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Dear Convenor

I am writing in response to the Committee's report on *The 2022/23 and 2023/24 audits of the Water Industry Commission for Scotland*, published on 16 May 2025. I would like to thank the Committee for this report which I found to be balanced and constructive. The issues highlighted in the section 22 reports into WICS have raised serious issues and I appreciate the scrutiny and time which the Committee has given to these matters.

I note that a number of the recommendations and conclusions in the report are specifically for WICS and understand that they will respond to you separately. However, let me put on record that, while it is for WICS to determine how they address these, I endorse the Committee's conclusions as they relate to WICS and the thrust of all relevant recommendations.

I will focus my response on those recommendations that are for Scottish Government. I have sought to address each of these in the table at Annex A and, more broadly, have set out below our response to each of the themed headings in your report. You will see that the Scottish Government is content to take forward the recommendations as noted and we have already taken action to address a number of these.

Response to headline conclusions

Before addressing the themes in the report, I can confirm that Scottish Ministers endorse the report's three headline conclusions and have set out our views in relation to these immediately below.

As a public body and economic regulator of Scottish Water, the Committee considers that WICS has failed to lead by example in respect of ensuring value for money, as evidenced by the significant weaknesses in its governance and financial management arrangements highlighted by the Auditor General for Scotland in his section 22 reports.

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I will start by reiterating the view of Scottish Ministers that the inappropriate expenditure highlighted in the successive section 22 reports was unacceptable. The then Cabinet Secretary for Net Zero and Energy commissioned a review into the financial governance at WICS (“the Independent Review”), the scope of which was then expanded to review historical transactions. The Independent Review was published in November 2024 and unfortunately confirmed that there were deep rooted and longstanding issues with compliance, scrutiny and culture.

We have worked with WICS to address these issues. During the summer of last year, an expedited process was undertaken to strengthen the WICS Board, appointing two interim members. One of these members, Ronnie Hinds, has since been appointed as interim Chair. This additional experience and expertise helped to support the interim Chief Executive and begin to provide Ministers with the assurance that the organisation is on a path to rebuilding public trust.

I have tasked Mr Hinds with completing the reset of the organisation. Mr Hinds has been working with the Scottish Government on the recruitment of three new members of WICS and securing a permanent Chief Executive. Interviews for both exercises are now completed with a permanent Chief Executive appointed on Thursday 26 June. The process will conclude for the remaining appointments very shortly.

On the basis of the evidence it received, the Committee considers that not one individual or body is responsible for the catalogue of failures that occurred at WICS. It is clear that the WICS Board and Audit and Risk Committee, along with the Scottish Government and the former Chief Executive all failed to meet the standards required of them and contributed to an unacceptable use of public funds.

Under the Scottish Public Finance Manual (SPFM), Accountable Officers have the responsibility for ensuring the organisation abides by the principles of Best Value as well as the propriety and regulatory of finances. In the case of WICS, the former Chief Executive was an experienced Accountable Officer of many years and should not have required either the Scottish Government sponsor team or the WICS Board to highlight the need to follow these principles at all times.

The Boards of public bodies have corporate responsibility for promoting efficient and effective use of resources and to ensure that the affairs of the organisation are conducted with probity. The WICS Governance Framework is clear that the Board also has corporate responsibility for ensuring that effective arrangements are in place to provide assurance on risk management, governance and internal control. The SPFM and the WICS Governance Framework clearly show how the organisation should have acted and it failed to meet these standards.

I also accept that the Scottish Government’s sponsorship of WICS was not as robust as it should have been. While sponsorship of individual public bodies is an operational matter for the relevant part of Scottish Government, I note that several of my senior officials have given evidence to the Committee and recognise that, in relation to WICS, there were shortcomings in how the Scottish Government had carried out its sponsorship function. Scottish Government has acted to remedy this, including the commissioning of a review into sponsorship of WICS (“the Internal Review”). This was published alongside the Independent Review in November 2024. The Scottish Government accepted the recommendations in that report and the sponsor team has completed all the management actions.

