

Written submission from Alan Sutherland, former Chief Executive, Water Industry Commission for Scotland, 4 November 2024

Introduction

- I served as the Chief Executive of the Water Industry Commission for Scotland from 1 July 2005 until 31 December, 2023. Prior to that, I was the Water Industry Commissioner for Scotland from 1 November 1999. I had a one-month introduction to Government during October 1999.
- I became an economic regulator as I considered that a public sector water and sewerage operator could be at least as efficient and effective as a private sector operator.
- I consider that WICS under my leadership, in partnership with the management and workers of Scottish Water, and Scottish Government, achieved considerable success in overseeing a significant improvement in the performance and cost effectiveness of the water industry in Scotland. The Scottish water industry was widely regarded as a laggard in 1999, it is now recognised internationally as a leader and, among other things, lead the way in introducing competition in the supply of water to business customers.
- I am proud of the efforts of WICS to develop a separate source of income. This amounted to, I think, around £4m over the years after direct disbursements (almost double our annual levy from Scottish Water).
- Looking back I was spreading myself too thin in performing my central role as economic regulator, in earning fee income for WICS, and in administering the office. I now recognise that I paid less attention than I should have done to the administration of the office.
- Following the retirement of my Deputy CEO, I had thought that I had put a suitable structure in place to support me in the management of the day-to-day activities of the Office. I was working very extended hours and had high expectations of myself and the output of the Office. As such, the shortfalls identified were not due to a lack of effort or commitment on my part.

Nature of this evidence

- On leaving WICS, I was required to delete or destroy all materials relating to my employment. I did not question this request.

Therefore, I have no written records, calendars or other information to inform or substantiate the evidence that I now provide. My intention in providing answers to the Committee is to be as accurate as possible, but I am relying only on my memory of events.

Responses to the Committee's questions

1. The Auditor General for Scotland (AGS) published his section 22 report on 20 December 2023.

Q1: Do you accept the findings of the section 22 report, if not, can you set your reason(s) why?

- I accepted the findings of the section 22 report. I wrote a response to the draft findings, agreed with my Chair (and, I think through the Chair, the other members of the Board).
- As I will explain later, I thought it important to try to explain the context of WICS' work, its dual role and its success in earning substantial outside revenue.
- The draft conclusions of the audit were a surprise. In previous years, WICS had always received a positive audit report and, before receiving the draft report, I had no reason to expect anything different. There were two aspects that particularly surprised me.

Training programme

- The training programme for the COO was not, as the Committee heard, a new initiative. Indeed, the high demands for strategic and analytical thinking required of the senior management of an economic regulator, especially one as important as WICS, had led to the office investing in similar training programmes on several occasions. There had always been a significant benefit both for the employee (personal development) and for the office (upskilling) in these programmes and, tangibly, in the cost savings that flow directly from staff retention.
- It was well known both among stakeholders and in the Sponsor Team that WICS invested in such courses.

- As far as I was, and am, aware, the Office followed the same approvals process for the training programme of the COO as the Office had done previously. These training programmes would have been reviewed as part of previous audits and, as such, I had thought that we were acting appropriately.
- I always considered the willingness of WICS to invest in its employees was an important retention tool given that the salaries that could be paid to key staff were lower than they could earn elsewhere.

Sub-let

- I was also surprised by the finding regarding the sub-letting of Moray House.
- During the Pandemic, WICS, in line with Government guidance, worked from home. WICS was well prepared for working from home because of efforts that had been undertaken to strengthen the resilience of the Office with access to IT and communications equipment.
- WICS was aware that its downstairs neighbour, Zero Waste Scotland (ZWS), had an interest in the WICS office space. It seemed prudent to offer ZWS the use of the WICS office space. I consider that the agreement with ZWS was beneficial to both ZWS and to WICS. ZWS got space that it required adjacent to its principal location. WICS did not pay for office space that it was not going to use.
- A price was agreed that, if continued to the end of the lease (2026, I think) fell just short of full cost recovery. It fell short by the proportion of the likely future liability for dilapidations that related to the years of the sub-let.
- However, it is important to note that if the sub-lease did not run until the end of the WICS lease term, ZWS would not have benefitted from a nine-month rent free period that had been negotiated at the start of the lease in 2010/1 (to apply only if the lease was extended beyond its initial 10 year term). This nine months' rent would have more than covered any likely dilapidations.
- I accept that, in an ideal world, the contract with ZWS would simply have mirrored the WICS contract with Stirling Council (the principal

landlord). I therefore understand why the auditor referred to the arrangement. However, the arrangement agreed with ZWS was their best and final offer and there was little prospect of WICS using the space for which it was contracted to pay.

- I believe the outcome was satisfactory and in the best interests of WICS and the Scottish Water customer (who funds the WICS levy).

Expenditure

2. During oral evidence on 21 March 2024, the Chair of WICS Audit and Risk Committee (ARC) commented that he had regular conversations with you “about public reaction to excessive spend, so there were challenges at the time.”

