013-14, NRW had a year-end carry-forward of £1.2 million in addition to £16.2 million of grant-in-aid and European funding that it had ring-fenced to carry forward to meet specific pressures in 2014-15, such as dealing with tree disease.
- b In 2014-15, NRW had a total carry-forward of £20.5 million, of which £18.2 million is for specific ring-fenced programmes.

NRW stated as part of its 2014-15 year-end financial analysis that it is a challenge to fully utilise funding meant for the construction of assets within a financial year which is subject to many factors such as the weather; and that it can be difficult to effectively plan and spend additional funding provided in-year for new Welsh Government priorities.

1.31 Our financial audit focuses on whether the financial statements give a true and fair view of the state of NRW's affairs. Part of this work involves understanding the financial processes and controls in place. Our financial audit raised no significant concerns regarding the financial management arrangements at NRW during 2014-15.

1.32 In 2014, the Welsh Government commissioned the Department for Business, Innovation and Skills' Better Regulation Delivery Office to undertake a review of NRW, against the principles of better regulation. The June 2015 report highlighted that NRW has a broad understanding of the principles of good regulation and is committed to embedding these in its ways of working. [Paragraph 2.17](#) provides more detail on the report's findings.

1.33 NRW's internal audit function generally provides adequate assurance to management of internal arrangements and controls. In both 2013-14 and 2014-15, the Head of Internal Audit gave moderate assurance¹⁷ in the overall adequacy and effectiveness of NRW's internal control environment. During 2014-15, internal audit gave substantial assurance to corporate governance and the performance framework. However, our 2014-15 financial audit of NRW noted that internal audit had provided an assurance role on the MyNRW Project Board but had not undertaken any detailed review of the new MyNRW financial systems. Internal audit has included coverage of the key financial systems in its 2015-16 annual programme, with work currently underway. Internal audit had also experienced some lack of capacity, due to staff being temporarily seconded to other NRW projects, which have now concluded.

NRW has successfully made major changes to its ICT systems, although work to fully integrate all ICT processes and embed new ways of working is still ongoing

1.34 NRW has made significant progress in rationalising its ICT arrangements, including migrating from three HR and finance systems into one new MyNRW system in 2014 (paragraph 1.28). This integration has contributed significantly to NRW's overall financial realisation of benefits with an estimated cash-realizable benefit over 10 years of £13 million including both ICT savings and staff cost savings. NRW has also created its own in-house ICT service, which NRW estimates has reduced the annual cost of ICT services from £13 million to £6 million. Across all its activities, NRW estimates its ICT savings will total £34 million over the 10 years from creation. However, some planned savings have not been realised as quickly as originally anticipated due to an underestimation in the volume of the work required and issues in exiting from legacy body contracts (paragraph 1.47).

1.35 As part of our 2014-15 financial audit of NRW, we reviewed the technical process and procedures followed by staff at NRW to merge financial management data from the previous systems. We did not identify any significant issues with the transfer of data into MyNRW or any material weaknesses in internal financial controls. However, our audit noted that the key financial systems within MyNRW had not been subject to any detailed internal audit coverage during the year (paragraph 1.33).

1.36 NRW has implemented cloud-based systems¹⁸ for all staff, the first public body in Wales to do so, and encourages use of technology through tablets, Yammer¹⁹ and Microsoft Lync²⁰. NRW has faced an additional challenge in terms of the levels of understanding of IT amongst its staff, some of whom have not used computers regularly, if at all, before. NRW has implemented a number of initiatives to support its staff to use new workplace technology and improve their understanding (Case Study 2).

17 A Moderate level of assurance is the second highest level of assurance out of four possible ratings, and is defined as 'some improvements are required to enhance the adequacy and effectiveness of the framework of governance, risk management and control'.

18 The electronic applications that NRW uses, such as Microsoft Office, and all electronic documents are stored on remote servers and accessed via the internet. Benefits include easier remote working and sharing of documents; and reduction in some in-house IT equipment such as servers.

19 Yammer is a private online social network that enables employees within the same organisation to share conversations, documents and pictures.

20 Microsoft Lync enables instant messaging, and voice and video conferencing between users via the internet.

Case Study 2 – Improving staff knowledge of ICT

Given the large-scale ICT change and variance in the pre-existing knowledge of staff, one key task for NRW was to promote a greater understanding of IT amongst its staff. To address this, the Business as Usual team has established a number of innovations to improve and monitor user experience of ICT which include:

- YouTube guides viewable by any staff at their desk, via mobile devices or at home
- An ICT survey
- Yammer groups, which have had a very good uptake
- Helpdesk
- Workshops

In addition, the Chief Information Officer travels to offices meeting colleagues and providing face-to-face dialogue on digital issues and future developments.

NRW IT officers feel that staff awareness is improving based on staff feedback, but recognise there is more progress to be made in user perception of ICT, in particular, users' awareness of processes for accessing support when they encounter IT issues and problems.

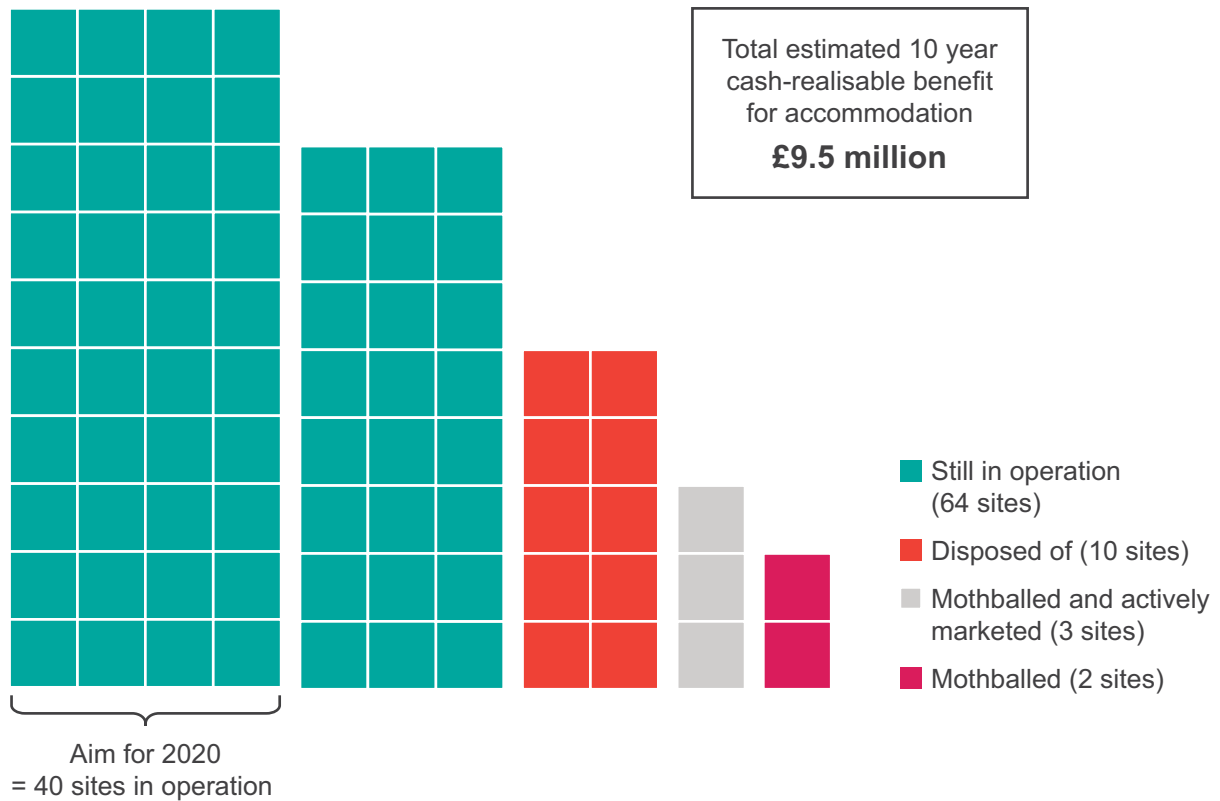
Source: Natural Resources Wales

- 1.37 NRW contracts an outsourced company to deliver support services for MyNRW, with a separate internal group called Business Support Service in place to manage this contract. Internal IT staff support NRW's Business As Usual functions. The Business as Usual team use a set of best practice guidelines for IT service delivery known as IT Infrastructure Library (ITIL). However, the good practice ITIL procedures were less well-established in the Business Support Service. There also seemed to be a very limited working relationship between the Business As Usual and Business Support Service teams rather than having a function embedded within the internal IT service that manages the relationship with outside suppliers on behalf of the whole organisation. Following early feedback from our study, NRW has now brought the Business Support Service into the 'Service Delivery and Support' umbrella within the internal ICT team, aligning them to the same ITIL-based processes and policies and transitioning the operational relationship with the outsourced company into ICT's remit.
- 1.38 NRW has been developing a new digital strategy and completed the framework and principles of this by the end of 2015. NRW had delayed full completion of the strategy until there was more certainty about the budget available for 2016-17.

NRW has made good progress in delivering its accommodation strategy by using a thorough appraisal process to reduce its number of sites by 19 per cent, although there is scope to improve capacity of the corporate assets function to deliver further benefits

- 1.39 A key area in which NRW expects to create savings and make efficiencies is in managing and rationalising its buildings, particularly given the duplication between the three legacy bodies of sites at some locations. NRW's sites include offices, depots used largely for equipment and vehicle storage, a laboratory facility, workshops and hatcheries. NRW has set out a clear vision and sense of purpose for asset management in its accommodation strategy, which links to a number of corporate objectives, and has taken into account wider strategic issues with board input where appropriate. The strategy outlines intentions to carry out an options appraisal for each accommodation site across Wales. NRW has also taken into account national work on asset management such as the National Assembly Finance Committee's 2013 report on **Asset Management in the Public Sector**. As part of this, NRW has engaged with the National Assets Working Group.
- 1.40 NRW has made good progress in rationalising its accommodation resources, although it has not met its target for the transition phase one, of reducing the number of sites by 20. From a starting point of 79 accommodation sites, NRW has put in place actions to reduce sites by 15 to 64 sites, a decrease of 19 per cent (Figure 8). The sites no longer in operation are distributed across Wales. The estimated annual savings from the sites no longer in operation are £362,000 with NRW estimating the total 10-year cash-realizable savings of the accommodation strategy at £9.5 million.

Figure 8 – Changes to the number of NRW sites following its accommodation rationalisation to October 2015



Source: Natural Resources Wales

1.41 As part of rationalisation, NRW has implemented a thorough options appraisal process for individual sites using the ‘Five Case Model’ as set out in HM Treasury’s Green Book. An example of this is the options appraisal for the laboratory services site in Llanelli ([Case Study 3](#)).

Case Study 3 – Option appraisal for laboratory services

NRW identified that its existing facility for laboratory services in Llanelli was no longer fit for purpose due to health and safety risks, and the potential to develop services was severely restricted.

NRW undertook a thorough options appraisal for the service with the appraisal report containing the case for change, consideration of local economic issues, jobs, scoring of options, and a lengthy cost and project appraisal for each option. Each of the shortlisted options was evaluated through the completion of an outline business case using HM Treasury processes. This helps ensure value for money and a sound decision-making process.

The options appraisal process included a NRW business group holding quarterly meetings to receive progress reports and discuss added value.

The appraisal identified a preferred option at Swansea University, which the Project Board selected. However, during commercial negotiations, this site became unavailable. The Project Board performed a further thorough evaluation of two joint-second ranking sites from the original appraisal and identified another location at Swansea University as the preferred location. NRW is working with the University and remain on track to move to the new laboratory in September 2016.

Source: Natural Resources Wales

- 1.42 Although NRW has made progress, capacity within the corporate assets team for delivering the accommodation strategy has been limited. Capacity is now developing, with a greater number of staff involved in asset management, a re-formed working group and more responsibility devolved to area operational managers.
- 1.43 Phase two of the accommodation strategy during the transformation phase is likely to involve challenging issues and dealing with more difficult sites. NRW's approach needs to take a longer-term view based on the future needs of NRW and link better with future strategic areas of importance such as workforce planning. Senior managers recognise the organisation needs to change its ways of working and there are plans to look at how NRW can use agile working across the whole organisation, which may present further opportunities for rationalisation.

1.44 NRW has basic data on the performance of its accommodation assets and understands many of the industry accepted standards for accommodation. It is tracking the net internal area of its buildings, which has reduced by nine per cent since April 2013 against a target of 14 per cent. However, there is limited detailed data on the use of buildings or how effectively NRW is rationalising its facilities management contracts, other than tracking accommodation savings as part of the Finance and Corporate Services performance dashboard. Our 2013-14 financial audit of NRW also identified issues with the quality and accuracy of information held by NRW in relation to assets, with differences between the estates team records of land owned and the finance department's Fixed Asset Register. However, our 2014-15 financial audit noted that management had acted positively regarding issues relating to asset verification by undertaking a detailed verification exercise and addressing process and policy deficiencies.

NRW has made good progress towards achieving financial savings and delivering other benefits intended from its creation

1.45 In November 2011, the Welsh Government set out a business case for the creation of NRW, which identified the intended financial savings and costs of a single body over a 10-year period from April 2013 to March 2023. In July 2013, following NRW's creation, the Welsh Government and NRW agreed a revised business case. This revised business case amended the profile of expected annual savings; however, the target for total savings over 10 years was almost identical at £158 million in cash terms. These benefits include both cash and other quantifiable savings of being a single, streamlined body, reducing duplication, simplifying processes, and achieving productivity gains. The total expected costs were £68.7 million in the original business case and £66.0 million in the revised business case. These costs cover expenditure on areas such as aligning three sets of systems and policies; aligning staff terms and conditions, particularly an increase in pension costs; and new branding and communication. This results in a net saving in the revised business case of £92.0 million in cash terms to 2022-23.

1.46 NRW has made good progress towards achieving the total intended financial savings set out in the revised business case (Figure 9). NRW measures both cash-realizable savings, and non-cash realizable savings²¹. The latest forecast in September 2015 shows that NRW has identified gross savings of £0.8 million in 2013-14 and £6.7 million in 2014-15, and forecasts that benefits in the pipeline will increase this to £17.7 million per year by 2018-19. For the 10-year period to 2022-23, NRW is on target with cash-realizable savings, but has yet to identify £15 million of the £31 million target for non-cash savings. NRW is confident it will achieve the non-cash target from efficiencies through the process improvement projects in the current transformation programme; however, NRW cannot accurately quantify these yet. Given the further continuous improvement processes in place including a specific Improving Efficiency and Service Delivery Programme aimed at improving service while reducing expenditure (Box 3), there are indications that NRW will increase the value of its non-cash savings over future years. This lower forecast for non-cash realizable benefits is the main reason why the total forecast net saving of £76.3 million is £15.8 million lower than the revised business case figure.

Figure 9 – Forecast total financial gross savings, costs and net savings over the 10-year period from April 2013 to March 2023 in cash terms

	Business case ¹ £ million	NRW forecast £ million
Cash-realizable savings	127.2	128.9
Non cash-realizable savings	30.9	16.2
Gross costs	-66.0	-68.8
Total net savings	92.1	76.3

Note:

1 These figures are from the revised business case, which the Welsh Government and NRW agreed in July 2013. The revised profile reconfigured the savings and costs expected per year with the total targeted gross savings almost identical and the total costs slightly reduced.