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We [the Committee] welcome the Auditor General for Scotland's intention to track and monitor progress on the matters identified in his section 22 reports, with a view to further public reporting if necessary.

We welcome that the Auditor General for Scotland intends to monitor WICS closely. As part of Scottish Government's sponsorship role, we will also continue to monitor progress against WICS's committed actions, and will be looking for evidence that these are being effective in addressing the issues that have arisen and long term change is being embedded.

We have been encouraged by the improved culture of compliance highlighted by Audit Scotland and WICS's internal auditors for the period since December 2023. This provides a good indication that the organisation is on the path to rebuilding public trust. However, we will not be complacent and my officials continue to ensure that escalated sponsorship measures, such as regular leadership assurance meetings, remain in place while the reset of WICS continues.

Response to themed headings

I will now move on to the other themed headings in the report.

Poor governance regarding approval of expenditure

In relation to the inappropriate expenditure highlighted in the section 22 reports, this has raised significant concern around the financial governance within WICS. The SPFM and the framework document between Scottish Government and WICS provided clear guidance as to how WICS should have approached approval for these items.

In terms of broader financial governance, the Independent Review of WICS concluded that:

- Refreshing policies and procedures alone will not be sufficient to place WICS on a firm footing to move safely forward. Equally, or more important, will be a reset in the 'tone from the top' and getting the basics right.
- There was limited evidence of challenge and related actions and follow-up in relation to the culture around value for money and the appropriateness of certain expenditure and policies that enabled such expenditure.
- Some senior staff and Board members may have been aware of issues relating to behaviour and culture over a period of time, and there was a lack of evidence to demonstrate action taken as a result.

For example, in the case of the Harvard training course and purchase of gift vouchers for staff, WICS should have presented a business case in advance of incurring expenditure to allow scrutiny and challenge by Scottish Government.

While it is for WICS to seek Scottish Government approval where expenditure is beyond delegated limits, novel or contentious, a more proactive approach to sponsorship scrutiny should have been applied in these cases and there is now a standing agenda item at WICS sponsorship meetings to discuss any potential approvals required. Our focus going forward is to ensure that WICS embeds a culture of compliance and understands the occasions when it must seek Scottish Government's timely approval and we are encouraged that WICS is now flagging high profile issues at an early stage.

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The lack of scrutiny applied by officials before providing retrospective approval for the Harvard course and the gift vouchers is also a matter of regret. As the Auditor General for Scotland has noted, lessons have been learned and I have been assured by officials that the WICS sponsor team will not approve expenditure retrospectively in future unless there is a clear case for it, which would only be in exceptional circumstances. I can also confirm that we have not received further requests for retrospective approval from WICS since the initial section 22 report in December 2023.

Weaknesses in financial controls

We agree with the Committee's findings that the financial controls within WICS were insufficient, including around expenses and hospitality. These conclusions are in line with our own Independent Review last year which found that a number of sample expenses were in excess of the maximum amount permitted by policy at the time, and that historical expenses policies were silent on key areas such as whether alcohol was permitted in subsistence claims.

We do, however, recognise that WICS quickly put in place an action plan to address the practices that enabled the inappropriate spending, and that the interim Chair set out additional actions to support the reset of WICS following the publication of the Independent Review. This provides further encouragement that the organisation is committed to rebuilding public trust.

The Scottish Government will not routinely have sight of a public body's individual expenditure items and would not expect to review internal policies such as those relating to travel or expenses unless what was proposed is considered novel or contentious. It is for WICS to set its own policies, in line with the SPFM and Best Value principles, and then, through its Board, to ensure there are appropriate internal control mechanisms in place. However, we recognise that the sponsor team was not providing constructive challenge in the way it should have. We have strengthened our sponsorship function and our abilities to spot any issues such as these in future through the measures set out below.

Role of the Scottish Government Sponsorship Team

We recognise there were shortcomings in the way the Scottish Government carried out its sponsorship role and immediate actions were taken to address this. This included escalation beyond normal governance arrangements and the establishment of monthly assurance meetings from January 2024 attended by the Chair and Chief Executive of WICS and the Scottish Government sponsoring Director/Director General.

