



## **AUDIT COMMITTEE**

Minutes of the Meeting of the Audit Committee (the Committee) held at British Waterways' London Office, 1 Sheldon Square, Paddington W2 6TT on Wednesday 11 January 2012 at 10.30 a.m.

### **PRESENT:**

Mr N Hugill (Chairman), Mr T Hales, Mr J Bridgeman and Mr R Green

### **APOLOGIES:**

Mr P Sarwal, Dr J Hargreaves

### **IN ATTENDANCE:**

M R Evans, Mr N Johnson, Mr P Ridal, Mr K Labbett, Mr A Glyde (all from BW), Mr J Dodwell (Trustee Designate, CRT), Mr S Maslin, Mr T Lincoln, Ms C Reid (all from Grant Thornton) and Mr M Devin (Prism Cossec, minutes)

### **12/A01 MINUTES OF THE PREVIOUS MEETING**

The minutes of the meeting of the Committee held on Wednesday 14 September 2011 were amended and approved.

### **12/A02 ACCOUNTING POLICIES (BW/A337)**

Mr Ridal introduced a report on (i) the process agreed with the UK and Scottish Governments for the preparation and signing of the statutory accounts following the transfer to the Canal and River Trust; and (ii) the accounting policies to be used in the preparation of the annual report and accounts for the year ended 31 March 2012 or longer period if extended.

The Committee (i) noted the process; and (ii) endorsed the proposed accounting policies appended to the report.

### **12/A03 EXTERNAL AUDIT APPROACH (BW/A338)**

Mr Lincoln presented Grant Thornton's audit approach memorandum, drawing to the attention of Committee members the key points. The date of the transition remained the key determinant driving the audit timetable, to which end Grant Thornton had held meetings with both Defra and the Scottish Government since the last Audit Committee meeting in September and in December had conducted a series of briefings for financial controllers on charity accounting.

Turning to the key audit issues, Mr Lincoln explained that the preparation and signing of the accounts, disclosure of the proposed statutory transfer of assets to the CRT and going concern statement were dependent upon the transfer date. Assuming disclosure of the transfer in the March 2012 year-end accounts, an extensive post-balance sheet event note would be required setting out the basis of the transaction and the proposed business model going forward in terms of funding.

The Committee agreed that a nuanced approach to the writing of the Group overview section would be required, including a full narrative report documenting the achievements of the past 50 years up to the transition to the CRT and sensitive to the concerns of a cross section of interest groups. To this end, **it was agreed** that a short form annual report should also be produced.

PR

It was noted that the going concern statement would apply to the 12 months from the date of the signing of the financial statements in relation to the trade and assets relating to BW Scotland post-transfer of the BW England & Wales assets to the CRT.

Mr Lincoln drew the Committee's attention the increase in the pension deficit to approximately £125m as at the date of the last valuation (30<sup>th</sup> November 2011), which was due to falls in gilt yields. Grant Thornton's actuarial specialists would be reviewing the valuation and actuarial disclosures to ensure appropriateness. Mr Bridgeman cautioned that several of the assumptions might be liable to significant change, prefacing his remark by declaring his interest as a pension fund trustee.

Mr Lincoln next considered the post-transaction accounting implications. Acquisition fair value accounting principles would be applied to assets transferred to the CRT and, in general, the accounts of the CRT would need to be prepared in accordance with UK GAAP and the Charity SORP and Mr Lincoln advised the Committee to seek the views of the Charity Commission with regard to the issue of accounting format. Mr Johnson, commenting on State aid, emphasised the importance of representing this as a continuation of ongoing Government support.

The Committee noted and approved Grant Thornton's fee proposal. Mr Ridal anticipated some revision to the figures set out in GT's report, specifically with reference to the transfer audit, and so with no further meetings of the Audit Committee scheduled until after completion of the statutory audit, **it was agreed** to delegate authority to Messrs Hugill and Ridal to consider and, if appropriate, approve modest incremental fees for advisory work in relation to this work. In addition, the Committee approved audit advisory work above £12,500.

