

Agenda – Public Accounts Committee

Meeting Venue:

Committee Room 3 – Senedd

Meeting date: 24 September 2018

Meeting time: 14.45

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(Pre-meeting)

(14.45 – 15.15)

1 Introductions, apologies, substitutions and declarations of interest

(15.15)

2 Natural Resources Wales: Scrutiny of Annual Report and Accounts 2017–18

(15.15 – 16.45)

(Pages 1 – 190)

Research Briefing

PAC(5)–24–18 Paper 1 – Natural Resources Wales Annual Report and Accounts 2017–18

PAC(5)–24–18 Paper 2 – Supplementary Memorandum of the Auditor General for Wales to the Public Accounts Committee: Timber Sales Contracts awarded by Natural Resources Wales

PAC(5)–24–18 Paper 3 – Natural Resources Wales Response to Annual Report and Accounts 2015/16: Updated action plan

Clare Pillman – Chief Executive, Natural Resources Wales

Kevin Ingram, Executive Director for Finance and Corporate Services, Natural Resources Wales

Peter Garson, Head of Commercial Operations, Natural Resources Wales



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Wales

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

(16.45)

Item 5 and Items 1 & 2 of the meeting on 1 October 2018

4 Natural Resources Wales: – Consideration of the evidence received

(16.45 – 17.15)

Document is Restricted



Annual Report and Accounts 2017/18



Noddir gan
Lywodraeth Cymru
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Chair's foreword

Welcome to our Annual Report for 2017/18. Here we have tried to capture some of the fantastic achievements of our dedicated staff at Natural Resources Wales (NRW): indeed, there is much for us to be proud of.

First and foremost, I want to thank all our people for what they have helped us deliver for the environment and for Wales. Their commitment, at a time when things have changed so much for them, is something that the Board and I value enormously.

During the first five years, we put a strong foundation in place for us to build on for the future. This formative phase was led by Dr Emyr Roberts and we thank him for this. I also want to express my gratitude to Kevin Ingram, who acted as our interim Chief Executive Officer, as we recruited a new Chief Executive, Clare Pillman, who we welcomed to Natural Resources Wales in early 2018.

In the few months that Clare has been in the role she has very quickly seen the potential within Natural Resources Wales, and the opportunities and challenges that need to be addressed to reach that potential: opportunities for integrated land management, renewable energy production and for the natural environment and its sustainable management to be fully recognised for the benefits it provides for people in Wales, and challenges in making ecosystems more resilient, tackling diffuse and agricultural pollution and supporting our staff through organisational change. I believe that we are already seeing a positive impact which will take us forward to achieve our ambitious Corporate Plan to 2022.

However, there have been challenges which need to be fully recognised in this Annual Report. I am deeply disappointed and concerned by the continuation of governance issues around the letting of timber sales contracts. The Board and I will entirely accept the Auditor General's findings and we are fully committed to ensuring these are urgently addressed. This is one of the top priorities for us and for our new Chief Executive who is already taking action to address these issues.

I believe that under Clare's leadership Natural Resources Wales can become a better place for our people to work, and that they, together with our partners, will endeavour to improve the state of our natural resources. As we all recognise, the environment that we care so much about faces grave challenges and pressures. But by looking after it and protecting those natural resources that underpin our health and well-being, we can play our part in helping create a better place now, and for future generations of the people of Wales.

Diane McCrea MBE
Chair

Performance Report

Overview

Over the following pages we offer our Chief Executive's perspective of our performance this year and outline the purpose of our organisation, our main roles and responsibilities as well as explaining how we have managed delivery of our objectives this year.

Chief Executive's statement

It is with great pride that I introduce my first Annual Report for Natural Resources Wales.

Since joining Natural Resources Wales I have felt extremely fortunate to meet and spend time with my new team and learn about the work they care about so much. They are extremely committed, knowledgeable and passionate about Wales; its environment, its communities and its wellbeing. In such a short amount of time I have found an organisation that has such potential. There are opportunities we need to explore and challenges we must face – but I am committed to making Natural Resources Wales an organisation that our staff, and Wales, can be proud of.

From the feedback I have had from staff I know there is a lot of work needed to achieve that. This is fuelled by their ambition for Natural Resources Wales to be the kind of organisation they believe it can be. This ambition is something I share with them and, together, we can change things for the better.

The depth of feeling our staff have for the environment is shared by the people of Wales – and rightly so. This can be seen from the upsurge in support to tackle the issue of plastics in our seas to more local concerns about trees being felled, pollution in our rivers or industrial facilities being built close to where they live. This presents us with both opportunity and a challenge to better explain what we do, why we do it and how it affects them.

There are also more pressing challenges for me within this report. Clearly we have not got everything right. I have been very concerned about our governance around timber contracts and our UK Woodland Assurance Standard (UKWAS) audit for 2017. It is my priority to work with our Board and our staff to ensure that we learn the lessons from these and that they do not happen again. Annual reports give us an opportunity to look back and identify those things we need to improve, but also to feel proud of what we have achieved and spur us on to greater things.

The fact that our staff care so much about their work, and the environment and communities they protect, is an incredible foundation to build on. We have new laws which recognise that the environment is fundamentally important to Wales – to its wellbeing, its wildlife and its economic prosperity.

I feel privileged to be a part of this organisation and to build for the future. We are here to champion the environment, to protect it and make sure that it can play its part in a better future for Wales.

Clare Pillman
Chief Executive and Accounting Officer

Date 13 July 2018

We are a Welsh Government Sponsored Body. Our purpose is to pursue the sustainable management of natural resources (SMNR) and apply the SMNR principles as set out in the [Environment \(Wales\) Act 2016](#) Wales is the first country in the world to create a single organisation that brings together many of the tools needed to help manage our natural resources coherently and in an integrated way.

Our roles and responsibilities include:

Adviser to the Welsh Government and to industry, land owners/managers, the wider public and voluntary sector

Regulator of industry and waste sites, and marine, forest and Designated Sites for example, protecting people and the natural environment

Designator for Sites of Special Scientific Interest (SSSIs), Areas of Outstanding Natural Beauty (AONBs) and National Parks and declaring National Nature Reserves (NNRs)

Responder to about 9,000 reported environmental incidents a year as a Category 1 emergency responder

Statutory consultee on about 9,000 planning applications a year

Manager of 7% of Wales' land area, including the Welsh Government Woodland Estate, National Nature Reserves and flood defences and running recreation facilities and a laboratory

Partner, educator and enabler, supporting and facilitating other organisations' work and helping people learn in and about the natural environment

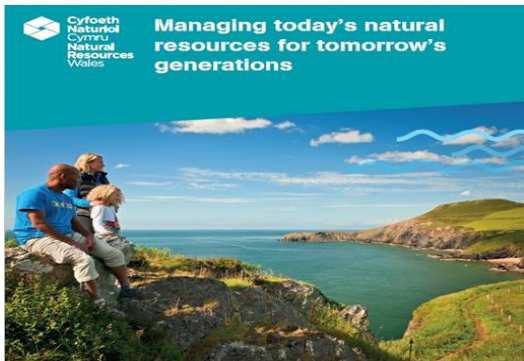
Evidence gatherer monitoring the environment, commissioning and undertaking research, developing and sharing knowledge and holding public records

Employer of approximately 1,900 staff as well as contractors and volunteers

In undertaking our work, we must also maximise our contribution to the seven Well-being Goals set out in the Well-being of Future Generations (Wales) Act 2015 [Well-being of Future Generations \(Wales\) Act 2015](#) and its five ways of working.

In common with the other public bodies in Wales, we have developed a set of Well-being Objectives to help us do this.

Introduced in our [Well-being Statement](#) in 2017 and reviewed as we developed this into our [Corporate Plan to 2022](#), these are our highest level, long-term organisational objectives for NRW, and were developed with both staff and stakeholders. Further details of our Well-being Objectives are available in our Corporate Plan.



We published our Corporate Plan to 2022 in March 2018. It was launched at the Senedd by our Chair Diane McCrea and new Chief Executive Clare Pillman, sponsored by Mike Hedges AM, Chair of Climate Change, Environment and Rural Affairs Committee. [Staff Videos](#) illustrated some of our work and Lawrence Conway, Sport Wales' Chair, highlighted the importance of our collaborative working both now and in the future.

There are several key areas that we recognise as **risks and issues** to manage in order to ensure delivery of our work:

- **Well-being, health and safety of our staff:** due to the varied and complex nature of our operational work, this is an ongoing risk, affecting both staff and others that work for us as well as achievement of our Well-being Objectives. We provide training and support for staff and we need to ensure this is continually improved. We know that low staff morale and the desire for a period of stability are important issues we need to address. Although the implementation of our Organisation Design project to restructure NRW in 2018/19 will involve further disruption in the short term, the new structure, based around local teams, will both provide more stability and help us work in the way recent Welsh legislation intends.
- **Internal governance:** particularly in relation to sales and contract management. We have increased our focus on our internal governance to both protect our resources and ensure value for money for the Welsh taxpayer.
- **Withdrawal from the European Union:** much of our work is governed by legislation from the European Union. We are following developments in Brexit negotiations closely as we are aware that their outcome could have a significant impact on our core activities and potential sources of external funding. We have a key role in Welsh Government advisory groups relating to the environment and will play a full part as actions are required to be taken in response to Westminster decisions.
- **Our annual financial settlement:** the short-term nature of our financial position brings uncertainty to our commitment to longer term plans and projects. We need to be prudent in our future assumptions, and, in the challenge of continuing public sector austerity, work closely with Welsh Government to establish and manage our financial position.
- **Cyber security:** we recognise that our cloud-based information and communications technology (ICT) system is vulnerable. We continually assess our protection to ensure it is proportionate to the likelihood and scale of threat we face. We continue to develop and improve staff training and awareness to promote a culture of diligence when using ICT equipment and services which help us to manage resultant risks.

Performance summary

We look after Wales' natural resources and what they provide for us – ensuring that the land and water we look after directly is sustainably managed and encouraging and supporting others to do the same: as our first Well-being Objective states – to champion the Welsh natural environment and the sustainable management of Wales' natural resources.

The Well-being of Future Generations (Wales) Act 2015 and the Environment (Wales) Act 2016 have given us a real opportunity to revolutionise the way we manage the natural environment in Wales and make the sustainable management of our natural resources a reality.

We are focussing on transforming our organisation to deliver more effectively, changing our structures and ways of working and ensuring we apply the SMNR principles to everything we do - for the benefit of Wales now and in the future. We still have change to come, as 2018/19 sees us implement our Organisation Design project which will restructure our organisation to help us provide more local services, integrated with those of other public bodies and partners.

Throughout these changes we have been continuing to deliver our core activities: managing forests and nature reserves; responding to flooding and pollution incidents; building and maintaining flood alleviation schemes and supporting communities through flood awareness work; protecting and promoting the resilience of ecosystems; providing advice and guidance to developers and land managers; issuing permits, licences and consents and ensuring compliance with their conditions, encouraging businesses to operate sustainably; developing renewable energy schemes; and providing and collating scientific evidence.

We have a wide range of significant achievements for 2017/18 - working in partnership with many organisations. The official opening of Pen y Cymoedd wind farm, at the head of Rhondda and Neath valleys; the instigation of our EU-LIFE funded Raised Bogs project, protecting and restoring this valuable habitat and carbon store; award winning work on collaboration with Wales' archaeological trusts and in establishing a nature reserve adjacent to a housing development in Buckley, North East Wales, as well as innovative work tackling metal mine pollution and work with the Wales Land Management Forum to trial new approaches to diffuse and agricultural pollution. We are leading the way in the ambition for the Welsh Government to be carbon neutral by 2030 through our Carbon Positive project. We are also proud of our input to all the Public Services Boards across Wales as one of their statutory members, showing how the natural environment can contribute to dealing with a wide range of local issues – from community safety and access to obesity and mental health. You can read about some examples of our work in the following pages.

We often have difficult and contentious issues to deal with: it's the very nature of our work. Barry biomass plant, our flood scheme at Roath in Cardiff and proposals for the M4 corridor around Newport, for example, are complex, emotive issues, where we need to balance legislative requirements with stakeholders' wishes and base our decisions and recommendations on the best evidence available.

In cases such as these, there are often very strong opinions on all sides and our decisions will not please everyone. We are an evidence-based organisation, working within a strict and complex regulatory regime and legislation which is not always easily understood. We are very keen to learn how we can work better with our customers and the general public in future, particularly for those high public interest sites, where explaining the rationale behind our decisions and recommendations is especially important.

Looking ahead, we will face further challenges, both in our core activities and as we re-organise and put our new organisational structure in place. We know we need to ensure ecosystems are resilient enough to continue providing the benefits and services we need. We also need to encourage business to adopt the highest social, cultural and environmental standards, delivering green growth and making Wales competitive, successful and sustainable. Leading by example, applying the SMNR principles and encouraging others to do so, as well as using the five ways of working will help us realise our purpose and, with our partners, move towards achieving our Well-being Objectives.

Performance Analysis

Our performance analysis describes how we design and scrutinise our performance framework; provides information on our key measures and targets, and more detailed examples of how we are working towards achieving our Well-being Objectives.

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 key duties are set through both a long-term outcome approach (our Well-being Objectives) and an annual Remit Letter to determine areas of our work that require a particular focus. These are incorporated into our Corporate Plan and annual Business Plan.

Our performance framework will develop over future years to demonstrate progress towards meeting our Well-being Objectives, share how we are using the nine SMNR principles in our work and describe how we will address priorities from Welsh Government's Natural Resources Policy and Public Services Boards' Well-being Objectives.

Of the 34 measures on our Business Plan dashboard:

22 met the target set

9 were within 10% of the target set

2 were not where we wanted them to be

One was not assessed

Our Progress is monitored by our Board and Welsh Government and published on our website three times each year. From 2018/19 our performance will be available on a quarterly basis.

The following pages of this report outline examples of how we are working to deliver our Well-being Objectives as well as our key performance information this year. They also demonstrate how we are working towards putting the sustainable management of natural resources at the heart of everything we do.

Each chapter covers a different Well-being Objective: it includes what our role is, what measures we use to know if we are meeting our targets and how we have performed in the last year.

We have also included case studies at the end of each section that help bring our work to life – often of course, these contribute to more than one of our Well-being Objectives. They also help illustrate our commitment to the five ways of working and our contribution to the seven Well-being Goals.

Well-being Objective 1 – Champion the Welsh environment and the sustainable management of natural resources (SMNR)

We aim to champion the natural environment in everything we do – in the information we provide, in supporting Public Services Boards and in putting the sustainable management of natural resources into practice across all our work – to help people make the most of the benefits it offers as well as valuing it for its own sake now and for future generations.

Our measures

- Complete Area Statements by December 2019
- Provide environmental expertise at Public Services Boards (PSBs)
- Embed SMNR through organisational change
- Meet our 5% carbon reduction target and complete our Carbon Positive Project
- Create 230 hectares of habitat by March 2018

2017/18 results

- We have identified 'Initial Areas of Focus' for our Area Statements based on the priorities in the Natural Resources Policy and working closely with stakeholders
- We have and continue to provide environmental expertise at PSBs ensuring the evidence and data we provide meets their needs
- We have trained over 500 staff giving them a foundation level understanding of SMNR and encouraging them to apply its principles to their day to day work. More training will take place in 2018/19
- We are on track to meet our carbon emission target based on our latest data available and our carbon positive project will continue into 2018/19
- We have not achieved our target to create 230 hectares of habitat by March 2018. Intended to be through peatland restoration, the relevant schemes unfortunately did not receive the required funding. However, we have taken the opportunity to undertake a detailed review of our habitat creation plans. Our Business Plan for 2018/19 includes how we will be working to improve biodiversity and ecosystem resilience by restoring, creating and improving the condition of habitats.

Examples of our work over 2017/18:

Developing Area Statements

We are co-producing seven Area Statements as a requirement of the Environment (Wales) 2016 Act, working with a wide range of stakeholders. They cover six geographical areas across Wales and the marine environment. Providing an evidence base for PSBs and others the Area Statements will help identify opportunities and challenges where the local natural environment can help address a wide range of issues or prevent them from worsening or happening in the first place.

Area Statements will help PSB members and others to consider the long term, focus on prevention and identify opportunities to collaborate and integrate their work, involving others such as the local communities the PSBs serve, as well as seeing the natural environment as 'part of the solution'.

National bodies sharing group

We are part of a national bodies sharing group - a group of public bodies working together at a national level with the Future Generations Commissioner's Office to share learning about the practical application of the Well-being of Future Generations (Wales) Act 2015. We look at how we can measure progress and demonstrate we are using the five ways of working; how we can collaborate and integrate our work, involving others; develop shared Well-being Objectives in the future where appropriate and how we can work together over the long term, preventing current issues becoming worse. Partners include Public Health Wales, Sports Wales, National Museum Wales, Higher Education Funding Council for Wales and the Welsh Government.

Landscape Institute Award for Nature Reserve shows how the natural environment can provide a wide range of benefits

A joint project with The Environment Partnership, Redrow Homes, Flintshire County Council and North East Wales Wildlife Trust to reclaim land to create a new wetland habitat has won a Landscape Institute award. The project has created a nature reserve in Buckley, north Wales as part of a major housing development.

The Heathlands Project involved creating a new wetland habitat from reclaimed land within and adjacent to the Deeside and Buckley Newt Sites Special Area of Conservation (SAC) alongside 300 new family homes.



The land was originally an abandoned claypit with an unsafe steep-sided lagoon. This lagoon had to be filled in to create open space for the new properties and over 50 ponds were also created as part of the new habitat.

Over 35,000 amphibians were relocated as part of the scheme and the new ponds will support a wide range of species in the area including the great crested newt. Not only will the new wetlands provide a place for wildlife, but also provide sustainable drainage for the planned housing estate as well as many hectares of public space.

The development will have a long-term management and monitoring plan to ensure the ecological success of the regeneration with part of the land being designated as a Site of Special Scientific Interest (SSSI) and Special Area of Conservation (SAC).

Well-being Objective 2 – Ensure land and water in Wales is managed sustainably and in an integrated way

A fully integrated approach to the sustainable management of land and water in Wales can reap multiple benefits across all sectors – farming, forestry, fisheries and the urban environment. However, this is not happening yet. We aim to put this approach into practice on the land and water we manage ourselves and encourage all land and water managers to adopt an SMNR approach.

Our measures

- Be bold and innovative using our new experimental powers to try new approaches
- Complete 100% of our bathing water quality checks
- Enable implementation of our Wales National Marine Plan, embedding SMNR in our processes
- Re-stock 1,000 hectares woodland by March 2018
- Advise water companies on their long-term plans by March 2018
- Determine 90% of permit applications within agreed timescales and continue to improve the permitting process

2017/18 results

- We are making good progress on our green marketplace project, including investigation into a potential trading platform for service providers
- We completed all our statutory bathing water samples for all 104 designated sites
- We continue to work on the Wales National Marine Plan with an expectation that this will be adopted in 2019
- Although we achieved our woodland restocking target, by re-stocking 1,250 hectares, almost half of which were areas felled due to infection from *Phytophthora ramorum*, unfortunately our land bank area is above target making us amber for this measure
- Water companies submitted their draft 25-year plans to Welsh Government in December 2017. We continue to work closely with water companies to help them meet their statutory environmental requirements and publish final plans in autumn 2018.
- We determined 96% of permit applications within agreed timescales

Examples of our work over 2017/18:

Living Levels Project secures Lottery funding

As we reported last year, the Living Levels Landscape Partnership (LLLP) aims to recapture, enhance and celebrate the Gwent Levels by reconnecting people to this unique place. A programme of 26 interconnected projects seeks to conserve and restore the natural heritage of important features of the area, to develop a far greater appreciation of the value of the landscape through improving interpretation, promotion and access and to inspire people to learn about and participate in the heritage of the Gwent Levels.

The Partnership is led by RSPB and we are a core partner, leading on two projects to tackle invasive species and fly tipping, and are contributing to many others, including a £500,000 project that will restore SSSI ditch habitats. At the end of 2017, after an 18-month development phase, the LLLP was awarded a £2.5 million grant from the Heritage

Lottery Fund which will help secure nearly £4 million funding in total. The delivery phase formally began in February 2018 and the scheme will be delivered over the next three and a half years.

Sustainable water catchment management and collaborative working in Bridgend

In collaboration with a number of organisations and communities (including Bridgend County Borough Council, local councillors, Garw Valley Community Council, Sustrans, Garw Valley Railway Society, Bryngarw Country Park, Keep Wales Tidy and Groundwork) we are promoting sustainable water catchment management in the Garw Valley in Bridgend.

Our coordination of actions to maintain, restore and create priority wetland habitat, will help to slow surface water run-off. This will help reduce flood peaks and minimise sediment running into the watercourse making the management of this water catchment sustainable in the long term. We have also helped to develop a local working group who help manage a community pathway along the valley corridor. Through this group we also aim to involve local communities and schools in management of the path, increasing the value of the route for recreation and as a wildlife corridor, and improving connectivity (for both biodiversity and people) along the valley. By working with local communities and organisations, we hope to prevent poor/unsustainable management practices and anti-social behaviour. In the long term we hope to promote the route more widely as a heritage trail and community project.

Spirit of Llynfi Woodland Project



The Spirit of Llynfi is a community woodland project developed on the former Coegnant Colliery site. It had already been identified as a prime location for new woodland planting and in 2014 we successfully applied for funding from the Welsh Government Nature Fund to transform it into a community woodland and manage the land in a different way, yielding a wide range of benefits.

At the same time the Upper Llynfi Valley was identified as one of the most health deprived areas in Wales by the NHS. When we began the project we consulted extensively with local people to ensure the woodland reflected the needs of the community.

Between November 2015 and March 2016, 60,000 trees were planted on the site including 7,500 planted by local schools and community volunteers. They included a wide range of native broadleaved species together with orchard fruit trees. The aim was to increase the biodiversity of the site as well as creating an attractive backdrop to the valley.

The site has continued to flourish with a wide range of new projects, often taken forward by the Llynfi Woodland Group - local people with a passion for their environment.

Well-being Objective 3 – Improve resilience and quality of our ecosystems

Our State of Natural Resources Report (SoNaRR) 2016 has identified that many ecosystems will not be adaptable enough to deal with climate change and other pressures in future and so may not be able to provide the services we need – such as clean air and water. We designate special sites such as National Nature Reserves and SSSIs, for example – but our work is much broader than this - we aim to take biodiversity and ecosystem resilience into account in all our functions, activities and decisions and help other public bodies do the same.

Our measures

- Provide expert input into Public Services Boards' (PSBs') Well-being Plans
- Develop a strategic approach setting out how we will work and collaborate to help deliver the Nature Recovery Action Plan
- 80% of actions on designated sites are complete or underway by March 2018
- Carry out tree health assessments and issue plant health notices on time
- Clear 715 hectares of trees on our estate to manage larch disease (*Phytophthora ramorum*)

2017/18 results

- All 19 PSBs' Well-being Plans have been approved by our NRW Board (some with conditions)
- We have produced a strategic steer for biodiversity and presented it to our Board
- 67% of actions on designated sites have been completed or are underway - we have not achieved our 80% target. This does however include a number of successes such as our Raised Bogs Projects
- At the request of the Welsh Government, we have stopped issuing tree health notices in order to review the extent of the disease
- 949 hectares of trees have been felled due to clearance of *Phytophthora ramorum* infection, above our intended target

Examples of our work over 2017/18:

Developing a strategic collaborative approach to delivering the Nature Recovery Action Plan

We want to deliver a step change in the way we work, to embed the maintenance and enhancement of biodiversity and resilient ecosystems into all the functions of our organisation so they are considered at an early stage of decision making, planning and project delivery. Our draft document – 'Vital nature: Making the connections between biodiversity and the people and places of Wales. NRW's strategic steer for biodiversity to 2022' - was presented at the NRW Board meeting in March 2018.

We aim to emphasise the multiple benefits and ecosystem services that can be derived from biodiversity and resilient ecosystems, such as pollination, cultural services (such as landscape, recreation and access to the outdoors) pollution reduction and water management. It also focuses on future action for biodiversity, addressing the root-causes of issues and undertaking preventative measures, applying the nine SMNR principles.

Raised Bogs Project gets underway

Our EU-LIFE funded Raised Bogs Project has now begun. Raised bogs are an important part of our ecosystem and very valuable for carbon sequestration. The aim of the project is to improve the conservation status of active raised bog and degraded raised bog in Wales, by directly addressing the causes of poor condition. This mainly relates to the effects of drainage for agriculture, historic peat cutting, fragmentation of peat bodies and loss of the characteristic morphology and habitat zonation of raised bogs, as well as colonisation by invasive species. The project will include seven of the eight raised bog SACs in Wales.

Celtic Rainforest National Nature Reserve extended

Ceunant Llennyrch National Nature Reserve (NNR) has been substantially extended, helping to protect much more of this special area. We manage a 12-hectare reserve – but the Woodland Trust (Coed Cadw) manages 300 hectares of land which has now also been granted NNR status.

Referred to as a Celtic rainforest due to its humid conditions, the whole area (the size of 400 football pitches) will be managed to restore and extend native woodland and bring other upland habitats into good condition.

It also provides an opportunity to improve public access so that more people can experience this special site. Its gorge woodland contains more than 200 species of mosses and liverworts, some of which have only been recorded in a few sites world-wide. More than 200 species of lichen live on the trees. It is also home to redstarts and wood warblers, otters and rare lesser horseshoe bats.

Water voles thriving in Wales

The water vole population in Wales is on the increase following a 10-year breeding programme. Since the 1970s water voles had declined by almost 90% and was one of the most endangered mammal species in the UK. Changes in riverbank management techniques and land use practices in the UK, together with the introduction of the North American mink for fur farming has had a devastating effect on their numbers.



In the 10 years since we began a captive breeding programme almost 1,000 water voles have been reared and released into the wild, helping to boost the population.

Working with local partners we have established four breeding colonies in south, mid and west Wales. The water voles typically produce six litters between March and late September, each with four to six young. The offspring are then released during the summer, into selected controlled sites with good habitat connectivity, so they are able to colonise the wider landscape.

M4 Corridor around Newport

The Welsh Government has proposals for a new section of motorway - the M4 corridor around Newport (M4CaN). We have provided detailed comment on a range of issues including flood risk, drainage, sustainability, protected species, historic landscapes, ecology and conservation and air and water quality, including at a recent public inquiry. In our role as advisor to Welsh Government, we have objected to the proposals as they currently stand, on four main grounds:

- **Flood risk** - we consider the Flood Consequence Assessment (FCA) does not fully demonstrate the consequences of tidal flooding can be acceptably managed/ mitigated over the lifetime of the project.
- **Designated sites** - we consider that the scale of permanent loss of SSSI in the Gwent Levels is both unprecedented and would be contrary to the statutory duties of the Wildlife and Countryside Act 1981 (as amended) and the Environment (Wales) Act 2016.
- **Protected species** (Bats) - we have raised an objection to the granting of the road orders due to the impacts of severance, habitat fragmentation and mortality associated with the construction and operation of the road.
- **Historic landscape** - the new section of motorway would result in a significant adverse effect on the historic landscape of the Gwent Levels which could not be effectively mitigated.

Now that the inquiry has concluded, inspectors are finalising their report. This will be submitted to the Welsh Government and ministers will then make their decision on approval.

Well-being Objective 4 – Reduce the risk to people and communities from environmental hazards such as flooding and pollution

We advise on, forecast and monitor the likelihood of flooding and, as well as developing flood defence schemes, support local communities to reduce their risks. Similarly, we advise and regulate industry and waste sites for example, to reduce the likelihood of pollution entering the wider natural environment – and we of course provide a response to environmental incidents that do occur despite best efforts. Aiming to be firm but fair, we will investigate incidents and use our full range of powers to tackle environmental crime when necessary.

Our measures

- Deliver an effective and co-ordinated incident response service by March 2018
- Maintain 99% of high risk flood risk and coastal risk management assets at target condition
- Construct flood alleviation schemes to reduce risk to 500 properties
- Develop a new approach and monitoring system for enforcement by March 2018
- Reduce the impact and number of the poorest performing waste and industrial sites

2017/18 results

- We were unable to assess our incident response service this year, but we have established a set of improvement targets to be achieved by April 2019
- We did not achieve our target of 99% of flood assets at target condition, achieving 97.5%
- We have seen improvements in flood alleviation schemes – achieving improved flood protection for 1,282 properties against a target of 500
- Our new approach for monitoring enforcement has made good progress, although some of our established targets remain outstanding at year end
- Poor performing sites improved again from 2016 –with three fewer in the industry sector and four fewer in the waste sector

Examples of our work over 2017/18:

New air quality thresholds to limit air pollution

Wales is now the largest producer of free range eggs in the European Union: there are now two hens for every one person in Wales. While this is good for the economy it can have a detrimental effect on air quality and wildlife because of the high levels of ammonia that intensive livestock units can produce. Ammonia is toxic: its build up can lead to species loss and can cause significant damage to habitats.

We issue permits for larger poultry units and we are a statutory consultee for applications considered by local authorities. While ammonia emissions have stabilised across the UK generally, they have increased significantly in Wales largely due to the expansion in poultry numbers. Because of this we have been working closely with colleagues in other UK agencies to investigate and quantify the impact of air pollution from livestock units. As a result of this work we will be establishing new air quality thresholds and will use this to underpin our permitting role and support our advice on planning applications.

Storm Emma's devastating impact on Holyhead Marina

During Storm Emma in March 2018, approximately 80 yachts and 15 commercial vessels were wrecked at Holyhead Marina as their floating pontoon moorings were ripped from their anchors and the marina pontoons, kept afloat by polystyrene, were broken apart. By the morning the devastating scale of the damage became clear - as well as the shells of broken vessels there were significant amounts of polystyrene and other debris within the harbour.

We played a key role in advising on the clean-up operation. We assessed the potential impacts on the environment from pollutants and advised on marine litter and disposal, and on marine invasive species. We worked closely and consistently with our partner agencies to minimise potential harm and have regularly been on site, providing advice and guidance to Holyhead Port Authority, Cyngor Sir Ynys Môn and the Marina owners.

Polystyrene recovery in this incident was more than an issue of simply reducing marine litter. The invasive carpet sea squirt (*Didemnum vexillum*) that had colonised the marina infrastructure at Holyhead could have spread from the marina on fragments of the rubber coating around the shattered polystyrene floats. This invasive marine animal has the potential to be very damaging to many marine interests, particularly to the shellfisheries that operate in the area. We gave this advice early and clearly so that actions to manage the invasive sea squirt were integrated with the incident polystyrene survey and collection work.



First Minister Carwyn Jones visited the site recently and announced up to £30,000 would be made available by the Welsh Government to help with the clean-up costs as well as additional money for affected local businesses.

We will be carrying out monitoring later this year to look for the presence of the carpet sea squirt outside of the Harbour.

Roath, Cardiff Flood Scheme

As part of our flood risk management work we aim to improve the protection to 500 more properties every year and although we are consistently meeting this target, some of our schemes have met with opposition from local residents. One of these is the Roath Flood Scheme – the project will reduce the risk of flooding for 405 properties (360 homes and 45 businesses). A campaign group has been established which is opposed to a particular part of the scheme - the felling of trees in the Roath Mill and Roath Brook Gardens - which seeks to protect around 60 properties. The campaign group believe that the flood risk is not real, that we have exaggerated the extent and that other options are available. They feel the loss of trees would spoil the local environment.

Although we believe we consulted extensively with the local community during the scheme's development and received planning consent there were a number of protests held once work began including people climbing trees to prevent them being felled. This

caused delays to the project, particularly as we needed to ensure the safety of everyone on the site before we could re-start work. We have continued to engage with the campaign group and the local community and have assured them that we will replant trees sympathetically to minimise short-term impacts on the local environment and wildlife. The first two phases of the overall scheme have continued and will be completed in the late summer: they will provide protection to approximately 350 homes and businesses in the area.