Source: Natural Resources Wales

21 Cash-realizable savings are a saving in the actual cash spent, for example no longer paying for finance support from the Environment Agency. Non-cash realizable savings are when the level of cash expenditure does not fall but the value gained from the expenditure is increased, for example, staff being co-located increases productivity, which allows for more work to be performed for the same cash cost.

Box 3 – Improving efficiency and service delivery programme

The improving efficiency and service delivery programme aims to ensure that NRW undertakes a coherent efficiency programme, primarily through a series of business-led service reviews and a 'success for less' efficiency project.

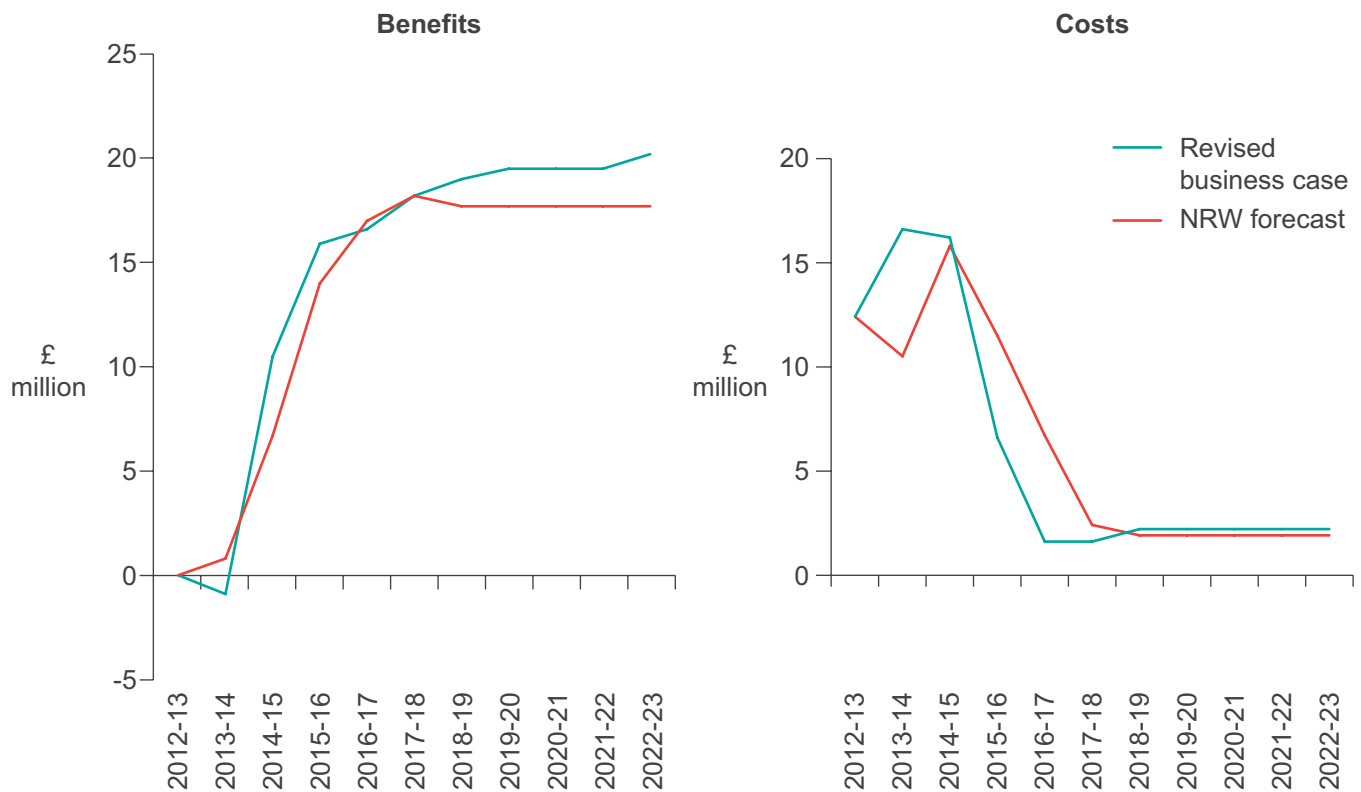
The objectives of the programme are:

- to ensure that all service reviews support the delivery of natural resource management;
- to ensure that all service reviews deliver an improved customer experience; and
- to ensure that all service reviews result in a service that is more affordable in the medium-term (through to 2020).

Source: Natural Resources Wales

1.47 NRW has identified costs of creation of £38.7 million over the three years from 2012-13 to 2014-15 and estimates total costs to 2022-23 of £68.9 million. This is £2.8 million higher than the revised business case. **Figure 10** shows the forecast distribution of costs and benefits by year. While costs were lower than forecast in 2013-14, NRW does not expect to achieve a reduction in costs or increase in benefits as quickly as it anticipated initially from 2014-15 onwards. In part, this was because NRW was unable to exit certain legacy arrangements as quickly as originally forecast. This resulted in a change in the cost and savings profile. In particular, negotiations to separate from the Environment Agency ICT provider Capgemini took much longer than anticipated resulting in exit costs being pushed back, and additional costs incurred of keeping the old arrangements for longer. NRW recognises that the scale and time required for some of the exit arrangements was underestimated in the business case.

Figure 10 – Per year distribution of estimated benefits and costs of NRW's creation, 2012-13 to 2022-23



Source: Natural Resources Wales

1.48 In order to track savings and wider benefits, NRW has a benefits framework in place. The December 2013 Gateway review of the transition programme (paragraph 1.18) identified that NRW had not, at that stage, put in place a benefits strategy and benefits realisation plan, and would be reliant on retrospectively measuring baselines and benefits achieved to date. Benefits tracking was difficult because even though NRW was able to draw upon a large amount of historical data, there was no single finance system, and a lack of agreed baselines. In the first half of 2014, NRW implemented a more robust framework for tracking the benefits of its creation, including a benefits realisation plan and framework. Now each directorate has benefits champions who collate and monitor benefits of the creation and other efficiencies. Officers document in detail benefits identified including a description and rationale for the benefit, any qualitative and quantitative benefits against a baseline, details of the previous legacy body arrangements, links to evidence sources, and other useful information such as risks or lessons learned.

- 1.49 After the year-end, NRW's finance department validates and amends the financial savings and costs identified through the benefits framework. This process takes into account the actual costs incurred by each directorate and what changes in costs can be attributed to NRW's creation. For example, the initial recording of a benefit may use an estimated annual staff cost saving, which does not equate exactly to the true cost saving. This process provides more accurate savings figures, however, it results in two systems for recording and in some cases, for reporting benefits. NRW has indicated that it is aiming to move to one, more integrated, system of recording.
- 1.50 The business case for the creation of NRW consolidated benefits identified by work streams relating to operational activities and corporate services. The work streams were established for the purposes of the business case and do not correlate to NRW's current organisational structure, or how NRW records the benefits. As such, NRW does not track benefits against these work streams and we have not sought to compare whether NRW is meeting the expected savings by work stream.
- 1.51 NRW is currently tracking all benefits, including those that have no financial saving, and those that have a financial cost but demonstrate non-financial benefits, such as more integrated working or improved communication with service users. Examples of benefits identified to date by NRW demonstrating cash, non-cash and no monetary benefits are in [Figure 11](#). However, NRW is finding it increasingly difficult and resource intensive to separate benefits arising specifically from NRW's creation from the impact of actions required to address further budgetary pressures.

Figure 11 – Examples of NRW benefits between 2013-14 and 2022-23

Name of benefit	Description	Total forecast 10-year cash realisable benefit	Total forecast 10-year non-cash realisable benefit
HR and Finance Services	Replacement of three HR and finance systems into one system with a single Business Support Service team, reducing staff required by 31 full-time equivalent	£13.3 million	–
Sample collection	Streamlined collection process and integrated IT systems resulting in faster results and more efficient route planning reducing miles driven and improving productivity.	£0.7 million	£2.3 million
Air quality emergency monitoring service	Service previously delivered under an Environment Agency framework contract with an external contractor now delivered in-house at a cost saving.	£0.3 million	–
Newborough Forest Integrated Approach	Creation of a single project team to manage a section of land comprising a designated bathing beach, National Nature Reserve, Site of Special Scientific Interest and forest.	No monetary benefits quantified, however, more consistent handling of issues and development of additional stakeholder communications including newsletter and drop-in sessions.	

Source: Natural Resources Wales

Part 2

NRW has learned from progress made and challenges faced and is now proceeding with a more ambitious and comprehensive change programme, necessary to transform itself for the future and deal with legislative changes and resource pressures



- 2.1 This section focuses on the arrangements in place for the next stage of NRW's change process, the transformation phase; the approach to dealing with legislative changes; and key internal and external challenges remaining.

Although NRW's transition programme was extensive, there were constraints and limitations which NRW has now addressed within its transformation programme

- 2.2 While NRW's transition programme was extensive (paragraph 1.18), the success of the programme was largely in putting in place required processes and strategies, with a tendency to achieve the 'low-hanging fruit' first. NRW gave less focus to more difficult and longer-term aspects such as culture change and people management. This was largely a result of time pressures. NRW has been open and frank about the work achieved to date and the limitations in what it has already implemented, recognising that it would have liked to have achieved more if additional resources were available. Senior staff have shown a high level of awareness of the key issues and the arrangements needed to move forward into the next phase of NRW's development.
- 2.3 NRW moved from its transition phase to a transformation programme from April 2015. The Gateway review of the transition programme in December 2013 recommended that achieving transformation for the organisation would be better effected with a more formal portfolio management approach to change given that the transition and transformation programmes consisted of multiple programmes in practice. NRW has incorporated this approach into its transformation programme. The change from the transition to transformation programmes has been a structured and well-managed process.
- 2.4 NRW's transformation programme demonstrates that it has prioritised areas that had been less well covered previously, such as people management, and that it is focussed on delivering NRW's vision and purpose. NRW has produced a report²² on the first two years in operation and has applied learning from experience gained during the transition phase to establish the transformation programme. NRW has also continued to use good practice from other sources to inform its transformation programme. NRW is engaging with the Wales Audit Office Good Practice Exchange team to facilitate sharing of its knowledge and experience across Welsh public services.

22 Creating the Foundation for Delivery – Transition Report, Natural Resources Wales, November 2015.

NRW has increased its focus on people management, although job evaluation remains a key risk

- 2.5 During its transition phase, NRW managed a number of staff-related projects to form the basis of its approach to workforce and people management including:
- the TUPE transfer of staff from the legacy bodies;
 - two voluntary exit schemes;
 - harmonisation of staff terms and conditions;
 - a single pay policy; and
 - a Wellbeing, Health and Safety strategy.
- 2.6 In April 2015, NRW implemented a new performance management system to replace legacy arrangements. The new system includes the completion of a Performance and Development Plan to set performance objectives and identify training and development needs. At the end of October 2015, 1,425 staff had completed a plan and logged it in the HR information system, equating to 73 per cent of permanent employees. NRW expects that additional staff have completed plans not yet on the system. Directorates collated over 2,100 training requirements noted in the plans in addition to over 2,000 training requests previously submitted as part of the Well-being, Health and Safety strategy rollout. NRW is scheduling training courses and developing a learning programme, which includes, as a priority, a management development programme.
- 2.7 From April 2015, NRW has increased its focus on people management, with one of the five main transformation programme strands being 'Developing our People and Teams'. Work streams within this programme include: job evaluation; developing and implementing various people policies; management leadership and capability; transformation portfolio culture change; learning and development; and equality and diversity ([Case Study 4](#)).

Case Study 4 – NRW's current actions and future plans for equality and diversity

Since its creation, NRW has placed importance on equality and diversity. NRW operates an equality and diversity forum, and has published two annual reports on its achievements in relation to equality. NRW participated in the Stonewall Workplace Equality Index in 2014 and 2015, improving its ranking year on year.

NRW considers the need for an Equality Impact Assessment for all of its policies and Board papers.

In April 2015, NRW published a Strategic Equality Plan for 2015 to 2019. NRW's equality plan objectives stem from the 'Good For' principles of environment, organisation, knowledge, business and people. The objectives are explicit on setting clear standards and expectations in service delivery, by understanding how communities access the services it provides, and any barriers NRW's customers face.

Within the transformation programme, the equality and diversity work stream includes actions to:

- implement the strategic equality plan and report quarterly on progress into the corporate dashboard;
- build networks with external partners to share good practice;
- embed equality into the procurement guidance; and
- improve self-disclosure of individuals' equality and diversity data through MyNRW to inform reporting and future plans.

NRW aspires for the workforce to be more representative of the protected characteristics and to develop a culture where people feel able to be themselves at work and are valued and respected.

Source: Natural Resources Wales

- 2.8 Part of the people programme includes the development of a formal Organisational Development and People Management strategy. In June 2014, NRW published a basic 'People Strategy' in place for 2014 to 2017 with links to the corporate plan and business plan. NRW intends the new strategy to address aspects such as workforce planning, succession planning, and talent management. NRW aims to publish this strategy by April 2016. In May and July 2015, the senior leadership team undertook two workshops on workforce planning, with the aim of producing a separate workforce plan linked to key priorities and future delivery. This work has informed current strategic reviews of the business, which will in turn drive the workforce plan.

- 2.9 NRW is currently undertaking an extensive job evaluation exercise. NRW has contracted an external company to support the exercise through the development of a job matching methodology and generic role profiles. NRW has a proactive and productive relationship with the relevant trade unions, which should assist the job evaluation process and is also developing a staff communication plan to manage staff expectations and mitigate the risks to morale that are inherent in job evaluation. NRW plans to complete job evaluation by February 2016. This is a very tight timescale and some actions included within the original project plan for achieving it have already slipped, although the target completion date has remained the same. It is important that the job evaluation approach is flexible enough to meet NRW's future business needs. There is a risk that role descriptions and job design resulting from the job evaluation exercise may not align with new service delivery arrangements, organisational development, and staff training and development; particularly because NRW intends to complete the job evaluation exercise before the Organisational Development and People Management strategy is in place.
- 2.10 NRW produces comprehensive data on its workforce profile, such as by age, gender, disability and pay grade. NRW is considering this data as part of its workforce planning. Data presented to the May 2015 workforce planning workshop showed that 14 per cent of staff were aged 55 or over and an additional 14 per cent were aged between 50 and 55. As part of the May and July workshops, each directorate considered its workforce strengths and weaknesses, with the Knowledge, Strategy and Planning directorate identifying a weakness in the age profile of its 'experts' due to the number of staff nearing retirement, which could result in loss of expertise. Several directorates noted that they are looking to implement better succession planning.
- 2.11 NRW had experienced issues with the accuracy of MyNRW data, including on sickness absence rates, but is currently building an improved approach to data collection via the MyNRW system. It has recently developed data on the number of current vacancies across the organisation and aims to improve data on equal pay following the job evaluation exercise. Now, the executive team regularly receives data on workforce information such as vacancies and appraisals, with data reported to the Board focussing on wellbeing, and health and safety issues.