NH/PR

Mr Evans queried Grant Thornton's position in relation to the procurement rules in the event that vesting was delayed beyond 31<sup>st</sup> March 2012. Mr Maslin explained that, in the event of a delay, Grant Thornton's current appointment covering the 2011-12 financial year would be extended automatically and that an issue would arise only if GT were commissioned to undertake work relating to the 2012-13 financial year.

## 12/A04 AUDIT COMMITTEE ARRANGEMENTS (BW/A339)

Mr Johnson tabled an appendix dated 10<sup>th</sup> January to his paper dated 21<sup>st</sup> December 2011, which set out the process, responsibilities and proposed timetable for the preparation of the annual report and accounts and Scotland separation assuming a vesting date of 31<sup>st</sup> March 2012. The appendix set out a suggested arrangement in the event of a delay in vesting as now seemed likely.

If the transfer were to be delayed beyond 1<sup>st</sup> April 2012, it was proposed that the annual report and accounts should be prepared as normal and laid before both the UK and Scottish governments as in previous years.

Any transfer to the CRT after 1<sup>st</sup> April would be accounted for as a disposal of assets from BW to the CRT as a significant transaction during the year ended 31<sup>st</sup> March 2013. BWS would then report on the period from 1<sup>st</sup> April 2012 to the transfer date (BW trading as a GB entity) and from the date of transfer to 31<sup>st</sup> March 2013 (Scotland only entity). Mr Johnson confirmed that the executive had endorsed this approach and further stated that the draft Transfer Order could be changed to accommodate this proposal. **It was agreed** to approve the approach outline above.

NJ

Mr Hugill enquired at what point it would be appropriate for BWS to select an auditor. Mr Johnson explained that the BW Board was able to make this selection subject to the approval of the Scottish government and that BWS could then either retain the appointed auditor or select an alternative auditor at some future point. Mr Maslin said that Grant Thornton would be happy to be appointed as auditor if invited to do so by the Scottish government. Mr Bridgeman emphasised the importance of carrying out the post-transaction audit in accordance with a timetable of the trustees' choosing rather than by a deadline imposed by government.

#### **12/A05 RISK UPDATE (BW/A340); CRT RISKS (BW/A341); SCOTTISH SEPARATION RISKS (BW/A342)**

Mr Evans presented an update on the corporate risk dashboard, highlighting the principal changes to the previous version, and asked the Committee to consider the current risks and adequacy of the management actions being taken.

##### Risk update

Environmental regulation remained a red risk because costs and obligations remained undefined. Similarly, the continued water shortage had resulted in a planned £700k spend on measures to improve flows into the waterways network to mitigate the impact of a potentially dry summer. On a more positive note, joint venture performance/banking covenants had moved from yellow to green following the exit from Gloucester Quays and reduction in Isis debt. It was also anticipated that the gap in steady state funding would narrow following the completion of the funding agreement.

The Committee discussed at length the issue of staff morale, which remained a red risk. This was being impacted not only by the transition to the third sector but also the planned re-location from Paddington to Milton Keynes. Strenuous efforts continued to be made using a variety of means, including focus groups and 'mending the line' initiatives to encourage line managers to manage staff expectations more appropriately although, as Mr Green noted, staff anxiety was quite normal given the extent of the changes now underway. Mr Green added that the executive team should focus also on the impact of the changes, especially Scottish separation, on IT systems. Mr Evans acknowledged that this was an area of weakness for many organisations undergoing change but said that this had received close attention and that 85% of systems remained unaffected by the planned changes.

### CRT project risks

Mr Evans presented Mr Stirling's report dated 23<sup>rd</sup> December. The principal movement in risk related to the parliamentary process, in particular, the 60-day consultation process to be conducted by the Efra Committee. Mr Bridgeman said that there should be no moratorium on good news stories during this period relating to the work being done by BW/CRT. The vesting date was likely to be delayed until June on account of the scrutiny process for the Transfer Order although this was outside the control of BW/CRT.