Landfill site suspended

We have taken action against the operator of a mid-Wales landfill site due to its pollution risk. Officers suspended the operator's permit after evidence showed that the site holds substantially more waste than is legally allowed. We also estimated that the waste stored at the site is significantly greater than permitted. Both are a breach of the operator's environmental permit. Every landfill site needs an environmental permit to operate, which details how the operator will manage the site to minimise the impact on air, land and water in the area.

As a result the operators are not allowed to tip any more waste in the landfill and we have now instructed the company to examine the potential risk that this waste poses. Last year we applied other legal measures, such as serving legal notices on the operator, to try to ensure the site was made compliant with the permit conditions. However, we have now needed to suspend the permit.

Civil sanctions help schools and community groups



We have used an alternate approach with a company that polluted the River Taff in May and September of 2016. Following the reports, it was found that waste from a site in Treforest had found its way into the river via an unchartered culvert. Although no fish were killed, the pollution killed aquatic invertebrates which are an important food source for fish like trout and salmon. Rather than prosecute, we accepted an offer by the company to use civil sanctions.

The company agreed to pay £40,000 to Gwyl Taf, a local project run by the South East Wales Rivers Trust. The project encourages schools and community groups to enjoy the River Taff in a positive and healthy way and will provide more long-term benefits for people and the environment. Investigative costs of £12,000 have also been paid to NRW which will go towards aiding officers in identifying hot spots for diffuse pollution

Proceeds of Crime Act

This year we have had two significant confiscation orders made under the Proceeds of Crime Act (POCA). POCA is a piece of legislation that allows us to make someone pay back any monies they have made through their illegal activity, helping to protect the environment while also helping to ensure a level playing field for legitimate businesses.

We have collaborated with Dyfed Powys Police, their accredited financial advisors and forensic accountants to investigate an illegal scrapyard in west Wales. The investigation took many months of hard work but ultimately led to a confiscation order of £289,000, with the operator serving a prison sentence.

A south Wales farmer has also been ordered to pay back £226,000 for using his land to deposit waste illegally.

Prosecution for illegal tree felling

Our Regulatory Woodland Officers, Environmental Crime Team and Legal Department worked together to bring the case to court when 200 veteran hedgerow birch trees were illegally felled in south Wales.

Evidence was collected and a case for prosecution was prepared. As part of our case we had to calculate an accurate value for the trees which had been felled. We normally use the commercial value of the timber, but in this case we also used 'The Helliwell System' which is used to calculate the visual and amenity valuation of trees and woodlands. We calculated this at over £50,000. We would not have granted a licence to allow these trees to be felled. In September the defendant was fined over £100,000 and ordered to pay almost £7,000 in costs plus a £170 victim surcharge – the maximum fine possible for an offence of this nature.

Well-being Objective 5 – Help people live healthier and more fulfilled lives

As well as providing a wide range of opportunities for recreation on the land we manage ourselves, we work with partners to encourage people to access the outdoors throughout Wales and improve their health and well-being. We support community projects and help people to learn about the value of the natural environment, its importance in day to day life and its part in Welsh culture and heritage.

Our measures

- Promote the use of the outdoors to get active and improve well-being
- Increase opportunities for local access that bring communities together
- Interpretation of data on attitudes to the natural environment taken from the National Survey for Wales by March 2018
- Review and maintain our recreational facilities by March 2018

2017/18 results

- We have successfully promoted the Wales Coast Path, the National Trails and maintained the 'NRW Places To Go' website
- Our Cyfle scheme, providing opportunities for work placements and volunteering, continues to be developed, with the new placements being managed by teams by April 2019
- Changes in timescales meant that we did not commission additional data analysis, however, we published four bulletins interpreting data relating to people's attitudes to various aspects of the natural environment
- We have completed a review of our recreational facilities have continued to maintain them throughout the year

Examples of our work over 2017/18:

Temtiwr – women's mountain biking event

We recently hosted 'Temtiwr' an event to encourage more women to take up mountain biking, at our Coed Y Brenin Forest Park. Organised in collaboration with Beics Brenin, Welsh Cycling, Dyfi Events and Infinite Exposures it offered 60 women the opportunity to improve their mountain biking skills, learn about bike maintenance and socialise with other riders.

Tracey Moseley, a former Downhill and Gravity Enduro Champion, hosted a question and answer session at the event and the weekend's activities also included mountain biking skills coaching, workshops, guided rides, yoga and a film showing.

Coed y Brenin has several purpose-built mountain bike trails ranging from forest roads trails for novices to 'black' grade trails for expert riders. The feedback for Temtiwr was extremely positive and it's hoped it will become an annual event.



‘By All Reasonable Means’

By All Reasonable Means: Least Restrictive Access to the Outdoors

has been developed to provide guidance for land owners to help ensure that access to the countryside and open spaces is equally available to people of all ages, circumstances and backgrounds.

A key concept in this guidance is to ensure the least restrictive access principle is applied when planning for access in the outdoors. A gap provides least restrictive access, followed by a gate and if that is not feasible then a stile. But it is not just about physical features, it is also about how people decide to visit a site, the usefulness of information they receive and their experience once they are there. Good information can help overcome many of the barriers that prevent people visiting a site in the first place.

The guidance aims to provide a realistic, practical and effective approach to access improvements, creating more accessible places for more people. It encourages land managers to identify those techniques that are most appropriate for their particular situation and help more people enjoy the outdoors.

Discovery backpacks

Last autumn our visitor centres at Bwlch Nant y Arian and Coed y Brenin offered children visiting the centres a ‘discovery back pack’ to help them explore the outdoors. The backpacks contain binoculars, a magnifying glass, a bug pot and nature identification cards along with a guide explaining how to use them. They also included some challenges to help get the children started – ranging from tree and bird spotting to bark rubbing and searching for minibeasts.

Dee Estuary boat trips

We have worked with the Harbour Master of the Dee Estuary to support a local group known as the Quay Waterman’s Association (QWA) to help develop safe and accessible recreational boat trips along the Dee Estuary, funded by various grants and charities. The two QWA boats are wheelchair accessible and enable people to develop a greater connection with the estuary.



Well-being Objective 6 – Promote successful and responsible business, using natural resources without damaging them

We want Wales to be seen as a great place to do business, embracing green growth, new sectors, research and innovation. As well as developing our own commercial activities, we want to encourage businesses to use resources efficiently and work towards a circular economy. We use our regulatory powers – permitting, monitoring to check compliance and enforcement – to protect the natural environment and to ensure that legitimate businesses are not undermined.

Our measures

- The impact and quality of our advice improves by December 2017
- We move to a commissioning led outward funding (grants) model by April 2018
- 700,000 cubic metres timber to market by March 2018
- Deliver our renewable energy programme
- Respond to planning consultations to agreed timescales

2017/18 results

- We scored four out of five when asking for feedback on the effectiveness of our advice, indicating that users surveyed either agreed or strongly agreed that our advice had had an impact on their decision making
- We received 200 expressions of interest for grants and selected 80 to be taken forward with additional advice provided for those applicants moving to the next stage
- We have put 744,000 cubic metres of timber to market in 2017/18
- The First Minister opened the Pen y Cymoedd windfarm in September 2017; the Cwm Saebren community led scheme was completed in February 2018. Construction of the Garwnant hydro scheme was completed in February 2018, and we continue to provide access to renewable energy projects adjacent to NRW managed land
- 97% of planning consultation responses were within agreed timescales (6,747 responses within deadline)

Examples of our work over 2017/18:

Wales largest onshore windfarm officially opened by First Minister

The Pen y Cymoedd wind farm, on NRW managed land at the top of the Rhondda and Neath valleys, has now been developed by Vattenfall and comprises 76 turbines producing enough electricity annually to power the equivalent of 188,000 homes or 15 per cent of



Welsh households. Our Energy Delivery Programme Team has worked closely with Vattenfall since 2005 to make this 228 megawatts renewable energy project a reality.

It is one of the first projects under our Enterprise Plan's Energy Development Portfolio to be completed and has brought significant economic benefits for Wales with

52% of the £400 million investment to build the project going to Welsh businesses and securing work for more than 1,000 Welsh workers over the past three years.

Operational since spring 2017, the project will continue generating fossil fuel free electricity until at least 2037. Our collaboration with Vattenfall to deliver this project not only stimulates positive economic change for Wales but also puts NRW at the forefront of the Welsh Government's low carbon economy, climate change and green growth programmes – all aligned to our purpose of managing the environment and natural resources sustainably.

River Dee Cockle Fishery

The River Dee Cockle Fishery has just completed its 10th consecutive opening season. A Regulating Order, which came into effect in 2008, has enabled us to manage the cockle bed sustainably. It is now a multi-million-pound fishery, accredited by the Marine Stewardship Council as sustainably managed. It gives licencees a regular income, feeds internationally important overwintering birds and contributes to the wider estuarine environment.

Barry biomass

We granted an environmental permit to Biomass No2 UK Limited in February 2018 to operate a waste wood gasification plant in Barry. The site is contentious within the local community, with strong opposition to the proposal from the public and local politicians. Our decision followed an extensive assessment of the company's plans and several consultations with local people and professional bodies including Public Health Wales and South Wales Fire and Rescue, and we have worked very hard to engage, inform, listen to and consult local residents.

Wales needs facilities like this one to process difficult to dispose of wastes, which aren't suitable for recycling and to mitigate the risks of wood storage sites catching fire. They require both planning permission and an environmental permit. Their location is determined through the local planning process. The permit considers whether a facility is capable of operating safely, efficiently and effectively. If we determine that the site can operate within the environmental, technological and health standards required, then we have no defensible reason not to permit it – we can't say no on the basis of a petition and vocal opposition, we have to work within the guidelines of our remit.

The conditions we have set in the permit require it to operate to the Best Available Techniques (BAT) and we will monitor activity at the site to ensure it continues to work within the agreed conditions of its permit. Waste and how we deal with it is an integral part of ensuring our resources are managed sustainably and our waste regulation activities are a vital part of helping to protect our environment and ensure a level playing field for legitimate operators.

Wylfa Newydd nuclear power station proposals

Horizon Nuclear Power propose to construct and operate a new nuclear power station at [Wylfa Newydd](#) on Anglesey - two advanced boiling water reactors generating up to 3100

megawatts of electricity, enough power to supply up to 5 million homes. We have a critical role to play in determining a number of environmental permits as well as providing expert advice to other organisations on the decision they need to make - planning permission for the new power station will be decided by the Secretary of State.

Over the past five years, we have provided substantial advice and guidance to the developer. We received the first of the main applications in October 2017 with a further four on the 1 June 2018. The applications include construction water and cooling water discharge, marine licensing, combustion installation, radioactive substances and later in 2018 for the abstraction of water.

We are committed to being open and transparent throughout this work and ensuring the public has the opportunity to contribute to the process. We will run two consultations for our permitting process - on the applications received and then on our draft decision.

Well-being Objective 7 – Develop NRW into an excellent organisation delivering first class customer service

We want to be the best organisation we can be, for our staff, our customers and the natural environment. This means we have undergone considerable change as an organisation, but following the staff restructuring that will take place in 2018/19, this rate of change will reduce considerably.

Our measures

- Quality of our collaboration with customers and other organisations
- Our new organisational design is complete by March 2018
- Deliver our Customer Focus Programme
- Implementation of our People & Teams Strategy

2017/18 results

- NRW and the Welsh Archaeological Trusts were winners of the Collaboration award at the Continuous Improvement in Public Services Awards for our joint working in natural and historic environments
- Our final draft structure for our Organisational Design was produced in May 2018 rather than March as we had planned
- We completed an internal and external customer survey in March. We will use the results to help develop our approach with customers and collaboration with partners
- We ran our people survey in January and February and are currently analysing the results – these will be provided by managers in April and the results will be published on our intranet

Examples of our work over 2017/18:

Improving customer service in NRW

We have been working closely with the Institute of Customer Service (ICS) and have recently completed an internal and external customer survey to help us understand customer needs and ensure we provide a consistently high level of service.

Improving the experience all our customers is at the heart of our Customer Focus Programme. In May 2017 the new [NRW Customer Statement](#) was launched on our website, following a review of the existing service information available for customers. The statement explains how customers can access our services and what to expect when they contact us. The statement also contains links to other areas of work to help customers easily find what they need.

Collaboration award

The Institute for Continuous Improvement in Public Services (ICiPS) held its UK 2018 award ceremony at Leeds Museum on 14th March, and we were very pleased to be invited. NRW and the four Welsh archaeological trusts: Clwyd-Powys, Dyfed, Glamorgan-Gwent and Gwynedd had collectively submitted our joint working in the natural and historic environments for the collaboration award; our work is encapsulated in a Memorandum of Understanding (MoU).

Not only was our submission nominated, but we came away as winners of the collaboration category: the linking hands on the glass trophy award aptly mirrors the ethos of our work. This will help us showcase our work, share good practice and raise awareness of the value of the ICiPS. The award recognises our change in culture to one of continuous improvement. This has benefitted each signatory, partner organisation and the natural and historic environment sectors: and the MoU has been the catalyst.

Collaboration has brought unity, purpose and strength across our organisations at all levels, it has enabled us to build capacity and develop expertise in specialist areas, run joint training events, reduce duplication and improve consistency. By positively working together it has drawn in other organisations creating a ripple effect of enhanced collaboration. The rewards of working in this way are many and contribute to the economic and social vitality of Wales.

NRW's equality, diversity and inclusion

We take our commitment to equality, diversity and inclusion very seriously and have had several successes during 2017/18:

- **Stonewall Index Improvement:** we climbed 52 places in the Stonewall Workplace Equality Index ratings to 15th best employer in Wales for LGBT+ people and 132nd in the UK.
- **Transgender Day of Visibility:** this year, the LGBT Network worked hard to be even more visible than before. One example of this has been our celebration of International Transgender Day of Visibility. We used the day as an opportunity to promote our Equalities Senior Advisor, Samantha Carpenter, as a positive openly trans role model.
- **Working towards dementia friendly accreditation:** our Dementia Friends Network now has over 200 friends throughout our organisation, who have raised over £1,500 for dementia research over the past year. We have now begun working towards full dementia friendly accreditation.
- **MS Employer of the Year:** In May 2017 NRW won the Multiple Sclerosis Employer of the Year Award for supporting one of our employees, helping to keep a valued member of our staff in a job he loves.

The wide range of case studies we have shown here illustrate the breadth of our work, and that as well as contributing to more than one of our own Well-being Objectives, they each also contribute to several of the Well-being Goals.

Clare Pillman
Chief Executive and Accounting Officer

Date: 13 July 2018

Accountability Report

Our Accountability Report outlines key features of how we manage our organisation. Over the following pages our Corporate Governance report explains who our Board and senior management team are, how they work and the governance arrangements in place to ensure effective management and oversight of our resources to achieve our objectives.

Our Remuneration and Staff Report describes how we address Board and senior management pay as well as providing an overview of the make-up of our staff numbers.

Our Parliamentary Accountability and Audit Report brings together additional requirements requested to demonstrate our accountability to the UK and Welsh Governments, regularity of expenditure and the final opinion from our Auditor.

Corporate Governance Report

Directors' Report

We employed five executive directors and two directors who, along with the Chief Executive formed our Executive Team during 2017/18.

Position	Post Holder	Length of Service
Chief Executive	Emyr Roberts	1 November 2012 – 31 October 2017
Chief Executive	Clare Pillman	26 February 2018 – present
Interim Chief Executive	Kevin Ingram	1 November 2017 – 25 February 2018
Executive Director of Finance and Corporate Services	Kevin Ingram	1 April 2013 – present
Executive Director of Evidence, Policy and Permitting	Ceri Davies	1 April 2013 – present
Interim Executive Director of Finance and Corporate Services	Niall Reynolds	1 November 2017 – 25 February 2018
Executive Director of Operations (North & Mid)	Tim Jones	1 April 2013 – present
Executive Director of Operations (South)	Gareth O'Shea	27 April 2015 – present
Executive Director of Organisational Development and People Management	Ashleigh Dunn	17 November 2014 – present
Director Customer, Communications and information	Catherine Love (née Smith)	22 April 2014 – present
Director Transformation Portfolio	Niall Reynolds	1 April 2013 – present

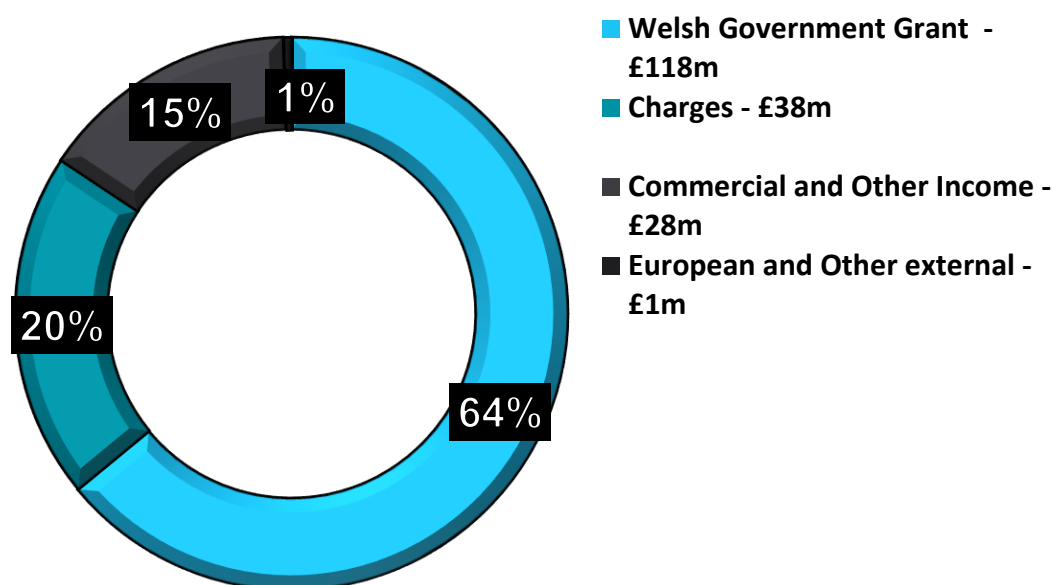
Our Executive Team Register of Interests is available [here](#)

Managing our finances

Funding

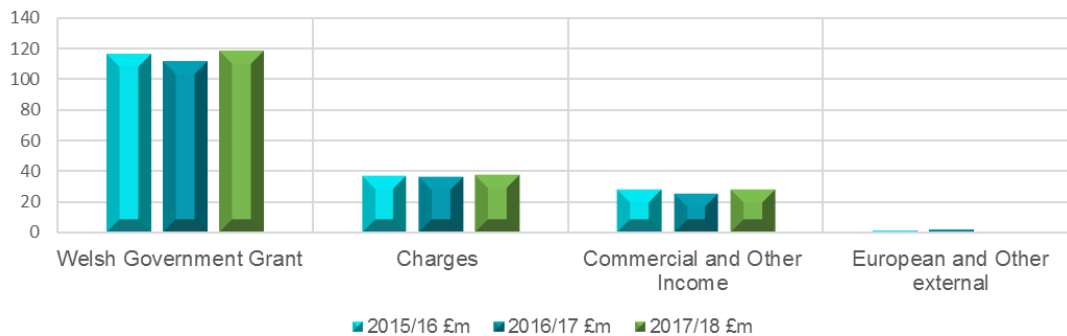
Our total income for the year was £67 million (note 6 on page 76). In addition, the Welsh Government provided £118 million Grant-in- Aid and other grants (Statement of Changes in Taxpayers' Equity on page 67) towards a range of outcomes, of which £38 million was allocated to flood and coastal risk management. In the financial statements, 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.

Funding by Type



In 2017/18 our funding increased from £174 million to £185 million with the biggest increase being the Welsh Government Grants (£7 million). Our core grant funding remained at the same level to the previous financial year, but we have received additional funding for new priorities and the flood and coastal risk management capital programme. An overall increase in charges (£2 million) was required to fund specific capital works on reservoirs via the abstraction charge – otherwise they have been kept at the same cash level as the previous financial year. Commercial and other income also increased last year by £3 million owing mainly to the buoyant timber market. This is illustrated in the graph below.

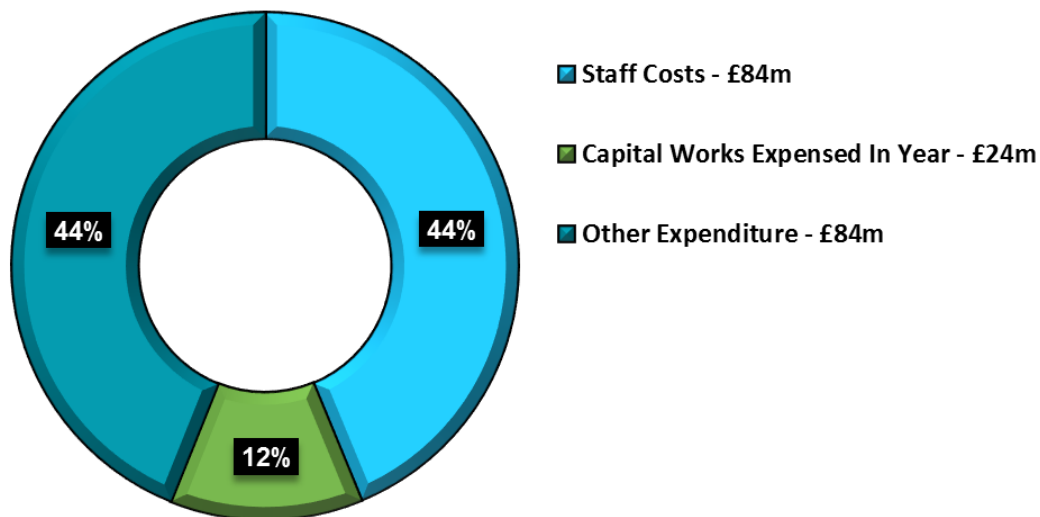
Funding by Financial Year



How we spent our money

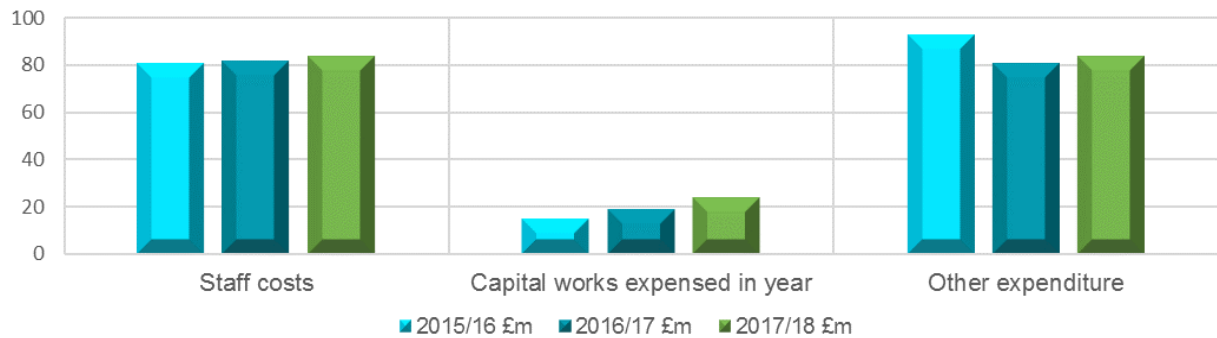
Our total expenditure was £192 million. The detailed breakdown by category of spend can be found in the Financial Statements and is also illustrated below.

Expenditure By Type



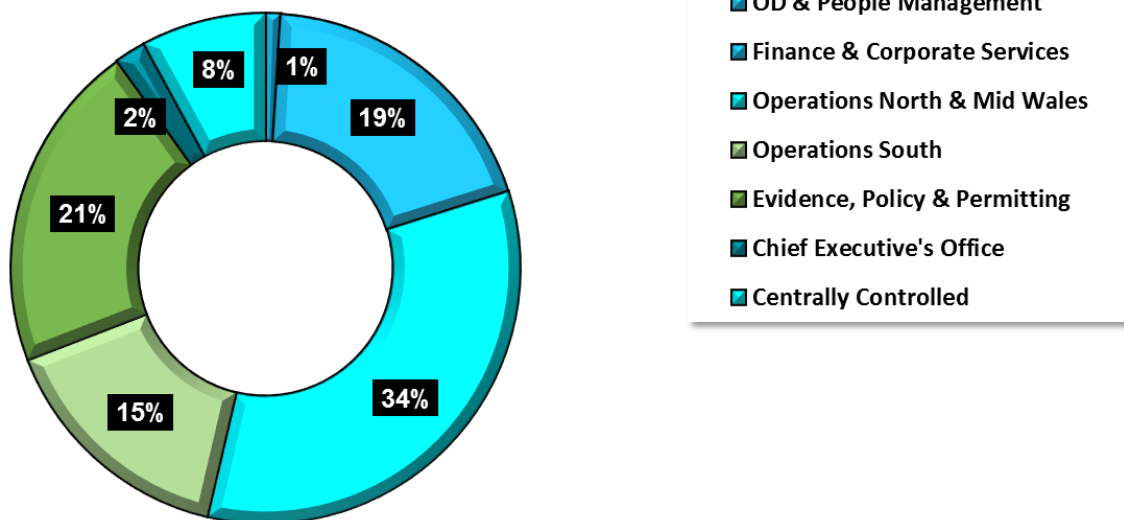
In 2017/18, our expenditure increased from £182 million to £192 million. This is not due to core activities but due to the cost of implementing the job evaluation scheme, investing in new priorities funded by additional Welsh Government grants and constructing flood and coastal risk management schemes. This is illustrated in the graph below.

Expenditure by Financial Year



The graph below shows how the money was spent by directorate. 49% of our expenditure was spent in our Operations teams, whilst another 21% was spent in our Environment, Permitting and Planning teams. 8% has been categorised as centrally controlled which accounts for non-cash movements such as depreciation. The remaining 22% was spend across the range of our corporate service departments, which have been benchmarked against other public-sector bodies.

Expenditure By Directorate



Managing our money

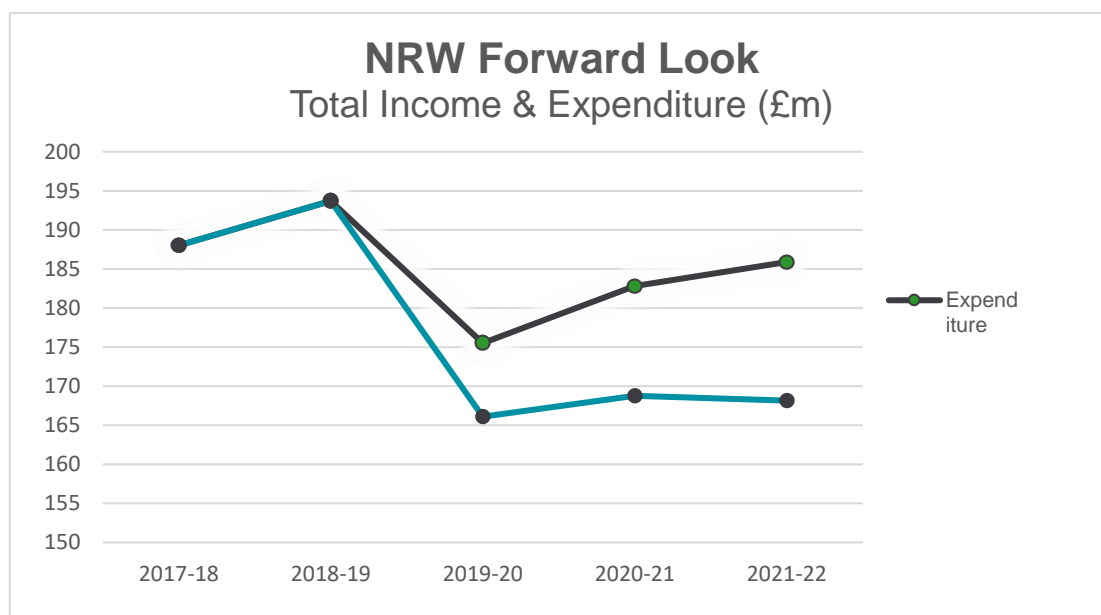
In 2017/18, our funding from the Welsh Government was at the same cash level as 2016/17. We also utilised our charges and commercial income in the undertaking of our activities. We received additional funding from the Welsh Government to tackle issues such as the spread of the tree health disease and embedding the sustainable management of natural resources. All budget allocations were scrutinised and approved by the Executive Team and Board. We have also benefited from an

extremely buoyant market and our timber sales topped £19 million for the first time in NRW.

Future look

We launched our Corporate Plan to 2022 and we are also about to launch our Finance Strategy. This has been produced alongside the Corporate Plan and pulls together all known factors affecting the financial position and sustainability of NRW to 2022. We are not underestimating the overall context in which we are operating in – there are significant challenges for the natural environment and for us as an organisation in ensuring our natural resources are sustainably managed. We also have a challenging financial environment – our non-flood revenue Grant in Aid budget was reduced by 5% in 2018/19, with another 5% reduction likely in 2019/20.

The table below shows the gap between income (including funding from Welsh Government) against expenditure before we have acted to bridge that gap.



Non-current assets

The value of our non-current assets was £949 million at 31 March 2018, a 6% (£57 million) increase compared to last financial year. The most significant component is the value of the forest estate and biological assets which accounts for £784 million of the total. We are required to undertake an independent quinquennial revaluation of freehold land, buildings and forest estate and that will next be undertaken in 2020/21. In the intervening years, our non-current assets, where they have a material impact on the financial statements, are revalued via the appropriate indices.

Payment of trade and other payables

Welsh Government has a commitment to pay 95% of suppliers within 30 days and we aim to exceed this target wherever possible. Performance for the whole year was 97% and represented a significant improvement on the previous financial year (91%). This helps to ease businesses' cash flow in the current challenging economic climate.

Debtor performance

Our continued effective management of commercial debt has seen us deliver a further improvement in commercial debt, demonstrated by the improvement in the average number of days it took customers to pay – 11 days compared to 36 days in 2016/17. Our management of regulatory debt has also led to an improvement in debt collection – from 3.7% of charges raised in 2016/17 to 2.4% in 2017/18.

Our bad debt provision for regulatory debt was £226,000 at 31 March 2018, relating to 45 customers, with one customer accounting for £105,000.

Going Concern

The Statement of Financial Position at 31 March 2018 shows positive taxpayers' equity of £911 million. The future financing of our liabilities is to be met by the Welsh Government Grant in Aid and the application of future income. We have already received approval for funding for 2018/19. Therefore, it is appropriate to adopt a going concern basis to prepare the Financial Statements.

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 estate, which sets how each forest will be managed to deliver strategy objectives over the next 10 years.

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

All national nature reserves, including those owned or managed by NRW, those managed through partnership arrangements, and those managed by third-parties, are managed in accordance with an approved management plan. These plans include conservation objectives for all recognised features of interest and identify necessary projects and work programmes. The plans are reviewed periodically and checked by our Conservation Management team, through a rolling programme of reviews and environmental audits.

Pensions

The pension liability is disclosed in the Financial Statements based on International Accounting Standard 19. The liability has decreased for the Local Government Pension Scheme from £42 million to £32 million in the year.

This is different from the basis used for funding calculations. The last formal revaluation of the fund was undertaken at 31 March 2016 and showed an overall funding position of 103%.

Auditors

Our accounts are audited by the Auditor General for Wales. The audit fee for 2017/18 was £171,000. That includes an additional fee of £15,000 for the Well-being of Future Generations Wales Act audit.

Corporate data

In July 2017 Natural Resources Wales was the victim of a sophisticated phishing attack, which led to a small number of email accounts being compromised. We have no evidence that corporate data was lost but have undertaken a thorough investigation of the event and are in the process of implementing a suite of recommendations to improve our resilience to future attacks of this nature.