NRW is working to improve its staff and stakeholder engagement, following evidence of weaknesses during the transition phase

- 2.12 During its first year of operation, NRW engaged in direct dialogue with staff, including involvement with managers and the senior leadership team, to discuss change and transition, and also published various internal communications. In its own review of the transition programme, NRW recognised that the wider understanding of the change process was poor; there was limited communication of the drivers for change and the successes achieved; and it was difficult to achieve an appropriate balance with its communications.
- 2.13 In October 2014, NRW launched a three-year communication strategy. As part of this strategy, in order to communicate its vision and future transformation programme to staff and wider stakeholders, NRW developed a 'roadmap', which it launched in January 2015. The roadmap sets out NRW's transformation vision; values and behaviours; and a timeline of key events from 2013 to 2020. While the aim was to explain some of the complexities associated with the process, due to time pressures, NRW launched the roadmap before the detail of the transformation projects was fully constructed and populated. As the detail of the transformation projects has become available, NRW has communicated this to staff.
- 2.14 NRW undertook its first People Survey in February 2015 in order to inform its ongoing transformation, gauge staff opinion and create a baseline for future surveys. The response rate was 58 per cent and showed mixed results. The main areas with the least positive responses were leadership and change; pay and benefits; learning and development; and whether the organisation would take action from the survey. Some of these areas reflect the scale and significance of the changes at NRW, and the weaknesses in communication of the programme. The majority of respondents answered positively to questions on organisational culture, organisational objectives and purpose, and their work (Figure 12). NRW is implementing an action plan to address key issues, including in relation to communication.

Figure 12 – Most and least positive question responses from NRW People Survey, February 2015

Survey questions	Positive percentage
Most agreement	
I am interested in my work.	94
I have some really good friendships at work.	87
I am trusted to carry out my job effectively. I have the skills I need to do my work effectively.	86
I am sufficiently challenged by my work. My manager is considerate of my life outside work. The people in my team are encouraged to come up with new and better ways of doing things. I am treated with respect by the people I work with.	85
Least agreement	
I feel that the organisation as a whole is managed well.	20
When changes are made in the organisation they are usually for the better.	17
I think that the different parts of the organisation work well together.	15
I feel that change is managed well in the organisation.	14
The pace of change in NRW is monitored and adjusted when necessary.	12

Source: Natural Resources Wales staff survey results

- 2.15 NRW is working on its communication with staff to improve staff engagement and understanding of the roadmap. NRW is undertaking workshops and road shows on various topic areas, encouraging senior staff to regularly 'floor-walk', utilising Yammer, and planning a new People Survey around February 2016. Each directorate has developed and is implementing its own plan to improve engagement and other key issues following the staff survey.
- 2.16 NRW is also strengthening its engagement with external stakeholders. NRW maintains a list of all external stakeholders, with account handlers for key stakeholders. Evidence to the Environment and Sustainability Committee's 2015 annual scrutiny of NRW suggested some inconsistencies in the communications to stakeholders. In response, NRW stated it is 'redoubling our efforts to improve communication', including:
- contacting all stakeholders who gave evidence to ensure they have appropriate contacts within NRW;
 - instigating workshops with angling groups to discuss further hatcheries proposals; and
 - investigating options to best assess how planning advice is being received, how effective it is, and how customers view the advice and service to enable further improvement.
- 2.17 NRW has improved its customer call centre and website feedback forms to respond better to public queries. The June 2015 Better Regulation Delivery Office report on better regulation found that NRW recognises the value of engagement and has put in place a variety of mechanisms to ensure those they regulate or who are impacted by regulation have the opportunity to share their views. However, it highlighted that more work could be done on the NRW website to make it more business friendly. NRW has already started work on running focus groups on business engagement, with the potential of creating a separate business hub on the website.

NRW is taking action to address identified weaknesses in its risk management, procurement and grants arrangements

- 2.18 NRW has basic risk management arrangements in place, which are developing. The NRW Board approved a risk management policy in October 2014. One of the main aims is for risk management to be part of mainstream management. Until September 2015, NRW maintained an operational risk register cross-referenced to outcomes in the Corporate Plan. The Audit and Risk Assurance Committee discussed this as a standing item each meeting. In September 2014, the Committee requested a strategic risk register to consider the wider environmental and natural resource management risks and challenges that can impact NRW's work. This took longer than the Committee's target completion date but resulted in the creation of a single corporate risk register in September 2015.
- 2.19 In September 2015, NRW's internal audit reported limited assurance²³ on risk management. The audit used HM Treasury's Risk Management Assessment Framework, which generates a score from level one to level five²⁴. The report found that the overall score for NRW was level one, with some good progress to level two. It also stated that NRW has 'a reasonable approach to taking risk into account in its delivery and decisions' but had not yet fully embedded key risk processes. Some of the key recommendations of the report were to:
- establish, communicate and maintain risk management guidance and procedures relating to the risk management policy;
 - arrange for staff risk training to be delivered for key staff, including senior management;
 - include risk management in job requirements, induction processes and performance assessments;
 - ensure that risk management is further embedded in the decision making process below the Board and Executive team level; and
 - decide at Board level what risk maturity level the organisation should aspire to and undertake a gap analysis with actions identified to achieve the agreed level.
- 2.20 As part of the transformation phase, NRW has recognised the potential for effective procurement to save money and drive efficiencies, as well as to contribute to achieving corporate objectives. On 1 April 2013, Wales-based procurement staff from the legacy bodies transferred to NRW. These staff had varying levels of experience but due to the set-up of the legacy bodies' procurement functions did not have direct experience of procuring the full range of goods and services that NRW required. Initially, these staff typically operated under legacy ways of working using legacy systems. Following the recruitment of a new Head of Procurement in October 2013, NRW formed a 'NRW Procurement Team', which has utilised the MyNRW system as a central source of expenditure data and management information. NRW officers consider that the staffing levels, skills and experience within procurement have improved significantly.

²³ A Limited level of assurance is the second lowest level of assurance out of four possible ratings, and is defined as 'there are significant weaknesses in the framework of governance, risk management and control such that it could become inadequate and ineffective'.

²⁴ Level 1 is the lowest rating where there is evidence that the organisation has awareness and understanding; the highest score, Level 5, refers to an organisation where there is excellent capability established.

- 2.21 In November 2013, NRW performed a self-assessment of its procurement function using the Welsh Government Procurement Maturity Model, scoring 0.39 out of four ('non-conforming'). The lowest scoring areas within the assessment were contract and supplier management, and performance management; and none of the eight areas assessed scored higher than one ('developing towards conforming'). NRW considered some of the key reasons behind the low score were a lack of a joined-up approach across the organisation; areas of good practice not being consistently applied across the organisation; and limited alignment with the Wales Procurement Policy Statement on which the maturity model is based. NRW officers also considered that, given the maturity model assesses how effectively an organisation is using procurement to support the delivery of its corporate objectives, it would be difficult for any new organisation to achieve this in its early stages.
- 2.22 Following its self-assessment, NRW implemented the Procurement Change Programme, and produced a procurement strategy for 2015 to 2017 (Box 4). The key drivers for the strategy are to drive efficiency and contribute to achieving sustainable development in Wales. The procurement strategy incorporates specific actions aimed at achieving a minimum maturity model score of two (conforming). The Welsh Government has recently revised its maturity model, following publication in June 2015 of an updated Procurement Policy Statement, and produced an updated assessment tool. NRW is performing a pilot assessment to test the new model, which will enable an early assessment of progress made. The Welsh Government is also in the process of contracting a third party to perform a formal independent assessment of NRW's procurement function by the end of March 2016 as part of its wider programme of public sector fitness checks. Following these assessments, NRW expects to review its Improvement Plan and, in conjunction with the Welsh Government, develop its procurement strategy for 2017 to 2022.

Box 4 – NRW Procurement Strategy

NRW's vision for procurement is to ensure 'that we only buy goods, works or services that we really need, to get the best value for money, so as to optimise the impacts on the environment, on people and on the local economy'.

The objectives of the procurement strategy and its associated improvement plan are to:

- develop a strategic approach to the management of procurement across NRW;
- deliver a common, corporate process of strategic sourcing, supplier relationship development, performance reporting and contract management;
- drive efficiency, reduce costs and deliver qualitative benefits throughout NRW;
- ensure compliance with relevant legislation, policies and procedures;
- enhance leadership, governance and skills within procurement;
- give more opportunity to local and SME suppliers to participate by increasing visibility of our procurement plans and opportunities; and
- maximise innovation, sustainability and natural resource management through our procurement activities.

The procurement strategy outlines priorities and actions against four key areas:

- 1 Development – ensuring the procurement team, and others involved in procurement activity, have the required capability and capacity for providing procurement expertise and advice, and supplier management.
- 2 Engagement – lowering barriers of working with SMEs, social businesses and larger scale enterprises; ensuring that procurement processes are open and transparent; and engaging with staff to understand and manage their consumption of resources.
- 3 Efficiency and value for money – delivering best value for money at all times and achieving savings and benefits through better reporting and monitoring; optimising performance of key suppliers; and reducing waste.
- 4 Governance – improving the balance between delivery and oversight by establishing appropriate corporate processes and better management of key suppliers.

Source: Natural Resources Wales

- 2.23 NRW is strengthening its arrangements for awarding grants to third parties to aid in the delivery of outcomes. The Countryside Council for Wales previously held statutory powers to distribute grants, with limited grant funding from the other two legacy bodies. The final round of Countryside Council for Wales' grants ended in March 2015 and NRW has managed two rounds of grant funding since its creation for grants starting from April 2015 and April 2016, with total funding committed to date of around £9 million. NRW expects to run a further round in 2016 for grants starting from April 2017.
- 2.24 One grant scheme previously run by the Countryside Council for Wales was the Communities and Nature project, distributing £14.5 million of European, Countryside Council for Wales, other public sector and private sector funds. NRW took over the management of this project on vesting day until the end date of 31 August 2014. The project was subject to a number of reviews including a Welsh Government Funding Office inspection which identified weaknesses prior to NRW's creation in project management and controls. NRW has amended its processes to address the review's recommendations and lessons learned from other reviews.
- 2.25 NRW is clear about wanting to be a funding organisation and feedback obtained by NRW from external partners and internal practitioners found that great value is put upon working in partnership by all involved. However, NRW acknowledges that round one of NRW grant funding was rushed and the Environment and Sustainability Committee raised some concerns about grant processes in its 2015 scrutiny. NRW is confident that it has dealt with these concerns in round two and has improved processes for existing round one partners. For example, the application process for round two is more transparent, with better information provided on assessment criteria and governance arrangements; clearer links between grant awards and corporate objectives; and an earlier digital launch. NRW is clear on the risk of partners not delivering but is mitigating this through due diligence and monitoring processes. However, monitoring of grants awarded in round one is under the old Countryside Council for Wales' rules, which NRW is currently updating to meet its needs. NRW and the Welsh Government have regular meetings that provide an opportunity to discuss grant expenditure and monitoring of grants. NRW's business improvement team is also reviewing its grant processes against lean principles to identify any further areas for improvement.

NRW has taken a pro-active approach to dealing with legislative changes and the prospect of new statutory responsibilities

- 2.26 NRW appears to be planning effectively and proactively for its new duties associated with the Well-being of Future Generations (Wales) Act 2015 and also with the Environment (Wales) Bill, which is expected to be enacted in spring 2016 (Appendix 2). NRW has clear plans to prepare for and implement both pieces of legislation, including a range of projects. NRW has made good progress in refining its overall business objectives to incorporate key elements of the legislation.
- 2.27 An overarching theme of the Environment (Wales) Bill is natural resource management. One sub-programme of NRW's transformation portfolio is 'embedding natural resource management' and the programme board includes representatives from across the organisation to embed the principles across all directorates. NRW is also currently analysing all business activities in terms of the resources used against outcomes achieved to understand better how resources are used and the potential for using them differently, in line with the new legislation.
- 2.28 NRW engages regularly with the Welsh Government and external groups regarding the legislation and associated activities. NRW's natural resource management manager has fortnightly meetings with relevant Welsh Government policy leads to discuss their work programmes, and provide and receive guidance. NRW also sits on the Welsh Government's own natural resource management programme board and reference group. NRW engaged extensively with the Welsh Government and the Welsh Local Government Association to prepare for the introduction of the Well-being of Future Generations (Wales) Act; and the NRW Chair or a non-executive member selected by the Chair will sit on an Advisory Panel to the Future Generations Commissioner. NRW actively participates with relevant groups such as the Wales Environment Link group, and is developing its engagement activities with local authorities to join shadow Public Service Boards where they exist.
- 2.29 There are risk registers associated with developing the organisation in terms of the Well-being of Future Generations (Wales) Act and the Environment (Wales) Bill, and the 2015-16 performance framework features key performance indicators (KPIs) in relation to both pieces of legislation. Reporting on progress for April to November 2015 showed that:
- NRW was within 10 per cent of its target to prepare to deliver its responsibilities under the Well-being of Future Generations (Wales) Act, having completed a Project Charter, established a project group in relation to Public Service Boards and run workshops with current Local Service Boards; but is behind schedule in understanding the available data and evidence to produce the first local well-being assessments due by May 2017;
 - two KPIs related to natural resource management were on target; and
 - NRW was on target to deliver the State of Natural Resources Report by September 2016 as proposed by the Environment (Wales) Bill.

- 2.30 NRW is aware that additional funding may not be available to meet all future statutory duties but is working to develop the natural resource management approach and is confident that this will lead to longer-term savings. In relation to the Well-being of Future Generations (Wales) Act, operational staff currently engage with 14 Local Service Boards, which will increase to an expected 22 Public Service Boards from April 2016. NRW sees this engagement as part of its core business rather than an additional cost pressure. In preparation for the expected Environment (Wales) Bill duties, the Welsh Government Nature Fund allocated £1 million to NRW in 2014-15 for natural resource management trials and setting up natural resource management projects. In June 2015, the Minister for Natural Resources indicated to the Environment and Sustainability Committee that there will be transitional costs for NRW in developing the natural resource management approach in line with the Environment (Wales) Bill, which may be covered by additional Welsh Government funding, but this will lead to future savings.
- 2.31 Aside from these two key pieces of legislation, NRW has dealt with the transfer of the functions, assets and staff of the three Internal Drainage Boards in Wales into NRW from 1 April 2015, bringing 19 staff and £1.4 million of income²⁵. The Welsh Government touched on the potential transfer of functions in the initial consultation for the creation of NRW in 2012. In November 2013, the Welsh Government announced the decision to transfer the functions, following a Public Accounts Committee report on Caldicot and Wentlooge Levels Internal Drainage Board in October 2013. NRW put in place an Internal Drainage Board Transition Programme with multiple work streams. The transition work included: legal and financial due diligence on the three Boards; integration of financial systems; discussions with the UK Department for Environment, Food and Rural Affairs regarding English land within the three Boards; and regular reporting to the Board, and Audit and Risk Assurance Committee. The update at the March 2015 Audit and Risk Assurance Committee noted that stakeholder feedback on the management of the transition was very positive.
- 2.32 In June 2015, the Welsh Government announced a role for NRW when the devolution to Wales of Landfill Disposals Tax comes into force from 1 April 2018. The new Welsh Revenue Authority will undertake the collection and management functions for the tax, but will delegate the compliance and enforcement functions to NRW.

²⁵ NRW receives income on an ongoing basis largely through drainage rates collected by local authorities through council tax and non-domestic rates; or rates paid directly to NRW from agricultural landowners.

2.33 Given the increase in both NRW's and other public bodies' responsibilities, there could be a lack of understanding from the public and stakeholders on the exact nature of NRW's role and the size of contribution that NRW can be expected to make towards environmental targets. NRW's work relating to the Well-being of Future Generations (Wales) Act is partly reliant on other members of the Public Service Boards, including local authorities. Some of NRW's other desired outcomes have shared accountability across the UK, Europe and globally, and NRW is reliant on significant effort from a range of partners to achieve them, including other public bodies, private firms, and individuals. For example, NRW has KPIs relating to specific actions to help halt biodiversity loss by 2020, but NRW's actions alone would not guarantee full compliance with European biodiversity targets for 2020.