Q2: What are your recollections of these discussions and the challenge by the Chair of WICS ARC, in respect of expenditure?

- My only recollection of interactions on expenditure with the Chair of the ARC (outside of the regular ARC meetings) before the results of the 2022/3 Audit were being finalised was my use of flexible plane tickets. My domestic situation required this flexibility and I had thought that I had the agreement of the Chair for what I was doing.
- I was always conscious that expenditure related to the office’s Hydro Nation activity should always be carefully labelled as such. With hindsight, it has become clear that this could have been done better.

Q3: Did anyone else in WICS challenge you regarding expenditure? If so, what was your response? If not, why do you think that might be?

- All expenditure of £5,000 or more was discussed by the senior team at what was termed ‘the Approvals Panel’. This sometimes was a relative formality (where expenditure was obviously required and not contentious) but, importantly, on some occasions, it led to a robust debate as to whether a proposal to spend was justified or not. I always considered the nature of these challenges to be healthy and constructive and considered that the senior team felt able to express their views on expenditure.

3. The Committee is aware that senior staff attended management courses that incurred substantial costs, for example courses at the Harvard Business School the London Business School and Columbia University. The Committee is also aware from the Grant Thornton report on Governance and financial arrangements and WICS's internal review of transactions that significant expenditure occurred in relation to meals, such as those that took place at L'Escargot Blanc and The Witchery in Edinburgh.

Q4: Can you explain why this type of expenditure occurred, and on reflection, do you consider that this type of expenditure could be considered as “excessive spend” for a public body?

In my view, it is important to separate these expenditures into three separate categories: the MBA arrangement; the Senior Management Training; and meals.

MBA Arrangement

- Any economic regulator relies on the quality of its analysis. As such, there is a vital need to attract and retain the best possible analytical talent in a highly competitive market for talent and where, almost invariably, the private sector alternatives offer more attractive salary packages.
- The office sponsored experienced analysts to study for an MBA. This arrangement was, to my recollection, agreed on two separate occasions with the Scottish Government. I still consider that this arrangement has been important both in the demonstrated retention of analysts and in their upskilling. More subjectively, it encouraged new, less experienced analysts to remain at WICS and to strive for the level of performance that would lead to the MBA sponsorship being offered.
- The arrangement worked as follows. To be eligible, an analyst had to have five years' experience with WICS (or with WICS and in another organisation requiring similar skills). The analyst had to be performing very well, documented in appraisals. If these conditions were met, the analyst became eligible for MBA sponsorship.

- One third of the cost would be paid by WICS. Two thirds of the cost would be the subject of a contract with the analyst. Under the contract, the analyst would be liable to repay the remaining two thirds of the cost to WICS. The analyst had an option to return to WICS (from a WICS perspective, the ideal situation) for a minimum of a further two years and, by so doing, extinguish the debt.
- This structure was used, as far as I recall, four times. Once for a programme at INSEAD in France, once for a programme in London run by the Booth School of the University of Chicago and twice for London Business School.
- On one occasion, an employee decided to leave WICS and repay the debt owed. On the other three occasions, the office benefitted considerably from the initiative. The employees returned and put their learning to use. They had received an excellent training and had had exposure to high quality fellow students and faculty. Not only did this give WICS access to a quality of employee that the office's pay-scales would not have allowed for, but it also ensured a level of experienced staff retention that is particularly important in a small office.
- I am firmly of the view that this programme was conducted well and benefited WICS and Scotland.

Senior management training

- The senior management training was also funded four times that I can recall. In each case, the training need was agreed in a performance appraisal. The choice of programme was left to the employee.
- My expectation was that the employee should identify a course that offered a programme that met the development needs identified in the appraisal. There is a very wide choice of short courses available. I maintained that the focus of the course should be tailored to the development needs of the individual. I often cautioned that it was worth checking the credentials of the faculty that would teach the course.
- There were no retention restrictions on these courses and this was, with hindsight, potentially, an oversight on my part. I fully expected the employee return to the office and this is exactly what happened.

In each case, the employee did however return to the office. The seniority of the staff that attended these courses had seemed to me to make it highly unlikely that they would leave WICS.

- The use of these courses was discussed with the Sponsor team of WICS at the Scottish Government and I was certainly never made aware of any concerns nor did I see any basis for concerns.
- The Board of WICS also knew about these courses. They too never, as far as I recall, expressed any concerns. The Board provided an opportunity to each member of staff to discuss their experience and their learnings.
- In one of my performance reviews, the benefits that I could receive from enrolling in a similar course were discussed. I never did enrol, because I never felt that I could free up the time that would have been required.
- I firmly believe that training is vital especially for senior staff. I acknowledge it is expensive, but it should be seen as an investment in human capital, good for WICS (as it increases the resilience and capability of the office) and for the Scottish water industry (as it makes WICS a more effective economic regulator).