Personal data

Some of the accounts compromised as a result of the phishing attack handled information of a sensitive nature and although we have no evidence that personal data was lost, we took the decision that it was right to inform a very small number of customers that their information potentially had been taken. We notified the Information Commissioner's Office of the incident and the action we had taken. We have undertaken a thorough investigation of the event and are in the process of implementing a suite of recommendations to improve our resilience to future attacks of this nature.

Corporate reporting

The following annual reports and plans are also available on our website:

- [Business Plan 2017/18](#)
- [Equality Annual Report 2017/18](#)
- [Welsh Language Annual Monitoring Report](#)
- [Gender Pay Gap Analysis](#)
- [Equality Action Plan 2018/19](#)

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 own environmental impact is included in Annex 1. This year we have:

- met our target to reduce our carbon footprint by 5% in relation to occupied buildings energy use and business travel
- retained certification to the UK Woodland Assurance Standard for the Welsh Government Woodland Estate we manage, following independent external audits and verification
- completed 67% of the National Nature Reserve management audit target and ensured any improvement actions identified were implemented
- purchased 22 sub 100 g/km cars and two new electric vehicles

Clare Pillman
Chief Executive and Accounting Officer

Date: 13 July 2018

Statement of Accounting Officer's responsibilities

Paragraph 23 (1) of the Schedule to the Natural Resources Body for Wales (Establishment) Order 2012 requires 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
- confirm that there is no relevant audit information of which Natural Resources Wales' auditors were unaware, and take all steps to make themselves aware of any relevant audit information and to establish that Natural Resources Wales' auditors are aware of that information
- confirm that the Annual Report and Accounts as a whole is fair, balanced and understandable and take personal responsibility for it and the judgements required for determining that it is fair, balanced and understandable.

The Additional Accounting Officer for the 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 she 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 delegated Accounting Officer for Natural Resources Wales, the Chief Executive is responsible for maintaining a sound system of internal control that supports the achievement of our 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.

I can confirm that information in our Annual Report and Accounts is a true and fair account of how the organisation has delivered its functions this year. I also confirm that there is no outstanding information that has been brought to my attention or that I am aware of that has not been brought to the attention of the Wales Audit Office.

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
- 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 Cabinet Secretary for Energy, Planning and Rural Affairs. We currently have 12 Board members, including myself as an executive member of the Board. We are led by our Chair, Diane McCrea. The remainder of the Board is made up of 10 non-executive members. There have been no changes to appointments this year.

The role and responsibility of the Board is to:

- provide strategic direction and leadership, driving performance and hold us to account for delivery of 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. We continue to support the development and implementation of the Welsh Government's legislative programme, while transforming our organisation through implementation of the Senior Management Review and Organisational Design Programmes. Implementing requirements of the Well-being of Future Generations (Wales) and the Environment (Wales) Acts have been key to our work this year, with the Board overseeing publication of our new Corporate Plan to 2022.

We held six two-day meetings across Wales this year, as well as a number of other development sessions. Standing items on our agenda include: well-being, health and safety; in-year finance and performance reporting; and strategic and operational updates from the Chair, Chief Executive, Committees, and Board Groups. To support our commitment that our work is 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](#)

Board member attendance

Board member	No. of possible meetings	No. of full meetings attended
Diane McCrea (Chair)	6	6
Madeleine Havard (Deputy Chair)	6	6
Andy Middleton	6	5 ¹
Ruth Hall	6	5 ¹
Nigel Reader	6	4 ²
Paul Williams	6	5 ³
Chris Blake	6	6
Howard C Davies	6	5
Elizabeth Haywood	6	5
Zoe Henderson	6	6
Karen Balmer	6	5
Emyr Roberts (CE up to 31 October 2017)	3	3
Kevin Ingram (acting CE)	2	2
Clare Pillman (CE from 26 February 2018)	1	1

¹ Andy Middleton was present on Day 1 and Ruth Hall present on Day 2 of the March 2018 meeting

² Nigel Reader was present at Day 2 of the January and Day 2 of the March 2018 meetings

³ Paul Williams was present on Day 2 of the September 2017 meeting

Our Board has four committees, each chaired by a Board member, and include at least three other Board members. In addition to the three formal committees, the Board has established a standing Flood Risk Management Advisory Group. We do not have a Nominations 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 outline membership of our:

- Audit and Risk Assurance Committee
- People and 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. The Accounting Officer attends every meeting, along with our Executive Director of Finance and Corporate Services.

This year ARAC addressed a range of issues including:

- Annual Report and Accounts 2016/17 and plans for this report, 2017/18
- Public Accounts Committee Scrutiny of Annual Report and Accounts 2015 /16 relating to NRW long-term timber contracts
- External and internal audit preparations and reports
- Cyber security internal controls

Board member ARAC attendance

Board member	No. of possible meetings	No. of full meetings attended
Ruth Hall	5	4
Nigel Reader	5	5
Chris Blake	5	5
Karen Balmer	5	4
Madeleine Havard ¹	2	2

¹ Madeleine Havard deputised at two meetings: one for Ruth Hall and one for Karen Balmer

People and Remuneration Committee

The People and Remuneration Committee (PARC), considers matters relating to people management, reward and organisational change. This includes oversight of the pay and conditions of employment of the most senior staff, an overall pay strategy for all staff employed by Natural Resources Wales, pension scheme provision, wellbeing, health and safety, equality and diversity and development of the Welsh language.

The People and Remuneration Committee advises on strategic organisational development, ensuring there is a clear strategy in place, effective and affordable organisation design and effective management of major change initiatives, with the intention of ensuring a well-motivated, high-performing and innovative workforce. The Committee also oversees on behalf of the Board, the embedding of excellence in customer care, as a key component of organisational culture.

The Chief Executive attends every meeting, along with our Executive Director of Organisational Development and People Management, and our Transformation Portfolio Director.

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

- Job evaluation scheme
- Well-being, health and safety
- Changes to pension schemes
- Director appointments and remuneration

Board member PARC attendance

Board member	No. of possible meetings	No. of full meetings attended
Paul Williams (Chair)	4	4
Nigel Reader	4	4
Zoe Henderson	4	3
Karen Balmer	4	4
Diane McCrea	1	1
Emyr Roberts	2	2
Kevin Ingram	1	1
Clare Pillman	1	1

Protected Areas 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 the confirmation of one SSSI due to unresolved objections to the notification.

Board member PAC attendance

Board member	No. of possible meetings	No. of full meetings attended
Andy Middleton (Chair)	1	1
Madeleine Havard	1	1
Paul Williams	1	1
Howard C Davies	1	1
Elizabeth Haywood	1	1

Flood Risk Management Advisory Group

The Group is advisory and reports to the Natural Resources Wales Board. Its primary responsibilities are to scrutinise Flood Risk Management (FRM) investment programmes for current and future years, and to consider key issues which may affect the delivery of FRM-related work in Wales.

The Group comprises four members of the Board along with the Executive Director for Finance and Corporate Services, Executive Director for Evidence, Policy and Permitting, Head of Flood and Incident Risk Management and Head of Finance.

The Group met twice in 2017/18 (July and October) and it reviewed areas including:

- prioritisation of flood risk management activities
- governance of the flood risk management capital programme
- the latest medium-term plan for our capital programme
- the current performance indicators relating to the condition of NRW maintained flood risk assets
- the Internal Drainage District rates and precepts for 2018/19.

It also visited the Crindau Flood Alleviation Schemes currently under construction in Newport.

Board Member FRM Advisory Group Attendance

Board member	No. of possible meetings	No. of full meeting attended
Madeleine Havard (Chair)	2	2
Nigel Reader	2	1
Elizabeth Haywood	2	2
Karen Balmer	2	2

Board groups

Outside of our formal meetings, Board members contribute to strategic development through 'task and finish' Groups providing advice as requested on specific areas of work e.g. our charging scheme, performance reporting

Board effectiveness

During 2017/18 we continued to develop the skills and workings of the Board - a key area in which the Board needs to develop. Using information from a Board effectiveness survey we ran specific workshop sessions looking at key areas the Board needed to develop, we made changes to how our Board meetings are run and how we gather feedback after each meeting to continually improve. We repeated a Board effectiveness survey and maturity matrix in February 2018 - this has allowed us to track trends since the last survey. The maturity matrix has been particularly useful in identifying further areas for improvement. After each Board meeting there is a catch and reflection meeting to identify quick improvements we can make and the Board is always seeking ways it can be more effective in the discharge of its duties as well as the support it can provide to the organisation and executive team.

Compliance with the UK Corporate Governance Code

Our organisational structure, policies and procedures are set in line with the UK Corporate Governance Code. Our leadership is consistent with expected senior management roles and responsibilities; supporting procedures are in place to ensure Board roles can operate effectively; our reporting routes are clear to ensure accountability and key internal controls are in place; remuneration is considered by

non-executives to ensure independence and we have regular meetings with our key stakeholders to maintain constructive working relationships.

Our Executive

Day-to-day management of our organisation is delivered through our Executive Team. 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 the Transformation Portfolio and our Organisational Design Project.

Each Directorate has a Directorate Delivery Plan, which is linked to corporate targets and outcomes within the annual Business Plan. These are reviewed on a 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.

Ministerial Directions

We have received one Ministerial Direction this year. In February 2018 the Minister for Environment, on behalf of her portfolio and the Cabinet Secretary for Energy, Planning and Rural Affairs, wrote to us to approve implementation of our Job Evaluation scheme but with a specific proviso. Both Ministers wanted 'the non-consolidated pay award proposed in 2017/18 to be consolidated into pay in 2018/19'. We accepted the Direction however in our response we estimated that the additional £800,000 recurring cost per annum would inevitably have financial consequences and implications for delivery of our future workplans as well as our workforce.

Our risk management framework

Our day-to-day risks are identified, evaluated and managed at a number of different levels. The Executive Team are responsible for managing corporate risks in line with achieving strategic objectives. The Board has set the risk appetite for the organisation and 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.

NRW is currently building on existing processes to implement a step change to embedding risk management throughout the organisation. The Executive Team are responsible for overseeing the implementation of the changes and report to ARAC and the Board on progress and for their scrutiny. Based on best practice approaches to managing risks, the key objective is to ensure that we have a consistent approach to identifying, measuring, controlling, monitoring and reporting risks.

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 openness and security, making sure that staff and customers are assured of the highest levels of protection. The Senior Information Risk Owner (SIRO) continues to lead an

integrated programme of work to strengthen our response to and resilience against cyber and information security threats. The General Data Protections Regulation (GDPR) Implementation Project has successfully delivered regulation compliance through a suite of policy and guidance and thorough staff communication and engagement.

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 remain positive with Executive Team members confirming that our control framework continues to develop and apply across all work areas. Policies and procedures continue to be introduced or revised as necessary to adapt to external changes or internal gaps identified. Consistency of application is still a concern in some areas, for example, information management, due to ongoing prioritisation of other key projects, such as organisational design (OD) as well as day job activities. Senior management are aware of this and will look to improve consistency through OD implementation along with a revised induction programme planned for 2018/19.

We have an established fraud and whistleblowing policy and reporting procedure in place to raise serious concerns about malpractice or impropriety. The policy has also been reviewed by the ARAC Committee during 2017/18 and there have been no formal whistleblowing incidents reported.

We have received 14 allegations of fraud, which have been handled in accordance with NRW's anti-fraud, bribery and corruption process. These are reported to our Audit and Risk Assurance Committee and have been handled using trained internal investigators and agreed procedures.

Audit report

Our Internal Audit team have completed their annual audit plan, with regular progress and feedback to the Audit and Risk Assurance Committee.

The opinion of the Internal Audit Manager, as set out in their annual assurance report is: "Natural Resources Wales can receive moderate assurance over the overall adequacy and effectiveness of its internal control environment, including its arrangements for governance and risk management in all areas except for commercial governance where, due to governance and control failures, the level of assurance is unsatisfactory."

Internal controls

In response to the Public Accounts Committee review last year, a number of improvements have been made across the organisation to strengthen the controls in place, notably within Procurement and Legal. However, this year, Wales Audit Office have brought to management's attention significant failures involving timber contracts. This, and four serious non-conformities identified by the UK Woodland

Assurance Standard (UKWAS) audit in November 2017 have raised concerns over the effectiveness of governance, including the absence or poor application of internal controls in that part of the business. In response to the UKWAS audit, an action plan has been put in place which has secured the retention of the accreditation in the short term.

Governance

Strengthening governance is a major part of the Organisational Design programme, due to be implemented in April 2019. This is in recognition of the gaps and weaknesses in the current arrangements, including clarity of roles and responsibilities of various boards, groups and committees, scrutiny of projects and initiatives, and accountability for managing risks.

Risk management

While there are examples of a diligent approach to managing risk associated with certain operational activities, Natural Resource Wales' enterprise wide risk management is not mature. This has been recognised by the Executive Team and steps are being made to address this.

External audit

The financial statements for 2015/16 and 2016/17 were issued with a qualified opinion on the basis of regularity as a result of issues highlighted in the letting of eight high value long term timber sales contracts in 2014. These contracts were terminated at 31 March 2017 and a number of transitional contracts were put in place to give time for new contracts to be let on an open market basis.

The Auditor General has identified further regularity issues with how these new contracts have been let and managed. We accept the findings and the seriousness of the matters raised. An independent review of this area is being performed which will result in a comprehensive action plan to ensure that these issues are not repeated. The Board and ARAC will provide detailed scrutiny and oversight going forward.

Clare Pillman
Chief Executive and Accounting Officer

Date: 13 July 2018

Remuneration and Staff Report (audited)

Remuneration Report

Remuneration policy

The Board has established a People and 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 People and Remuneration Committee comprises 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. 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 is only for consistent outstanding performance as assessed by the Chief Executive and confirmed by the Remuneration Committee.

There was no pay deal for all staff for the period 1 July 2016 to 30 June 2017. It was deferred pending implementation of our new Job Evaluation Scheme and the associated new pay and grading structure.

There is a social partnership agreement in place with five trade unions and the setting of terms and conditions for staff below the Executive Team members 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. As part of the Job Evaluation proposal a 1% non-consolidated pay deal was agreed and implemented for 2017/18. This will be consolidated into pay from 2018/19.

Service contracts

All appointments to the Board are made on behalf of the Cabinet Secretary for Energy, Planning and Rural Affairs.

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 consistent with the Civil Service Compensation Scheme. Board members are not entitled to compensation.

Board members' remuneration

Board Member	Employment Contract	Salary 2017/18 (£5,000 range)	Salary 2016/17 (£5,000 range)
Karen Balmer ^{1,2}	9-11-17 to 8-11-18	15-20	10-15
Chris Blake ¹	9-11-17 to 8-11-18	10-15	10-15
Howard Davies ¹	9-11-17 to 8-11-18	10-15	10-15
Dr Ruth Hall CBE ¹	1-11-17 to 31-10-18	10-15	10-15
Dr Madeleine Havard ^{1,3} (Deputy Chair)	1-11-17 to 31-10-18	15-20	15-20
Elizabeth Haywood ¹	9-11-17 to 8-11-18	10-15	10-15
Zoë Henderson ¹	9-11-17 to 8-11-18	10-15	10-15
Diane McCrea (Chair) MBE ⁴	1-12-15 to 30-11-18	40-45	40-45
Andy Middleton ^{1,5}	1-11-17 to 31-10-18	10-15	10-15
Nigel Reader CBE ^{1,6}	1-11-17 to 31-10-18	10-15	15-20
Sir Paul Williams OBE ^{1,7}	1-11-17 to 31-10-18	15-20	15-20

¹ These board members were re-appointed for another year. The appointment of NRW's Non-Executive Directors or Board Members is the responsibility for Welsh Government and are appointed on varying lengths of terms.

² Karen Balmer was appointed as Chair of the Audit and Risk Assurance Committee (ARAC) from 1 September 2017. For 1 April 2017 to 31 August 2017, the full year equivalent salary is £10,000 to £15,000. The full year equivalent salary as ARAC Chair is £15,000 to £20,000.

³ Madeleine Havard is the Deputy Chair of the Board and the Chair of the Flood Risk Management Advisory Group.

⁴ During 2016/17, Diane McCrea's time commitment was 72 days per annum from 1 April 2016 to 31 August 2016 and 96 days per annum for 1 September 2016 to 31 March 2017. During 2017/18, Diane McCrea's time commitment from 1 April 2017 to 31 August 2017 is 96 days and 72 days from 1 September 2017 to 31 March 2018. Her full time equivalent salary based on 72 days per annum is £30,000 to £35,000 and is £40,000 to £45,000 based on 96 days per annum.

⁵ Andy Middleton is Chair of the Protected Areas Committee.

⁶ Nigel Reader was Chair of the Audit and Risk Assurance Committee until 31 August 2017. The full year equivalent salary as ARAC Chair is £15,000 to £20,000. From 1 September 2017, the full year equivalent salary is £10,000 to £15,000.

⁷ Sir Paul Williams is Chair of the People and Remuneration Committee and the Transformation Advisory Group.

Executive Team's remuneration

Executive Team Member	Salary		Benefits in kind		Pension benefits ⁶		Total	
	(£5,000 range)		(nearest £100)		(nearest £1,000)		(£5,000 range)	
	2017/18	2016/17	2017/18	2016/17	2017/18	2016/17	2017/18	2016/17
Clare Pillman ¹ (Chief Executive)	10-15	0	0	0	5,000	0	15-20	0
Dr Emyr Roberts ² (Chief Executive)	120-125	145-150	0	0	(8,000)	26,000	115-120	170-175
Ceri Davies	100-105	100-105	0	0	7,000	40,000	105-110	140-145
Ashleigh Dunn	90-95	90-95	0	0	36,000	36,000	125-130	125-130
Kevin Ingram ³	100-105	95-100	0	0	58,000	36,000	160-165	130-135
Tim Jones	90-95	90-95	0	0	20,000	13,000	110-115	100-105
Catherine Love	75-80	75-80	0	0	30,000	30,000	105-110	105-110
Gareth O'Shea	90-95	90-95	0	0	24,000	34,000	115-120	120-125
Niall Reynolds ⁴	80-85	75-80	0	0	26,000	26,000	105-110	100-105
Clive Thomas ⁵	0	40-45	0	0	0	72,000	0	115-120

¹ Clare Pillman was appointed as Chief Executive on 26 February 2018. The full year equivalent salary is £130,000 to £135,000.

² Dr Emyr Roberts finished on the 31 October 2017. The salary figure reported includes a payment of £35,000 to £40,000 which was made under the terms of a settlement agreement. The full year equivalent salary is £145,000 to £150,000.

³ Kevin Ingram acted up as Chief Executive for the period 1 November 2017 to 25 February 2018 and the full year equivalent salary during this period is £120,000 to £125,000. The full year equivalent salary for the rest of the year is £95,000 to £100,000.

⁴ Niall Reynolds acted up as the Executive Director of Finance and Corporate Services for the period 1 November 2017 to 25 February 2018 and the full year equivalent salary during this period is £85,000-£90,000. The full year equivalent salary for the rest of the year is £75,000 to £80,000.

⁵ Clive Thomas finished on the 31 October 2016. The full year equivalent salary for 2016/17 is £75,000 to £80,000.

⁶ 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.

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 people and 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 People and 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 & Customs as a taxable emolument. None of the Board members or Executive Team received benefits in kind during 2016/17 and 2017/18

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

Pension benefits

Executive Team member	Accrued Pension at pension age as at 31/03/18	Accrued Lump Sum at pension age as at 31/03/18	Real Increase in pension at pension age	Real Increase in Accrued Lump Sum at pension age	CETV at 31/03/18	CETV at 31/03/17	Real Increase in CETV
	£000	£000	£000	£000	£000	£000	£000
Clare Pillman ¹ (Chief Executive)	0-5	0	0-2.5	0	21	17	3
Dr Emyr Roberts ² (Chief Executive)	65-70	195-200	0	0	1543	1476	(8) ³
Ceri Davies	35-40	65-70	0-2.5	(0-2.5)	698	656	(6) ³
Ashleigh Dunn	5-10	0	0-2.5	0	106	72	24
Kevin Ingram	30-35	40-45	2.5-5	0-2.5	442	380	29
Tim Jones	35-40	115-120	0-2.5	2.5-5	820	749	17
Catherine Love	5-10	0	0-2.5	0	67	48	12
Gareth O'Shea	40-45	75-80	0-2.5	(0-2.5)	672	619	8
Niall Reynolds	35-40	70-75	0-2.5	0-2.5	701	642	14

¹ from 26 February 2018.

² until 31 October 2017.

³ 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 they have 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 or 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.

Compensation for loss of office

Emyr Roberts left under the terms of a settlement agreement on 31 October 2017. He received a compensation payment of £35,000 to £40,000.

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 where applicable. It does not include severance payments, employer pension contributions and the CETV.

In 2017/18, no employees (2016/17: none) received remuneration in excess of the highest-paid director. The banded remuneration of the highest paid Director in the financial year 2017/18 was £130,000 to £135,000 (2016/17: £145,000 to £150,000). This was four times (2016/17: 5.2 times) the median remuneration of the workforce which was £32,090 (2016/17: £28,215). Staff pay scales range from £16,835 to £64,424. Directors' remuneration is shown in the table above.

Staff report

Number of staff by headcount and full time equivalent (FTE) at 31 March 2018.

	Male		Female		Total	
	Headcount	FTE	Headcount	FTE	Headcount	FTE
All employees	1,221	1,127	903	800	2,124	1,927
of which:						
Leadership team	15	15	7	6	22	21
Executive team	4	4	4	4	8	8

Number of staff by headcount and full time equivalent (FTE) at 31 March 2017.

	Male		Female		Total	
	Headcount	FTE	Headcount	FTE	Headcount	FTE
All employees	1,190	1,096	858	758	2,048	1,855
of which:						
Leadership team	14	14	6	5	20	19
Executive team	5	5	3	3	8	8

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

	2017/18			2016/17
	Permanent Staff	Others	Total	Total
Directly employed	1,730	61	1,791	1,834
Agency and contract staff	0	91	91	73
Total	1,730	152	1,882	1,907

The average full time equivalent number of staff employed on capital projects was 104.7 (2016/17: 122.6)

Staff cost

	2017/18			2016/17
	Permanent staff	Other staff	Total	Total
	£'000	£'000	£'000	£'000
Wages and salaries	54,930	9,375	64,305	62,051
Social security costs and other taxation	5,633	912	6,545	5,855
Other pension costs	11,702	7,040	18,742	13,260
Total net salary costs	72,265	17,327	89,592	81,166
Other expenditure for staff		Note		
Exit package costs			184	4,935
IAS 19 (pensions) additional service charge		13	10,978	8,710
Less early retirement pension costs			(18)	(638)
Less in-year LGPS pension contributions			(12,181)	(7,558)
Transfer to provision for Annual Compensation Payments			0	78
Other staff costs			4	4
Movement in accrued holiday pay			223	16
Total other expenditure for staff			(810)	5,547
Less amounts charged to capital projects			(4,651)	(5,208)
Total staff costs			84,131	81,505

Details of NRW's pension obligations 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 £4.9 million of expenditure on consultants.

Pension schemes

Natural Resources Wales is a member of two pension schemes. The Principal Civil Service Pension Scheme is an open scheme and Natural Resources Wales is a closed member of the Environment Agency Pension Fund under a community admission agreement. Further details of these pension schemes are 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 schemes, but Natural Resources Wales is unable to identify its share of the underlying assets and liabilities. The scheme actuary valued the PCSPS 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 2017/18, employer's contributions of £5,794k were payable to the PCSPS (2016/17: £5,658k) at one of four rates in the range 20% 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 2017/18 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. Employer's contributions of £59k (2016/17: £44k) were paid to one or more of the panel of three appointed stakeholder pension providers. Employer contributions are age-related and range from 8% to 14.7%. 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 were due to the partnership pension providers at the balance sheet date, and no contributions were prepaid.

Local Government Pension Scheme contributions

Natural Resources Wales 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. Every three years the EAPF undertakes a valuation in conjunction with the Scheme Actuary. The March 2016 valuation assessed the EAPF financial position with a funding level of 103% (2013: 90%). 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 UK Government introduced regulations in 2016 which require LGPS funds to pool investments to improve efficiency. Brunel Pension Partnership, was created, comprising the EAPF and nine other LGPS funds to meet this obligation.

Natural Resources Wales has a community admission agreement with the EAPF 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. The 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 2017/18 the employer's contribution rate was 21.9% (2016/17: 21.2%). In 2017/18 employer's contributions of £12,181k were paid to the LGPS (2016/17: £7,558k) which included an additional payment to reduce the balance on the IAS 19 pension fund.

Exit packages

The total number of exit packages by cost band:	2017/18	2016/17
Under £10,000	2	3
£10,001 - £25,000	1	15
£25,001 - £50,000	3	43
£50,001 - £100,000	1	43
£100,001 - £150,000	0	0
Total	7	104

Total resource cost for 2017/18 was £194,000 (2016/17: £4,885k)

There were no compulsory redundancies in 2017/18 and 2016/17.

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. One exit package in 2017/18 was not covered by the Civil Service Compensation Scheme. 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 in which 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 (not subject to audit)

Our sickness absence rate for the rolling year (1 April 2017 to 31 March 2018) showed an average of 7.3 days lost per employee and equates to 3.3%. This was against a target of an average of up to 7 days lost, which equates to 3.1% of available working days.

Disability policies (not subject to audit)

During 2017/18, NRW continued our work on the disability agenda. In August 2016, we were awarded Disability Confident Employer status which replaced the Two Tick Scheme. We offer job applicants who declare a disability and who meet the minimum job criteria a guaranteed interview and we are 100% compliant with this commitment.



We have an active Assisted User Group staff network which provides advice and opinion on both existing and new IT and telephony issues for members of staff that have reasonable adjustments made to their workspaces. We have found this group particularly useful due to their ability to test new initiatives such as accessibility to our externally hosted staff surveys.

With an ageing workforce, it is important to us that we recognise and support people suffering with dementia and continue to work closely with the Alzheimer's Society Cymru to achieve accreditation over the next two years. We have dementia friendly objectives in our Equalities Action Plan for 2018/19.



Externally facing we are active on all of the Public Services Boards and are ensuring that the voices of disabled people, along with all other protected characteristics are heard, listened to and acted upon. This will help ensure that our services are accessible to all.

Other employee matters (not subject to audit)

During 2017/18, we concluded the consultation on our new Job Evaluation Scheme. This has seen a significant investment and for the first time brings the whole of NRW onto aligned salaries and pay scales. In concluding this scheme, we worked in partnership with the Trade Unions.

Off-payroll engagements (not subject to audit)

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 £245 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 2018, for more than £245 per day and that last for longer than six months	Number of contractors
The total number of existing engagements as of 31 March 2018	64
of which:	
The number that have existed for less than one year at time of reporting	34
The number that have existed for between one and two years at time of reporting	15
The number that have existed for between two and three years at time of reporting	5
The number that have existed for between three and four years at time of reporting	7
The number that have existed for four or more years at time of reporting	3

For all new off-payroll engagements, or those that reached six months in duration, between 1 April 2017 and 31 March 2018, for more than £245 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.	9
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.	9
The number for whom assurance has been requested	9
of which:	
• The number for whom assurance has been requested and received.	9
• 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

The Welsh Government's Managing Public Money rules require disclosure of losses and special payments by category, type and value where they exceed £300,000 in total and for any individual items of £300,000 or more.

Individual losses of £300,000 or more

A payment of £300,000 was made in settlement of a financial loss claim due to licencing changes implemented under the Restoring Sustainable Abstraction (RSA) programme.

Losses and special payments by category

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

Category or type of loss	2017/18 Number	2017/18 £'000	2016/17 Number	2016/17 £'000
Write-off of irrecoverable debts	72	67	59	107
Write-off of Communities and Nature Project	0	0	0	0
Loss of assets	20	48	6	66
Other losses (cash losses, fruitless payments, unenforceable claims, or gifts)	13	30	6	89
Special payments ¹	9	745	9	825
Total	114	890	80	1,087

¹ Refer to 'compensation for loss of office' in the Remuneration and Staff Report for the details of one of the special payments.

Clare Pillman
Chief Executive and Accounting Officer

Date: 13 July 2018

Certificate and Independent Auditor's Report of the Auditor General for Wales to the National Assembly for Wales

Report on the audit of the financial statements

Opinion

I certify that I have audited the financial statements of Natural Resources Wales for the year ended 31 March 2018 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, including a summary of significant accounting policies. These financial statements have been prepared under the accounting policies set out within them. The financial reporting framework that has been applied in their preparation is applicable law and HM Treasury's Financial Reporting Manual based on International Financial Reporting Standards (IFRSs) as adopted by the European Union.

In my opinion the financial statements:

- give a true and fair view of the state of Natural Resources Wales' affairs as at 31 March 2018 and of its net operating costs for the year then ended; and
- have been properly prepared in accordance with Welsh Ministers' directions issued under the Natural Resources Body for Wales (Establishment) Order 2012.

Basis for opinion

I conducted my audit in accordance with applicable law and International Standards on Auditing in the UK (ISAs (UK)). My responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of my report. I am independent of the body in accordance with the ethical requirements that are relevant to my audit of the financial statements in the UK including the Financial Reporting Council's Ethical Standard, and I have fulfilled my other ethical responsibilities in accordance with these requirements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Conclusions relating to going concern

I have nothing to report in respect of the following matters in relation to which the ISAs (UK) require me to report to you where:

- the use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the Accounting Officer has not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the body's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Other information

The Accounting Officer is responsible for the other information in the annual report and accounts. The other information comprises the information included in the annual report other than the financial statements and my auditor's report thereon. My opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in my report, I do not express any form of assurance conclusion thereon.

In connection with my audit of the financial statements, my responsibility is to read the other information 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 report.

Qualified opinion on regularity

In my opinion, except for the possible effects of the matters described in the below '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.

Basis for qualified regularity opinion

Note 6 to the financial statements records timber income of £19.5 million in 2017-18 (£16 million in 2016-17).

I qualified my 2015-16 and 2016-17 regularity opinion with regard to the award of a series of eight inter-related timber sales contracts. These contracts were terminated on 31 March 2017 and 59 timber sales contracts were let by Natural Resources Wales in 2017-18 to manage its exit from the eight contracts. In 2017-18, Natural Resources Wales received £2.8 million timber income in respect of these 59 timber sales contracts.

I have qualified my 2017-18 regularity opinion in relation to the award of the 59 timber sales contracts as follows:

In letting the 59 timber sales contracts, Natural Resources Wales failed to demonstrate good reason for departing from its own policy of openly marketing timber. Furthermore, Natural Resources Wales did not properly document the decision-making process that led to the award of the transitional contracts in general, and the determination of the transitional volume in particular. As a consequence, I have significant uncertainty that Natural Resources Wales acted in compliance with principles of public law and I have qualified my regularity opinion accordingly.

Under Natural Resources Wales' framework of authority it is required to refer any activities which appear novel, contentious and/or repercussive to its sponsor department within the Welsh Government. Natural Resources Wales did not refer its decision to enter into the 59 timber sales contracts, which I consider to be novel, contentious and/or repercussive, to its sponsor department. Furthermore, thirteen of the contracts were not authorised in accordance with Natural Resources Wales'

Scheme of Delegation. I therefore consider the transactions relating to these contracts to be unlawful and I have qualified my regularity opinion accordingly. I have seen no evidence that Natural Resources Wales took into consideration the market price of the timber being sold within the 59 timber sales contracts, when determining the contract prices. I therefore have significant uncertainty as to whether Natural Resources Wales complied with the requirements of both its own Establishment Order and state aid rules and I have qualified my regularity opinion accordingly.

Further details on these matters are set out in my accompanying Report on pages 59 to 62.

Report on other requirements

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 the Natural Resources Body for Wales (Establishment) Order 2012.