The Internal Review recognised that progress had been made in improving the sponsorship function since the first section 22 report was published and made recommendations for further improvement. The main findings included:

- A need to review and refresh the framework document between Scottish Government and WICS and ensure roles and responsibilities are clear and understood.
- Concentration of sponsorship in one individual.
- A lack of resources and a new and inexperienced sponsorship team.

In response to this, officials have completed a number of management actions including:

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- Worked with WICS to agree an updated framework document between Scottish Ministers and WICS, published in February 2025.
- Documented clear roles and responsibilities for sponsorship from Director level down.
- Set out the plan for the resources required to deliver those roles and responsibilities and bolstered the capacity of the sponsor team.
- Completed all recommended sponsorship training across the sponsor team.

The team's focus is now on building sustainable improvements to lock in these early actions. Further actions taken since publication of the Internal Review include the establishment of sponsor team representation at WICS Board meetings regularly as an observer and the structural separation of the policy and sponsorship teams within the Water Industry Division. We have further increased the capacity of the sponsorship team in 2025 and clarified escalation routes with WICS.

I note that the Auditor General for Scotland intends to look at Scottish Government sponsorship of public bodies more broadly. Scottish Government is committed to transparency and will provide the necessary input to this broader piece of work by the Auditor General for Scotland as and when required. The Director General for Net Zero has taken measures across the portfolio to strengthen the sponsorship approach.

Following the issues highlighted regarding WICS last year, our Public Bodies Support Unit has been undertaking improvement work in relation to sponsorship across the whole of Scottish Government and worked with Directors General, their leadership teams and sponsor teams to conduct a risk review of all public bodies. This consisted of two elements: completion of a RAG rating template; and individual deep dives for each portfolio. As a result of this, the following main recommendations were identified:

- Sponsorship should be viewed as a specialism;
- A peer-led sponsorship network should be established;
- More support for sponsor teams should be available when issues arise; and
- Additional activity is undertaken at a Director General level, including annual deep dives.

Work on these four areas has been taken forward by officials who will be happy to provide further information to the Auditor General for Scotland.

Role of the Board

I agree with the Committee that the WICS Board did not sufficiently meet its duties to promote the efficient, economic and effective use of resources, consistent with the principles of Best Value. Nor did it ensure that effective arrangements were in place to provide assurance on risk management, governance and internal control. These duties are set out clearly in the framework document.

The Independent Review concluded that it would be important to reset the 'tone from the top' of the organisation and get the basics right. As set out above, Scottish Ministers have taken steps to strengthen the WICS Board, both in number and in diversity of skills and expertise. For example, the two members appointed on an interim basis last summer have substantial experience in public sector governance.

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Former Chief Executive's departure

As Audit Scotland noted in their section 22 report for 2023-24, Ministers made clear to WICS that the settlement agreement for the former Chief Executive did not follow due process and officials were not made aware that WICS were intending to use a settlement agreement until after it had been signed. Once this was known, Scottish Government took immediate steps to halt any payments and ensure that WICS made a documented business case for their approach. Feedback and advice from relevant Scottish Government teams was sought in line with the SPFM, albeit retrospectively.

I am unable to comment on conversations that the former Chief Executive claims took place with the former Deputy Director. However, we recognise that the sponsor team should have been more proactive in supporting the Board to consider the options available and how value for money should have been evidenced. Steps have been taken to put in place clear processes and routes of escalation of risks and issues and a systematic approach to engagement, rather than heavy reliance on any one individual.

As the Committee notes, the SPFM was updated in March 2024 to provide clarity on instances where the Accountable Officer of a public body is the subject of a settlement agreement.

Other significant issues

Organisational culture

We recognise from our Independent Review that WICS had significant issues to overcome, including around compliance with governance and fostering a culture where it is safe to challenge and staff views are heard. We believe that the actions taken by WICS, coupled with the measures Scottish Government has taken to improve our own sponsorship function, are supporting these long-term cultural improvements.