Dinners

- As I recall, the WICS Corporate Plan in 2021 explicitly allowed for expenditure to develop the Office's international footprint and increase its international revenue. To my mind, this specific line item agreed in the Corporate Plan formalised an understanding that had been in place for several years, dating back to the EU funded assistance to the Romanian regulator of public services. Hospitality is an element of consultancy life.
- I recall only one dinner at the Witchery. It was with visitors from a similar organisation to WICS in Australia. The cost of such a dinner would (or should) have been tagged to our Hydro Nation activities and covered by the income generated.
- The dinner at L'Escargot Blanc followed an all-day strategy session with the Scottish Government. That day's discussions included how we might progress WICS's international activities and how Scotland could fund the levels of investment that it would require in its water industry. These strategic discussions continued throughout dinner.

At the time, I considered that this event was covered by the agreed allowance for the development of WICS' international activity. No-one at the time, or afterwards during my tenure, suggested otherwise.

4. In the section 22 report, the AGS states— “Unusually for a public body, the Commission’s existing policies do not explicitly prohibit the purchase of alcohol as a business expense.”

Q5: Why did WICS not have a policy that prohibited the purchase of alcohol as a business expense? Was this something that was ever challenged by the Board or by the Scottish Government’s sponsor team?

- I was unaware that WICS should have a policy prohibiting the purchase of alcohol. My limited exposure to other public organisations gave me no reason to think such a policy was in force at these organisations or required by WICS.
 - WICS’ internal auditors were diligent in suggesting where WICS did not have policies that were up to date. I do not recall the absence of such a policy being highlighted to me.
 - At no time did either the Scottish Government or the Board suggest to me that such a policy should be introduced. Both were well aware that WICS had no such policy.
5. In relation to the approval of expenditure for the Chief Operating Officer’s participation in an advanced management course, as set out in the section 22 report, the Director-General Net Zero stated during oral evidence— “From what I can see, there was a failure in the policies and their application. The framework was pretty clear about the responsibilities of the board, the chair, the chief executive and the sponsor team. In this case, the delegated authorities were breached and the proper process was not followed.”
 6. When asked, during the same evidence session why the internal audit team had not picked up expenditure relating to the Harvard Business School course, the Chair of WICS ARC stated— “The

challenge there is that the CEO had chosen to interpret the rules in a way that suggested that he did not need to refer the matter to anyone, to take anyone's advice or to run it by anyone”.

Q6: To what extent do you agree with the above statements made by the Director-General Net Zero and the Chair of WICS ARC?

- I can understand the view expressed by the Director General Net Zero. His view is consistent with that taken by the Auditor General.
 - However, both my Board and the Scottish Government were made aware that this training programme was planned. They also knew that WICS consistently invested in the training of its staff.
 - As I noted earlier, I had thought that the office was simply following the same process as it had done previously and, as such, had been subject to audit.
 - With hindsight, I can now see that the COO's choice of Harvard (given its fame and perceived prestige) may have made this course more contentious than the courses at Dartmouth College and Columbia that members of staff had chosen previously.
 - I note the view of the Chair of the ARC. From my perspective, the Board was well aware of the course for the COO and, as I said, later gave her opportunities to discuss her experience.
 - I discussed the proposed training with the sponsor team. The development need for such a course was identified in the appraisal of the COO carried out by my then deputy CEO.
7. In his letter of 27 February 2024, the AGS provided a copy of correspondence between the Scottish Government and you in respect of the two areas identified in the section 22 report where Scottish Government approval should have been obtained for expenditure relating to gift vouchers for staff and a training course.
8. In your email to the Scottish Government of 2 November 2023, you describe the expenditure relating to gift vouchers as being “an oversight on our part.” Regarding the training course, you stated that it “reflects a different interpretation of appropriate rules – but, on reflection, we should have alerted you to the expenditure.” You go on to explain that— “Our procurement policy requires expenditure over

£100k to be approved by the Scottish Government, and over £20k if it is a single supplier purchase. We did not seek approval for this purchase since it was below £100k and it wasn't the type of purchase that could be competitively tendered. Audit Scotland believe we should have sought approval”.

9. In his section 22 report, the AGS is quite clear that “Scottish Government approval is required for any service above £20,000 that has not been awarded via a competitive tender exercise”.

Q7: On reflection, do you still consider that your interpretation of the rules in the procurement policy, as you have set out in your email of 2 November 2023, is correct?

- The issuing of Christmas vouchers to staff above the appropriate limit was a genuine oversight. WICS did not have any form of funded Christmas party or lunch and had developed a custom of providing a modest gift, in line with the rules, to staff at Christmas.
- The offering of the £100 vouchers was actually suggested to me by a member of the senior team. The rationale was that the staff had worked particularly hard and helped earn record levels of international income during the year. I considered the suggestion to be very sensible and appropriate in the circumstances. I was not aware that the amount offered exceeded any limit and, as far as I can recall, no-one raised this with me.
- I recognise that I should probably have been aware that there was a limit but the total cost of this Christmas gesture was, I think, less than 2% of the external revenue earned in that year.
- I have explained the background to the decision on the training course above. It followed, as far as I remember, the approval procedures in the office. I considered that I was doing the right thing for the office and for the individual concerned. As I have explained previously, training was an important retention tool and the office certainly always benefitted from the experience gained by colleagues from attending these training programmes.
- Obviously, if I had understood that the office had not followed proper procedures previously, I would have acted differently. However, I did agree with the appraisal finding that it was in the

interests of WICS and the COO for her skills to be developed further.