In my opinion, based on the work undertaken in the course of my audit:

- the information given in the Governance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and the Governance Statement has been prepared in accordance with Welsh Ministers' guidance;
- the information given in the Annual Report for the financial year for which the financial statements are prepared is consistent with the financial statements and the Annual Report has been prepared in accordance with Welsh Ministers' guidance.

Matters on which I report by exception

In the light of the knowledge and understanding of the body and its environment obtained in the course of the audit, I have not identified material misstatements in Annual Report or the Governance Statement.

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

- proper 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.

Responsibilities

Responsibilities of the Accounting Officer for the financial statements

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 the Natural Resources Body for Wales (Establishment) Order 2012

and Welsh Ministers' directions made there under, for being satisfied that they give a true and fair view and for such internal control as the Accounting Officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Accounting Officer is responsible for assessing the body's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless deemed inappropriate.

Auditor's responsibilities for the audit of the financial statements

My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of the auditor's responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website www.frc.org.uk/auditorsresponsibilities. This description forms part of my auditor's report.

Responsibilities for regularity

The Accounting Officer is responsible for ensuring the regularity of financial transactions.

I obtain sufficient evidence 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.

Huw Vaughan Thomas
Auditor General for Wales
16 July 2018

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.
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 55 to 58 contains my opinion that the financial statements give a 'true and fair view'.
4. My certificate also includes my 'regularity' opinion, ie 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. I qualified my regularity opinion on NRW's 2015-16 and 2016-17 accounts on the basis that the agreement of eight inter-related long-term timber sales contracts with a sawmill operator (the Sawmill Operator) did not comply with the framework of authority under which NRW was operating. Furthermore, on the basis of the information provided by NRW in relation to its decision-making procedure. I was also unable to satisfy myself that the decision to agree those contracts was lawful and did not involve the provision of State Aid.
5. This year I have qualified my regularity opinion on NRW's 2017-18 accounts. This relates to the award by NRW of 59 new timber sales contracts to the Sawmill Operator, a timber harvesting company owned by the Sawmill Operator and a further timber harvesting company. The reasons for my qualification are set out in paragraph 13.

Background

6. In May 2014, NRW entered into a Memorandum of Agreement with the Sawmill Operator. The Memorandum of Agreement related to eight long-term connected timber sales contracts.
7. Under the terms and conditions of the Memorandum of Agreement, which was also reflected in some but not all of the contracts), the Sawmill Operator agreed to construct and operate a new saw line at its sawmill by 31 March 2016, (which was subsequently extended by agreement to 31 March 2017). Under the terms

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.'

and conditions of the Memorandum of Agreement, if the saw line was not constructed and operating by this date the contracts would terminate. In February 2017, the Sawmill Operator informed NRW that it did not intend to construct the saw line.

8. In March 2017, NRW entered into negotiations with the Sawmill Operator with the view to putting in place transitional contractual arrangements to take effect from 31 March 2017 when the long-term contracts terminated. The proposal was to offer the Sawmill Operator short-term contracts to cover the transitional period between the termination of the long-term contracts and NRW remarketing the timber volume in the terminated long-term contracts. These new contracts would be awarded without seeking competition from the market.
9. By 31 March 2017, NRW reached an agreement in principle with the Sawmill Operator. However, on that date NRW was contacted by a timber harvesting company which had acted as the harvesting agent on the terminated long-term contracts (the Timber Harvesting Company). The Timber Harvesting Company, which is a completely separate organisation to the Sawmill Operator, asked to be included in the contractual arrangements to be put in place from 1 April 2017. NRW agreed to award some of the transitional contracts to the Timber Harvesting Company.
10. The long-term contracts terminated on 31 March 2017 and during 2017-18 NRW entered into 59 transitional contracts. Twenty one of the transitional contracts were awarded to the Sawmill Operator (and a timber harvesting company owned by it).
The remaining 38 contracts were awarded to the Timber Harvesting Company.
11. NRW's 2017-18 financial statements record that NRW received timber income of £2.76 million in respect of the 59 transitional contracts. NRW anticipates that it will receive a further £0.18 million in 2018-19. These figures represent the net sales price of the timber after contractor deductions for harvesting and haulage.

Conclusions

12. In auditing NRW's 2017-18 financial statements, I considered the regularity of the transactions included within those accounts relating to the transitional contracts. I have doubt as to whether NRW acted in accordance with its statutory duties, public law principles and State Aid rules in awarding 59 timber sales contracts to three contractors during 2017-18. In consequence, I am unable to positively affirm that the transactions in NRW's 2017-18 financial statements conform to the framework of authority governing them. I have therefore qualified my regularity opinion accordingly.
13. My reasons for reaching this conclusion is as follows:
 - For a decision of a public body to be lawful it must be made in accordance with applicable legislation and with public law principles. Public bodies must (a) take into account and (b) follow relevant policies, unless they have a good reason to depart from them. At the very least they must have stated clear reasons for the departures. NRW departed from its own policy as set out in its published Timber Marketing Plan 2017-22 when it entered into 59 timber sales contracts without openly marketing the timber. NRW

has been unable to demonstrate that it had good reason to depart from its stated policy.

- Public law requires public bodies to take into account all relevant considerations and disregard irrelevant considerations when taking decisions. One way in which public bodies can demonstrate that they have complied with this principle is by fully documenting the considerations they have taken into account. NRW failed to properly document the decision-making process that led to the award of the transitional contracts in general, and the determination of the transitional volume in particular. This means that I now have significant uncertainty as to whether NRW took into account all relevant considerations, and disregarded irrelevant ones.
 - NRW is required to comply with its Framework Document and Managing Welsh Public Money, which together require NRW to refer novel, contentious and or repercussive proposals to the Welsh Government. I consider that the proposal to enter into the transitional contracts was novel, contentious and/or repercussive. NRW entered into the transitional contracts without making a referral to the Welsh Government and in consequence I consider that NRW did not meet this requirement.
 - NRW's Board made a Scheme of Delegation under the provisions of the Natural Resources Body for Wales Establishment Order 2012 (the Order). This Scheme of Delegation grants delegated powers to specified NRW office holders to agree timber sales contracts on behalf of NRW. Thirteen of the transitional contracts were not authorised in accordance with the Scheme of Delegation, and I therefore consider that they were not entered into lawfully.
 - Article 8 of the Order states that in considering whether or not to exercise any power conferred upon it by or under any enactment, NRW must take into account the likely costs and benefits of the exercise or non-exercise of that power'. I have seen no evidence that NRW took into account the market price of the timber being sold within the transitional contracts, when determining the contract prices. In consequence, I am not satisfied that NRW complied with Article 8 of the Order and that it took all relevant factors into account when making its decisions.
 - NRW is required to comply with State Aid rules. I consider that NRW did not follow proper procedures to satisfy itself that its actions complied with State Aid rules when entering into the transitional contracts. It did not seek to ensure that the prices in the contracts were at market rates, and by NRW's own admission it did not consider its own legal advice which had highlighted the risk that the transitional arrangements could have State Aid implications.
14. Whilst my report on NRW's 2017-18 financial statements focusses on the regularity matters set out paragraph 10, in my view, there are wider lessons that NRW needs to learn.

15. In February 2017, NRW was facing a situation where very substantial timber contracts would terminate at the end of March 2017. Alternative arrangements were required to ensure that the ending of these contracts did not have an adverse effect on timber processors and customers, as well as NRW's own income. NRW had to act quickly, but in its haste it did not follow due process and disregarded principles of good governance. My audit found that:
- documentation of the decision-making process was wholly inadequate;
 - it was unclear who had made decisions and the rationale for those decisions;
 - contractual operations commenced in advance of written contracts being signed;
 - communications regarding the transitional arrangements, both internally and with the Welsh Government, were incomplete and on some occasions inaccurate; and
 - the proposal to enter into transitional arrangements was both significant and potentially contentious but was not subjected to proper scrutiny.
- Furthermore, no written reports were made to NRW's Board or Audit and Risk Assurance Committee (ARAC) in respect of this matter.
16. When I reported on NRW's 2015-16 financial statements I was concerned that NRW did not appear to fully accept my criticisms of their actions and sought to downplay their significance. The fact that the issues raised in my report on NRW's 2017-18 financial statements are so similar to those included in my report on NRW's 2015-16 financial statements has confirmed that NRW did not treat the findings of my 2015-16 report sufficiently seriously.
17. I am, however, encouraged that when my auditors informed NRW of the provisional findings of this audit, NRW's response was constructive, there was an acceptance of the seriousness of the matters raised, and a commitment to ensure that rigorous action is taken to ensure both that policies and procedures are improved and that cultural and behavioural issues are addressed.
18. I have not sought to conclude on whether the contracts entered into by NRW in 2017-18 represented value for money. 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.
19. I have provided a supplementary memorandum to the Public Accounts Committee, with further detail on the reasons I have qualified my regularity opinion on NRW's 2017-18 financial statements.

FINANCIAL STATEMENTS
and
NOTES TO THE ACCOUNTS

for 2017/18

Statement of Comprehensive Net Expenditure

For the year ended 31 March 2018

	Note	2017/18 £'000	2016/17 £'000
Staff costs	3	84,131	81,505
Capital works expensed in year	4	23,599	19,402
Other expenditure	5	84,280	81,344
Total operating expenditure		192,010	182,251
Charge income	6	(37,597)	(36,065)
Commercial and other income	6	(27,986)	(25,147)
European and other external funding	6	(890)	(1,681)
Total operating income		(66,473)	(62,893)
Net operating expenditure		125,537	119,358
Financing on pension scheme assets and liabilities	13.3	1,088	1,651
Net expenditure for the year		126,625	121,009
Other comprehensive net expenditure			
Pension actuarial remeasurements	13.3	(9,848)	(6,657)
Revaluation			
Net gain on revaluation		(10,656)	(5,356)
Total comprehensive net expenditure for the year		106,121	108,996

The notes on pages 68 to 97 form part of these accounts.

Statement of Financial Position

As at 31 March 2018

		31 March 2018	*Restated 31 March 2017	*Restated 1 April 2016
	Note	£'000	£'000	£'000
Non-current assets				
Property plant and equipment	7.1	814,430	764,935	745,211
Heritage assets	7.1	6,432	6,432	6,432
Biological assets	7.1	113,125	105,643	102,450
Intangible assets	7.2	14,809	14,939	13,340
Financial assets		95	140	140
Total non-current assets		948,891	892,089	867,573
Current assets				
Assets held for sale		451	938	180
Inventories		798	805	759
Trade and other receivables	9	13,821	12,249	16,496
Cash and cash equivalents	10	43,539	26,801	22,735
Total current assets		58,609	40,793	40,170
Total assets		1,007,500	932,882	907,743
Current liabilities				
Trade and other payables	11	(22,970)	(14,484)	(19,568)
Provisions	12	(1,227)	(823)	(1,582)
Total current liabilities		(24,197)	(15,307)	(21,150)
Assets less current liabilities		983,303	917,575	886,593
Non-current liabilities				
Pension liabilities	13.3	(32,484)	(42,465)	(46,957)
Financial liabilities	8	(39,992)	(39,998)	(39,991)
Total non-current liabilities		(72,476)	(82,463)	(86,948)
Assets less liabilities		910,827	835,112	799,645
Taxpayers' equity and other reserves				
General fund	SoCTE	216,830	203,289	197,532
Revaluation reserve	SoCTE	726,481	674,288	649,070
Pensions reserve	SoCTE	(32,484)	(42,465)	(46,957)
Total taxpayers' equity		910,827	835,112	799,645

* The financial position as at 31st March 2017 and 1st April 2016 has been restated to reflect an adjustment to the valuation of the Forest Estate. Details of the restatement are included in Note 1.10

The notes on pages 68 to 97 form part of these accounts.

Clare Pillman
Chief Executive and Accounting Officer

Date: 13 July 2018

Statement of Cash Flows

For the year ended 31 March 2018

	Note	2017/18 £'000	2016/17 £'000
Cash flows from operating activities			
Net operating expenditure	SoCNE	(125,537)	(119,358)
Adjustment for non-cash transactions		22,568	19,344
(Increase)/Decrease in trade and other receivables	9	(1,612)	4,310
Increase/(Decrease) in trade and other payables	11	7,921	(5,077)
Decrease in provisions	12	(149)	(132)
Net cash flow from operating activities		(96,809)	(100,913)
Cash flows from investing activities			
Purchase of property, plant and equipment	7.1	(3,386)	(3,218)
Purchase of intangible assets	7.2	(2,526)	(4,042)
Proceeds on disposal of property, plant and equipment		1,086	1,165
Net cash flow from investing activities		(4,826)	(6,095)
Cash flows from financing activities			
Grants from Welsh Government	SoCTE	118,373	111,074
Net Financing		118,373	111,074
Net increase in cash and cash equivalents in the period		16,738	4,066
Cash and cash equivalents at the beginning of the period		26,801	22,735
Cash and cash equivalents at the end of the period	10	43,539	26,801

The notes on pages 68 to 97 form part of these accounts.

Statement of Changes in Taxpayers' Equity

For the year ended 31 March 2018

	General Fund £'000	Revaluation Reserve £'000	Pension Reserve £'000	Total £'000
Opening balance (Restated)	203,289	674,288	(42,465)	835,112
Comprehensive net expenditure for year	(106,121)	0	0	(106,121)
In-year movement				
In year revaluation	0	63,463	0	63,463
Realised revaluation	11,270	(11,270)	0	0
Actuarial gain on pension scheme	(9,848)	0	9,848	0
Decrease in pension liability	(133)	0	133	0
Total in-year movement	1,289	52,193	9,981	63,463
Funding				
Grants from Welsh Government	118,373	0	0	118,373
Balance at 31 March 2018	216,830	726,481	(32,484)	910,827

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 68 to 97 form part of these accounts.

Comparative figures for the year ended 31 March 2017 (Restated)

	General Fund £'000	Revaluation Reserve £'000	Pension Reserve £'000	Total £'000
Opening balance	197,532	655,860	(46,957)	806,435
Correction to Opening Balance	0	(6,790)	0	(6,790)
Opening Balance (Restated)	197,532	649,070	(46,957)	799,645
Comprehensive net expenditure for year	(108,996)	0	0	(108,996)
In-year movement				
In year revaluation	0	33,349	0	33,349
Correction to in year revaluation	0	40	0	40
Realised revaluation	8,171	(8,171)	0	0
Actuarial gain on pension scheme	(6,657)	0	6,657	0
Increase in pension liability	2,165	0	(2,165)	0
Total in-year movement	3,679	25,218	4,492	33,389
Funding				
Grants from Welsh Government	111,074	0	0	111,074
Balance at 31 March 2017 (Restated)	203,289	674,288	(42,465)	835,112

Note 1 Accounting policies

1.1 Requirement to prepare accounts

The financial statements have been prepared in accordance with the 2017/18 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, and intangible non-current assets to fair value as determined by the relevant accounting standard.

These financial statements are based on the going concern principle.

1.3 Grant in aid

Grant in aid and other grants received from Welsh Government are treated as financing received from a controlling party. The receipts are recorded as a financing transaction and are credited directly to the general reserve in the Statement of Financial Position and not through the Statement of Comprehensive Net Expenditure.

1.4 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. To correspond to accounting treatment by Welsh Government, the net value of windfarm option fees after deducting the payment to Welsh Government, is shown within renewable energy income in note 6.

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 other grant contributions received is recognised as income within the Statement of Comprehensive Net Expenditure.

1.5 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.

1.6 Internal drainage districts

NRW acts as the drainage board that runs fourteen internal drainage districts in 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 drainage rates, special levies and precepts for 2017/18 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

Effective in these financial statements

All International Financial Reporting Standards (IFRS), interpretations and amendments effective during this reporting period have been adopted in these statements.

Effective for future financial years

IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors, requires disclosures in respect of new IFRSs, amendments and interpretations that are, or will be applicable after the reporting period. There are a number of IFRSs, amendments and interpretations that have been issued by the International Accounting Standards Board that are effective in future reporting periods. Those with relevance to Natural Resources Wales are outlined below. Natural Resources Wales has not adopted any new IFRS standards early and will apply the standards upon formal adoption in the FReM.

IFRS 15 – Revenue from Contracts with Customers

This standard replaces all existing IFRS guidance on revenue recognition. It is effective from 1 January 2018 and has been incorporated into the 2018/19 Financial Reporting Manual. The core principle of IFRS 15 is that an entity recognises services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. It also introduces substantially greater disclosure requirements to address the shortcomings of the previous Standards (IAS 1 and IAS 18). The impact of this standard on Natural Resources Wales' financial statements is currently being assessed.

IFRS 9 – Financial Instruments

This standard includes a number of improvements to the previous standard IAS 39, to simplify the reporting of financial instruments so as to provide users with more useful information about an entity's credit losses at all times. This is effective from 1 January 2018 and has been incorporated into the 2018/19 Financial Reporting Manual. The impact of this standard on Natural Resources Wales' financial statements is currently being assessed.

IFRS 16 – Leases

This standard is effective from 1 January 2019. It will supersede all existing IFRS standards on leases. It is likely to result in a uniform accounting treatment for all leases, with the distinction between operating and finance leases removed. IFRS 16 is expected to have an impact in financial reporting terms which will be assessed when further guidance is forthcoming from HM Treasury.

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.

1.10 Prior periods restatement

An error was discovered in a valuation report provided to NRW by an external valuer which impacts on the Property, Plant and Equipment value under Non-current assets as at both 31 March 2016 and 31 March 2017. This was due to the solum value in one area of the Forest Estate being overstated by £6,750k. The error has been corrected by restating each of the affected financial statements line items for the prior years as follows:

Statement of Financial Position

	31st March 2017 £'000	1st April 2016 £'000
Non Current Assets		
Property Plant and Equipment Reported	771,685	752,001
Property Plant and Equipment Correction	(6,750)	(6,790)
Property Plant and Equipment Restated	<u>764,935</u>	<u>745,211</u>
Revaluation Reserve		
Reported	681,038	655,860
Correction	(6,750)	(6,790)
Restated	<u>674,288</u>	<u>649,070</u>

Statement of Changes In Taxpayers' Equity

Comparative figures for the year ended 31 March 2017

	Closing Balance 2016/17 £'000	Opening Balance 2016/17 £'000
Revaluation Reserve		
Reported	681,038	655,860
15/16 Correction	(6,790)	(6,790)
16/17 Correction	40	0
Restated	<u>674,288</u>	<u>649,070</u>

2. Analysis of net operating expenditure by segment

For the year ended 31 March 2018

	OD & People Management	Finance & Corporate Services	Operations North & Mid Wales	Operations South	Evidence, Policy & Permitting	Office of the Chief Executive & Transformation	Centrally Controlled	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Reported by segments								
Expenditure	1,880	36,964	64,390	29,690	40,188	3,873	15,025	192,010
Income	0	(35,691)	(29,515)	(2,157)	(1,584)	0	2,474	(66,473)
Total	1,880	1,273	34,875	27,533	38,604	3,873	17,499	125,537
Capital expenditure	0	4,396	1,772	174	129	0	0	6,471

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

OD & People Management	Provides organisational development and people management services.
Finance & Corporate Services	Provides financial, ICT, legal and procurement support. Manages buildings and fleet.
Operations North & Mid Wales	Delivers sustainable management of natural resources at an operational level within North and Mid Wales. Also provides capital programme management and commercial operations for the whole of Wales.
Operations South	Delivers sustainable management of natural resources at an operational level and via a network of local teams, within the counties of South Wales. Also delivers planning and marine services for the whole of Wales.
Evidence, Policy and Permitting	Manages the strategic, environmental and spatial planning functions, permitting and flood and coastal risk management.
Office of the Chief Executive and Transformation	The Office of the Chief Executive includes governance, audit and risk assurance, secretariat, external relations and communications, customer contact centre, and transformation.
Centrally Controlled	Income and expenditure controlled centrally and not allocated to directorates. It includes depreciation, book value of fellings, year end accruals for provisions.

Although reported separately to management, Chief Executive, External Relations and Communications, and Transformation are within the same directorate (Office of the Chief Executive) and therefore have been aggregated here. The expenditure in the Office of the Chief Executive is 2% of the total expenditure.

Analysis of net operating expenditure by segment (continued)

Comparative figures for the year ended 31 March 2017 (Restated)

	OD & People Management	Finance & Corporate Services	Operations North & Mid Wales	Operations South	Evidence, Policy & Permitting	Office of the Chief Executive & Transformation	Centrally Controlled	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Reported by segments								
Expenditure	7,185	29,238	58,069	29,598	36,727	4,049	17,385	182,251
Income	0	(35,423)	(25,873)	(2,269)	(1,697)	(77)	2,446	(62,893)
Total	7,185	(6,185)	32,196	27,329	35,030	3,972	19,831	119,358
Capital expenditure	0	6,315	211	376	358	0	0	7,260

3. Staff costs

Further details of staff costs and numbers are now disclosed from page 48 within the Accountability Report.

	2017/18			2016/17
	Permanent Staff £'000	Other Staff £'000	Total £'000	Total £'000
Wages and salaries	54,930	9,375	64,305	62,051
Social security & Other taxation costs	5,633	912	6,545	5,855
Other pension costs	11,702	7,040	18,742	13,260
Total net salary costs	72,265	17,327	89,592	81,166
Other expenditure for staff			(810)	5,547
Less amounts charged to capital projects			(4,651)	(5,208)
Total staff costs			84,131	81,505

4. Capital works expensed in year

	2017/18	2016/17	31 March 2018	31 March 2017
Categories	Actual £'000	Actual £'000	Committed £'000	Committed £'000
Operational Work	21,922	17,431	7,316	14,323
Capital grants	1,677	1,971	209	692
Total	23,599	19,402	7,525	15,015

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.

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.
- Improvements to reservoirs where the Reservoirs Act 1975 places that responsibility on the reservoir owner. Specifically these measures are taken in the interests of safety.

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

	2017/18	Restated 2016/17
	£'000	£'000
Cash items		
Bought in services	17,064	17,811
Reservoir operating agreements	8,281	5,542
ICT costs	4,837	3,572
Materials and equipment	4,072	3,843
Office running costs	3,604	3,727
Service levels agreements	3,545	6,493
Fleet costs	3,325	3,506
Forest roads network maintenance	2,775	3,320
Grants	2,663	3,251
Rents	2,241	2,089
Staff related costs	2,034	2,075
Collaborative agreements	1,753	2,421
Travel and subsistence	1,155	1,146
Rates	834	840
Fees and court costs	760	1,064
Losses and special payments	738	914
Operational costs	549	630
Statutory audit fees	171	185
European grants	76	100
Finance lease interest	14	33
Sub-total	60,491	62,562
Non-cash expenditure		
Value of sold timber	11,971	7,935
Depreciation, amortisation and impairment	11,702	11,246
Losses	115	173
Movement on other provisions	553	(705)
Movement on provision for doubtful debt	(27)	(63)
(Gain) / Loss on disposal	(525)	196
Sub-total	23,789	18,782
Total	84,280	81,344

Details of write-offs and special payments are shown in the Accountability section on page 54.

The Fleet and Operational expenditure figures for 2016/17 have been restated following the introduction of fleet recharging in 2017/18. The insurance premiums for vehicles and plant were £303k in 2016/17 and they are now included under fleet costs, rather than operational costs.

6. Income analysis

For the year ended 31 March 2018

	2017/18 £'000	2016/17 £'000
Abstraction charges	19,349	17,988
Environmental permitting regulations: water quality	6,364	6,560
Environmental permitting regulations: installations	3,078	3,043
Nuclear regulation	2,458	1,783
Environmental permitting regulations: waste	2,294	2,311
Fishing licences	1,244	1,161
Other environmental protection charges	1,101	1,058
Hazardous waste	657	1,013
Water resources rechargeable works	632	620
Emissions trading and carbon reduction commitment	307	266
Marine licensing	113	262
Charge Income	37,597	36,065
Timber income	19,534	16,070
Renewable energy income	3,640	3,336
Income from estates	2,374	2,720
Internal drainage district income	1,265	1,617
Provision of information and services	726	920
Legal costs recovered and Proceeds of Crime Act income	303	264
Miscellaneous income	103	164
Interest receivable	35	43
Income towards site clean up costs	6	13
Commercial and other income	27,986	25,147
European income ⁺	656	487
Grants and contributions	234	1,194
European and other external funding	890	1,681
Total income	66,473	62,893

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

6.1 Analysis of fees and charges

Year ending 31 March 2018	Income billed £'000	Expenditure £'000	Surplus/ (Deficit) £'000
Abstraction charges	19,098	19,349	(251)
Environmental permitting regulations: water quality	6,455	6,364	91
Environmental permitting regulations: installations	3,093	3,078	15
Nuclear regulation	2,460	2,458	2
Environmental permitting regulations: waste	2,140	2,294	(154)
Fishing licences	1,244	1,244	0
Other environmental protection charges	1,081	1,101	(20)
Hazardous waste	904	657	247
Water resources rechargeable works	632	632	0
Emissions trading and carbon reduction commitment	296	307	(11)
Marine licences	113	113	0
Total	37,516	37,597	(81)

Comparative figures - year ending 31 March 2017	Income billed £'000	Expenditure £'000	Surplus/ (Deficit) £'000
Abstraction charges	18,219	17,988	231
Environmental permitting regulations: water quality	6,643	6,560	83
Environmental permitting regulations: installations	3,090	3,043	47
Nuclear regulation	1,758	1,783	(25)
Environmental permitting regulations: waste	2,177	2,311	(134)
Fishing licences	1,161	1,161	0
Other environmental protection charges	966	1,058	(92)
Hazardous waste	1,006	1,013	(7)
Water resources rechargeable works	620	620	0
Emissions trading and carbon reduction commitment	262	262	0
Marine licences	280	266	14
Total	36,182	36,065	117

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 depreciation 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 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 – regulation of deposits, removals, construction projects on or under the sea bed and all forms of dredging.
- 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, flood defence consents, reservoir compliance, development planning advice 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. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, if appropriate.

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 costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. They are not revalued and are transferred to the appropriate non-current asset category when completed and ready for use.

Indexation and Revaluation

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 last professionally revalued at 31 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, were 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 were quality assured by the NRW Principal Surveyor. All valuers had 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 last valued at 31 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. External professional surveyors were used for those assets where we have future rental income on our land. Cefn Croes Windfarm was valued by Bidwells and the telecommunications portfolio by Strutt & Parker.

For specialised assets where there are no market comparables, '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. Typically these assets include flood risk management works such as gauging stations and water resource assets such as boreholes. These assets are accounted for in the Statement of Financial Position at depreciated replacement costs.

In between professional revaluations, the forest estate, land, buildings, operational structures and biological assets are indexed annually using an appropriate index.

Where movement in the indices for plant and machinery, information technology and intangible assets are material, these assets are re-valued under the modified historical cost convention.

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 and amortisation

Land (forest estate and non-forest land) and intangible rights to land are not depreciated, unless the land 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 useful lives used for depreciation purposes are:

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

The range in the useful lives above 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 gain or loss on disposal. 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 carrying amount of the assets and depreciation based on the asset's original 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, a loss in economic benefit or reduction of service potential. 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 only those impairment losses that do not result from a clear consumption of economic benefit or reduction of service potential should be 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. Impairment losses that arise from a clear consumption of economic benefit or reduction in service potential should be taken in full to the Statement of Comprehensive Net 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 and a sale within 12 months of the reporting date is considered to be highly probable. Management is committed to a plan to sell and the asset is being actively marketed in its present condition at a price which is reasonable in relation to its current condition.

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 and are recorded as current assets in the Statement of Financial Position.

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 2017 (Restated)	626,724	54,418	14,484	22,153	13,320	72,855	818	804,772	105,643	6,432	916,847
Additions	0	280	190	1,490	0	1,070	482	3,512	0	0	3,512
Assets commissioned in year	0	0	0	521	96	66	(635)	48	0	0	48
Disposals and derecognition	(1)	(231)	(137)	(2,577)	(186)	(43)	0	(3,175)	0	0	(3,175)
Movement from/(to) held for sale	(28)	317	231	(114)	0	0	0	406	0	0	406
Fellings	(8,802)	0	0	0	0	0	0	(8,802)	(3,162)	0	(11,964)
Indexation and revaluation	53,252	3,834	1,121	0	0	6,534	0	64,741	10,644	0	75,385
Reclassification	0	(6)	0	0	50	(36)	6	14	0	0	14
At 31 March 2018	671,145	58,612	15,889	21,473	13,280	80,446	671	861,516	113,125	6,432	981,073
Depreciation											
At 1 April 2017 (Restated)	0	0	694	15,352	10,205	13,586	0	39,837	0	0	39,837
Charged in year	0	0	820	1,629	3,114	3,188	0	8,751	0	0	8,751
Disposals and derecognition	0	0	(4)	(2,454)	(186)	(11)	0	(2,655)	0	0	(2,655)
Movement from/(to) held for sale	0	0	6	(87)	0	0	0	(81)	0	0	(81)
Indexation and revaluation	0	0	48	0	0	1,173	0	1,221	0	0	1,221
Reclassification	0	0	0	0	48	(35)	0	13	0	0	13
At 31 March 2018	0	0	1,564	14,440	13,181	17,901	0	47,086	0	0	47,086
Carrying amount at 1 April 2017 (Restated)	626,724	54,418	13,790	6,801	3,115	59,269	818	764,935	105,643	6,432	877,010
Carrying amount at 31 March 2018	671,145	58,612	14,325	7,033	99	62,545	671	814,430	113,125	6,432	933,987
Asset Financing											
Owned	625,316	53,486	14,325	6,882	99	62,545	671	763,324	113,125	6,432	882,881
Leased	45,829	5,126	0	151	0	0	0	51,106	0	0	51,106
Carrying amount at 31 March 2018	671,145	58,612	14,325	7,033	99	62,545	671	814,430	113,125	6,432	933,987

Buildings include dwellings with a carrying amount of £291k. Our other buildings are offices and workbases.