NRW recognises that there are some risks and significant internal and external challenges for it to address in order to sustain its planned pace of progress towards transformation, whilst continuing to deliver savings

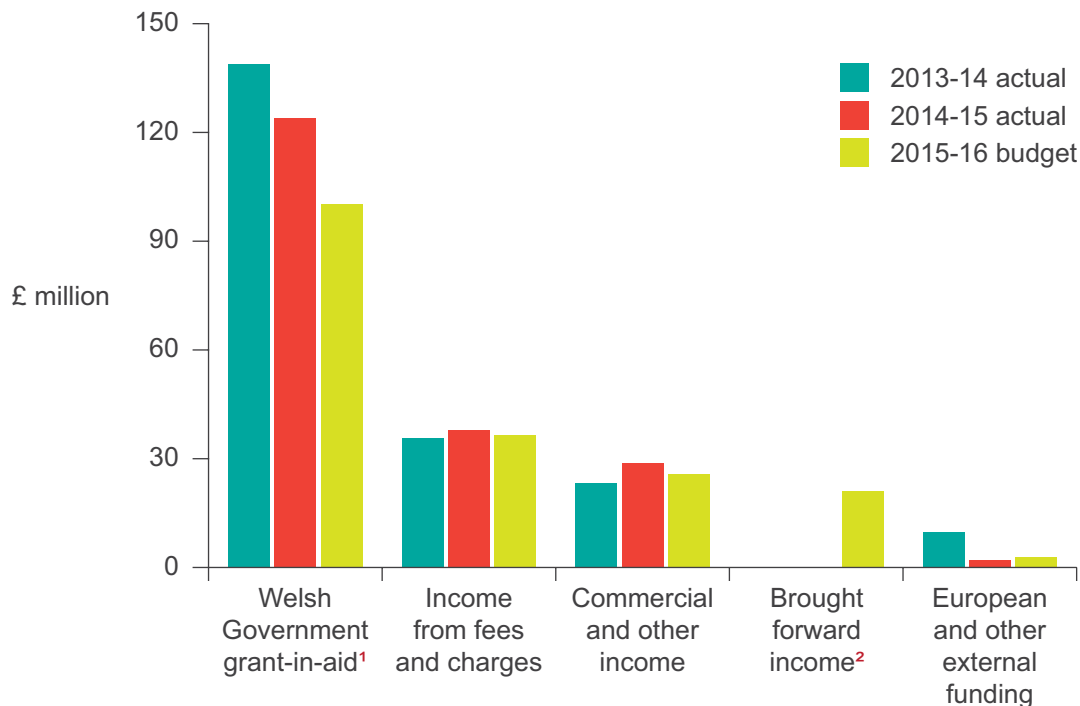
NRW is likely to face increased financial uncertainty and is modelling assumptions about future budgets and cost pressures to develop medium-term financial plans

2.34 NRW receives income from:

- grant-in-aid funding from the Welsh Government;
- fees and charges such as water abstraction charges to take water from rivers and groundwater; fishing licences; and hazardous-waste charges;
- commercial and other income such as the sale of timber and renewable energy; and
- European and other external funding.

2.35 **Figure 13** shows the income reported in the 2013-14 and 2014-15 annual accounts and the latest budgeted income for 2015-16 reported to the Board in October 2015. Total budgeted income for 2015-16 is £187 million; £6 million lower (three per cent) than 2014-15's actual income and £21 million lower (10 per cent) than 2013-14's actual income. Although income has reduced, and, in particular, grant-in-aid income has reduced significantly, the profile of income is impacted by one-off income granted in 2013-14 and 2014-15 for issues such as tree disease (**paragraph 1.16**) and transition costs. Core grant-in-aid funding reduced by £3.2 million in 2015-16.

Figure 13 – NRW income from 2013-14 to 2015-16 in cash terms



Note:

- 1 The profile of grant-in-aid income is impacted by one-off income granted in 2013-14 and 2014-15 for issues such as tree disease (paragraph 1.16) and transition costs.
- 2 Brought forward income relates to income from a number of sources, which was received in 2014-15 but specifically ring-fenced for projects in 2015-16.

Source: Natural Resources Wales

2.36 NRW also has the ability to carry forward income either for specific planned projects or because the Welsh Government has awarded additional grant-in-aid late in a financial year (paragraph 1.30). In 2015-16, NRW brought forward £21.2 million of funding.

2.37 NRW reports its costs to the Board based on staff costs, non-staff costs, revenue projects such as those relating to transformation, and capital projects such as the Flood Coastal Risk Management Programme. Figure 14 shows the breakdown in budgeted spend by category for 2015-16 as at April 2015. Latest analysis at the January 2016 Board meeting showed that NRW was below budget on expenditure to December 2015, due to planned underspend on capital projects. NRW is forecasting to maintain this underspend and carry forward income into 2016-17 to help mitigate expected reductions in income.

Figure 14 – Budgeted spend by category for 2015-16, as at April 2015

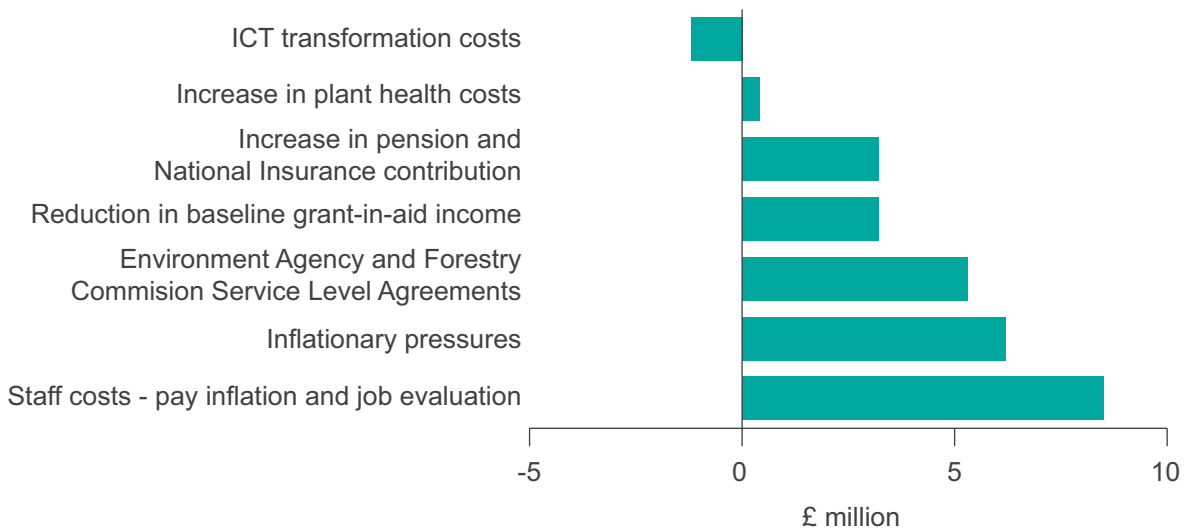
Type of expenditure	£ million
Staff costs	80.0
Non-staff costs	65.9
Capital projects	28.2
Revenue projects	12.9
Total expenditure for 2015-16	187.0

Source: Natural Resources Wales

- 2.38 Future budget reductions, in-year cuts in core funding and further financial pressures increase the risks of reductions in services and of NRW failing to achieve its outcomes. NRW models a range of budget scenarios to plan for the fluctuations in budgets. Prior to September 2015, NRW's long-term expectation was to make 25 per cent savings by 2020, based on a five per cent reduction in grant-in-aid in cash terms year on year. It had implemented a suite of efficiency measures to manage the impact of the current £3.2 million grant-in-aid funding cut and was identifying further strategies to achieve the 25 per cent cut. However, in September 2015 the Welsh Government asked NRW to consider scenarios for a higher level of reduction in grant-in-aid each year over the next three years, and indicated at that time that it was expecting to have to reduce the revenue grant-in-aid for 2016-17 by 10 per cent.
- 2.39 In December 2015, following the publication of its 2016-17 Draft Budget, the Welsh Government confirmed to NRW a cash-terms reduction of eight per cent on a like-for-like basis in the revenue grant-in-aid funding for 2016-17 related to non-flood risk management, and a five per cent reduction in flood risk management grant-in-aid. The Welsh Government has maintained capital grant-in-aid at current levels. More detail on future years' budgets will not be available until the publication of the new Programme for Government, following the May 2016 National Assembly elections.

- 2.40 NRW is still working to the assumption of total budget reductions of 25 to 40 per cent by 2020. NRW informed us it finds annual budget allocations from the Welsh Government restrictive but manages the impact through its financial planning and modelling. However, there is a risk that budget cuts require an even greater prioritisation of work with difficult decisions to be made, particularly given uncertainty over any additional funding for new statutory responsibilities (paragraph 2.30). NRW considers that the expected level of budget cuts will require fundamental changes to the purpose and structure of NRW.
- 2.41 As part of its financial modelling, NRW has estimated the additional cost pressures it incurs that were not included within the original business case costs. For 2015-16, NRW estimates additional cost and funding pressures of £26 million (Figure 15). NRW is aiming to mitigate these costs through delivering the cash-realiseable benefits from the business case; reducing headcount; reprioritising activities; and driving efficiencies.

Figure 15 – NRW additional 2015-16 cost pressures compared with business case estimates

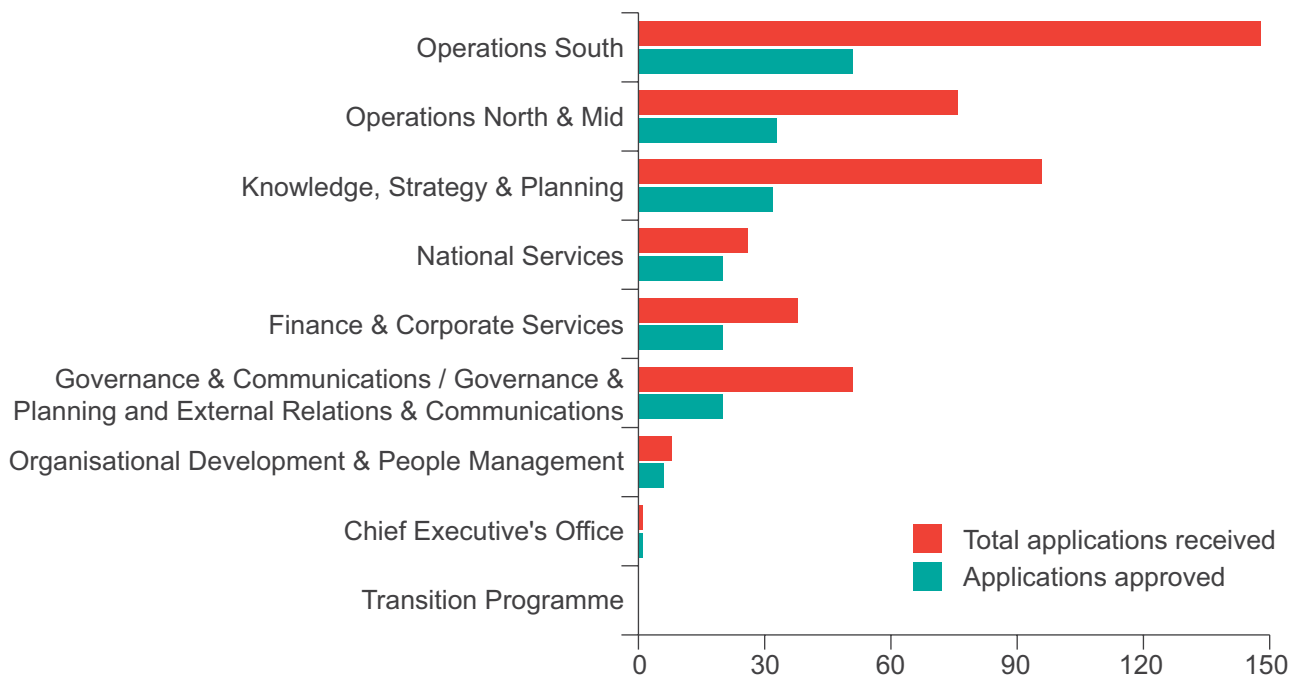


Source: Natural Resources Wales

NRW has reduced its headcount across business functions largely using voluntary exits however it has subsequently identified skills gaps in some areas and is likely to face further capacity pressures

- 2.42 NRW is likely to experience further resource pressures, given the reduction in the number of staff since its creation, the complex transformation programme underway, and additional statutory responsibilities (paragraph 2.25 and Appendix 2). NRW has reduced its staff numbers from 2,186 (2,082 full-time equivalents) on vesting day to 2,017 (1,919 full-time equivalents) in October 2015. NRW has achieved this decrease predominantly through two voluntary exit schemes. NRW funded the schemes using £6 million of repayable Invest-to-Save funding from the Welsh Government. NRW is repaying £2.5 million in 2015-16, and is due to repay £1.8 million in 2016-17 and £1.8 million in 2017-18.
- 2.43 NRW assessed all exit applications against criteria to determine if the skills could be lost, and a lessons-learnt review of the first scheme stated the scheme 'had minimal impact on the business and it is considered that the right staff were allowed to leave'. Across both schemes, NRW received 444 applications, of which it approved 183. Applications and approvals were spread across NRW's business areas, and some applications were rejected in all directorates bar the Chief Executive Office (Figure 16). Three of the approved applications were posts from the leadership team.

Figure 16 – Number of voluntary exit scheme applications received and approved, by directorate



Source: Natural Resources Wales

- 2.44 NRW is undertaking workforce planning to assess the remaining workforce against future requirements (paragraph 2.8). However, a recent workforce planning workshop highlighted a number of areas with skills gaps, and budgetary pressures could result in further staff cuts. One key directorate likely to face more substantial capacity pressures is Organisational Development and People Management, given the significant ongoing activity to deliver major projects under the transformation programme area 'Developing our People and Teams' (paragraph 2.7). In some areas, NRW is recruiting additional staff, however, niche posts, such as in nuclear regulation, have been hard to fill and, in some cases, the posts remained vacant for over four months but are now filled.
- 2.45 Given the capacity pressures, there is a further risk that additional resources required on matters such as job evaluation could cause distractions for other transformation areas and would result in slippages. This could lead to delays in achieving benefits and give a negative perception of the transformation process to staff, the Welsh Government and other external stakeholders.

NRW's Board is experiencing changes in relation to its membership, the time available for each member, and a shorter length of appointment

- 2.46 The tenure of the original NRW Board ended in October 2015. The Welsh Government invited five Board members to continue for a second term and looked to appoint a new Chair and five new members. The Welsh Government extended the tenure of the existing Chair from August 2015 to 30 November 2015, and on 3 November 2015, the Minister for Natural Resources announced the appointment of a new Chair and five members. Given the strength of the previous Board (paragraph 1.25), changes in membership could cause a lack of continuity and capacity and slow previous progress. NRW has developed a clearer induction process and materials for the next Board term and proposed a buddy system to pair new and existing Board members to try to mitigate this risk.
- 2.47 From November 2015, the Welsh Government is cutting the number of days each year per Board member from 60 to 36, with the number of members remaining the same as the original Board in operation from April 2013 at 10 members²⁶ plus the Chair and Chief Executive. All Board members are paid on a daily rate and so the changes will represent a financial saving. The Welsh Government considers the reduction in time reflects the move from transition to transformation, and the effectiveness of the executive team. However, continuing Board members have expressed concern that the reduction in time per member will impact negatively on the support they can offer.