10. The WICS submission of 10 June 2024, set out that WICS's internal review of transactions identified the provision of legal advice through a King's Counsel (KC). The WICS submission of 31 July 2024 stated that—

“A retainer has been in place to secure the services of a member of the King's Counsel with specialist regulatory knowledge for more than a decade...In the months following my appointment I have since removed the retainer for the services of this KC.”

11. The issue of the KC retainer was discussed during the oral evidence session on 19 September 2024, where the Interim Chief Executive of WICS confirmed that the KC contract had been terminated and provided information on how specialist legal advice could be obtained going forwards.

Q8: In respect of the KC retainer, the Committee is keen to establish—

- **Your reasons for having a KC on retainer for over a decade.**
- **Whether this arrangement was ever reviewed.**
- **Your views on the new approach that is now being taken by WICS to seek specialist legal advice.**
 - The legislation surrounding charging, performance expectations and the process for Strategic Reviews of Charging is rather complex. As I understand it, the Scottish Government recognised this complexity and was planning a major piece of legislation to address these issues.
 - The opinion of a KC had been essential on many occasions during the period of the retainer. This is a highly specialist area and the KC in question had absolutely unparalleled experience in water regulation.
 - The Sponsor Team was well aware of the retainer arrangement that WICS had with the KC and on a good few occasions asked WICS to test a viewpoint with the KC. One relatively recent example was on the timing of the next Strategic Review of Charges.

- The retainer was included in the WICS’ budget and, I think, specifically mentioned in the Corporate Plan.
- It is considerably cheaper to be able to access the same expert over time and much cheaper than appointing a lawyer to the permanent staff who, most likely, would not have the specialist expertise in any event. This ensures that there is no cost associated with ‘getting up to speed’ and that there is an appropriate institutional memory that understands what has happened and why it happened.
- The nature of KCs is that they operate, as I understand it, on a ‘taxi rank’ principle – first come, first served. The retainer ensured that the KC should not do anything that conflicts with the interests of WICS and that he should always be available (often at short notice).
- The arrangement with the KC was discussed internally in the preparation of each iteration of the WICS Corporate Plan.
- I do not know how WICS will in future access the expertise previously provided by the KC, but my understanding is that WICS and its solicitors may consult him as and when required. Importantly, he will only be able to assist if he is free of conflicts and available. I would worry that the lack of a retainer could both increase cost and reduce the consistency of institutional memory.
- I regard the advice and support that I received from the KC as having been of the utmost importance. WICS would have been less successful in its regulation of Scottish Water and its development and stewardship of the non-household retail market if it had not had access to this advice and support.

12. Both the WICS internal review of transactions and the Grant Thornton report identified instances where WICS’s policies relating to the booking of travel had been breached. The Grant Thornton report highlighted two flights which had been booked on a credit card, where the travel provider had not been used for booking. These flights were to Brasilia (£6,753.25, 10/7/2023) and Kigali (£4,600.15, 1/11/2023).

13. During oral evidence, the Interim Chief Executive of WICS stated—
 “Both those particular trips were for the former chief executive officer.

The one to Rwanda was for an International Water Association conference; the other was for a peer review exercise that he was undertaking in Brasília, which had been commissioned by the Organisation for Economic Co-operation and Development. Both trips were booked by the former CEO himself, using his own credit card. That was not in line with the applicable policy at the time, which was to utilise Corporate Travel Management, the Government approved travel provider, unless it could be demonstrated that better value could be achieved elsewhere.

Q9: Can you explain your decision to book these flights on your credit card rather than following the policy of booking travel through the Government approved travel provider?

- As far as I can see from my personal records, the Credit Card used must have been an Office card in my name.
- My experience over the years of the approved travel provider had been very poor – both with regard to pricing and to responsiveness in the event of a change in plans. I needed flexibility in my travel arrangements and also sensible routings (allowing, for example, bags to be checked to a final destination).
- On frequent occasions, I was accessing better prices than were offered by the travel provider. On occasion, I was asked by colleagues to allow them access to rates that I was being quoted.
- It should be noted that the trip to Rwanda did not take place and the ticket was refunded less a modest administration fee. The trip to Brasilia on behalf of the OECD was paid by the OECD. I was working to particular timings as required by them and to a particular, and limited, budget. Only by taking a route via Sao Paolo was it possible to stay within the budget allowed by the OECD. My experience suggests that it would have been unlikely that such a solution would have been offered by the travel provider.