The amount held in the Revaluation Reserve for these assets at 31st March 2018 was £725,645k (£673,299k at 31st March 2017 - restated)

Comparative figures for the year ended 31 March 2017 (Restated)

	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 2016	611,803	53,918	12,782	24,373	12,894	67,654	3,185	786,609	102,450	6,432	895,491
Correction to opening valuation	(6,122)	(668)	0	0	0	0	0	(6,790)	0	0	(6,790)
At 1 April 2016 (Restated)	605,681	53,250	12,782	24,373	12,894	67,654	3,185	779,819	102,450	6,432	888,701
Additions	0	2	1,282	1,030	0	304	600	3,218	0	0	3,218
Assets commissioned in year	0	4	0	1,212	426	884	(2,355)	171	0	0	171
Disposals and derecognition	0	(180)	(234)	(4,201)	0	(82)	(612)	(5,309)	0	0	(5,309)
Movement from/(to) held for sale	0	(519)	(365)	(75)	0	0	0	(959)	0	0	(959)
Fellings	(5,872)	0	0	0	0	0	0	(5,872)	(2,109)	0	(7,981)
Indexation and revaluation	26,667	2,099	1,019	0	0	4,081	0	33,866	5,302	0	39,168
Correction to in year revaluation	248	(208)	0	0	0	0	0	40	0	0	40
Reclassification	0	(30)	0	(186)	0	14	0	(202)	0	0	(202)
At 31 March 2017 (Restated)	626,724	54,418	14,484	22,153	13,320	72,855	818	804,772	105,643	6,432	916,847
Depreciation											
At 1 April 2016	0	0	315	17,586	6,063	10,644	0	34,608	0	0	34,608
Charged in year	0	0	579	1,814	4,142	2,512	0	9,047	0	0	9,047
Disposals and derecognition	0	0	(61)	(3,884)	0	(40)	0	(3,985)	0	0	(3,985)
Movement from/(to) held for sale	0	0	(139)	(60)	0	0	0	(199)	0	0	(199)
Indexation and revaluation	0	0	0	0	0	464	0	464	0	0	464
Reclassification	0	0	0	(104)	0	6	0	(98)	0	0	(98)
At 31 March 2017	0	0	694	15,352	10,205	13,586	0	39,837	0	0	39,837
Carrying amount at 1 April 2016 (Restated)	605,681	53,250	12,467	6,787	6,831	57,010	3,185	745,211	102,450	6,432	854,093
Carrying amount at 31 March 2017 (Restated)	626,724	54,418	13,790	6,801	3,115	59,269	818	764,935	105,643	6,432	877,010
Asset Financing											
Owned (Restated)	583,800	49,578	13,790	6,351	3,115	59,269	818	716,721	105,643	6,432	828,796
Leased (Restated)	42,924	4,840	0	450	0	0	0	48,214	0	0	48,214
Carrying amount at 31 March 2017 (Restated)	626,724	54,418	13,790	6,801	3,115	59,269	818	764,935	105,643	6,432	877,010

Buildings include dwellings with a carrying amount of £290k. Our other buildings are offices and workbases.
The amount held in the Revaluation Reserve for these assets at 31st March 2017 was £673,299k (Restated)

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 was valued as appropriate for obtaining a fair value. In the intervening years, custom indices are provided by Clegg & Co and 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 2018. 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 2018 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/guidance-and-advice/environmental-topics/wildlife-and-biodiversity/find-protected-areas-of-land-and-seas/national-nature-reserves/?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 2017	6,790	2,456	11,796	472	1,661	23,175
Additions	174	0	388	5	2,392	2,959
Assets commissioned in year	0	0	1,613	0	(1,661)	(48)
Disposals and derecognition	(45)	0	(92)	0	0	(137)
Indexation and revaluation	0	0	0	0	0	0
Reclassification	1,220	(102)	(1,132)	0	0	(14)
At 31 March 2018	8,139	2,354	12,573	477	2,392	25,935
Amortisation						
At 1 April 2017	3,359	83	4,699	95	0	8,236
Charged in year	1,233	9	1,583	126	0	2,951
Disposals and derecognition	(47)	0	(1)	0	0	(48)
Indexation and revaluation	0	0	0	0	0	0
Reclassification	225	(60)	(178)	0	0	(13)
At 31 March 2018	4,770	32	6,103	221	0	11,126
Carrying Amount at 1 April 2017	3,431	2,373	7,097	377	1,661	14,939
Carrying Amount at 31 March 2018	3,369	2,322	6,470	256	2,392	14,809
Asset Financing						
Owned	3,369	2,322	6,470	256	2,392	14,809
Carrying Amount at 31 March 2018	3,369	2,322	6,470	256	2,392	14,809

The amount held in the Revaluation Reserve for these assets at 31st March 2018 was £836k (£989k at 1st April 2017)

Comparative figures for the year ended 31 March 2017

	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 2016	5,895	2,419	4,392	161	6,461	19,328
Additions	124	16	2,551	189	1,162	4,042
Assets commissioned in year	643	0	4,853	122	(5,789)	(171)
Disposals and derecognition	(44)	(9)	0	0	(173)	(226)
Indexation and revaluation	0	0	0	0	0	0
Reclassification	172	30	0	0	0	202
At 31 March 2017	6,790	2,456	11,796	472	1,661	23,175
Amortisation						
At 1 April 2016	2,257	56	3,643	32	0	5,988
Charged in year	1,048	30	1,058	63	0	2,199
Disposals and derecognition	(44)	(3)	(2)	0	0	(49)
Indexation and revaluation	0	0	0	0	0	0
Reclassification	98	0	0	0	0	98
At 31 March 2017	3,359	83	4,699	95	0	8,236
Carrying Amount at 1 April 2016	3,638	2,363	749	129	6,461	13,340
Carrying Amount at 31 March 2017	3,431	2,373	7,097	377	1,661	14,939
Asset Financing						
Owned	3,431	2,373	7,097	377	1,661	14,939
Carrying Amount at 31 March 2017	3,431	2,373	7,097	377	1,661	14,939

8. Financial liabilities and instruments

8.1 Financial liability

The financial liability of £39,992k 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.

£5,544k was paid to Dŵr Cymru Welsh Water during 2017/18 (2016/17: £5,332k) 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 2018 £'000	31 March 2017 £'000
Accrued income	5,572	3,367
Trade receivables	3,835	3,700
Provision for doubtful debt	(323)	(350)
VAT receivable	2,617	3,763
Prepayments	1,692	1,607
Other receivables	222	139
Deposit	206	23
Total	13,821	12,249

10. Cash and cash equivalents

	31 March 2018 £'000	31 March 2017 £'000
Opening balance	26,801	22,735
Net change in cash and cash equivalent balances	16,738	4,066
Total	43,539	26,801

The following balances were held at 31 March

Government Banking Service	35,078	18,906
Other bank accounts	8,460	7,894
Cash in hand	1	1
Total	43,539	26,801

Cash and cash equivalents include cash in hand and financial provisions (see note 1.8) which are held in Government Banking Service and Barclays bank accounts. Financial provisions are not available for use by NRW.

11. Trade and other payables

	31 March 2018 £'000	31 March 2017 £'000
Trade payables accrual	10,698	3,867
Deferred income	6,671	6,687
Holiday pay	1,845	1,622
Trade payables	1,671	291
Bonds and deposits	1,421	1,425
Finance leases	487	458
Other payables	177	134
Total	22,970	14,484

12. Provisions

	Early departure costs	Other	Total
	£'000	£'000	£'000
Balance at 1 April 2017	205	618	823
Provided in the year	0	1,116	1,116
Released in year	0	(40)	(40)
Used in the year	(149)	(523)	(672)
Balance at 31 March 2018	56	1,171	1,227
Estimated timing of discounted cash flows			
Due within one year	31	1,171	1,202
Due between one and five years	25	0	25
Total	56	1,171	1,227

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.

Provision for early departure costs consist of annual compensation payments to former staff who left under legacy bodies' early retirement programmes.

Other provisions include £917k of grant offers to fund work to be undertaken up to 31 March 2018 but which will not to be claimed until June 2018 and £254k for other claims. It is expected that all of these will be paid within the next twelve months.

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 4.6% and 8.05% for members of classic, premium, classic plus, nuvos and 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 8% and 14.75% (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 0.5% of pensionable salary 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 1 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, primarily governed by the LGPS Regulations 2013 and the LGPS (Transitional Provisions, Savings and Amendment) Regulations 2014. 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 £10.978 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 2016. The assets taken at market value (£2.7 billion) were sufficient to cover 103% of the value of liabilities in respect of past service benefits which had accrued to members. NRW accepted the independent actuary's recommendation in respect of future employer contributions. The next triennial actuarial valuation will be as at 31 March 2019 and will be used to set employer contribution rates for the three-year period starting 1 April 2020.

The annual report and financial statements for the EAPF estimated that it had sufficient assets to meet 102% of its expected future liabilities at 31 March 2018 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 real terms discount rate in these financial statements is therefore 1.1% lower than the rate used in the EAPF financial statements. This lower rate results in a higher value being placed on liabilities. 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 2.1% per annum. The estimated contribution payable by NRW, excluding any discretionary lump sum payments, for the year to 31 March 2019 will be approximately £2.289 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 2016 updated to 31 March 2018. The assumptions underlying the calculation of a net liability at 31 March 2018 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 2018	31 Mar 2017
	% p.a.	% p.a.
Pension Increase Rate	2.10%	2.10%
Salary Increase Rate	2.40%	2.40%
Discount Rate	2.70%	2.60%

Average future life expectancy at 65	Males	Females
Current Pensioners	22.6 years	24.4 years
Future Pensioners (People aged 65 in 20 years)	24.3 years	26.7 years

13.2 Fair Value of Assets for the year ended 31 March 2018

Asset Category	31 March 2018 (£'000)				
	Quoted	Unquoted	Undetermined	Total	%
Equity Securities:					
Common Stock	82,482	166	0	82,648	24%
Preferred Stock	26	0	0	26	0%
Rights/Warrants	0	0	0	0	0%
Other Equity Assets	276	0	0	276	0%
Debt Securities:					
UK Government Bonds	0	33,902	0	33,902	10%
Corporate Bonds	0	29,442	0	29,442	9%
Other	0	1,698	315	2,013	1%
Pooled Investment Vehicles:					
Equities	0	0	40,940	40,940	12%
Bonds	27,659	0	32,798	60,457	18%
Funds - Common Stock	2,269	0	26,019	28,288	8%
Funds - Real Estate	422	1,763	9,360	11,544	3%
Funds - Venture Capital	0	44	0	44	0%
Venture Capital and Partnerships:					
Partnerships & Real Estate	0	42,558	0	42,558	12%
Other Investment:					
Stapled Securities	458	0	0	458	0%
Derivative Contracts:					
Equity Derivatives - Futures	(43)	0	0	(43)	0%
Forward FX Contracts	0	87	0	87	0%
Cash and Cash equivalents					
All	0	0	8,502	8,502	3%
Totals	113,548	109,659	117,934	341,141	100%

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

Period ended 31 March 2018	Assets	Obligations	Net (liability)/ asset
	£'000	£'000	£'000
Fair value of employer assets	323,540	0	323,540
Present value of liabilities	0	366,005	(366,005)
Present value of unfunded liabilities	0	0	0
Opening Position as at 31 March 2017	323,540	366,005	(42,465)
Service cost			
- Current service cost*	0	10,978	(10,978)
- Past service cost (including curtailments)	0	0	0
- Effect of settlements	0	0	0
Total service cost	0	10,978	(10,978)
Net interest			
- Interest income on plan assets	8,502	0	8,502
- Interest cost on defined benefit obligation	0	9,590	(9,590)
- Impact of asset ceiling on net interest	0	0	0
Total net interest	8,502	9,590	(1,088)
Total defined benefit cost recognised in Profit or (Loss)	8,502	20,568	(12,066)
Cashflows			
- Plan participants' contributions	1,962	1,962	0
- Employer contributions	12,199	0	12,199
- Contributions in respect of unfunded benefits	0	0	0
- Benefits paid	(6,710)	(6,710)	0
- Unfunded benefits paid	0	0	0
Effect of business combinations and disposals	0	0	0
Expected closing position	339,493	381,825	(42,332)
Remeasurements			
- Change in demographic assumptions	0	0	0
- Change in financial assumptions	0	(8,200)	8,200
- Other experience	0	0	0
- Return on assets excluding amounts included in net interest	1,648	0	1,648
- Changes in asset ceiling	0	0	0
Total remeasurements recognised in Other Comprehensive Income (OCI)	1,648	(8,200)	9,848
Exchange differences	0	0	0
Fair value of employer assets	341,141	0	341,141
Present value of funded liabilities	0	373,625	(373,625)
Present value of unfunded liabilities	0	0	0
Closing position as at 31 March 2018	341,141	373,625	(32,484)

* The current service cost includes an allowance for administration expenses of 0.6% of payroll.

13.4 Sensitivity analysis

Change in assumptions at 31 March 2018:	Approximate % increase to employer liability	Approximate monetary amount (£000)
0.5% decrease in Real Discount Rate	11%	42,946
0.5% increase in the Salary Increase Rate	2%	9,134
0.5% increase in the Pension Increase Rate	9%	33,181

13.5 Duration of defined benefit obligation

The duration of the defined benefit obligation (i.e. the weighted average of the time until payment of future cash flows) for scheme members calculated at the last triennial valuation as at 31st March 2016 was calculated by the actuary as 20.4 years.

14. Capital commitments

	31 March 2018 £'000	31 March 2017 £'000
Property plant and equipment		
Plant and machinery	77	312
Transport equipment	82	0
Operational structures	1,311	481
Total	1,470	793
Intangible assets		
Information technology - software licences	0	6
Information technology - software development	351	195
	351	201

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 2018			
	Land	Buildings	Vehicles	Total
	£'000	£'000	£'000	£'000
Obligations under operating leases are:				
Not later than one year	79	1,397	248	1,724
Later than one year and not later than five years	196	2,258	449	2,903
Later than five years	1,760	191	0	1,951
Total value of obligations	2,035	3,846	697	6,578

	31 March 2017 (Restated)*			
	Land	Buildings	Vehicles	Total
	£'000	£'000	£'000	£'000
Obligations under operating leases are:				
Not later than one year	109	1,787	394	2,290
Later than one year and not later than five years	267	3,433	687	4,387
Later than five years	1,684	202	0	1,886
Total value of obligations	2,060	5,422	1,081	8,563

* Following a review of land and building operating leases which was undertaken during the year, some leases were reclassified and the break clause for one lease was corrected. The 31 March 2017 figure has been amended from £10,595k to £8,563k.

15.2 Finance leases

Obligations under finance leases are:

Not later than one year	13
Later than one year and not later than five years	41
Later than five years	365
Total value of obligations	419

31 March 2018		
Land	Vehicles	Total
£'000	£'000	£'000
13	68	81
41	0	41
365	0	365
419	68	487

Obligations under finance leases are:

Not later than one year	13
Later than one year and not later than five years	38
Later than five years	209
Total value of obligations	260

31 March 2017		
Land	Vehicles	Total
£'000	£'000	£'000
13	129	142
38	69	107
209	0	209
260	198	458

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 2018 are :

	31 March 2018	31 March 2017
	£'000	£'000
Not later than one year	11,606	8,033
Later than one year and not later than five years	16,712	20,734
Later than five years	268	201
Total	28,586	28,968

17. Lease receivables

Assets (land and buildings) which are leased to external parties under an operating lease are capitalised in accordance with the non-current assets policy which is 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 2018	Restated* 31 March 2017
	£'000	£'000
Not later than one year	1,035	1,112
Later than one year and not later than five years	3,362	3,615
Later than five years	12,643	12,926
Total	17,040	17,653

* Following a review of lease receivable agreements during the year, Energy Delivery Programme agreements are now included and the 31 March 2017 figures have been restated accordingly from £9,310k to £17,653k.

18. Contingent liabilities

Natural Resources Wales has the following contingent liabilities:

	31 March 2018	31 March 2017
	£'000	£'000
Public and employee liability	151	111
Civil claim	225	0
Total	376	111

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

8 public and employee liability claims have been made against Natural Resources Wales and the amounts are disclosed above. The claims are for damages and personal injury. Formal proceedings has been served for a civil claim by a third party for the use of stones by Natural Resources Wales and one of its predecessor bodies.

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

HMRC Audit

An HMRC audit of Natural Resources Wales' treatment of Construction Industry Scheme and Off-payroll working (IR35) is under way and will continue into 2018/19. In accordance with IAS 37, an unquantifiable contingent liability is disclosed to recognise the possibility of non-compliance liabilities arising from the audit.

Job Evaluation Grievances

In 2018/19 we are considering grievances from staff in relation to job evaluation. This will have an impact on staff related expenditure if any of those grievances are upheld.

Judicial Reviews

Two judicial reviews have been brought against Natural Resources Wales during the year.

The first is by Sundorne Products (Llanidloes) Limited, a subsidiary of Potter's Waste Management Limited in respect of a suspension notice served by NRW on the 18th January 2018 in relation to the company's operation of a landfill site at Bryn Posteg, Llanidloes pursuant to an environmental permit. The suspension notice served pursuant to Regulations 37(1) and (6) of the Environmental Permitting (England and Wales) Regulations 2016 was considered necessary as the operator had accepted significantly more waste material onto it's site than was permitted with a resultant risk of pollution due to landfill gas, odour and emissions to ground and surface waters, and changes in the stability of the landfill. the Notice requires the operator to take steps to remove that risk.

The second judicial review has been brought by Atlantic Recycling Limited in respect of a statutory notice issued by NRW on the 20th February 2018 pursuant to Schedule 5, Part 3, Paragraph 10 of the Transfrontier Shipment of Waste Regulations 2007 requiring the repatriation of waste which had been transported to Poland between 5th May and 5th July 2017. The waste consisted of 1204.6 tonnes of "refuse derived fuel" / "mixed municipal waste". The matter is complex and involves the Environment Agency, the relevant competent authority in Poland and the Polish recipient company, all of which have now been joined to the proceedings as interested parties.

19. Events after the end of the reporting period

There are no events to report after the end of the reporting period.

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 Welsh Government 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 Environment Agency, Forestry Commission and HMRC.

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 £'000	Total income £'000	Amount owed by NRW at 31 March 2018 £'000	Amount owed to NRW at 31 March 2018 £'000
Aberystwyth University	Emyr Roberts	Council Member and Chair of the Audit and Risk Committee	0	5	0	0
Canal and River Trust	Ruth Hall	Member of Board in Wales and National Council	0	23	0	0
Cardiff University (Public Policy Institute for Wales)	Ruth Hall	Governor/Vice Chair	8	11	0	0
Cardiff Metropolitan University	Sir Paul Williams	Honorary Fellow	0	1	0	0
DEFRA including: Joint Nature Conservation Committee and Support Company	Diane McCrea/ Madeleine Havard	Board Member of JNCC & Non-Executive Director of JNCC Support Co.				
	Nigel Reader	Independent member of JNCC Audit and Risk Assurance Committee				
DEFRA Audit and Risk Committee	Nigel Reader	Ex-officio member (as Board Member of Natural England and Audit and Risk Assurance Committee)	8	3	0	0
Animal and Plant Health Agency	Nigel Reader	Non-Executive Board Member and Audit and Risk Assurance Committee member				
Leonard Cheshire Disability	Elizabeth Haywood	Board Member and Trustee	0	1	0	0
National Association of Areas of Outstanding Beauty	Howard Davies	Chief Executive	33	0	0	0
National Trust	Ruth Hall	Council Member	201	14	0	0
Natural England	Nigel Reader	Non-Executive Board Member and Audit Committee Chair	106	0	0	0
Wild Ground (formerly known as North East Wales Wildlife Ltd)	Karen Balmer	Trustee	2	0	0	0
North Wales Wildlife Trust	Howard Davies	Trustee and Honorary Vice President	190	0	0	0
SP Energy Network Holding Ltd	Elizabeth Haywood	Non-Executive Director	16	30	0	0
Swansea University	Emyr Roberts	Honorary Professor	282	4	244	0
TGV Hydro Ltd	Chris Blake	Director	37	0	6	0

Annex 1 Corporate Environmental Report



**Cyfoeth
Naturiol
Cymru
Natural
Resources
Wales**

Environmental Management System Corporate Environmental Report 2017/18

Our vision

Proud to be leading the way to a better future for Wales by managing the environment and natural resources of Wales sustainably.

Our purpose

Through the new Environment (Wales) Act 2016, we

- must pursue the sustainable management of natural resources, and;
- apply the principles of sustainable management of natural resources;
...in the exercise of our functions.

Introduction

Our Environmental Management System (EMS) is helping develop NRW into an excellent organisation by maintaining our ISO14001:2015 certification, our forest certification against the UK Woodland Assurance Standard and by reducing our own environmental impact and carbon footprint.

Our focus during this year has been to:

- reduce our carbon footprint – decarbonisation;
- achieve conformity against the UK Woodland Assurance Standard;
- improve the status of designated features, access and interpretation on protected sites we manage;
- reduce the average emissions of cars in the NRW fleet – decarbonisation

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 & Accounts. During the coming years, we will continue to improve our corporate environmental reporting in working towards integrated reporting.

Summary of performance

This year we have:

- met our target to reduce our carbon footprint by 5% in relation to occupied buildings, energy use and business travel;
- retained certification to the UK Woodland Assurance Standard for the Welsh Government Woodland Estate we manage, following independent external audits and verification
- completed 67% of the National Nature Reserve management audit target and ensured any improvement actions identified were implemented
- purchased 22 sub 100 g/km cars and two new electric vehicles

Table 1: Corporate Environmental Report summary table

2015/16	Units	2015/16	2016 /17	2017/18
Greenhouse gas emissions ²	consumption (tCO ₂ e)	6,021	5,115	4,387
Estate energy	consumption (m kWh)	6.9	6.3	6.0
	expenditure (£k)	657	776	618
Estate waste	generated (tonnes)	864	1,424	1,141
	expenditure (£k)	205	225	273
Estate water	consumption (m ³)	78,395	76,283	50,908
	expenditure (£k)	39	32	25

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.

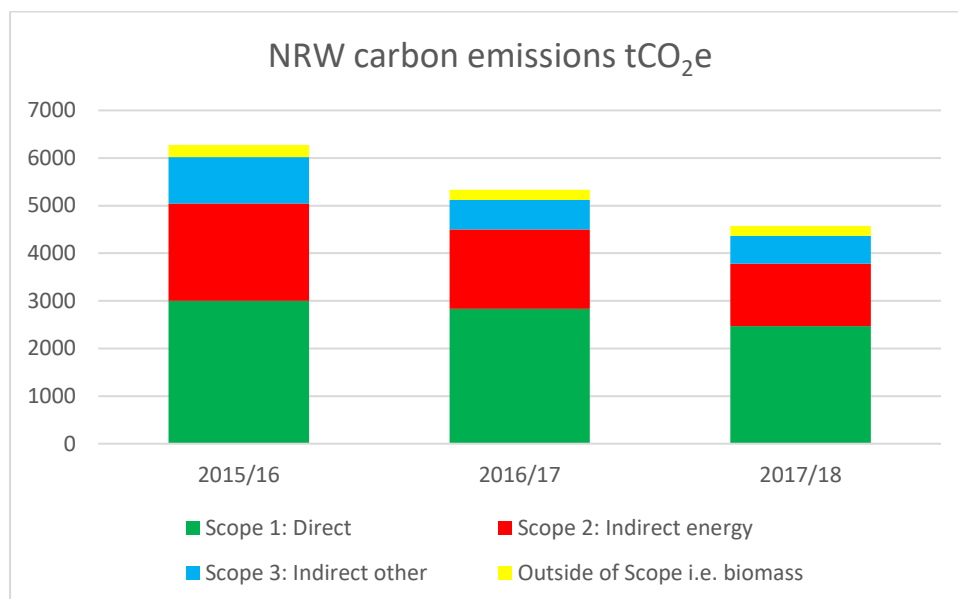
In summary:

- carbon emissions decreased in 2017/18 by 14.2% compared with the previous year
- energy use decreased in 2017/18 by 4.7% compared with the previous year
- waste generated decreased in 2017/18 by 19.9% compared with the previous year
- water consumption decreased in 2017 /18 by 33.3% compared with the previous year

Greenhouse gas emissions

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

Our greenhouse gas emissions are outlined below:



Carbon emissions decreased in 2017/18 by 14.2% compared with the previous year.

Scope 1 direct emissions decreased by 13.0%, due to the decrease in fuel use in badged and operational vehicles and machines.

Scope 2 energy indirect emissions decreased by 20.8%, this was due to the reduction in electricity use in both occupied buildings and unmanned sites.

Scope 3 other indirect emissions decreased by 2.3%, owing to grey vehicle and hire car mileage decreasing.

Table 2: Greenhouse gas emissions

Greenhouse gas emissions	2015/16	2016/17	2017/18
Scope 1: direct emissions (tCO ₂ e)	2,999	2,835	2,466
Scope 2: energy indirect emissions (tCO ₂ e)	2,048	1,662	1,317
Scope 3: other indirect emissions (tCO ₂ e)	974	617	603
Total gross GHG emissions (tCO₂e)	6,021	5,115	4,387
<i>Outside of scopes (i.e. biomass)</i>	253	220	208

Note 1: Data not externally verified – limited assurance.

Note 2: The Scope 3 other indirect greenhouse gas emissions include; train travel, air travel, grey fleet travel, lease car travel, hire car travel, water and waste.

Note 3: Scope 3 emissions from the purchase of goods and services, aggregates use in construction and timber use are not included.

Energy

Our total energy use (which includes electric, mains gas, LPG, heating oil and biomass) in both occupied and unoccupied buildings has decreased by 4.7% based on the previous year's data.

Electricity use in occupied buildings decreased by 9.6%, while electricity used in unmanned sites decreased by 0.8%.

A reduction in biomass and LPG used was mainly due to the installation of a new biomass boiler at our Coed Y Brenin visitor centre.

There were slight increases in mains gas (1.0%) and heating oil (3.5%) used. In the last year we have increased the amount of energy we generate from renewables from 1.4% to 2.2% in our occupied buildings. The increase was mainly due to installation of a hydro power scheme at our Garwnant visitor centre.

In March 2018 we installed photovoltaic panels at five sites and will see the benefit of the energy generated in 2018/19. We also installed LED lighting at 13 sites in 2017 - 2018. Both the photovoltaic panels and LED lighting were funded by the Welsh Governments Invest to Save scheme.

The carbon emission savings were higher than expected due to the DEFRA greenhouse gas conversion factor for UK electricity decreasing further in 2017. This was due to a significant decrease in coal generated electric and an increase in gas and renewables generation.

Table 3: Energy consumption

Resource use – Estate energy	Units	2015/16	2016/17	2017/18
Energy used: Occupied sites	consumption (kWh)	5,550,100	5,209,072	4,918,340
	consumption (tCO ₂ e)	2,011	1,723	1,436
Energy used: Unoccupied sites	consumption (kWh)	1,319,745	1,131,651	1,122,103
	consumption (tCO ₂ e)	610	466	395
Renewable energy: Self-generated	generation (kWh)	81,713	76,649	106,856
	consumption (% of energy used)	1.4%	1.4%	2.2%
Energy used: Total	consumption (kWh)	6,869,845	6,340,723	6,040,443
	consumption (tCO ₂ e)	2,621	2,189	1,830
	expenditure (£k)	657	777	618

Water

Mains water consumption in our offices reduced by 368 cubic metres (6.2%) compared with the previous year. Our water use intensity (m³/FTE) is 3.1, which is below the average of 4.0 for water use ³, and we have set a further reduction target for 2018/19.

The mains water at our non-office sites increased by 851 cubic metres (15.5%) compared with the previous year. This was mainly due to an increase in mains water usage at our Bwlch Nant Yr Arian visitor centre (473 cubic metres increase) and several toilet blocks at Tregaron, Geirionydd and Newborough (362 cubic metres combined increase). The increase was due to an increase in the number of visitors at the respective sites.

Water used to operate our fish hatchery site was the most significant water abstraction use this year, at 36,721 cubic metres. This however was a reduction of 25,968 cubic metres compared with the previous year. This usage was the key factor in total overall water usage reducing by 25,375 cubic metres (33.3%).

Table 4: water consumption

Resource use – estate water	Units	2015/16	2016/17	2017/18
Water supplied - office use: - mains supply - abstraction	consumption (m ³) consumption (m ³)	6,830 3	5,923 15	5,555 22
Water supplied - non-office use: - mains supply - abstraction	consumption (m ³) consumption (m ³)	5,555 65,981	5,488 64,850	6,339 39,014
Water use intensity (for office use)	m ³ per FTE	3.4	3.3	3.1
Water supplied: Total	Consumption (m³)	78,395	76,283	50,908
	Expenditure (£k)	39	32	25
	Consumption (tCO₂e)	27	26	18

Travel

Our travel needs include; travel to manage sites, responding to serious environmental incidents, taking samples, dealing with flooding, site meetings and inter-office travel.

In 2017/18 we travelled 7,269,097 miles a reduction of 889,230 miles (10.9%) compared with the previous year.

³ Average = 4m³ per FTE (Source: Water key performance indicators and benchmarks for offices and hotels. C657 CIRIA www.ciria.org)

This was mainly due to a reduction of 623,867 miles (10.3%) in badged vehicle mileage. This equates to a carbon saving of 133 tCO₂e and a cost saving of over £50,000.

We will continue to reduce inter-office travel using our travel decision tree and by increasing the use of Skype conferencing, which will reduce further the need to travel.

Table 5: Travel detail

Travel by vehicle	Units	2015/16	2016/17	2017/18
Badged vehicles	miles travelled	5,833,839	6,064,812	5,440,945
	expenditure (£k)	800	768	749
Lease vehicles	miles travelled	1,649,345	191,730	0
	Expenditure (£k)	162	18	0
Grey vehicles ⁴	miles travelled	552,343	639,064	590,998
	expenditure (£k)	244	287	266
Hire	miles travelled	256,654	322,505	261,039
	expenditure (£k)	59	74	88
Train	miles travelled	865,693	864,366	938,418
	expenditure (£k)	221	223	183
Air	miles travelled	18,898	71,057	33,661
	expenditure (£k)	6	19	9
Bicycle	miles travelled	1,944	2,346	2,301
	expenditure (£k)	< 1	< 1	< 1
Motorbike	miles travelled	4,475	2,447	1,735
	expenditure (£k)	1	1	1
Total vehicle travel	Miles travelled	9,183,191	8,158,327	7,269,097
	Expenditure (£k)	1,493	1,390	1,291

Waste minimisation and management

Overall waste generated decreased in 2017/18 by 19.9% compared with the previous year.

The office waste to landfill decreased by 11.6%, however the total amount of fly-tipped waste increased by 28.6%. Fly-tip is any waste deposited illegally by third parties on land we manage. Once deposited we become the owners and are responsible for the disposal and associated costs.

The carbon emissions were higher than expected due to the DEFRA greenhouse gas conversion factor for waste to landfill increasing in 2017. This was due to a change in the calculation methodology that is not comparable with previous years.

Table 6: Waste generated

⁴ Grey vehicles are staff's own private vehicles

Waste generated	Units	2015/16	2016/17	2017/18
Office waste landfilled	consumption (tonnes)	266	241	213
	consumption (tCO ₂ e)	122	101	125
	expenditure (£k)	25	22	24
Office waste recycled / reused	consumption (tonnes)	451	934	600
	consumption (tCO ₂ e)	9	20	28
Office waste incinerated	consumption (tonnes)	14	15	27
	consumption (tCO ₂ e)	< 1	< 1	< 1
Fly-tipped waste	consumption (tonnes)	133	234	301
	consumption (tCO ₂ e)	32	65	135
Total waste	Consumption (tonnes)	864	1,424	1,141
	Consumption (tCO₂e)	164	186	274
	Expenditure (£k)	205	225	273

Sustainable procurement

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, to optimise the impacts on the environment, on people and on the local economy."

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.

The approach ensures we link our supply choices to our policy priorities and objectives, making the right choices to help reduce the consumption of primary resources, using materials with fewer negative impacts on the environment and implementing effective performance monitoring and transparency.

Behaviour change

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

Environmental incidents

There have been fifteen environmental incidents because of our work or that of our contractors. This compares with ten environmental incidents in the previous year. There was one high category environmental incident in 2017/18 relating to sea water

ingress to a freshwater reën leading to fish fatalities. No enforcement action will be taken as the incident was caused by asset failure due to third party interference. When incidents occur because of our work (or that of our contractors), we review what has happened, and act to address the root cause of the incident.

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), suppliers data (e.g. train miles) and finance data, using the most accurate source/s we have available. We also look to minimise use of any estimated data in our reporting, and we are working to improve in this area.

Carbon Positive Project

NRW's Carbon Positive Project was funded by the Welsh Government to show leadership in decarbonisation in Wales' public sector and beyond. It has explored how our organisation can address its carbon impact across buildings, transport, land and operational assets and procurement of goods and services.

The Project looks beyond the carbon emissions we currently report on as part of our Environmental Management System (EMS) to understand our wider net carbon status (the balance of our emissions and sequestration). The Project has calculated the net carbon status for NRW, accounting for both greenhouse gas emissions and carbon sequestration across the whole of NRW's estate. The calculation builds upon the information from our EMS to understand the emissions of the organisation in its wider sense, including for example, emissions from the purchase of goods and services, timber production and construction, and to recognise the role of the NRW-managed estate for carbon. A report setting out the approach and the calculation will be published in 2018.