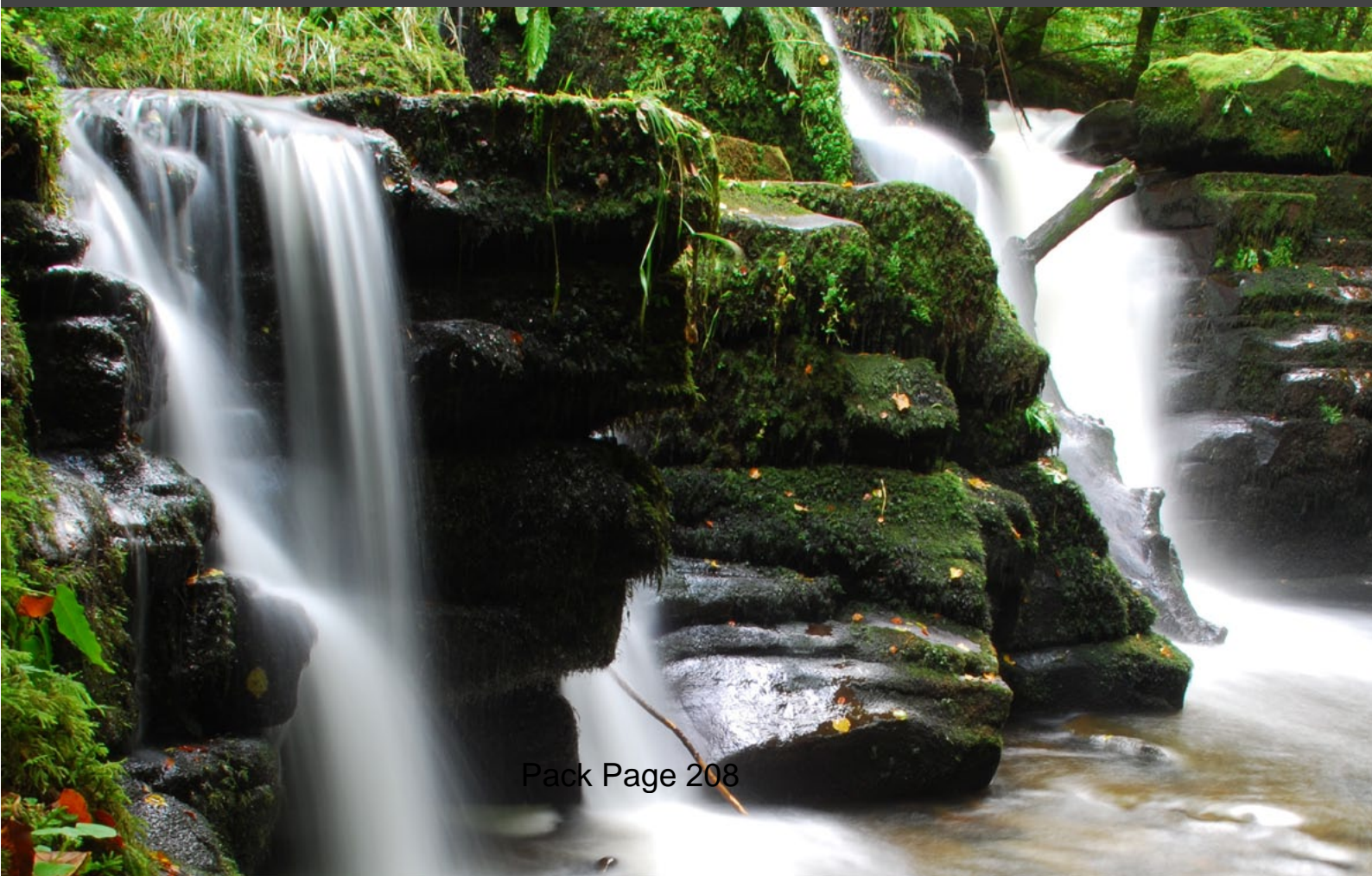
²⁶ From January 2014 to October 2014, the NRW Board had nine members; and from November 2014 to October 2015, it had eight members.

2.48 We note that the tenure of Board members for the new term, excluding the Chair, will be two years from 1 November 2015 to 31 October 2017. This is shorter than the original Board tenure of three years and shorter than some other Welsh Government sponsored bodies, for example, recent appointments for the National Museum Wales advertised a tenure of four years, and Sport Wales has a current tenure of three years. The term of the new NRW Chair is three years. A shorter tenure could result in a risk of a lack of continuity and loss of experience after a short time period; and too much focus on the short term. However, we understand that the Welsh Government wanted the opportunity to be able to consider the dynamics and skills mix of the Board after two years, and will seek to reappoint members if it assesses that the Board is working well.

Appendices

Appendix 1 - Audit scope and methods

Appendix 2 - Indicative NRW responsibilities and timeline relating to the Well-being of Future Generations (Wales) Act 2015 and Environment (Wales) Bill, 2016 to 2020



Appendix 1 - Audit scope and methods

The scope of our work

The overall scope of our work was whether NRW has in place, or is developing, effective governance arrangements that support delivery of its key priorities and outcomes. Our examination covered progress against intended performance; vision and strategic direction; accountability arrangements; management of resources; sponsorship arrangements with the Welsh Government; and the way in which NRW has been preparing for the implications of the Well-being of Future Generations (Wales) Act and Environment (Wales) Bill.

The study focused on administrative aspects of NRW and the extent to which these support good governance and operational effectiveness. The study did not review NRW's operations or regulatory decisions in detail, nor did it examine the rationale for establishing NRW.

The Welsh Government has procedures to conduct a probationary review of newly formed sponsored bodies following two years of operation. Having already included this study of NRW in his work programme, the Auditor General confirmed to the Welsh Government that he expected that this review would cover the ground that would otherwise be in a separate probationary review, drawing also on our work in auditing NRW's annual financial statements. The Auditor General wrote to the Welsh Government in November 2015 to provide a summary of key findings relevant to the scope of the Welsh Government's probationary review requirements.

Audit methods

Our study fieldwork involved:

- interviews with NRW Board members, executives and staff;
- a review of documents provided by NRW and the Welsh Government; and
- attending and observing an NRW Board meeting.

We drew upon established audit methods and approaches in relation to governance, including our corporate assessments of local authorities in Wales and our annual 'structured assessment' of NHS bodies.

To avoid duplication, where possible, we drew upon the results of recent work, including work by NRW and the National Assembly, particularly:

- a staff satisfaction survey undertaken by NRW (February 2015);
- NRW's own review of its first two years of operation, **Creating the Foundation for Delivery – Transition Report** (November 2015);

- scrutiny of NRW by the Environment and Sustainability Committee of the National Assembly between May 2014 and July 2015, including responses to a stakeholder survey, evidence sessions, the Committee's final letter and NRW's response;
- internal audit work undertaken by NRW's internal audit team on a range of areas, and by the Welsh Government's internal auditors on the sponsorship arrangements with NRW; and
- a review of NRW against the Principles of Good Regulation by the Better Regulation Delivery Office.

The study team liaised with other Wales Audit Office colleagues in order to co-ordinate links with other financial and performance audit work, including:

- financial audit work undertaken as part of the annual external audit of final accounts, including following-up risks in relation to integration of financial systems, financial controls, the financial statements, responding to financial pressures, achieving savings, and the annual governance statement;
- the Auditor General's value-for-money studies on coastal flooding and erosion (ongoing); and **Managing early departures across the Welsh public bodies** (February 2015);
- the Wales Audit Office's Good Practice Exchange support to the NRW Board Members' development programme;
- links established with NRW by the Wales Audit Office Sustainable Development Manager in relation to implementing the Well-being of Future Generations (Wales) Act and preparing for the forthcoming Environment (Wales) Bill, which is expected to receive Royal Assent by spring 2016; and
- responses from the NRW Board and senior leadership team to the Wales Audit Office **Picture of Public Services** report June 2015 survey questionnaire.

Appendix 2 - Indicative NRW responsibilities and timeline relating to the Well-being of Future Generations (Wales) Act 2015 and Environment (Wales) Bill, 2016 to 2020

Responsibilities for NRW under the Well-being of Future Generations (Wales) Act 2015

The Well-being of Future Generations (Wales) Act 2015 requires NRW to sit on the Public Service Board for each local authority area. The aim of Public Service Boards, in operation from April 2016, is to improve the economic, social, environmental and cultural well-being of its area by working to achieve the well-being goals. Each Public Service Board must prepare and publish a 'Local Well-being Plan' setting out objectives and review the plan annually to show progress.

NRW must also meet the general requirements of the Act applicable to Welsh public bodies, including setting and reporting on its own objectives to achieve the seven well-being goals; and applying a sustainable development principle across all its activities²⁷.

Expected responsibilities for NRW under the Environment (Wales) Bill

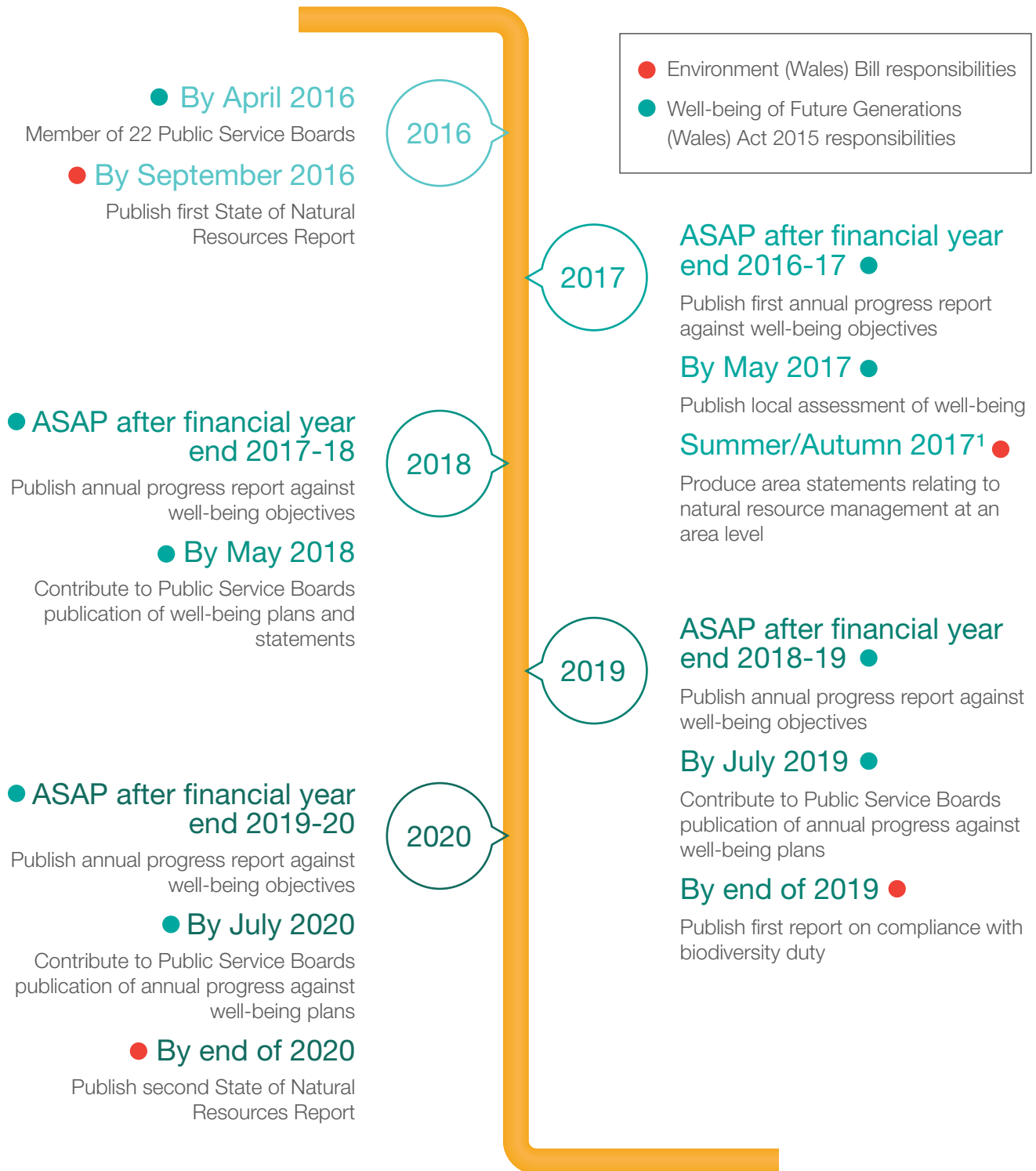
The Environment (Wales) Bill, due to be enacted by spring 2016, places specific responsibilities on NRW to produce:

- a State of Natural Resources Report every five years giving an assessment of natural resources and how well they are being managed in a sustainable way; and
- area statements to identify at a local level the priorities, risks and opportunities for managing natural resources sustainably and what actions to take²⁸.

²⁷ Well-being of Future Generations (Wales) Act 2015 – The Essentials, Welsh Government, June 2015.

²⁸ Overview of the Environment (Wales) Bill, Welsh Government, May 2015

Timeline of key responsibilities



Notes:

¹ The exact timeframe for area statements has not yet been confirmed.

Source: Welsh Government

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Mr Nick Ramsay AM
Chair
National Assembly for Wales Public Accounts
Committee
National Assembly for Wales
Cardiff Bay
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CF99 1NA

10 April 2017

Dear Nick,

Public Accounts Committee – 28 March 2017

At the PAC session on 28 March, we agreed to provide further information on several topics, as follows:

How are timber sale contracts arranged and priced?

The contracts awarded to the operator under the Memorandum of Agreement were a combination of 4 existing Standing Sales Long Term Contracts (LTCs) for Spruce that were extended and 4 new LTCs for Larch.

Several factors affect the prices in individual contracts:

Method of Sale: The contracts were either 'Standing Sales' where the customer bears the cost of felling the timber and associated haulage, or 'Roadside Sales' where NRW bears the costs. The prices in the contracts will reflect these different methods of sale.

Site Conditions: The site conditions will dictate the method of felling and consequently impact on the price i.e. steep ground working is more expensive than flat ground. The location will also impact on the cost of haulage in delivering the timber to the customer.

Tree size and timber quality: Much of the larch is of a smaller tree size and of poorer quality than our other crops. This reduces the proportion of higher value saw-logs. Furthermore the cost of processing infected Larch are higher due to bio-security restrictions.

In all cases the contracts allowed for a price review to take place using defined formulas at specified intervals to ensure changes in market prices were taken into account.

Cost of legal advice in relation to challenging the findings contained in the Auditor General's Report

During the Auditor General for Wales's investigation, the WAO sought independent legal advice on several aspects of the contracts, which he shared with us; these included:

- whether the contracts were sales contracts or fell under public procurement;
- advice on public law;
- advice on state aids.

As the Auditor General acknowledges in his report, the issues raised a number of complex legal issues. As Accounting Officer, I felt it appropriate, given the complex issues raised, to take our own independent legal advice in order to protect the position of Natural Resources Wales in the event of possible legal challenge. The advice I have received does not always correspond with that of the Auditor General's. The cost of obtaining that advice was £22,300.

Practice adopted by NRW in managing staff sickness

We have developed and implemented a number of NRW policies and procedures to more effectively manage sickness absence in the workplace on a consistent basis. In addition, we have ensured access for managers and staff to an effective occupational health and employee assistance service provision to support staff who are unwell and ensure their timely return to work.