Staff training

14. In a written submission to the Committee of 24 April 2024, WICS's Chief Operating Officer stated that when preparing her development

plan— “My plan included courses at the Said Business School in Oxford and Edinburgh Business School at costs of less than £10k. Over the course of the next few months and several conversations, Alan insisted that I focus on 5 schools in North America, suggesting Harvard, Yale and Stanford, as he considered these to be much more appropriate for my development.”

15. During oral evidence on 21 March 2024 (col 19) and 19 September 2024 (col 26), the WICS Chair also stated that you had a preference for staff to attend training courses in the United States.

Q10: Do you agree with the above comments regarding your preference for these courses and if so, can you explain why?

- I recall only two conversations with the COO on the subject of her planned training. There may have been other discussions with colleagues. The first conversation that I recall explained the potential benefit of such training and focused on the desirability of identifying a course that would meet the development needs that had been agreed in the COO’s appraisal with the Deputy CEO. I explained how the two options that WICS had used previously (Dartmouth College and Columbia) had worked precisely because they had met the development needs of the participants. I suggested that the COO review a range of courses and suggested London Business School, INSEAD, the Judge School at Cambridge, SAID at Oxford and various US schools. I would not have suggested Yale as I was unaware of its school of business.
- At no time do I recall suggesting that the US options were intrinsically superior. WICS has recruited successfully from the Judge School, and funded four analysts to attend LBS, Booth and INSEAD. Each of these options had received very favourable feedback from the participants.
- The second, and only other, conversation that I recall, took place when the COO had herself narrowed her choice down to three options. I do not remember the third option, but the first two were, I think, Stanford and the Harvard option that was ultimately chosen. I did not know enough about any of the suggested options to provide any form of steer other than to reiterate that the content of the

curriculum and the faculty teaching the course should be seen as the deciding factor in making a final decision.

- I note the Chair considers that I had a strong preference for US options. As I have sought to make clear, I consider that the nature of the curriculum and the faculty delivering the course should be the decisive factor and not the location of the school. This informed my approach to this topic as evidenced by the fact that WICS staff attended UK and European courses as well as US ones.

16. We understand from the Director-General Net Zero's response of 10 June 2024 and WICS's submission of 31 July 2024 that WICS had an MBA policy in place to help retain senior staff.

Q11: Can you explain the particular difficulties WICS faced in retaining staff and whether any alternative options were considered or implemented to help improve staff retention?

- As I mentioned previously, WICS submitted an initial MBA policy and then, I seem to recall, a second refined version a few years later.
- It is incorrect to say that the MBA initiative was designed to retain “senior staff” – it was targeted at experienced analysts, who were still at a relatively early stage of their careers. There were two principal motivations for the MBA policy.
- The first was to encourage analysts to stay longer with WICS. WICS had quickly built a reputation as a place where budding analyst talent got a good training and broad exposure to regulatory issues.
- WICS was regularly losing analysts after a relatively short period (from memory, I think the average stay was less than three years). These analysts were typically able to increase their salary by a substantial percentage by making the move into the broader finance or regulation arena.
- As a rule of thumb (before the Hydro Nation work started), it took about a year to provide the basic training and experience, a further year to consolidate this experience and the analyst was generally very productive from year three. This timeline for training was closely linked to the cycle of resetting charges every four or five years as was the practice at that time.

- The second rationale for the MBA policy was to develop future senior staff in house. This was a critical need for a small organisation that needs to have a strong degree of resilience in its senior management team.
- When the Director of Competition left in 2008 and the Director of Analysis retired around 2011, WICS was faced with a challenge given the loss of experience and senior level resource. WICS engaged recruitment consultants to support its efforts in trying to replace these individuals.
- During these search processes, it became clear that the market rate for replacing the most senior members of the team (when the Director of Competition left in 2008 and when the Director of Analysis retired around 2011) was considerably in excess of the salary scales that WICS had agreed with the Scottish Government. I discussed with the Sponsor team whether WICS could do anything to adjust scales, or as an exception, pay this higher amount. I was informed that there was nothing that could be done.
- In neither case were WICS able to replace the previous post holder with an individual who would have been an immediate – or even a medium term - like for like replacement. WICS was prepared to offer the maximum rate within the agreed salary band for the Director role. The recruitment consultants could not identify an affordable short list.
- The Booth programme was instrumental in helping an individual grow into the competition role. This individual remained with the office for more than the minimum two-year period but was recruited [REDACTED] as a Senior (Board member) Director. Again, WICS could not have matched the salary that was on offer.
- Two of the senior team that I had in place at the end of my tenure had benefitted from this MBA incentive.
- I consider that the office benefitted considerably from these programmes and would have been less effective in the absence of this important investment in key, high performing, staff.

Other options

- Initially WICS paid bonuses to staff based on their performance against objectives. These bonuses were agreed with the then

Scottish Executive. The bonuses often varied significantly reflecting differences in performance. They could be zero. They were also structured to encourage staff to remain loyal to WICS (the potential size of bonus available increased during the regulatory control period) so that WICS had the structure to deal with the price control for the next control period (the most intense period of the regulatory cycle).