### Scotland risks

Mr Evans presented Mr Dunlop's report dated 4<sup>th</sup> January. It was noted that proposals were being developed to grant delegated authority to BWS and these would be considered by the BW Board in either March or April.

It was noted that Scottish Government would be unable to appoint Grant Thornton as auditor until after the Transfer Order had completed its passage through parliament. Mr Hugill requested that this be communicated to Dr Hargreaves.

## **12/A06 INTERNAL AUDIT PLAN 2012-13 (A/343)**

Mr Labbett presented the Internal Audit plan and asked the Audit Committee to comment on and approve the general direction of travel and coverage of the plan.

Mr Labbett explained that the plan had been developed to cover the period 2012-13, the first period of the CRT, allocating resource over a range of carefully identified strategic objectives. Whilst most of the key processes and standards remained unchanged, a new workstream relating to compliance with the regulatory regime for charities had been factored into the plan. It was acknowledged that, as the trustees considered the developing risk profile of the CRT, they may wish to re-prioritise tasks and include new ones into the internal audit plan.

The Committee considered the role of the corporate website in attracting donors and volunteers for the CRT. Mr Evans said that the website would be a critical gateway for potential supporters and Mr Hugill enquired how the Internal Audit team might assist in the management of the risks associated with the website. Mr Labbett replied that this area was receiving attention and that more work would be done in the forthcoming financial year to provide assurance as to the resilience of the new website.

The Audit Committee approved the internal audit plan and commended it to the Audit Committee of the CRT.

## **12/A07 INTERNAL AUDIT PROGRESS REPORT (BW/A344)**

Mr Labbett introduced his report, stating that the work of the Internal Audit Team during the period had included efficiency, safety and performance measurement reviews. As a result of this work, an issue had been identified relating to contract management and the need for improved tendering processes and a methodology for investigating potential irregularities.

Mr Glyde summarised the precise nature of the irregularities and steps being taken to address these. A supervisor had on five occasions shared tenders from one company with another whilst both were competing for the same tender. Consequently, one company had an unfair advantage over the other and BW had awarded contracts unfairly. It had transpired that the supervisor had in June 2011 declared a relationship with the relevant company but had not done so on his previous returns.

This extent of this risk was considered to be more likely in the case of small contracts, ie those below £20k, at which point more formal tendering processes are applied. In the instance cited, the same individual had both commissioned and certified the work.

Appropriate management action was in progress to address this problem. Specifically, the Internal Audit and Legal Departments had worked closely together to establish a framework to underpin a more robust contract management system and Vince Moran was implementing the agreed procedure.

Mr Hugill enquired how this issue might have been identified had the incident cited above not occurred. Mr Labbett replied that his team carried out healthchecks to identify trends, for example, an increase in the number of contracts awarded to a specific contractor. In the case cited, Internal Audit had identified similar trends in the same location and was working with the Legal and HR Departments to address the issue. A further update would be provided in a subsequent report to the Audit Committee.

Summarising, Mr Green, whilst noting the actions outlined above, stressed the importance of ensuring that the Audit Committee concentrated on managing principles and policies and not on managing outcomes.

The Audit Committee noted that the Property Committee would be considering a report at its meeting on 1<sup>st</sup> February on the risk management process for the acquisition and ongoing management of Daisyfield, an investment property believed to have been underperforming since its acquisition in July 2007. The key point for the Audi Committee was that a more robust process had superseded the investment policy in place at the time.

## **12/A08 DATE OF NEXT MEETING**

Mr Johnson hoped to be able to provide greater clarity by the end of February as to whether the next scheduled meeting on Wednesday 13 June would be a meeting of the BW or BWS Audit Committee.

There being no further business, the Chairman closed the proceedings at 1:00pm.

---

**Chairman**