The Project also evaluated the range of potential mitigation measures to reduce our carbon impact as an organisation, seeking input from both staff and other organisations. The evaluation sets out the wide range of potential measures open to NRW and captures the predicted costs, carbon benefit, and wider benefits these measures could provide to NRW as well as exploring the potential scale of adoption across the organisation.

To pilot some of these measures, the Project delivered a series of demonstration projects, including: electric vehicles and charging infrastructure; solar PV on buildings and operational assets; peatland restoration, woodland planting; and trialling carbon planning tools in large procurement frameworks. These helped to inform the feasibility, costs and benefits NRW might see from the adoption of proposed measures.

The opportunities identified through the evaluation of mitigation options will help to build a strategic, costed and prioritised programme of delivery for NRW to address its carbon impact over the next 3-5 years, to steer decarbonisation in NRW moving forward and to embed carbon management across the organisation. This plan will be principally for internal use and will be finalised in 2018.

The Project continues to share its approach and experiences to disseminate best practice and lessons learnt in carbon management across Wales' public sector and to assist in the delivery of Wales' ambition for a carbon neutral public sector by 2030.

Future strategy

Next year we want to:

- reduce our carbon footprint further and have set a target to reduce our carbon dioxide emissions (tCO₂e) from occupied buildings, travel and water use by 5% based on 2017/18 data
- maintain certification against the UK Woodland Assurance Standard (UKWAS) and the ISO14001:2015 environmental standard
- improve the status of designated features, access and interpretation on protected sites we manage
- develop mechanisms for active travel to be the favoured choice of NRW commuter travel and for appropriate business journeys – decarbonisation
- further Improve the organisation's environmental performance

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Proud to be leading the way to a better future for Wales by managing the environment and natural resources sustainably.



Correspondence welcomed in both Welsh and English

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Auditor General for Wales

Supplementary Memorandum of the Auditor General for Wales to the Public Accounts Committee

Timber Sales Contracts awarded by Natural Resources Wales

Date issued: July 2018

Document reference: 623A2018-19

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 2018.

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Supplementary Memorandum – Timber Sales Contracts awarded by NRW

Summary

- 1 On 2 March 2017, I laid before the National Assembly for Wales a report on the accounts of Natural Resources Wales (NRW). The report set out my reasons for qualifying the 2015-16 regularity opinion on NRW's financial statements. At the same time, I provided a supplementary memorandum to the National Assembly for Wales' Public Accounts Committee (PAC) setting out further detail on my reasons for qualifying the regularity opinion. My report and memorandum related to NRW's decision to award eight high value timber sales long-term contracts to a Sawmill Operator in May 2014.
- 2 I found that in entering into the 2014 contracts, NRW:
 - did not comply with its framework of authority, in that it failed to refer the proposal to award the contracts to the Welsh Government as required by the Welsh Government's publication, Managing Welsh Public Money;
 - failed to demonstrate that it complied with public law principles in the decision-making process which resulted in the award of contracts to the Sawmill Operator; in that the decision-making process which led to the award of contracts to the Sawmill Operator was neither robust nor transparent and NRW was unable 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; and
 - it was unclear whether NRW complied with State Aid rules when it entered into contracts with the Sawmill Operator. This uncertainty was created as a consequence of NRW's decision to award the contracts to the Sawmill Operator without conducting any relevant market testing, and NRW being unable to provide persuasive reasoning to support a conclusion that seeking alternative providers would have proved fruitless.
- 3 The PAC carried out its own inquiry into the matters contained within my audit report and published its report in June 2017. The report concluded 'we believe that NRW could and should have ensured that there were good governance arrangements in place in the contracting process, and in failing to establish effective governance arrangements, it is unable to demonstrate how it acted lawfully. We do not believe there is any evidence to demonstrate whether the contracts represent value for money'. The PAC's report recommended that NRW 'undertake a full evaluation of its governance arrangements relating to contracting processes, clearly setting out lessons learned with specific reference to the timber sales contracts referred to in this report'.

- 4 I subsequently qualified my regularity opinion on NRW's 2016-17 financial statements for the same reasons set out in paragraph 2. This was a consequence of the fact that the long-term contracts NRW entered into in May 2014 were still operating and the 2016-17 financial statements included income relating to these contracts.
- 5 A Memorandum of Agreement linked to the eight long-term contracts referred to in my previous report included a requirement for the Sawmill Operator to construct and commence operating a new saw line at its sawmill by 31 March 2016 (which was subsequently extended by agreement to 31 March 2017). Under the terms and conditions of the Memorandum of Agreement (which was also reflected in some but not all of the contracts), if the saw line was not constructed and operating by this date the Memorandum and contracts would terminate. In February 2017, the Sawmill Operator informed NRW that it did not intend to construct the saw line.
- 6 In March 2017, NRW entered into negotiations with the Sawmill Operator with the view to putting in place transitional contractual arrangements to take effect from 31 March 2017 when the long-term contracts terminated. The proposal was to offer the Sawmill Operator short-term contracts to cover the transitional period between the termination of the long-term contracts and NRW remarketing the timber volume in the terminated long-term contracts. These new contracts would be awarded without seeking competition from the market.
- 7 By 31 March 2017, NRW had reached an agreement in principle with the Sawmill Operator. However, on that date NRW was contacted by a timber harvesting company which had acted as the harvesting agent on the terminated long-term contracts (the Timber Harvesting Company). The Timber Harvesting Company, which is a completely separate organisation to the Sawmill Operator, asked to be included in the contractual arrangements to be put in place from 1 April 2017. NRW agreed to award some of the transitional contracts to the Timber Harvesting Company.
- 8 The long-term contracts terminated on 31 March 2017 and during 2017-18 NRW entered into 59 transitional contracts. Twenty one of the transitional contracts were awarded to the Sawmill Operator and a timber harvesting company owned by it, (the Sawmill Operator's timber harvesting company). The remaining 38 contracts were awarded to the Timber Harvesting Company.
- 9 NRW's 2017-18 financial statements record that NRW received timber income of £2.76 million in respect of the 59 transitional contracts. NRW anticipates that it will receive a further £0.18 million in 2018-19. These figures represent the net sales price of the timber after contractor deductions for harvesting and haulage.
- 10 As set out in paragraphs 19 to 21, as part of my report on NRW's accounts, I consider the regularity of transactions included within NRW's accounts. I therefore considered the regularity of the transactions included within NRW's 2017-18 financial statements relating to the transitional contracts. I was unable to satisfy myself of the regularity of these transactions and I have therefore qualified my

regularity opinion accordingly. Within this supplementary memorandum I have set out the reasons for my qualification. These are:

- a) NRW departed from its own policy as set out in its published Timber Marketing Plan 2017-22 when it entered into 59 timber sales contracts without openly marketing the timber. NRW has been unable to demonstrate that it had good reason to depart from its stated policy (see paragraphs 25 to 33).
- b) NRW's rationale for determining the volume of timber to be contracted under the transitional arrangements is not supported by the available contemporaneous documentation (see paragraphs 34 to 40).
- c) NRW is required to comply with its Framework Document and Managing Welsh Public Money, which together require NRW to refer novel, contentious and or repercussive proposals to the Welsh Government. I consider that the proposal to enter into the transitional contracts was novel, contentious and/or repercussive. Whilst NRW informed the Welsh Government of its intention to put in place transitional arrangements, it did not make a formal referral to the Welsh Government as it was required to do (see paragraphs 41 to 49).
- d) NRW's Board made a Scheme of Delegation under the provisions of the Natural Resources Body for Wales Establishment Order 2012 (the Order). This Scheme of Delegation grants delegated powers to specified NRW office holders to agree timber sales contracts on behalf of NRW. Thirteen of the transitional contracts were not authorised in accordance with the Scheme of Delegation, and I therefore consider that they were not entered into lawfully (see paragraphs 50 to 59).
- e) Article 8 of the Order states that NRW 'in considering whether or not to exercise any power conferred upon it by or under any enactment, NRW must take into account the likely costs and benefits of the exercise or non-exercise of that power'. I have seen no evidence that NRW took into account the market price of the timber being sold within the transitional contracts, when determining the contract prices. In consequence, I am not satisfied that NRW complied with Article 8 of the Order and that it took all relevant factors into account when making its decisions (see paragraphs 60 to 71).
- f) NRW is required to comply with State Aid rules. I consider that NRW did not follow proper procedures to satisfy itself that its actions complied with State aid rules when entering into the transitional contracts. It did not seek to ensure that the prices in the contracts were at market rates, and by NRW's own admission it did not consider its own legal advice which had highlighted the risk that the transitional arrangements could have State Aid implications (see paragraphs 72 to 75).

11 In consequence of the matters set out in paragraph 10, I have significant uncertainty as to whether NRW acted in accordance with its statutory duties, public law principles and State Aid rules.

- 12 Whilst my report on NRW's 2017-18 financial statements focusses on the regularity matters set out paragraph 10, in my view, there are wider lessons that NRW needs to learn.
- 13 In February 2017, NRW was facing a situation where very substantial timber contracts would terminate at the end of March 2017. Alternative arrangements were required to ensure that the ending of these contracts did not have an adverse effect on timber processors and customers, as well as NRW's own income. NRW had to act quickly, but in its haste it did not follow due process and disregarded principles of good governance. My audit found that:
- documentation of the decision-making process was wholly inadequate;
 - it was unclear who had made decisions and the rationale for those decisions;
 - contractual operations commenced in advance of written contracts being signed;
 - communications regarding the transitional arrangements, both internally and with the Welsh Government, were incomplete and on some occasions inaccurate; and
 - the proposal to enter into transitional arrangements was both significant and potentially contentious, but was not subjected to proper scrutiny. Furthermore, no written reports were made to NRW's Board or Audit and Risk Assurance Committee (ARAC) in respect of this matter prior to entering into the arrangements.
- 14 It is disappointing that the urgency of the situation arose because NRW failed to properly monitor the long-term contracts and plan for the eventuality that the contracts would terminate. NRW had already extended the requirement of the Sawmill Operator to construct the new saw line by a year to 31 March 2017, at which point, if the saw line had not been constructed and operating, the contracts would fall. A new saw line typically has a construction period of 12 to 18 months and therefore NRW should have been aware many months before March 2017 that the saw line was very unlikely to be constructed. The termination of the contracts was eminently foreseeable and NRW should have developed detailed plans which would have given the Sawmill Operator and Timber Harvesting Company time to source alternative timber supplies and NRW time to arrange to market the timber within the long-term contracts from 1 April 2017 thereby minimising market disruption.
- 15 When I reported on NRW's 2015-16 financial statements I was concerned that NRW did not appear to fully accept my criticisms of their actions and sought to downplay their significance. The fact that the issues raised in my report on NRW's 2017-18 financial statements are so similar to those included in my report on NRW's 2015-16 financial statements has confirmed that NRW did not treat the findings of my 2015-16 report sufficiently seriously.

- 16 I am, however, encouraged that when my auditors informed NRW of the provisional findings of this audit, NRW's response was constructive, there was an acceptance of the seriousness of the matters raised, and a commitment to ensure that rigorous action is taken to ensure both that policies and procedures are improved and that cultural and behavioural issues are addressed. NRW has told me that it intends to commission a full independent review of the issues raised in my report on NRW's 2017-18 financial statements. The scope of the planned review will include examining the breadth of the governance and contract management of timber sales and marketing. The findings of the review will be used to inform changes within NRW's timber sales and marketing arrangements to ensure the matters highlighted in my report are not repeated in the future. NRW is aiming to ensure that the independent review is completed in the autumn of 2018.
- 17 Included in Appendix 1 is a detailed chronology of events relating to the award of the contracts.

Reasons for qualification of my regularity opinion

- 18 Under Article 23(5) of NRW's Establishment Order 2012 (the Order), I am required to:
- examine, certify and report on NRW's statement of accounts;
 - provide a copy of the certified statement of accounts together with my report on it to NRW; and
 - no later than four months after the statement of accounts is submitted, lay before the National Assembly for Wales a copy of the certified statement of accounts and my report.
- 19 In addition to certifying that the financial statements give a true and fair view of the state of Natural Resources Wales' affairs as at 31 March 2018, I provide a regularity opinion certifying that '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'.
- 20 In providing my regularity opinion, I form a view on whether in the exercise of its functions, NRW has:
- acted within its statutory remit;
 - complied with relevant legislation;
 - acted in accordance with principles of public law; and
 - complied with the framework of authority which governs it, eg the provisions of NRW's Framework Document and ministerial directions given under Article 11 of the Order.
- 21 My regularity opinion, takes the form of positive assurance, which means that I state whether transactions are in accordance with the authorities that govern them. Where there is significant uncertainty that transactions within NRW's accounts are

irregular and/or unlawful, I am unable to provide a clear regularity opinion on the accounts. This is because positive assurance cannot reasonably be given where there is significant uncertainty.

- 22 I have doubt as to whether NRW acted in accordance with its statutory duties, public law principles and State Aid rules in awarding 59 timber sales contracts to three contractors during 2017-18. In consequence, I am unable to positively affirm that the transactions in NRW's 2017-18 financial statements conform to the framework of authority governing them. I have therefore qualified my regularity opinion accordingly.
- 23 However, a decision is not unlawful unless and until declared so by a Court (or, in the case of State Aid, a Court or the European Commission). Therefore, in the absence of a legal challenge the contracts remain valid and enforceable.
- 24 I have set out in the following section the considerations I have taken into account in reaching my decision to qualify my regularity opinion on NRW's 2017-18 financial statements.

Failure to demonstrate good reason for departing from NRW policy

- 25 For a decision of a public body to be lawful it must be made in accordance with applicable legislation and with public law principles. Public bodies must (a) take into account and (b) follow relevant policies, unless they have a good reason to depart from them. At the very least they must 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.
- 26 In January 2017, NRW published a Timber Marketing Plan 2017-2022 (the Plan). The plan is essentially a policy which sets out how NRW will market timber, which will generally be on the open market. The Plan includes the caveat that 'in exceptional circumstances only we may decide to negotiate the sale of timber to customers who are able to respond quickly to unexpected events'. This implies an urgency requirement insofar as the decision would be to negotiate with customers who are able to respond quickly.
- 27 I have considered whether NRW was faced with exceptional or unexpected and urgent circumstances which meant that it could rely on the caveat within the Plan to enter into timber sales contracts without seeking competition. It might be expected that the early termination of the long-term contracts, resulting from the decision of the Sawmill Operator not to construct a new saw line was an unexpected event.
- 28 However, as set out in paragraphs 13 to 14, this event should have been expected if NRW had managed the long-term contracts differently. I also note that on 15 March 2017, NRW's then acting Head of Commercial Operations (now permanent in post) wrote to the Sawmill Operator stating 'we believe that the action we need to take is to bring these [long-term contracts] to a close and re-market the

equivalent volume in accordance with the direction set out in our recently published five-year [Plan]’.

29 I consider that there was not an urgent or exceptional circumstance, and NRW was not entitled to rely on the caveat within the Plan. In my view, NRW departed from its policy when it decided not to openly market these timber contracts in 2017-18.

30 I acknowledge that public bodies may depart from their own policies where they first considered their policy and second, are able to demonstrate a good reason to do so, and I accept that NRW could have constructed a reasoned case and rationale for departing from the Plan. For example:

- On 16 February 2017, NRW’s then Chief Executive emailed the Welsh Government stating that NRW needed to be mindful of investment made by the Sawmill Operator and the role timber processing plays in the rural economy (see Appendix 1, paragraph 2.9). I accept that NRW has a legitimate role in maintaining the market and supporting businesses.
- In May 2017, NRW’s acting Head of Commercial Operations wrote to NRW’s then Chief Executive, (albeit after the implementation of the transitional arrangements) giving the following reasons for the contract awards:
 - to avoid damaging the timber supply chain. In the event that the long-term contracts ended with no transitional provision, contractors could be put out of work through no fault of their own; and
 - to avoid adversely affecting NRW’s timber income as the lead in time for marketing timber would have resulted in a major dip in NRW’s income (see Appendix 1, paragraph 3.24).

31 Whilst the above seem like good reasons, there is little documentary evidence to show that these reasons were being considered at the time the contracts were entered into. (I have found NRW’s failure to keep proper records of its decision-making process of particular concern, see paragraph 13.)

32 Furthermore, other evidence provided by NRW suggests that NRW may have had other and/or alternative reasons for entering into the transitional contracts. These include:

- NRW was seeking to implement a new timber management IT system in the period in question. Significant difficulties were experienced which hampered NRW’s ability to openly market timber. This could have been a good reason, although NRW has not sought to rely on it and there is no documentary evidence that it was relied upon.
- On 23 February 2017, NRW’s acting Head of Commercial Operations emailed NRW’s then Chief Executive discussing the volume which could be potentially awarded under transitional arrangements. The email states that the timber volume with the long contracts for roadside logs could be remarketed in April 2017 on short-term contracts and [the Sawmill Operator] would be able to bid for new contracts alongside any other customer (see Appendix 1, paragraph 2.19). However, on 28 March 2017, NRW offered the

Sawmill Operator 49,575 tonnes of roadside spruce and larch logs and bars as part of the transitional arrangements.

- NRW's current Head of Marketing, who supported NRW's then Head of Marketing in the negotiations with the Sawmill Operator, has told my auditors that he himself would have had a different negotiation strategy to the one actually employed. He would have offered a lower transitional volume than that agreed and would have sought to negotiate harder on price.

33 I therefore consider that NRW has been unable to demonstrate that it had good reason to depart from its Plan when it entered into 59 timber sales contracts without seeking competition from the market. I am therefore not satisfied that NRW complied with principles of public law when entering into the contracts, and that the resultant transactions are lawful.

Failure to demonstrate that only relevant considerations were taken into account when determining contract volumes

- 34 On 22 March 2017, NRW's then Head of Marketing emailed the Sawmill Operator with a proposal to sell 194,248m³ obs of timber¹ to the Sawmill Operator under transitional arrangements (Appendix 1, paragraph 2.25). Of this volume 8.1% was for roadside log and bars. The offer equated to 41.1% of the existing long-term contract volumes. On 28 March 2017, at a meeting with the Sawmill Operator, NRW increased the offer to 251,973m³ obs. Of this volume 24.4% was roadside log and bars. The revised offer represented 43.3% of the long-term contract volume (Appendix 1, paragraphs 2.32 to 2.36).
- 35 NRW told my auditors that the volume offered was determined by a combination of objectives, to:
- provide continuity of supply to timber processors to enable them to meet their contracted commitments;
 - give the forestry contractors time to find alternative work; and
 - give NRW the lead in times needed to re-market the timber over a phased period to avoid placing an excessive amount of timber on the market at any one time.
- 36 However, in my view, NRW's position on this matter is inconsistent with contemporaneous documentation which suggests that the volume was linked to the value of investment the Sawmill Operator maintained it had made to its premises, rather than the factors set out in paragraph 35 above:

¹ One tonne in weight of softwood timber is equivalent in volume to approximately 1.24 cubic metres obs

- An internal NRW briefing note dated 17 February 2017, setting out options for transitional arrangements set out the proposal that transitional volume would be proportionate to the amount of investment the Sawmill Operator had undertaken at its sawmill (see Appendix 1, paragraphs 2.10 to 2.11).
- In an email dated 20 February 2017, NRW's acting Head of Commercial Operations instructed NRW's then Head of Marketing 'refine your de-commitment profile based on reducing the total transitional volume to 40%' (see Appendix 1, paragraph 2.14).
- On 31 March 2017, NRW's then Head of Marketing emailed NRW's then Chief Executive, setting out the rationale used for determining the volume offered, 'we used a swings and roundabout approach to make the whole volume fit the ratio of the proportion of investment made by [the Sawmill Operator]' (see Appendix 1, paragraphs 2.52 to 2.53).

- 37 It is unclear why the transitional volume increased between 22 March 2017 and 28 March 2017. NRW's response to this question is that 'NRW quickly recognised that the setting up and tendering of those contracts would have risked NRW's ability to deliver its overall programme by missing the crucial Spring and early Summer 2017 market. In turn this would have caused disruption to the supply chain and the ability for contractors to find alternative work. Consequently, an increase in transitional volume was agreed.' Whilst I acknowledge that this may have been the reason for increasing the offer volume, NRW holds no contemporaneous documentation to support its position. Furthermore, NRW has been unable to provide me with any contemporaneous documentation that sets out the decision to significantly increase the proportion of roadside timber relative to standing timber within the offer to the Sawmill Operator.
- 38 NRW has acknowledged that 'the business rationale, risk appetite and documentation in support of the calculations of transitional volume should have been much clearer and subject to wider scrutiny.'
- 39 Public law requires public bodies to take into account all relevant considerations and disregard irrelevant considerations when reaching decisions. One way in which public bodies can demonstrate that they have complied with this principle is by fully documenting the considerations they have taken into account.
- 40 NRW's failure to properly document the decision-making process that led to the award of the transitional contracts in general, and the determination of the transitional volume in particular. This means that I now have significant uncertainty as to whether NRW took into account all relevant considerations, and disregarded irrelevant ones.

Failure to refer novel, contentious and/or repercussive activities and proposals to the Welsh Government

- 41 The principal document that provides authority for NRW transactions is the 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, which includes compliance with the 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.'
- 42 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 relevant Welsh Government sponsor team is required for any novel, contentious or repercussive proposals.
- 43 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.
- 44 I have considered the latest version of the Welsh Government's Managing Welsh Public Money (January 2016). This document says 'paragraph 3.8.2: The framework document (or equivalent) agreed between a public body and its sponsor Branch always provides for the sponsor Branch to exercise 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. Public bodies should refer to their sponsor Branch any issues which appear novel, contentious or repercussive'.
- 45 The NRW Framework Document sets out in relation to expenditure that NRW must obtain written approval in advance of proceeding with any proposal which could be considered to be novel, contentious or repercussive. However, for income (including disposal proceeds from the Welsh Government Woodland Estate) it states 'NRW must seek as far as possible to maximise its income... where this is consistent with its functions and is in line with the agreed Corporate Plan'.
- 46 In my view, NRW was required to refer to the Welsh Government any novel, contentious or repercussive proposals relating to income. I consider that the transitional contracts were novel, contentious and/or repercussive because:
- the contracts were not advertised on the open market and were not awarded in accordance with NRW's Timber Marketing Plan (see paragraphs 25 to 33).

- the contracts with the Timber Harvesting Company had a clause described as 'exceptional' by NRW (the clause required the Timber Harvesting Company to sell spruce and larch logs and bars to the Sawmill Operator, see Appendix 1, paragraph 3.8).
- NRW clearly regarded the termination of the long-term contracts and the introduction of transitional arrangements to be significant matters as it felt it necessary to communicate with the Welsh Government in relation to these matters.

47 I acknowledge that NRW did communicate with the Welsh Government regarding its intention to enter into transitional arrangements. Emails from NRW on 15 March 2017 and then on 3 April 2017 to the Welsh Government set out in broad terms NRW's intention to contract with the Sawmill Operator, and provided a schedule of the timber volumes NRW was seeking to contract with the Sawmill Operator (Appendix 1, Paragraphs 2.23 and 2.49). However,

- neither the Welsh Government nor NRW regard these communications as being framed as a referral of novel, contentious or repercussive proposals in accordance with Managing Welsh Public Money, and the Welsh Government did not treat it as such; and
- the communications did not provide full details of the proposals. As set out in Appendix 1, paragraph 2.50, they did not make mention of the proposal to contract with the Timber Harvesting Company and they did not accurately record the volume to be contracted under the transitional arrangements.

48 NRW now accepts that the proposals should have been referred to the Welsh Government as novel, contentious and/or repercussive and takes the view that approval should have been sought to enter into the transitional contracts.

49 I consider that NRW did not meet the requirements of the Framework Document and Managing Welsh Public Money to refer a novel, contentious and/or repercussive proposal to the Welsh Government. I consider that the transactions related to these contracts which are included within NRW's financial statements for 2017-18 were outside the framework of authority governing them and are therefore irregular. In consequence, I have qualified my regularity opinion on NRW's 2017-18 financial statements.

Failure to comply with NRW's Scheme of Delegation

50 The functions of NRW are set out in the Natural Resources Body for Wales Establishment Order 2012 (the 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.

- 51 NRW's Board has approved a Financial Scheme of Delegation called 'Managing Our Money' under which all financial activities of NRW have been delegated to an agreed level of authority or specific post holder. It allows the Board to delegate decision-making responsibility for certain financial matters.
- 52 The Scheme of Delegation is the method by which NRW's Board delegates its function of entering into contracts to individual members of staff and is a mechanism for risk management and financial probity. If contract authorisations are non-compliant with the Scheme of Delegation transactions in respect of those contracts will be items of account contrary to law.
- 53 As set out in Appendix 1, paragraph 3.3 to 3.5, the Financial Scheme of Delegation sets out the office holders authorised to enter into timber sales contracts, and the contract values to which their delegations extend.
- 54 Each of the transitional contracts were authorised individually by NRW officers.
- 55 As set out in Appendix 1, paragraph 3.6, 13 of the 59 transitional contracts were not authorised in accordance with the Scheme of Delegation. NRW has been unable to provide evidence that five contracts were authorised and eight were authorised by NRW officers without the necessary delegation to authorise contracts awards of the value they signed off.
- 56 The estimated value of the contracts not properly authorised was £2,752,248 and NRW received income in respect of these contracts of £1,868,773 in 2017-18.
- 57 I further note, that NRW's Financial Scheme of Delegation 'requires some delegated actions to be reported at Board level, when they involve either significant sums of money or where they are potentially contentious, novel or sensitive'. As set out in paragraphs 41 to 49, I consider that the decision to award these 59 transitional contracts was novel and contentious. The decision to award the transitional contracts was not reported to NRW's Board, and therefore I consider this a further breach of NRW's Scheme of Delegation.
- 58 NRW has told my auditors that in hindsight it considers that it would have been better to have considered approving the contracts on a collective basis, in recognition of the fact that the contracts were negotiated collectively. As set out in Appendix 1, paragraph 2.15, I note that NRW's then Chief Executive stated that he needed to ratify any final agreement on the transitional arrangements, but for some reason, he did not formally authorise or ratify the arrangements. However, I acknowledge that the Scheme of Financial Delegation as drafted did not require multiple concurrent contracts awarded to a single supplier to be considered collectively for delegation purposes, nor did it give NRW's Chief Executive the power to authorise the contracts or amend the lines of delegation.
- 59 I consider that in those instances where NRW has failed to comply with its Scheme of Delegation, the transactions included within NRW's 2017-18 financial statements are contrary to law. In consequence, I have qualified my regularity opinion on NRW's financial statements.

Failure to demonstrate compliance with the requirements of NRW's Establishment Order and State Aid rules when setting contract prices

Contract Pricing

- 60 During the course of my audit of the transitional contracts my auditors experienced significant difficulty obtaining clarity from NRW in respect of
- how the prices being paid for timber sold by NRW under transitional contracts had been determined;
 - how the pricing mechanism contained within the contracts for the sale of standing trees to the Timber Harvesting Company and the Sawmill Operator's timber harvesting company was intended to operate in practice; and
 - the considerations NRW took into account when agreeing contract prices.
- 61 This lack of clarity was due to a failure of NRW to maintain adequate records of its pricing negotiations, and how rates it had agreed had been applied within the contracts themselves. In consequence, the audit was unnecessarily protracted and my auditors had to undertake considerably more work than would have been the case had NRW adequately documented its pricing negotiations.
- 62 The first reference to transitional contract pricing is set out in the notes of a meeting between NRW and the Sawmill Operator on 28 March 2017, in which NRW agreed to put forward a pricing proposal for the transitional contracts (see Appendix 1, paragraph 3.10). NRW has been unable to locate a copy of any pricing proposal it made to the Sawmill Operator.
- 63 On 31 March 2017, the Sawmill Operator emailed NRW confirming prices it would pay for spruce and larch logs and bars. The prices specified represented an increase on the larch prices in the terminated Long-Term Contracts, (Appendix 1, paragraph 3.10). An internal email sent by an NRW officer to colleagues on 21 April 2017, confirmed the prices that had apparently been agreed and also specified the amount that could be deducted from the sales price for haulage (Appendix 1, paragraph 3.13).
- 64 NRW initially told my auditors that the prices specified in the emails of 31 March 2017 and 21 April 2017 applied to all the transitional contracts, including the contracts for the sale of standing trees awarded to the Timber Harvesting Company and the Sawmill Operator's timber harvesting company.
- 65 However, my auditors found that the amounts specified in the haulage rates for standing sales contracts were in most cases higher than the rates set out in the email of 21 April 2017. The effect was that NRW received less income than would have been the case if the rates set out in the email of 21 April 2017 had been applied.

- 66 My auditors also found that 17 of the contracts with the Timber Harvesting Company (which NRW had classified as 'pipeline' contracts as the contracts related to forest areas where felling operations had commenced before 31 March 2017), applied the rates set out in the terminated long-term contracts. If the prices for spruce and larch logs and bars as set out in the emails of 31 March 2017 and 21 April 2017 had been applied to all the transitional contracts, I have calculated that NRW would have received £186,231 more in income during 2017-18 than was actually the case.
- 67 I accept that NRW was entitled to apply different haulage rates to the contracts with the Timber Harvesting Company and the Sawmill Operator's timber harvesting company than the ones agreed with the Sawmill Operator. I also accept that NRW was entitled to align the prices set within the pipeline contracts to those which had applied to the terminated long-term contracts. However, I find it unacceptable that NRW has kept no records setting out its reasons for applying the prices it did to the transitional contracts.
- 68 NRW may determine the price at which it sells timber, however, the market price is a relevant factor which NRW should take account in determining the contractual prices. Furthermore, the market price is relevant in terms of whether NRW is conferring a potentially unlawful advantage contrary to the State Aid rules (see paragraphs 72 to 75).
- 69 My auditors have compared the prices that NRW achieved for timber sales under the transitional contracts against:
- i. the Forestry Commission's Timber Price Indices Data to March 2017; and
 - ii. NRW's average sales prices for the first quarter of 2017-18.
- Whilst this analysis does not take into account all potential variabilities, it indicates that there is serious doubt as to whether the transitional contracts were priced at market rates, (although I note that the Sawmill Operator contends that the transitional contracts it was awarded were priced at market rates). Furthermore, the prices contracted for the pipeline contracts awarded to the Timber Harvesting Company were set at the long-term contract rates. NRW had already acknowledged in an internal briefing note dated February 2017, that the income from the Sawmill Operator's long-term contracts was at that point £1m lower than could have been achieved on the open market (see Appendix 1, paragraph 2.2).
- 70 Article 8 of the NRW Establishment Order 2012 (the Order) states that 'in considering whether or not to exercise any power conferred upon it by or under any enactment, the Body must take into account the likely costs and benefits of the exercise or non-exercise of that power'. I have seen no evidence that NRW took into account the market price (and therefore, State Aid) when determining the price under the contracts. NRW has acknowledged that whilst its legal advisors advised that entering into transitional arrangements could have State Aid implications (see Appendix 1, paragraphs 2.16 to 2.17). NRW did not consider or address this risk.

- 71 In failing to consider whether the transitional contracts were priced at market rates, I am not satisfied that NRW complied with Article 8 of its Order and took all relevant considerations into account.

State Aid

- 72 The information I have considered in respect of the pricing of the transitional contracts also leaves me with doubt as to whether NRW complied with EU State Aid rules in its award of the transitional contracts.
- 73 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, 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.
- 74 NRW was advised by its legal advisors on 20 February 2017 that entering into transitional arrangements could have State Aid implications (see Appendix 1, paragraphs 2.16 and 2.17). However, NRW does not appear to have taken this advice into consideration when entering into the transitional contracts.
- 75 I consider that NRW did not follow proper procedures to satisfy itself that it was acting in compliance with State Aid rules when entering into the transitional contracts, as it did not seek to ensure that the prices in the contracts were at market rates, and by NRW's own admission it did not consider its own legal advice which had highlighted the risk that the transitional arrangements could have State Aid implications.