- Around 2010 (from memory), the Scottish Government required WICS to remove bonuses. No other financial incentives were available to WICS.
- As far as I can recall, most of the really good analyst leavers left because of the difference in remuneration available to them elsewhere.
- It is still not clear to me what else, beyond the training offer, WICS could have done materially to improve the retention of its most talented analysts.

Dual role

17. The Chair of WICS ARC stated during oral evidence on 21 March that “There is a lot of tension in terms of approach between running a domestic regulator—a small body—and an international consultancy” and that clear guidance was required in this area. This subject was also discussed during the oral evidence session on 19 September 2024, where the Chair of the Board stated— “I still suggest that we need to continue to undertake hydro nation-related activity, but in a way that allows us to separate the functions, as you suggest. There is a grey area, and it is quite difficult to combine the two, as you just outlined—I accept that conclusion. That is under review, in discussion with the Scottish Government, which the Government witnesses can confirm. The issue is on our horizon, and it is very important to have greater clarity.”

Q12: What challenges and difficulties did you face in leading an organisation with a dual role as a public body regulator and an income stream generator?

- There were real challenges with regard to the development of revenue earning work.

- There was an initial Board concern about the office being distracted from the 'day job'.
- When Government took steps to make it clear that WICS should be pursuing revenue generating opportunities, there were further concerns about whether WICS had an undue competitive advantage due to its core levy funding from Scottish Water. Legal advice was taken to provide reassurance to the Board (and the Scottish Government informed).
- There was also a concern as to whether WICS could actually earn enough revenue to make the efforts worthwhile and would receive this revenue.
- I felt a consistent pressure from Government to identify and pursue opportunities. This pressure increased when Scottish Water started to do less in this area.
- Government would often ask for material for documents that they were working on. The international activities featured in the Government's report to Parliament on 'Scotland as a Hydro Nation' and in considerations about the potential for revenue generation by public bodies.
- Throughout this time, there was discussion as to whether there should be a separate legal entity established to ring fence the costs and resources of the revenue generating activity. A registration of a company name 'WICS International' was completed, but never activated.
- My own view had always strongly favoured a separation of these activities.
- After the success of the EU funded Romanian project, Government was keen to explore whether a separate entity could be established within the EU or perhaps through the Scottish Government presence in Brussels to continue to access EU funding. The EU officials with whom WICS had worked appeared to be keen.
- Over the last several years, there was frequent WICS Board discussion as to whether projects should be pursued and whether or not the new entity should be triggered. There were strong arguments in favour (the separation of resources), but the residual concern about cross-subsidies remained. It never happened.

- There was a need for tax and accounting advice. WICS always sought to manage these obligations very diligently. The costs of this advice were relatively modest relative to the revenue generated.

Q13: What advice, if any, was sought and received from the Scottish Government Sponsorship Team on how to balance the requirements of an income stream generating organisation against the requirements it was required to adhere to as a public body, such as those set out in the SPFM?

- A legal separation of WICS revenue generation activities was discussed frequently. Government tended to be more supportive of a separation in discussions about how this might be pursued when revenue was being earned at the time.
- I certainly do not recall any discussion of how these activities sat with the SPFM.

Q14: What clarity, if any, do you feel would benefit a public body such as WICS which is trying to manage a dual role?

- I consider that there are likely to be quite a few public bodies (given their specialist expertise) that could earn revenue by leveraging their experience. To do so successfully would, in my view, require three important steps.
- There should be a clear, unequivocal mandate to pursue revenue generation in order that all stakeholders understand the expectations of Government.
- There should be agreed expectations about what ‘success’ would look like and what expenditure could be incurred to develop a pipeline of projects.
- Some form of separation (whether that be an accounting or a legal separation) is essential. I had seen Scottish Water’s legal separation of its international activities as an exemplar.

Culture and behaviour

18. In his section 22 report, the AGS stated that— “I am concerned that the current culture within the Commission does not have sufficient focus on ensuring the achievement of value for money in the use of public funds.”

19. The section 22 report concluded that— “Value for money should be a key consideration for all expenditure incurred by public bodies and the findings of the auditor highlight unacceptable behaviour, by senior officials within the Commission, in the use of public funds”
20. The Committee has explored these issues in the written and oral evidence that it has received. During oral evidence on 19 September 2024, the Chair of WICS ARC stated— “I received the letter from Audit Scotland before it finalised and published its audit. It highlighted not only that issue but a whole series of other concerns about behaviour, and that is what got me and the board fired up. A lot of those things were unknown to us and quite surprising, and we jumped into action based on that...That said, the behaviours and the pattern of behaviour that were highlighted caused us real concern.”

Q15: Do you agree with the written and oral evidence the Committee has received in relation to the concerns raised about the culture and behaviours at WICS?