We have committed to managing risk of mental health absence through delivery of mental health first aid training and emotional resilience training.

In NRW in the last 12-24 months we have focussed our attention on improving the quality and quantity of our absence data to develop the way we monitor and manage sickness absence.

We have used multiple internal communication channels to raise awareness of the policies and procedures, new recording system and support provisions to all staff in NRW. This is an area of work that requires continual monitoring and focus, which again we achieve through regular communication with managers and staff. Absence management data is reviewed by the NRW Board, Executive Team and local management.

Notwithstanding the above developments, it is clear that the dedication, commitment and pride that NRW staff show to meeting the objectives of NRW minimise the occurrence of sickness absence.

Internal Audit Report


This will be forwarded as soon as the work is completed.

Business Case

The Business Case is attached. It has been redacted in several places to protect the names of the parties who were involved in the commercial negotiations at the time.

I also wish to inform the Committee that as the operator has not complied with the requirement in the Memorandum of Agreement to install an additional log line, the contracts lapsed on 31 March 2017. New contracts have been put in place to ensure an orderly wind-down of the previous contracts over the coming months while we re-market the remaining timber in accordance with our Timber Marketing Plan.

Yours sincerely,



Emyr Roberts

**Prif Weithredwr, Cyfoeth Naturiol Cymru
Chief Executive, Natural Resources Wales**

Natural Resources Wales

Executive Team Paper

August 2013

Paper Title:	Developing Options for Larch investment and wider guidance on replacement of existing Spruce LTCs
Paper Prepared By:	Jerry Pritchard - Head of Timber Marketing for NRW
Purpose of Paper:	To have a final position by Sept 31st in order to make a final offer to on Larch investment and to give a wider position to the trade on our future Spruce Marketing plans and intention.
Recommendation:	<ul style="list-style-type: none"> • Seek HMO/Head of Operation agreement • For Head of Operations to seek Head of Enterprise support for an agreed course of action

1. Issue

- 1.1 We are reaching the final stages of the Phytophthora Ramorum (PR) Larch awards. The rapidly escalating position on Larch infection made evident during 2013 means Natural Resources Wales (NRW) needs to stimulate more processing capacity specific to Larch processing and contractor felling resource.
- 1.2 The scale of challenge on PR has unavoidably linked Spruce production and Spruce Long Term Contract policy intent as a major dependency to the decision on Larch investment in Wales.
- 1.3 The Larch processing investment is key critical to the marketing of Larchwood for both private and public sectors in Wales and the Marches over the following 10 years to 2024.

2. Progress to date

The spread of PR in Wales has been more rapid than had been initially predicted. The disease has now progressed from the original epicentre of the Afan and Dulais valleys to encompass an area stretching from the Welsh border at Wentwood to Talybont-on-Usk, Taf Fechan and most forests west of this line to Brechfa and Caniston in Pembrokeshire. Standing infected stands are now totalling nearly one million cubic metres over bark standing (m³obs) on the Welsh Public Estate with further infection likely next year but it is difficult to determine the extent that will be encountered, but the disease spread can only be slowed not contained.

There is also an increasing incidence in identification of the disease in privately owned woodland but currently only at small percentage of the problem encountered on the Public Estate, this expected to rise in the coming years.

To counter this spread on the public estate and provide a positive action plan NRW released two standing sale long term contracts in the spring of 2013, these contracts committed to a total volume of 560,000m³obs larch over a period of five years in the Coed y Cymoedd Forest District (CyC) and 100,000m³obs in Llandovery FD. There was also a planned release of a Direct Production contract for the western areas of CyC in the second half of the calendar year.

As the spring 2013 progressed and the larch came in to needle the extent of the disease spread from the last known points of the infection September 2012 became clearer. The disease had taken firm hold in Llandovery Forest District where there had only been sporadic outbreaks during 2012 and there had been a dramatic progression east throughout the CyC FD. It was obvious that the planned Long Term Contracts (LTCs) were now not sufficient to deal with the disease at its current rate of expansion. The disease control plan and larch replacement strategy were revisited and larch felling was increases from 220,000m³obs in 2014 to 350,000m³obs per annum for following five years, 2015 – 2020 (see table 1 below)

Table 1
Larch Clearance plan revised July 2013
(Figures in 100ks)

	CYC	Llan	CYM	CYG	Totals
2013/14	115	25	10		150
2014/15	140	65	15		220
2015/16	190	138	20	2	350
2016/17	190	138	20	2	350
2017/18	200	120	28	2	350
2018/19	130	130	65	26	351
2019/20		130	180	40	350
2020/21		74	110	40	224
2021/22			110	40	150
2022/23			110	40	150
2023/24			30	40	70
2024/25				40	40
2025/26				40	40
Total	965	820	698	312	2795

The total volume of larch available from public and private woodland in Wales and the Marches could be as high as seven million m³obs during this period.

The tender returns were evaluated and scored during July 2013 and it was recommended that three parties that made bids all be awarded contracts. This decision was made on the back of the quality and solutions offered in the bids and the fact that there was now more volume to place into contracts due the unforeseen increase of disease spread.

An offer of three standing sale contracts each totalling 65,000m³obs per annum for five years were offered in CyC two to [redacted] and one to [redacted]; this award will take out the need to run the proposed Direct Production (DP) tender in CyC, planned for released in the autumn of 2013. This DP tender opportunity will be moved to Llandovery Forest District as part of the revised disease control strategy and to provide the platform to produce larch log bar material for the DP options discussed later on in this paper.

A further standing contract was offered to [redacted] for 65,000m³obs in Llandovery FD. This offer was made to support the intended new milling infrastructure investment at [redacted] sawmills in recognition that without an offer of supporting volume the project would have no chance of approval by the [redacted] management board. This offer was made for a maximum of ten years but the location of the contract would have to migrate northwards following advance of the disease through Wales once the Llandovery volume had been worked out.

The overall result was that each bidder received an offer for at least the minimum contract volume that was on offer, although the areas of the offer had changed.

Currently larch that has been offered to the market by NRW and the private sector has been absorbed by the processors by substitution, by taking larch and not spruce or other species, but there is a limit to how much of this can be achieved with out damage to their businesses, as some of their customers will not accept larch in the finished products. There is a need to increase the overall processing capacity for larch and ensure that as much material as possible is going into value markets, fencing and garden products for example whilst the hope is that some will also go into the housing market.

3. Scope

Two of the three bidders are quite satisfied with the outcome of the tender, [redacted] have secured enough volume to continue their plans for a fuel pellet and CHP plant located in [redacted] [redacted] are confident of being able to harvest and market 130,000 m³ of larch per annum from Coed Y Cymoedd FD an area where they have a good track record for delivery with some extremely challenging sites completed under a winch LTC let four years ago, but at much lower annual volumes.

[redacted] were not content with the offer that was made to them, even though Llandovery FD is significantly closer to the mill at [redacted], both tree size and tree form in the Llandovery FD are superior to that offered in Coed Y

Cymoedd. The offer of 65,000m³obs standing should produce approximately 30,000 tonnes of mill material at 14cms plus.

We were aware that [redacted] needed a further supply guarantee of larch volume before committing increase the capacity at [redacted]. To assist in this [redacted] were also offered an under pinning volume from the proposed DP long term contract that will be centred in the western areas of Llandovery FD. The total offer was 55,000 tonnes of larch per annum from NRW, against a production capacity assumed to be between 100,000 and 110,000 tonnes per annum with the potential to increase even further if supply and markets can be found but we presume that calculations have been worked on a production volume of 100,000 tonnes per annum.

[redacted] have also indicated that investment at [redacted] will not take place unless they can be offered some surety on continuing supply of the spruce element for the mill. They are aware that spruce supply from Wales will be tight whilst the larch is being dealt with and are keen to secure as much volume as they can (reference Table 8). The current position is they have access to 64,000 tonnes of spruce sawlog material made up from:

Table 2
Current Long Term Contracts

Contract	Location	Roadside/Standing	Annual Volume M ³ obs .	Log /bar
L13790	Tywi Dyfi Hafren Sarnau	Roadside	41,000 obs logs 18cms+	33,000 m ³ ub
L12480	Tywi Hafren Sarnau	Roadside	12,400 obs bars 14cms – 18cms	10,000 m ³ ub
L12406	Vrnwy	Standing thin and clearfell	20,000m ³ obs	8,000 tonnes Log and Bar
L12407	Coed y Cymoedd	Standing harvester clearfell	30,000m ³ obs	13,000 tonnes Log and Bar
Total			103,400m ³ obs	64,000 units of sale m ³ ub/tonnes

[redacted] are looking for reassurance that this volume total will continue to be offered to the company in the form of Long Term Contract agreements.

4. Options for the Larch

4.1 [redacted] put in a counter offer to the NRW proposal, which offered the standing sales parcel in Llandovery of 65,000m³ obs and access to larch

logs produced by direct production to make up a volume of 55,000 tonnes to the sawmill, this would commit all DP larch production from Llandovery FD. The counter offer was that [redacted] would take the entire volume of log and bar off one of the [redacted] contracts based in CyC FD and become co owner of the contract, [redacted] would then work the parcel offered in Llandovery FD instead of [redacted]

There would then not be a substantial reliance on DP logs to make up the volume to 55,000 tonnes per annum. However their proposal would then commit [redacted] to harvesting 195,000m³obs per annum on the larch long term contracts. This poses substantial business risk to NRW in that;

- [redacted] trading with FCW has never exceeded 90k per annum and the average over the last 5 years is 67,000m³obs. We would be asking them to increase to over 200,000k in a very short time as they still have open market commitment and we would not want to loose them in that market.
- Reducing the presence of [redacted] in the market could also be counter productive; their annual trading for standing sales in Wales over the last 5 years has been 138,000m³ obs with a good mix of LTC and open market sales.
- [redacted] taking all the log and bar from one of the south Wales contracts plus material for the Llandovery contract may well cause supply problems for both [redacted] and [redacted] who were bid partners in the [redacted] offer as well as [redacted]

4.2 It is the preferred option for NRW that [redacted] allow [redacted] to harvest a co-owned LTC in Llandovery FD and that [redacted] purchase an element of log from [redacted] from the contracts they secured in South Wales, this volume could amount to 15,000 tonnes of log and bar per annum once the new saw line is running. The volume would be sourced from the more northerly forest areas in Coed y Cymoedd to reduce the transport costs but the exact location and volumes would be for [redacted] and [redacted] to agree upon. This scenario reduces the standing sale risk associated with expanding the [redacted] business too quickly and keeps [redacted] in place as a strong player in the Welsh market.

- It allows [redacted] to distribute the log material in South Wales with too much constraint keeping [redacted] and [redacted] Timber in the market as is their expectation after entering agreement with [redacted] for supply in the initial tender bid.

- Any volume commitment will cease after 5 years as the Coed y Cymoedd contract will have come to an end as all the larch will have been felled and market. This contract closure will allow further access for supply to the mill for the private sector that should be coming into the market with larger volumes by that time
- The commitment of NRW providing 55,000 tonnes of larch material for a period of five years to the development is maintained through three routes, 15,000 tonnes from in CYC, 30,000 tonnes from the standing contract in Llandovery and a balance of 10,000 tonnes from the Direct Production in western Llandovery FD.

However this volume alone will not be acceptable to as they will view the volume as a possible volume stream that may come to them should not have any other options for the material, it is unlikely that either party would enter into a contractual commitment to receive or supply. DP could offer to cover the volume that were to supply as well as the 10,000 tonnes that is mention above making the DP offer 25k tonnes per annum. Volume would be sourced from Llandovery FD initially but may also come from Coed y Mynydd and Coed y Gororau as the disease progresses north. Commitment could be offered over a 10 year period.

5. Why is this decision a priority?

We must try to ensure that the proposed development at goes ahead as it will provide a marketing solution to the sawlog element that will be coming forward from the potential seven million cubic metres of standing larch that will need to be felled in Wales and the Marches over the next 10 to 12 years.

Larch production is set to increase to 350,000m³ obs from the public estate in the next two years additional production capacity will be needed by then if we are to maximise revenue returns as current facilities would struggle to continue to absorb larch to this figure. Further private sector volume will also be coming on stream in this period.

This development will enable growers to maximise returns for material to 14cms top diameter and to a short length (2.45meters), currently there are no mills in Wales milling timber infected with Phytophthora Ramorum to 14cms TD. currently cut material to 16cms top diameter and will take a poorer quality than the standard green specification for sawlogs but have a very limited requirement minimum short length of 3.1metres.

The development will well placed in the centre of Wales to take material from all directions which will help in reducing overall timber haulage costs for the growers.

Alternative markets are chipwood or biofuel, higher carbon storage through production of milled timber will be achieved by supporting this development.

are a progressive company who will move this proposed development in to another if their production plants leaving site under invested and having to wait for the next cycle of updating which could be some years away.

6. Options for delivery of Spruce LTCs

The marketing plan and the sales plan will need to be heavily adjusted to accommodate the proposed larch volume during the coming years. The swing to larch will be absorbed mostly through a delivery by standing sales merchants using long term contracts. This will severely restrict what else can be marketed through the standing sales delivery method.

I. Do nothing - allow LTCs to expire and the wait until marketing strategy rewrite before any further opportunities given.

This would most likely convince that investing in the plant at this point of time would not be a good idea and they would focus further investment into other mills within the group leaving badly under invested and running on machines that are getting very dated. Some equipment is still in place from when the mill was commissioned in 1981.

However it would be fair to all those who did not gain access to long term contracts in the last rounds as the market would be invited to make fresh bids for the material they would have a chance to make a bid should they chose to. It would also conform to the current marketing strategy in keeping the LTC balance between 40% and 60% of the total volume offered in the sales plan and offering opportunities to the market when volume became available. This is in line to what the trade at large are expecting after the messages we have given them in the last few trade liaison meetings

II. Extend LTCs to all parties at current levels with reduction in open market short term sales:

On DP this would not too much of a hardship, we are committed to as out lined above, 8,333 tonnes of spruce log and 6,250 tonnes of spruce log per annum but it would be useful to refresh these contract as they expire as we looking to get synergy on sites with log and bar contracts going to one buyer.