Appendix 1 – Timeline relating to the award by NRW of 59 timber sales contracts to a sawmill operator and two timber harvesting companies in 2017-18 as part of transitional arrangements

Part 1

1. Summary

- 1.1. On 2 March 2017, I laid a report on the accounts of Natural Resources Wales (NRW) before the National Assembly for Wales setting out my reasons for qualifying my regularity opinion on NRW's accounts for 2015-16. I also provided a supplementary memorandum to the National Assembly for Wales' Public Accounts Committee (PAC) setting out further detail on the matters contained within the report on NRW's accounts. These documents are available on the website of the National Assembly for Wales.
- 1.2. The report on the accounts related to the award by NRW of eight timber sales long-term contracts in May 2014 connected by a Memorandum of Agreement. Under the contractual terms, NRW agreed to sell both standing trees and pre-felled timber to a sawmill operator (the Sawmill Operator). The Sawmill Operator used a timber harvesting company (the Timber Harvesting Company) to harvest the standing trees. The Sawmill Operator agreed, as a condition of the Memorandum of Understanding and contracts, that it would construct and operate a new saw line at its Welsh premises by 31 March 2016. This deadline was subsequently extended by agreement of both parties to 31 March 2017.
- 1.3. I was unable to provide an unqualified regularity opinion on NRW's accounts for the following reasons:
 - NRW did not comply with its framework of authority in that it failed to refer the proposal to award the contracts to the Welsh Government (a proposal that was contentious and repercussive in several ways) as required by the Welsh Government's publication, Managing Welsh Public Money;
 - NRW failed to demonstrate that it complied with public law principles in the decision-making process which resulted in the award of contracts to the Sawmill Operator. I concluded that the decision-making process which led to the award of contracts to the Sawmill Operator was neither robust nor transparent and NRW was unable 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. The degree of uncertainty was such that I was unable to positively conclude that the decision to award the contracts to the Sawmill Operator was regular; and
 - There was doubt as to whether NRW complied with State Aid rules when it entered into contracts with the Sawmill Operator. This uncertainty was created as a consequence of NRW's decision to award the contracts to the Sawmill Operator without conducting any relevant market testing, and NRW being unable to provide persuasive reasoning to support a conclusion that seeking alternative providers would inevitably have proved fruitless.

- 1.4. The PAC carried out its own inquiry into the matters I brought to its attention in respect of the long-term contracts and published its findings in June 2017, recommending that NRW:
- 'undertake a full evaluation of its governance arrangements relating to contracting processes, clearly setting out lessons learned with specific reference to the timber sales contracts referred to in [the] report;
 - review its delegation arrangements alongside its awareness raising of State Aid law, public law and the processes for awarding contracts. We recommend the findings of this evaluation are shared with the Public Accounts Committee to enable this Committee to monitor implementation and progress against identified changes; and
 - review its internal governance arrangements to ensure that its accounting officer, Executive Team and Board should have a much greater role in scrutinising contracting processes and the awarding of contracts. It is imperative that these processes are robust with a clear and demonstrable audit trail that decisions have been taken on a fair and sound basis'.
- 1.5. On 5 July 2017, NRW's then Chief Executive wrote to the PAC accepting in full the PAC's recommendations. I subsequently qualified my regularity opinion on NRW's 2016-17 financial statements for the same reasons set out in paragraph 1.3. This was a consequence of the fact that the long-term contracts NRW entered into in May 2014 were still operating and the 2016-17 financial statements included income relating to these contracts.
- 1.6. As set out in paragraph 1.2, a Memorandum of Agreement to the eight long-term contracts referred to in my previous report included a requirement for the Sawmill Operator to construct and commence operating a new saw line at its sawmill by 31 March 2016 (which was subsequently extended by agreement to 31 March 2017). Under the Memorandum of Agreement (which was also reflected in some but not all of the contracts), if the saw line was not constructed and operating by this date the contracts would terminate. In February 2017, the Sawmill Operator informed NRW that it did not intend to construct the saw line.
- 1.7. In March 2017, NRW entered into negotiations with the Sawmill Operator with the view to putting in place transitional contractual arrangements to take effect from 1 April 2017 when the long-term contracts terminated. The proposal was to offer the Sawmill Operator short-term contracts awarded to cover the transitional period between the termination of the long-term contracts and NRW remarketing the timber volume in the terminated long-term contracts. These contracts would be awarded without seeking competition from the market.

- 1.8. By 31 March 2017, NRW had reached an agreement in principle with the Sawmill Operator. However, on that date NRW was contacted by a timber harvesting company which had acted as the harvesting agent on the terminated long-term contracts (the Timber Harvesting Company). The Timber Harvesting Company, which is a completely separate organisation to the Sawmill Operator, asked to be included in the contractual arrangements to be put in place from 1 April 2017. NRW agreed to award some of the transitional contracts to the Timber Harvesting Company.
- 1.9. The long-term contracts terminated on 31 March 2017 and during 2017-18 NRW entered into 59 short-term contracts. Twenty one of the transitional contracts were awarded to the Sawmill Operator and a timber harvesting company owned by it, (the Sawmill Operator's timber harvesting company). The remaining 38 contracts were awarded to the Timber Harvesting Company. NRW's stated intention was to achieve 'an orderly wind down' of the long-term contracts.
- 1.10. NRW's 2017-18 financial statements record that NRW received timber income of £2.76 million in respect of the 59 transitional contracts. NRW anticipates that it will receive a further £0.18 million in 2018-19. These figures represent the net sales price of the timber after contractor deductions for harvesting and haulage.
- 1.11. Having considered the circumstances surrounding the award of these contracts, I have significant concerns regarding the regularity of the contract awards and of the transactions relating to these contracts. In consequence, I have qualified my regularity opinion on NRW's 2017-18 annual accounts. The reasons for my qualification are set out in paragraph 10 of the supplementary memorandum.
- 1.12. In this appendix, I set out the events that led to NRW entering into the transitional arrangements.

Part 2

2. Implementation of transitional arrangements

Termination of long-term contracts awarded to the Sawmill Operator in May 2014

- 2.1 On 17 January 2017, NRW's acting Head of Commercial Operations (who has since been permanently appointed to this role) emailed NRW's then Chief Executive setting out that 'our larch [Long Term Contracts] with [the Sawmill Operator] were linked to a timescale for investments at [the Sawmill Operator's premises]. The expectation was that the new line should be up and running by the end of March 2016. They were granted an extension last year to give them an additional 12 months to make the investment. [NRW's Head of Marketing] is requesting an update from [the Sawmill Operator] on progress with the investment [at its premises]. However, the indications are that there has been significant further slippage'. The email also notes that because timber prices had risen since the contracts had been awarded in 2014, they now offered poor value for money. The acting Head of Commercial Operations requested NRW's then Chief Executive's consent for him to 'take stock of the situation and options in order to brief you and to recommend a way forward'.
- 2.2 On 31 January 2017, in advance of a meeting that had been arranged with representatives of the Sawmill Operator, the then Chief Executive emailed NRW's acting Head of Commercial Operations requesting information regarding the performance of the contracts. NRW's acting Head of Commercial Operations responded on 3 February 2017 providing a draft briefing paper setting out concerns regarding the performance of the contracts which included:
- the Sawmill Operator had only made approximately £5m of the expected £17m capital investment expected at its Welsh premises and that the construction of a new saw line which was agreed in the Memorandum of Agreement had not taken place.
 - the Memorandum of Agreement required the Sawmill Operator to actively expand the market for larch products, increasing the overall value of the product base and concentrating on the development of larch timber in the construction market. The briefing paper noted that whilst the Sawmill Operator had made efforts to increase the amount of larch going to the construction market, much of the larch production at its sawmill had been used to provide sawn products for the fencing panel market, which was not a new market and did not represent either construction or a higher market value.
 - the Sawmill Operator had not been flexible in respect of the contractual pricing mechanism, and as the market value of larch had increased since the award of the contracts, NRW had received approximately £1m in income less than it would have achieved if the timber had been openly marketed.

- 2.3 The briefing paper concludes given the change in circumstances since the contracts were awarded it 'would make it extremely difficult to justify a further extension in the timetable for completing the investment'.
- 2.4 On 8 February 2017, NRW's Head of Legal Services emailed legal instructions to NRW's legal advisors seeking advice on 'the strength of our case for potentially not granting a further extension to the deadline for investments and instead terminating the contracts'.
- 2.5 On 13 February 2017, NRW legal advisors advised that if the Sawmill Operator could not comply with the deadline for construction and operation of the new site and NRW refused to agree to any request for a further extension of time, the contracts and the overarching Memorandum of Agreement which connected them would come to an end. They advised that the prospect of termination could be used as a means to renegotiate the terms of the Memorandum of Agreement and the contracts with a view to varying the agreements or entering into a new arrangement. However, any such negotiation should proceed on the basis that the negotiations were without prejudice to NRW's position that with effect from 31 March 2017 the Memorandum of Agreement and the contracts would terminate.
- 2.6 On 16 February 2017, NRW's then Chief Executive and NRW's acting Head of Commercial Operations met with representatives of the Sawmill Operator to review the contracts and to discuss the progress being made by the Sawmill Operator to construct the new saw line and commence its operation by 31 March 2017.
- 2.7 NRW's notes of this meeting record that NRW was informed by the Sawmill Operator that it was not commercially viable for it to construct the saw line it had been contracted to construct (a saw line to process small/short bars), but there was 'scope for an expansion in the capacity for larger logs' on the proviso that the long-term contracts were not terminated.
- 2.8 The notes also record that:
- the Sawmill Operator was told that if the new saw line was not constructed and operational by 31 March 2017 the contracts would be terminated; and
 - the Sawmill Operator threatened to sue NRW to recover the £4m the Sawmill Operator said it had already invested, to close its Welsh premises and that 'NRW would face some political difficulties given the employment that [the sawmill] supported and the economic contribution it makes'.
- 2.9 On 16 February 2017, NRW's then Chief Executive emailed the Welsh Government attaching a briefing document setting out an outline of what was discussed in the meeting held on 16 February 2017. The note stated that NRW would write to the Sawmill Operator setting out its position and that in drafting this letter NRW would 'be mindful of investments that [the Sawmill Operator has] already undertaken at its Welsh premises and the role that timber processing plays in the rural economy'.

- 2.10 On 17 February 2017, NRW's acting Head of Commercial Operations sent a draft briefing paper, (addressed to the Welsh Government) to NRW's then Chief Executive setting out the history of the long-term contracts and outlining four options for managing the timber volumes currently within the contracts with the Sawmill Operator after 31 March 2017. Against each option were set out perceived risks and benefits. The options were as follows:

Exhibit 1: options for managing the timber volumes

Option 1 – Allow the contracts to terminate at the end of March 2017 on the basis that the new saw line would not be constructed.

Option 2 – Renegotiate the long-term contracts by terminating some contracts and allowing some contracts to run for a further period or until the end of their contracted duration. The reduced volume to be calculated at 40% of the original long-term contract volume, ie proportionate to the amount of the expected capital investment (£10m) as against that actually made by the Sawmill Operator (£4m).

Option 3 – Renegotiate long-term contracts and reset the baseline unit price of timber to reflect open market timber values.

Option 4 – Agree a further extension of time for the investment and/or negotiate alternative capital investment by the Sawmill Operator to increase processing ability.

- 2.11 The briefing note sets out some of NRW's considerations in developing the options. These included:
- the threat of job losses could 'be expected to generate some political controversy'; and
 - the Sawmill Operator would 'face a difficult position if NRW terminates the [long-term contracts]. The company has indicated that it is unable to secure finance for investments, without there being the guarantee of a significant part of the volume needed. Meanwhile other timber processors have been making significant investments without the [long-term contracts] with NRW'.
- 2.12 The briefing paper invited 'the Welsh Government's view on the options and recommendations'. In the event, NRW has told my auditors that its then Chief Executive decided not to send the briefing paper to the Welsh Government on the basis that it decided that the matters in the briefing paper were matters for NRW to determine. NRW did verbally brief the Welsh Government on developments but did not communicate the options it was considering to the Welsh Government.
- 2.13 On 17 February 2017, NRW's Head of Legal Services emailed NRW's legal advisors attaching the notes of the meeting of NRW and the Sawmill Operator on 16 February 2017) and a copy of the draft briefing note addressed to the Welsh Government (paragraph 2.2). The Head of Legal Services requested further legal

advice on the contractual issues which existed between NRW and the Sawmill Operator.

- 2.14 On 20 February 2017, NRW's acting Head of Commercial Operations emailed NRW's Head of Marketing, then Chief Executive and Head of Legal Services stating, 'I think that Option 2 is probably the most appropriate as it focusses on reduction in contracted volume, in proportion to incomplete investments, but without introducing the complication of imposing price change' and asked the Head of Marketing 'can you refine your de-commitment profile based on reducing the total [long-term contract] volume to 40%'.
- 2.15 On 20 February 2017, NRW's Head of Legal Services emailed NRW's legal advisors updating his instructions of 17 February 2017 and attaching a copy of the email from the acting Head of Commercial Operations (see paragraph 2.14). The legal instruction states that NRW's then Chief Executive 'takes the view that it is for the NRW team to deal with the negotiations with the caveat that he, as Accounting Officer, would need to ratify any final agreement (and he adds that in light of [my then draft report on NRW's 2015-16 accounts], NRW would need to consider Welsh Government and Board scrutiny)'. He also expresses the view that 'it is too early to seek Welsh Government "approval" as we don't know how the negotiations might go'.
- 2.16 On 20 February 2017, NRW's legal advisors advised that:
- as the saw line had not been constructed the contracts would terminate on 31 March 2017;
 - the fact that the Sawmill Operator had made some £4m investment was in their view irrelevant as a new saw line had not been constructed and was not operating, and they could see no possible basis of a claim against NRW by the Sawmill Operator;
 - in respect of the options outlined, there was no provisions for the original contracts to be varied and it would be preferable for NRW to negotiate new contracts; and
 - that options 2, 3 and 4 had potential State Aid implications.
- 2.17 NRW's legal advisors also returned a copy of NRW's options matrix contained within the draft briefing paper referred to in paragraph 2.10 with suggested tracked amendments in red. These amendments drew attention to the fact that renegotiating contracts with the Sawmill Operator could have procurement and/or State Aid implications.
- 2.18 On 21 February 2017, NRW's acting Head of Commercial Operations emailed a draft letter addressed to the Sawmill Operator to NRW's Head of Legal Services, copied to other NRW colleagues recording what had been discussed in the meeting of 16 February 2017 and setting out NRW's position in respect of the existing long-term contracts. The draft letter was shared with NRW's legal advisors who suggested a number of amendments to the draft.

- 2.19 On 23 February 2017, NRW's acting Head of Commercial Operations emailed the amended letter addressed to the Sawmill Operator to NRW's then Chief Executive. The covering email stated 'the final paragraph [of the letter] with the invitation to propose a wind down of the Standing Sales contracts is the avenue which [the Sawmill Operator] can negotiate a solution. About 65% of the contracted volume is Standing Sales and there are operational reasons why these should not be terminated on 31 March. The same does not apply to the roadside log contracts, where we can continue to manage the harvesting operations while we remarket the volume from April on short-term contracts which [the Sawmill Operator] would be able to bid for alongside any other customer'.
- 2.20 On 24 February 2017, NRW's acting Head of Commercial Operations wrote to the Sawmill Operator. The finalised letter states that at the meeting of 16 February 2017:
- the Sawmill Operator had been informed that if the new saw line was not operating by 31 March 2017 the contracts would terminate;
 - the Sawmill Operator threatened legal action against NRW if the contracts were terminated; and
 - the Sawmill Operator maintained that it had made £4m of capital investment at its Welsh premises.
- 2.21 In the letter of 24 February 2017, NRW's acting Head of Commercial Services also requested details of the basis of any claim the Sawmill Operator had against NRW and requested evidence of the investments that the Sawmill Operator had claimed to have already undertaken (said to be around £4m). NRW forwarded a copy of its letter to the Sawmill Operator to the Welsh Government for information.
- 2.22 On 7 March 2017, the Sawmill Operator responding to NRW's letter reiterating its threat of a legal claim. Whilst the letter listed investments made, no evidence was provided to support the amount of capital investment the Sawmill Operator maintained had been made at its premises.

Offer of future timber volume to the Sawmill Operator

- 2.23 Following receipt of the letter from the Sawmill Operator dated 7 March 2017, NRW's Head of Commercial Operations drafted a letter to the Sawmill Operator setting out NRW's position and reflecting the advice NRW had received from its external legal advisors. The letter, which was sent to the Sawmill Operator on 15 March 2017 states 'we value the role that [the sawmill] plays in the timber supply chain in Wales and wish to ensure that before the [long-term contracts] end, you have the opportunity to purchase alternative volume. We also think that in order to do this and to ensure that we secure best value for timber, we need to phase the purchasing opportunities over a period. We therefore propose to meet with you on a without prejudice basis, to discuss a profile for staggering the end dates of the [long-term contracts] in a sequence that would enable us to market the volume and provide scope for you to purchase equivalent volume. I must stress however, that the buying opportunities would be on the open market and that they are likely to be

mainly in the form of short-term contracts in line with the current Marketing Plan. If [you wish] to take up the phased closure of the [long-term contracts], we would need to enter into a new Memorandum of Agreement to cover the period as the existing Memorandum will end at the end of March'. NRW forwarded a copy of the letter to the Welsh Government to keep it informed of developments.

- 2.24 NRW's acting Head of Commercial Services has told my auditors that he received a phone call from a representative of the Sawmill Operator on 17 March 2017 who told him that the Sawmill Operator would like to take up the offer of discussing a 'transitional plan'. NRW's Head of Commercial Operations has told my auditors that he notified NRW's then Chief Executive and then Head of Legal Services by email and asked the then Head of Marketing to prepare a supply profile for transitional volume that could be put to the Sawmill Operator by the middle of the following week.
- 2.25 On 22 March 2017, NRW's acting Head of Commercial Operations emailed NRW's then Head of Legal Services asking him to prepare a revised memorandum of agreement to 'cover the period in which we are phasing out the contracts'. The email states that NRW's then Head of Marketing had produced a schedule that he would be sharing with the Sawmill Operator. Later that day, NRW's Head of Marketing emailed the Sawmill Operator attaching a spreadsheet setting out a proposed transition plan which would take effect on the termination of the long-term contracts on 31 March 2017. The spreadsheet indicated that NRW was prepared to sell the following volume of timber to the Sawmill Operator post the termination date as part of transitional arrangements.

Table 1: Transitional volume proposed to be offered to the Sawmill Operator as set out in an email from NRW's Head of Marketing to the Sawmill Operator on 22 March 2017

	Committed pipeline	Additional volume	Total volume
Roadside timber	7,700 tonnes	5,000 tonnes	12,700 tonnes
Standing timber	49,500m ³ obs	129,000m ³ obs	178,500m ³ obs
Total units of supply	57,200	134,000	191,200

- 2.26 The 'committed pipeline' volume related to completion of felling in forest areas where operations had commenced before 31 March 2017. The total transitional volume that NRW's then Head of Marketing was proposing to provide to the Sawmill Operator equated to approximately 22.9% of the timber NRW had set out in its Timber Marketing Strategy it would sell to the market in 2017-18.
- 2.27 The spreadsheet records that the transitional volume, when added to the volume the Sawmill Operator had already received under the long-term contracts before 31 March 2017, meant that the Sawmill Operator would have received 41.1% of the volume that had been contracted in 2014.

- 2.28 The spreadsheet also sets out NRW's plans for releasing timber (which had been part of the long-term contracts) to the market for sale by open tender during 2017-18. It states that 90,685 tonnes of timber would be released in competitive sales between 31 May 2017 and 28 February 2018.
- 2.29 On 24 March 2017, NRW's then Head of Legal Services emailed NRW's acting Head of Commercial Operations and then Head of Marketing stating that it was essential that a phone meeting took place with NRW's legal advisors to finalise the revised Memorandum of Agreement and for him and NRW's legal advisors 'to understand the emerging negotiation picture here. In particular, [has the Sawmill Operator] now indicated that [it] will go quietly and agree an orderly wind down of the [long-term contracts]?'
- 2.30 On 27 March 2017, NRW's then Head of Legal Services emailed the acting Head of Commercial Operations and then Head of Marketing reminding them that the long-term contracts would expire on 31 March 2017 without any further action from NRW and setting out further advice he had received from NRW's legal advisors referring to the need for NRW to comply with the post-termination clauses contained within the long-term contracts, namely to enable the Sawmill Operator to remove upon payment any timber felled prior to the termination date and to remove their own buildings, equipment, etc from NRW's land. He stressed that 'it is important that NRW act in accordance with all the post termination provisions in the contract and as if the contract has expired as otherwise [the Sawmill Operator] might be able to maintain that the contract has continued on the same terms and NRW has waived the termination provisions'.
- 2.31 Later that day, NRW's acting Head of Commercial Operations wrote to NRW's then Head of Legal Services stating that 'I am not sure that the post termination provisions will suffice as we are seeking to ensure a smooth transition from supply on these contracts to the commencement on new contracts (which may or may not be purchased by [the Sawmill Operator]). We aim to agree a set of staggered end dates for the various contracts with [the Sawmill Operator] tomorrow (29th). Although some contracts will end immediately and the post termination clauses may apply, others will continue for some weeks or months'. On 28 March 2017, NRW's then Head of Legal Services replied to the acting Head of Commercial Operations, 'we may be at cross purposes. I, and [our legal advisors] are not suggesting that we rely on the post termination provisions as a negotiating position'.

Negotiations with the Sawmill Operator

- 2.32 On 28 March 2017, NRW's acting Head of Commercial Operations, the then Head of Marketing and the then Head of Harvesting met with a representative of the Sawmill Operator to discuss a future agreement between the Sawmill Operator and NRW. The notes of the meeting record that the purpose of the proposal was held 'with the intention of making an agreement on volumes to be offered and worked during 2017-18 to facilitate an orderly closure of the [long-term contracts]. The proposal seeks to allow a smooth transformation of timber to market, give time for supply chain to adjust as there are hauliers and timber contractors who are attached to these contracts, some making substantial investments in labour/equipment and to allow the company time to adjust its buying profile to supply the saw mill'.
- 2.33 The notes also record that NRW offered the Sawmill Operator 41,875 tonnes of felled timber and 141,000m³ obs of standing timber over a period of one year (182,875 units of supply in total), with the volume being phased out over the four quarters of the financial year with 97.7% of the transitional volume being sold by 31 December 2017 as shown in table 2.

Table 2: Planned phasing out of transitional contract volume as per meeting between NRW and the Sawmill Operator on 28 March 2018 (excludes pipeline volume)

	Quarter 1	Quarter 2	Quarter 3	Quarter 4	Total
Roadside timber	16,750 tonnes	12,561 tonnes	8,375 tonnes	4,189 tonnes	41,875 tonnes
Standing timber	78,000m ³ obs	51,000m ³ obs	12,000m ³ obs	-	141,000m ³ obs
Total units of supply	94,750	63,561	20,375	4,189	182,875
% of transitional volume	51.8%	34.8%	11.1%	2.3%	100%

- 2.34 The notes of the meeting state that 'the standing sales volumes will be provided through new coupes and coupes that are currently being worked will be treated as pipeline volume. It is anticipated that the final total across all contracts will be 928,000 units of sale. This equates to 43.3% of the original offer', ie the transitional and pipeline volume, when added to the volume the Sawmill Operator had already received under the long-term contracts before 31 March 2017, meant that the Sawmill Operator would have received 43.3% of the volume that had been contracted in 2014.

2.35 The notes of the meeting refer to 'pipeline volume' but do not explicitly state whether the 182,875 units of supply offered at the meeting include 'pipeline volume' the statement that 'this equates to 43.3% of the original offer'. The statement indicates that the Sawmill Operator was offered 57,200 units of pipeline volume in addition to the 182,875 units. The offer therefore amounted to 240,075 units of supply. This represented a 29.7% increase (in m³ obs) to the proposal emailed to the Sawmill Operator on 22 March 2017.

Table 3: Comparison of transitional volume proposed to be offered to the Sawmill Operator by NRW's Head of Marketing on 22 March 2017 and the volume offered to the Sawmill Operator at a meeting of 28 March 2017

Proposal 22 March 2017	Committed pipeline	Additional volume	Total volume
Roadside timber	7,700 tonnes	5,000 tonnes	12,700 tonnes
Standing timber	49,500m ³ obs	129,000m ³ obs	178,500m ³ obs
Total units of supply	57,200	134,000	191,200

Proposal 28 March 2017	Committed pipeline	Additional volume	Total volume
Roadside timber	7,700 tonnes	41,875 tonnes	49,575 tonnes
Standing timber	49,500m ³ obs	141,000m ³ obs	190,500m ³ obs
Total units of supply	57,200	182,875	240,075

2.36 As well as the change in the overall volume of timber offered by NRW, as shown in Table 3, there was a significant change in the ratio of roadside timber to standing timber, resulting in the Sawmill Operator being offered a far higher volume of roadside timber than had been originally proposed on 22 March 2017.

2.37 NRW's Head of Commercial Operations has told my auditors that the offer volume was increased because the Sawmill Operator expressed major concerns that the level of supply initially offered, particularly of roadside logs, was too low to sustain the current number of shifts being operated at its sawmill. In addition, by 28 March 2017 NRW had realised that if its supply of roadside timber to the Sawmill Operator ended on 31 March 2017, it would need to remarket the equivalent log volume very quickly if it was to meet its overall sales programme. This would have proved very difficult as NRW was introducing a new timber marketing ICT system on 1 April 2017 which would have prevented NRW from setting up and tendering contracts quickly.

- 2.38 However, NRW does not hold any contemporaneous documentation setting out why the offer was increased, and the notes of the meeting of 28 March 2017 do not record the comment attributed to the Sawmill Operator in paragraph 2.37. Furthermore, NRW has been unable to provide my auditors with any evidence that the increase in the offer volume was reported internally.
- 2.39 The increase in the offer of roadside timber as part of transitional arrangements came shortly after NRW had announced in its Timber Marketing Plan 2017-2022 (January 2017) its intention to decrease its direct production working (which results in roadside sales) from 380,000m³ obs to 280,000m³ obs in 2017-18.
- 2.40 The offer made to the Sawmill Operator at the meeting of 28 March 2017 represented 29.6% of NRW's planned timber supply to the market during 2017-18. It also equated to 74% of the annual volume of roadside timber and 106% of the standing timber that had been contracted to the Sawmill Operator under the terminating long-term contracts.
- 2.41 On 29 March 2017, NRW's acting Head of Commercial Operations emailed NRW's then Head of Legal Services setting out his understanding of the meeting with the Sawmill Operator on 28 March 2017. The email indicates that the acting Head of Commercial Operations' understanding was that the transitional arrangements would 'stagger the closure of the [long-term contracts]' and 'this will include a price adjustment for the larch timber on some of the contracts to be extended'. The email refers to the need for a new Memorandum of Agreement to be agreed with the Sawmill Operator and a request that the Head of Legal Services draft this document.

Introduction of an additional contractor

- 2.42 On the morning of 31 March 2017, NRW's then Head of Marketing emailed NRW's acting Head of Commercial Operations regarding the proposed transitional arrangements. In this email he set out:
- he would that day inform the Sawmill Operator and the Timber Harvesting Company, (which had been subcontracted by the Sawmill Operator to harvest standing timber under the long-term contracts) that the long-term contracts would terminate at the end of the day;
 - existing arrangements would transfer to new contracts and new contracts would also be drawn up for the new volume within the transitional plan; and
 - a proposal that new roadside agreements would be set up each quarter.

- 2.43 In the afternoon of 31 March 2017, NRW's then Head of Marketing received an email from the Timber Harvesting Company. The email states 'can you contact [the Sawmill Operator] and ask them to get in touch with us as they seem to be studiously avoiding us at the moment. We find ourselves in a pernicious position, we in good faith negotiated with [the Sawmill Operator] to support the investment at [its premises], we all know what has happened there. We have done everything that has been asked of us and essentially been hung out to dry. I have no idea how [the Sawmill Operator] will conduct themselves going forward but my suspicion is that they will look to take the harvesting back in house unless you can provide some context in your new contractual arrangements to protect our interests. The [long-term contract] states that we are the nominated harvesting agents; as you are completely in the driving seat in this arrangement can we not be offered the same arrangement in the [new] contracts? It is surely a case of adding that line in the contract that applies to the remaining volume An alternative is to simply reassign our original contract back to ourselves as the original basis for the arrangement was to support the investment. Can we arrange a conference call for Monday to discuss this?'
- 2.44 NRW's then Head of Marketing replied stating that NRW was available for a conference call on 3 April 2017 and that he would alert the Sawmill Operator of the need to call the Timber Harvesting Company.
- 2.45 Later that afternoon, the Sawmill Operator emailed NRW's then Head of Marketing and the then Head of Harvesting thanking them for their call earlier that day and confirming prices it agreed to pay to purchase spruce and larch timber logs and bars.
- 2.46 NRW's acting Head of Commercial Operations emailed the Sawmill Operator 20 minutes later attaching a letter notifying it that the long-term contracts would expire that day and the post termination provisions of the long-term contracts would take effect. In addition, proposing that NRW and the Sawmill Operator negotiate in good faith to enter into new arrangements, reflecting terms to be agreed between the parties, including (but not limited to) an attached matrix and otherwise with a view to achieving an orderly wind down of operations. The letter sent to the Sawmill Operator had been prepared by NRW's then Head of Legal Services with input from NRW's legal advisors.
- 2.47 The Sawmill Operator was asked to confirm by signing a copy of the letter that it agreed to the terms set out in that letter. The email from NRW states that 'just to be clear the existing contract numbers will end today with no further authorisation of uplift of timber against the contract numbers. On receipt of your confirmation, we will set up new contract numbers with the revised larch prices to cover the winding down period'. The attached supply schedule records the intention to offer the Sawmill Operator 41,875 tonnes of roadside timber and 141,000m³ of standing timber, 182,875 units of supply in total. Whilst the schedule is consistent with the notes of the meeting between NRW and the Sawmill Operator on 28 March 2017 (paragraphs 2.32 to 2.35), it does not include the additional 'pipeline volume' of

57,200 units that had been offered to the Sawmill Operator in the email sent by NRW's Head of Marketing to the Sawmill Operator on 22 March 2017 (see table 3).

2.48 On the morning of 3 April 2017, NRW's acting Head of Commercial Operations emailed the Sawmill Operator. The email was in response to a telephone call received by the Head of Commercial Operations from the Sawmill Operator on 31 March 2017 in which the Sawmill Operator had requested an increase in the proposed timber volumes. The email from NRW's Head of Commercial Operations stated that 'I have reviewed with [NRW's then Head of Marketing] the supply schedule and it would not be appropriate to add additional volume, including spruce and we feel the profile is reasonable and proportionate The reason for the supply schedule is not just to enable [you] to adapt to the ending of the [long-term contracts], but to enable the supply chain to plan and adapt. We therefore expect [you] to engage with the affected contractors and provide them with at least the level of protection afforded by the supply schedule provides for'.

2.49 The same morning, NRW's acting Head of Commercial Operations wrote to the Welsh Government setting out that the long-term contracts with the Sawmill Operator had terminated on 31 March 2017 and that the Sawmill Operator had 'chosen not to challenge this and to instead enter into discussion with us about how to wind down the contracts. Our legal advice was to use the post-termination contract provisions and accept that the contracts would expire on 31 March'. This statement was incorrect. NRW's legal advisors had advised that the long-term contract post-termination provisions could not be used to offer the Sawmill Operator future volume as part of winding down arrangements. The email to the Welsh Government included attachments including the post termination letter and a schedule showing the timber NRW proposed to sell to the Sawmill Operator under the transitional arrangements (Table 4).