The sponsor team has seen positive improvements in the compliance culture and WICS highlight any areas of expenditure that could breach delegated authority at an early stage. I tasked the interim Chair, upon his appointment, with resetting the organisation and we will continue to support WICS to make the changes to structures and staff required to deliver a more effective organisation. The way in which this is delivered is a decision for WICS but we are supportive of the restructuring work already underway. In terms of staff support, I understand that WICS has appointed dedicated HR resource and hope this again helps staff feel empowered to undertake their roles with clarity and know how to raise any concerns.

Remit of WICS

The Committee's report, alongside the section 22 reports and our own Independent Review, has highlighted significant historical issues. However, I do not want to lose sight of the good reputation that WICS has held as an economic regulator or the important role it plays in the water sector in Scotland.

Independent economic regulation is a core part of protecting consumer bills. Scottish Water is a natural monopoly as the sole provider of water services across Scotland. Effective economic regulation, through the setting of efficiency targets, places the financial pressure to drive efficiencies in the absence of competitors. In the context of ageing assets and climate and population change, it will be more vital than ever that there is effective regulation of Scottish Water and that customers are getting value from their publicly owned company. As

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officials indicated at Committee, we have no plans to look at a different structure for WICS at this time.

I have, however, agreed that WICS should pause all international consultancy work until 2027 to allow them to focus on resetting the organisation and the work on the Strategic Review of Charging for the next regulatory period (2027-33). As set out in previous correspondence to the Committee, any resumption of the international workstream would require Ministerial approval and need to be supported by a business case and governance model that sufficiently separates it from WICS's core regulatory work. Irrespective of any past or future tensions between undertaking core regulatory functions and commercial-facing work, it is for the Accountable Officer for WICS to satisfy themselves, and Parliament, that any expenditure is made in compliance with the requirements of the SPFM.

Shared services

The Scottish Government continues to encourage public bodies to consider options for shared services as part of the wider Public Service Reform agenda. This will remain a live consideration as part of our sponsorship of WICS. We would draw to the Committee's attention that WICS already shares certain facilities with Zero Waste Scotland (ZWS), and is working with ZWS to consider future shared services arrangements.

I would again like to thank the Committee for this important report.



GILLIAN MARTIN

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ANNEX A

Paragraph	Recommendation	Response
50	The Committee is concerned that despite the Scottish Government being aware of the high-cost training policy that WICS had in place for senior staff, it did not reassure itself that the appropriate procurement processes were in place or whether its approval was required. We seek assurances that lessons have been learned from this failing.	<p>Accept. Discussion of upcoming procurement and any novel or contentious expenditure is now routinely included on the agenda for the sponsorship meetings between Scottish Government and WICS, to provide early warning where assurance or approval might be required.</p> <p>However, it should be noted that the Accountable Officer of WICS, rather than the Scottish Government, is responsible for ensuring that the procurement of individual purchases is in line with the SPFM and relevant internal processes. Approval for items of expenditure should only be escalated to sponsor teams where they breach delegated authority limits or could be considered novel or contentious.</p>
66	We recommend that the Scottish Government ensures that all public bodies review their relevant policies to ensure that they are in line with the Non-Salary Rewards section of the Scottish Public Finance Manual.	<p>Accept. The Scottish Government's quarterly RAG assurance process is regularly reviewed to ensure it is fit for purpose, reflecting prominent issues on which assurance is sought. Following the WICS section 22 report, the RAG rating includes assessment of whether public bodies have reviewed all existing and relevant policies with a lens on public finance. The RAG returns are reviewed on a quarterly basis and, should there be any issues highlighted, these will be explored with the relevant sponsor team and public body.</p> <p>Specifically in relation to WICS, it has revised its financial policies in full including expenses, taxable benefits and gifts.</p>