- In general, I consider that WICS was careful in how it spent its levy funding. The two areas of expenditure that were the biggest areas of expenditure after the salaries of staff were consultancy support and rent. WICS kept its use of consultants as low as possible, by using them only to challenge developed thinking. My understanding is that WICS made less use of consultants than other economic regulators. As I have explained, WICS was pro-active in seeking to minimise rent costs during and after the pandemic.
- The WICS levy reduced in real terms over the last several years. Despite these reductions, and supported by income generation, WICS refunded Scottish Water and licensed providers on several occasions. I was proud that WICS was able to do this.
- WICS had a good set of financial procedures that were scrutinised regularly at different levels. Exceptions were highlighted. WICS and I were far from perfect but there was a consistent desire to improve.
- With hindsight, WICS could have been clearer about the separation of expenditures, resource use and revenues between its revenue generating and day-to-day activities.

- As explained earlier, it was clear to me that expenditure on developing revenue generating activities was unlikely ever to sit easily with day-to-day activities. This explains why I pursued the specific allowance for international business development in the Corporate Plan.
- As noted, I felt a considerable pressure to pursue international revenue generation and, again with hindsight, I was more attentive to the revenue opportunity and its delivery than to ensuring it was being kept demonstrably separate.
- I find the comments on culture to be disappointing. Staff retention (with the exception of analysts that moved on for salary reasons) was generally very high.

Relationship with Scottish Government sponsor team

21. During oral evidence on 19 September, the Committee sought clarity on the relationship between WICS and the Scottish Government Sponsorship Team. The Scottish Government’s Director of Energy and Climate Change stated— “I think that we all have lessons to learn from what has happened. There were shortcomings in the way in which we carried out our sponsorship function in relation to WICS. Part of the sponsorship function is to provide support to the organisation, but part of it is also to provide constructive challenge, and there were instances where we did not do that. The Director of Energy and Climate Change went on to add— “I have some personal reflections. As the director who is responsible for the area, I recognise that I should have provided more assurance and oversight to WICS”.

Q16: The Committee is interested to hear your reflections of the nature of your relationship with the Scottish Government Sponsorship Team and whether you considered it sufficient during your tenure as Chief Executive.

- I considered the relationship to be constructive and open. As noted earlier, I was regularly challenged to pursue international activities. I was consulted on policy and regulatory issues about which the Deputy Director was concerned. I tried to be as supportive as possible. I thought the relationship worked well.

- With hindsight, I would have benefitted from more advice on how to handle the two aspects of WICS activity. In particular, it would have been good if there had been clarity from Government as to how this should be handled.
- There were regular liaison meetings. Perhaps, given the extent of the international activities, these meetings could have taken place more often or there should have been separate sessions on the management and reporting of the international activities.

Q17: What was the frequency of your contact with the Scottish Government Sponsorship Team, and how was this contact made?

- I talked very regularly with the Deputy Director – probably of the order of four to five times a week, as a minimum. I consider that I shared all material issues with him. For example, I discussed the staffing constraints faced by WICS on a regular basis. I discussed how WICS used training as a retention tool. I discussed my concerns about the salary pressure on the base budget of WICS in the absence of international income. I was not aware of any material concerns of the Sponsor Team as to how the office was being administered.
- I met the Director only once that I can recall and this was shortly after the Director took up the post.

22. During oral evidence on 19 September 2024, the Committee sought clarity on when WICS first made the Scottish Government aware that a section 22 report was going to be published. The Interim Chief Executive told the Committee that— “I think that the email that had appended the section 22 report was to inform the sponsor division of the section 22 report. I think that it was on the Monday, Mr Greene, and I can remember phoning the then deputy director on the Friday to make clear of the section 22 report, having realised that there was no correspondence between the former CEO and the sponsor team. That was in early December, but I would have to get the exact date for you”.

Q18: Can you recall when you notified the Scottish Government’s Sponsorship Team that a section 22 report was going to be published?

- I was in very regular contact with the Deputy Director about the issues raised in the audit. This regular contact continued during some annual leave in Italy that I had at the end of November. It was the Deputy Director who, during that period of leave, suggested that I write to the Auditor General to seek to explain the expenditures highlighted in the report and to put them in the context of the very considerable revenues that WICS has earned.
- My relationship with the Deputy Director was such that I would have told him immediately that I knew both about the potential for a Section 22 report and when it actually happened.
- These regular conversations continued until I resigned.

Q19: What ongoing training that was available to you in your role as an Accountable Officer? For example, was specific training on changes or updates to the Scottish Public Finance Manual ever provided by the Scottish Government?

- I attended a residential course for Accountable Officers early in my time at WICS. This was at the suggestion of a then Scottish Executive secondee that had been provided to assist me in learning the ropes of working in the public sector.
- I enrolled myself in a Scottish Government course in September or October after I became aware of the audit findings.
- At no time did the Sponsor Team suggest that I was falling short in my duties as Accountable Officer of WICS or that I was not following the rules appropriately. I had taken considerable comfort from the open relationship that I had with them. There were no suggestions of new requirements, the meeting of which could have been supported by further training.
- Given the relationship, I would have expected and welcomed open feedback.

Relationship with the Board

23. During the oral evidence session on 19 September, the Chair of the Board stated— “The relationship between the board and the executive, including the chief executive, is vital for good governance.”