Table 4: NRW's summary of transitional timber volume offered to the Sawmill Operator as notified to the Welsh Government on 3 April 2017.

	Offer Q1 Apr – Jun 2017	Offer Q2 Jul – Sep 2017	Offer Q3 Oct – Dec 2017	Offer Q4 Jan – Mar 2018	Total to be Offered 2017/2018
Road side Timber	16,750 tonnes	12,563 tonnes	8,367 tonnes	4,189 tonnes	41,877 tonnes
Standing Timber	78,000 m ³ obs	51,000 m ³ obs	12,000 m ³ obs		141,000 m ³ obs
Total units of supply	94,750	63,563	20,367		182,877

- 2.50 Whilst the schedule provided to the Welsh Government indicated that the Sawmill Operator had been offered 182,877 units of supply, as shown in Table 3, the Sawmill Operator had been offered 240,075 units of supply. The volume set out in the information provided to the Welsh Government was understated by 30.6% because it did not include the pipeline volume which had also been offered under the proposal for transitional arrangements. NRW has told my auditors that it accepts that 'all the volume should have been stated in the schedule'. The email to the Welsh Government did not set out that earlier the same morning NRW had agreed to contract with the Timber Harvesting Company for transitional standing timber (see paragraphs 2.43 and 2.54).
- 2.51 Later that morning, the Sawmill Operator emailed NRW its signed letter agreeing to 'negotiate in good faith' and a signed copy of the supply schedule NRW had sent to it on 31 March 2017. On receipt of this email, NRW's acting Head of Commercial Operations wrote to NRW's then Chief Executive and Head of Legal Services stating that the Sawmill Operator had agreed to the post-termination arrangements for the long-term contracts. He also wrote to the Welsh Government informing it that the Sawmill Operator had agreed to the winding up of the long-term contracts and that 'the reason for phasing out the supply over a period of months is not just to enable [the Sawmill Operator] to adapt to the ending of these [long-term contracts], but to enable the supply chain to plan and adapt to the ending of these [contracts]. It will also avoid adverse impact on NRW's timber income which would be an inevitable consequence of the disruption associated with complete cessation of all supply'.
- 2.52 NRW's then Chief Executive responded to the acting Head of Commercial Operations stating that 'the termination seems to have gone very smoothly and I'm pleased that we were able to reach agreement before the end of March'. He went on to state 'I am, though, likely to be pressed at the next PAC as to why these volumes were selected and how they compare with the previous contracts. In particular, I note that [the contract volume for one forest district] is for a higher volume than the original contract. I'd also be grateful for an explanation on the price differences which [the Head of Marketing] mentions. Could I have a briefing note please to cover these points?'
- 2.53 The then Head of Marketing emailed the then Chief Executive with responses to his queries. In answer to the question about 'why these volumes were selected', the Head of Marketing stated 'we used a swings and roundabouts approach to make the whole volume fit the ratio of the proportion of investment made by [the Sawmill Operator], we have only offered 12,000 out of 30,000 [40%] on the mid Wales standing spruce contract for example'. The Head of Marketing also set out the increases (from the long-term contracts) in larch sale prices that had been negotiated at the meeting of 28 March 2017.

- 2.54 At just before 5pm on 3 April 2017, the Head of Marketing emailed the Timber Harvesting Company confirming that the following had been discussed in a telephone call that morning and setting out:
- The long-term contracts had terminated on midnight on 31 March 2017.
 - There would be 'no uplift of timber' until new contracts had been put in place with the [Timber Harvesting Company].
 - There would be a 'presumption' that log and bar suitable for the Sawmill Operator from the current work sites and 'those offered in the step out arrangement' would be sold to the Sawmill Operator.
 - All new coupes were to be sold on the new larch prices that were agreed with [the Sawmill Operator] on 31 March 2017.
 - All contracts that have been partly worked would be reissued to [the Timber Harvesting Company] directly under new contracts.
 - All new coupes would also be issued to [the Timber Harvesting Company] directly under new contracts.
 - It was sensible to agree a contractual clause that stated that [the Sawmill Operator] is given the suitable log and bar.
 - 'The volume to be offered this year is 42,000m³ obs on the Llandovery arrangement and [72,000m³ obs] on the [Coed y Cymoedd] arrangement..... NRW intended getting all the volume contracted by end of [Quarter 3]'.
- 2.55 On 6 April 2017, the Timber Harvesting Company emailed NRW's Head of Marketing asking for the new contracts to be speeded up and asking for confirmation that 'NRW will negotiate all the remaining volume on the [standing larch long-term contracts] with ourselves? In effect that there is nothing in the NRW/[Sawmill Operator] agreement that gives them the right to negotiate the remaining volume going forward, they only have the right to receive the log and bar element of the standing crops.'
- 2.56 NRW's Head of Marketing replied later that day stating: 'The agreement is that we will make available the volumes that we have stated. They have agreed that you will remain the agents to harvest the remaining volume? They cannot purchase the timber directly so you by default will have the contracts. As far as I am concerned, they will have access to the larch and spruce of the sites, minor species were not discussed nor prices adjusted so it is better if they are marketed locally, best value if they are willing to meet that price all well and good. [The Sawmill Operator has] never negotiated the individual parcels in the past so why would they want to do that now? I would expect that the matrix for harvesting rates will still be used. Our contract managers are working on this as quickly as they can but this is additional work and has to be shoehorned in, they have other sale deadlines to meet as well. If they don't get that done there will be no June offers'.

Part 3

3. Award of transitional contracts

Contract Authorisations

- 3.1. Between April 2017 and March 2018, NRW entered in 59 transitional contracts.
- 3.2. Eleven of these contracts were contracts for the roadside sale of timber to the Sawmill Operator, 11 were for the sale of standing trees to the Sawmill Operator's timber harvesting company and 38 were for the sale of standing trees to the Timber Harvesting Company. NRW subsequently withdrew three of the contracts it had awarded to the Timber Harvesting Company and have told my auditors that this was due to delays by the Timber Harvesting Company commencing harvesting operations.
- 3.3. NRW's Board has adopted a Scheme of Delegation called 'Managing Our Money' under which all financial activities of NRW have been delegated to an agreed level of authority or specific post holder. It allows the Board to delegate decision-making responsibility for certain financial matters.
- 3.4. The Scheme of Delegation is the method by which NRW's Board delegates its function of entering into contracts to individual members of staff and is a mechanism for risk management and financial probity.
- 3.5. Table 5 sets out the NRW office holders who have been specified in the Scheme of Delegation as having been granted authority to enter into timber sales contracts on behalf of NRW.

Table 5: Delegated Authority for approving timber sales: Managing Our Money

Limit	Authorised Body or Person(s)
£250,000 and over	Head of Enterprise
Up to £250,000	Head of Marketing or Head of Harvesting
Up to £100,000	Sales Manager North or Sales Manager South or Operations Business Systems Manager

- 3.6. During the course of the audit my auditors found that 13 of the transitional contracts were not approved in accordance with NRW's Scheme of Delegation, and in five of these cases NRW was unable to demonstrate that the contracts had been authorised by any NRW officer. Table 6 provides a summary of the contract authorisations.

Table 6: Summary of contract authorisations against requirements of Managing Our Money

Contractor	Number of contracts	Authorised in accordance with Scheme of Financial Delegation	Value of contract above delegation limit of authorising officer	Not authorised by NRW
Sawmill Operator	11	5	6	0
Timber Harvesting Company	38	34	1	3
Sawmill Operator's timber harvesting company	10	7	1	2
Total	59	46	8	5

3.7. The estimated value of the contracts not properly authorised was £2,752,248 and NRW received income in respect of these contracts of £1,868,773 in 2017-18.

Contract Terms and Pricing

- 3.8. The transitional contracts NRW entered into during 2017-18 were generic timber sales contracts. However, into each contract with the Timber Harvesting Company NRW inserted a non-standard contract term stating, 'the purchaser shall in the first instance, offer all larch logs, larch bars and spruce bars arising from this contract to [the Sawmill Operator]. All other species/products may be marketed to achieve best value. All gate prices realised, including changes, shall be notified to NRW'. NRW's acting Head of Commercial Operations told my auditors that the inclusion of the non-standard contract term was 'exceptional' and no comparable term had been included in other NRW timber sales contracts.
- 3.9. The contracts do not specify the gross price to be paid by the Sawmill Operator to purchase larch logs, larch bars and spruce bars harvested by the Timber Harvesting Company.
- 3.10. The notes of the meeting between NRW officers and the Sawmill Operator on 28 March 2017 state that the Sawmill Operator 'agreed to look at increasing the price of the larch material that goes to [its Welsh] sawmill; NRW to put forward a pricing proposal'. NRW has not been able to provide my auditors with a copy of any pricing proposal it put to the Sawmill Operator. However, as set out in paragraph 2.45, on 31 March 2017 a representative of the Sawmill Operator emailed NRW's then Head of Marketing and the then Head of Harvesting, 'to confirm the prices as

discussed'. The spruce prices were stated to be as per the [long-term contract] mechanism and the larch prices 'for the coming 12 months'. The prices set out in the email were as follows:

Spruce prices per the mechanism:

Log £46.05 at roadside²

Bar £42.94 at roadside

Larch prices for the coming 12 months:

Log £46.46 delivered³

Bar £38.50 delivered.

- 3.11. Whilst not explicitly stated in the email, it is clear from the contracts entered into that the above prices were per tonne.
- 3.12. An internal email from the then Head of Marketing to the acting Head of Commercial Operations on 3 April 2017 states that 'the larch increase is as follows, logs are increased by £4.46 a tonne, bars are increased by £6.50 a tonne'. The increases related to the prices for larch which had applied within the terminated long-term contracts.
- 3.13. On 21 April, NRW's Timber Sales Manager South emailed other members of NRW's timber sales team following a discussion she had held with a representative of the Sawmill Operator. In the email she set out the prices that she considered had been agreed in respect of the pricing of the transitional contracts. The prices set out were consistent with those set out in paragraph 3.10. However, the email provides some additional information:
- the haulage rate to be applied for larch had been agreed at £11 per tonne and therefore the roadside price for larch logs per tonne was £35.46 (£46.46 - £11.00) and larch bars £27.50 (£38.50 - £11.00); and
 - the haulage rate to be applied for spruce had been agreed as £8.50 per tonne and therefore the delivered price for spruce logs was £54.55 per tonne (£46.05 + £8.50) and for spruce bars £51.44 (£42.94 + £8.50).
- 3.14. NRW told my auditors that the above rates had been applied to all the 59 transitional contracts regardless of whether those contracts were with the Sawmill Operator, the Sawmill Operator's timber harvesting company or the Timber Harvesting Company.

² Roadside price is the price the purchaser will pay if they buy at roadside, ie the gross sale price less the cost of haulage borne by the purchaser equals the roadside price.

³ Delivered prices are the prices the purchaser will pay if the product is delivered to its premises. However, if the purchaser has to transport to its premises, the delivered price will be offset for haulage costs.

- 3.15. However, my auditors found that whilst the prices set out above had been applied to the roadside contracts agreed with the Sawmill Operator, they had not been fully applied to the contracts made with the Sawmill Operator's timber harvesting company and the Timber Harvesting Company.
- 3.16. My auditors found that the amounts specified in the haulage rates for standing sales contracts with the Sawmill Operator's timber harvesting company and the Timber Harvesting Company were in most cases higher than the rates set out in the email of 21 April 2017. The effect was that NRW received less income than would have been the case if the rates set out in the email of 21 April 2017 had been applied.
- 3.17. My auditors also found that the 17 contracts with the Timber Harvesting Company (which NRW had classified as 'pipeline' contracts) had been priced at the same rates as those within the terminated long-term contracts. NRW had recognised in January 2017 that the prices within the long-term contracts were below market rates (see paragraph 2.2). As set out in Table 7, if the rates set out in the emails of 31 March 2017 and 21 April 2017 had been applied in full to all the transitional contracts, NRW would have received £186,232 more income in 2017-18 than was actually the case.

Table 7: Difference in income receivable by NRW in 2017-18 as a consequence of not applying the prices set out on 31 March 2017 and 21 April 2017

Sawmill Operator: Roadside Contracts	£0
Sawmill Operator's timber harvesting company: Standing Contracts	-£58,898
Timber Harvesting Company: Standing Sales, Non-Pipeline	-£110,494
Timber Harvesting Company: Standing Sales, Non-Pipeline	-£16,840
Total	-£186,232

- 3.18. NRW has not been able to provide my auditors with any contemporaneous documentation setting out the basis on which the prices within the transitional contracts were set or that it took steps to ensure that the prices were at market rates. The contemporaneous documentation, which does exist, indicates that the Sawmill Operator notified NRW of the prices (see Paragraphs 2.45 and 3.10).

Contract volumes

3.19. The timber volumes contracted for sale within the transitional arrangements, and how this compared to the amounts offered to the Sawmill Operator on 22 March 2017 and 28 March 2018 is set out in Table 8.

Table 8: Changes to the volume of timber offered under transitional arrangements.

Proposal 22 March 2017	Committed pipeline	Additional volume	Total volume
Roadside timber	7,700 tonnes	5,000 tonnes	12,700 tonnes
Standing timber	49,500m ³ obs	129,000m ³ obs	178,500m ³ obs
Total units of supply	57,200	134,000	191,200

Proposal 28 March 2017	Committed pipeline	Additional volume	Total volume
Roadside timber	7,700 tonnes	41,875 tonnes	49,575 tonnes
Standing timber	49,500m ³ obs	141,000m ³ obs	190,500m ³ obs
Total units of supply	57,200	182,875	240,075

Contractual volumes awarded 2017-18	Sawmill Operator and its timber harvesting company	Timber Harvesting Company	Total volume
Roadside timber	65,377 tonnes	0 tonnes	65,377 tonnes
Standing timber	43,321m ³ obs	210,287m ³ obs	253,608m ³ obs
Total units of supply	108,698	264,991	318,985

3.20. As shown in Table 8, the total volume of timber contracted to be sold to the Sawmill Operator and its timber harvesting company and the Timber Harvesting Company under transitional arrangements amounted to 318,985 units of supply. This was 72% higher than the volume in m³ obs offered to the Sawmill Operator on 22 March 2017 and 33% higher than that negotiated with the Sawmill Operator on 28 March 2017.

- 3.21. NRW has told my auditors that the volumes included in the transitional contracts awarded in 2017-18 'were not the volumes intended for supply' and that the contracted volumes have been inflated because the contracted volume in the pipeline contracts includes a significant amount of timber that had been harvested prior to 1 April 2017. I am unclear why NRW entered into new contracts to sell timber that had already been harvested and sold under contracts that had terminated. NRW has told my auditors that whilst it accepts it should have only included 'remaining volume' in the contracts, it never intended to provide higher volumes than those agreed at the meeting with the Sawmill Operator of 28 March and it continued to work to the volumes agreed at that meeting.
- 3.22. The volume contracted with the Sawmill Operator and its timber harvesting company and the Timber Harvesting Company amounted to 39.4% of the total timber volume that NRW had said in its Timber Marketing Plan it would make available to all purchasers in 2017-18. The contracted volume represented 97.6% of the annual volume of roadside sales and 141% of the annual volume of standing sales within the terminated long-term contracts.
- 3.23. On 4 May 2017, NRW's then Chief Executive emailed NRW's acting Head of Commercial Operations requesting information regarding the 'transitional arrangements'. One of the pieces of information he requested was 'a reconciliation between what was agreed in the original contracts and what the company will actually be getting – both in terms of volume and in value'.
- 3.24. On 11 May 2017, the acting Head of Commercial Operations responded by email to the then Chief Executive setting out a rationale for entering into the transitional arrangements. The email states that: 'The decision to wind down the supplies, as shown in the phasing out volumes, was made to avoid damaging the timber supply chain and to avoid adversely affecting NRW's timber income in 2017-18. Immediate cessation of supply on 31 March would have created a huge impact, with harvesting operations being stopped and contractors being put out of work through no fault of their own. Some harvesting contractors and hauliers would inevitably have gone out of business. The lead in time for remarketing the volume would have resulted in a major dip in NRW's timber income which would have been very difficult to catch up on as the spring is the time of year with the greatest demand for timber'. Attached to the email was a spreadsheet which was purported to represent the volume of timber provided to be sold under the transitional arrangements, and the percentage of the original long-term contract volume that would be supplied to the Sawmill Operator by the end of the transitional arrangements. Neither the email nor the spreadsheet referred to the involvement of the Timber Harvesting Company in the transitional arrangements.
- 3.25. A summary of the information provided to the then Chief Executive is set out in Table 9.

Table 9: Volume of timber offered under transitional arrangements as per email from NRW's acting Head of Commercial Operations to NRW's then Chief Executive of 11 May 2017.

	Original LTC volume	Supplied to 31/3/17 under the LTCs	Transitional volume 2017-18	Total supply volume	% of LTC volume to be supplied by 31/3/18
Roadside timber	670,000 tonnes	191,300 tonnes	41,875 tonnes	233,175 tonnes	34.8%
Standing timber	1,475,000m ³ obs	498,200m ³ obs	141,000m ³ obs	639,200m ³ obs	43.3%
Total units of supply	2,145,000 units	689,000 units	182,875 units	872,375 units	40.7%

- 3.26. The transitional volume of 182,875 units of supply set out in the attachment to NRW's acting Head of Commercial Operations email to NRW's then Chief Executive of 11 May 2017 was understated. As shown in Table 3, NRW had agreed at its meeting with the Sawmill Operator on 28 March 2017 to provide transitional volume of 240,075 units of supply.
- 3.27. The covering email from the acting Head of Commercial Operations to NRW's Chief Executive states that 'I have arranged for figures on values to be provided and hope that we can get these to you tomorrow [12 May 2017]'.
- 3.28. On 19 May 2017, NRW's newly appointed Head of Marketing emailed NRW's then Chief Executive attaching an updated version of the spreadsheet provided to the Chief Executive on 11 May 2017. The updated spreadsheet recorded that the estimated sale value of the timber sold to the Sawmill Operator from the commencement of the long-term contracts in 2014 up to 21 March 2017 was £11,013,286. The spreadsheet does not record the estimated sales value of timber contained within the transitional contracts, although this information was requested by the Chief Executive in his email to NRW's acting Head of Commercial Operations on 4 May 2017.

Part 4

4. Contractual sales

- 4.1. NRW set out in its transitional plan that it would phase the sale of the transitional timber (see Table 4) so that 90% of the roadside volume and all the standing transitional volume would be sold by 31 December 2017. In the event 9 of the 11 roadside contracts had contract periods running until 31 March 2018 and sales continued on these contracts into March 2018. Of the 48 standing sales contracts, 26 had contract periods extending beyond 31 December 2017, and 10 of these extended into 2018-19. NRW does not hold any documentation setting out the rationale for its deviation from the transition plan.
- 4.2. Table 10 summarises the volume of timber sold in 2017-18 under the transitional contracts.

Table 10: Timber sold under transitional contracts during 2017-18 compared to total volume agreed with the Sawmill Operator and contracted volume

	Proposal 22/03/2017	Proposal 31/03/2017	Contracted volume	Transitional sales to 31/03/2018
Roadside timber	12,700 tonnes	49,575 tonnes	65,377 tonnes	45,453 tonnes
Standing timber	178,500m ³ obs	190,500m ³ obs	253,608m ³ obs	132,439 m ³ obs
Total units of supply	191,200	240,075	318,985	177,892

- 4.3. In December 2017, my auditors commenced an audit of the transitional arrangements, and since then NRW has sought to minimise the volume of timber being sold under the transitional contracts. This has involved suspending operations on some contracts and resolving not to extend the contract period on other contracts where the contracted volume had not been delivered by the end of the contracted period. NRW estimates that a further 40,300m³ obs of standing timber will be sold to the Timber Harvesting Company in 2018-19 under the terms of the transitional contracts.
- 4.4. The income value to NRW of the timber sold under the transitional contracts in 2017-18 is 2.76 million and is estimated to be 0.18 million in 2018-19.

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We welcome correspondence and telephone calls in Welsh and English.
Rydym yn croesawu gohebiaeth a galwadau ffôn yn Gymraeg a Saesneg.



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Mr Nick Ramsay
Chair
National Assembly for Wales, Public Accounts
Committee
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12 September 2018

Dear Nick,

Natural Resources Wales Response to Annual Report and Accounts Scrutiny 2015/16

In June I wrote to you to outline the approach we have taken in response to the original action plan following the Public Accounts Committee scrutiny of our Annual Report and Accounts 2015/16.

In advance of our session at the Public Accounts Committee on 24 September I enclose an updated action plan summarising further progress.

Since I wrote to you last, I have commissioned Grant Thornton LLP to undertake a comprehensive review of the key commercial business areas, governance arrangements and the behavioural and cultural aspects that led to the award of the Long-Term Timber Sales Contracts and the transitional arrangements that were subsequently put in place. Grant Thornton have already met with me, NRW Board Members and Wales Audit Office. I would note that parts of our original action plan may be supplemented by any recommendations or learning out of the Grant Thornton review.

I would like to take this opportunity to ask whether I am allowed to make an opening statement at our session on 24 September?

With best wishes,

Clare Pillman
Prif Weithredwr, Cyfoeth Naturiol Cymru
Chief Executive, Natural Resources Wales

A copy of this letter has been sent to:

- Andrew Slade, Director of Environment and Rural Affairs at Welsh Government
- Wendy Burris, Welsh Government Sponsorship Team
- Derwyn Owen, Wales Audit Office

PAC Recommendation 1: We recommend that Natural Resources Wales undertake a full evaluation of its governance arrangements relating to contracting processes, clearly setting out lessons learned with specific reference to timber sales contracts referred to in this report.

Action Ref.	NRW Action	NRW Lead	How we will do this	Status	Progress update
1.1 Pack Page 183	Identify the key areas of the organisation that are charged with entering or the ongoing management of contracts.	Executive Director of Finance and Corporate Services	Consider the breadth of NRW operational and corporate work and acknowledge teams that are involved in contract management.	Completed	Teams Identified: <ul style="list-style-type: none"> Enterprise: Timber Production; Energy Development; Other Estate Income; Recreation and Tourism; Analytical Services. Corporate: Procurement; Grants & Partnerships, Future Regulations and initiatives delivered jointly with other bodies
1.2	Review the process of evaluation, negotiation and awarding of contracts and other external commitments for the key areas identified in action 1.1	Head of Governance and Planning	<p>Governance process mapping of Procurement (goods, works and services); Projects (non flood), Projects (flood); Timber Sales; Grants and Collaborative Agreements.</p> <p>The following teams follow non flood project governance processes: Analytical Services, Energy Delivery, Future Regulation</p>	Completed	A continuous improvement project was completed to process map decision making, approvals, roles and responsibilities within our contract management frameworks. This work was superseded by development of the Commercial Activity Governance Policy to support the Enterprise Plan.

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Action Ref.	NRW Action	NRW Lead	How we will do this	Status	Progress update
1.3 Pack Page 184	Review governance arrangements of Sales and Procurement contracts to ensure all 'significant' contracts let without competition (individually or collectively) are: <ul style="list-style-type: none"> considerate of the approval limit within the FSoD of the letting of timber sales contracts the rationale for letting contracts without competition is documented, including clear evidence of matters such as urgency and market conditions or evidence that there is only one suitable or available purchaser; and the letting is subject to consideration of procurement regulations, State Aid and risk of legal challenge. Audit and Risk Assurance Committee will be briefed about the new controls for timber contracts let without competition, (by 7 June 2018) 	Head of Commercial Services - Sales Contracts Head of Procurement - Purchase Contracts	Significant has been defined as £5m for Procurement and £0.5m for Commercial Activity.	Completed	Head of Sales and Marketing has developed a STA form and guidance.
			It has been determined that significant in the context of contracts let without competition shall be the OJEU limit, currently set at £106k.	On-going	We continue to refine our reporting to ARAC and expect the external review by Grant Thornton to inform ways of working
			The Head of Commercial Operations will be responsible for informing NRW's ARAC in the event that a contract without competition reaches this threshold.	On-going	As part of the restructure, recruitment of a new Head of Commercial Services, reporting to Executive Director of Finance and Corporate Services, is underway.
			In addition, Head of (Timber) Sales and Marketing will develop a new Single Tender Action (STA) process which includes clear justification (like that used by Procurement) to document contracts awarded without competition. This process will consider State Aid compliance.	Completed	See above
1.4	Review and strengthen the controls around financial decisions and external commitments which involves commitments entered into without open competition.	Head of Commercial Services - Sales Contracts	Controls have been reviewed along with our financial scheme of delegation and the procedures for current and future activity under the Enterprise Plan. Clarify existing procedures for certain types of commercial agreements such as 3rd party Access requests Where there is no such process, we will develop a generic STA for non-timber	On-going	Grant Thornton are reviewing these controls.

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Action Ref.	NRW Action	NRW Lead	How we will do this	Status	Progress update
			commercial agreements entered into without competition		
1.5	Ensure teams handling contract decisions are aware of NRW response to improve quality of documentation and records of decision making (See action 2.4)	Head of Governance and Planning	Provide training as part of the Public Law Training in action point 2.4	On-going	<p>Our Document Management System (DMS) provides our corporate repository of information and evidence which is used to inform future decisions, provide a clear audit trail and enable historical research,</p> <p>We have already provided staff across NRW with training on using the DMS which is a key tool in providing evidence of transparency and accountability through our decisions.</p> <p>Grant Thornton are reviewing these controls.</p>
	A protocol is put in place for handling post contract negotiations and evidence requirements of any amendments.	Head of Commercial Services	<p>The Head of Sales and Marketing will assess the guidance that we have to ensure it fit for purpose</p> <p>An assessment will be made of the way in which the Timber Management Package (TMP) system embeds the guidance into the business process in a way that is proportionate to risk and the level of authority required.</p> <p>We will evaluate the potential to develop system reports in TMP to monitor performance.</p>	<p>On-going</p> <p>On-going</p> <p>On-going</p>	<p>Grant Thornton are reviewing these controls.</p> <p>Further development of the TMP is currently being assessed.</p> <p>Grant Thornton are reviewing these controls.</p> <p>See above</p>

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Action Ref.	NRW Action	NRW Lead	How we will do this	Status	Progress update
1.7	Enterprise Programme Board to review their process to ensure they are effective in challenging / scrutinising all aspects of new commercial enterprises.	Head of Commercial Services	Following approval of our new Enterprise Plan July 2017 a Commercial Activity Policy Project has been set up to develop governance and scrutiny arrangements of current and future activities under the new structure.	On-going	Commercial Activity Policy approved by Executive Team in June 2018. Detailed procedures are now being drafted.

PAC Recommendation 2: We recommend Natural Resources Wales review its delegation arrangements alongside its awareness raising of State Aid law, public law and the processes for awarding contracts. We recommend the findings of this evaluation are shared with the Public Accounts Committee to enable this Committee to monitor implementation and progress against identified changes.

Action Ref.	NRW Action	NRW Lead	How we will do this	Status	Progress update
2.1	Review the Financial Scheme of Delegation (FSoD) to ensure that the appropriate checks / actions / escalation required when dealing with novel, contentious and repercussive issues are included in sign off procedures.	FSoD Coordinator	FSoD has been reviewed. Instructions are clear however broader examples will be added during our next revision of the scheme.	On-going	An amended definition describing novel, contentious and repercussive transactions was agreed at Executive Team in August 2018 and will be considered for NRW Board approval in September 2018. .
2.2	Review Non-Financial Scheme of Delegation to ensure appropriate checks / actions / escalations that are required when dealing with novel, contentious and repercussive issues are included in sign off procedures.	Governance Partner	NFSOD requires full review in 2018 following Organisational Design restructure of the organisation.	On-going in line with OD timetable.	Organisational Design is on track for 1 April 2019. As part of the restructure, recruitment of a new Head of Commercial Services, reporting to Executive Director of Finance and Corporate Services, is underway.
2.3	Develop a workshop to cover State Aid and deliver to staff in the following teams (deemed as most likely to encounter these issues): <ul style="list-style-type: none"> Grants and Partnerships, New Enterprises, Future Regulations Procurement 	Head of Legal Services	State Aid workshops delivered identified staff during September and October 2017. State Aid staff guidance document prepared.	Completed	5 State Aid workshops have been delivered to 81 staff in identified teams. A guidance document was prepared and shared with all attendees.

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Action Ref.	NRW Action	NRW Lead	How we will do this	Status	Progress update
2.4	<p>Develop a presentation on Public Law including documentation of decision making and concepts of novel, contentious and repercussive issues; and deliver to staff in the following teams (deemed as most likely to encounter these issues):</p> <ul style="list-style-type: none"> • Grants and Partnerships • New Enterprises • Future Regulations • Procurement 	Head of Legal Services	Provide a Public Law presentation to relevant NRW teams.	Completed	<p>8 Public Law sessions have been delivered to 166 staff in identified teams.</p> <p>This is now part of a programme of legal training for staff across the organisation. Further workshops in Autumn 2018 already have an additional 109 staff signed up.</p>
	Share results with Public Accounts Committee through this action plan and subsequent update.	Chief Executive	To be shared with PAC in November 2017.	Completed	Action Plan progress was shared with the PAC in November 2017, a follow up letter in April 2018, and this action plan update in September 2018.

PAC Recommendation 3: We recommend that Natural Resources Wales review its internal governance arrangements to ensure that its accounting officer, Executive Team and Board should have a much greater role in scrutinising contracting processes and the awarding of contracts. It is imperative that these processes are robust with a clear and demonstrable audit trail that decisions have been taken on a fair and sound basis.

Action Ref.	NRW Action	NRW Lead	How we will do this	Status	Progress update
3.1	Review internal governance arrangements to ensure <ul style="list-style-type: none"> • clarity of the remit of Boards and Committees • appropriateness of the escalation routes • effectiveness of the oversight they provide 	Head of Governance and Planning	Board and sub-committee Terms of Reference reviewed during summer 2017.	Completed	All Terms of Reference are reviewed annually.
			We are introducing standardised internal governance arrangements to address planning, performance, risks management, with new escalation routes and scrutiny.	On-going	This review is integral to the work of the Business Boards that are being created as part of Organisational Design and how they will operate. New Executive Team ways of working have been implemented to ensure effective oversight of organisation. Senior management corporate governance training is booked in November 2018
3.2	Review NRW Governance arrangements to ensure all 'significant' income and expenditure contracts (above a financial ceiling to be set by NRW) should: <ul style="list-style-type: none"> • consider the approval limit within the FSoD of 	Head of Commercial Services - Sales Contracts Head of Procurement - Purchase Contracts	Significant has been defined as £5m for Procurement and £0.5m for Commercial Services	Ongoing	The FSoD Co-ordinator in consultation with the Enterprise team is working on ensuring that procedures comply with the thresholds set by NRW and this work will be included as an output of the commercial activity governance project.

Action Ref.	NRW Action	NRW Lead	How we will do this	Status	Progress update
Pack Page 190	<p>the letting of timber sales contracts</p> <ul style="list-style-type: none"> • be referred to Executive Committee/NRW Board for approval; and • be subjected to appropriate scrutiny which may include seeking legal advice on State aid rules and/or compliance with procurement regulations, and formal consideration as to whether the contracts should be referred to the Welsh Government as potentially novel, contentious or repercussive. 				Grant Thornton are reviewing these controls.
	<p>3.3 Roll out an initiative to improve the quality of</p> <ul style="list-style-type: none"> • the documentation submitted to the Boards, Committees and Senior Management Groups • the record taking to document decisions they make. 	Head of Governance and Planning	Revised templates have been established for Terms of Reference, Agenda Planning, Agenda Standing Items, Minutes, Actions Logs Risk Registers etc.	Ongoing	<p>Work continues on standardising Terms of Reference and associated documents for the various Boards, Committees and Senior Management Groups.</p> <p>See above re. Executive Team ways of working.</p>