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		Since the first section 22 report, the gift vouchers highlighted by the Auditor General for Scotland have ceased.
83	The Committee is unclear how the Scottish Government was able to conclude that it was appropriate to provide retrospective approval for expenditure relating to the training course at Harvard Business School and gift vouchers, given the lack of supporting detail provided by WICS.	<p>Accept. We recognise that consideration of the request from WICS was not robust and there appeared to be a lack of appreciation of the alternative options available to the sponsor team.</p> <p>These conclusions were made by the former Deputy Director of the sponsorship team therefore we cannot comment further on the decision making process, beyond the oral evidence previously provided to the Committee.</p>
84	The Committee considers that the Scottish Government should have challenged WICS appropriately and carried out its own due diligence before considering retrospective approval.	Accept (see paragraph 83 response).
85	The Committee is seriously concerned at the Scottish Government's response of there being 'no material benefit' in challenging the expenditure relating to the training course and gift vouchers that it was asked to approve retrospectively and shares the Auditor General for Scotland's view of the potential impacts of taking such an approach.	Accept (see paragraph 83 response). As covered in later evidence session, the implications of the body not operating in accordance with the framework document on delegated limits and the sponsor teams scrutiny of this is understood.
95	The Committee notes the Scottish Government's decision not to provide retrospective approval for two further expenditures that WICS should have obtained its approval for. It is reassuring that	Noted. The lessons learned from WICS were the focus of a series of public body sponsorship deep dives held last year with Director Generals. These deep dives will be held annually to strengthen the sponsorship oversight.

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	<p>lessons appear to have been learned by the Scottish Government with regard to providing retrospective approval. The Committee seeks assurance that the lessons learned on seeking and providing retrospective approval have been shared across all Director-General portfolio areas in the Scottish Government and with public bodies.</p>	<p>The WICS experience has also been the topic of the recently-introduced Scottish Government peer-led sponsorship network. The discussion there covered the events relating to retrospective approval alongside other issues that arose.</p> <p>For public bodies, adherence to the Scottish Public Finance Manual, including around the authorisation and timing of any expenditure, is a key part of the framework documents which are agreed between public bodies and Scottish Ministers.</p>
125	<p>The Committee also welcomes confirmation from the Auditor General for Scotland that no further non-compliant expenditure was found between January and March 2024, but this must be kept under close scrutiny.</p>	<p>Noted. We are encouraged that no non-compliant expenditure has been identified since the publication of the first section 22 report. We have put in place a systematic approach to sponsorship which will enable us to seek long-term assurance around improvements to financial governance and culture.</p>
143	<p>It is clear to the Committee that there have been significant weaknesses and failings in the Scottish Government's sponsorship of WICS. These have led to a failure to ensure appropriate safeguarding of public funds. The Committee would have expected the Scottish Government to fully comply with the requirements of the Governance Framework.</p>	<p>Accept. The recommendations of the Internal Review into sponsorship of WICS, published on 7 November 2024 were accepted by the sponsorship Director. All of the management actions from that report have been completed.</p> <p>The framework document between Scottish Ministers and WICS was revised in February 2025 to make the respective roles and responsibilities of WICS and Scottish Government clearer and to ensure there is a systematic approach to engagement rather than heavy reliance on any one individual.</p>
152	<p>The Committee recommends that the Scottish Government reviews whether improvements can be made to its RAG rating system that would help</p>	<p>Accept (see paragraph 66 response). The quarterly RAG process is regularly reviewed to ensure it is fit for purpose. It will be reviewed again before next year's audit cycle begins</p>

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	it identify emerging issues of concern within public bodies at an early stage, such as those uncovered in the recent annual audits of WICS.	to ensure it meets current needs and helps sponsor teams to identify and address issues early.
166	The Committee notes the changes that have been made in Board membership since the publication of the 2022/23 report. Given the challenges that WICS faces in rebuilding the trust and confidence of Public Audit Committee stakeholders and the public as a regulator, we recommend that Scottish Ministers give consideration to ensuring the maximum number of Board members, with the required financial and governance skills, are appointed.	Accept. A public appointments recruitment round has recently been undertaken in relation to WICS. We expect to confirm the appointment of new Board members shortly and will be seeking to bring the number of Board members up to the maximum permitted by WICS's founding legislation.
167	The Committee also recommends that current Board members undertake refresher training on their roles and responsibilities and the financial management and reporting requirements of public bodies. The Committee welcomes the recommendation in the independent review of WICS's governance arrangements that WICS and the Scottish Government give consideration to any further training and support required by the Board and the Audit and Risk Committee.	<p>Accept. The WICS Board is predominantly made up of members who have joined after the initial section 22 report and have either completed the mandatory training relatively recently or will do so as part of their induction. We particularly recognise the importance of this training, and setting the right Board culture, given that three new board members are shortly to be appointed. WICS has confirmed that its induction training has been reviewed and will now go further than the mandatory training and include specific modules relating to the functions of WICS (e.g. competition law). Existing Board members are also invited to this induction programme.</p> <p>Board members now also undertake the same mandatory training as WICS staff (e.g. cyber security, fraud awareness).</p>