Table 4
Other Standing Sale Long Term Contracts

Contract	Merchant	Annual Volume	Delivery
L12404		25,000m ³ obs	Clearfelling Winch work
L12408		17,500m ³ obs	Difficult to market material
L12410		10,000m ³ obs	Difficult to market material
L12405		31,000m ³ obs	Clearfelling Winch work
Total		83,500m ³ obs	

Table 5
Possible Standing LTC Commitment

Merchant	Annual Volume m ³ obs	Thin volume m ³ obs	Fell volume m ³ obs	Years to current completion date
old contracts	50,000	8,000	42,000	1 year
Proposed new larch Contracts	260,000		260,000	5 years
old contracts	42,500	10,000	32,500	1 year
	10,000	5,000	5,000	2 years
	31,000		31,000	2 years
Total	393,500	23,000	370,500	

Table 6
Annualised Programme

	Direct Production Non Larch	Direct Production Larch	Standing Sales Non Larch	Standing Sales Larch	Totals
Thinning	100,000		90,000		190,000
Felling	230,000	70,000	120,000	280,000	700,000
Fell Totals	300,000		400,000		
Totals	330,000	70,000	210,000	280,000	890,000
	400,000		490,000		890,000

Table 7
Total Annual Program 2013 to 2021 Thinning and Felling
(All quantities in units of 100k m³obs)

Forest Year	Thinning program	Fell spruce other conifer	Fell larch	Thin and fell
2013/14	215	495	150	860
2014/15	190	375	305	870
2015/16	190	380	327	897
2016/17	215	345	327	887
2017/18	230	315	335	880
2018/19	240	305	346	891
2019/20	245	315	330	890
2020/21	265	505	130	900

Table 8
Assumed Spruce in programme 2013 to 2021
(All figures 100k m³obs)

Forest Year	Thinning spruce (71%)	Fell spruce (85%)	Total spruce	Spruce log bar (40% thin 80% fell)
2013/14	152	351	503	341
2014/15	135	319	454	287
2015/16	135	323	458	270
2016/17	152	293	445	257
2017/18	163	268	431	244
2018/19	170	259	429	241
2019/20	174	268	442	248
2020/21	188	429	617	361

To extend the contracts in Table 4 would reduce our ability offer to open market to less than 100,000m³obs per annum from a programme of 490,000m³obs, of which 20,000 would be clear felling infected larch in south Wales and leaving no other clear fell to offer all to offer. The balance of any open market standing sales offers would be 76,500m³obs thinning This is going to have a dramatic effect on our open standing sales market customers, with
and left with very little opportunity to buy volume. Letting LTCs come to an end will put an additional 83,500m³obs into the market in 2015 and will ease the open position, although further opportunities for LTCs should then be offered to the market focused on thinning delivery from the standing sale sector.

By allowing these commitments to come to the natural end we could refocus our attention on delivering our standing sales thinning through long term contract agreements and build up resource to carry out this important part of the programme.

III. Extend LTCs to [redacted] alone with balance going to new LTCs through a competitive process and open market sales.

Extend the current LTCs held directly and in co ownership for supply of spruce wood by 5 years at full volume and for a further 5 years at a reducing annual volume so by year 15 they will be on 20% of the current volumes and all spruce contracts would be wound out the following year, 2024

Table 3
Proposed Spruce LTC Volumes

Supply Year	Annual DP Log	Annual DP Bar	Standing	Standing Log Bar	Total annual L+B supply
Current position carries to 2018	33,000	10,000	50,000	21,000	64,000
Position in 2019	33,000	10,000	50,000	21,000	64,000
Position in 2020	26,400	8,000	40,000	16,800	51,200
Position in 2021	19,800	6,000	30,000	12,600	38,400
Position in 2022	13,200	4,000	20,000	8,400	25,600
Position in 2023	6,600	2,000	10,000	4,200	12,800
Position in 2024	0	0	0	0	0

We recognise that there be a danger of seeming to favour [redacted] if only volume that was destined to their facility was granted a long term contract extension, having the effect of reducing opportunity for others in future sales.

Extension of the two standing LTCs will further reduce the volume we have to offer in this market and also reduce the amount of spruce available to other users. In mitigation of this likely impact it is likely that the private sector subject to price will gain additional entry and penetration into the market place which in terms of overall woodland management would be a positive consequence in the market place.

would be gaining market assurance but the benefit and need for the Larch disease solution must ride high in NRW's decision making given no one else has come forward through the tender process with a solution to the disease control challenge NRW faces on the WGME. It is unlikely that we would see an equally good proposal come forward if we went out to the market with this volume. Time is also of the essence failure to offer the LTC extensions could jeopardise the planned investment at

IV. Any other proposals

We could consider offering all our standing sale merchants a base volume in a long term contract agreement at maybe 50% of their historic trading levels. This offer would have to focus on delivery of the thinning programme. Giving some assurance that there would be some investment in thinning equipment, where it is currently required. Potentially the thinning volume could rise from the current annual figure of 190,000m³ obs to some where around 350,000m³ obs we have to point the market in this direction if they want continued supply of material. This would also help to maintain our fragile standing sales customer base which is dominated by three large players, and

We should not ignore the part the private sector should play in ensuring that this development goes ahead, NRW could facilitate a co operative approach from the private sector to guarantee a log supply to the sawmill. This will have the effect of increasing confidence for the board to sign off the investment proposals at | and guarantee that private growers have access to market at an assured price. Initial contact with growers in Wales has been positive although wary of making firm commitments.

7. Recommendations and decisions

It is essential that the proposed development at is secured for the good of the growers in Wales and the Marches as the new facility will substantially increase milling capacity for short length and small diameter logs in Wales where the only current high capacity is at

To deliver this development the company has requested that they have continued assurance for volume from NRW via retaining existing long term contract agreements for spruce and entering into further agreements for larch.

There is no easy decision or option here and we recognise that some parties will feel disadvantaged by whatever option we choose

However and as time is now of the essence we recommend option 3 in order to secure a prime objective of a disease management solution in the face of year on year growth of the Phytophthora ramorum disease spread across Wales

This will entail offering to the following in outline:

- NRW should agree to extend the current spruce supply contracts that equate to 64,000 tonnes of log bar material through both the standing and roadside methods of sale. NRW will have to decide which areas are best suited to deliver the contracts as the current commitment for 30,000 tonnes of standing harvester forwarder spruce wood in Coed Y Cymoedd forest district would be impossible to maintain whilst the larch contracts are being delivered in that area. Coed y Mynydd would seem a more likely option or splitting the volume between Llandovery FD and Coed Y Mynydd FD, to boost the production in the Tywi block. This volume should be offered in full for a further 5 years and wind out for further 5 years (as shown in Table 3)
- NRW should offer 65,000 m³ obs of standing larch in Llandovery FD to be worked by this offer could be extended to a 10 year offer and moved north as the disease progresses through out Wales. To allow to harvest all three larch LTCs would be high risk for NRW, by firstly expecting the company to double current trading within 12 months and secondly by weakening strongest competitor in the Welsh market. This contract should be offered in stages reaching full volume once the new facility is fully operational.
- NRW should offer to under pin the standing sales offer with direct production material to a maximum larch log and bar total from the public estate of 55,000 tonnes per annum, this could commit 25,000 tonnes of log bar production arising from larch felling work in the western forest blocks of Llandovery FD and any larch arising from sanitation felling in the northern forest districts. Full volume would not be offered until the new mill becomes fully operational. This commitment should reduce after five years by 5000 tonnes per annum. The released volume being offered on the open market.
- NRW should accept that may sell a share of the sawlog and bar volume derived from the contracts they have secured in Coed y Cymoedd FD, this will be decision to be made between the two parties involved.
- NRW should continue encouragement for a commitment from the private sector growers for supply to via some sort of long term co operative supply agreement. This volume could be vital in securing the investment required for increasing processing capacity to add value to diseased larch in Wales and the Marches.

- NRW should allow other Long Term Contracts to come their natural end so we can reposition our commitments and deliver future objectives, increased levels of thinning for example. retain their LTCs as they have committed to develop an important increase in capacity for small diameter short length log in Wales. Allowing contracts to end will release 67,000 m3 of standing timber and 15,000 m3 of spruce sawlog back to the market over the next 2 years.

8. Communications

Once the decision on which way we are to go with our marketing for the next few years and we have assurance on the levels of spruce, other conifer and larch in the programme we need to engage with individual customers, trade bodies and private sector growers and our own staff within WHaM and a wider audience. This can be achieved by;

- Holding a trade liaison meeting for our customers
- Arranging a series of one to one meetings with customers
- Holding meetings with trade bodies and growers representatives
- Updating the Web site to reflect the plan and the effects it will result.
- Updating the Marketing Strategy to reflect changes, spring 2014
- Ensuring that WHaM Staff are well briefed with the changes to programme and the marketing of the programme.

9. Assurance

10. Terms and Conditions of a future contracts

- Contracts must contain milestones for the investments that have been promised in both harvesting and processing capacity. Failure to carry out the required investments will be a serious breach of contract and will bring about termination if not rectified.
- Contracts must contain the harvesting and haulage price matrixes that will determine the costs for jobs that are to be negotiated. They must contain the offer prices and indicated volumes to each of the customers mentioned in the bid.
- Contracts must contain the pricing review matrixes that were submitted for each product and for the tracking and review of harvesting and haulage costs

- Contracts must contain the quoted figure for contract management and the profit element to be used in negotiation for timber parcels.
- Contracts must commit contract holders to install the correct levels of contract management and site supervision on or before commencement date.

11. Risk assessment

- NRW could be criticised for only extending the current long term contracts to the supply with spruce through their direct and co owned contracts, this can be managed and justified by securing the investment proposed for
- The loss of the development at will condemn at least 15% of the current larch crops in Wales and the Marches into lower value markets over the next 12 years. Some processors may chose to invest further in adding value or increasing capacity in larch but currently there are no other offers on the table.
- That rely wholly on NRW to back their investment plans which could alienate the private growers.
- That there will be very little spruce to offer standing sales merchants over the next five years and any increase is mostly likely going to have to come from long term contracts delivering the increasing thinning programme.

12. Benefits

By supporting the proposal we will ensure that

- A much needed development for maximising value of poorer quality larch timber is installed.
- Over capacity for processing larch is increased for the benefit of both public and private owners.
- The opportunity to penetrate the house building sector with wood grown in Wales is further improved.
- There will be stability in the market as the amount of larch infected by Phytophthora Ramorum increases as the disease spreads north and east through Wales and the Marches.
- The building of the new mill at will also create a value market for minor species in the longer term as the company will

increase input of other species once supply of larch material starts to reduce.

Appendix 1: Map of Forest Areas

Appendix 2: Map of current larch infection and Control Area



Long Term Timber Sales Contracts


INTERNAL AUDIT REPORT

May 2017

Distribution of Report (as agreed with clients)

Name	Title
Peter Garson	Head of Operational Services South
Ian Sachs	Head of Harvesting
Jerry Pritchard	Head of Marketing
Emyr Roberts	Chief Executive
	Audit & Risk Assurance Committee
	Wales Audit Office

Engagement Opinion

Opinion	RAG
<p>Moderate Some improvements are required to enhance the adequacy and effectiveness of the framework of governance, risk management and control. (For the range of opinions, see Annex C)</p>	Yellow 

EXECUTIVE SUMMARY

Based on our review we are able to give a **moderate** audit opinion. This rating means that some improvements are required to enhance the effectiveness of the framework of governance, risk management and control around the Long Term Sales Contracts.

NRW inherited the 2011-16 Timber Marketing Strategy from Forestry Commission Wales (FCW). One aim of the Strategy was focussed on developing and sustaining a strong timber supply chain in Wales and encourage value adding. A proportion of the programme was therefore allocated to Long Term Contracts that were designed to encourage companies bidding for them to invest into infrastructure to enhance the supply chain capacity within Wales. This resulted in contractual responsibilities which added extra requirements into the sales contract. Ultimately, this also increased the risk exposure from those contracts for NRW, (because the supply chain investments were beyond NRW's direct control).

Currently, one live contract remains, which was conditioned on the construction of a plant, financed by the company itself. We have been informed by the Head of Marketing that, at the time of letting the contract (by FCW), legal advice was sought to ensure the contract was legally compliant.

NRW also ring-fenced a small quantity of timber to be sold to specific customers, who therefore did not have to purchase it via a competitive sales process. These customers were in a receipt of a Wood Energy Business Scheme (WEBS) grant, which NRW did not want to see fail, but positively contribute to Welsh economy instead.

While we have not identified any significant issues with the existing contracts, NRW may wish to review its approach to long term timber sales, to ensure NRW is not building in unnecessary conditions into our sales contracts and all sales are conducted via a competitive process.

NRW's new 5 year Timber Marketing Plan, which came into effect on the 1st April 2017, reduces the proportion of timber sales through Long Term Contracts and indicates that where we do enter into new LTCs, their focus will be to achieve outcomes that are more directly related to the management of the forest such as increasing the amount of thinning.

A full description of all findings and recommendations can be found below.

BACKGROUND

Timber sales contracts are an essential source of income for NRW. In 2015/16 this amounted to £16.5m. In addition, harvesting timber is an essential part of our sustainable management of the Welsh Government Woodland Estate.

The recent Wales Audit Office (WAO) review of one of NRW's long-term timber contracts identified a number of shortcomings, whereby NRW were not able to provide evidence to support the decisions and actions taken in letting and awarding the contract and appropriateness of the agreed terms and conditions.

The purpose of this consultancy assignment was to assess and provide reasonable assurance to the Accounting Officer and management that appropriate and sufficient evidence exists to support the other current NRW long-term timber sale contracts and that the contracts were drafted and awarded in accordance with NRW policies procedures.

We reviewed the following:

- NRW's understanding of the current (at the time) market conditions for timber,
- The process of identifying the sales marketing options to optimise the outcomes,
- The documentation around marketing the sales,
- The oversight of the shortlisting and selection of the contractors,
- Controls around contract negotiations and contract award process,
- Management oversight, escalation and consultations on the sales process (i.e. what controls/processes existed to help to identify contentious, novel, repercussive or state aid issues).

Outside scope (What we didn't look at):

- We did not look at whether the contracts represent value for money.

The full Terms of Reference for this audit are included as Annex B.

EXPLANATION OF OPINION, KEY FINDINGS AND RISKS

Understanding of market conditions for timber and marketing the sales opportunities

NRW produces Long Term Production forecasts within which annual volumes of timber that can be released to the market are specified. In addition, the UK timber market is being monitored on capacity, imports, and prices. This review did not explore the work that contributed to the above knowledge of the market.

In relation to the existing long term contracts (where applicable), we reviewed the process for identifying timber for sales and presenting it to the market in such way that reflects market demand, capacity, capability and found it to be satisfactory.

NRW and FCW before it, as part of their long term Timber Marketing and Sales strategy, explicitly encouraged the bidders to invest in infrastructure and technology that would create and develop a strong Welsh timber market. This was used as one of the scoring criteria for evaluating bids. Consequently, FCW and NRW entered into some contracts which were conditioned on a construction of the agreed infrastructure. One of the current live contracts has this as a condition of sale. However, the company funded all costs associated with construction.

By entering into such contractual arrangements, NRW takes on a degree of risk by introducing complexity into the condition of sale. If the conditions of sale are not met, then potentially the contract would have to be terminated, additional costs incurred as a result of having to re-tendering the timber to market, cause financial loss to the supplier and reputational damage to NRW.

Shortlisting and selection of the companies

There are currently six live Long Term Timber Sales contracts. Regarding three of them that were awarded through an open market competition, we were satisfied that an appropriate marketing and tendering process took place, proportionate to the size of the sale.

The evaluation guidelines exist and the records of scoring tendering criteria appear to be consistent with the guidelines.

The other three current Long Term Contracts relate to a sale of timber to ring-fenced companies, which received a government grant to purchase machinery in order to establish a market for biomass in Wales. The sales were smaller (totalling approx. 48,000m³ timber to the value of £710k over a period of 5 years) and were made at market prices. These contracts were on a reducing sliding scale and will end in 2018.

The practice of ring-fencing, instead of competitive sale process, can expose NRW to risk of being accused of preferential treatment for some suppliers in the market. Going forward, this practice has been reviewed and will no longer be used, also the proportion of timber sold through long Term Contracts will be considerably reduced.

Contract negotiations and contract award process

We discussed with the Head of Marketing the process of reviewing tenders and selection of the successful bidder. Evidence for one of the contracts was reviewed and found to be sufficient.

We were assured by the Head of Marketing that there have been no significant changes between the terms and conditions advertised for the tendered contracts and what was subsequently awarded. However, we were unable to verify this as not all the information was not available.