Q20: The Committee is interested to hear any reflections that you may have on the relationship between the Board and the executive during your tenure as Chief Executive.

- I consider that the relationship between the senior management and the Board was broadly as one might expect. At times, the executive felt that the Board gave insufficient attention to some matters that it considered important to the successful regulation of Scottish Water or the stewardship of the non-household retail framework. The Board members did not always agree on whether or how the international activities should be pursued. I sought to ensure that there was maximum disclosure to the Board.
- Each of the Board members would, doubtless, have their own views. I would note that I found the Board members to be quite challenging but, generally, supportive.

24. WICS's Governance Framework, page 7 paragraph 13, states that—
“The chair, in consultation with the Board as a whole, is also responsible for undertaking an annual appraisal of the performance of the Chief Executive”.

Q21: Can you confirm if annual performance appraisals were held by the Chair as per WICS's Governance Framework?

- Performance reviews were carried out each year. My performance was always rated positively. At no point do I recall there being any suggestion that I should be doing things differently with regard to the administration of the Office.

Departure arrangements

25. The Committee has explored the arrangements that were in place for your departure from WICS through oral and written evidence. WICS's written submission of 31 July provides information on these arrangements.

26. The Committee also explored during oral evidence whether your departure was directly linked to the section 22 report. The Committee heard from the Chair of the Board that— “The former CEO resigned, stating that he felt that he had set up WICS and had worked there for 24

years, and that he had outlived all that he could do for WICS, and that he therefore tendered his resignation. There was no specific linkage to the section 22 report.” and “The board decided to accept his resignation after extensive discussion of all the options”

27. The Chair of WICS ARC also told the Committee during oral evidence that— “His reaction to the section 22 was, “I am going to choose to resign.” We thought, “Okay, let’s talk through that,” and Donald MacRae and the board navigated through that process.”

Q22: To what extent do you agree with the above statements made by the Chair of the Board and the Chair of WICS ARC with regard to your departure arrangements?

Q23: The Committee is keen to establish the options that were discussed by you and the Board in relation to your departure from WICS. Apart from your offer to resign, what other options, if any, were suggested, either by you or the Board?

Q24: Did you feel that you had no choice but to leave the organisation following the section 22 report?

- I will answer questions 22, 23 and 24 together.
- I can agree only in part.
- It quite quickly became clear to me that the Board did not see the efforts at earning international income to be any form of mitigation relating to the conclusions of the audit or the Section 22 Report.
- In consultation with my wife, and recognising our family situation, we decided that it would be best that I retire.
- I sent a draft letter to both the Chair and to the Deputy Director of the Sponsor Team on a Sunday in early December. This letter proposed a retirement date of 31 October 2024. I chose this date because it would have been exactly 25 years since I took office as the Water Industry Commissioner for Scotland on 1 November 1999.
- As I recall, the Chair called me later that day. He asked whether I was sure that I wanted to pursue this course of action. I confirmed my intention and explained that I saw it as the right thing to do to support the transition to a new Chief Executive (10 months seemed to me to be a reasonable timeframe in which to make such an appointment).

- I also discussed with him the likelihood of a PAC hearing if a Section 22 Report was issued. The Deputy Director had explained this process to me in increasing detail over the preceding weeks. I accepted the shortfalls identified in the audit but considered that my efforts to increase revenue were a mitigation.
- The Chair said to leave it with him. He would discuss my draft letter with the other members of the Board and revert.
- I told my Directors of my intention to retire on the Monday.
- In conversation a day or two later, the Deputy Director questioned me as to whether my approach was the right one. He reiterated the likelihood of PAC inquiry and that I should perhaps negotiate an earlier exit. At this point, I had no intention of taking that suggestion.
- The Chair called me after a meeting at Scottish Water's offices to say that the Board broadly supported my request, with one or two minor caveats. He asked me to meet him in Edinburgh.
- At that meeting two members of the Board were present. They said that the Board wanted me to leave immediately.
- On two occasions during that meeting I was asked to leave the room for about half an hour. In line with the relationship I had with the Deputy Director, I called him to update him on what was happening.
- After the second absence, the Chair offered to pay notice and required that I leave immediately. This notice was consistent with my letter of appointment by the then Minister to the role of Chief Executive of WICS in July 2005.
- A very brief resignation letter was subsequently agreed. I sent this letter.
- I was required to destroy any and all materials relating to my employment at WICS. I did so diligently.
- To summarise, I am certain that I had no choice but leave WICS in the manner that I did.
- Leaving in this way was a huge personal disappointment as I considered that I had been effective in my role as the economic regulator of Scottish Water for a very long time. I was proud of what had been achieved.
- I should like to reiterate that I accept the findings of the audit but I consider that the shortcomings identified were not, in any way, the result of a lack of effort or commitment on my part.

28. Should there be any further information you feel would assist the Committee in its scrutiny of the section 22 report, please feel free to include this in your response

- I have nothing further to add.
- This evidence is as complete as it can be given that I have no records available to me.