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194	It is the Committee's view that the Scottish Government failed to recognise the unusual circumstances faced by the Board when managing the departure of the former Chief Executive and that they should have been more proactive in providing the Board with advice.	Accept. We recognise that the sponsor team could have been more proactive in encouraging WICS to consider whether alternative options were available. However, the Scottish Public Finance Manual is clear. In the case of a settlement agreement, there needs to be a business case, and this needs to be presented to the Scottish Government for feedback and advice. This did not happen ahead of a settlement agreement being agreed.
196	The Committee has significant concerns that the former Chief Executive appears to have been encouraged to negotiate an early exit date by the Scottish Government sponsor team. The early exit secured by the Board has hampered the Committee's ability to hear the former Chief Executive's full account of the failings at WICS during his tenure and its subsequent Public Audit Committee scrutiny of the issues arising from the audit reports. For any similar situations in the future, we expect Accountable Officers to remain in post, wherever possible, in order to be held accountable by Parliament.	The Scottish Government believes in transparency and is keen to facilitate the legitimate scrutiny from all Committees. However, Ministers and Boards of public bodies can only ensure that Accountable Officers remain in post within the terms of that individual's conditions of employment.
209	The Committee is disappointed that the independent review of WICS's governance arrangements found that some senior officials and the Chair of the Board and the Audit and Risk Committee were aware of culture and behaviour issues at WICS, yet there was a lack of evidence to demonstrate action had been taken to address these issues.	Accept. Scottish Government has strengthened its WICS sponsorship function and put systematic engagement and escalation processes in place to ensure that issues are socialised at the appropriate level and that relationships are not concentrated in any one individual.

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226	It is clear to the Committee that tensions exist between WICS's role as an economic regulator and its international consultancy work, which generated substantial funds for the public purse. Given this unique position, it is even more surprising that robust arrangements were not in place to ensure financial propriety and effective governance by WICS, its Board and the Scottish Government.	The undertaking of revenue raising activity, including international consultancy work, did not preclude the need for the WICS Accountable Officer to adhere to the Scottish Public Finance Manual or WICS's own internal processes. While Scottish Government would support any considerations around the need for clearer separation of a public body's functions, it was for the Accountable Officer, supported by the WICS Board, to ensure that appropriate financial governance was in place and that regularity, propriety and value for money were demonstrated across all expenditure.
228	As part of this process the Committee recommends that the Scottish Government and WICS seek feedback on all aspects of the work WICS has provided to international clients to help determine the value of its work. The Scottish Government and WICS should also consider the most appropriate model or organisation to take this work forward were it to be resumed. The Committee is clear that should international work resume, there should be no return to the culture and behaviours identified in the audit reports.	<p>We are content that WICS has shared feedback from international clients and note that testimonials were provided to the Committee by WICS in correspondence. We recognise the value of this previous work to WICS and to the reputation of Scotland's water industry model. However, the current focus for WICS should be resetting its financial governance and culture and preparing for the next regulatory price control period.</p> <p>We agree that a business case including appropriate models for WICS delivering any future international consultancy work would be considered ahead of any decision that the activity should resume.</p>
232	The Committee recommends that as part of its organisational transformation, WICS gives consideration to where it can most usefully share services with the Scottish Government or other public bodies in order to optimise its resources.	Agree. The Scottish Government continues to encourage public bodies to consider options for shared services as part of the wider Public Service Reform agenda. This will remain a live consideration as part of our sponsorship of WICS.

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