Contract extensions and variations and management

The quantities and species of sold timber are regularly monitored and recorded against contracts. All contracts have a degree of variations between the quantities agreed to be harvested and the actual quantities - which are tolerated (both over and under the agreed

amounts). Overall, 25% variation is accepted on “child” contracts (which are sub parts of the full “parent” contract) but the overall volume of sales need not be affected by this. However, occasionally the overall quantity harvested differs substantially from the “parent” contracts (with no formal extensions in place).

No penalties are imposed in the events where the contract does not harvest the required amount.

The practices described above may have an impact on NRW’s ability to sell timber efficiently and competitively.

The practice of packaging purchase of services by NRW (e.g., clearance of low value timber) into a sales contract occurs on some Standing Sales Long Term Contracts. The practice of packaging purchase within a sales contract was reviewed by WAO last year and no recommendations were made. However, there is a risk that without the tendering for the service, as would be the case in a typical procurement process, the prices might not be competitive or market tested. Nevertheless, the Head of Marketing believes that the approach used secures best value for the reasons explained in Key Finding 4.

Management oversight

We have not reviewed how contracts are managed on a day to day basis, as this fell outside of the scope for this review.

We saw evidence of monitoring and dealing with performance against contract, specifically – haulage-related breaches and other Terms and Conditions.

The evidence of annual review of the contracts and performance against them is not always summarised on the contract files. There is a risk that, without this information, contract management may be less effective. However, the need for this regular appraisal has already been identified by the timber Marketing Manager who is putting measures in place to address this gap.

Long Term Timber Contracts Agreed Action Plan

The agreed actions have been categorised according to the level of importance we attach to them. They are defined as:

HIGH (H)	The action addresses critical weaknesses that would result in serious risks and/or an unacceptable level of risk to the delivery of objectives.
MEDIUM (M)	The action addresses control weaknesses that carry a risk of undesirable effects in loss, exposure, poor value for money or missed business opportunities and benefits in the context of the delivery of objectives.
LOW (L)	The action addresses minor control weaknesses and/or areas that would benefit from the introduction of improved working practices in the context of the delivery of objectives.

Key Finding 1	<p>FCW Sales Strategy, later adopted by NRW</p> <p>In response to one of the objectives in the Welsh Government’s Woodland Strategy, FCW aimed to help Wales to develop longer term capacity to process/utilise timber and timber products. The intention was to encourage investment in infrastructure which would create a permanent market within the region.</p> <p>This strategy was reflected in FCW approach to marketing and sales and consequently, in some of the sales contracts. This approach was continued by NRW, albeit that NRW has now developed the subsequent 5 year Timber Marketing plan.</p> <p>We identified one large (approx. £18m over 12 years) NRW long term timber sales contract which stated “this agreement is conditioned upon the execution of the construction contract”. The construction referred to the building of a wood fuel burning energy plant (financed entirely by the company itself).</p> <p>The contract was awarded in 2006 via a tendering exercise which attracted a high level of interest. Availability of and investment in infrastructure (capacity and technology) was one of the scoring criteria for this contract.</p> <p>Legal advice was sought on the construction of the contract to ensure it was legally compliant, however, copy of the advice has not been retained.</p>
Risk	<p>Introducing additional conditions within the sales contract adds to complexity of the transaction and loads the risk of the contract performance onto NRW. If the condition is not met, there is a risk that NRW can terminate the contract – which is likely to be detrimental to NRW as well as to the company.</p>

Agreed Actions:	Priority	Action owner:	Target date:
<p>1</p> <ul style="list-style-type: none"> • NRW has already implemented a new marketing plan which reduces the use of LTCs. We no longer use LTCs to encourage investments in the timber processing sector. • The lessons from this review will be adopted in NRW's future enterprises. <p>Additional comment: With reference to the specific LTC, the investment has taken place and therefore the risk to the contract is low.</p>	<p>M</p>	<p>Peter Garson, Head of Operations, South</p>	<p>Immediate</p>

<p>Key Finding 2</p>	<p>Ring-fencing timber for sales to specific buyers</p> <p>There are 3 small (totalling approx. 48,000m³ timber to the value of £710k over a period of 5 years) contracts that were awarded to companies without going through a competitive tendering and sales process.</p> <p>This was because NRW agreed to ring-fence a small quantity of timber (we have been told it was around 3% of available timber) for sale to companies that were successful in obtaining a Wood Energy Business Scheme (WEBS) grant for investment in timber processing machinery, but who needed security of supply in order to make the investment. FCW's intention was to help to ensure that these government-encouraged investments succeed.</p> <p>Two of the three contracts were with the same company. All 3 will end in within the next 2 years.</p> <p>We have been told by the Head of Marketing that the sale was at market value, (using open market values for equivalent timber.)</p> <p>No contracts of this sort have been awarded since then by NRW as the practice of ring fencing stopped when the WEBS grant scheme closed.</p>			
<p>Risk</p>	<p>Although the sale was at market rate, this could be construed as preferential treatment.</p>			
<p>Agreed Actions:</p>		<p>Priority</p>	<p>Action owner:</p>	<p>Target date:</p>
<p>2</p>	<ul style="list-style-type: none"> Practices of ring-fencing should not be re-introduced. The lessons from this review will be adopted in NRW's future enterprises. 	<p>M</p>	<p>Peter Garson, Head of Operations, South</p>	<p>Immediate</p>

<p>Key Finding 3</p>	<p>Dealing with under and over sales</p> <p>Long term contracts consist of an overarching “parent” contract and the sub-parts relating to specific coups – so called “child” contracts.</p> <p>We note that each “child” contract has some variations between the quantities offered for sale and actuals. Generally, 25% variance on the “child” contract is accepted, but we identified that occasionally there are larger variances. These variations can be - over and above agreed sales, below that quantity, or no timber was collected at all.</p> <p>On LTCs, the variances on the individual “child” contract are monitored and subsequent coups adjusted. It is expected that, cumulatively, this would prevent large variances at the overall “parent” contract level. However this is not always the case. We noted that one contract is forecasted to achieve a lower sales volume (29% under) and one higher (20% over).</p> <p>In the event where the total quantity significantly exceeds that which was agreed, there were no formally agreed contract extensions or variations (with 2 minor exceptions).</p> <p>There could be variety of genuine reasons why the company could not collect timber. Where the timber remains unsold it is offered back to the market, unless there is a good reason why it is not appropriate (such as protected species nesting).</p>			
<p>Risk</p>	<p>If the actual amount sold significantly exceeds the one the company tendered for, then this might be seen as a way of securing extra sale without having to compete for it in an open market.</p> <p>When the contractor fails to collect the timber there is a risk that NRW might be financially disadvantaged, if there are costs associated with re-presenting timber back to the market.</p>			
<p>Agreed Actions:</p>		<p>Priority</p>	<p>Action owner:</p>	<p>Target date:</p>
<p>3</p>	<p>Ensure that the variations on “child” contracts are managed to minimise the cumulative effect on the “parent” contract level.</p>	<p>L</p>	<p>Ian Sachs, Head of Sales and Marketing</p>	<p>30 April 2017</p>

<p>Key Finding 4</p>	<p>Packaging up purchase of service into sales contract</p> <p>Where there is a big variation in the value of products, it is common to set different prices for each product within the LTC sale. Sometimes the lowest price products can have a “negative value”. This means that the company that has purchased timber (and carries out harvesting itself), is also harvesting other - not valuable - materials at the same time.</p> <p>The “negative value” occurs when the harvesting costs exceed the value of the product. Effectively, NRW pays the contract-holder to remove these products. The “negative value” products typically comprise at least 20% of the crop (mainly tips and dead-wood).</p> <p>NRW provides an incentive to the contract holder to remove all products, rather than just remove the higher value products and leave an excessive to clear amount of waste timber on site (where it would make replanting hazardous and expensive.)</p> <p>It is regarded by the management as impracticable and very expensive to remove the low value products as a separate operation. In addition, this clearing process is important in maintaining a clean and healthy estate.</p> <p>As the price for each product relies on a negotiation of working costs, it is difficult to demonstrate “market testing” of this, albeit the Sales Team have considerable experience of working costs and timber values from open market sales.</p> <p>The approximate value of the “negative sales” is £100k per annum, which represents around 15% of the value of the LTCs involved.</p> <p>Recent WAO review of another long term timber contract which included “negative sales” did not raise this as an issue.</p> <p>Finally, the Operations Business Systems Manager said that she was satisfied that the risk of company clearing valuable timber and charging for “negative value” products is being well managed through NRW’s timber security controls. This assertion was noted but not tested, as outside the scope for this review.</p>			
<p>Risk</p>	<p>There is a risk that NRW may not be paying a competitive rate to clear the low value materials.</p>			
<p>Agreed Actions:</p>		<p>Priority</p>	<p>Action owner:</p>	<p>Target date:</p>
<p>4</p>	<p>Review the “negative sales” periodically, or as part of contract reviews, to confirm that negotiated prices reflect market value.</p>	<p>L</p>	<p>Ian Sachs, Head of Sales and Marketing</p>	<p>30 April 2017</p>

<p>Key Finding 5</p>	<p>Maintaining information</p> <p>In order to provide good continuity of service, various information about day-to-day performance of contracts needs to be brought together and documented.</p> <p>This information currently exists in numerous forms (paper/electronic or personal knowledge) and locations.</p> <p>In particular, annual summary of contract performance, including any contract breaches and H&S infringements, needs to be documented to demonstrate that contract is performing well. Although we have been informed that this information is considered when contracts are being reviewed, this isn't clearly evidenced.</p> <p>In addition, some of the reports and management information relating to contracts are not dated, it can be unclear who produced them (NRW or the company) and lack context.</p>			
<p>Risk</p>	<p>Incomplete management information may impact on NRW's ability to assess contracts effectively and may lead to sub-optimal decisions (e.g. granting an extension where contract is underperforming).</p>			
<p>Agreed Actions:</p>		<p>Priority</p>	<p>Action owner:</p>	<p>Target date:</p>
<p>5</p>	<ul style="list-style-type: none"> Document each contact performance and carry out a formal annual review of each of them. Ensure that the management information is dated, the author is known and the context (i.e. in header/title) is apparent. 	<p>L</p>	<p>Ian Sachs, Head of Sales and Marketing</p>	<p>30 April 2017</p>

LIMITATIONS

We have prepared this report solely for the use of the Natural Resources Wales and its Accounting Officer following an audit conducted at a point in time and it was not written for any other purpose. Therefore, we take no responsibility for any reliance that a third party (i.e. other than the Natural Resources Wales) may place on it. Where this report has been made available to a third party, it is on the understanding that the third party will use the report only for the purpose agreed and will not distribute it or any of the information contained in it outside of the third party.

Agreed Terms of Reference

INTERNAL AUDIT ENGAGEMENT - TERMS OF REFERENCE

Long Term Timber contracts – Terms of Reference**Background**

The recent Wales Audit Office (WAO) review of one of NRW's long-term timber contract identified a number of shortcomings, whereby NRW weren't able to provide evidence to support the decisions and actions taken in letting and awarding the contract and appropriateness of the agreed terms and conditions.

Review Objective – Purpose

The purpose of this assignment is to assess and provide reasonable assurance to the Accounting Officer and management that appropriate and sufficient evidence exists to support the other NRW long-term timber sale contracts and that the contracts were drafted and awarded in accordance with NRW policies procedures. In addition, we will review whether an audit trail of decision-making process exists.

Business Objectives (of Activity)

Timber sales contract are an essential source of income for NRW. In 2015/16 this amounted to £16.5m. In addition, harvesting timber is an essential part of our management of the Welsh Government Woodland Estate.

Review Scope (What we look at)

We will examine long term timber sales contracts and evidence to support decisions made that led to letting/awarding the contracts.

We will look at:

- NRW understanding of the current (at the time) market conditions for timber,
- The process of identifying the sales marketing options to optimise the outcomes,
- The documentation around marketing the sales
- The oversight of the shortlisting and selection of the contractors,
- Controls around contract negotiations and contract award process,
- Management oversight, escalation and consultations on the sales process (i.e. what controls/processes existed to help to identify contentious, novel, repercussive or state aid issues).

Outside scope (What we won't look at)

- We will not look at whether the contracts represented value for money.

Business Risks (Factors which would impact on the achievement of the activity objectives)

- If NRW cannot demonstrate that the contracts have been let following a competitive process, then we can be exposed to the risk of challenge from WAO, Welsh Government or the market.

- If we are unable to demonstrate that we have safeguarded NRW against the risk of state aid or that we have given adequate consideration to issues that can be seen as novel, contentious or repercussive, we might be challenged on validity and probity of our decision making.

Audit approach (How we will do it)

As with all of our audit work, we will adopt a risk-based approach where possible. Files, records and other forms of evidence will be examined, both manual and electronic, and relevant staff will be interviewed to identify and assess risks, document systems and evaluate controls.

By reference to documentation and consultation with staff we will determine what controls have been established to help ensure that risks are managed appropriately. We will then assess both the adequacy of the design and the effectiveness of these controls.

Following our initial evaluation, appropriate testing will be undertaken as considered necessary to establish the adequacy of management controls and whether they have been implemented an embedded effectively across the organisation.

Any emerging thoughts will be discussed with management during the audit. At the end of fieldwork, an exit meeting will be held to present our findings, confirm factual accuracy and agree corrective actions. Following this meeting, a draft report will be issued for final comments prior to issuing the final report.

Contacts

Assignment Sponsor	Emyr Roberts, Chief Executive
Assignment contacts	Peter Garson – Head of Operational Service South Jerry Pritchard – Head of Marketing Ian Sachs - Head of Harvesting Claire Evans - Harvesting Team -Operational Business Systems Manager
Report Distribution (to be confirmed)	Emyr Roberts - Chief Executive Peter Garson – Head of Operational Service South Kevin Ingram – Executive Director for Finance and Corporate Services David Cavell – Head of Legal Members of the Audit and Risk Assurance Committee Wales Audit Office




Proposed timetable of events is (provisional dates)*

Draft report date	April 2017
Response from Management	April 2017
Final report	May 2017

*: Dates are indicative. The planning, scope, approach and timetable for this audit may change in the light of preliminary findings. We will advise you of any significant changes to the timetable.

Agreed by Audit	Dorota Lee, IA Manager (HIA)	Date: 10/03/2017
Agreed by Audit client	Emyr Roberts, Chief Executive	Date: 10/03/ 2017

Overall Opinion Key

Coverage	Core Definitions for Annual and Engagement Opinions	Optional RAG	Factors influencing choice of opinion
Governance, risk management and control framework Assurance Opinion on mitigating controls over the risk to the delivery of objectives	Substantial The framework of governance, risk management and control is adequate and effective.	Green 	<ul style="list-style-type: none"> • Adequacy and Effectiveness of the governance, risk management and control framework • Impact of any weakness on delivery of objectives • Extent of risk exposure • Materiality: by value to the entity, by value in the engagement context and by nature (e.g. irregularity and reputational risk) • We may also take account of Management responses to recommendations/ management actions
	Moderate Some improvements are required to enhance the adequacy and effectiveness of the framework of governance, risk management and control.	Yellow 	
	Limited There are significant weaknesses in the framework of governance, risk management and control such that it could be or could become inadequate and ineffective.	Amber 	
	Unsatisfactory There are fundamental weaknesses in the framework of governance, risk management and control such that it is inadequate and ineffective or is likely to fail.	Red 